

# Mladá veda

## Young Science



Špeciálne vydanie



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# **GEOPOLITICKÁ ROLE NOVÉ HEDVÁBNÉ STEZKY VE FINANČNÍCH ASPEKTECH**

## **GEOPOLITICAL ROLE OF THE NEW SILK ROAD PROJECT IN THE FINANCIAL ASPECTS**

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### **Abstract**

The article deals with geopolitical role of China in the New Silk Road coordinates in the XXI century. China's New Silk Road project aims at achieving long-term economic, financial and political objectives. Its east-west land route will enable China to spread huge financial resources reserves and exert influence on the world's consumption regions. Collective leadership in communist party with long-term perspective in finances through the New Silk Road project that will connect almost whole world. China's the New Silk Road project is a "one stone kills three birds" strategy that will help China achieve international, domestic and political objectives in the long-term by opening up new trade, financial and investment opportunities that will reshape the global balance of economic power. Through an economic land - called the Silk Road Economic Belt that includes countries on the ancient Silk Road through Central and West Asia, the Middle East and Europe, and trough a sea route – called the 21st Century Maritime Silk Road that links China's port facilities with the African coast through South and South East Asia, moving up through the Suez Canal to the Mediterranean. All of these initiatives give possibility to make stronger yuan and spread it in the world.

Key words: The New Silk Road project, financial integration processes, international trade

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## **Abstrakt**

Článek se zabývá geopolitickou rolí Číny v oblasti nové hedvábné stezky ve 21. století. Projekt Čínské nové hedvábné cesty se zaměřuje na dosažení dlouhodobých hospodářských, finančních a politických cílů. Východo-západní pozemní trasa umožní Číně rozšířit obrovské finanční rezervní zdroje a ovlivnit světové spotřební regiony. Kolektivní vedení komunistické strany, s dlouhodobou perspektivou v oblasti financí, prostřednictvím projektu nové hedvábné stezky propojuje téměř celý svět. Čínský projekt nové hedvábné stezky je strategií "one stone kills three birds", která pomůže Číně dlouhodobě dosáhnout mezinárodních, domácích a politických cílů otevřením nových obchodních, finančních a investičních příležitostí, které změní celosvětovou rovnováhu ekonomické síly. Prostřednictvím ekonomické pumpy – tzv. ekonomická zóna hedvábná stezka, která zahrnuje země na staré silniční cestě přes střední a západní Asii, Střední východ a Evropu a po mořské trase – nazvané námořní hedvábná stezka 21. století. Ta spojuje čínská přístavní místa s africkým pobřežím přes jižní a jihovýchodní Asii a vede dále přes Suezský průplav ke Středomoří. Všechny tyto iniciativy umožňují vytvořit silnější měnu (yuan) a rozšířit ji ve světě.

Klíčová slova: projekt nové hedvábné stezky, procesy finanční integrace, mezinárodní obchod

## **Introduction**

The new Chinese Silk Road as an innovative economic strategy consists of two programs: the Silk Road Economic Belt Program and the ASEAN Seaport Network, informing the Economic Intelligence. The first part of the strategy is to arrange an infrastructure modernized China-Europe route of communication, which will enable the organization of continuous supply of goods along the Europe-China route, significantly reducing the time spent on deliveries (Europe and China's New Silk Roads, 2016). China itself initially supposed to add about \$ 2.5 trillion to its own annual trade turnover in ten years of strategy implementation. This should be due to the intensification of trade relations with the countries in the belt of the new Silk Road. China not yet in a hurry with the final plan, however, the strategy is announced gradually becoming a reality, creating new institutions: China created Asian Infrastructure Investment Bank (AIIB) and Silk Road Foundation. Potential for the new Silk Road will account for 55% of world GDP, 70% of the world's population (Asian Infrastructure Investment Bank, 2017).

If this initiative is implemented in practice, it can seriously affect the geopolitical landscape and lead to the creation of a number of alternative economic associations and opportunities. The concept of the economic role of the New Silk Road project involves not only the creation of a network of profitable transport corridors and the unification of infrastructure for convenient transportation of goods along the route. This is not just a line on the map. In fact, today the new Silk Road project is all mutually beneficial routes and economic ties (Shepard, 2016). The New Silk route does not imply the existence of a specific route on the map. It involves the creation of an economic space on the basis of mutually beneficial cooperation (Chi, 2016). On a global scale, it aims to create an alternative regional economic space and to make yuan stronger on the global currency markets.

## Main material and results

This long-term dream can connect east and west through huge infrastructure projects where both sides might get win-win results.



Figure 1 – The New Silk Road project – Chinese Dream  
Source: Chi (2017a)

The New Silk Road idea was first conceived in October 2013 as a pillar strategy to realise President Xi Jinping's "Chinese Dream"; made official in March 2015 as One Belt One Road project. The Belt and Road forum in Beijing in May 2017 outlined action plans to boost trade and investment along the Belt and Road routes (Xi, 2017).

Internationally, it should unleash an infrastructure boom by connecting China with Asia, Europe and Africa by land and sea, and boost yuan internationalisation by encouraging its usage in both trade and financial transactions (Chinas New Silk Road is Getting Muddy, 2017). Politically, Beijing hopes to use the New Silk Road to secure foreign trade relationships to counteract major trade pacts, such as the Trans Pacific Partnership (TPP) and the Transatlantic Trade and Investment Partnership (TTIP) that have excluded China, and to breakout of the US "pivot Asia" policy that blocks China's expansion eastward (Chi, 2017a). Financial resources in the New Silk Road project include:

- the Silk Road Fund with 40 billion US dollars this fund is open and involves the participation of investors in their activities (Asian Infrastructure Investment Bank, 2017), however, it is not yet clear who will invest money and how to attract them;
- Asian Infrastructure Investment Bank with 57 countries-participants that signed memorandum 20 of April 2015 with 100 billion US dollars (Asian Infrastructure Investment Bank, 2017);

- Exim Bank of China will allocate 60 billion US dollars for projects (Ansar et al., 2016);
- State Development Bank of China – 110 billion US dollars (Ansar et al., 2016).

Totally, Chinese government plans invest 2.5 trillion US dollars for infrastructure projects (Action plan, 2015).

The New Silk Road aims at building a massive network of trade and infrastructure for China to expand into countries in Asia, Central Asia, the Middle East, Europe, Africa. It should also go a long way to deepen yuan internationalization.

Investment projects that had been started according to the New Silk Road plan:

- Kenya Part of the initial fund was invested in the construction of a Mombasa–Nairobi Standard Gauge Railway.
- Pakistan US\$1.65-billion investment in the Karot Hydropower Project and other hydropower projects in the region as part of the China-Pakistan Economic Corridor (Silk Road Fund's 1st investment makes China's words into practice, 2017).
- Russia Acquisition of 9.9% of Yamal LNG project, a liquefied natural gas project in Sabetta, located north-east of the Yamal Peninsula, from Novatek (China daily, 2015)

Optimists think Beijing has an implementation strategy for the New Silk Road projects by pointing to many examples of Chinese-funded projects. The New Silk Road initiative is not a coherent trade and investment plan but a series of wide-ranging projects that serve Beijing's economic and political aspirations. Different levels of the Chinese government have used the initiative as an excuse to launch investment projects. The media and many analysts have assumed that all these are the New Silk Road projects, even though they may not have any official the New Silk Road status. The reality is that the New Silk Road initiative is a vision based on an evolving concept (Jeremy Page, 2014).

China's economic, financial and political leverage will inevitably grow, but that might be a trade-off for countries anxiously seeking economic development but are ignored by the multinational development banks. China is putting its interests first, but there are also benefits for the participant countries in the New Silk Road project – Belt and Road initiative (Silk Road Project, 2017).

According to analysis of China's foreign contracted and completed projects - raising numbers of new foreign contracts since announcement are continuous to grow and foreign revenue showing fluctuations in an increasing direction.



Figure 2 – China's foreign contracted and completed projects in Belt and Road initiative  
Source: CEIC (2017)

China is shifting to lower but higher quality growth of gross domestic product (GDP) comparing with 34 members –countries in the Organization for Economic Cooperation and Development (Chi, 2017a).

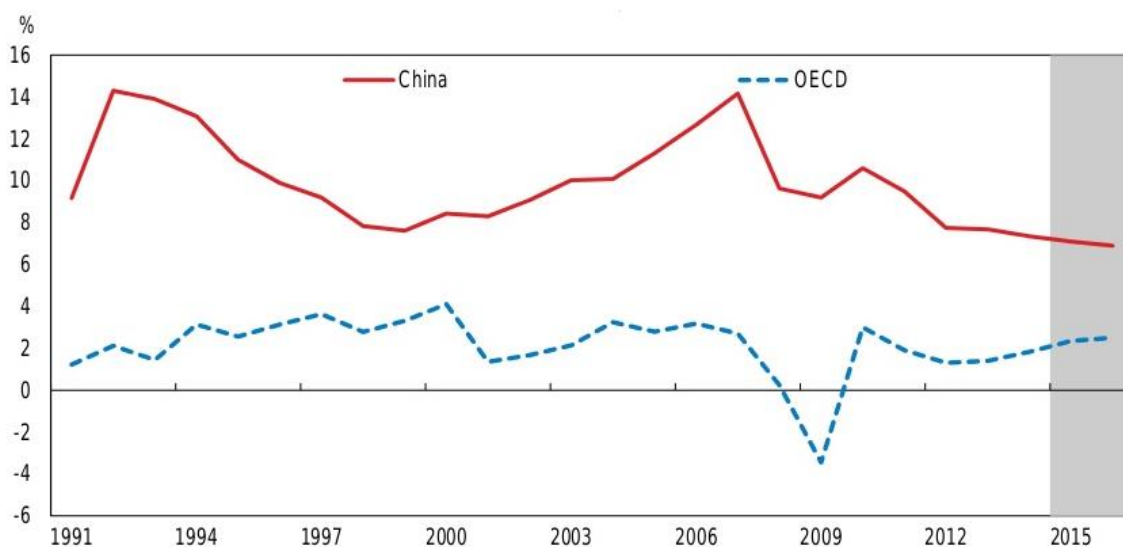


Figure 3 – Growth GDP of China and OECD countries.  
Source: OECD (2017)

As main ideas and goals of Chinese government that they have declared domestically:

- moderate prosperity for all by 2020
- China is a modern State in all respects by 2049.

Major challenges:

- Navigate the economic transition
- Rehabilitate the environment, to change situation with pollution.



First step of internationalization is trade.

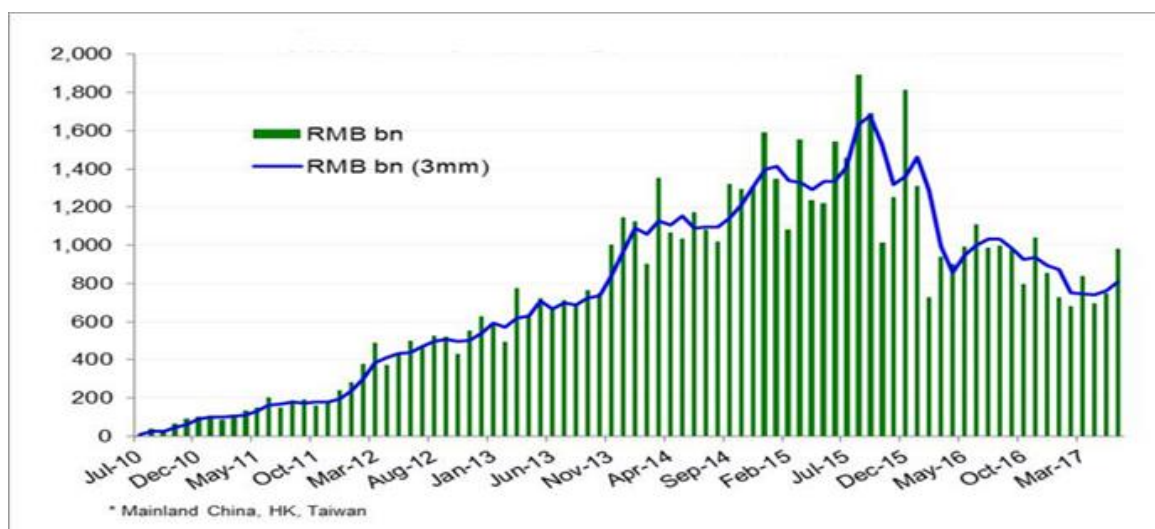


Figure 4 – Chinese currency – RMB (yuan) trade settlement 2010-2017  
Source: CEIC (2017)

Trade settlement in RMB surged from 10 bn/month in 2010 to a peak of RMB 2 trn/month in mid-2015. Over RMB3 trn swap lines signed with more than thirty central banks. RMB in the SDR is a recognition of its international role.

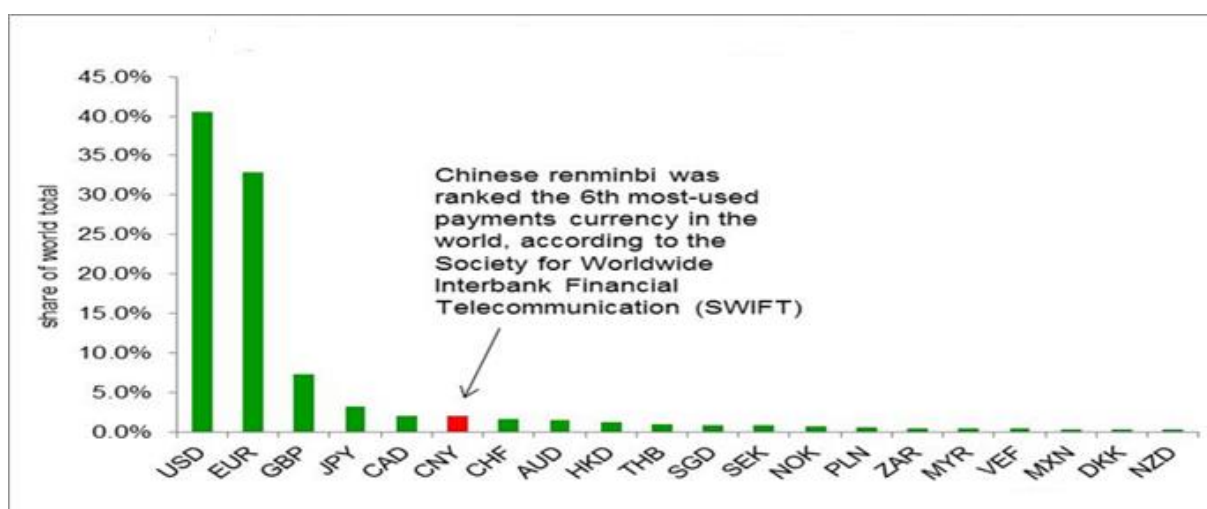


Figure 5 – Global payments currencies (June 2017)  
Source: SWIFT (2017)

The second step - internationalization of RMB (yuan) as global player in the currency market (Chi, 2017b). That will need such actions as:

- The first step is hitting a limit; current account surplus is not conducive to internationalization;
- A demand for money approach to analyze the next step (Transactional demand - foreign trade; Precautionary demand - reserve currency, savings; Speculative demand - investment);



- Developing precautionary and speculative demand for the RMB; i.e. using RMB for financial transactions;
- Need a deep and mature Chinese capital market, with RMB financial instruments and hedging tools made available to global players in both the onshore and offshore markets.

Among the USD, JPY, EUR, GBP and RMB, the RMB is likely to see growing international usage in the coming years. Beijing's continued financial liberalization - RMB a growing part of the global financial infrastructure. AIIB, Silk Road Fund, New Development Bank & policy banks' international lending to boost RMB's global role under Belt & Road. Most major currencies are failing to serve as a store of value by not being able to deliver stable positive returns. May the RMB be an alternative. China is the biggest country implementing the largest amount of structural reforms. The USD's dominance in global payments has been eroded. Euro's challenge has come and gone - the "European Dream" has been disrupted. When global trade re-accelerates, the biggest momentum will be in emerging markets led by China - the share of RMB-denominated trade will rise at the expense of the G3 currencies (Chi, 2017b).

Financial integration is an important underpinning for implementing the Belt and Road Initiative in the New Silk Road project. It should be deeper financial cooperation, and make more efforts in building a currency stability system, investment and financing system and credit information system in Asia. These tasks the New Silk Road project could realize through expand the scope and scale of bilateral currency swap and settlement with other countries along the Belt and Road, open and develop the bond market in Asia, make joint efforts to establish the Asian Infrastructure Investment Bank and BRICS New Development Bank, conduct negotiation among related parties on establishing Shanghai Cooperation Organization (SCO) financing institution, and set up and put into operation the Silk Road Fund as early as possible. Also they need to strengthen practical cooperation of China-ASEAN Interbank Association and SCO Interbank Association, and carry out multilateral financial cooperation in the form of syndicated loans and bank credit. Through the efforts of governments of the countries along the Belt and Road and their companies and financial institutions with good credit-rating to issue renminbi bonds in China. Qualified Chinese financial institutions and companies are encouraged to issue bonds in both renminbi and foreign currencies outside China, and use the funds thus collected in countries along the Belt and Road project (New China, 2015).

According to the New Silk Road project Chinese side should improve the system of risk response and crisis management, build a regional financial risk early-warning system, and create an exchange and cooperation mechanism of addressing cross-border risks and crisis. Also they should increase cross-border exchange and cooperation between credit investigation regulators, credit investigation institutions and credit rating institutions. The most important that the Silk Road Fund should give full play to the role of and that of sovereign wealth funds of countries along the Belt and Road, and encourage commercial equity investment funds and private funds to participate in the construction of key projects of the Initiative. All of these investigations that Chinese government should pay attention on the role of institutions and their strength in solving different issues in accordance to such ambitious geopolitical project.

The pool of offshore RMB (yuan) comes from accepting RMB from Chinese importers. What really counts is a country's exports to China, having a larger amount of exports to China settled in RMB (yuan) than imports settled in RMB (yuan) is a necessary and sufficient condition for a country to build a large RMB pool (Chi, 2017b).

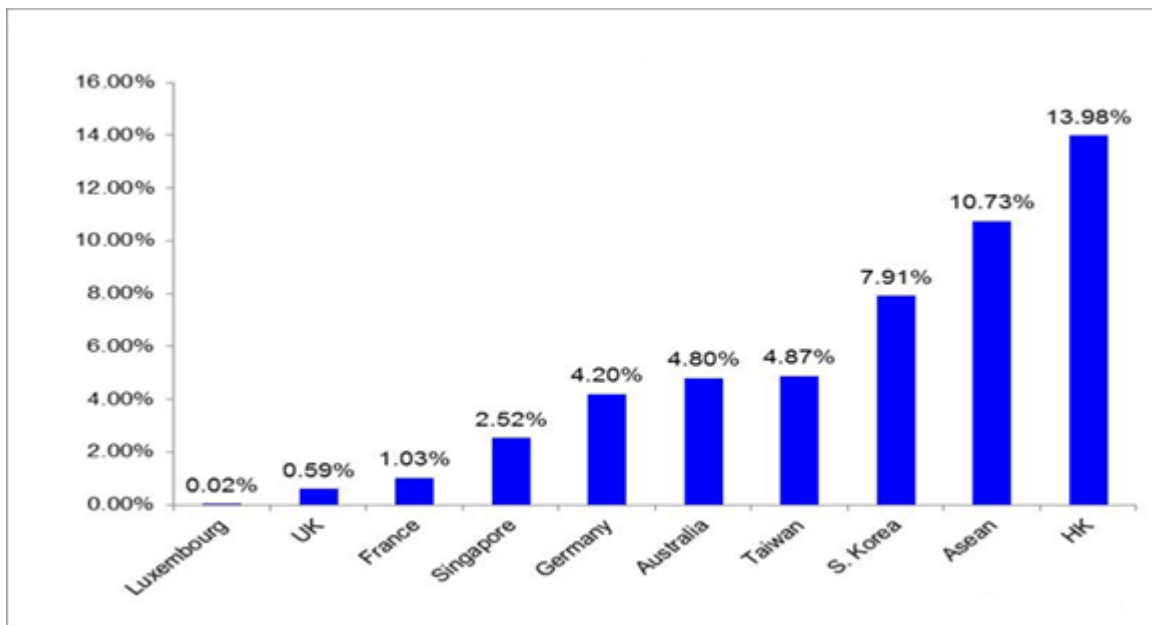


Figure 5 – Exports to China as % of China's total imports in 2010-2015 average  
Source: CEIC (2017)

Expansion of offshore RMB market increases the technical merits of the RMB becoming an asset class (Chi, 2017b). Further investment quota (QFII, RQFII) expansion before full capital account opening. ETFs / Stock Connect / Mutual Recognition etc. Direct access to China's onshore stock market.

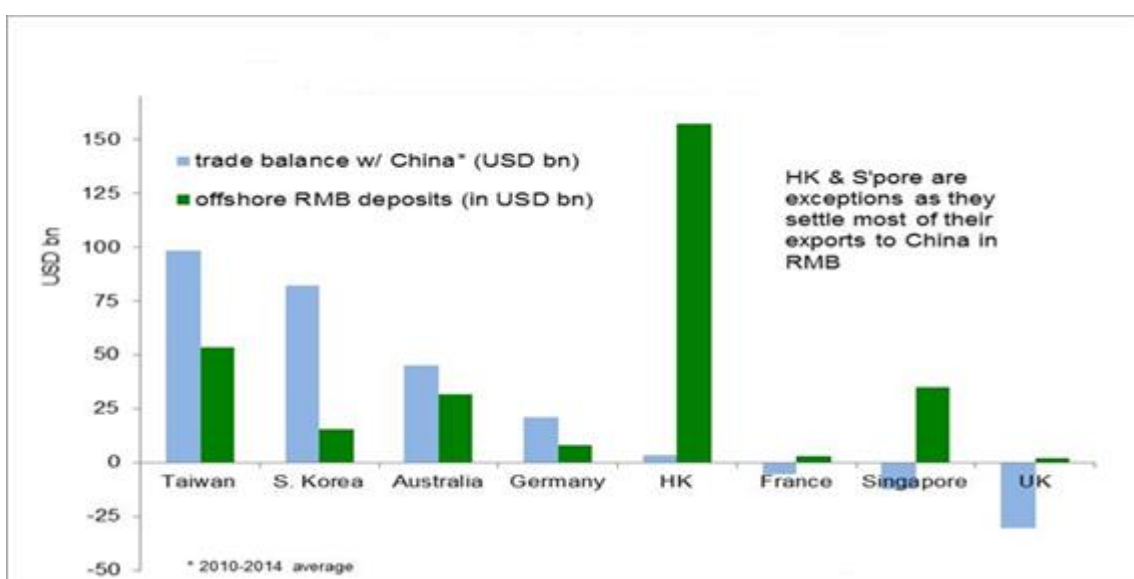


Figure 6 – Economies running trade surplus with China accumulate more RMB (yuan)  
Source: CEIC (2017)

Evidence so far suggests that the Asian Infrastructure Investment Bank represents an evolution rather than a revolution in development finance. Together with the AIIB, the New Silk Road is a bold strategy that must be taken seriously as it may prove a long-term stimulus not only for China's growth but also for the growth of the developing world (as the latter badly needs infrastructure investment). The investment opportunities will likely outweigh the risks if China goes by its words in encouraging free trade and abides by international norms and market rules. But if the New Silk Road initiative is a smokescreen for China to advance its self-interest at the expense of the others, it could be a disruption for markets. At this point, the New Silk Road project deserves the benefit of the doubt to be a positive force for the global system, also it will create new work places as urbanisation follows industrialisation as labour and consumption move to areas where jobs exist, and jobs are created where investment exists.

### **Conclusion**

Carrying out the program of development of Western China, the leadership the People's Republic of China is implementing its own script for building Eurasian space with the help of "Economic Belt of the Great Silk Road" in the New Silk Road context, the integration of economic complexes with neighbouring countries of Central Asia with the further exit to the market European countries. The main task of the New Silk Road project is to promote the collection the development of vast space, including in a number of regions – from Northwest Provinces of China, Central Asia to the Caucasus, Central and Eastern Europe. China's offer is multifaceted. The project concept is targeted to stimulate economic growth, infrastructure development, logistics their clusters, the deepening of trade and investment ties. According to developing of the New Silk Road project the turnover between the countries of Asia and Europe will increase annually on average by 2-3%; by 2020 it will increase to 240 million tons or in monetary equivalent – 1,8 trillion dollars USA. The leading role in its provided will be played by the Chinese manufacturers. A strategically important issue for China is the optimization of international transport flows and the development of cross-border transport infrastructure tours The development of railways is a component of long-term implementation strategic goals of the New Silk Road project that will spread financial flows.

It is conceivable that global demand for RMB as working capital by the private sector and as foreign exchange reserves by the official institution sector will only increase. In the past two decades, all new roads (in terms of telecom infrastructure projects and financial architecture development etc.) led to the European cities, such as Paris, Frankfurt, Brussels and Luxemburg. In the next two decades, all new roads of telecom infrastructure, railways, ports, airports and financial engineering will likely lead to Chinese cities, such as Shanghai, Hong Kong, Beijing. Accompanying these new roads will the rise of the renminbi as a global currency on the international financial market.

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