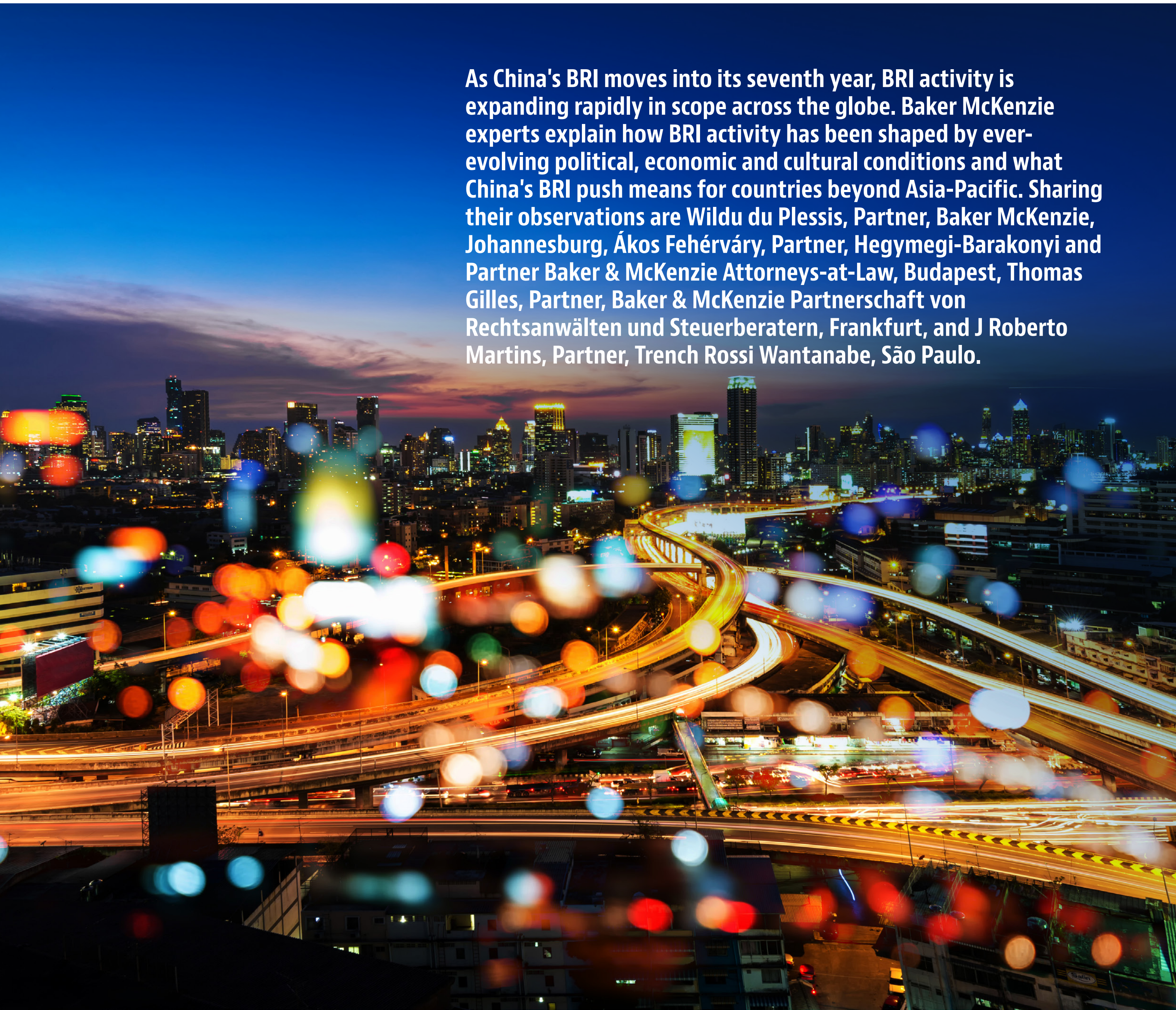
The Belt and Road Initiative

Cultural and geopolitical forces shape global BRI activity



As China's BRI moves into its seventh year, BRI activity is expanding rapidly in scope across the globe. Baker McKenzie experts explain how BRI activity has been shaped by ever-evolving political, economic and cultural conditions and what China's BRI push means for countries beyond Asia-Pacific. Sharing their observations are Wildu du Plessis, Partner, Baker McKenzie, Johannesburg, Ákos Fehérváry, Partner, Hegymegi-Barakonyi and Partner Baker & McKenzie Attorneys-at-Law, Budapest, Thomas Gilles, Partner, Baker & McKenzie Partnerschaft von Rechtsanwälten und Steuerberatern, Frankfurt, and J Roberto Martins, Partner, Trench Rossi Wantanabe, São Paulo.

What is the significance of BRI's expanding global reach beyond Asia?

While the direct impact of BRI varies throughout the world, its political and economic potential and significance is universally recognized.

Wildu du Plessis | Johannesburg, South Africa

BRI is a means to diversifying trade relationships and tap into Africa's vast potential.

BRI activity allows China to diversify its trade relationships with the world, and helps it to stabilize its foreign reserves by maintaining competitive export prices and building investor confidence towards China. On the ground, we see that Chinese policy banks are looking at Africa's potential through the lens of BRI. Over the last three years, Chinese companies have spent about USD 19 billion on energy and infrastructure projects in Africa. In order to keep up this momentum, it is important to think about how development finance institutions and state banks can boost BRI funding.

Ákos Fehérváry | Budapest, Hungary

Central and Eastern European countries welcome BRI activity to boost their economic growth.

The expanding reach of BRI shows that Europe understands China's role on the global stage. Countries in Central and Eastern Europe, especially Hungary, are still very much open to Chinese investment and BRI projects despite the rise of protectionist policies in the region. Their motivation is two-fold: some countries are keen to obtain the latest technology, while others need infrastructure development and welcome foreign investment as key support to their economic growth.

Thomas Gilles | Frankfurt, Germany

BRI is altering the global play of businesses.

Currently, we see individual European countries forming bilateral agreements with China on BRI in order to push for economic development or to capitalize on new business opportunities. However, as more countries in the EU region build such ties, it is possible that the European Union (EU) may develop a more united economic strategy towards Chinese BRI in the future.

BRI activity is gaining ground in Europe: to formally endorse BRI, some countries in the EU have signed a Memorandum of Understanding (MOU), or term sheet, with China. Notably, in 2019, Italy signed an MOU, showcasing that even one of the biggest and oldest European economies is open to China's BRI activity.

The sheer magnitude of the BRI as an initiative and as a strategy cannot be understated. Businesses want to become part of the BRI 'ecosystem' by being associated with the vast number of BRI-funded and BRI-branded projects throughout the world. There is reason to believe that China's BRI may eventually become so significant that it will involve the EU, which would undoubtedly further amplify the impact the BRI has on the global economy.

J Roberto Martins | São Paulo, Brazil

BRI is pioneering a new form of international dialogue.

With each new BRI project, countries are changing the way they do business. The very nature of BRI is constantly evolving, because there are efforts to reshape, adjust and improve the format of global cooperation. Increasingly, companies are using new knowledge, new processes and new alliances to build common ground and to start a dialogue with local governments to ensure that BRI investments provide meaningful returns for all parties.

While infrastructure projects have dominated BRI so far, what are some other trends we observe in Europe, Africa and Latin America?

While infrastructure projects dominate, real estate, energy, utilities, technology and Fast-Moving Consumer Goods (FCMG) are up-and-coming sectors.

Wildu du Plessis | Johannesburg, South Africa

BRI activities can help to unlock Africa's potential as a trade and business hub.

In Africa, we see a lot of investments in sectors like FMCG, healthcare, retail property and education. While BRI activity in these sectors cannot match the scale of infrastructure projects, these developments are still key because Africa is now a land of global opportunity. BRI projects and investments in Africa are really about unlocking the massive opportunity of establishing trade and business because Africa is one of the few remaining developing economies of the world. With the development on the Africa Continental Free Trade Agreement (AfCFTA), there are now bigger and broader opportunities to develop investments in services and other trade areas beyond infrastructure.

Ákos Fehérváry | Budapest, Hungary

Central Europe is experiencing an increased diversity of BRI activity.

Recently increased interest may be seen for renewable energy projects in Central Europe. Chinese investments have also recently expanded to other areas such as manufacturing, logistics and real estate.

While there isn't a huge volume of activity in this area yet — as compared with traditional infrastructure — there seems to be a shift in investment that will continue to interest China in the future.

J Roberto Martins | São Paulo, Brazil

Latin America is prime ground for investments in energy, power and possibly high technology.

A majority of Chinese investments in Latin America are in the energy and power sectors. For instance, China Three Gorges Corporation (CTG) has 60% of its overseas assets in Brazil and they have just acquired a power company several months ago.

This expansion of Chinese activity beyond infrastructure is definitely a trend which is motivated by three main factors. First, the BRI is a platform that showcases China's prowess and status as being the number one country in foreign trade. Second, BRI activity and investment are China's gateway to building significant global relationships; and third, the BRI further cements China's established role as one of the best countries at developing technology.

With BRI activity in Brazil, we see a two-step strategy for infrastructure developments. Investing in traditional infrastructure is the first step. For example, some Chinese companies have come to Latin America (to Brazil) and secured some energy assets, such as buying parts of the state grid, including thousands of kilometres of transmission lines.

The second step is to convert or upgrade these secured traditional infrastructure assets for high-end technology. That can open up a whole new dimension for BRI activity in the future.

Thomas Gilles | Frankfurt, Germany

Digital silk road activity is expanding the scope of BRI and raising company profiles.

BRI projects have the ability to raise business profiles because of the high visibility of BRI, all over the world. This is why more businesses want to be associated with BRI.

Many annual business plans or reports in Europe now include a section on China and China's BRI projects. This shows that businesses know they need to respond to both the actual and perceived importance of BRI and that they are beginning to think about BRI opportunities in the space of the digital silk road activities. Globally, we see BRI projects expanding to encompass digital silk road and industrial projects.

Find out how sustainability is a key part of the future of the BRI.
Read the full report here.

What are some necessary conditions to successful multilateral BRI projects in the future?

China emphasized that the new wave of BRI should be marked by increased collaboration and openness. Running BRI projects more smoothly in the future will depend on understanding regulatory policies, local conditions, effective project management in different cultures and geographies, and procuring funding from various sources.

Wildu du Plessis | Johannesburg, South Africa

Finding success in multilateral BRI projects in Africa depends on three main factors.

The first main factor of success is to have a stable regulatory environment or framework that can inspire investor confidence. China has a role to play in outlining clear regulatory policy for BRI investment and activity, which will boost confidence in partnering nations, foreign investors and global businesses. Clear and certain policy will reduce the perceived risks associated with BRI and smooth the path to success.

A second factor of success in multilateral BRI projects is the need for alternative financing structures beyond policy banks and development finance institutions (DFIs). Currently, China has a strong presence in the DFI arena, which has boosted BRI activity on a global scale. However, the role of commercial banks is crucial in bridging the funding gap for BRI. Active engagement between DFIs and commercial banks is needed to attract commercial banks to fund BRI projects. Such a collaboration can be facilitated by trusted advisors who can act as catalysts of coordination and cooperation between DFIs and commercial banks.

The third factor for success is having a thorough project preparation plan. This is essential in helping any BRI project to reach a bankable position. This happens when there is a successful cooperation between DFI, commercial bank and private equity funding. In Africa, for instance, savings can't be deployed because there isn't a uniform standard of sophisticated capital markets across the continent but there is a unique potential because there are a lot of private savings (access to private equity) that can and should be mobilized.

Ákos Fehérváry | Budapest, Hungary

All parties of multilateral BRI projects need to establish strong partnerships to mitigate risks.

Chinese companies look for trusted partnerships so they can familiarize themselves with the local regulations and conditions, including knowledge of the specific political and legal environment. Many Chinese companies engage in thorough preliminary research and analysis to build a good foundation for any joint BRI relationship.

Businesses in Europe need to understand nuances in mindset and culture of Chinese business, which allows for room to accommodate varying requirements and processes. For example, understanding the decision making and reporting structures in Chinese companies is important, particularly when collaborating with State Owned Enterprises (SOEs).

J Roberto Martins | São Paulo, Brazil

Localized knowledge of project management and funding matters, especially in Latin America.

Having local knowledge of the regulatory framework is absolutely essential to the success of BRI projects in Latin America, where managing projects is quite different than in other regions. One key example in Latin America is Brazil, which is an attractive market for BRI activity, accounting for 50% of the total Latin America market. As most of the infrastructure projects in Brazil are ordered based on a public tender process, incoming BRI investors will need strong knowledge of this public tender process. They would also benefit from localized knowledge on how to assess competition, submit proposals and manage the flow of processes in Brazil.

Another key area of local knowledge necessary to BRI investors relates to funding. In Latin America, procuring funds tends to be more problematic in bigger countries such as Brazil or Argentina, but easier in smaller economies like Chile, which tend to be more open to international banks.

It is also important to have an awareness of new opportunities in Latin America. In Brazil, until a few years ago, most projects were funded by the government. These days, public funding has become less readily available. This not only favors Chinese companies and BRI in general but also other investors who want to enter the market or strengthen their presence in the region.

BRI investors should consider looking for funding in capital markets, either through debt or equity. For Chinese investors, it is possible to look to the capital markets debt and to issue soft debt instruments. Given that capital markets in Latin American countries are relatively sophisticated, BRI companies will be able to access capital market issuance of bonds to fund BRI activity.

Thomas Gilles | Frankfurt, Germany

Thorough and careful project management will make for a successful BRI project.

Businesses that pay attention to the intricate needs of a multilateral BRI project will find that managing stakeholder needs is important. Even if a project is rooted in a BRI strategy, companies should tackle the project just as they would any other 'non-BRI' infrastructure project. This means that partner countries should adjust to and account for differences in culture, rules and standards in order to see the project completed.

Part of this vital project management will see companies allocate resources to managing organizational changes across the supply chain to improve efficiency. Such a strategy will strengthen their team's ability to manage expanding relations both within and beyond China.

Mitigating risks is an important part of successful BRI projects.
Read this *Asian Legal Business* article by Baker McKenzie experts.

How will BRI projects be affected by China's current focus on increasing transparency and sustainability?

The depth and breadth of BRI has great potential to further the worldwide agenda on sustainability.

Wildu du Plessis | Johannesburg, South Africa

Through the BRI, China will lend a lot of weight to how businesses think about sustainability.

It is absolutely inevitable that Environmental, Social and Corporate Governance (ESG) and sustainability will become increasingly important in BRI projects. Over the last ten years, ESG has grown in sophistication and importance. With China now being a leading voice driving this issue of sustainable finance, we can expect it to be a major area of focus for BRI activities. Chinese funders and investors are now becoming as focused on sustainability and ESG as any of their counterparts in the US or Western Europe.

Ákos Fehérváry | Budapest, Hungary

China's push for sustainability is good for the environment and for business.

China's commercial banks are now more active than before in issuing green credit for BRI projects. In fact, earlier this year, the Industrial and Commercial Bank of China (ICBC) issued the world's first green Belt & Road Inter-bank Regular Cooperation bond (BRBR bond), equivalent to USD 2.2 billion (denominated in three currencies: USD, Euro and RMB). This is a clear signal that sustainability is becoming more and more important for BRI. Considering the sheer scale and volume of BRI activity, this momentum represents great potential for China to further the sustainability agenda through its global BRI projects.

Thomas Gilles | Frankfurt, Germany

Sustainability and ESG will bring both disruption and opportunities for the BRI.

Without a global, standardized set of green investment principles or ESG playbook, sustainability and ESG have disrupted the stability of BRI activity. The lack of common standards mean that there are greater risks for companies seeking sustainable investment because lapses in ESG disclosures could threaten future procurement of funds.

However, China's emphasis on sustainability brings opportunities for economies and individual businesses to ramp up their efforts in addressing sustainability and ESG obligations through BRI activity. As more businesses become accustomed to ESG practices, the more familiar they will be with disclosures, reporting and documentation. Now, with the growing momentum of BRI activity in Europe, there is great potential for the sustainability and ESG agenda to be implemented far and wide.

J Roberto Martins | São Paulo, Brazil

The world of BRI business is inseparable from sustainability and ESG.

False reporting or incomplete ESG disclosures can jeopardize BRI projects. Such infractions can implicate any stakeholder involved in a BRI project, including lenders. This can complicate BRI projects for Chinese investors, because ESG represents a potential high-risk area in the project pipeline.

This is why many BRI companies now consider the bottom line alongside ESG matters, juggling the interests of many stakeholders beyond investors alone. This is particularly true in Latin America, especially in Brazil, where social licensing is important. In every project, affected communities need to be consulted for approval. They have to be heard as part of the licensing process as the social part of ESG.

Additionally, BRI projects need to implement safeguards around potential corruption. In the case of Latin America, this issue is emblematic in Brazil and other countries. BRI projects now have to face banks who are keen on making sure compliance checks are in place. There is also the need to comply with anti-bribery clauses. In lapsed cases when there is an issue, banks can then accelerate the whole debt. Such lapses needs to be avoided in BRI projects in order to keep costs low.

Want more resources to understand how the BRI impacts your business? **Visit Baker McKenzie's dedicated BRI hub today.**

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