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Belt and Road Initiative - Recent developments

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Introduction

In 2013, President Xi Jinping first introduced China's Belt and Road Initiative ("BRI") to the world.[1] It was seen as an endeavour to re-establish China's place at the centre of the economic and geopolitical arena. Yet, what first began as a project to revive the ancient silk road's prosperity by building a Silk Road Economic Belt (on land) in tandem with a 21st-Century Maritime Silk Road, has now expanded to include partner countries all over the globe with five major priorities: (i) policy coordination; (ii) infrastructure connectivity; (iii) unimpeded trade; (iv) financial integration; and (v) connecting people. Today, almost nine years into the launch of the BRI and given its ever-evolving and highly political nature, it remains difficult to draw a systematic assessment of the advantages, drawbacks, and achievements of the BRI. Yet, it is hard to ignore the profound impact of the BRI on partner countries, especially during the Covid-19 pandemic. In this regard, 2021 has been a year of transformation for the BRI with several adjustments performed by the Chinese authorities to maintain the sustainability of the initiative. Russia's aggression towards Ukraine will no doubt prompt further adjustments from BRI actors, although not directly by China itself, which remains unsurprisingly circumspect so far.

This article aims to address the BRI's development in 2021 (I) before considering future trends of BRI projects in the coming year (II).

I. BRI's development in 2021

Given the shadow that the Covid-19 pandemic has cast on the global economy during 2020-2021, BRI projects have not been immune to negative impacts of varying extents, depending on their location and type. Nevertheless, 2021 has also been marked by progress in the BRI as seen by the recent data available (A), as well as policy adjustments related to green energy reform and sustainable development (B).

(A) BRI progress in 2021: the data

According to China's Ministry of Commerce,[2] which published data on 24 January 2022 on China's investments and cooperation with its BRI partners for the year 2021,[3] non-financial direct investments across 57 BRI partner countries amounted to RMB 130.97 billion (approximately USD 20.3 billion), an increase of 1.7% compared to 2020. The steady increase in the amount of capital invested in BRI projects was not the direct result of more BRI projects being implemented, given that the value of new contracts entered into for construction projects for 2021 was reported to be RMB 864.76 billion (approximately USD 134.04 billion), down 11.4% from 2020.

Geographical focus

While there continues to be a significant number of new investment projects in East Asia,[4] there has also been an increasing focus on the development and financing of new BRI projects in African and Middle Eastern BRI partner countries in 2021.[5]

For example, Iraq has been a significant recipient of BRI investment in 2021.[6] In September 2021, CITIC Construction won the bid for the first and second phases of the construction of the Al Khairat heavy oil power plant in the Karbala province.[7] Each phase of the project is expected to be worth approximately USD 2.85 billion. CITIC Construction will lead the project as the EPC general contractor and is additionally involved in assisting the owner in obtaining financing for the project with the Iraqi government as guarantor.[8]

Other BRI energy projects in Iraq agreed in 2021 include the development of the Mansuriya gas field by Sinopec together with Iraq's Midland Oil Company as well as a 2 GW power PV project, currently in permission stage developed and owned by power Construction Corporation of China valued at USD 3.7 billion. Aside from energy projects, Chinese contractors have also been active in 2021 in the infrastructure space in Iraq, with four aviation-related construction projects reportedly worth USD 810 million, including the rebuilding of the Nasiryiah International Airport.[9]

Industry focus

In terms of industry focus of BRI projects[10], as to be expected the energy and transport sectors remain the focus of BRI projects in 2021 – eight out of the ten largest projects indexed by the CGIT with values ranging from USD 1.32 billion to USD 7.07 billion fall within these two categories. Within the transport sector, rail projects take the lead as a sub-category, with four out of the five of the largest BRI projects belonging to this sub-sector. As regards the energy sector, while oil remains the most important sub-category, 19 out of the 42 entries recorded by the CGIT are hydro and alternative energy projects – which accords with China's announcements of a shift of BRI investment towards renewable/sustainable energy projects.

(B) The BRI in 2021: policy changes

The BRI has also undergone some interesting policy shifts, such as the move towards a focus on green energy and sustainable development. Pursuant to the official guidelines dated 5 January 2022 and published the next day by the Chinese government (关于印发《对外投资合作建设项目生态环境保护指南》的通知) (the "Notice"), the twenty-five provisions of the guidance are aimed at promoting sustainable development, the green BRI concept, improving environmental protection and management in foreign investment projects, and providing a better level of service in new construction project opportunities.[11]

According to Article 3 of the Notice, companies either investing in or directly responsible for foreign investment projects should comply with ecological and environmental laws, regulations, and policy standards of the host state and, to the extent such standards are not available or relatively low, they are encouraged to adopt international common rules and standards or, if stricter, China's standards. The Notice then sets out the obligations and recommendations that companies are expected to take into account at each stage of their investment. At the pre-investment stage of a merger or acquisition, for example, Article 5 of the Notice recommends implementing due diligence to properly evaluate ecological and environmental risks of the target, while Article 6 sets out obligations for corresponding analysis of environmental impacts which are mandatory before a construction project commences. Such obligations are similarly provided for subsequent phases of a project, from implementation to operation and, finally, decommissioning or closure of the project.

Sector-specific guidelines have also been provided. For instance, Article 10 of the Notice requires companies to prioritise clean and green renewable energy projects over other types of energy projects. In relation to another key sector of BRI projects, transportation infrastructure, Article 13 of the Notice provides, for example, that

companies are to select routes and sites which minimise the environmental impact of the project and avoid nature reserves and important wildlife habitats.

II. Future trends / BRI in the next year

Next, investors will be keen to (A) ascertain the impact of recent geopolitical developments on the BRI before (B) considering the possible challenges that lie ahead for BRI projects and the parties involved.

(A) The BRI and Russia's aggression on Ukraine

China's stance in the first days of the conflict initiated by Russia's unprovoked invasion of Ukraine has been unsurprising: urging restraint on the ground and pleading for dialogue between the two countries. It has refused to back either side publicly, thereby walking on a tightrope given that Russia's aggression on Ukraine arguably runs afoul of China's traditional defence of state sovereignty and territorial integrity. Such appearance of neutrality can also be understood by the deep political economic ties Russia and China enjoy, and the fact that the BRI "ground" segment and corridors run through Russia and numerous former CIS countries (Azerbaijan, Uzbekistan and Kazakhstan).

The Russian government's war of aggression has brought about a new dimension to the relationship between China, Russia, and Ukraine. China cannot risk antagonising Russia for fear that all these projects may be derailed if Russia were minded to exercise its influence over its former satellite states; however, China also has significant economic ties with Ukraine and a sizeable population of Chinese nationals living in Ukraine (at least before the onset of the invasion).[12] Conversely, Russia cannot afford to lose China's unofficial support for fear of further isolating itself, especially in the light of the harsh sanctions that have been imposed on it by Western nations as a result of its invasion.

(B) Looking ahead – where do these developments take us?

The geopolitical events of this year, coupled with the gradual policy shift of the BRI in the past year towards greener energy and sustainable development, will have major consequences in terms of disputes relating to BRI projects or countries.

In relation to sustainable development, it is unclear the extent to which the Notice may make any real impact towards the nature and conduct of BRI projects. While the language of some of its provisions suggests that there is a positive obligation of compliance (the use of the word “要”, i.e., have to), in contrast with other provisions which are aspirational in nature (e.g., “尽量避免”, i.e., avoid as much as possible), there are no real means of enforcing such positive obligations provided in the Notice itself. Furthermore, although China was meant to have ended coal financing last year, in the first half of 2021 Chinese developers committed to an involvement in three new coal power plant projects in Bosnia, Indonesia and Vietnam respectively.[13] With recent reports this year of how the Chinese financing institutions will cease financing the planned Bosnian coal power plant,[14] such reversal of position in contravention of previously agreed deals may result in disputes arising between Chinese banks and/or companies and their counterparties in BRI partner countries.

Reports of other troubled transactions have also recently come to light. One flagship BRI project that has been under scrutiny is the financing, construction, and operation of the USD 3.8 billion Mombasa-Nairobi standard gauge railway in Kenya. In 2021, it was reported that Kenya had taken over operation of the railway from China Road and Bridge Corporation (“CRBC”), having become increasingly dissatisfied with the railway's operating costs.[15] The contract between Kenya Railways and CRBC has also been subject to litigation in Kenya on the grounds that the procurement process, which was not open to public tender, did not comply with Kenya's 2005 public procurement laws.[16] Another railway project which has run into difficulties in the past year is the Joydebpur-Ishwardi double-line project in Bangladesh, one of two major railway expansion projects in the

country. Although it was previously agreed during Xi's visit to Bangladesh in 2016 that this would be one of the several projects funded by China, in June 2021 it was reported that the Chinese would be pulling funding from the project.[17] Another BRI project that has generated significant attention is the development of the Doraleh Container Terminal and the Port/Free Trade Zone in Djibouti. Indeed, it has given rise to several arbitrations worth hundreds of millions of dollars and has spun off litigation in a number of jurisdictions.[18] Recently, in January 2022, the Hong Kong Court of Appeal finally handed down its ruling in relation to the ongoing litigation in Hong Kong commenced by DP World against China Merchants Port Holdings Company Limited ("**China Merchants**") regarding the latter's negotiations and dealings with the Djibouti government for the development of this project, citing *inter alia* a breach of Djibouti's New Civil Code and, alternatively, unfair competition.[19] The Court of Appeal dismissed China Merchants' appeal for the matter to be heard in Djibouti instead of Hong Kong, agreeing with the lower court that China Merchants has not discharged its burden of proof of showing the Djibouti Court to be clearly or distinctly more appropriate as the forum for trial notwithstanding the fact that Djibouti law is the governing law of the claims.[20] These examples of troubled transactions are evidence of the challenge faced by both Chinese contractors and their foreign counterparties when navigating such complex projects involving multiple parties, state and private, over an extended period of time.

Regarding the Russian aggression in Ukraine, the sanctions exercised by the US, the EU and their allies may have had an indirect adverse impact on Chinese companies dealing with both Russian counterparties and EU/US counterparties. In practice, Chinese companies seeking to continue doing business in sanctioning countries may have to, like their EU/US counterparts, stop collaborating on Russian projects to avoid the bite of such sanctions. Such decisions halting business operations in the relevant countries will undoubtedly bring a wave of contract terminations, specific performance claims and *force majeure* and/or hardship notices under the relevant applicable laws.

Ukraine itself also participates in the BRI and multiple Chinese-backed projects and investments have already been implemented in the country.[21] In this regard, the Russian invasion would have caused and continue to cause (i) work stoppages (due to the destruction of sites or employee evacuations); (ii) partial or total disruption of supply chains relevant to BRI projects (with additional costs and delays being borne and disputes as to the liability for these costs arising); and/or (iii) disruption to existing supply contracts for natural resources (with disputes arising also over indexation issues).

Conclusion

In 2021, BRI projects have mostly continued to progress, with growth recovering after the Covid-19 pandemic which brought the world economy to a standstill. The policy shift towards clean and green energy and construction projects has also presented new challenges to BRI actors to adapt their participation in existing and new BRI projects.

However, while the war in Ukraine continues, uncertainties surrounding energy security will deepen. In the circumstance, and if China continues to maintain a somewhat neutral position on the conflict, economic ties between China and Russia could increase as sanctions driven by the West narrow Russian companies' options for economic partnership.

In practice, in 2022, this means that BRI investors will need to focus on:

- Understanding the impact of Ukraine sanctions on their existing commercial and contractual relationships;
- Protecting their contractual rights in existing projects by securing communications and carefully monitoring and documenting any change in their ability to perform their obligations given changed

circumstances; and

- Ensuring that due consideration is given to (i) force majeure and/or hardship clauses; and (ii) dispute resolution mechanisms when concluding any new contracts that may be impacted by the recent developments.

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