



# HOW BELT AND ROAD FITS IN TO THE OVERALL GEO-POLITICAL PICTURE; ESPECIALLY RISKS AND OPPORTUNITIES



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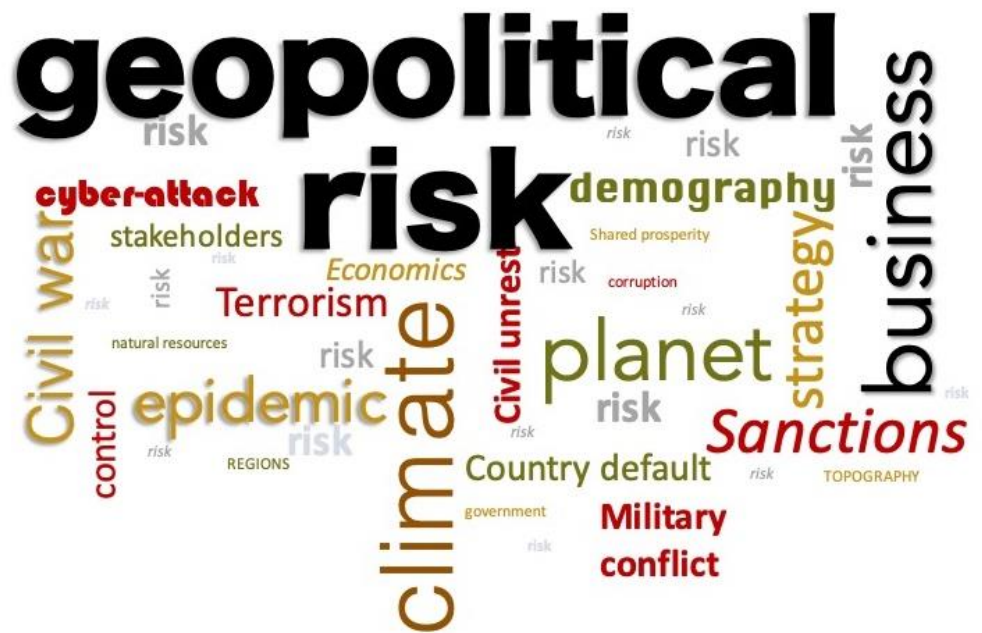


## Introduction

The Belt and Road initiative (BRI) has the potential to deliver unparalleled benefits across the globe. However, realising the opportunities means understanding the risks and designing appropriate strategy to mitigate them. This article considers how Belt and Road fits in to the overall geo-political picture, highlighting the risks and opportunities which companies, whether state owned, multinational or privately owned, need to take account of if they are to navigate that road successfully and, above all, protect value.

## What is Meant by Geopolitics and Geopolitical Risk?

If geo-politics is the study of the influence of such factors as history, geography, economics and demography on policy, particularly on state policy, then geopolitical risks are first and foremost those stemming from the interaction of political entities in the international arena. But the scope is much wider than that and includes other risks such as: military conflict, civil war, terrorism, civil unrest, cyber-attack, the impact of sanctions, country default, epidemics, energy security, climate change - the list could go on. The point is, risks cannot be looked at in isolation. Rather they need to be fully understood as part of an integrated risk assessment which considers how risks are inter-related.



## Four Key Contemporary Geopolitical Themes

### The global landscape is increasingly fragile



...and as a result, susceptible to short-term behaviour by corporations and governments alike. Market uncertainty is pervasive, and confidence is deteriorating, while many see increased risks of cyclical downturn. Globally, but particularly in the West, frustration with years of stagnant wages, the effect of technology on jobs and uncertainty about the future have fuelled popular anger, nationalism and xenophobia.

In response, some of the world's leading democracies have descended into deep political dysfunction which has exacerbated, rather than quelled, this public frustration. Unequal societies are polarizing. The paradox is that while

we have seen historic reductions in poverty, the social contracts that have held society together in many countries are fraying. For some this has been an era of unparalleled resources and technological advancement but for many it has been a time of increasing insecurity.

### Trust in international and official institutions is crumbling



...and the rules-based international order is under threat as it has not been for seven decades. At the same time, the global security environment remains in fluid transition, addressing insecurity associated with the perception of unsolvable challenges. Add to that the populism represented by Trump, Brexit and the success of disruptive nationalist parties in a number of countries and that fluidity is now a roller coaster in which old certainties are rapidly being consigned to the dustbin.

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## The sun is setting on 400 years of a European, or western, centric world



... a fact which will prove to be increasingly uncomfortable for those states which have been top dog under the old order. The fact is that the economic centre of gravity is shifting from the West to Asia, while the balance of power is moving as America retreats from global leadership and China expands its influence. This re-emergence of China as a regional and global player poses profound challenges which will impact on perceptions of the BRI and require careful management.

## Environmental issues



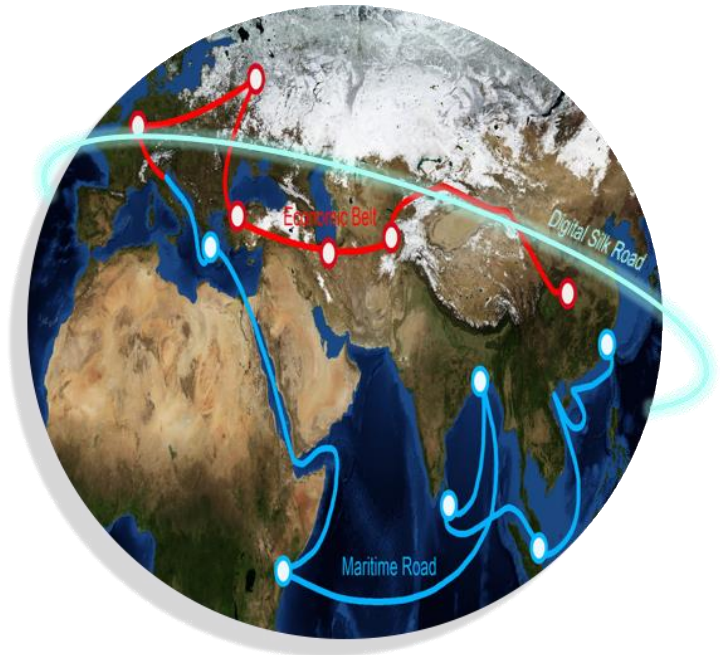
... particularly climate change, pose an increasingly existential risk, if not to humanity, then almost certainly to the way we live now. The UN's intergovernmental panel on climate change recent report stated that if global warming is to be limited to 1.5 degrees centigrade by 2030, man-made greenhouse gas emissions need to start falling immediately. This puts environmental/social/governance (ESG) risks absolutely front and centre of any strategy for risk management. It also, paradoxically, presents opportunities for BRI.

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## Is BRI the Game Changer of the 21st Century?

BRI is a fundamental piece in the global geopolitical jigsaw. Given the scale, ambition, investment needed and geographical scope of the project, it is difficult to see it any other way. The facts speak for themselves: a requirement for over US \$1 trillion in investments, largely in infrastructure development for ports, roads, railways and airports, as well as power plants and telecommunications networks. And a geographical scope which covers over 70 countries, accounting for about 65 per cent of the world's population and around one-third of the world's GDP. The scale is staggering. And herein lie its risks and opportunities.



## Fundamental risks of BRI

The most immediate risk BRI faces is right here in Hong Kong. The fact is, what we are witnessing on our TV screens is raising real questions about the **stability of Hong Kong**, the survival of 'one country/two systems' and Hong Kong's viability as the conduit for international investment in BRI. Clearly the current situation cannot go on and law and order must be restored peacefully if business confidence is to be maintained.

The consequences of China's rise to global power is that, like it or not, BRI is also seen in some quarters as a **means of establishing Chinese hegemony**. Brutally put, BRI is now being cited by critics as an example of debt-trap diplomacy in which China gains influence overseas by bankrupting its partners and bending them to its will. A number of countries



have already expressed their concerns at the risks of unmanageable debt as a result of Chinese financial support for BRI projects: Malaysia, Montenegro, Sri Lanka, Pakistan, Myanmar, Nepal, Ethiopia, Djibouti are all examples of this.

That BRI has got itself into this position is a measure of the extent to which risk has not been understood and the necessary risk mitigation strategies not put in place. So the final risk to highlight is that of not understanding risk in an integrated manner: whether political, security, social or cultural – and not linking risk and strategy.

One size does not fit all and however welcome Chinese money may be, importing Chinese labour, construction material to build, for example, a highway from Montenegro's port of Kotor on the Adriatic sea toward Serbia has sent a very negative message about BRI and demonstrates a failure to understand the cultural dynamics of a small, proud Balkan nation. Similarly, BRI made few friends in 2017 when Sri Lanka was forced to hand over the port of Hambantota on a 99 year lease to Chinese firms as part of a \$1bn debt repayment. And there are other examples.

## Key Opportunities of BRI

In the past five years BRI has moved a long way from its original concept as a massive infrastructure project connecting Asia, Europe and Africa. **It has transformed a substantive part of the developing world** and gained **greater traction globally** with Italy the first G7 country, and the 130<sup>th</sup> country overall, to sign up to it.

While returns on investment are probably better seen over 10-15 years, there have been **clear short-term benefits** that have boosted host country economies and benefitted both the Chinese and international companies involved, particularly in construction. Longer term, BRI's potential remains strong so international companies considering investing should take comfort from the Chinese leadership's recent call for higher quality development of BRI, together with recent direction from the Chinese government calling for standardized funding sources, improved risk management and better guidance on financing. **Hong Kong's opportunity lies in acting as the super connector** for Chinese banks looking for partnerships with international lenders to improve financial governance and manage debt and investment risk.

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If it is to be effective, this focus on **better quality and viability** to attract international funding must be backed with **effective risk management** and **improved project planning** and preparation, both of which require **effective independent, third party assurance** that the risks posed by a particular project are understood and that strategy is in place to manage those risks. **China cannot mark its own BRI homework and**, if it is to cultivate greater international participation in funding and development projects, will need independent and experienced risk experts able to reassure international funders and companies that the risks of investing in BRI are manageable and will generate long term returns.

This needs **deep desk-based analysis, together with ‘boots on the ground’ assessment** by experienced professionals really capable of getting under the skin of a country, company or project. **Risks need to be assessed at the international, national and local level.** Too often, what is going on in a specific province or region can bear little relation to what might be happening at a national level. In a word: **China should be looking for ‘best in class’ international risk management.**

The essence of this approach is **shared prosperity**. Stakeholders, whether regionally, nationally or locally need to feel that they will benefit from a project. People have to buy in to BRI rather than feel that by hosting a BRI project they might end up with an unsustainable debt. This needs a nuanced approach based on a detailed understanding of local culture and attitudes.



In strategic terms, BRI needs to be less global grand gesture with a Chinese flag on top of it and more an indirect, nuanced approach which takes account of the specific risks, together with the developmental needs and aspirations of partner countries and communities. Such an approach is more likely to reassure international companies that lessons have been learned from some of the negative experiences of BRI and dispel perceptions that it is about Chinese influence-projection and hegemony. **Soft power, leading from behind and winning hearts and minds should be the watchwords.**

In this context, it should be noted that Zhou Xiafei, deputy secretary general of China's national development and reform commission, has said that BRI projects would benefit from involvement by international professional services in order to help multinational companies and Chinese state-owned enterprises navigate the cultural, regulatory and other challenges in BRI countries. He is right.

## Climate Change: an opportunity?

As unlikely as it seems, it is possible that one of the greatest opportunities for the BRI may be created by the risk of climate change. While the balance of power may be shifting from the West to Asia, getting buy-in to BRI from international companies means that China, and those seeking Western investment, must understand and take account of Western perceptions, particularly the increasing importance placed on managing Environmental, Social and Governance risks (ESG) by Western investors. Of course, this focus is not the prerogative of Western companies. For example, the exemplary approach taken by Royal Golden Eagle, the Indonesian-led group of world-class companies specialising in resource-based manufacturing, whose ethos is founded on 'what is good for community, country, climate, customer and company'. However, BRI should note the letter Larry Fink, CEO of Blackrock, the world's largest asset manager with \$6.84 trillion in assets under management as of June 2019, in which he told CEOs of companies Blackrock invest in that:





*'companies that fulfil their purpose and responsibilities to stakeholders reap rewards over the long-term. Companies that ignore them stumble and fail. This dynamic is becoming increasingly apparent as the public holds companies to more exacting standards. And it will continue to accelerate as millennials – who today represent 35 percent of the workforce – express new expectations of the companies they work for, buy from, and invest in...'*

The message is clear: if BRI projects are to attract investment from international investors, they must demonstrate, unequivocally, their ESG credentials. And this requires effective strategy for managing ESG project risk.

## Conclusion

The BRI could be China's opportunity to demonstrate its environmental leadership credentials to the world. While much of the rest of the world prevaricates over the measures needed to control global warming, perhaps only China has the will, determination and means to demonstrate the bold action needed to prevent catastrophe. After all, in the last two decades China has proved itself capable of exponentially rapid economic growth and of building massive infrastructure projects with extraordinary speed and dynamism. Could China be the global power in the 21<sup>st</sup> century capable of giving the world the lead it needs to save the planet? And could BRI be the catalyst?



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