**China’s Belt and Road Initiative:**

**Analyzing the Economic Feasibility of Brownfield vs. Greenfield Investments**

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1. **Introduction**

In an astonishing rapidity, China has transformed from a non-industrialized nation to the global leader in manufacturing and exports. The country’s drastic metamorphosis is widely attributed to former president Deng Xiaoping’s modernization and economic reform efforts which shifted the Chinese economy into its current socialist market model. Beginning in 1978, foreign direct investment (FDI) began flowing into the country as a result of Deng Xiaoping’s Open Door Policy that incentivized foreign investment and technological advancement.[[1]](#footnote-1) FDI encapsulates all international equity holdings in which the owner has considerable control and influence over the asset.[[2]](#footnote-2) Over the past four decades, China has accumulated more than $3 trillion in FDI and continues to be one of the largest recipients of international investment.[[3]](#footnote-3) Although still considered to be a developing country with an emerging market, China is attractive to foreign investors due to components such as a large labor force and growing middle class that will fuel further economic growth.

Compared to FDI, Chinese outward direct investment (ODI) initiatives followed a much slower growth trajectory for the first twenty years due to a capital shortage and demand for internal domestic development. In 1999 however, China shifted its economy following former president Jiang Zemin’s Go Out policy that encouraged state-owned enterprises (SOEs) to acquire assets abroad in hopes of developing successful SOEs into transnational corporations.[[4]](#footnote-4) Additionally, China’s new membership in the World Trade Organization further propelled its model of economic liberalization.[[5]](#footnote-5) Chinese ODI accelerated throughout the following decade, exhibiting an astonishing annual growth rate of 55% from 2003 to 2009.[[6]](#footnote-6) The vast majority of Chinese ODI flowed into developing economies, although China also significantly increased its investment into developed countries with the intent to attain technological advancement and market expansion.[[7]](#footnote-7) For example, with numerous enterprises in developed countries struggling in the face of the Great Recession, Chinese enterprises swooped in to capitalize on the economic opportunity. While FDI inflows around the world plummeted by 14% in 2008, China’s ODI doubled from $26.5 billion to $55.9 billion.[[8]](#footnote-8) These trends are indicative of a structural shift in China’s economic development model from a country that historically was a large recipient of inbound investment to a country that now contributes large sums of diversified investment internationally.

Xi Jinping’s rise to presidency in late 2012 began the shift to a new outlook on China’s international presence. Branded as the “China Dream,” the president touted his vision of China’s prospective position as a leading world power by 2049.[[9]](#footnote-9) President Xi’s anticipation demonstrates departure from the strategies of China’s former leaders, who conventionally followed Deng Xiaoping’s “bide and hide” strategy, under which China adopted unobtrusive foreign policies, rather than attempting to take the lead in international affairs.[[10]](#footnote-10) Contrary to previous president Hu Juntao’s “Peaceful Rise” vision in which China would be a practical but compliant member of the global community, President Xi Jinping has assumed a more disruptive perspective of China’s position, which is contingent upon the assertion of China’s leadership in developing economies and ability to stay on the forefront of technology.

Under Xi Jinping’s leadership, Chinese ODI continued to climb. By 2016, China became the second-largest international investor in the world. In the same year however, Chinese government officials began restricting ODI due to diminishing foreign reserves and a weakening renminbi.[[11]](#footnote-11) Although this affected all Chinese enterprises, POEs were especially disadvantaged by the credit ceilings of the government’s new regulations.[[12]](#footnote-12) Furthermore, Western countries have begun establishing stricter screening procedures and higher regulatory barriers for accepting Chinese investments, thus threatening China’s strategic overseas investment in developed countries.[[13]](#footnote-13) Chinese ODI flows into the United States and Europe both dropped by almost 60% in 2018 as a result of the protectionist policies enacted by both the investing and recipient nations.[[14]](#footnote-14) These hurdles for Chinese ODI investment will likely challenge China’s future economic influence in developed countries.

China’s investment trends reflect the unique inclination of recent emerging markets to employ ODI in order to acquire strategic assets and opportunities. Chinese ODI flow into developed economies were traditionally made in order to expand on technology development or knowledge of advanced manufacturing methods which are currently lacking domestically.[[15]](#footnote-15) Under this method, China utilized international expansion in order to compensate for competitive disadvantages of its traditional existence as a market outsider in the global economy. On the other hand, China’s investment in other developing economies allows for the application of its own competitive advantages internationally. For example, several Chinese enterprises have invested in underdeveloped countries of Southeast Asia in order to leverage their cost-effective manufacturing and maximize production abilities.[[16]](#footnote-16) Furthermore, international investments in developing countries allow for China to extract valuable natural resources such as minerals, metals, and energy sources.[[17]](#footnote-17) In obtaining new assets and opportunities through international expansion, China aims to bolster domestic economic and social development in order to compete in an increasingly globalized world.

Brownfield and greenfield investments are often used by corporations that seek to broaden their international reach through FDI in other countries. These multinational corporations generally purchase, lease, or build new facilities, such as factory plants and office spaces, abroad. The greenfield ODI strategy emphasizes the construction of a new venture from the ground up. While there are several benefits to the greenfield expansion model, such as design flexibility and the ability to cater to the unmet needs of the targeted customer segment, there are often also higher costs and risks involved. For example, new greenfield developments do not have the guarantee of consistent, proven market demand. In contrast, brownfield expansion refers to an investment in which a corporation chooses to purchase an existing facility, rather than creating a new one. While adjustments will likely need to be made in order to cater to the host company’s needs, the process is much more efficient, as the company will not need to spend as much money or time in developmental planning or getting bureaucratic approval for necessities such as zoning permits and paperwork. In exchange for business expansion, the foreign country receiving the FDI benefits from the increase in labor demand and economic competitiveness.[[18]](#footnote-18)

Although the discussion of strategic brownfield and greenfield models typically pertain to the private sector, this investment framework can be applied when evaluating the success of China’s ODI, which is typically dominated by state-owned enterprises (SOEs), rather than privately-owned enterprises (POEs). As China has continued to strengthen its international presence primarily through investments in other developing countries, it has adopted ambitious methods such as the vast-spanning Belt and Road Initiative (BRI). Announced by President Xi Jinping in 2013, the Belt and Road Initiative is a strategic bilateral development plan that seeks to foster connectivity through the development of infrastructure and linkage of land, sea, and air routes across 70 countries in Asia, Europe, and Africa.[[19]](#footnote-19) While this global project was promoted by the Chinese government as being mutually beneficial, the actual results have proved to be controversial.

Ultimately, this paper examines the pitfalls and potential risks raised by inconsistencies of the Belt and Road Initiative (BRI). Through exploring the historical economic development of China through ODI, this paper will challenge the classification of the BRI as a traditional ODI project as it does not fall under conventional international investment methods. Instead, this paper asserts that the BRI embodies a hybrid development model attempting to maximize both profitability and political reach that is largely synergetic to China’s strategic transition into a global leader and economic superpower. Utilizing this theory, the effectiveness of greenfield vs. brownfield development strategies will be applied in order to contrast the failure of the Port of Hambantota in Sri Lanka with the success of Port Piraeus in Greece. Through these BRI case studies, the conclusion is drawn that brownfield investments with a successful track record are more effective than new greenfield developments in areas where consumer demand remains uncertain.

1. **The Belt and Road Initiative (BRI)**

In September 2013, President Xi unveiled the audacious strategy of building a “New Silk Road Economic Belt” that aimed to connect China with a wide host of countries across Europe and Asia. Throughout the coming months, the president would expand his bilateral Belt and Road Initiative to also include a “21st century Maritime Silk Road” that would create shipping routes connecting to ports in Asia, Europe, and Africa.[[20]](#footnote-20) According to President Xi, the goal of the BRI is to coordinate economic development strategies, amplify market potential through regional infrastructure development, increase local labor demand and jobs, and encourage cultural understanding in participating countries.[[21]](#footnote-21) The proposed area of this “New Silk Road” was to cover over 70% of the world’s population, 55% of global gross national product, and 75% of known energy reserves.[[22]](#footnote-22) If successfully implemented, economic corridors and shipping routes created by the BRI could benefit millions of individuals living within its vicinity, particularly in developing economies where large infrastructure gaps were present. Moreover, the foundational establishment of new infrastructure could initiate a positive feedback loop for foreign investment in underdeveloped BRI recipient countries, under which initial infrastructure will enhance the investment prospects and in turn, attract greater FDI inflows.[[23]](#footnote-23)

Since the announcement of the BRI, the construction of several bilateral and regional land, sea, and air transportation projects have commenced in order to foster cross-border economic connectivity. By the end of 2018, China had signed sea transport agreements with over 47 countries and has contributed in building 42 ports in 34 different countries, including Port of Hambantota in Sri Lanka and Port Piraeus in Greece. Similarly, the Chinese have participated in the construction of several international railways and bridges across Europe, Asia, and Africa. In addition, China had expanded air routes to offer air transport services to over 40 countries across the BRI route.[[24]](#footnote-24) In order to finance these large infrastructure projects, Chinese SOEs and private enterprises draw from a variety of different funds including the Asian Infrastructure and Investment Bank (AIIB), the Silk Road Fund, the BRICs New Development Bank (NDB), and the Shanghai Cooperation Organization (SCO).[[25]](#footnote-25) While previous ODI projects were carried out on an ad hoc basis, new construction proposals that are branded as BRI projects are much likelier to reap the benefits of support from the Chinese government through perks such as cheap financing options.[[26]](#footnote-26)

1. **BRI Controversies and Concerns**

Despite the immense promise of China’s monumental project, several concerns have arisen regarding the structural layout of the BRI. Chinese officials have denied that the BRI has a political agenda; however, it is worthy of noting the geopolitical concerns. The majority of financing for BRI projects are sourced by Chinese loans to the recipient countries, rather than grants. Although President Xi emphasized that the BRI is founded on the grounds of “mutual trust, equality, inclusiveness and mutual learning, and win-win cooperation,”[[27]](#footnote-27) there is considerable apprehension about China’s true motive in the costly infrastructure development projects. The majority of countries that have signed onto BRI agreements are developing economies with smaller markets. The risk of debt default is significantly more likely when these underdeveloped economies are issued loans that have a high debt-to-GDP ratio.[[28]](#footnote-28) Critics contend that the BRI is an instrument for China’s “debt-trap diplomacy” practice in which the BRI countries that fail to pay off large Chinese loans are forced to cede land or pass policies that are favorable to China in order to recuperate losses. [[29]](#footnote-29)

Although strategic underlying geopolitical motives are certainly present in the BRI, this focus is greatly overstated by foreign observers. There appears to be few geographic restraints on BRI membership, challenging the claims that strategic geopolitical expansion is China’s main motive for the Belt and Road Initiative. Although there has been a great deal of Chinese propaganda pushing forth this monumental global project, the specific details are unclear. President Xi has emphasized abstract goals such as policy coordination, economic and cultural connectivity, and financial integration, yet has failed to produce a concrete plan for project targets. Furthermore, Chinese reports claim that more than one hundred countries belong to BRI, but these loose agreements are often informal and subject to change.[[30]](#footnote-30) It is often difficult to distinguish between BRI projects and regular ODI initiatives, due to the lack of transparency surrounding bilateral deals. With no explicit definition beyond vague objectives, the BRI has become a blanket term used by the Chinese government which encapsulates general Chinese financing, investment, and construction projects abroad.

Thus, while the BRI has been branded as a Chinese ODI initiative, upon closer examination, it actually resembles a hybrid model in which the Chinese state seeks to combine high profitability and geopolitical motivation into a single policy. Typically, enterprises that seek to expand globally secure one of three types of financial support that vary in which the funding prioritizes the orientation between strategic national interests and market profits. While commercial finance aims to make profit, policy-based finance seeks to support national strategies without regard to conventional market principles or profitability. Developmental finance attempts to strike a sustainable blend of both financing options and promotes the national interest while breaking even or maintaining a slim profit margin on the project.[[31]](#footnote-31) In contrast, the BRI attempts to maximize profits while bolstering China’s international presence as part of President Xi’s “China Dream” political vision. While seeking to obtain both components, the results of this hybrid financing model have proven to be varied, as demonstrated in the case studies of the Port of Hambantota and the Port of Piraeus.

1. **Port of Hambantota**

The construction of the Sri Lankan Port of Hambantota began in 2008, with the first phase of the port opening in 2010. The Export-Import Bank of the People’s Republic of China (EXIM) funded 85% of the first phase configuration, which in total cost $361 million.[[32]](#footnote-32) Upon completion, the Port of Hambantota was originally expected to be the largest maritime port in the world. Located in the important access point to the Indian Ocean, Sri Lanka intercepts a strategically critical shipping lane that is one of the busiest global trade routes in the world, with 64% of global trade passing through.[[33]](#footnote-33) The Port of Hambantota had large promise due to its geographic location, and expectations were high for the construction of this maritime port.

However, the results of phase one proved to be disappointing, with extremely low throughput that did not justify the large quantities of Chinese capital that had been poured into the port’s construction. The majority of cargo ships passing Sri Lanka chose to dock at the nearby port in Colombo instead; while 3,667 ships berthed at the Port of Colombo in 2012, the Port of Hambantota only attracted 34 ships.[[34]](#footnote-34) In 2016, the Port of Hambantota was still failing to be profitable, only bringing in $11.8 million of revenue with a pre-tax operating profit of $1 million. In the same year, Sri Lanka’s foreign debt climbed to $25.3 billion.[[35]](#footnote-35) In response to this debt burden, Sri Lanka signed a 99-year lease in 2017 to operate the Port of Hambantota as a Private-Public Partnership (PPP) initiative with China Merchants Port Holdings Company Limited (CM Port) for $1.1 billion. This agreement granted a 70% majority stake ownership of the Port of Hambantota and 15,000 acres of surrounding land that is being converted into an industrial zone that aims to increase traffic through the port.[[36]](#footnote-36) The remaining 30% ownership stake remained in the commercial control of the Sri Lanka Ports Authority (SLPA) with the government of Sri Lanka retaining overall port ownership.[[37]](#footnote-37) It is important to note that this is not a debt-equity swap in which China cancels Sri Lanka’s debt in exchange for the port. The lease deal is completely separate and independent of the EXIM Bank loans that Sri Lanka’s government is still working to pay off.[[38]](#footnote-38) Furthermore, while EXIM Bank invested in the initial development of the Port of Hambantota for the political reason of progressing President Xi’s BRI plans, the CM Port’s involvement in the port’s lease is evidently commercial. If CM Port can rework the port so that it becomes profitable, this Chinese partial-SOE will reap most of the benefits from the additional development.

In the media, the failure of the Port of Hambantota project is most often referenced in speculating about the hidden geopolitical motives of the BRI and the failure of China to maintain its promises of equity and mutual beneficiality in its global infrastructure development. Following the 99-year lease agreement, there was speculation in the international community of China’s intentions to establish a military base in the Port of Hambantota. However, those fears were quelled by Sri Lankan public officials who rejected the theories, including Prime Minister Ranil Wickremesinghe and the Chief of Defense Staff Shavendra Silva. As Wickremesingh asserted in August 2017, “Sri Lanka headed by President Maithripala Sirisena does not enter into military alliances with any country or make our bases available to foreign countries.”[[39]](#footnote-39) Therefore, the precedent set by these government officials refute the argument that Hambantota will become a strategic location for Chinese military deployment.

In addition, the high interest rates of commercial loans granted by China’s EXIM Bank in the initial phase one construction of the Port of Hambantota are often cited to support the argument of China’s “debt trap diplomacy” tactics. Contrary to the popular narrative however, only two of the five received by the Sri Lankan government were obtained as commercial loans that had interest rates ranging as high as 6%. The majority of China’s $1.3 billion loans were concessionary; meanwhile, the two commercial loans only amounted to $357 million collectively.[[40]](#footnote-40) Out of the $55 billion of debt that Sri Lanka had amassed, only 11% were Chinese loans from infrastructure projects and the Chinese loans granted for the construction costs of the Port of Hambantota amounted to less than 5% of total foreign debt that Sri Lanka was expected to repay.[[41]](#footnote-41) These statistics challenge the accusations of the Port of Hambantota being a debt-trap instrument used by China in order to accumulate greater geopolitical power. Sri Lanka’s foreign debt distress is more reflective of the poor financial decision of former president Mahinda Rajapaksa’s government to accept any foreign loans with high interest rates during a period in which the country urgently required fiscal consolidation instead.

On a larger scale, the failure of Port of Hambantota indicates the pitfalls of the Chinese greenfield development strategy when attempting to both maximize profitability and fulfill President Xi’s amorphous BRI goals. Although the evidence does prove definite geopolitical motives, such as China’s desire to avoid the Strait of Malacca choke point, the inability of the Port of Hambantota to achieve its projected success is much more representative of the Chinese government’s failure to conduct proper due diligence when approving the construction of new BRI projects. Building a port in Hambantota had been part of the Sri Lankan government’s development plan since 2002. Elected in 2005, former president Mahinda Rajapaksa had made promises to develop Sri Lanka’s southern region, including his hometown of Hambantota.[[42]](#footnote-42) Both Rajapaksa and Chinese developers ignored the fact that the Port of Colombo, Sri Lanka’s biggest port which was located just 150 miles away and handled 95% of the country’s international trade, had not reached its handling capacity. Much of the Port of Hambantota’s services overlapped the existing amenities that were already offered by the Port of Colombo. Furthermore, EXIM Bank was the only institution that made an offer to fund the construction of the Port of Hambantota, indicating that other potential investors did not see the benefits outweighing the large risks in this port project.[[43]](#footnote-43) The 99-year lease of the Port of Hambantota to CM Port, the largest port operator in China, represents a last-ditch effort for China to transform this failed BRI infrastructure project into a profitable venture. On top of the $1.2 billion lease payment, CM Port is expecting to spend another $700-800 million on development in order to bring the port to full capacity operational level.[[44]](#footnote-44) The huge cost of this additional development highlights the unexpected difficulty in scaling up new infrastructure in attempts to create a market that is currently lacking. Thus, it was clear that there was lacking demand for a new Port in Hambantota, yet China’s focus on commencing on commencing greenfield development as quickly as possible to establish the feasibility of President Xi’s BRI and “China Dream” vision were based on faulty, unproven ideals that overlooked the reality of Hambantota, Sri Lanka.

1. **Port of Piraeus**

The acquisition of the Port of Piraeus by the Chinese shipping and logistics SOE, China Ocean Shipping Company (COSCO), reflected China’s ODI strategy of investing in existing infrastructure in developed countries that were discounted as a result of the global financial crisis. In the midst of Greece’s government-debt crisis in 2009, the Greek government agreed to lease two container terminals of the Port of Piraeus to COSCO for 35 years. Although there was protest and concern over the labor conditions under Chinese supervision, the Port of Piraeus continued its growth and development as a critical distribution center and transhipment hub in Europe and the Mediterranean. Economic performance and productivity at the Port of Piraeus drastically improved under COSCO operations; the cargo volume passing through Chinese operated port terminals tripled in 2012, merely three years after the initial lease was signed. By 2014, the Port of Piraeus became the fastest growing container port in the world.[[45]](#footnote-45) Since COSCO purchased 51% majority stake ownership of the Port of Piraeus in 2016, the port’s gross profit has more than doubled to nearly $80 million, undergoing a dramatic 128% growth in just three years.**[[46]](#footnote-46)** COSCO has continued to push ahead on the project, with future plans to turn the Port of Piraeus into Europe’s biggest commercial port.

While COSCO has greatly contributed in amplifying efficiency and economic productivity, the massive success and promising profits that have been accumulated through China’s investment in the Port of Piraeus cannot solely be attributed to COSCO’s involvement. Prior to Chinese engagement, the Port of Piraeus was already a long established and reputable port. Before the financial shock of the Great Recession was fully felt by the global supply chain, the Port of Piraeus reported its gross profits in 2007 to be $48.5 million, the port’s all-time high after consistent year-on-year growth.[[47]](#footnote-47) It is clear that the Port of Piraeus demonstrated consistent historical performance and would be a secure investment choice. The successful case of Chinese investment in the Greek Port of Piraeus demonstrates the effectiveness of brownfield acquisitions for such a large infrastructure project such as the BRI. These brownfield investments often have a proven track record of profitability and market demand and additional Chinese BRI capital can be utilized to further strengthen and enhance these operations while progressing President Xi’s BRI objectives in a practical and sustainable way.

1. **Conclusion**

Through contrasting two completed BRI projects, Sri Lankan Port of Hambantota with the Greek Port of Piraeus, it is evident that brownfield developments with an established financial record are safer and more profitable investments than BRI greenfield projects, which are often constructed without proper due diligence. While greenfield projects of the BRI promise to fill in infrastructure gaps and create a mutually beneficial economic and cultural exchange, Chinese efforts are often problematic and do not lead to the expected positive outcomes which it promotes. As demonstrated by the failure of the Port of Hambantota to meet expectations, large-scale greenfield BRI projects are typically characterized by long cycles, slow payback, and uncertain profitability-- all of the financial risks that are associated with the greenfield development framework. There is often high uncertainty associated with these greenfield projects due to factors including political instability of recipient countries, inability for developing countries to pay back large Chinese loans, and hasty projects that are constructed without proven evidence of demand. Moving forward, China should instead focus on channeling its BRI funding into brownfield investments that have established records of economic demand.

The Belt and Road Initiative is largely representative of China’s pivot away from its traditionally acquiescent international presence that had been promoted by former president Deng Xiaoping into the global political and economic leader of President Xi Jinping’s “China Dream.” Although China has been a long-time investor in developing markets, the BRI emphasizes a new level of economic connectivity between both developing and developed countries across Europe, Asia, and Africa. Despite the optimism of participating BRI countries, the unspecified focus of the BRI is indicative of a wider issue of insufficient planning that will continue to result in project pitfalls if not immediately addressed. The hybrid model that the BRI follows fails to set clear objectives and instead attempts to address both the economic and political front at once. Economically, it aims to maximize China’s industrial capacity and provide reliable transportation routes for transnational trade. Politically, the BRI aims to advance Xi Jinping’s “China Dream,” by strengthening the country’s leadership in international development and foreign affairs. As China strives to attain success in both aspects, the lack of clear priorities often lead to inefficiencies that are detrimental on both ends of political credibility and economic profitability.

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