

The Silk Road Economic Belt and the 21st Century Maritime Silk Road

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Fung Business Intelligence Centre



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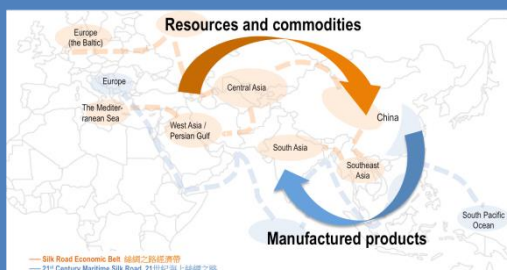
I. Introduction

The concepts of the Silk Road Economic Belt and the Maritime Silk Road were first introduced by Chinese President Xi Jinping during his visits to Kazakhstan and Indonesia in 2013.

The Central Government has since then further elaborated on the idea of building the Silk Road Economic Belt and the 21st Century Maritime Silk Road. The concept is often shorthand as the “One Belt One Road” Initiative, or more simply as the Belt and Road.

The Belt and Road: New Sourcing and Selling Opportunities

While the Belt provides ample opportunities for sourcing resources and commodities from the West and Central Asia, the emerging South and Southeast Asian countries along the Road are potentially vast consumer markets. According to a report by Ernst & Young in 2013, emerging Asia will account for one quarter of the global consumer products market and generate 38% of the global consumer products growth by 2017.



Source: Compiled by the Fung Business Intelligence Centre

On 28 March 2015, during the Boao Forum for Asia, China’s National Development and Reform Commission, in conjunction with China’s Foreign Ministry and Commerce Ministry, issued an action plan for the Belt and Road, bringing the concept one important step closer to realization.

Titled the “Vision and Actions on Jointly Building Silk Road Economic Belt and 21st Century Maritime Silk Road”, the official document lays out the basic goals of the “One Belt One Road” Initiative: “It is aimed at promoting orderly and free flow of economic factors, highly efficient allocation of resources and deep integration of markets; encouraging the countries along the Belt and Road to achieve economic policy coordination and carry out broader and more in-depth regional cooperation of higher standards; and jointly creating an open, inclusive and balanced regional economic cooperation architecture that benefits all.”

The Initiative’s current priority is infrastructure connectivity. Towards that end, the Chinese government has facilitated the establishment of the Asian Infrastructure Investment Bank and set up a US\$40 billion Silk Road Fund.

Geographic Coverage

According to the action plan, the Belt will have three routes and the Road will have two routes (for a graphic representation of these routes, please refer to Exhibit 1).

- The Silk Road Economic Belt:
 - China—Central Asia—Russia—Europe (the Baltic)
 - China—Central Asia—West Asia—Persian Gulf—Mediterranean Sea
 - China—Southeast Asia—South Asia—Indian Ocean
- The 21st Century Maritime Silk Road:
 - Coastal China—South China Sea—Indian Ocean—Europe
 - Coastal China—South China Sea—South Pacific

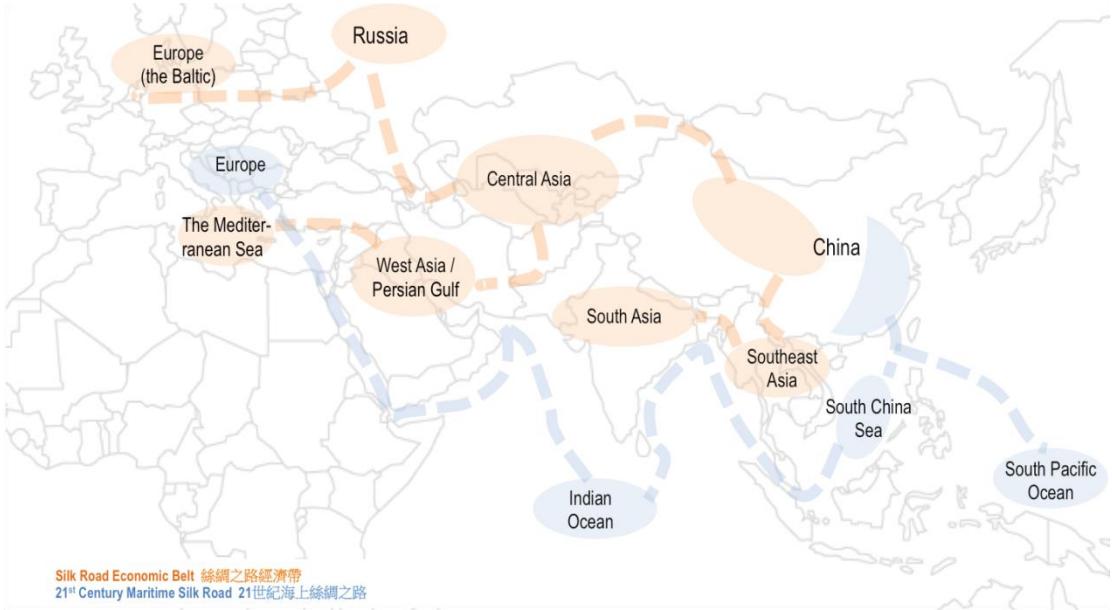
On the same day that the official action plan of the Initiative was announced, China's President Xi also revealed in his speech that around 60 countries along the routes have shown interest in taking part in the development of the Belt and Road.

Based on the five routes specified by the action plan, the *Fung Business Intelligence Centre* has identified 58 countries that are most likely to be taking part in the Initiative (please see the Appendix for the full list of the countries and the relevant economic indicators).

Together, the countries along the Belt and Road will create an “economic cooperation area” that stretches from the Western Pacific to the Baltic Sea. According to our research, these 58 countries jointly account for 64.2%, 37.3% and 31.4% of the world's population, GDP and household consumption respectively today (Exhibit 2). Many of these countries are home to the emerging middle class and hold the key to economic growth in the future.

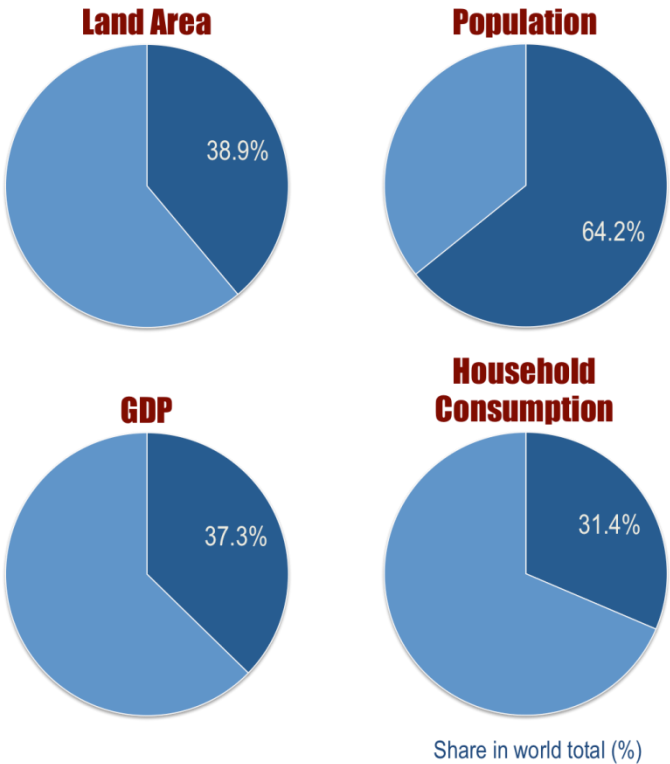
The action plan also specifies the positioning of various regions and provinces in China in the Initiative (Exhibit 3).

Exhibit 1. Geographic Coverage of the Silk Road Economic Belt and the 21st Century Maritime Silk Road



Source: Compiled by the Fung Business Intelligence Centre based on the FRAMEWORK chapter of the “Vision and Actions on Jointly Building Silk Road Economic Belt and 21st Century Maritime Silk Road”

Exhibit 2. Economic Significance of One Belt One Road Countries



* For a full list of the countries included in the computation, please refer to the Appendix.
Source: The World Bank, compiled by the Fung Business Intelligence Centre

Exhibit 3. Regions & Provinces in China: Positioning in the One Belt One Road Initiative



Source: "Vision and Actions on Jointly Building Silk Road Economic Belt and 21st Century Maritime Silk Road", compiled by the Fung Business Intelligence Centre

II. The Vision

The vision of the One Belt One Road Initiative is to realize the “Five Links”, which refer to linkages in policies, infrastructure, trade, finance and people. The “Five Links” can be summarized as follows:

The “Five Links”

While the traditional Silk Road was primarily a route for trading goods and cultural and technological exchange, the new Silk Road set out the “Five Links” as its goal. The “Five Links” refer to linkages in policies, infrastructure, trade, finance and people.

1. Policy coordination

- Policy coordination among the countries along the Belt and Road is crucial for the success of the Initiative. According to the Initiative’s vision, the countries will coordinate their economic development strategies and policies, and work out together plans and measures for regional cooperation.
- Countries along the Belt and Road will set up a multi-level inter-governmental macro policy exchange and communication mechanism.

2. Capacity building

- Countries along the Belt and Road will improve the connectivity of their infrastructure and harmonize standards.
- Countries will push forward constructions of port infrastructure, remove bottlenecks

in land-water transportation channels, promote cooperation of ports, and increase sea routes and the number of voyages.

- Countries will expand platforms for comprehensive civil aviation cooperation and improve aviation infrastructure.
- Cooperation in the connectivity of energy infrastructure will also be promoted.
- Countries will jointly advance the construction of communications networks, such as cross-border optical cable networks and satellite information networks.
- Countries will strengthen cooperation in science and technology by establishing joint laboratories and promoting personnel exchanges.

Huge Need for Infrastructure Financing in Asia

According to the Asian Development Bank, between 2010 and 2020, Asia needs to invest a total of around US\$8 trillion in national infrastructure in order to maintain current levels of economic growth. However, many Asian countries are suffering from a large infrastructure deficit, mainly due to budgetary constraints and a lack of investment capital.

- China will advance cooperation between countries along the Belt and Road on areas such as youth employment, entrepreneurship training and vocational skills

- development.
- Countries along the Belt and Road will also boost student exchange programmes.

3. Liberalization and facilitation of trade and investment

- Countries along the Belt and Road will enhance customs cooperation in areas such as information exchange, mutual recognition of regulations and mutual assistance in law enforcement. A “Single-window system” will be established in border ports. Moreover, the countries will promote online checking of inspection and quarantine certificates and facilitate mutual recognition of Authorized Economic Operators (AEOs).
- Countries will lower non-tariff barriers and improve the transparency of technical trade measures.
- Countries will take actions to advance investment facilitation and to eliminate investment barriers. Negotiations on bilateral investment protection agreements and double taxation avoidance agreements will also be pushed forward.
- Countries will expand mutual investment areas. In particular, cooperation in non-fossil energy sectors such as hydropower, nuclear power, wind power and solar power will be strengthened.
- Countries will also promote cooperation in emerging industries such as new-generation information technology, biotechnology, new energy

technology and new materials.

- Countries will cooperate in building various forms of industrial parks such as overseas economic and trade cooperation zones and cross-border economic cooperation zones.

4. Financial cooperation

- Countries along the Belt and Road will strengthen financial cooperation and increase their efforts to build currency stability systems, investment & financing systems and credit information systems in Asia.
- Countries will push forward the establishment of the Asian Infrastructure Investment Bank, the BRICS New Development Bank, the Shanghai Cooperation Organization (SCO) financing institution and the Silk Road Fund.
- Countries will create or further develop their bond markets. China will support the governments in the countries along the Belt and Road as well as companies and financial institutions with good credit-ratings to issue yuan bonds in China. Meanwhile, qualified Chinese financial institutions and companies will be encouraged to issue bonds in yuan or in other currencies outside China.
- Countries will expand the scope and scale of bilateral currency swaps and settlements.
- Commercial equity investment funds and private funds will be encouraged to participate in the construction of key projects of the Initiative.

III. Actions Already Performed

- For more than a year, the Chinese government has been actively promoting the One Belt One Road Initiative.
- China has signed Memorandum of Understandings (MOUs) of cooperation on the joint development of the Belt and Road with some countries, and on regional cooperation, border cooperation, or mid- to long-term development plans for economic and trade cooperation with other countries. It has also proposed outlines of regional cooperation plans with certain adjacent countries.
- China has enhanced communication and consultation with countries along the Belt and Road, and promoted a number of key cooperation projects in the fields of infrastructure connectivity, industrial investment, resource development, economic & trade cooperation, financial cooperation, cultural exchanges, ecological protection and maritime cooperation.
- The Chinese government has facilitated the establishment of the Asian Infrastructure Investment Bank and the Silk Road Fund, and has reinforced the investment function of the China-Eurasia Economic Cooperation Fund.
- China has also promised to offer 10,000 scholarships to countries along the Belt and Road every year.

The Asian Infrastructure Investment Bank and the Silk Road Fund

The Asian Infrastructure Investment Bank (AIIB) was formally established in October 2014. As of 29 March 2015, 42 countries had joined or applied to join the AIIB as founding members, including the UK, Germany, France and Italy.

In December 2014, Beijing launched its US\$40 billion Silk Road Fund along the lines of a long-term private equity venture to improve transport and trade links in countries and regions along the Silk Road. The Fund is expected to be similar to the World Bank's investment arm International Finance Corp and the African Development Bank's mutual development fund. Financed by a small group of investors, the Fund targets infrastructure construction, exploration of natural resources, and industrial and financial cooperation.

IV. Business Implications

1. Infrastructure construction – Capacity building to start with hardware, especially in the early stage of the One Belt One Road Initiative

- Infrastructure projects related to the Initiative, such as those invested by the Asian Infrastructure Investment Bank and the Silk Road Fund, will benefit the construction machinery companies, infrastructure construction companies, building materials producers, as well as infrastructure operators.
- According to the Initiative, priority will be given to linking up unconnected road sections and removing transport bottlenecks.
- In particular, the plan for the construction of a Eurasian high-speed transport corridor linking Beijing and Moscow will be pushed forward.
- Connectivity within the Belt and Road region will be greatly enhanced.

2. Finance – Yuan internationalization to accelerate

- Financial integration is an important underpinning for implementing the Belt and Road Initiative, the process of which will create demand for more professional services in financial and related sectors.
- The fundraising for large-scale infrastructure projects will provide opportunities for the further development of bond markets in Asia.
- China will encourage companies to issue yuan bonds within China as

well as overseas to fund projects for the One Belt One Road Initiative. The move is expected to boost demand for the currency.

- As trade and other economic activities along the Belt and Road expand, the demand for settling trade in yuan will also increase, if only to reduce exchange risks.

3. Trade and logistics – Regional flows to enjoy rapid growth

- According to the Initiative, China is going to negotiate with countries and regions along the Belt and Road to establish more free trade areas.
- In addition, China will cooperate with countries along the Belt and Road to lower non-tariff barriers and to jointly improve the transparency of technical trade measures, which will in turn liberalize and facilitate trade.
- China will also promote cross-border e-commerce and other similar innovations to bring consumers cheaper and better imported products.
- The increased level of trading activities will also benefit the logistics industry.

4. Distribution and retail – The Maritime Silk Road is well positioned to capture the emerging middle class

- According to an OECD study in 2010, globally, the size of the middle class may increase from 1.8 billion people in 2009 to 3.2 billion by 2020 and to 4.9 billion by 2030. Almost all of this growth (85%) comes from Asia: by 2030, Asia will represent 66% of the global

- middle-class population.
- Equally striking is the growth in purchasing power of the middle class in Asia. Globally, consumer spending from the middle class may grow from US\$21 trillion in 2009 to US\$56 trillion by 2030. Again, over 80% of the growth comes from Asia: by 2030, Asia will represent 59% of the global middle-class consumer spending.
- Asian spending power could be large enough to offset the stagnant spending growth in the developed economies. The shift in demand will also be disruptive to the existing global supply chains.

The Emerging Middle Class along the Silk Road

Globally, consumer spending from the middle class may grow from US\$21 trillion in 2009 to US\$56 trillion by 2030. Over 80% of the growth comes from Asia: by 2030 Asia will represent 59% of the global middle-class consumer spending.

5. Tourism – More frequent exchanges among the Belt and Road countries

- China will cooperate with countries along the Belt and Road on tourism.
- Application processes for tourist visas in countries along the Belt and Road will be streamlined.
- In particular, tourism cooperation between the Tibet Autonomous Region and neighboring countries such as Nepal will be promoted.

Appendix I

List of Countries Included in Computing the Percentage Shares Shown in Exhibit 2 - Economic Significance of One Belt One Road Countries

The following countries are selected by the *Fung Business Intelligence Centre*, based on the FRAMEWORK Chapter of the “Vision and Actions on Jointly Building Silk Road Economic Belt and 21st Century Maritime Silk Road” and President Xi Jinping’s speech on 28 March 2015.

	Land area (sq. km, 2014)	Population (million, 2013)	GDP (current US\$ billion, 2013)	Household consumption (current US\$ million, 2013)
North and East Asia	China	1,357,380.0	9,240.3	3,446.8
	Russia	143.5	2,096.8	1,089.1
	Mongolia	2.8	11.5	6.2
	Kazakhstan	17.0	231.9	117.5
	Kyrgyzstan	5.7	7.2	6.8
Central Asia	Tajikistan	8.2	8.5	9.5
	Turkmenistan	5.2	41.9	5.3
	Uzbekistan	30.2	56.8	30.4
	Afghanistan	30.6	20.3	16.6
	Armenia	3.0	10.4	9.2
West Asia	Azerbaijan	9.4	73.6	30.8
	Bahrain	1.3	32.9	11.6
	Cyprus	1.1	21.9	Not available
	Georgia	4.5	16.1	11.5
	Iran	77.4	368.9	0.0
	Iraq	33.4	229.3	0.0
	Israel	8.1	290.6	164.3
	Jordan	6.5	33.7	27.3
	Kuwait	3.4	175.8	42.5
	Lebanon	4.5	44.4	31.5
	Oman	3.6	79.7	22.8
	Qatar	2.2	203.2	24.1
	Saudi Arabia	28.8	748.4	222.2
	Syria	22.8	Not available	Not available
	Turkey	74.9	822.1	582.7
	United Arab Emirates	9.3	402.3	200.4
	Yemen	24.4	36.0	Not available
	Brunei	0.4	16.1	3.6
	Cambodia	15.1	15.2	12.6
	Indonesia	249.9	868.3	484.8
Southeast Asia	Laos	6.8	11.2	7.3
	Malaysia	29.7	313.2	160.0
	Myanmar	53.3	Not available	Not available
	Philippines	98.4	272.1	199.4
	Singapore	5.4	297.9	110.5
	Thailand	67.0	387.3	210.8
	Vietnam	89.7	171.4	111.5
	East Timor	1.2	1.3	0.9
	Bangladesh	156.6	150.0	109.3
	Bhutan	0.8	1.8	1.0
South Asia	India	1,252.1	1,876.8	1,071.9
	Maldives	0.3	2.3	Not available
	Nepal	27.8	19.3	15.1
	Pakistan	182.1	232.3	188.6
	Sri Lanka	20.5	67.2	44.9
Eastern Europe	Estonia	1.3	24.9	12.8
	Latvia	2.0	31.0	17.5
	Lithuania	3.0	45.9	27.2
	Ukraine	45.5	177.4	129.0
	Belarus	9.5	71.7	36.8
	Moldova	3.6	8.0	7.4
	Poland	38.5	525.9	320.2
	Greece	11.0	242.2	172.5
	Italy	59.8	2,149.5	1,300.3
	Germany	80.6	3,730.3	2,086.6
Southern and Western Europe	Netherlands	16.8	853.5	384.5
	Kenya	44.4	55.2	44.2
East Africa	Egypt	82.1	272.0	220.8
Total	50,443.7	4,574.6	28,195.6	13,601.2
Share of One Belt One Road Countries in world total	38.9%	64.2%	37.3%	31.4%

Source: The World Bank, compiled by the Fung Business Intelligence Centre

Appendix II

Latest Developments on the 'One Belt One Road' Initiative (as of end April 2015)



China pledges to deepen cooperation with Asian and African countries

At the Asian-African Summit 2015 held in Jakarta, Indonesia, China's President Xi Jinping delivered a speech calling for win-win cooperation among Asian and African countries.

President Xi promised to grant zero-tariff treatment by the end of this year to 97% of the tariff items imported from the least developed countries (LDCs) which

have diplomatic ties with China, and to continue to provide assistance to developing countries without any political preconditions.

President Xi also announced that, in the coming five years, China would offer 100,000 training opportunities to developing countries in Asia and Africa; continue hosting gathering among Asian and African youths to promote friendship and would invite 2,000 Asian and African young people to visit China and join the gathering; establish a China-Asia-Africa cooperation center to promote exchanges and cooperation; and set up an exchange and study program on international

law between China and the Asian-African Legal Consultative Organization.



China promises investment of US\$46 billion in Pakistan

During the landmark two-day visit of China's President Xi Jinping to Pakistan in April, China signed agreements with Pakistan promising investment of \$46 billion. The focus of the spending is on building a China-Pakistan Economic Corridor (CPEC), a 3,000-kilometre road and rail link from China's north-western city of Kashgar to Pakistan's Gwadar Port, a deep-sea port situated on the Arabian Sea. The mega plan not only covers the construction of highways and railways, but also oil and gas pipelines and electricity projects.

The CPEC is expected to spur investments, boost bilateral trade flows between the two countries, improve infrastructure, and help ease the energy shortage in Pakistan. According to Reuters, under the CPEC agreement, US\$15.5 billion worth of coal, wind, solar and hydro energy projects will be built by 2017, which will add 10,400 megawatts of power to Pakistan's national grid. By 2021, another 6,120 megawatts will be added to the country's national grid at a cost of US\$18.2 billion. A US\$44 million optical fibre cable between the two countries will also be built.

Also during Xi's visit, Pakistan's Karot Hydropower Project became the first recipient of funding support from

China's US\$40 billion Silk Road Fund.

The two countries also set the target of lifting bilateral trade to US\$20 billion in three years, up from the current US\$16 billion.

Talking about the China-Pakistan Economic corridor, the Pakistani Prime Minister Nawaz Sharif said, 'This corridor will benefit all provinces and areas in Pakistan, and transform our country into a regional hub and pivot for commerce and investment. It will also enable China to create a shorter and cheaper route for trade and investment in south, central and west Asia, and the Middle East and Africa. This corridor will become a symbol for peace and prosperity.'



Silk Road Fund makes its first investment

China's Silk Road Fund makes its first investment in a hydropower project in Pakistan. During China's President Xi Jinping's visit to Pakistan, the Silk Road Fund unveiled its investment in the Karot Hydropower Project in Pakistan, the first investment project since the Fund's establishment in December 2014. The project is expected to cost about US\$1.65 billion. (As of the time of writing, it is still not clear how much of the investment amount will come from the Silk Road Fund.)

The Karot Hydropower Project, which is scheduled to start operation by 2020, will be run by the Chinese side for 30 years before being handed over to the Pakistan government.

The Silk Road Fund will continue to find investment opportunities for other projects under the framework of the China-Pakistan Economic Corridor, and will also look for opportunities involved in the Belt and Road initiative.



Founding members of AIIB finalized at 57

57 countries have submitted their applications and become the founding members of the Asian Infrastructure Investment Bank (AIIB), with the application deadline closing on 31 March. Of the 57 founding members, 37 are from Asia and Oceania, and the rest are from Europe, Africa and Latin America. (Note that the deadline for founding membership application has passed. The AIIB will continue to accept ordinary members, which hold voting rights but have less say in the rule-making process.)

Representatives of the 57 founding member countries will convene in late April and late May to deliberate on the AIIB charter. With the signing of the charter expected to take place by the end of June, the AIIB is set to be launched by the end of this year.



Turkey joins AIIB as a founding member

Turkey has become a founding member of the Asian Infrastructure Investment

Bank (AIIB), according to a statement released by China's Ministry of Finance on 10 April. As a founding member of the bank, Turkey possesses the right to establish the rules for the bank's activities.



China and Turkey boost economic ties

Ever since China and Turkey upgraded their relations to a strategic partnership in 2010, the two countries have enjoyed booming development in bilateral trade and investment relations.

In 2014, China became Turkey's 2nd largest source of imports and 19th largest market of exports, according to data from the Turkish Statistical Institute. Total trade volume between the two countries amounted to US\$27.8 billion in 2014, a 42.6% increase compared with US\$ 19.5 billion in 2010.

Besides, Turkey has become increasingly popular among Chinese investors. A group of Chinese enterprises, such as Hainan Airlines, China's major locomotive maker CSR Corporation Ltd. and agribusiness New Hope Group, have already invested in Turkey, in areas such as transportation, energy, telecommunications, mining and tourism. It is also noteworthy that the Ankara-Istanbul high-speed railway, one of the signature projects of the Turkish government, is jointly built by a Chinese-Turkish Consortium.

In November 2014, Turkish President Recep Tayyip Erdogan expressed his

support for the Silk Road Economic Belt and Maritime Silk Road Initiative that put forward by China, during a meeting with Meng Jinzhou, special envoy of China's President Xi Jinping. As a country that enjoys favorable location stretching to

Asia, Europe and the Middle East, Turkey's participation in the Initiative will definitely help break infrastructure bottlenecks, further integrate markets, and better allocate resources in the region.

The Fung Group is a privately held multinational group of companies headquartered in Hong Kong whose core businesses are trading, logistics, distribution and retailing. The Fung Group employs 46,800 people across 40 economies worldwide, generating total revenue of more than US\$24.65 billion in 2014. Fung Holdings (1937) Limited, a privately held business entity headquartered in Hong Kong, is the major shareholder of the Fung group of companies.

The Fung Business Intelligence Centre collects and analyses market data on sourcing, supply chains, distribution and retail. It also provides thought leadership on technology and other key issues shaping their future.

Headquartered in Hong Kong, FBIC leverages unique relationships and information networks to track and report on trends and developments in China and other Asian countries. In addition, its New York-based Global Retail & Technology research team follows broader retail and technology trends, specialising in how they intersect and building collaborative knowledge communities around the revolution occurring worldwide at the retail interface.

Since its establishment in 2000, the FBIC (formerly known as the Li & Fung Research Centre) has served as the knowledge bank and think tank for the Fung Group. Through regular research reports and other publications, it makes its market data, impartial analysis and expertise available to businesses, scholars and governments around the world. It also provides advice and consultancy services to colleagues and business partners of the Fung Group on issues related to doing business in China, ranging from market entry and company structure, to tax, licensing and other regulatory matters.

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