China Politics & Policy

China warned of risk to banks from One Belt, One Road initiative

Experts concerned about political factors driving $900bn road and rail projects

Chinese labourers work on the Karakoram highway, a 'One Belt, One Road' project in northern Pakistan © AFP

JANUARY 26, 2017 by: **Don Weinland** in Hong Kong

Beijing's plan to invest almost $1tn in infrastructure in some of the world's poorest countries is raising concerns of risks for the Chinese banks backing the projects.

Turmoil in countries such as Venezuela, where China has lent $65bn (http://next.ft.com/content/18169fbe-33da-11e6-bda0-04585c31b153) during the past decade, has led to a recalibration of the level of risk facing the One Belt, One Road (https://ig.ft.com/sites/special-reports/one-belt-one-road/) project in emerging markets, experts say.

President Xi Jinping's signature foreign policy initiative envisions a new wave of global growth spurred by roads and rail links spanning some of the poor regions (http://next.ft.com/content/e99ff7a8-0bd8-11e6-9456-444ab5211a2f) such as east India, Africa and Central Asia. It has been likened to the US Marshall Plan of the 1950s and interpreted as China's first concerted effort to lead global development as the US, under the presidency of Donald Trump, retreats from its global role.

The Chinese government has announced more than $900bn in projects, some already under way, with most of the funding set to come from China's policy banks and commercial lenders.

But the investments have been driven more by China’s desire to exert global influence than focusing on real demand for infrastructure, Fitch Ratings warned in a report on Thursday.

Related article

Map: Key projects on the new Silk Road (http://next.ft.com/content/80c6e51a-4ccf-11e6-88c5-db83e98a590a)

Transport and energy projects connecting Central Asia

That means banks risk becoming entangled in projects where commercial logic and demand for roads and bridges are subordinate to political considerations.

“The lack of commercial imperatives behind Obor projects means that it is highly uncertain whether future project returns will be sufficient to fully cover repayments to Chinese creditors,” Fitch said on Thursday.

Credit ratings for countries where China has big infrastructure plans provide a gauge for the projects’ underlying creditworthiness, Fitch said. Most of the countries are of speculative sovereign-rating grade but several, such as Laos, are not rated at all.

Laos will be the recipient of a high-speed railway expected to cost about $7bn — or more than half the impoverished Southeast Asian country’s gross domestic product.

Banks’ rapid expansion into such infrastructure lending could expose China to overseas asset quality problems at a time when they are already burdened with non-performing loans at home.

“If the infrastructure is paid out of the government, it may not be a big issue but if it involves the publicly listed banks, it will have great impact on the asset quality if the infrastructure turns out to be not economically feasible,” said Simon Lee, assistant dean at the Chinese University of Hong Kong Business School.

Such problems materialised in earlier Chinese investments in emerging markets. Last year China was forced to renegotiate billions of dollars of loans to Venezuela as the South American economy bordered on collapse (http://next.ft.com/content/aadf657c-7f4a-11e6-8e50-8ec15fb462f4) following the oil price plunge.

“Venezuela has exposed the risks to the plan. After that case, there has been a period of rethinking these deals,” said Shen Jianguang, Mizuho’s chief economist for China, noting that announcements of new projects have since slowed. “Even though the deals are signed with countries, what happens if the country has a crisis?”

High-speed rail projects in Indonesia and Thailand have also stalled because of political issues and disagreement on financing, according to a note from Standard Chartered.

The Fitch report on Obor was a rare dissenting voice among global institutions, the majority of which have praised the initiative.

The Asia Infrastructure Investment Bank, which launched in 2013 and will help fund Obor, announced this week it had attracted 25 new members (http://next.ft.com/content/671d8ac4-e18a-11e6-8405-9e5580d6e5fb) including Ireland, Canada, Ethiopia and Sudan to the group of 57 founding members. While the UK has been a staunch supporter of the initiative, the US has sought to press some countries (http://next.ft.com/content/41c3c0a0-59cd-11e4-9787-00144feab7de) not to join.

China has been adamant that projects are evaluated on a commercial basis and that Obor was not an aid programme.

Zhang Ying, a professor at Erasmus University's Rotterdam School of Management, said Fitch may underestimate the true demand for infrastructure where China plans to invest.

"Rapid expansion in overseas infrastructure lending is driven by Chinese firms' rapid growth and the large demand from local markets stimulated by China's Obor initiative, not decided by China's bank itself," Prof Zhang said, noting that shareholders have approached the projects cautiously.

Read latest

James Kynge
China stakes claim for illiberal globalism

Recommended for you

Fast FT
Fitch warns on expected returns from One Belt, One Road

China capital controls
Renminbi in retreat as international payment currency