

# China's Economic Integration in Central Asia in the Context of the Proclaimed "One Belt, One Road" Initiative

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**Abstract.** Based on scientific and practical ideas about regional economic integration, a modern strategy of China's integration is presented. It is considered in the context of the initiative "One belt, one road", proclaimed by the leadership of the country. Arguments are given that the initiative is designed to solve the problems of Chinese domestic and foreign economic policy through the development of a large-scale project in Central Asia. The processes of economic integration of China with one of the largest partners in the region – Kazakhstan. According to the results of the study, Kazakhstan is of interest to China as a "gateway" to Central Asia, through which the main transport and energy corridors pass. The methodological basis of the study was the publications of domestic and foreign authors in the field of integration, methods of regional integration, as well as forms and conditions of its implementation. In course of the study, general scientific methods of research, economic and statistical analysis, and expert evaluation were applied. The practical application of the results of the study is the development of economic integration in the Eurasian space, considering the dominance of China in Central Asia.

## 1. Introduction

Before XX century, we could observe integration in various organizational forms of decision-making; it resulted from an objective need to promote linkages among different governments. Over time, integrational processes have involved more world parts and regions, including Asian.

In the second part of XX century, integration became much more structured due to the results and threats of a global nature. Asian integrational strategy was focused on a gradual movement forward considering opportunities and avoiding long-standing obstacles.

The beginning of XXI century stated a new character of integrational linkages due to the change of constitutional-territorial principle of integration arrangements for the principle of global spatial interaction [1,2,3]. In Asia, conclusions of regional agreements are irrelevant to state political regimes and levels of economic development. Supranational institutions are replaced with market, formal structures, and associations giving priority to promotion of goods and services, capital and labor force without exceptions and limitations.

So, regional economic integration is one of the most important phenomena in Asia. Interest to its research is based on strengthening of several processes, which will state future interconnectedness and interdependence of different states in Central Asia. In this regard, much depends on modern solutions in the sphere of economic integration, which is being developed by China in the context of the initiative “One belt, one road”.

## **2. The relevance, scientific value**

Commonly, conceptualization of a phenomenon starts from research of conceptual apparatus. Let us remind you that the term “integration” origins from the Latin word “*integratio*”, which means replenishment. Before XX century, it was used mainly in natural sciences, and then scientists started to use it for analyze of social-economic processes. Dozens of terms related to economic integration occurred on that basis. Three main scientific schools influenced this process: federalism, neo-functionalism, and a theory of inter-governmental cooperation. Despite controversial opinions on role of the policy and its economic interaction, proponents acknowledge the multiplicity of the development of global economic relations.

Research of intergonial issues typically starts from perspective of regionalism and globalization. Both approaches base on the term “region”, which in the modern sense, is a space with a set of features, rather than geographic territory. We primarily mean international or global regions performing as totality of sub-, meso-, and macro-regions [4].

Regarding international integration, we would like to point at two other terms, “regionalism” and “regionalization”. Some scientists don’t find any differences between them, while other strongly insist upon the opposite. Modern scientific works have examined the following principal types of regionalism: “new” and “old”, or “open” or “close”. The main feature of modern regionalism is that integration today involves not only national states, but also non-governmental agents, such international organizations, transnational corporations (TNC), etc., and openness to other countries.

Scientists observing prevalence of economic processes in integration base on the term “regional economic integration”. Basics of the theory of economic integration in the 1960’s was developed by the Hungarian economist Bela Balassa [5]. Note bilateral trade agreements, along with the multilateral (for example, on Customs Union), also represent an integration association. Results principally depend on the efficiency of interactions among agents of economic and social spheres.

Scientific papers also research contradictions to be solved during integration, among them are the following [6]: independence - complex interrelationship; co-operation – competition; principle of unanimity – majority principle; national sovereignty – supra-nationalism; elitism – democracy; integrity – multiculturalism; European identity – national identity; alliance’s consolidation – enlargement of the union.

## **3. Problem statement**

As is well known, different integrational strategies show up-to-date interconnectedness and interdependence of economies of different countries. Current strategy of integration of the Peoples Republic of China considered in the context of the initiative “One belt, one road” was proclaimed by the leadership of the country in 2013. Official documents of the PRC state mechanisms of implementing the strategy, the principal tools follow:

- investment and lending;
- construction of infrastructure based on economic model “construction contract plus financing and operation”;
- increase of RMB’s circulation in regional commerce.

On content, the initiative “One belt, one road” cannot be described as an example of classic integration. Firstly, its processes should be developed as macro-projects; and secondly, “by boosting political contacts, construction of a single road network, trade links, currency flows, and people’s contacts” [4]. In this regard we should remind you that both, bilateral and multilateral cooperation, having their own features missions mutually reinforce and complement one another [7,8]. That’s why

it is important to explain the way Chinese leaders implement traditional methods and tools of bilateral and multilateral interaction for development of objective conditions for effective implementation of the initiative “One belt, one road”.

#### 4. Theoretical part

Scientists have no doubt that the initiative “One belt, one road” is aimed at solution of issues of internal and external economic policy of China. Indeed, regarding the extensive project in Central Asia, the administration of China stated the following task-list [9]:

- infrastructural interdependence of countries. In the context of this task, the countries-members should focus on the development of co-operation among infrastructural objects, including ports, stocks, terminals, and communications;
- liberalization and achievement of unimpeded trade will contribute to the development of the Customs Cooperation of countries-members through the development of information exchange, facilitation of mutual recognition of standards and technical regulations, creation of a single window facility, reducing the level of non-tariff barriers;
- achievement of financial integration. The solution of this task is based on development of stable investment and financial systems, assistance to international financial systems designed in China, such as The Asian Infrastructure Investment Bank, AIIB, The New Development Bank (NDB), formerly referred to as the BRICS Development Bank, and the Silk Road Fund;
- political co-ordination. Within this task, the governments should co-ordinate their economic strategies and politics, develop joint plans and measures to deepen regional integration;
- ensure interlinking relationship among peoples [10]. In pursuit of this goal, we intend to increase co-operation in spheres of education, tourism, science, and exchange of information and technologies [11].

In the contest of tools by means of which the strategy will be achieved, let us show an evidence that the following decisions have turned into crucial for establishment of co-operative relations in China, emphasize on economic integration and reliance on strategic bilateral co-operation. Consequently, the region of China was guided by the philosophy of integration, under which the process' members complement one another.

In Central China, they use multilateral format as a tool of political influence; it researches standards of international business, adapting itself to the “game rules”. Note priorities of arrangement of co-operation in Shanghai used to be facing strong Russian opposition. Territory and water conflicts of China with other countries of the region impede its overall development and progress.

For the recent seventeen years, China has invested the largest percentage of total volume of foreign capital in countries of Central Asia. Direct foreign investment from China to the countries along transport routes of the mega-project calculates over 70 billion USD. Kazakhstan, Kyrgyzstan, and Tajikistan are especially important among all governments of the region [7]. Almost half of the investment was directed in extractive sector, then transport, and industrial.

Frequently for funding projects, China transmits its credit resources to the countries rich in mineral resources. These are low-interest loans (1,5–3,0%) for extended periods (up to 20 years) allowed grace periods. Often in practice, in cases when money repayment becomes difficult, China provides the scheme “investment in exchange for raw materials”, which provides with opportunity to pay off the loans supplying natural resources or providing access to the deposits of raw materials [12].

The following methods of interaction with foreign entrepreneurs are ideal for China: obtaining of assets in property or ownership of over a half of total assets; achievement of a right for full exportation of raw materials or export of over a half of total raw materials; business assembly activities through the involvement of Chinese labor force, Chinese technologies and equipment [13].

China is developing infrastructure to boost export. Under the initiative “One belt, one road”, three projects of international transport corridors are being carried out. Note in Central Asia, there are competing projects: The International North–South Transport Corridor (INSTC); The Trans-Asian

Railway (TAR); and international transport program involving the European Union aimed at Central Asian region TRACECA (Transport Corridor Europe-Caucasus-Asia) [14,15,16].

Significant investment has been transferred by the International Center for Cross-Border Cooperation “Khorgos”. It includes Kazakhstan and Chinese lands totaling 560 hectares linked through a special “bridge” over the state border. For seven years, tourists, goods (cargoes) and vehicles have been moving freely within the Center; this is a unique innovative form transboundary cooperation, which should turn into an attraction point for investment.

In the regard of internationalization of trade with goods and services, the regional strategy of the PRC focuses on extension of RMB circulation. The achieving of this goal results mainly from the conclusion of the agreements (SWAp agreements) of exchange of local currencies for yuan. Since 2011, such agreements have been signed with Kazakhstan, Uzbekistan, and Tajikistan for total amount about two billion USD, and the agreement with Kyrgyzstan is under negotiation. Moreover, a part of the credit is transmitted solely in yuan. After a sharp drop in 2014, foreign trade turnover of China with countries of Central Asia continued its rising and amounted to over 100 billion USD in following years. In international commerce, we are observing a tendency of growth of export and import volume.

So, the effectiveness of relations of China with certain countries in Central Asia result from division of politics and economy, unlimited national sovereignty, slowly changing culture and different economic potentials of the states-applicants for inclusion in Chinese project, as well as their different legal framework. Another considerable factor is a uniform legal basis which two countries use as a guidance of principles and standards of international law.

## 5. Practical value

From the perspective of the initiative “One belt, one road”, Kazakhstan is attractive to China as a “gate” to Central Asia, which is on the route of main transport and energetic corridors and facilitates a transportation of goods all over the Eurasian Economic Union and, from there, further into Europe. For its part Kazakhstan commenced the implementation of the national program “Shining Path” (“Nurly Zhol” - Kazakh language) which confirms a shift away from resourced-based economic orientation. The program focuses on the development of transport infrastructure in Kazakhstan to provide better linkage to external markets. The mega-projects of China and Kazakhstan follow similar principal goals.

The relationship between two countries has rapidly developed in the last decade. China became the second (12,0%) exporter of the Republic of Kazakhstan, following the EU (53,5%). In recent years, the volume of Kazakhstan export to China has exceeded the import, however, the foreign trade turnover with China has been declining [17]. The main lines of China’s import from Kazakhstan are metals, such uranium and copper ores, ironstones, and gold, and mineral products and chemicals; while it exports fabrics, vehicles, footwear and headwear, metal, animal skins and other goods. The key-role in securing raw material supplies to China for fuel production will be, most probably, played by Kazakhstan [12].

Half of the current investment projects are being implemented in Kazakhstan due to the Peoples’ Republic of China. This is roughly 70% of total volume of Chinese investment to Central Asia [6]. Many large companies of China are represented in Kazakhstan being significant members of its economic projects; while only few Kazakh companies are in the market of China [18].

In 2017, a private equity joint China-Kazakhstan “Nurly (Bright) Investment Fund” was based. The trust fund level is about 300 million USD. The coverage of investment includes Kazakhstan (50%) and other countries-members of the project “One belt, one road” (50%). These funds are to be allotted to priority sectors of economy, including development of technology-intensive, innovative, and knowledge-based projects.

Oil and gas industries are in a focus of attention of bilateral cooperation. In this sphere, Kazakhstan intends to decrease an influence of foreign TNCs, eliminate Russia’s monopoly on purchase of hydrocarbon, and turn into a principal transit supplier of oil and gas to China. China needs the diversification of raw-materials’ delivery routes. In total volume of oil exploitation in Kazakhstan, the

share of China has risen to 22,5%, so, currently, it is ranking third, after domestic investor (28%) and the USA (24%). Five of eleven affiliate oil producing companies of the state-owned oil and gas company of Kazakhstan “KazMunayGas” (KMG) (“QazMunayGaz” – in Kazakh language) are registered as partnerships with individual share of China or its right for purchase, among them are PetroKazakhstan Inc. and Manghystaumunaigas MMG. The Kazakhstan company Manghystaumunaigas MMG has been sold to The China National Petroleum Corporation (CNPC) repaying back of 10 billion USD loan. Chinese credit organizations provided Kazakhstan with the loans, which currently represent slightly more than a quarter of total foreign investment [19].

From perspective of bilateral co-operation, transport infrastructure and logistic projects are the most promising, because they focus on provision of access to oil and gas reserve in areas and increase of transit through rail and motorway corridors. Domestic lines of transportation are currently under construction, for example, a new rail line Zhezkazgan-Beyneu [20]. In the Special Economic Zone “Khorgos – Eastern Gate”, 12 projects for total amount of 470 billion KZT in 2018. By 2020, daily freight traffic will achieve 20 million tons, and 35 million tons by 2030. Another transport/logistics center in form of the partnership of KTZExpress JSC and Lianyungang Inc. is under construction on the East Coast of China in Lianyungang.

The principal project for Kazakhstan is an international transport corridor “Western Europe-Western China”. In Kazakhstan, this route passes through five regions and has significantly reduced delivery time of goods. So now, the transportation from the Chinese port Liaoning to the EU border takes only ten days. In expert opinion, the total volume of cargo transportation will increase in 2.5 times by 2020 году and average annual economic benefit will achieve the amount of 33,9 billion KZT. Future development of cargo transportation results from the agreement of the national joint-stock company “Kazakhstan Temir Zholy” and “China State Railway Group Company”, Ltd.

Chinese is having active crediting policy toward Kazakhstan financing projects with participation of Chinese companies on concessional terms, including industrial projects, ecologically unsound for Kazakhstan. For example, the project of modernization of «Atyrau Refinery» LLP focuses on production of benzol, which is not used for petrol production, but in petrochemicals sector. Chinese investment is beneficial for economic activity in the energy and industrial sectors, area of transportation, and agriculture. Note Kazakhstan had been getting credits and direct investment from China before 2015 too, but to a lesser extent [7, 21].

Therefore, bilateral relations are rapidly growing due to the import of Chinese goods, investment in the energy sector (development of oil fields, uranium and other raw materials exploration), supply of trade credits, export of oil, uranium, and metal. The economic presence of China in Kazakhstan contributes to these processes. The relationship between two countries cannot be described as equal: Kazakhstan supplies China with non-renewable natural resources, such oil, gas, and other materials, while imported goods from China to Kazakhstan consists of final products. Low production cost of Chinese goods automatically turns the most of Kazakhstan producers into uncompetitive in the market. Consequently, we observe the risk of unilateral raw-material orientation of Kazakhstan economy. This tendency is strategically unfavorable for Kazakhstan due to unpredictable commodity prices in global market doubled with unilateral Chinese investment transmitted mainly to gas and oil industries.

## 6. Conclusion

Through channels of bilateral co-operation and methods of multilateral collaboration with focus on economic integration, the government of China developed objective conditions for effective implementation of the initiative “One belt, one road”. Multilateral format is being used as a tool of political influence, and due to its implementation, China is absorbing international standards adjusting to the “game rules”.

China has chosen the most economically effective bilateral form of strategic co-operation. The key-factor of its implementation is a distinctly restricted legal framework. As a result, we have been observing a constant growth of Chinese FDI in Central Asia in such sectors as energy, transport, oil and gas industries, and general development of infrastructure. Economic relations favorable for China

have been established with Kazakhstan, Kyrgyzstan, and Tajikistan, which however, cannot be described as equal.

As part of the initiative “One belt, one road”, we could observe the development of economic integration of China with Kazakhstan which is one of the largest partners in Central Asia. The intensity of economic presence of China in Kazakhstan is rapidly increasing. Apart from this, Kazakhstan supplies China with non-renewable natural resources, such oil, gas, and other materials, while imported goods from China to Kazakhstan consists of final products. For Kazakhstan China is one of the most important investors, significant importer of oil and other raw materials. Generally, the Chinese integrational strategy has proven to be more efficient than the Kazakh one.

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