

POLICY PAPER

# GEORGIA-CHINA RELATIONS: THE GEOPOLITICS OF THE BELT AND ROAD

JOSEPH LARSEN

October 2017



GEORGIAN INSTITUTE OF POLITICS

TBILISI



**Policy Paper**

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AND ROAD**

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**Joseph Larsen**

**October 2017**

**ABSTRACT**

China has shown a growing interest in Georgia. Cooperation is largely confined to the economic sphere. However, a stronger Chinese presence in the context of the Belt and Road Initiative could have major geopolitical significance.

**Tbilisi**



საქართველოს პოლიტიკის ინსტიტუტი  
GEORGIAN INSTITUTE OF POLITICS

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## EXECUTIVE SUMMARY

Georgia enjoys a growing relationship with China, especially in the economic sphere. China has become an important trade partner and source of Foreign Direct Investment (FDI) and the two countries share common positions on certain diplomatic issues. Due to its small size and geographical distance from China, it is unlikely that Georgia will become a key strategic or security priority for China in the future. That being said, Georgia can leverage certain advantages to punch above its weight in the bilateral relationship – in particular its unique geographic location as a bridge between Europe and Asia. Georgia possesses three key features that make it attractive as a participant in China’s Belt and Road initiative (BRI): Free Trade Agreements (FTAs) with both the European Union (EU) and China; an outlet to the Black Sea and overland links with Turkey, which offer platforms from which China can more efficiently conduct trade with the European Union (the second factor augmenting the first); and a flexible position at the fulcrum of two regional formats important for the BRI’s success – the Georgia, Ukraine, Azerbaijan, and Moldova (GUAM) group and the Azerbaijan, Georgia, Turkey trilateral group (AGT). Moreover, Georgia’s small size means that a relatively small commitment from the Chinese perspective could have an outsized impact. For Georgia, the strategic implications of involvement in the BRI are significant. While both GUAM and AGT are weakly institutionalized and neither has major strategic importance for China currently, a sustained Chinese presence creates added incentives for deepened regional economic cooperation – a fact which could strengthen Georgia’s role as a bridge between Europe and Asia. There are signs that is already happening. Moreover, Chinese engagement in the region has the potential to change Russia’s strategic calculus by increasing the cost of destabilizing neighboring states, including Georgia. That has the potential to ease the geopolitical pressure currently applied by Russia, thereby advancing Georgia’s key security objective.

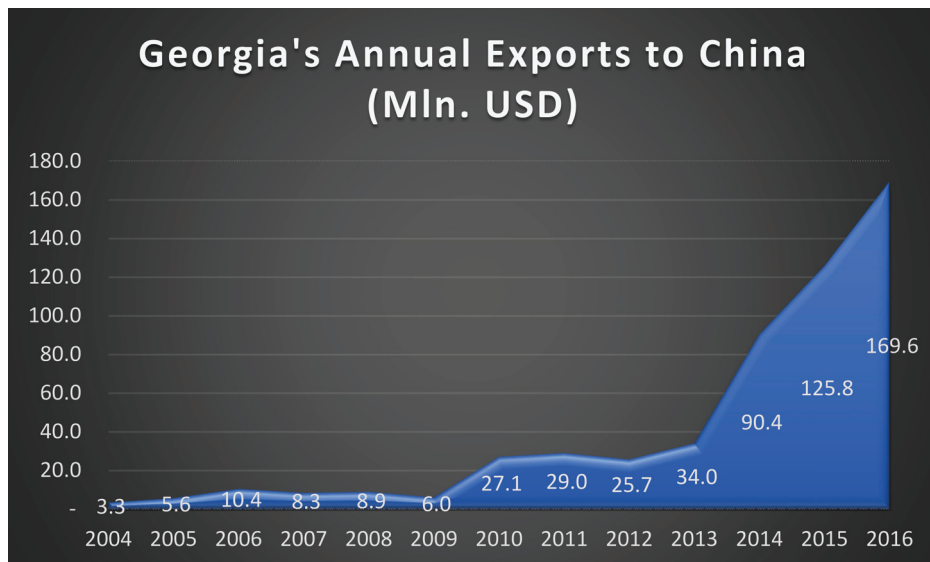
This paper first provides an overview of the current state of China-Georgia bilateral relations. The second section provides background of the BRI and analyzes Georgia’s specific role within the initiative, relying on academic literature and statements and papers produced by government bodies in both countries. Third, this paper assesses the geopolitical implications of the BRI, including the possibility that engagement with China within the BRI framework can help strengthen Georgia’s strategic position, especially vis-à-vis Russia. Fourth, this paper addresses the BRI’s potential for failure. The paper concludes by providing policy recommendations for the Georgian government to maximize the benefits of engagement with China within the BRI framework.

## GEORGIA: A PARTNER FOR CHINA IN THE SOUTH CAUCASUS

The People’s Republic of China extended official diplomatic recognition to the Republic of Georgia on June 9, 1992. Bilateral ties have advanced gradually in the 25 years since. Cooperation is mostly confined to the economic sphere, focusing on FDI and trade. Bilateral trade has expanded significantly since trade relations were first established in 1992, and especially since 2010, as Georgia’s economy recovered from the 2008 August War.

### Georgia-China Ties in the Economic Sphere

Trade relations have expanded precipitously since Georgia’s economy began to recover from the 2008 August War. Georgian exports to China increased from just \$6 million in 2009 to \$170 million in 2016, accounting for eight percent of Georgia’s exports worldwide.<sup>1</sup> Over the same period, Chinese exports to Georgia increased from \$175 million to \$548 million, putting it third after Turkey and Russia. The overall volume of bilateral trade increased by 223 times from 1992 to 2014 – from less than \$4 million to \$823 million. Georgian exports to China are currently dominated by minerals, including copper ores and concentrates.<sup>2</sup>



<sup>1</sup> “Georgian exports by countries”, GeoStat, accessed June 14, 2017, [http://geostat.ge/index.php?action=page&p\\_id=134&lang=eng](http://geostat.ge/index.php?action=page&p_id=134&lang=eng).

<sup>2</sup> “Product Exports by Georgia to China 2015”, wits.worldbank.org, accessed September 6, 2017, <http://wits.worldbank.org/CountryProfile/en/Country/GEO/Year/2015/TradeFlow/Export/Partner/CHN/Product/All-Groups>.

## Georgia's Annual Exports to China

Year	2009	2010	2011	2012	2013	2014	2015	2016
<b>Amount (Thsd. USD)</b>	5,965.54	27,050.41	28,970.02	25,674.69	33,955.97	90,393.33	125,800.20	169,586.85
<b>Percentage increase, year-on-year</b>	N/A	353.44%	7.09%	-11.37%	32.25%	166.20%	39.17%	34.80%

Source: GeoStat<sup>3</sup>



<sup>3</sup> Ibid.



## China's Annual Exports to Georgia

Year	2009	2010	2011	2012	2013	2014	2015	2016
<b>Amount (Thsd. USD)</b>	174,571.29	335,160.02	527,701.10	614,416.70	612,250.18	733,467.55	587,298.86	547,768.81
<b>Percentage increase, year-on-year</b>	N/A	91.99%	57.45%	16.43%	-0.035%	19.80%	-19.93%	-6.73%

Source: GeoStat<sup>4</sup>

The trade relationship should be augmented by the FTA signed by the two countries in May 2017. According to the FTA, Georgia will eliminate tariffs on 95.6% of Chinese export categories, while 91% of Georgia's export categories will be exempt from tariffs immediately upon the agreement's entry into force.<sup>5</sup> An additional 3% of Georgia's export categories will be exempted from tariffs within five years from entry into force. The FTA is likely to be favorable to Georgia—given the fact that Georgia already allows the import of nearly all Chinese imports at near-zero tariffs, its exporters stand to gain disproportionately from the reciprocity secured by the FTA. A 2015 feasibility study conducted by the Tbilisi-based Policy Management Consulting Group (PMCG) estimated that the elimination of all tariffs on Chinese goods would result in a 1.6-2.2% annual increase in Chinese exports to Georgia.<sup>6</sup> By contrast, China's elimination of all tariffs on Georgian goods would result in a 9% annual increase in Georgian exports to China.<sup>7</sup> Trade liberalization promises to expand opportunities for Georgian exporters without the risk of flooding the country's consumer markets with cheap import goods. Chinese exporters will benefit marginally while Georgian exporters will enjoy vastly increased access to Chinese consumer markets, especially for wine and non-alcoholic beverages.<sup>8</sup>

China has also become an important source of FDI for Georgia. In 2014, inbound FDI from China amounted to \$218 million, putting it in fourth place behind Azerbaijan, The Netherlands, and The United States.<sup>9</sup> The largest single foreign investor in Georgia is Hualing

<sup>4</sup> "Georgian Imports by Countries", GeoStat, accessed June 14, 2017, [http://geostat.ge/index.php?action=page&p\\_id=134&lang=eng](http://geostat.ge/index.php?action=page&p_id=134&lang=eng).

<sup>5</sup> "China, Georgia sign FTA", The State Council of the People Republic of China, last modified May 15, 2017, accessed August 17, 2017, [http://english.gov.cn/news/international\\_exchanges/2017/05/15/content\\_281475656216746.htm](http://english.gov.cn/news/international_exchanges/2017/05/15/content_281475656216746.htm).

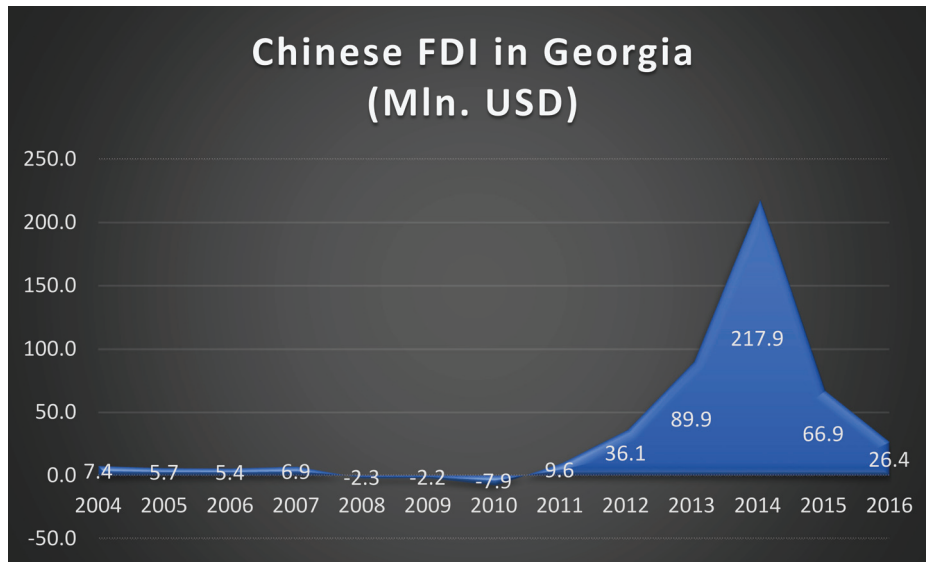
<sup>6</sup> "Joint Feasibility Study on China-Georgia Possible Free Trade Agreement", PMC Research Center, July 30, 2015, accessed June 30, 2017, p. 121.

<sup>7</sup> Ibid, p. 122.

<sup>8</sup> Ibid.

<sup>9</sup> "Foreign Direct Investments by Countries", GeoStat, accessed June 18, 2017, [http://geostat.ge/index.php?action=page&p\\_id=2231&lang=eng](http://geostat.ge/index.php?action=page&p_id=2231&lang=eng).

Group, a Chinese company that has invested more than \$500 million dollars in eight projects in Georgia since 2007.<sup>10</sup> The company's projects include a Free Industrial Zone in Kutaisi, a sprawling residential and commercial complex outside Tbilisi, and a wood processing plant, among others.<sup>11</sup> Hualing Group employs more than 3,000 people in its various enterprises in Georgia.



### Chinese Foreign Direct Investment in Georgia

Year	2009	2010	2011	2012	2013	2014	2015	2016
<b>Amount (Thsd. USD)</b>	-2,236.97	-7,882.02	9,643.09	36,126.09	89,874.19	217,944.39	66,947.63	26,433.30
<b>Percentage increase year-on-year</b>	N/A	-247.88%	222.34%	274.63%	148.78%	142.50%	-69.28%	-59.02%

Source: GeoStat<sup>12</sup>

Chinese companies have established footholds in Georgia's service sector, especially in the fields of finance, telecommunications, and tourism. In telecommunications, two Chinese companies are important market players – ZTE Corporation and HUAWEI Technology Co.,

<sup>10</sup> "Hualing Group – Top Investor of Georgia", hualing.ge, accessed September 6, 2017, <http://hualing.ge/language/en/hualing-group-top-investor-of-georgia/>.

<sup>11</sup> "Projects", Hualing.ge, accessed June 10, 2017, <http://hualing.ge/language/en/tbilisi-sea-new-city-2/>.

<sup>12</sup> "Foreign Direct Investments by Countries", GeoStat, accessed June 14, 2016, [http://geostat.ge/index.php?action=page&p\\_id=2231&lang=eng](http://geostat.ge/index.php?action=page&p_id=2231&lang=eng).

Ltd – specializing in the provision of mobile phone services. In finance, Hualing Group purchased a controlling share in Georgia’s Basis Bank in 2012.<sup>13</sup> In 2016, Basis Bank received a \$5 million credit line from the state-owned Development Bank of China – an example of Chinese state involvement in matters of foreign investment and commerce.

However, it should be noted that inbound FDI has fallen off since 2014. That is due to the preponderance of one firm, Hualing, as the main source of FDI.<sup>14</sup> The company made most of its investments between 2007 and 2015. New large investors are needed. Liu Bo, economic and commercial counsellor of the Chinese Embassy in Georgia, expressed optimism in an interview in 2016:

*Georgia has a very good investment environment and a simple tax regime. It is attractive to potential investors from many countries including China ... The decrease of FDI from China in 2015 does not mean that Georgia is no longer an attractive place for Chinese investors.*<sup>15</sup>

Georgia is a member of several Chinese-led multilateral institutions, including the Asian Infrastructure Investment Bank (AIIB). Tbilisi hosted the AIIB’s sixth meeting of chief negotiators in 2015. According to the AIIB, Georgia is “strategically located at cross roads [sic] between the Black Sea and the Caspian Sea making it a regional transit corridor. By investing in transportation and other communication infrastructure, it can play a significant role in regional trade by providing increased connectivity between Western Asia, Central Asia and Europe.”<sup>16</sup> On June 15, 2017, Georgia signed a \$114 million agreement with the AIIB, according to which the bank will finance the Batumi Bypass Road Project. The project is intended to facilitate the flow of commercial traffic between Georgia and Turkey, which could serve Chinese interests as well as those of Georgia.<sup>17</sup>

Georgia’s primary importance to China is its role as a transportation hub linking Asia to Europe via the BRI launched by China in 2013. Georgia is already a member of the Transport Corridor Europe-Caucasus-Asia (TRACECA), a regional infrastructure initiative which

<sup>13</sup> “Hualing Group enters into preliminary agreement to acquire majority stake of Bank Republic, a subsidiary of Societe Generale in Georgia”, Hualing.ge, accessed August 7, 2017, <http://hualing.ge/language/en/hualing-group-enters-into-preliminary-agreement-to-acquire-majority-stake-of-bank-republic-a-subsi-dary-of-so-ciete-generale-in-georgia/>.

<sup>14</sup> Giorgi Mzhavanadze (senior researcher at the International School of Economics at Tbilisi State University) in discussion with the author, September 2017.

<sup>15</sup> Madona Gasanova, “Chinese Investments to Georgia to Surge in 2016”, The Financial, accessed September 7, 2017, <http://www.finchannel.com/index.php/world/georgia/56004-chinese-investments-in-georgia-to-surge-in-2016>.

<sup>16</sup> “Georgia: Batumi Bypass Road Project”, AIIB.org, accessed July 5, 2017, <https://www.aiib.org/en/projects/approved/2017/batumi-bypass-road-project.html>.

<sup>17</sup> Ibid.

the BRI seeks to build upon.<sup>18</sup> Additionally, Georgia is a participant in the Trans-Caspian International Transport Route (TITR). The TITR was established under the auspices of the BRI in October 2016 to connect China to Ukraine and Turkey via Kazakhstan, Azerbaijan, and Georgia.<sup>19</sup>

While China accounts for a growing portion of Georgia's foreign trade turnover and is an important source of FDI, there is little risk it will become overdependent on China, as some smaller Asian nations have become. The same factor that limits China's presence in Georgia—geographic distance—helps insulate Georgia from overdependence, as do its strong economic ties to regional actors such as Azerbaijan, the EU, and Turkey. A relatively small—and not increasing—proportion of consumer goods imported into Georgia come from China. Many of the categories of consumer goods that China exports are currently supplied by other markets, especially Turkey.<sup>20</sup>

## Georgia-China Ties in Diplomacy and Security

China has heretofore shown little diplomatic or strategic interest in Georgia or in the South Caucasus more generally. Rather, it tends to focus on less-politicized issues such as trade relations and infrastructure investment. China has no military presence in the region and is unlikely to establish any in the foreseeable future. However, Georgian and Chinese diplomatic interests align on certain key issues, in particular state sovereignty and territorial integrity. In September 2008, the Chinese Foreign Ministry expressed its concern at the “latest development in South Ossetia and Abkhazia”, referring specifically to Russia's decision to recognize both breakaway territories as independent republics.<sup>21</sup> China has continued to express support for Georgia's territorial integrity in the years since.<sup>22</sup> Notably, that support has been firmer than China's support for Ukraine's territorial integrity. For example, in March 2014 China abstained from voting on a United Nations Security Council resolution to

<sup>21</sup> “China ‘concerned’ of situation in S. Ossetia, Abkhazia”, Xinhua News Agency, last modified August 28, 2008, accessed June 14, 2017, [http://www1.china.org.cn/international/foreign\\_ministry/2008-08/28/content\\_16349443.htm](http://www1.china.org.cn/international/foreign_ministry/2008-08/28/content_16349443.htm).

<sup>22</sup> Paul Stronski and Alexandra Vreeman, “Georgia at Twenty-Five: In a Difficult Spot”, Carnegie Endowment, last modified May 25, 2017, accessed June 1, 2017, <http://carnegieendowment.org/2017/05/25/georgia-at-twenty-five-in-difficult-spot-pub-70074>.

<sup>18</sup> TRACECA was launched in 1993 under the leadership of the European Union to foster trade facilitation and road, rail, and maritime transport in the region between the EU and Central Asia. It originally included eight countries—Armenia, Azerbaijan, Georgia, Kazakhstan, Kyrgyzstan, Tajikistan, Turkmenistan, and Uzbekistan—with Iran, Moldova, Romania, Turkey, and Ukraine joining later.

<sup>19</sup> Yerbolat Uatkhanov, “Kazakhstan, Azerbaijan and Georgia sign Trans-Caspian International Transport Route protocol”, The Astana Times, last modified April 7, 2017, accessed August 14, 2017, <http://astanatimes.com/2017/04/kazakhstan-azerbaijan-and-georgia-sign-trans-caspian-international-transport-route-protocol/>.

<sup>20</sup> In 2015, total consumer goods imports from China were worth \$257 million, less than 6% of the total. By contrast, consumer goods imports from Turkey—Georgia's leading source of imports—were worth \$693 million, nearly 16% of the total (source: [wits.worldbank.org](http://wits.worldbank.org)).

declare invalid the results of the Crimea referendum. Stronger support for Georgia clearly indicates that cooperation extends beyond the fields of trade and investment.

Georgia is not a member of the Shanghai Cooperation Organization (SCO), a Chinese-led multilateral security organization launched in 2001. However, its interests often align with those of the organization's members. The SCO is devoted to combatting the "three evils" of terrorism, separatism, and extremism, to which Georgia is also committed. During and after the Russian invasion of Georgia in August 2008 the SCO member states refused to support Moscow's position despite appeals from the Russian Foreign Ministry. Instead, they issued a statement titled the "Dushanbe Declaration" that called on all parties to solve the "existing problems" in South Ossetia through dialogue and negotiation.<sup>23</sup> The Dushanbe Declaration was a diplomatic defeat for Russia, which had lobbied the SCO to clearly back its position and recognize South Ossetia and Abkhazia as independent states, to no avail.<sup>24</sup>

Chinese interests in Georgia currently focus on the economic sphere. However, as demonstrated above, the two countries share a common foundation for closer diplomatic cooperation. Additionally, deepening economic relations have a geopolitical corollary – by increasing its economic footprint, China would have a growing interest in Georgia's stability and security. That interest stands to increase as Georgia expands its involvement with the BRI.

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<sup>23</sup> "Dushanbe Declaration", Shanghai Cooperation Organization, last modified August 27, 2008, accessed August 15, 2017, <http://eng.sectsc.org/load/198068/>.

<sup>24</sup> "SCO Fails to Back Russia over Georgia", RFE-RL, last modified August 28, 2008, accessed June 28, 2017, [https://www.rferl.org/a/SCO\\_Fails\\_To\\_Back\\_Russia\\_Over\\_Georgia/1194578.html](https://www.rferl.org/a/SCO_Fails_To_Back_Russia_Over_Georgia/1194578.html).

## THE BELT AND ROAD

China officially announced the Belt and Road initiative in 2013, hailing it as “the project of the century.”<sup>25</sup> The BRI is a diverse series of projects and encompasses both land and sea corridors and includes 65 countries, nearly two-thirds of the world’s population, and one-third of global GDP. More of a concept rather than a clearly-defined set of projects, it is a flexible initiative that covers new and pre-existing projects. The BRI aims to open trade routes for Chinese products and promote enhanced security on China’s western flank, including in its restive border region of Xinjiang. The BRI is also intended to secure the stable flow of energy supplies from Russia and Central Asia. From the Chinese perspective, reducing physical and political barriers to trade will open new markets for its exports and foster regional security through enhanced cooperation. If implemented successfully, the project promises to promote all four of the Chinese government’s main foreign policy aims<sup>26</sup>: 1) Pacifying its periphery (through economic development and cooperation on counter-terrorism activities); 2) sustaining high economic growth (by securing foreign markets); 3) maintaining internal order (see goals number 1 and number 2); and 4) cementing its international status (by becoming a regional power in Eurasia).



Economist.com

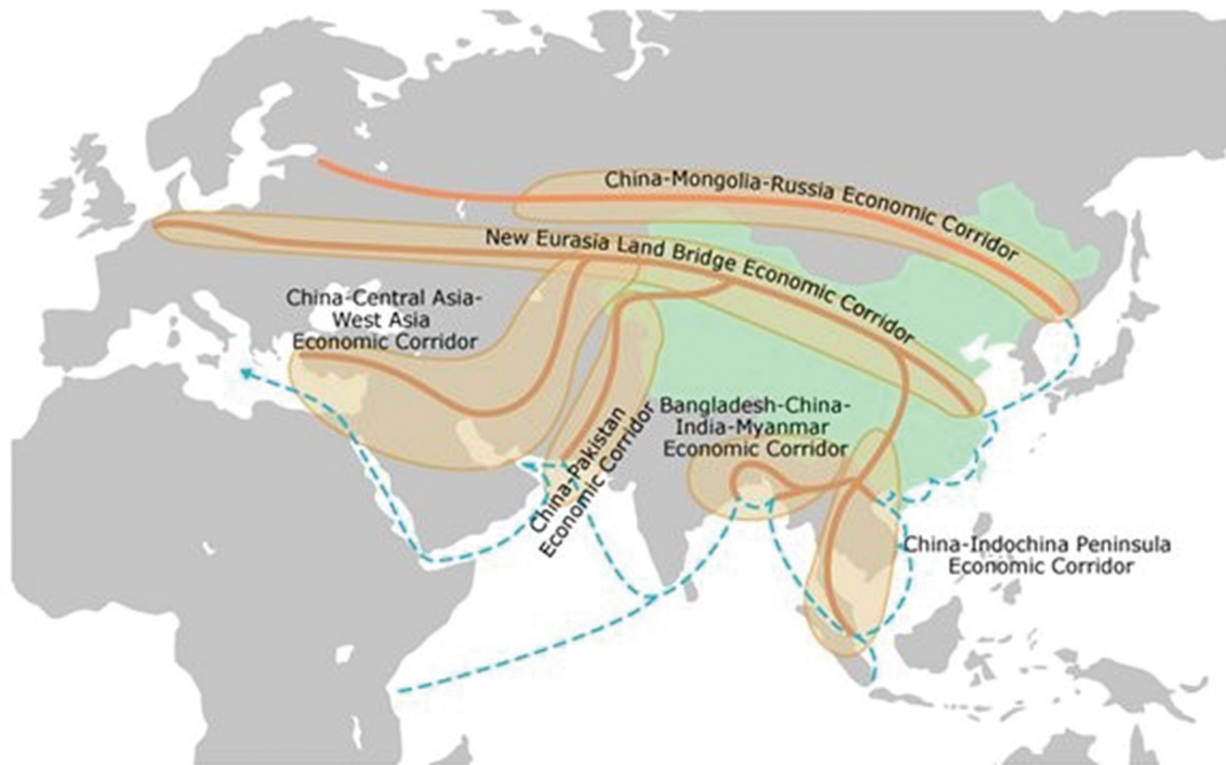
Source: The Economist

<sup>25</sup> The initiative was originally titled “One Belt, One Road” but was later re-branded due to political considerations.

<sup>26</sup> Robert D. Blackwill and Ashley J. Tellis, “Revising U.S. Grand Strategy Toward China”, Council on Foreign Relations, Special Report No. 72, March 2015, accessed August 22, 2017, p. 10-17.

The BRI is divided into a land component, the Silk Road Economic Belt (SREB); and a sea component, the 21st Century Maritime Silk Road. The overarching goal of the SREB is to “shorten the distance between China and Europe” through investment in new and existing transport corridors.<sup>27</sup> It encompasses six corridors that connect China to Europe via different overland routes (Georgia is directly involved in the China-Central Asia-West Asia Corridor). The diversified nature of the SREB is intended to give China maximum strategic leverage. Because China will have multiple connections to Europe, no other country will be able to leverage its position to dictate terms of trade or investment. It is thus one belt weaved from a number of independent strands. The BRI tends to focus on bilateral agreements between China and its junior partners rather than broader multilateral groupings, hence the “hub and spokes” metaphor is frequently used. However, the initiative’s massive scope means that participant countries have incentives to cooperate on the multilateral level.

#### The Belt and Road Initiative: Six Economic Corridors Spanning Asia, Europe and Africa



Source: Hong Kong Trade Development Council

The Chinese government is financing the project via three state-sponsored financial institutions: The Silk Road Fund, the China Development Bank, and the Export and Import Bank of China. According to an estimate by the European Council on Foreign Relations, the

<sup>27</sup> Pieter Van Dijk and Patrick Martens, “The Silk Road and Chinese interests in Central Asia and the Caucasus: the case of Georgia” (presentation, MSM 2016 Research Conference, August 30, 2016 (p. 3)).

Chinese government alone can provide as much financing per year as the World Bank and Asian Development Bank combined.<sup>28</sup> Additionally, two Chinese-led multilateral institutions are providing financing for the project: the Beijing-based AIIB and the Shanghai-based New Development Bank (NDB; sometimes referred to as the “BRICS Bank”) – with a combined registered capital of \$150 billion. Private investors from China and around the world are also putting money into BRI-related projects.

Total investment in BRI-related infrastructure projects amounted to an estimated \$401 billion in 2016, an increase of 2.1% from the previous year.<sup>29</sup> While that increase is modest, it should be noted that average economic growth in BRI countries decelerated in 2016. Another \$93 billion were invested in BRI-related mergers and acquisitions in 2016.<sup>30</sup>

A report by PWC found that average project value increased in 2016, as more value was generated despite an absolute drop in the number of projects being implemented.<sup>31</sup> That means that the Chinese government as well as the companies and financial institutions implementing the project are seeking quality over quantity in terms of projects – what PWC calls a “flight to quality.”<sup>32</sup> Given Georgia’s attractiveness to profit-seeking investors, such an approach could give it an advantage over countries with weaker business environments.

## Georgia’s Place on the Belt and Road

Due to this paper’s emphasis on Georgia-China relations, space is devoted to analysis of the SREB only. Georgia’s government has made considerable efforts to deepen relations with China in the context of the initiative. In a May 2017 interview with China’s Xinhua news service, Georgian Finance Minister Dmitri Kumsishvili emphasized the potential of Georgia’s involvement in the SREB to “promote regional connectivity, enhance human exchanges, and expand trade and investment.”<sup>33</sup>

Georgia is involved directly in the China-Central Asia-West Asia Corridor – one of six overland corridors making up the SREB – stretching from China in the east to Turkey and the Black Sea in the west. Georgia offers both land and sea transport routes that are important

<sup>28</sup> Mathieu Duchâtel, François Godement, Kadri Liik, Jeremy Shapiro, Louisa Slavkova, Angela Stanzel and Vessela Tcherneva, “Eurasian Integration: Caught Between Russia and China”, European Council on Foreign Relations, last modified June 7, 2016, accessed July 10, 2017, [http://www.ecfr.eu/article/essay\\_eurasian](http://www.ecfr.eu/article/essay_eurasian).

<sup>29</sup> Gabriel Wong, Simon Booker, and Guillaume Barthe-Dejean, “China and Belt & Road Infrastructure: 2016 review and outlook”, PWC B&R Watch, February 2017: 9.

<sup>30</sup> *Ibid.*, p. 11.

<sup>31</sup> “China and Belt & Road Infrastructure: 2016 review and outlook”: 11.

<sup>32</sup> *Ibid.*

<sup>33</sup> “Interview: Georgia to contribute to Belt and Road Initiative: deputy PM”, Xinhua News Agency, last modified May 10, 2017, accessed August 4, 2017, [http://news.xinhuanet.com/english/2017-05/09/c\\_136266698.htm](http://news.xinhuanet.com/english/2017-05/09/c_136266698.htm).



to the China-Central Asia-West Asia Corridor. First, Georgia provides an overland route to Turkey, especially via the Baku-Tbilisi-Kars (BTK) railway. Once that railway is completed, combined with the Yavuz Sultan Selim Koprosu Bridge connecting Asia to Europe across the Bosphorus, Georgia will have an uninterrupted rail link to Europe.<sup>34</sup> Second, Georgia can serve as a maritime outlet to Europe via its ports in Batumi, Poti, and Anaklia. The \$2.5 billion Anaklia Black Sea Deep Water Port Project is of particular importance. Scheduled for completion by 2020, it will be Georgia's first-ever deep-water port at 17 meters, capable of handling 900,000 Twenty-Foot Equivalent Units (TEU) annually, roughly 50 percent more than the capacity of Poti, currently Georgia's largest seaport.<sup>35</sup> The port complex will include a Free Industrial Zone allowing businesses to produce goods for export under a tax-free regime.

The China-Central Asia-West Asia Corridor builds upon the transport route already created by TRACECA, which Georgia has participated in since its inception in 1993.<sup>36</sup> Building upon rather than supplanting TRACECA is indicative of the concept underpinning the BRI: China is attempting to build a diverse and inclusive set of transportation corridors which complement existing infrastructure initiatives.

The BRI presents an opportunity for Georgia to maximize its potential as the fulcrum of two nascent regional groupings, the Georgia, Ukraine, Azerbaijan, and Moldova (GUAM) group and the Azerbaijan, Georgia, Turkey trilateral group (AGT). Within GUAM, Georgia is uniquely positioned to link China to Ukraine and Moldova via its Black Sea ports. That is increasingly important, as Ukraine-China trade volumes have grown significantly since 2013. In 2015, China was the largest consumer of Ukraine's agricultural exports and the third-largest consumer of its exports overall.<sup>37</sup> In 2015, Ukraine formally became part of the SREB, sending a train to China via the TITR that passes through Georgia, Azerbaijan, and Kazakhstan.<sup>38</sup>

<sup>34</sup> John C.K. Daly, "China deepens its presence in Georgia via its 'One Road, One Belt' initiative", *The Central Asia-Caucasus Analyst*, last modified December 12, 2016, accessed June 28, 2017, <https://www.cacianalyst.org/publications/analytical-articles/item/13413-china-deepens-its-presence-in-georgia-via-its-one-road-one-belt-initiative.html>.

<sup>35</sup> Joseph Larsen, "Georgia: The Black Sea Hub for China's 'Belt and Road'", *The Diplomat*, last modified May 3, 2017, accessed August 7, 2017, [https://www.google.ge/url?sa=t&rct=j&q=&esrc=s&source=web&cd=1&cad=rja&uact=8&ved=0ahUKEwilpt-VktvVAhXqO5oKHUpkBDMQFggkMAA&url=http%3A%2F%2Fthediplomat.com%2F2017%2F05%2Fgeorgia-the-black-sea-hub-for-chinas-belt-and-road%2F&usg=AFQjCNGn-8pRvhl1HvTQ2-\\_6p5mm1tuLkqg](https://www.google.ge/url?sa=t&rct=j&q=&esrc=s&source=web&cd=1&cad=rja&uact=8&ved=0ahUKEwilpt-VktvVAhXqO5oKHUpkBDMQFggkMAA&url=http%3A%2F%2Fthediplomat.com%2F2017%2F05%2Fgeorgia-the-black-sea-hub-for-chinas-belt-and-road%2F&usg=AFQjCNGn-8pRvhl1HvTQ2-_6p5mm1tuLkqg).

<sup>36</sup> While still officially in operation, TRACECA is widely viewed as a failure. From its launch in 1993 up to the time of writing, the European Commission, the driving force behind the process, has financed only 85 projects worth a total of 178 million euros.

<sup>37</sup> [www.trademap.org](http://www.trademap.org), accessed August 7, 2017.

<sup>38</sup> "Ukraine expects new infrastructure projects from Belt and Road forum: deputy minister", *Xinhua News Agency*, last modified May 1, 2017, accessed August 9, 2017, [http://news.xinhuanet.com/english/2017-05/01/c\\_136247844.htm](http://news.xinhuanet.com/english/2017-05/01/c_136247844.htm).

In addition to participation in the Trans-Caspian International Transport Route, Georgia has directly strengthened its infrastructure links with Ukraine. Completion of the Anaklia Black Sea Deep Water Port is expected to foster increased bilateral trade.<sup>39</sup> The new port will be able to service 10,000 TEU container ships bound to and from Ukraine's ports – ships which are too large for Georgia's existing ports at Batumi and Poti. Given that all four GUAM countries are participating in the BRI to varying degrees, the initiative should give them added incentive to cooperate on matters of infrastructure and trade.

Georgia can play a similar role in AGT. First announced in the 2012 Trabzon Declaration, the group came about following the launch of the Baku-Tbilisi-Ceyhan oil pipeline, and is thus both the product of and the impetus for regional cooperation. The group primarily functions as a mechanism for guaranteeing energy flows from Azerbaijan and Central Asia to Turkey, with Georgia acting as a geographic bridge.<sup>40</sup> The three countries already host the BTK railway, which forms part of the China-Central Asia-West Asia Corridor. AGT exemplifies the spillover effects of economic cooperation: Since 2014, the countries have participated in annual defense ministerials.<sup>41</sup>

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<sup>39</sup> "Anaklia port – Georgia's key to the new 'Silk Road' of the 21st century", Front News International, last modified August 6, 2017, accessed August 14, 2017, <https://frontnews.eu/news/en/9871/Anaklia-port-Georgias-key-to-the-new-Silk-Road-of-the-21st-century>.

<sup>40</sup> Michael Hikari Cecire "Turkey-Georgia-Azerbaijan: Trilateralism and the Future of Black Sea Regional Geopolitics", The Central Asia-Caucasus Analyst, last modified October 16, 2013, accessed August 3, 2017, <https://www.cacianalyst.org/publications/analytical-articles/item/12837-turkey-georgia-azerbaijan-trilateralism-and-the-future-of-black-sea-regional-geopolitics.html>.

<sup>41</sup> Zaur Shiriyev, "Institutionalizing a Trilateral Strategic Partnership: Azerbaijan, Georgia, Turkey", Konrad Adenauer Stiftung, 2016, accessed September 6, 2017, [http://www.kas.de/wf/doc/kas\\_43884-1522-1-30.pdf?160111112351](http://www.kas.de/wf/doc/kas_43884-1522-1-30.pdf?160111112351).

## GEOPOLITICAL IMPLICATIONS

The Chinese authorities have taken pains to present the BRI as an economic rather than a geopolitical undertaking. The BRI is usually referred to in official communications as an “initiative” rather than a “strategy.” Chinese Foreign Minister Wang Yi even stated in 2015 that the initiative was “not a tool of geopolitics.”<sup>42</sup>

A 2015 white paper published by the Chinese National Development and Reform Commission emphasized that the BRI is aimed at “broader and more in-depth regional *cooperation*” [emphasis mine].<sup>43</sup> The white paper identifies five “connections” to be secured by the BRI, of which three are primarily economic (infrastructure, trade, and finance) and two primarily strategic (policy communication and “connecting the people’s minds”).<sup>44</sup> The white paper makes clear that the Chinese government intends for the BRI to be an open, inclusive format for cooperation among sovereign states. It does not intend it to compete with institutionalized regional structures such as the EU and the Eurasian Economic Union (EEU).

The BRI is primarily economic in nature. However, the geopolitical implications are obvious. Trade and investment do not occur in a political vacuum; states cannot conduct geo-economics without conducting geopolitics. Writes Robert Gilpin: “The role of markets in achieving those goals are determined by political processes.”<sup>45</sup> Even the market activity of private Chinese firms is affected by political considerations.

The white paper expresses specific geopolitical objectives, framing the BRI as a means of “embracing the trend towards a multipolar world”, a clear reference both to China’s status as a rising international power and to the relative decline of the U.S.<sup>46</sup> Whether deliberate or not, economic engagement in Central Asia and the South Caucasus will give the Chinese government a direct interest in maintaining regional stability. In the words of one scholar of Chinese foreign policy based in the US, “Beijing is hoping that BRI can further expand China’s diplomatic influence in Asia and beyond.”<sup>47</sup>

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<sup>42</sup> “China’s 2015 diplomacy focuses on ‘Belt and Road’”, *Chinadaily.com*, last modified March 3, 2015, accessed July 5, 2017, [http://www.chinadaily.com.cn/china/2015twosession/2015-03/08/content\\_19750295\\_2.htm](http://www.chinadaily.com.cn/china/2015twosession/2015-03/08/content_19750295_2.htm).

<sup>43</sup> “Vision and Actions on Jointly Building Silk Road Economic Belt and 21st-Century Maritime Silk Road”, National Development and Reform Commission, Ministry of Foreign Affairs, and Ministry of Commerce of the People’s Republic of China, last modified March 28, 2015, accessed July 5, 2017, [http://en.ndrc.gov.cn/newsrelease/201503/t20150330\\_669367.html](http://en.ndrc.gov.cn/newsrelease/201503/t20150330_669367.html).

<sup>44</sup> *Ibid.*

<sup>45</sup> Robert Gilpin, *Global Political Economy: Understanding the International Economic Order* (Princeton University Press, 2001): 24.

<sup>46</sup> *Global Political Economy*: 24.

<sup>47</sup> Xiaoyu Pu, “One Belt, One Road: Visions and Challenges of China’s Geoeconomic Strategy”, *Academia.edu*, accessed June 15, 2017: 115.

In 2012, Wang Jisi, dean of international strategic studies at Peking University and one of China's most influential scholars, called for a strategy of "Westward March" in response to the Obama administration's "Pivot to Asia."<sup>48</sup> Wang's idea was studied closely by Chinese policymakers for feasibility and the potential reactions it would elicit from external states. Wang and other proponents of Westward March view it as a shrewd strategy for managing relations with the U.S.: The two countries share common interests in the region and deeper Chinese engagement can give it strategic leverage vis-à-vis the U.S., a country that needs powerful partners to help stabilize Afghanistan and Pakistan.

The geopolitical motivations and aims of BRI are still being articulated. However, it cannot be disputed that the project has an important geopolitical component, mainly to solidify China's status as the dominant power in Eurasia. That point is of particular importance to Georgia, given its fraught relations with Eurasia's traditional hegemon, Russia. Greater assertiveness on the part of China has the potential to alter Russia's strategic considerations in Georgia and the wider region.

## China-Russia Relations on the Belt and Road

For Russia, the geopolitical implications of the BRI are complex. Russia agreed to support the initiative in 2015, albeit with some trepidation. In May 2015, Russia and China declared a partnership between the BRI and the Russia-led EEU. In a speech following his meeting with Chinese President Xi Jinping, Russian President Vladimir Putin touted "the integration of the Eurasian Economic Union and Silk Road projects" and the two countries' shared interest in creating a "common economic space on the continent."<sup>49</sup> Russia is involved in the BRI through participation in two SREB corridors: The China-Mongolia-Russia Corridor and the New Eurasian Land Bridge. Russia views the initiative largely as a mechanism for legitimating the EEU on the global stage and funneling Chinese investment into Russia and other EEU member countries.<sup>50</sup> The BRI could also buoy Russian energy producers by diverting Central Asian energy supplies away from Europe toward China, thereby increasing European demand for Russian supplies.<sup>51</sup>

<sup>48</sup> Yun Sun, "March West: China's Response to the U.S. Rebalancing", The Brookings Institution, last modified January 31, 2013, accessed July 5, 2017, <https://www.brookings.edu/blog/up-front/2013/01/31/march-west-chinas-response-to-the-u-s-rebalancing/>.

<sup>49</sup> "Russia, China agree to integrate Eurasian Union, Silk Road, sign deals", RT, May 8, 2015, accessed July 10, 2017, [https://www.google.ge/url?sa=t&rct=j&q=&esrc=s&source=web&cd=1&cad=rja&uact=8&ved=0ahUKEwiDyt6gldvVAhWkdpoKHZoMbb4QFggoMAA&url=https%3A%2F%2Fwww.rt.com%2Fbusiness%2F256877-russia-china-deals-cooperation%2F&usq=AFQjCNFqVoOc3Fow\\_NSKeLuWaQ4C2n32ZA](https://www.google.ge/url?sa=t&rct=j&q=&esrc=s&source=web&cd=1&cad=rja&uact=8&ved=0ahUKEwiDyt6gldvVAhWkdpoKHZoMbb4QFggoMAA&url=https%3A%2F%2Fwww.rt.com%2Fbusiness%2F256877-russia-china-deals-cooperation%2F&usq=AFQjCNFqVoOc3Fow_NSKeLuWaQ4C2n32ZA).

<sup>50</sup> Richard Ghasy and Jiayi Zhou, "The Silk Road Economic Belt: Considering security implications and EU-China cooperation prospects", Stockholm International Peace Research Institute, February 2017, accessed June 15, 2017: 40-41.

<sup>51</sup> Ibid.

In official statements, both countries refer to the two initiatives as complementary, not competitive. China is viewed as the leader in economic development in Asia, while Russia is viewed as the main provider of security and military hardware. It is widely believed that Russia has chosen to participate in the BRI as a hedge against its deepening isolation from Europe, while China seeks to benefit from Russia's military presence in Central Asia. In the Chinese view, Russia plays an important role fostering stability and supporting counterterrorism activities in Central Asian states, key priorities given instability in Kyrgyzstan and in China's western province of Xinjiang.

The two roles cannot be compartmentalized. Russia has recently turned eastward out of necessity to mitigate the effects of its isolation from the EU. It is largely dependent on China economically and is viewed by the Chinese authorities as a junior partner. Unless Russia is willing to take on a subordinate role indefinitely the current arrangement is not a recipe for sustainable strategic partnership. If history is an indicator, Russia will tire of an imbalanced power dynamic. China's leverage is likely to only increase as its economy expands and Russia's continues to stagnate. Moreover, Russia is only one of many participants in the BRI. China will have numerous options for transporting goods to Europe that don't require Russia's involvement.

While Russian state officials have been careful not to reveal any actual or potential cracks in the relationship, some Russian experts are more outspoken. In a 2009 interview (prior to announcement of the BRI) Mikhail Troitskiy of the Moscow State Institute of International Relations summed up Russian suspicions of China generally:

*We are also suspicious of China's actions in Central Asia and Africa. The debate that is beginning to go on here is about how China is trying to subjugate Russia. Many see China as a rival and we should be alert to the potential China threat – especially in the Far East, where there deep fears of falling into China's orbit.<sup>52</sup>*

Another Russian sinologist pointed to Chinese engagement in the Russian Far East and Central Asia while commenting that "China is turning into a competitor and is becoming a big headache."<sup>53</sup>

Moreover, the EEU and the BRI don't appear to be as compatible as the Russian and Chinese authorities claim. The two initiatives have drastically different institutional designs—the EEU is regional and protectionist; the BRI is extra-regional and inclusive.<sup>54</sup> China views the BRI as a flexible initiative that does not supplant other regional groupings but overlaps with them. For example, China views Russia, Kazakhstan, and Kyrgyzstan as key partners

<sup>52</sup> David Shambaugh, *China Goes Global: The Partial Power* (New York: Oxford University Press, 2014): 85.

<sup>53</sup> *Ibid.*

<sup>54</sup> "The Silk Road Economic Belt: Considering security implications and EU-China cooperation prospects": 40.

in the project, despite all three being members of the EEU. The issue is that the principles of inclusiveness and flexibility are not reciprocated by Russia. The Moscow-led EEU is a customs union with high external tariffs, including tariffs imposed on Chinese goods. This has already created direct problems for Kyrgyzstan, which had to raise tariffs on Chinese goods in order to comply with the EEU's common external tariff, causing trade diversion and resulting in higher consumer prices.<sup>55</sup> The BRI offers potentially greater economic benefits than the EEU – more flexibility, more global interconnectivity, and greater access to foreign investment. Increasing the potential for future friction is that China prefers to conduct diplomacy on the bilateral level, the BRI being essentially a dense web of bilateral agreements. Such an approach does not afford Russia preeminent status in China's dealings with junior EEU members. Despite all the talk of complementarity, Chinese and Russian interests are not closely aligned.

## Geopolitical Implications for Georgia

There are no indications that China and Russia are butting heads over the South Caucasus. However, given the outsized place the region holds in Russian conceptions of statehood and national security, more Chinese engagement is bound to be viewed as a threat in certain Russian policy circles. The Georgian government must develop a strategy for dealing with Russian-Chinese relations that is both cautious and conscious of opportunity. For example, Georgia should promote Chinese engagement for both economic and strategic reasons. Not only can trade and investment links with China help spur economic growth, they also have the potential to ease pressure applied by Russia. Writes Rumer, Sokolski, and Stronski:

*While Beijing and Tbilisi are more economic than security partners, Chinese investment in Georgia does provide certain unanticipated security benefits. In light of Moscow's increased economic and political dependence on Beijing, a greater Chinese presence in the country potentially raises the costs to Russia of engaging in large-scale military escalation.<sup>56</sup>*

One can imagine a hypothetical scenario in which Russia threatens escalation with Georgia, either by dramatically increasing its military presence in Abkhazia and South Ossetia or by threatening military action or economic sanctions. Such a scenario would run counter to Chinese interests commensurate with the degree of its engagement with Georgia. Given Russia's economic and diplomatic dependence on China, the latter could pressure it into refraining from such an escalation. China could cut off investment to Russia and other EEU member countries as well as leverage its advantageous position with regard to trade in

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<sup>55</sup> "The Eurasian Economic Union: Power, Politics and Trade", International Crisis Group, Europe and Central Asia Report #240 (2016): 11.

<sup>56</sup> Eugene Rumer, Richard Sokolsky, and Paul Stronsky, "U.S. Policy Toward the South Caucasus: Take Three", Carnegie Endowment, May 31, 2017, <http://carnegieendowment.org/2017/05/31/u.s.-policy-toward-south-caucasus-take-three-pub-70122>.

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goods.<sup>57</sup> As the senior partner with vastly superior financial resources, China wields a much larger stick. Additionally, deepening economic dependence on China could provide an implicit check on any escalation by Russia.

That being said, Sino-Russian friction could pose its own set of problems for Georgia. If Russia no longer feels its interests are compatible with the BRI it could attempt to interfere in it, for example by discouraging other EEU member states from participating in BRI projects. While that would not affect Georgia directly, the lack of overall success of the project could make investments in Georgia less attractive for China. Thus, a delicate balance is ideal: Enough of a Chinese presence to stimulate economic growth and ease Russian pressure, but not enough to invite a backlash by Russia.

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<sup>57</sup> Russia is more dependent on the bilateral trade relationship. By 2016, 14.1% of Russia's total trade turnover was accounted for by trade with China. By contrast, in 2015 the Russian market accounted for only 2% percent of China's imports and 1.5% of its exports (Sources: EY, World Bank).

## POTENTIAL PITFALLS

Like any ambitious multilateral initiative, the BRI has the potential to fail. Firstly, because it is more a concept than a clear set of projects, its overall success or failure will be difficult to assess. Second, the initiative is dependent on deepening cooperation among a multitude of states with disparate goals and perspectives and, in some cases, historical legacies of war and ethnic and religious hatred. Success requires more than a generous stream of Chinese investment dollars.

If not implemented properly, the BRI could suffer the same fate as past failed grandiose initiatives, ultimately sputtering due to lack of profitability. While the Chinese government has stressed that the initiative will be run according to market principles, skeptics such as Fitch Ratings expect that related projects will not be subject to adequate financial scrutiny.<sup>58</sup> Additionally, Chinese banks have a poor track record of managing risks and efficiently allocating resources to infrastructure projects. There is a risk that political objectives will win out over sound financial logic, leading to diminished profitability. The Chinese government has made efforts to address such risks. In August, the National Development and Reform Commission announced it would begin providing stronger guidance to Chinese companies investing in BRI initiatives on how to manage financial risks.<sup>59</sup>

Moreover, the initiative could be hampered by security concerns. Earlier this year, terrorists in Pakistan killed 12 Chinese citizens in two separate incidents. General anti-Chinese sentiment is also a concern in some participating countries. The problem has already presented itself in several Central Asian countries; concerns about Chinese control of land led to protests in Kazakhstan in 2016, and the Chinese embassy in Kyrgyzstan was bombed the same year. Anti-Chinese sentiment is palpable in Georgia, as well: In 2014, Shalva Natelashvili of the Labor Party stated publicly that Georgia “cannot afford Chinese expansion.”<sup>60</sup>

Lastly, Georgia’s importance to the BRI cannot be taken for granted. Georgia has the potential to form a transport and logistics hub between Europe and Asia but still faces stiff competition from Russia and maritime countries such as Iran and Pakistan (which are involved in the 21st Century Maritime Silk Road). In order to make good on its potential, Georgia’s government and private sector must demonstrate that the country is worthy of sustained economic and political commitment.

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<sup>58</sup> “Fitch: China’s One Belt, One Road Initiative Brings Risks” Reuters, last modified January 26, 2017, accessed August 9, 2017, <http://www.reuters.com/article/idUSFit987609>.

<sup>59</sup> “China to Curb ‘Irrational’ Overseas Belt and Road Investment-State Planner” Reuters, last modified August 18, 2017, accessed August 21 2017, <https://www.reuters.com/article/us-china-economy-odi-idUSKCN1AY-0FN>.

<sup>60</sup> “Newsletter #16”, Media Development Fund, accessed August 7, 2017, <http://eurocommunicator.ge/mdf/uploads//16%20ENG-MDF-GDI%20Newsletter.pdf>.



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## CONCLUSION

Georgia-China economic relations have proceeded apace since the two countries established diplomatic relations in 1992. Bilateral links are notable in the fields of trade and FDI, with the two countries signing an FTA in May 2017. Greater access to the Chinese consumer market combined with FDI from China will promote Georgia's economic development. Economic relations also provide a jumping-off point for closer cooperation in other fields, namely diplomacy and (potentially) security. As China's economic footprint grows, it will have a greater interest in maintaining stability in Georgia and the South Caucasus more generally. Georgia's participation in the BRI is of particular importance, as it provides a format for closer ties with China as well as multilateral cooperation with neighboring states, increasing its regional profile.

Georgia's unique geographical location and position at the fulcrum of GUAM (Georgia, Ukraine, Azerbaijan, Moldova) and the Azerbaijan-Georgia-Turkey trilateral group allow it to act as a bridge between Europe and Asia. Georgia can help "shorten the distance between China and Europe", a key goal of the BRI. Moreover, Georgia's strong business and regulatory environment provide advantages in the service sector, another important component of the BRI.

A deepening relationship with China in the context of the BRI has the potential to promote Georgia's security by easing pressure applied by Russia. As a junior partner within the BRI, Russia lacks leverage vis-à-vis a financially superior China. Beijing could increase the costs of Russian military escalation in the region, including in Georgia. By altering Russia's strategic calculus, a greater Chinese presence in the region has the potential to advance Georgia's key security objective, which is reducing the threat posed by Russia.

## RECOMMENDATIONS

- The government must ensure full and effective implementation of the DCFTA with the European Union and the FTA with China. Effective implementation of both agreements will allow the country to become a trading hub between Europe and Asia, bolstering its export industries and making it more attractive to foreign investors, including from China.
- Georgia's domestic policies must match the objectives of Chinese investors. The government should produce an action plan to clearly articulate its goals and priorities vis-à-vis relations with China. The action plan should include specific policies for promoting Chinese investment in Georgia. In particular, both the government and businesses associations should actively promote Georgia as a destination for Chinese FDI. Inbound FDI has fallen off since 2014, indicating that a more focused approach is needed.
- Georgia should take advantage of its unique position in both GUAM and the tri-lateral group to promote itself as a bridge between Europe and Asia. In particular, Georgia can form the fulcrum of China-Turkey and China-Ukraine trade and infrastructure routes.
- Georgia must improve its domestic infrastructure and governance in order to become a more attractive economic partner. In addition to successful completion of the BTK railway, Georgia must improve the railway connections with its ports, especially the Anaklia Black Sea Deep Water Port.
- Infrastructure development is important. However, Georgia should also leverage its position as a regional leader in the service sector. In particular, Georgia's government and private sector should focus on developing its banking, IT, and telecommunications sectors in order to become a regional services hub. Comparative advantage in these sectors will complement the investments in physical infrastructure made under the BRI. They will also ensure that Georgia is not overly dependent on its role as a transportation hub.
- Georgia should view Sino-Russian relations cautiously. While Georgia should attempt to exploit its relationship with China to strengthen its strategic position vis-à-vis Russia, it should not attempt to drive a wedge between the two powers. Deepening relations with China need not lead to further deterioration of ties with Russia.
- China should be viewed as an option, not an alternative. China is an important source of investment and foreign trade that can bring a degree of stability to the region and ease geopolitical pressure applied by Russia. However, it is unlikely to make a hard power commitment to the region and certainly cannot replace NATO as Georgia's primary security partner. Relations with China should complement Georgia's efforts at Euro-Atlantic integration.





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