

THOUGHT LEADERSHIP BRIEF

KEY POINTS

- ▶ The BRI has led to institutional responses that have increased policy capacity in host countries in Southeast Asia
- ▶ Most effort has focused on creating policy frameworks to direct and negotiate projects. Less attention has gone to strengthening management and monitoring capacity, and providing greater voice to civil society, which may be more crucial to ensuring project sustainability
- ▶ The sustainability of BRI projects benefits both China and the host country. Hence, the Chinese side also should improve its due diligence to ensure that projects do not lead to unsustainable outcomes

The Belt and Road Initiative as a Catalyst for Institutional Development: Evidence from Indonesia, Malaysia, and Myanmar

Angela Tritto



Photo credit: Angela Tritto

Issue

Many of the narratives about China's Belt and Road Initiative (BRI) have been polarized and lacking empirical foundations. Most importantly, analyses have often neglected the role of host countries' agency in negotiating, selecting, managing, and monitoring BRI projects. China's BRI presents a set of options for host countries to engage with China and to attract its capital and technology. On the one hand, Chinese State-backed companies and banks provide resources and, on the other hand, host countries employ these resources according to their needs and their development frameworks.

Institutional quality is widely regarded as a crucial determinant for attracting foreign direct investments (FDI). Critics of the BRI have argued that by targeting developing countries with weak institutions and rule of law, the BRI could lead to an increase in corruption and to poorly conceived infrastructure projects. Indeed, without proper governance and oversight from states and corporations, the BRI could also contribute to environmental degradation and undesirable health and social outcomes. As an example, China has already become the largest source of financing for coal power plants globally, which will not only lock

host countries into fossil-dependent futures, but also contribute to rising emissions of pollutants and carbon that will harm population health and contribute to climate change. Such investments of course are made only at the request or with the assent of host governments, who prioritize short-term growth objectives and may be influenced by rent-seeking opportunities in the mining sector.

But can the BRI also act as a positive catalyst for institutional development? Is there evidence that host countries can, through their agency and by introducing new institutions and policy frameworks, leverage the BRI for their sustainable growth? If so, the BRI could become a vehicle for improving a country's business environment, for rebalancing its development by directing infrastructure and other investments to under-developed regions, for introducing new technologies to the country, and for creating new jobs and knowledge skills.

After all, the development benefits of this initiative heavily depend upon the actions and agency – of key actors (both government and enterprises) on both sides.

Assessment

To investigate the implementation of the Belt and Road Initiative, five field research trips were made to Indonesia, Malaysia, and Myanmar in which interviews with policy-makers, business executives, and leaders of chambers of commerce were conducted. The interviews revealed that all three countries have devised new policy frameworks aimed at leveraging Chinese capital and technology to support their nations' development agendas. Indonesia and Malaysia have instituted a dedicated China desk within their investment promotion or coordination agencies, and Myanmar has BRI Committee led by Daw Aung Sang Suu Kyi herself. Some governments have established new regulations or improved mechanisms to attract more FDI. The additional volume of State-led capital mobilized by the BRI in such a short time has prompted countries to make their investment process more efficient, creating

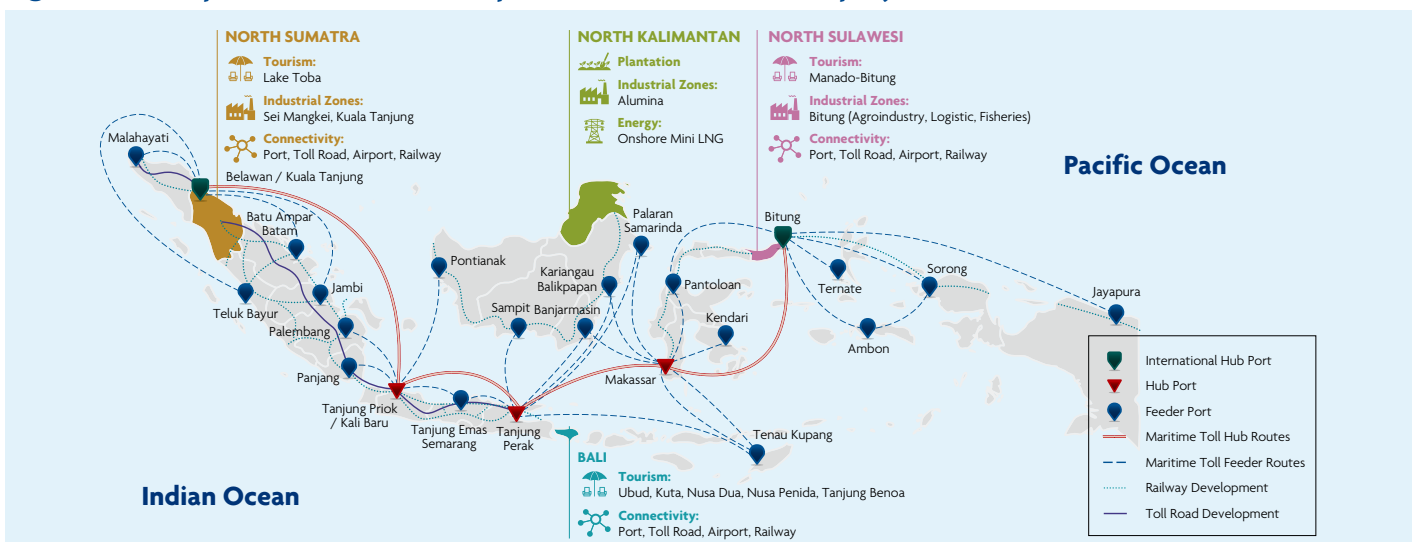
sufficient institutional and policy capacity to be able to attract, manage, and monitor large-scale projects. At the same time, each country continues to face institutional challenges in developing governance systems that promote sustainable development outcomes and reflect the concerns of all stakeholders.

Indonesia

Indonesia is an example of a host country taking a very proactive approach to the BRI. Despite strong anti-China public sentiment, President Widodo followed his predecessor and continued to court medium to long-term Chinese investments to fulfill national development goals. In 2014, he launched his Global Maritime Fulcrum Initiative (GMF), which in many aspects mirrors China's Maritime Silk Road. In 2017, he unveiled a plan to direct Chinese - and subsequently other foreign investments to four Indonesian provinces: North Kalimantan, North Sulawesi, North Sumatra, and Bali. The aim is to increase infrastructure and FDI in these relatively underdeveloped areas, and to connect them to the rest of Indonesia, improving land and maritime connectivity.

The Indonesian government also started a considerable institutional restructuring. The creation of the Coordinating Ministry of Maritime Affairs addressed the need to oversee the implementation of the GMF and lead relevant bilateral negotiations and projects, coordinating internally and externally with China's National Development and Reform Commission. Led by a Chinese expat who lived in Indonesia for over twenty years, the newly established China desk of BKPM, the Indonesia Investment Coordinating Board promotes the country to potential Chinese investors and explains all investment-related regulations to existing businesses. Indonesian government agencies implemented numerous reforms to improve the business environment and accelerate investment realization, such as upgrading the Online Single Submission for business license application, also by consulting the growing number of Chinese companies.

Figure 1: Four provinces have been prioritised for future BRI projects



Indonesia’s policy capacity and institutional restructuring have been among the most impressive; however, the largest BRI-facilitated deals are concerned with the exploitation and development of mineral resources. While these investments led to increased energy capacity – albeit using fossil fuels, and to more value-added exports, a recent report¹ exposed the corruption and rent-seeking behaviour by local and top-ranking politicians into the mining sector. Hence, despite Widodo’s anti-corruption campaign, powerful interests and families still dominate the country, and bribery is still far from eradicated. Moreover, the government is taking an increasingly confrontational stance towards local environmental groups, cutting them out of consultations.

Malaysia

Malaysia is the quintessential example of how, if not adequately managed, governments can use BRI-linked capital unproductively. Under the government of PM Najib Razak (2009-2018), Chinese-backed projects were often negotiated in closed-door meetings and underwent minimal scrutiny. Later, investigations alleged that some of these deals such as the TSGP oil and gas pipeline connecting Borneo to peninsular Malaysia and the MPP Malacca-Johor pipeline were used as vehicles to cover impending debt payments for the 1MDB – Malaysia’s strategic development fund. Embezzlement of the fund became one of the largest graft scandals in modern history, leading to active mobilization against Najib’s corrupt regime, and eventually to his demise. The return of his opponent, Dr. Mahathir Mohamad, saw for the first time in Malaysian history an opposition coalition rise to victory. The new government remains supportive of the BRI, but it has promised a much more transparent and cautious approach, canceling and re-negotiating projects with overinflated costs.

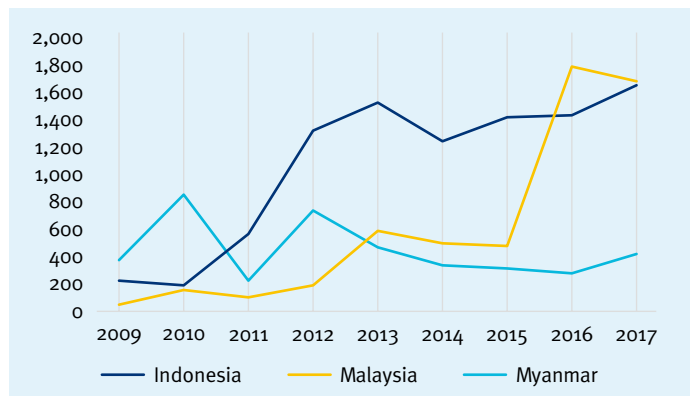
The tendency of Chinese companies to go ‘incentive shopping’ in different Malaysian states is pushing the federal government towards the implementation of stricter requirements on transparency, stronger monitoring of the FDI approval process, and towards the re-drafting of investment incentives. This shift has led to a higher emphasis on localization and on prioritizing high-tech investments to develop Malaysia as one of the digital and automation hubs in Southeast Asia. Furthermore, the country is increasingly turning down investments related to polluting industries while implementing stricter environmental requirements and providing incentives for green FDI. The Malaysian Ministry of International Trade and Investment (MITI) established the Belt and Road Initiative National Secretariat (BRINS) right after the signing of the BRI Memorandum of Understanding between Malaysia and China. In 2019, BRINS was renamed China Section to reflect better the work of the department, which also encompasses other non-BRI related bilateral matters.

Myanmar

Being one of the least developed countries in Southeast Asia, and caught in a prolonged humanitarian crisis that is eroding not only the country’s international reputation but also the government’s ability to function effectively, Myanmar is in a state

of limbo. In recent years, the bitter controversy over the Myitsone dam, which mobilized thousands of people against the potential environmental damage of a large hydropower project to be built by China Power, froze the long-established China-Myanmar diplomatic relations². The case also set a precedent for other civil society-led environmental movements against large-scale hydropower dams in the region. Nevertheless, Chinese investments in the country are set to rise. After the last Belt and Road Forum for International Cooperation, the two governments resumed their collaboration and signed an MOU to move forward with construction of the China-Myanmar Economic Corridor (CMEC). Before signing, the government of Myanmar asked China to agree to three essential conditions, in line with the country’s sustainable development plan. These are that China must allow Myanmar to seek financing from international institutions, to invite other tenders, and to have the last say in which proposed projects can go ahead³. China proposed 38 projects under the CMEC, and so far, Myanmar approved nine of them that are currently being reviewed by the relevant ministries. In November 2018, the country also inked a framework for the development of the Kyaukphyu deep seaport and Special Economic Zone (SEZ) in Rakhine state, which will bring USD 1.3 billion in Chinese investment in its first phase.

Figure 2: Chinese FDI to selected countries (USD mil)



Source: China Ministry of Commerce

Myanmar instituted a Steering Committee for the implementation of the BRI, chaired by State Counselor Daw Aung San Suu Kyi to align BRI projects with national plans, policies, and internal procedures. The committee comprises 18 Union ministers, five chief ministers, the foreign affairs permanent secretary, and the chairman of the Naypyitaw Council⁴. At the same time, an institutional restructuring of the investment-related authority is underway, with a PPP (Public-Private Partnership) office being set up to deal with the task of coordinating large scale projects in which national or state governments are participating. However, the strong power of the ruling military junta, and their complicated relationships with the independent armies fighting for more independence or secession, are weakening Myanmar’s governance capacity. Caught between this internal struggle and the possibility of incurring international sanctions if the Rohingya crisis is not resolved, the Burmese government is trying to move things forward through the CMEC to boost economic growth through much-needed connectivity. However, a key point of complaint coming from the vibrant civil society groups in the country is the lack of transparency, as the government has disclosed very

Read all HKUST IEMS Thought Leadership Briefs at



<http://iems.ust.hk/tlb>

few details of upcoming BRI projects. While the State Councilor is known to avail herself with international counsels, her closed-door, one-to-one meetings with President Xi draw suspicion, and the centralization of power and lack of engagement with local civil society may pose challenges to future BRI projects.

Recommendations

The research shows that countries are instituting local BRI policy frameworks and institutions in response to the opportunity to attract large-scale BRI infrastructure projects and FDI. The increase in investments and the tendency of Chinese companies to lobby local governments to receive better conditions are leading to governments reforming the investment process, and centralizing approval authority. In addition, governments are trying to improve the business climate by making licensing and approval processes more efficient, in consultation with business associations and large foreign investors.

In Indonesia and Myanmar, governments are mostly creating institutional structures and processes to optimize the selection and planning stages of large investment projects. They have established frameworks for the negotiation and directed investments towards specific industries or geographical areas. However, host countries also should prioritize strengthening their management and monitoring mechanisms, as well as appropriate regulations, especially in three areas: transparency and corruption, environmental sustainability, and social sustainability (i.e., localization and transfer of skills). Indonesia is doing well with respect to localization and transfer of skills, while Malaysia is prioritizing environmental sustainability and

transparency mechanisms. Myanmar is still at an early stage, but already has institutionalized the prioritization of environmental and social goals.

Maximizing the sustainable benefits of BRI projects requires joint efforts by host countries and China. Institutional development that results in stronger institutions and better governance will ultimately benefit China by increasing the positive impacts of the BRI. However, institutional change takes time and where local governance remains imperfect, Chinese government officials and investors should strengthen their own due diligence to avoid projects that lead to unsustainable outcomes. If China indeed aims to achieve a sustainable Belt and Road Initiative, it should not adopt a “pollution first, fix later” model of economic development, nor replicate it in other countries. If curbing corruption and promoting green technologies are now priorities in China, Chinese companies should abide by the same standards abroad, and strive towards meeting international standards. Likewise, if China truly aspires to become an internationally recognized leader, and promote people-to-people bond, adopting a more transparent approach and opening a meaningful dialogue to respect other nationalities and ethnicities should also be a priority.

¹ Greenpeace, Jatam, ICW, Auriga. Coalruption. <https://auriga.or.id/wp-content/uploads/2018/11/COALRUPTION-EN-1.pdf>

² Agence France-Presse, 2019. Thousands protest China-backed Myitsone mega-dam in Myanmar ahead of Aung San Suu Kyi's Beijing trip. SCMP. <https://www.scmp.com/news/asia/southeast-asia/article/3007230/thousands-protest-china-backed-myitsone-mega-dam-myanmar>

³ Lwin, N., 2019. Gov't Spells Out Conditions for Signing BRI Deals with China. The Irrawaddy. <https://www.irrawaddy.com/business/govt-spells-conditions-signing-bri-deals-china.html>

⁴ The Naypyitaw Council is the executive body under the President of Myanmar that administers Naypyidaw Union Territory.



T: (852) 3469 2215

E: iems@ust.hk

W: <http://iems.ust.hk>

A: Lo Ka Chung Building,
The Hong Kong University
of Science and Technology,
Clear Water Bay, Kowloon

With support from



Angela Tritto (Ph.D., City University of Hong Kong), is a Postdoctoral Fellow at IEMS, HKUST, and a research affiliate at the Southeast Asia Research Centre at City University of Hong Kong. Currently, she is working on three interrelated research projects on the Belt and Road Initiative (BRI) in Southeast Asia. Her areas of research interests include environmental policies and technologies, sustainable development, and heritage management. She is currently leading a research project titled “Green and Smart or Black and Clumsy? Examining the Role of Chinese Investors in ASEAN’s Sustainable Development.” Her past and upcoming publications include research articles on eco-innovations in heritage management, fintech, smart cities, and a series of case studies on the Belt and Road Initiative in Indonesia, Malaysia, and Myanmar.