

Panel 4: Europe and Asia: Financial Connectivity. Risks, Challenges, and Opportunities.

Main theses

- 1.** Financial connectivity is, perhaps, one of the main aspects of the new integration processes. It has always been: globalization and exchange between continents was due to trade. Marco Polo, Columbus, and many other European explorers were motivated by new trade opportunities, i.e. had financial interest in creating new connections.
- 2.** When we look it from the trade prospective only, there are two very clear messages. First, China has become the largest trading partner for many countries, including European. Second, there is more trade and investment between developing countries that it used to be before.
- 3.** There is a new layer of financial integration and financial connectivity. Internationalization of dollar and euro, new ways of avoiding currency risks and cross-border transactions: using a reserve currency, using new digital currencies (we've seen quite a number of coins claiming to serve this need), using other alternatives, for example, WB debt to China issued in Market SDRs.
- 4.** Part of the financial connectivity is, of course, currency wars. I won't spend too much time on currency wars, but this is certainly a risk and a challenge. One country's monetary policy may affect the flows of money, especially when the currency is used for international transactions. One would also remember Triffin's paradox.
- 5.** I've mentioned China more than once. Today, it is hard to talk about connectivity without talking about Belt and Road Initiative.

Coming from this region and being from Kazakhstan, a country where the BRI—then OBOR—was first announced and which is one of three main partners, gives me a task to talk more about challenges and opportunities of BRI.

- 6.** I will shortly tap into overall discussion of BRI and then move to the third part of the agenda to share our own experience in enhancing the benefits and alleviating the risks. There are a few important features of the Belt and Road Initiative.
- 7.** First, as the name suggests, it is an initiative, not a specific program or project. This initiative was proposed by the Chinese government, but from my point of view, the underlying idea is to have international cooperation and result in a number of different programs undertaken by participating countries and enhanced by international programs. From the very beginning it was an international task and it should continue to be such. It is quite symbolic that the program was announced not in China, but in a different country, in Kazakhstan precisely. I was there when President Xi announced the start of the initiative in October 2013 in Astana, Kazakhstan.
- 8.** Second feature of the BRI is the horizon: it is a long-term initiative, which undertakes very long-term projects. The horizon may well go beyond just 5 or 10 years, but the idea is to have well-connected world in maybe 50 years or even more. The nature of infrastructure projects also assumes that the parties will invest in long-term projects like roads, long pipelines, modernization of vast existing infrastructure etc. This immediately means that private sector may initially be more reluctant to engage and this is why government participation, either via improved institutions or participation in PPP, is very important.

9. The geography of BRI is also important, especially after relatively recent changes in Washington regarding the Trans-Pacific Partnership. I think the changed views and especially current situation suggests that China would benefit more by strengthening the relationship and cooperation with the countries West or South of China: Central Asia, Eastern Europe, Middle East, or South Asia.
10. Thus, another feature that I'd like to mention is the current economic situation in participating countries. Most of the countries in this region and especially those participating in the initiative are still developing. Some of them are less developed, some are emerging, other considered frontier, but almost all of them have great potential and are attractive for investment. The rise of middle class in China and South-East Asia, high prospects of growth in Central Asian and Eastern European countries, connection of the region to resource-rich Gulf Region—those are potential benefits and enablers for advancing connectivity along Belt and Road. On the other hand, existing stance of these countries requires significant improvement. We need better institutions, including rule of law, we need more connectivity and a significant upgrade, we need to embrace new technology—from the very beginning the Belt and Road should be both physical and digital.
11. Important issue is that financing connectivity has always been the key component of the BRI. There are a few large multinational institutions directly involved in the initiative: AIIB, New Development Bank (BRICS), and Silk Road Fund to name the main ones. There is also Shanghai SE or IFFO at the Hong Kong Monetary Authority and many others.
12. We see significant investments coming from these institutions and from the private sector, and we will see even more. But we must always bear in mind that BRI is not a charity program. In fact,

- private participants are reluctant to invest if the commercial viability of the projects is under question. We also see projects which neglected corporate governance standards and now are suffering debt burden. Indebtedness is also a form of financial connectivity, but we all agree that it is not a very healthy one.
- 13.** So, financial connectivity, especially when at least one agent is an emerging economy with weaker institutions, brings a significant challenge of transparency and right corporate governance. I believe that with the right “rules of the game”, i.e. standards and financial regulation, connectivity brings a lot of opportunities. I am a firm believer of BRI, interconnectedness and closer integration, but we all must play by the rules.
 - 14.** Finally, I want to spend a few minutes talking about our experience of Kazakhstan and Astana International Financial Centre (AIFC). Because financial connectivity requires stable agent-institutions, and AIFC is aiming at becoming the main financial services hub in the region and connecting East and West. We want to prove Rudyard Kipling wrong!
 - 15.** There are two aspects, which interest us as one of the key Chinese partners: hard infrastructure and its financing.
 - 16.** Infrastructure is important for the Central Asian countries and Kazakhstan in particular. Our economic development is now based on the fact that Kazakhstan will be connecting East and West. This includes, for example, transporting manufactured goods from China to Europe or commodities from Caspian Sea to China. I am sure that a lion share of goods arriving to Europe, to Vienna, from China are passing through Kazakh steppes.
 - 17.** Kazakhstan has committed to invest in infrastructure even before the announcement of BRI — it was part of our President’s program. Indeed, we have always relied on exporting commodities,

like oil and metal mining or agriculture. However, now we pay even more attention to sustainable development and adding value. Kazakhstan goal is to become a service economy, in which infrastructure and associated financial services play the most important role. Together with China we've built the largest dry port in the world and connected it to ports on the Caspian Sea.

18. In addition to this, I believe that the New Economic Silk Way would also benefit from a strong financial center, which would also include mercantile exchange in addition to stock and bond trading. To answer these challenges Kazakhstan has already secured a few important steps:

- i. We are launching the Astana International Financial Centre to serve as the platform and financing facilitation office for the investment projects in the region, including infrastructural projects.
- ii. The financial center will have its own jurisdiction based on English common law and independent regulation.
- iii. In cooperation with Shanghai Stock Exchange, Silk Road Fund, Nasdaq, and Goldman Sachs, we set up the new Astana International Exchange. In the first stage, it will allow issuing cash equity and bonds, but in the latter stages we plan to introduce derivatives and commodities.
- iv. The stock exchange will offer an opportunity to trade in different currencies such as Kazakh tenge, US dollar, Russian ruble, and Chinese renminbi.

19. AIFC serves our "portion" of the Belt & Road project, being a local financial center. But I hope that already in the near future, we will be able to host regional services.

- 20.** Summing this up, I would like to say that a deeper financial and economic integration in the Eurasia region is needed and, to some extent, is inevitable. We must tie our connections, and regional projects like BRI or even our International Financial Center will add to this integration.