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Chapter 5

The One Belt One Road Initiative and the Changing Multi-scalar Governance of Trade in China[1]

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Introduction

Although China is the world's largest trader and one of the largest recipients of foreign direct investment (FDI), since 2010, it has been faced with slower economic growth, combined with declining foreign trade (World Bank, 2017; WTO, 2016a; WTO, 2017a).[2] To tackle this, the Chinese leadership is aiming to shift the base of the country's economy from its reliance on investments and external trade towards domestic consumption, as well as from manufacturing towards services. A concurrent challenge has been China's regional economic imbalance – the overly strong economic weight of Eastern China's first tier cities – that has resulted in rising cost and congestion in the coastal regions, and dragging development in the peripheral inland regions. In recent years, China has striven to balance regional disparities through a number of policies that affect its provinces, including rules on inward FDI and various regulations steering different industries. This is paralleled with China's changing foreign trade policies and a geographical shift in its regional trade agreements. All of these policies aim at actively keeping investment inside China. From the investing companies' perspective, moving or expanding operations from China's major coastal cities to inland cities has become a viable option due to the cost advantage of the latter. The majority of multinational firms, however, are engaged in global production chains, importing components and/or exporting intermediate or finished products from their bases in China. Therefore, companies that are located in Western or Central China, for example, need to transport their exports and imports across the country to reach the Eastern coast harbors that are the main cross-border points of China's international trade.

The aim of this chapter is to assess the prospective effects of China's new policy, in particular the "One Belt, One Road" (OBOR) initiative, on the regional orientation of its foreign trade. The main question is *how are China's regional development aims related to the OBOR*

initiative reflected in the multi-scalar governance of trade in China and beyond? Taking the perspective of European companies, this will be discussed by analyzing the business response to China's sub-national and foreign trade policies. The analysis focuses on the current institutional environment for trade in China, including formal and informal institutions (North, 1990; Holmes et al., 2013), and considers the prospects for the changing multi-scalar governance of trade in the future. Multi-*scalar* indicates governance on many scales that are not hierarchical but coexist in complex ways (Jessop, 2005), different from multi-*level* that implies super- and subordination (Neuman, 2007). Therefore, multi-scalar governance of trade refers to trade policies at different scales - sub-national, national, and international - that co-evolve in relation to each other (cf. Kettunen, 2004; 2016). It encompasses possible inter-provincial trade barriers, national trade policies affecting the country's imports and exports, and the international trade negotiations and agreements in which a country may be engaged. Trade policies are part of the institutional framework that constrains the operations of companies, and informal institutions (i.e. practices and social codes) impact strongly on firms, especially in emerging economies (Peng, 2003; Peng et al., 2008; Meyer and Peng, 2016).

Two underlying aspects motivate the analysis. First, sub-national trade policies refer to the question of the potential cross-provincial trade barriers that companies may encounter in transporting goods across Chinese provinces. It has been suggested in prior literature that various restrictions and costs are introduced at provincial borders because of the economic competition between the provinces. This could be the case even more so with the debt problem that Chinese provinces currently face. Prior research on the topic has been conducted mainly using quantitative methods, such as by Young (2000), Poncet (2003; 2005) and Wong (2012), who studied domestic trade barriers and market integration in China. Others have estimated, for example, the level of local protectionism (Bai et al., 2004), or spatial spillovers in China (Bai et al., 2012). In the absence of reliable data on China's cross-provincial trade, indirect measures of domestic trade barriers, based on various data sources such as provincial input-output data, were often applied. The other way to study trade barriers, suggested here, is to take a qualitative approach and interview company representatives based in China. This approach has the advantage of getting information about real-life business experiences on cross-provincial trade policies. There appears to have been little such research, and a gap can be found as to firm-level analyses on sub-national trade barriers.

Second, China's external trade policies are also expected to change because of OBOR related developments, such as the New Silk Road linking China with Europe and the Middle

East (e.g. Kuester, 2017). The OBOR brings a strategic focus to the Chinese government's "go out" initiative that encourages Chinese companies to search for new markets and investment opportunities abroad (EIU, 2015). Led by the highest levels of the government, this initiative will be facilitated by engaging in trade and investment agreements with OBOR trade partners. The free trade agreements (FTAs) would support China's trans-boundary projects that are planned to be financed through the China-initiated Asia Infrastructure Investment Bank (AIIB). If these FTAs are successfully concluded and put into force, they will further shift the regional balance of China's economy from coastal regions towards inland regions, by way of increasing China's trade with its Eurasian neighbors.

These two aspects related to OBOR are examined in this chapter, drawing from different sources of data including the WTO's trade policy reviews, the World Bank's *Doing Business* indicators, and the European Chamber of Commerce's business surveys from China. In addition, the author conducted seven complementary personal interviews with core informants on the topic (either on location or over the phone) in 2015-2017, namely the representatives of companies and support organizations based in Chengdu, Beijing, and Shanghai. The interviewees are Finns, Swedes, or Chinese, and all are at the management level in their respective organizations, such as general managers. They are referred to anonymously in the text, indicating the type of organization that they represent.

It is argued here that the OBOR related changes in China's regional policies would have marked implications for the regional orientation of its foreign trade. While nowadays most of China's exports and imports pass through the major ports in Eastern and Southern China that are the main entry and exit points for foreign trade, the OBOR initiative might rather shift trade flows to pass through the Eurasian continent, transported on rail or land between China and Europe. This would positively affect companies located in *China's interior* – along the "Belt" - since they would have an advantage because of shorter transport times.

In the section that follows, China's trade policies are discussed first by glancing at the regional development aims of the current Five-Year Plan (FYP) and the OBOR initiative, and then by analyzing the institutional trade environment for foreign firms in China, regional differences, and the case of Chengdu as a host city for foreign investment especially by European firms. The chapter ends with sketching the prospective changes in the regional emphases of China's trade policy that will possibly affect the geography of Asia-wide international trade policies and trade flows.

The OBOR Initiative, Regional Development and Trade Facilitation

The One Belt, One Road initiative was launched in late 2013 to develop infrastructure for new trade routes. These include the "Silk Road Economic Belt" connecting China through railway with Central Asia, Europe, and the Middle East, and the "21st Century Maritime Silk Road" to develop marine routes from coastal China to the Indian Ocean and the Mediterranean (FBIC, 2016). Being part of China's global economic strategy, the geographical scope of OBOR is ambitious, with 64 countries taking part in the plan in Europe, the Middle East, Central Asia, and South Asia.[3] Infrastructure development focuses on railways, roads, ports, and airports to enhance transport between continents and to speed economic development in the region. The initiative is backed by the newly established Asia Infrastructure Investment Bank to finance the planned large-scale infrastructure development (AIIB, 2017; ECN, 2016a; Tang, 2015).[4] The OBOR plan is important in China's national strategy, which intends to connect China with its major trade partners.

Within China, OBOR is one of the major regional integration plans that are China's priorities for regional economic planning in the current 13th Five-Year Plan (2016-2020). The FYP delineates the plans to coordinate regional development to achieve balanced growth by developing infrastructure in Western China and shifting excess industrial capacity from coastal cities to Western regions (PwC, 2015: 6). Besides the OBOR initiative, the other two plans are the integration of the Beijing-Tianjin-Hebei region, and developing the Yangtze River Economic Belt, all of which are presented in their own sections in the FYP for the first time (ECN, 2016a). The Yangtze River Economic Belt is particularly relevant for the OBOR initiative, as it focuses on industry transfer from coastal to inland regions, with the idea of enhancing differentiated industrial clustering around key urban centers in 11 provinces: Guizhou, Yunnan, Sichuan, Chongqing, Hunan, Hubei, Jiangxi, Anhui, Zhejiang, Jiangsu, and Shanghai. The aim of the plan is to encourage collaboration in economic development between provinces and a more integrated approach to infrastructure planning in China (ibid.: 4). This is noteworthy, given the long history and the still prevailing state of competition between the provinces.

These plans are being quickly followed in the provinces. China's provinces are currently putting forward different kinds of infrastructure- and other project-plans "dressed in an OBOR gown" in order to receive "political blessing" for them, as one of the interviewees put it.[5] However, it can be expected that the plans will be followed more on paper than in practice. This is based on the earlier experiences of foreign firms on these kinds of policies: for example, the

European business circles in China anticipate that the provincial bureaucracies will "demonstrate little willingness to enact centrally-planned reforms" (ECCC, 2016a: 30). In spite of the central government aiming to coordinate cross-provincial planning, the foreseeable availability of subsidies for particular sectors ensures that local governments will compete with one another for resources, which potentially leads to overcapacity and "price wars" (ECN, 2016a: 15). This is referred to by the Economist Corporate Network as "persisting localism", indicating that provinces will continue to compete rather than cooperate with each other. Previously, localism has been evident in industries such as steel or solar panels, and can be expected in the future in emerging industries, such as cloud computing and semiconductors (ibid.).

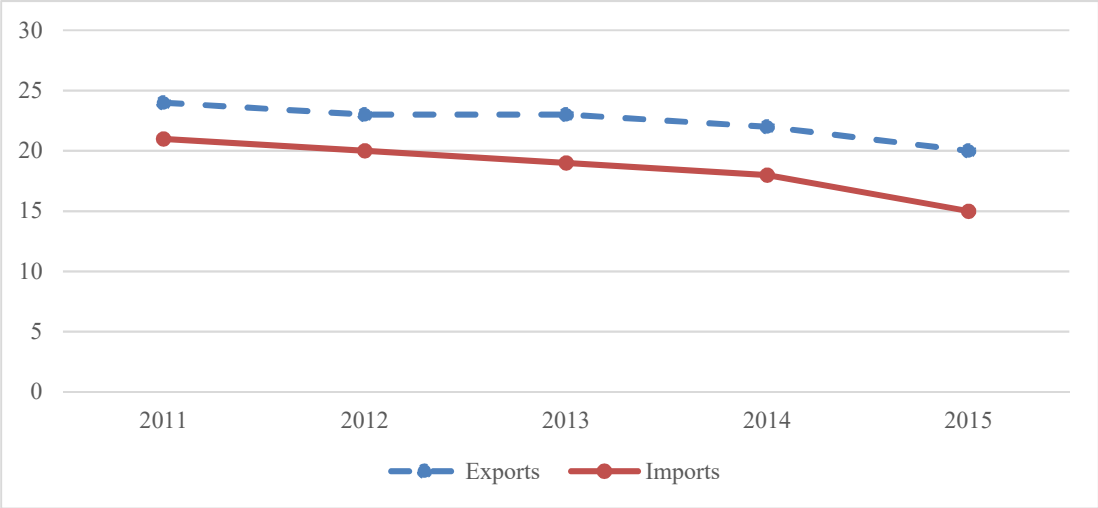
In addition to developing the inland provinces, China also aims to reform the foreign trade environment in major coastal cities and provinces by establishing free trade zones. It launched the first national free trade zone (FTZ) in Shanghai in 2013, and three others in Tianjin and the Guangdong and Fujian provinces in 2015, and more are expected in the future (ECN, 2016a: 8). The 13th FYP intends to open up trade and investment by adopting a "negative list" approach to market access. This approach means that, if a foreign investment project is not included on the negative list, it will be granted *national* treatment, i.e., similar to domestic firms. The reform is piloted in the FTZs until end-2017 with nation-wide implementation expected in January 2018 (ibid.: 9). However, the response among foreign businesses still seems to be moderate. For example, according to a survey among companies originating from the European Union (EU) countries, about 15% of the over 500 respondents had established a presence in the FTZs by 2016, indicating a somewhat cautious interest (ECCC, 2016a).

Furthermore, in order to overcome China's regionally diverse practices in trade facilitation, reforms are ongoing to eliminate regional differences in customs procedures. China has worked on harmonizing customs clearance across its 42 customs areas since 2012. However, "special customs supervision areas" still exist, and different customs procedures are applied in different areas – in some instances this is done on a trial basis to assess if they work. In 2014, China started to integrate the 42 customs areas into fewer larger clusters to harmonize the clearance processes. According to authorities, this integration has taken place, resulting in the creation of five clusters, including Beijing/Tianjin/Hebei, the Pearl River provinces, and the Yangtze River Economic Belt (WTO, 2016a: 48). The latter should have implications in harmonizing trade facilitation between the Chengdu and Shanghai customs points, for example.

China's Institutional Environment for Trade: National Trade Policies

As China remains the world's biggest trading nation, developments in its regulatory environment for foreign trade are relevant for the whole global trade regime. However, China's foreign trade has been affected by the recent slowing of the global economy. Both exports and imports declined in China in 2015, while the importance of foreign trade in its overall economy has also somewhat diminished. The share of China's exports of its gross domestic product (GDP) was 21% in 2015, after having been 27% in 2010 (WTO, 2016a: 26). Figure 1 below shows the downward trend of the share of merchandise exports and imports in China's GDP. This is partly explained by the decline in import oil prices, as well as the strengthening of China's domestic demand (WTO, 2016a: 15). China's main trade partners have remained much the same over the last few years. The main destinations of China's exports are the United States, the EU, Hong Kong, the countries of the Association of Southeast Asian Nations (ASEAN), Japan, and South Korea. The main sources of China's imports, in comparison, are the EU, the ASEAN countries, South Korea, the United States, Taiwan, and Japan. During the last decade, China's trade with its regional neighbors has grown the most rapidly.

Figure 1. China's merchandise trade as a percentage of GDP, 2011-2015.



(Source: WTO, 2016a)

Much of China's foreign trade is foreign investment induced. For several years, China has been among the largest recipients of inward FDI globally. It was the third-largest destination for FDI inflows in 2015 – behind only the United States and Hong Kong – while it had ranked first for the two preceding years, in 2014 and 2013 (UNCTAD, 2016: 5). It can be expected that China will retain this position also in the future. According to an international survey on

investment prospects, both multinational enterprises and investment promotion agencies regard China as the second-most promising destination for FDI for the years 2016-2018, while in the previous year, it was ranked as the number one destination for FDI. (ibid.: 27-28.) This trend has been complemented by the more recent very rapid growth of outward FDI, China having become one of the largest sources of foreign investment globally.

Therefore, as China is assumed to remain a leading foreign trader, the institutional framework governing its trade – and the possible impact of OBOR – is of key interest for business and policy alike. When analyzing the institutional environment for trade, attention is paid here both to formal and informal spheres of the trade regime. These refer to the laws and regulations (i.e., formal institutions) governing foreign trade, as well as to the everyday practices, norms, and social codes (i.e., informal institutions) of the authorities in enforcing the regulations (cf. Holmes et al., 2013). To put it briefly, institutions are "the rules of the game" (North, 1990), and the institutional approach to business studies maintains that the strategic choices of companies are driven not only by their resources, capacities, and industrial dynamics, but also by the institutional constraints that they face in a particular business environment (Peng, 2003). Especially in emerging economies, institutions have a strong impact on the performance of firms (Peng et al., 2008; Meyer and Peng, 2016). Next, formal institutions are analyzed based on international comparisons of regulatory environments, and informal institutions are discussed by drawing from business surveys and interviews regarding business sentiment in China. The latter refers to the experiences of foreign firms on how host country authorities implement laws, regulations, and policies, and how local officials treat foreign firms.

Regulatory framework

Regarding the *formal* institutional framework at the national scale, China does moderately in international comparison, being in between the easiest and the most difficult global regulatory environments. Since 2004, the World Bank has assessed changes in national business environments globally among a large number of countries, in order to rank them according to the ease of doing business. The assessments focus on regulations that either enhance or constrain business activity, and result in quantitative indicators by comparing the (at present) 190 economies of the world. The rankings can be seen as indicative of the formal regulatory environment in the respective economies. In these comparisons, China has performed variably during the last few years, its position improving to 78 in 2017. Table 1 shows the overall rank and selected sub-categories relevant to firms engaged in foreign trade in China. Throughout the

years, trading across borders has become relatively more difficult. In the other facets of the regulatory environment, China performs best in enforcing contracts, while starting a business remains highly bureaucratic and burdensome for firms.

Table 1. Ease of doing business (with selected sub-categories) in China, various years.

	2011 N=183	**2014** N=189	**2017** N=190
Overall rank	79	96	78
Starting a business	151	158	127
Trading across borders	50	74	96
Enforcing contracts	15	19	5

Source: World Bank (2010; 2013; 2016).

If we compare China with other economies in the world, such as the three other BRIC countries (Brazil, Russia, and India), its business environment in 2017 appears to be somewhat easier than that of Brazil (rank 123) or India (rank 130), but more difficult than in Russia (rank 40). Other East Asian economies also seem to perform better, namely Japan (rank 23) and South Korea (rank 5), not to speak of the Nordic countries (Denmark 3, Finland 13, Iceland 20, Norway 6, and Sweden 9). However, it must be noted that the indicators only assess the *formal* regulations (for example, the procedures, time, and cost to complete all formalities for exports or imports). The informal practices by the authorities in enforcing and implementing these regulations are not considered.

When it comes to the foreign trade environment, China is relatively open for a developing economy. China became a member of the World Trade Organization (WTO) in 2001, and has reportedly improved its external trade regime since then. As can be seen in Table 2, China's overall tariff level (the so-called Most Favored Nation tariff) [6] – referring to the average tariff for all imports from all countries except those with which China has a free trade agreement – is 9.5 %. The tariffs can vary considerably in different product categories, depending on the protection level for the industry in question. For agricultural products, China's average import tariff is notably higher than for non-agricultural ones, i.e., all other sectors combined.

Table 2. Import tariffs of China, compared to USA, the EU, Japan and South Korea.

	China			**USA**	**EU**	**Japan**	**Korea**
	MFN	APTA	ASEAN	MFN	MFN	MFN	MFN
Simple average tariff (%)	9.5	8.8	0.7	4.8	6.3	6.1	14.1
Agriculture	14.8	13.8	1.7	9.1	14.1	16.3	60.0
Non-agriculture	8.6	8.0	0.6	4.0	4.3	3.6	6.6
Duty-free tariff lines (%)	9.7	10.0	94.8	36.8	26.1	40.1	15.9

Note: APTA refers to preferential tariffs for imports under Asia-Pacific Trade Agreement.[7] ASEAN refers to preferential tariffs for imports under China-ASEAN FTA.[8]

Source: WTO (2016a; 2016b; 2016c; 2017b; 2017c).

Table 2 also presents two examples of China's trade agreements, i.e. the Asia-Pacific Trade Agreement (APTA), and the FTA with ASEAN. It is noticeable that the tariff reductions are quite modest in APTA, reflecting a loose agreement with less ambition towards trade liberalization. In contrast, imports from the ASEAN countries are largely free, the average tariffs being close to zero. This indicates that trade between China and the ASEAN countries has been notably liberalized, thanks to the free trade agreement since 2004. Concerning OBOR, the implication is, if China manages to sign effective FTAs with partner countries, a real liberalization will occur and a change in the geographical emphasis of trade is assumed to follow.

When China's current tariff levels are compared with its major export destinations, import protection in China (average tariff at 9.5 %) is clearly at a higher level than in the USA, the EU, or Japan, all of which are developed economies with average import tariffs of around 5-6%. This is opposite for the case of South Korea, which has a distinctly high tariff protection for agricultural products, 60 %, resulting in a total average rate of over 14% (Table 2). In addition, tariff rates are lowest in the United States, and slightly higher in the EU and Japan. The share of duty-free tariff lines indicates the percentage of zero-tariff product categories, which is clearly highest in the China-ASEAN FTA. While China's tariff levels reflect it being an emerging economy, there is an ongoing debate over how its status is regarded in the WTO. When China joined the WTO in 2001, it requested to be considered a 'market economy' after 15 years, i.e., in December 2016. However, this has been opposed by other major WTO members, notably the EU and the US who do not regard it feasible. Giving a trading partner market economy status implies that its economy is based on open competition (e.g., domestic

prices are set by competition, not the government), which is not the case in heavily subsidized Chinese export industries (FT, 2016).

Overall, China seems to have moderate trade barriers when it comes to formal policies and regulations affecting trade. This is especially so considering China's level of economic development, its tariff barriers being notably lower than those of South Korea, for example. It can be expected that the level of China's overall tariff protection will be lowered because of its newly negotiated FTAs and OBOR related FTA initiatives that will add to the volume of zero-tariff trade, and because of the simultaneous multilateral processes in trade liberalization.

Enforcement of the regulations

As noted above, it is not only the formal legislation but also the *informal* practices of authorities in the implementation of regulations that affect foreign trade. These refer to the social codes and norms of local authorities in enforcing and executing trade policies, including how efficiently and lawfully customs officials carry out customs clearance, how they interpret the rules and regulations, whether they treat all companies equally according to the law, and whether arbitrary practices – such as the favoring of domestic companies, or the demands caused by corruption – exist. These informal institutions are deeply culturally rooted in everyday norms and social codes that often affect the business environment more than the legislation itself, particularly in emerging economies (Peng, 2003). They may also have regional variations, as is discussed later in this chapter.

Data on the enforcement of regulations can be acquired from, for example, business surveys, as well as from directly interviewing representatives of companies that operate in China. According to the latest business confidence survey of the European Chamber of Commerce in China (ECCC, 2016a), European companies perceive that the business outlook has become gloomier in China. Altogether, 506 companies responded to the survey, and over half of them (56 %) considered that the Chinese business environment had become more difficult in the previous year. The most significant regulatory obstacles are administrative issues, an unpredictable legislative environment, and the discretionary enforcement of regulations. Other major problems are the perception of being less welcome than 10 years ago, the recent tightening of internet controls, foreign companies receiving unfavorable treatment compared to Chinese companies, environmental regulations being strongly enforced against foreign firms, and foreign companies being discriminated against through national-security-related legislation (ibid.: 8). These challenges, as well as the slower growth of the Chinese

economy, have resulted in the expansion plans of European firms being significantly lower than just three years ago. In 2013, as many as 86% of firms planned to expand in China, whereas in 2016, only 47% did (ibid.: 52).

Similarly, in a survey conducted among 104 Nordic firms (mainly Swedish, Finnish, and Danish) in China, the major business challenges included a perceived preference for domestic companies and unfair procurement practices by Chinese officials (CEMAT, 2014). Both of these were expected to either remain the same or worsen in the near future. However, the majority of the firms still perceived their five-year business outlook in China as optimistic (74 out of 104 firms), and more than 90 firms are planning further investments in the country. When asked about legal and regulatory challenges hindering business, the biggest problems were in customs delays and trade regulations, heavy bureaucracy, unclear legislation, and tax administration. All were expected to remain the same in the next 1-2 years by the majority of respondents. It is quite significant that problems related to foreign trade were regarded as the worst among all regulatory challenges.

Protectionism appears to be a major challenge in the enforcement of regulations, informally, and is manifest in the favoring of local firms, and in the discrimination against and unfair treatment of foreign-invested firms. This was indicated in an earlier study on the protectionism encountered by foreign companies, based on 14 interviews with Finnish firms in China (Kettunen, 2014). The main forms of protectionism appeared to be informal practices from the side of the authorities and included:

- being monitored more strictly than local companies,
- Chinese firms being able to circumvent the rules,
- foreign firms not being treated the same as local ones, e.g. in getting permits or large investment projects,
- foreign firms' intellectual property rights (IPR) leaking to Chinese competitors through the authorities,
- only Chinese firms receiving the government's support packages,
- strict, slow, or unclear procedures in exports and imports.

In exports and imports, the interviewees referred to the unfair practices by local customs authorities and the generally unpredictable customs clearance. Problems include the slow clearance times and the loss of value-added-tax (VAT) refund in exports, in spite of formal policies (ibid.: 411).

Therefore, informal institutions seem to pose at least as high a barrier to trade as formal institutions in China. An additional problem for foreign firms is that the informal rules appear not to be the same for them as for local companies. As informal institutions are slow to change – even if the formal rules are changed – it can be expected that they will remain constant for the foreseeable future. However, there seem to be regional differences in this respect, as discussed next.

The Case of Chengdu: Sub-national Trade Barriers?

Chengdu is a growing hub, being the capital city of Sichuan province and the economic and political center of Southwest China. It has a population of over 10 million (estimates varying between 11-14 million) and is an important financial, commercial, and transportation hub of the region. Chengdu hosts a large number of international companies in its main industries – automobile, machinery, electronics, information technology (IT), medicine, as well as finance and logistics. The region of Southwest China is of interest regarding OBOR, particularly as the city of Chengdu is an OBOR railway hub and one of the centers where China applies its policy to develop inland regions. Besides hosting huge industrial parks to attract foreign businesses e.g. in the automobile or IT industries, Chengdu also aims to develop the innovation capacity of the region, which is still lagging behind that of major coastal cities (Wang and Yuan, 2015). However, recent urban planning for Chengdu's 'new district' ambitiously combines science, enterprises, housing, and recreation, in order to nurture innovation (China Daily, 2016). The plans reflect the idea of innovation districts that promote sustainable urban development and simultaneously upgrade the economy (Katz and Wagner, 2014).

The institutional environment, both formal and informal, appears to be more supportive of foreign businesses in Chengdu than that in the cities of Eastern China. This regional variation is evident in the company surveys of the European Chamber of Commerce. Its chapter in Southwest China has ca. 140 member companies, of which two thirds are located in Chengdu and one third in Chongqing (ECCC, 2016b). Several points in the survey indicate that European firms in Southwest China observe being treated more favorably than those located in major coastal cities. In addition, they consider having less frequently encountered missed business opportunities due to regulatory difficulties. In contrast to firms in Beijing, Tianjin, Shanghai, or South China, European firms located in Southwest China perceive:

- being more welcome now than 10 years ago,
- receiving favorable treatment more often,

- having fewer missed business opportunities due to market access restrictions or regulatory barriers,
- there being less overcapacity in their sector,
- less often that the 'golden age' in China is over for multinational companies (ECCC, 2016a).

Similarly, for Nordic firms, Chengdu is a preferred location especially concerning future operations, whereas existing operations in Southwest China are still relatively rare (CEMAT, 2014). In the survey of 104 companies, the Southwest region (mostly Chengdu and Chongqing) hosted only 17 of the respondents' units, whereas Shanghai hosted 146 different kinds of units (such as China headquarters, sales offices, or Asia-Pacific headquarters). However, it is notable that Chengdu appears to be the most popular prospective location to open new operations in, or to which to transfer existing ones when moving to non-first-tier cities. Most of the respondents were planning to open a sales office in Chengdu, but some were also planning a China regional office. The foremost factors for expanding into China's non-first-tier cities were increasing market reach, decreasing manufacturing costs, obtaining distribution channels, as well as reaching partners or facilities already located there. Apart from Chengdu, other preferred future locations include Nanjing and Xi'an. A more recent phenomenon is the moving of operations to a new locality after being acquired by a Chinese company.[9] While Chengdu has been increasingly attracting foreign firms, some have also moved to other locations in China. This may happen - not only because of problems in the local business environment, but also because of changes in the organization of a global production chain.[10] In one case, a lead firm in an industrial cluster was reorganized, which left some of its subcontractors to find new customers, and some a new business altogether in another location in China.[11]

The challenges that foreign firms encounter in Chengdu's business environment are partly related to fast economic growth and partly due to the regulatory environment. The major problems for European firms include low air quality, a difficult regulatory environment, reduced communication between firms and the local government, procedures in customs clearance, difficulties in healthcare services and registration processes for foreigners, restricted government procurement, and slow internet speed and poor internet access (ECCC, 2016b). These inhibit the growth of investments in many respects, such as attracting the necessary workforce for innovation-driven businesses and research and development operations. Yet it is noteworthy that, in comparison with other Chinese regions, firms perceive Chengdu as an easier business environment, as shown above.

For firms located in Chengdu, engaging in foreign trade involves transporting goods to and from major port cities, such as Shanghai, passing through several provinces. Most deliveries take place by road, as China has invested heavily in the construction of highways in the mid-western region for the last two decades.[12] This is also backed by the government subsidies for road and rail traffic that have resulted in partly concealed transport costs. Other forms of transport include air and waterways, opposite ends of the spectrum where price and size of products are concerned. Air transport is suitable for high value-added light and small goods, whereas inland waterway routes are cost-efficient for bulky and less expensive goods. Waterway transport along the Yangtze River is considered reasonably mature with related services, with the Luzhou Port as Sichuan's biggest port located between Chengdu and Chongqing.[13] It is also one of the aims of the 13th FYP and the OBOR initiative to connect the provinces along the Yangtze River more closely to each other, which would ease the moving of exports and imports across the country.

When it comes to *sub-national trade barriers*, there appear to be no specific tariffs, fees, or bureaucracy when crossing provincial borders. The question of inter-province transport and trade barriers were discussed in company interviews in Chengdu and other parts of China. According to informants, the choice of transportation mode depends on the distance, time limitation, and size and value of the delivery. An engineering company that transports large semi-finished products from factories to delivery sites, e.g. between Shanghai and Chengdu, uses fast delivery trucks because of the too long lead time by train.[14] In general, there are no difficulties in moving goods between provinces. Some sector-specific regulations apply, such as special packing for chemical goods. In addition, transportation requires authorized enterprises, carrier insurance liability, qualified drivers, and registered special vehicles, which can be quite complicated. [15] However, the need for transport varies between industries. For companies in services, such as IT and software, there is rarely a need to transport tangible goods – usually only when importing investment goods. One company, for example, bought the laboratories for its new unit from abroad, and the foreign supplier took care of the shipments to Chengdu.[16] Similar findings that there are no particular trade barriers on China's provincial borders were found in Svensson's (2013) interviews with eight companies, including Alfa Laval, SKF, and Nissan Motor. None of the respondents had experienced, or heard of, specific obstacles to cross-provincial trade. Many commented that the Chinese market is 'unified' and there are no formal restrictions for selling across provinces (ibid.: 32-35).[17]

Regarding customs clearance for foreign trade in Chengdu, there are three main entry/exit ports in Sichuan province: at Shuangliu International Airport, the Chengdu International Container Logistic Zone, and at Luzhou Port. According to the Dutch business support office, Chengdu Customs provides companies with one-stop clearance services. 'Fast track' procedures allow imported goods to be conveyed to bonded zones directly after a one-time customs clearance at Shuangliu Airport (CG, 2014). This concerns exports and imports from abroad directly to and from Chengdu. When goods are on their way, there is no customs clearance or quarantine procedure at other provincial borders.[18] However, there may be additional costs due to road maintenance fees and charges for the use of the maritime harbor.

To sum up, while China formally aims to improve its regulatory environment, the realities as seen from the business level give a somewhat more pessimistic outlook. European firms observe an increasingly difficult environment with discriminatory policies and practices, as well as deteriorated circumstances for foreign trade, especially in major coastal cities. In comparison, the inland growth hub Chengdu – one of the nodes of the OBOR New Silk Road – appears to have a more favorable institutional environment for firms. This indicates a potentially continuing shift of economic activity from coastal regions to China's interior, one of the aims related to the OBOR.

China's International Trade and Investment Agreements

The Chinese government considers FTAs important in integrating the country into the global economy and, at the same time, speeding up domestic reforms (MOFCOM, 2017). One of China's earliest FTAs was signed with ASEAN in 2004, whereas most of its existing 15 preferential trade agreements were launched in the 2010s. Half of the FTAs are bilateral agreements with Asia-Pacific countries, such as Singapore, South Korea, Pakistan, Australia, and New Zealand (WTO, 2017d). In regional Asia-wide constellations, China has been a member of the Asia-Pacific Economic Cooperation (APEC) forum since 1991, and a signatory to APTA since 2001 and to the China-ASEAN FTA since 2004. However, APEC is essentially a discussion forum and APTA has not reached significant liberalization in trade, as was noted earlier. Only the FTA with ASEAN appears to have proven results in eliminating formal trade barriers, as was observed concerning tariff protection in China. From this, it is clear that FTAs with a sound tariff-reduction scheme will have a real impact on trade flows.

Some of the recent developments in China's FTA front are directly related to the OBOR initiative. In 2017, China and Russia had negotiations on a China-Eurasian Economic Union trade and economic cooperation agreement, and decided to carry out a feasibility study on a Eurasian Economic Partnership Agreement (MOFCOM, 2017). It has been further reported that China aims to negotiate FTAs with many – if not all – of the trade partners that are part of the OBOR plan, i.e. 64 countries in Europe, the Middle East, Central Asia, and South Asia (Tekes, 2016).

In line with the OBOR initiative, China will pursue new FTAs with countries related to trans-boundary projects. The most important negotiations in this respect are for the Regional Comprehensive Economic Partnership (RCEP) that China aims to accelerate with its regional neighbors. The RCEP is a proposed free trade agreement between the ten ASEAN countries and the six countries with which ASEAN has FTAs in force, namely Australia, China, India, Japan, South Korea, and New Zealand. This agreement would increase China's reach to markets and regions within the OBOR initiative, while also strengthening its role in the Asia-Pacific economy. In contrast, China is not a member of the Trans Pacific Partnership (TPP) and its latest FYP does not mention the TPP. Instead, China has openly promoted only the RCEP (ECN, 2016a). The prospect for speeding up RCEP talks has since increased, due to the changes in the United States' administration and the withdrawal of the US from the TPP in early 2017.

As a result, several rounds of negotiations have been held for the RCEP in 2017, with China and Singapore reportedly striving to speed up the process even further (Reuters, 2017). The RCEP would complement China's existing 15 preferential trade agreements, many of which were signed with small economies that are not significant in China's external trade (e.g. Jiang 2010). During the last two years, however, China has signed FTAs with Australia and the Republic of Korea, both important trade partners (WTO, 2016a; MOFCOM, 2017). Some of the other FTAs under negotiation that China might want to push forward with include the China-Gulf Cooperation Council FTA and the upgrading of the China-Pakistan FTA, as both are relevant for the OBOR initiative.

Furthermore, in recent years China has been one of the most active countries in the world in concluding International Investment Agreements that are highly relevant in light of the infrastructure investment projects along the OBOR. The purpose of investment agreements is to liberalize and protect cross-border investments, and to define procedures for dispute resolution if mutual commitments are not met (UNCTAD, 2016). The most common type of these agreements is the Bilateral Investment Treaty (BIT), which aims to promote and protect

investments made by enterprises or individuals from the respective countries in each other's territory. China has 110 such BITs in force, and several more signed but not yet in force (UNCTAD, 2017). The other type of agreement is called a Treaty with Investment Provisions (TIP), such as China's TIP with the ASEAN countries. They can be treaties with limited investment-related provisions, treaties that contain framework clauses only, or FTAs and economic partnership agreements that encompass investment issues. Recent examples of the latter are China's FTAs with Australia and with the Republic of Korea (UNCTAD, 2016: 102).

In addition, China is working to negotiate investment agreements with two major trade and investment partners, the EU and the US (ECN, 2016a). The possible agreement with the EU has the potential to facilitate and protect investments made under the OBOR initiative for a railroad connecting the two continents. The EU and China have been negotiating a bilateral investment agreement since 2014, and they agreed on the scope of the deal in 2016 (DG Trade, 2016). The future agreement would aim to ease the regulatory environment, including transparency, licensing, and authorization procedures on FDI. Moreover, China's activity in the OBOR initiative has been noted, and has gotten a reaction within Europe. One such response is the EU's launching of the EU-China Connectivity Platform in order to counterbalance the situation so that China does not "hurry alone with the initiatives"[19]. The Connectivity Platform aims to foster transport connections between the EU and China based on the Trans-European Transport Network (TEN-T) framework and OBOR, and to promote green transport with projects based on sustainability (COM, 2017).

Discussion: The Prospects for Changing Multi-scalar Governance of Trade

China is striving to develop its inland provinces, as well as infrastructure and transportation between major coastal cities and selected regions and cities in its interior. Its objective is to balance regional differences, and to shift some of the economic emphasis from congested first tier cities to second and third tier cities in the provinces. These regional development goals are included in China's current FYP and are brought into its international initiatives, such as OBOR.

This chapter has discussed China's sub-national and international trade policies related to OBOR, particularly the regulatory environment for trade from the perspective of foreign businesses in China. The business sentiments are understood as reflecting the ease of cross-border investments, which are at the heart of the OBOR initiative with its international reach. The institutional framework affecting company-level operations in China has been explored by

analyzing the formal and informal institutional constraints (North, 1990; Peng, 2003; Holmes et al., 2013) that firms encounter in their trade-related activities. It has been found that the business outlook has recently become somewhat gloomier. Problems include China's security-related legislation, burdensome bureaucracy, arbitrary enforcement of regulations, and worsened internet access, all of which make the regulatory environment more difficult for foreign companies. Business surveys and company interviews indicate that firms perceive the enforcement of regulations, informal practices, and the treatment of foreign companies as more unfair than the legislation itself. This points towards informal institutions being a more relevant constraint than formal ones for foreign firms in the Chinese business environment. However, there are distinct regional differences in China as to the firms' perceived business confidence. European firms located in Southwest China, for example, observe being 'more welcome' than firms in coastal cities. They perceive less protectionism, unfair treatment, and discrimination by the local authorities than firms located in first tier cities. This potentially enhances regional development in China's interior, especially in the transportation hubs along the "Belt", such as Chengdu. Being a significant air, rail, and highway transportation hub, the physical infrastructure for foreign and domestic trade in Chengdu is developing fast.

Furthermore, it is argued that the OBOR related changes in China's regional policies will have marked implications on the regional orientation of its foreign trade. Concerning the OBOR initiative, there are *three specific developments* that can be discerned with regard to the possible changes in the multi-scalar governance of trade in China. First, economic activities – including foreign investments – continue to shift from China's Eastern coast towards the FDI hubs in its interior, such as Chengdu. This will further increase China's internal transport and cross-provincial trade. However, the first tier cities remain important major hubs as well. Second, cross-provincial trade barriers are at a notably low level, and will be further reduced along with the development of the inland provinces and the transportation routes to and from major ports. At the same time, China's formal trade environment continues to improve, while informal constraints remain. Third, trade flows between China and Europe through the Eurasian continent are expected to grow because China and the EU are the two biggest markets in the OBOR initiative. This is an opportunity for firms in inland provinces, as it reduces the transport time for exports and imports between China and Europe when compared to existing maritime routes. However, the eventual operability of the "Belt" route will be subject to geographical and potentially political challenges.

In addition, in line with the OBOR policy, China is pursuing new FTAs related to its trans-boundary projects, which it will facilitate through international cooperation within the AIIB. These FTAs, if concluded, will provide a transnational framework for the initiative at both political and business levels. When it comes to regional development – and improving the transport infrastructure as part of it – China's previous priorities have focused on developing its domestic network of roads and railways. Its future priorities, in turn, focus on developing the rail and marine routes abroad, connecting China's inland hubs to foreign trade hubs in its OBOR partner countries.

The findings of this chapter support the idea that the regional development aims of the OBOR initiative are reflected in the multi-scalar governance of trade in China. Striving to develop its interior, China wants to ease the *sub-national* trade environments in inland hubs along the railway routes that cross the mainland and extend into OBOR partner countries. Inland hubs, such as Chengdu, compete for investments by offering a more favorable business environment compared to coastal cities where business is becoming tighter. *National* trade policy, reflected in the average tariff levels, remains somewhat protective. *Internationally*, governments in Asia and elsewhere seek bilateral FTAs to overcome the slow multilateral process. China pursues new free trade agreements with selected priority trade partners – the OBOR partner countries – in order to liberalize trade and thus facilitate cross-border infrastructure investments for its One Belt, One Road initiative.

Notes

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[2] The growth rate of China's real gross domestic product (GDP) was 7.8% in 2013, 7.3% in 2014, 6.9% in 2015, and 6.7% in 2016 (World Bank 2017). China's merchandise exports declined by 3% in 2015 and further by 8% in 2016, and, at the same time, merchandise imports declined by 14% and 5%, respectively (WTO 2017a).

[3] For the list of countries, see e.g. FBIC (2016).

[4] The AIIB was established by China and 20 countries from Asia and the Middle East in late 2014, and later extended to over 50 member countries including those from Europe (AIIB, 2017).

[5] Interview at a support organization, Beijing, 19 October 2016.

[6] MFN is a tariff with Most Favored Nation status, i.e., the lowest tariff a country can apply to imports from another country. WTO members are required to grant MFN status to other members.

[7] Member countries: Bangladesh, China, India, Laos, South Korea, and Sri Lanka.
[8] Imports from Brunei, Cambodia, Indonesia, Laos, Malaysia, Myanmar, Philippines, Singapore, Thailand, and Vietnam.
[9] Interview at a vehicle manufacturing company, Chengdu, 9 April 2015.
[10] Interview at an IT services company, Chengdu, 7 April 2015.
[11] Interview at a software company, Beijing, 27 April 2015.
[12] Interview at a support organization, Shanghai, 26 October 2016.
[13] Interview at a support organization, Shanghai, 8 November 2016.
[14] Interview at an engineering and service company, Shanghai, 19 June 2017.
[15] Interview at a support organization, Shanghai, 8 November 2016.
[16] Interview at an IT services company, Chengdu, 7 April 2015.
[17] It remains unclear, however, whether the company representatives were asked about the concrete procedures at provincial borders, such as any possible payments collected, burdensome paperwork, or any other practices that the cross-provincial checkpoints may have when goods are transported from one province to another. In addition, it may be that the respondents have no direct experience of the matter if their distributors take care of cross-provincial transport.
[18] Interview at a support organization, Shanghai, 26 October 2016.
[19] Interview at a support organization, Beijing, 19 October 2016.

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