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RED DRAGON ON THE BLACK SEA

Understanding the Security
Consequences of Chinese Involvement
in Georgian Infrastructure

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By Benjamin Zalinger

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Cover: A pedestrian walks past an advertisement of The Export-Import Bank of China (China Exim Bank) in Shanghai, China, 4 November 2014. Credit: Oriental Image via Reuters Connect.

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Executive Summary

- China is making political and economic inroads into Europe by financing and constructing physical infrastructure.
- Georgia, a small non-EU member with an urgent need for infrastructure investment, is particularly vulnerable to Chinese influence and predation.
- The Belt and Road Initiative is the most concerning form of Chinese involvement in Georgian infrastructure; loans from the policy banks behind the initiative threaten Georgia's governance standards and sovereignty.
- The Asian Infrastructure Investment Bank, which has proved its commitment to high lending standards, is bringing concrete and sustainable benefits to Georgia through its lending there.
- Unfairly subsidized Chinese companies active in Europe pose a different kind of threat, distorting local markets and capturing global industries.
- The U.S. can support Georgia's development and shield it from Chinese predation through the Development Finance Corporation and the Blue Dot Network.

Introduction

Soon it will be possible for a Chinese-made appliance to head west along the old Silk Road route, travel along roads financed by the Asian Infrastructure Investment Bank (AIIB), arrive in Europe at the Chinese-operated port of Piraeus in southern Greece, then turn north and eventually cross over Mali Ston Bay in Croatia on a bridge constructed by Chinese companies using EU funds. The journey of this humble appliance illustrates the various ways in which Chinese companies, institutions and government initiatives are already involved in transportation infrastructure in and around Europe.

Chinese investments, particularly those made under the auspices of the Belt and Road Initiative (BRI), pose a serious danger to countries' governance and are extending Chinese political influence into the heart of Europe. The next European country to play host to infrastructure built or financed by China may well be Georgia, which needs huge investments to achieve its ambitious goal of becoming a major logistics hub.

China's involvement in infrastructure brings both risks and opportunities. Some countries, including Georgia, are especially vulnerable, and U.S. policymakers should help them mitigate the dangers that come with the BRI and state-linked Chinese companies. Georgia is potentially susceptible to exploitative Chinese behavior because it faces a precarious security situation and urgently needs new infrastructure. The country's pressing need for upgraded roads and ports creates an opening for Chinese political influence, debt traps and market distortions that could steer it away from becoming a successful and stable democracy and market economy.

Georgia is a particularly useful case study for Chinese infrastructure and influence because it faces a unique confluence of vulnerabilities, external threats, and ties to Western businesses, governments and institutions. As a small, middle-income country of only 3.7 million, with a GDP of \$17.6 billion (about half as much as Vermont¹), Georgia is vulnerable to Chinese economic predation. At the same time, its political, economic and security relationships with the United States and European countries create clearer avenues for Western policymakers to support its development and shield it from abuses. As the U.S. learns to compete with China in infrastructure financing, Georgia is an ideal place to start.

Chinese companies, investors and institutions have already invested and lent hundreds of millions of dollars to the small Caucasus nation, and their involvement will likely only increase, for two reasons.



Passengers walk past a Georgian Railway train at the railway station in Tbilisi. Georgia's strategy of becoming a transit hub depends on new and upgraded infrastructure that will allow large volumes of goods to travel quickly and efficiently through the country. This includes rail and road links and especially upgraded port facilities. Credit: REUTERS/David Mdzinarishvili

The first is the covid-19 pandemic, which has hobbled Georgia's economy and created an acute need for new investments while straining the financial resources of Western governments and companies that might have provided those investments.² Additionally, multilateral development banks (MDBs), an important source of infrastructure financing for Georgia, are diverting resources toward pandemic relief. The European Bank for Reconstruction and Development (EBRD), for instance, has committed all its outlays for 2020 and 2021 (€45 billion in total) to responding to covid-19.³ The second development is the failure of the Anaklia port project, Georgia's largest-ever infrastructure project and the centerpiece of its development strategy. The project, which was backed by MDBs and Western investors, is years behind schedule and has become mired in domestic political disputes. The public bickering over the

port could sour Georgia's relationship with important donors and hurt its reputation with investors. This makes Chinese involvement, which comes with fewer strings and less scrutiny, more attractive to Georgian politicians.

Parliamentary elections on October 31, which saw the ruling Georgian Dream party retain power, suggest that the recent trend towards politicizing infrastructure projects will continue. Despite slumping approval ratings and charges of economic mismanagement, Georgian Dream held off a challenge by an opposition coalition led by the polarizing ex-president Mikhail Saakashvili.⁴ Although Western observers described the election as free and competitive,⁵ opposition parties have rejected the results and some groups have raised serious concerns, including the International Republican Institute, which has reported allegations of vote buying,

intimidation, and misuse of government resources.⁶ This disputed nature of the election will further deepen domestic political.

Background

Every Chinese company, loan and project in Georgia should not be lumped together. Rather, Chinese involvement in infrastructure development takes several forms, each with its own challenges. This report will consider three ways in which China is involved with infrastructure project abroad: the AIIB, the BRI and private Chinese companies that receive unfair government subsidies while competing for contracts.

The AIIB, a China-led and -founded MDB, is a prominent player in Georgian infrastructure and has lent more than \$200 million. It is backing two major projects, a hydropower plant and a bypass road, and has provided €50 million in covid relief.⁷ Like other MDBs such as the World Bank and the EBRD, the AIIB sets high standards for transparency, debt sustainability and environmental protections. Its lending benefits the countries where it operates, including Georgia. At the same time, the AIIB increases Beijing's soft power and burnishes its credential as an alternative to U.S. global leadership.

The BRI, meanwhile, poses a serious danger to countries' sovereignty and governance. Alluding to China's hold over Greece, which has received significant investments through the BRI, then-EU commissioner Jean-Claude Juncker lamented in 2019 that "One country isn't able to condemn Chinese human rights policy because Chinese investors are involved in one of their ports."⁸ Hungary, another recipient of significant Chinese investment, has also vetoed EU condemnations of Chinese human rights violations.⁹ The BRI is fueled by lending from two giant state-run policy banks, the China Development Bank (CDB) and the Export-Import Bank of China, which

together hold approximately \$3 trillion in assets.^{10,11} The opaque deals they offer, with details like loan terms and state guarantees kept secret, often trap countries in debt and fuel corruption rather than providing sustainable economic benefits for host countries. Fortunately, these policy banks are almost entirely absent from Georgia; loans have come instead from commercial outfits such as the Hualing Group and ZPMC, a manufacturing giant. Keeping the policy banks out by ensuring that Georgia has access to other sources of financing should be a priority for the United States.

Chinese companies are also involved with infrastructure projects that are not associated with either the BRI or the AIIB. For example, the China Railway Construction Corporation was involved in building the East-West Highway Corridor Improvement project in Georgia, which is funded by the World Bank.^{12,13} This would not be a problem were it not for the fact that many Chinese companies often benefit from unfair government subsidies. Subsidies to state-linked and politically connected companies distort markets and allow them to underbid local and Western competitors.¹⁴ China also uses subsidies to pursue strategic goals, such as capturing market share in important industries. China is not the only country to provide subsidies to its companies, but its vast resources and state-led economic model make it a particularly flagrant and dangerous offender: It spends 3% of its annual economic output on direct and indirect subsidies to businesses.¹⁵

The dangers posed by certain forms of Chinese involvement should be viewed against the backdrop of Georgia's urgent need for new infrastructure: Billions of dollars of investments are required in order to achieve long-term economic growth and security. Georgia is far from alone in this respect among European countries. According to the Global Infrastructure Outlook, a G20 initiative, Europe's infrastructure gap (the difference between how much investment is needed and how

much is actually being made) will reach \$2 trillion between now and 2040.¹⁶ Building new transportation infrastructure is about more than a few percentage points of economic growth; it has significant strategic and security consequences. Without strong and sustainable economic growth, which requires robust physical infrastructure, Georgia and its neighbors in Europe will be vulnerable to foreign interference and populist politicians who thrive on economic crisis and disappointment. Additionally, ports, railroads and highways help determine whom countries trade with. Today, too many roads in Georgia and eastern Europe point toward Moscow, thanks to legacy Soviet infrastructure. Reorienting infrastructure and trade flows toward the rest of Europe will help embed Georgia in the Euro-Atlantic community and pry it free from Russian influence.

Infrastructure and Security in Georgia

In Georgia, transportation infrastructure is inextricably linked to national security, and only significant investment can transform the country into a logistics hub and align it with the Euro-Atlantic economic and security system. Georgia needs billions of dollars from abroad and the services of international construction companies, some of which will inevitably come from China.¹⁷ Certain forms of Chinese involvement in financing and building Georgia's new infrastructure carry some risk of malign political influence, debt traps and market distortions. These risks must be balanced, though, against Georgia's urgent need for security and new infrastructure.

Georgia is in a precarious security situation: Russia not only considers the country part of its sphere of privileged interests, but also occupies 20% of its territory. Georgia does not enjoy the collective security guarantee of NATO membership, and the Kremlin actively opposes Georgia joining the alliance.

Georgians see their future in the West, culturally, economically and politically.¹⁸ Many believe greater integration with the Euro-Atlantic world — and being seen by the United States and Europeans as a vital partner and indivisible part of that community — is their country's best path out from the threat of Russian domination. Current and former Georgian officials consistently stress that the key to that strategy, and therefore the key to their country's security, is Georgia's plan to transform itself into a transit and logistics hub between Europe and Asia.^{19,20,21,22} Doing so would connect Georgia more deeply with Europe's economy. As European businesses benefit from access to Eurasia via Georgian ports, their governments will recognize that they have economic interests at stake in Georgia and pay more attention to its security situation.²³ Future Russian aggression that threatens European investment or trade routes in Georgia will surely elicit a stronger response.

Anaklia: The Linchpin of Georgian Infrastructure Development

Georgia's strategy of becoming a transit hub depends on new and upgraded infrastructure that will allow large volumes of goods to travel quickly and efficiently through the country. This includes rail and road links and especially upgraded port facilities. The single most important piece of infrastructure Georgia needs is a deep-water port. Large ships with capacities of up to 10,000 TEUs (a unit of cargo capacity equivalent to a standard shipping container) are already plying the Black Sea, making use of deep-water ports on the Western shore. Georgia's existing ports can handle only 1,500 TEU vessels.²⁴ Without a deep-water port that can host those larger vessels, Georgia will struggle to become a major transit hub for East-West trade.²⁵

Seeking to address this gap, the Georgian government signed a contract with the Anaklia Development Consortium (ADC) in 2016 to construct a massive new deep-water

Red Dragon on the Black Sea



Visualization of the Anaklia Deep Sea Port. Credit: Anaklia Development Consortium.

port at Anaklia. The port's nine phases of development, which will take decades to complete, are expected to cost \$2.5 billion, making it the biggest infrastructure project in Georgia's history.²⁶ The first phase, originally scheduled to be completed by 2021, will make Anaklia an operational port able to berth Panamax vessels. It has a price tag of \$620 million, which is a gargantuan investment in Georgia's small economy, equivalent to 3.5% of its GDP and 12% of the government's 2020 budget.²⁷

Private and institutional investors were lined up to finance Anaklia, and the involvement of multiple MDBs guaranteed that the project met high standards for transparency, environmental impact and economic feasibility. An American company, SSA Marine, was going to operate the port and the Georgian government would maintain ultimate political control over it and eventually own it outright after a concessionary period.²⁸ This model —

combining private (and mostly Western) investors and MDBs — ensures transparent financing and sustainable economic benefits and doubtlessly pleased policymakers in the U.S. and EU, both of which backed the project. ADC managed to raise \$70 million from private sources and signed commitment letters worth a combined \$400 million with the EBRD, AIIB, Asian Development Bank (ADB) and the U.S. Overseas Private Investment Corporation (OPIC), which has since become the International Development Finance Corporation (DFC).^{29,30} Anaklia looked to be the polar opposite of Hambantota, the Sri Lankan port that serves as an object lesson for the dangers of the BRI. China provided the financing for that project, saddled Sri Lanka with unpayable debts for a commercially infeasible project, and ultimately took control of the port.³¹

Instead of realizing this dream of high-quality, transparently financed infrastructure, the Anaklia project has run

Developing Georgia's Maritime Infrastructure



To view the full interactive map, visit: <https://cepa.org/red-dragon-on-the-black-sea/>
Map: Center for European Policy Analysis • Created with Datawrapper

aground. Progress on the port has stopped, thanks to domestic political squabbling and disputes among the Georgian government, ADC and the institutional investors backing the project. ADC charges that the government has carried out a “well-orchestrated campaign to destroy the project,” despite initially supporting it.^{32,33} The consortium claims that officials from the Georgian Dream party scared off potential investors and undermined the confidence of the MDBs backing the project, causing them to demand sovereign guarantees for the \$400 million they had pledged. The government denies ADC’s version of events and accuses the

consortium of failing to meet its obligation to raise sufficient funds.³⁴ The government refused to guarantee the MDB loans and in doing so threatened the bulk of funding for Anaklia.³⁵ It ultimately canceled its contract with the consortium in January 2020, effectively mothballing the Anaklia project.³⁶

Anaklia’s fate casts a pall over future investments in Georgian infrastructure, especially from private companies.³⁷ Large infrastructure projects take years to complete and produce returns, so reliable political support is crucial for winning investors’ confidence. If Georgia cannot attract foreign investors to future infrastructure projects

or faces additional scrutiny and conditions from MDBs because of the Anaklia debacle, it will be tempted to turn to China for financing. BRI projects in Georgia will not deliver the transparency, sovereignty over critical infrastructure or ties to Western businesses that Anaklia had promised.

U.S. Support for Georgian Infrastructure

U.S. policy can shield Georgia from the worst aspects of Chinese infrastructure investments, such as debt traps, and mitigate the risks from other forms of involvement, including subsidized companies competing for contracts. The United States is already involved in supporting Georgia's infrastructure development, and its existing tools — particularly the DFC — can serve as the foundation for a more robust response to the threat of Chinese involvement in Georgian infrastructure.

The U.S. has supported infrastructure development in Georgia, and the Anaklia project specifically, in several ways. The chief source of American support comes from the DFC, which provides loans, equity financing and technical assistance to developing countries to advance U.S. foreign policy goals.³⁸ It has been active in Georgia since 1993 and has provided more than \$600 million in financing and political risk insurance to dozens of projects.³⁹

The DFC was created to counter the BRI by offering countries an alternative to China's opaque deals and debt-trap diplomacy.⁴⁰ It operates at a far smaller scale, however, with a total lending capacity of only \$60 billion, and cannot replace Chinese loans everywhere in the world. To make up this shortfall in funding, the U.S. has launched the Blue Dot Network, a DFC-led initiative to galvanize private investment in infrastructure projects that meet high standards of transparency, debt sustainability and environmental protections.⁴¹ The network, of which Australia and Japan are also founding members, will certify high-

quality projects in the hopes of attracting private investors who otherwise view infrastructure projects warily. By using the vast pool of global private capital, the Blue Dot Network aims to come closer to matching the scale of the BRI.⁴²

Chinese Involvement in Georgian Infrastructure Projects

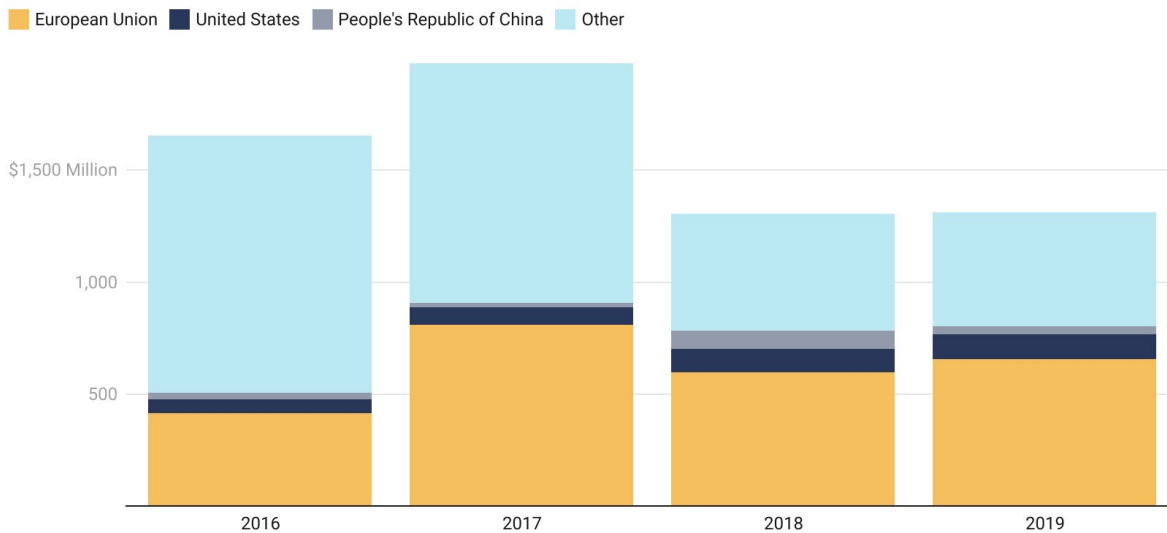
Georgia and China enjoy a good economic relationship. The two countries signed a free-trade agreement in 2017, which helped their trade grow by 44% from 2016 to 2018.⁴³ China, which trades more with Georgia than the U.S. does,⁴⁴ is now the sixth-largest market for Georgian exports and the third-largest consumer of Georgian wine.⁴⁵ In the 10 years through 2019, Chinese direct investment in Georgia totaled \$650 million, 5% of the total for that period and roughly equal to inflows from the U.S.⁴⁶

China is not the largest player in Georgian infrastructure, and Belt and Road-themed events held in Tbilisi have elicited more enthusiasm from regional partners such as Turkey than from the Chinese.⁴⁷ Still, some Chinese companies and investors are active in Georgia (including Hualing Group, Georgia's single-largest foreign investor⁴⁸) and the AIIB is funding several major projects. Additionally, China has a strategic interest in Georgia's transportation infrastructure; Georgia lies along a potential new trade route from China and could help free Chinese exporters from their uneasy reliance on Russian railways. No one should be surprised if Chinese banks play a larger role in Georgian infrastructure projects in the future, especially if funding from the West dries up thanks to pandemic-induced recessions or investors' wariness.

The AIIB in Georgia

The AIIB is not an organ of the Chinese state: It is a genuinely multilateral institution with

Foreign Direct Investment in Georgia



Foreign Direct Investment presented in Millions of US Dollars

Chart: Center for European Policy Analysis • Source: National Statistics Office of Georgia • Created with Datawrapper

an independent secretariat. At the same time, the bank was founded by the Chinese government, is led by a Chinese national and is headquartered in Beijing. China is the largest shareholder and has by far the largest voting share with 28%, enough for a veto over major decisions.⁴⁹ The AIIB is as central to China's development strategy as the IMF is to America's global financial leadership. It is also significant as a bellwether for Chinese intentions, given that it is one of the few China-founded multilateral institutions in the world.

Loans from the AIIB pose none of the dangers associated with BRI lending because the AIIB adheres to the same kind of lending practices as the World Bank and other MDBs. Since opening its doors in 2016, the AIIB has worked closely with its fellow development banks and has co-financed numerous projects with them.⁵⁰ The AIIB has also earned the praise of Suma Chakrabarti and Takehiko Nakao, former presidents of the EBRD and ADB, which highlights the degree to which the wider development financing community has accepted the Chinese-led bank.⁵¹

In addition to Anaklia, the AIIB has backed two other large infrastructure projects in Georgia. The first is the Batumi bypass road project, which will reduce the “intolerable level” of congestion around the port and resort city of Batumi.⁵² The AIIB and ADB are each lending \$114 million, while the Georgian government is contributing \$87 million to the project.⁵³ The AIIB is also lending \$100 million for the Nenskra hydropower plant, a \$1 billion renewable-energy project.⁵⁴ The plant, which is also receiving funding from the ADB, EBRD, European Investment Bank and the Korean Development Bank, is designed to address shortfalls in Georgia's domestic energy production during the winter and reduce the country's reliance on energy imports from Russia and Azerbaijan.⁵⁵ These projects are a boon for Georgia's economy and security and by supporting them, the AIIB is bringing real benefits to Georgia.

At the same time, the AIIB poses its own kind of challenge. More than 100 countries have joined the bank (despite initial U.S. opposition), which has earned a good reputation among the development

community, providing a diplomatic victory for China.⁵⁶ The more success the AIIB has, and the better its international reputation, the more soft power Beijing can wield. The AIIB also provides a template for other Chinese multilateral institutions that could displace existing U.S.-led institutions. Providing evidence of China's constructive global leadership potential may be the biggest risk the AIIB poses to U.S. interests.

For Georgia, this is less of a concern. Transparent and sustainable financing from the AIIB for important infrastructure projects brings clear benefits to Georgia. By co-financing projects with other MDBs, the AIIB allows its sister organizations to stretch their money further and back more projects in Georgia and elsewhere. Rather than undermining international lending standards, as the Obama administration initially feared it would, the AIIB has adhered to and even reinforced existing norms.⁵⁷

The BRI in Georgia

The BRI, the vague and sprawling centerpiece of China's economic foreign policy, is stubbornly hard to define, though some patterns are evident.⁵⁸ At its heart are cheap and opaque loans for physical infrastructure, especially transportation projects. China offers financing for big projects and in return gains political influence, contracts for Chinese construction and engineering companies, and other foreign policy objectives. Most of the money comes from two Chinese policy banks, the CDB and the Export-Import Bank of China. The scale of their lending is immense: China's policy banks now lend more to developing countries and hold more assets than Western-backed MDBs, including the World Bank.^{59,60}

These banks are almost completely absent from Georgia. The CDB has provided \$65 million in credit to Georgian banks, but this money is intended to expand lending to Georgian SMEs, not finance ambitious infrastructure projects.^{61,62} The danger to

Georgia from the BRI is therefore a question of future projects and loans, not current ones. Between a pandemic-induced global downturn and a business reputation scuffed by Anaklia's failure, Tbilisi has more reasons than ever to consider easy financing from Chinese policy banks. For countries looking to politicize infrastructure spending (as Georgia's government has been accused of doing over Anaklia⁶³), loans from Chinese policy banks made under the auspices of the BRI are a tempting option because they do not come with the same level of scrutiny or feasibility studies as loans from MDBs and Western governments.

The consequences of accepting those loans can be grave. The BRI may not be an unalloyed evil — existing institutions cannot cover the world's multitrillion-dollar infrastructure gap, and China has proved willing to invest in places deemed too risky by other lenders — but at its worst, the BRI is a serious threat to governance standards and sovereignty in participating countries.⁶⁴ Thanks in no small part to its lack of transparency, the BRI often saddles countries with unaffordable white elephants and unsustainable debt, fuels corruption, damages the environment and compromises national sovereignty by ceding ownership of critical infrastructure to China.⁶⁵

U.S. interests — and Georgia's security — would be harmed if Tbilisi finances future infrastructure projects using opaque loans from China's policy banks. Investments from Chinese companies or institutions can juice Georgia's economy and development, but only if they are made in a transparent fashion and go toward commercially feasible projects, not Chinese strategic priorities.

Chinese companies in Georgia

China exerts economic influence through its companies, not just through government initiatives and institutions like the BRI and CDB. This includes both state-owned enterprises (SOEs) and private companies, at least 70% of which have party committees embedded in them.⁶⁶ Most Chinese

Red Dragon on the Black Sea



Cityscape of the port city of Batumi. The Batumi bypass road project, designed to reduce congestion around the port and resort city of Batumi, is one of several projects supported by the AIIB in Georgia. Credit: Dmitry A. Mottl via Wikimedia Commons.

companies working in places like Georgia are acting legally and constructively. Welcoming enterprises from around the world allows open economies to benefit from robust competition and international commerce, but because the Chinese government exerts so much control over its companies and supports them so aggressively,⁶⁷ their involvement in infrastructure projects carries some risks.

The biggest danger for Georgia comes from unfairly subsidized companies. Building physical infrastructure is expensive and complex. Dozens of companies can be involved in a single project, providing services such as construction and goods such as steel pipes or gantry cranes. When companies use government subsidies to underbid their competitors, it distorts markets and harms efficient companies that do not benefit from subsidies.

China is not the only country that subsidizes or supports its corporations, but it is a particularly bad offender. In 2018, the Chinese government provided a record \$22.3 billion in subsidies to publicly listed companies. When private companies (which are not required to disclose subsidies) are taken into account, the true total of corporate subsidies is as high as \$62 billion, many times what the U.S. government provides to American companies.⁶⁸ This figure does not even include indirect assistance, such as protective trade barriers and access to below-market government loans.

Chinese construction companies are active in Georgia because they are cheaper than their competitors.⁶⁹ It is difficult to assess whether that is due to unfair subsidies or genuine competitiveness, and whether they are distorting markets or harming Georgian competitors.⁷⁰ For example, Shanghai Zhenhua Heavy Industries Co. (ZPMC)

won a multimillion-dollar international tender to provide 12 gantry cranes for the port of Anaklia.⁷¹ In 2018, ZPMC reported approximately \$173 million in government subsidies.⁷² This does not necessarily mean that ZPMC would not have won the Anaklia tender without subsidies; the company is a global leader in ship-to-shore cranes and controls a commanding 70% of that market.⁷³

Addressing foreign subsidies in procurement processes is challenging. Buyers do not always have the information or resources to determine whether or not bidders are receiving subsidies and have incentives to select low bids regardless of market distortions.⁷⁴ Robust procedures to identify and reject unfairly subsidized bids are therefore required to prevent state-linked Chinese companies from dominating Georgia's markets and critical infrastructure.

Policy Recommendations

Chinese involvement in constructing and financing Georgia's infrastructure presents a challenge to policymakers in Washington, Tbilisi and Brussels. Companies and institutions from China present a mix of risk and opportunity for Georgia that must be carefully balanced. The situation is complicated by Georgia's urgent need for new infrastructure, particularly a deep-water port, without which the economy will stagnate and Russian influence will continue. The threat posed by the BRI has been sharpened by the deep global recession caused by covid-19 and a worrying trend toward the politicization of infrastructure projects in Georgia — a trend that will likely continue after the Georgian Dream's latest acrimonious electoral victory. Given the urgency of Georgia's security situation, it cannot afford to adopt sinophobic policies that exclude all Chinese investors and companies. Instead, Georgia and its partners must find a strategy that avoids the harmful elements of the BRI and unfairly subsidized companies while taking advantage of the

opportunities afforded by other forms of Chinese involvement, such as the AIIB.

The different forms of Chinese involvement — the BRI, AIIB and unfairly subsidized enterprises — pose different levels of risk and require different responses. The U.S. should adopt three policies in response to China's activities that will protect Georgia from malign influence and market distortions without impeding constructive investment and growth: embrace the AIIB as a genuinely responsible actor, address subsidies by promulgating best practices and conducting investigations, and attract transparent investments to Georgian infrastructure projects through the DFC and the Blue Dot Network.

1. Embrace the AIIB

The AIIB has proved that it is committed to responsible and transparent lending practices and is providing real benefits for Georgia through its support for infrastructure projects. The U.S. should, through organizations like the DFC, work closely with the AIIB in Georgia to co-finance important projects such as Anaklia. It should also continue to encourage collaborations between the AIIB and MDBs that the U.S. is a member of, including the World Bank, EBRD and ADB.

Embracing the AIIB also means exempting it from growing U.S.-China competition. American policymakers should not target the AIIB as part of a wider campaign to pressure or punish China. Doing so would undermine U.S. claims that it supports a rules-based international order, given that the AIIB follows international best practices and has close relationships with other MDBs. Instead, the U.S. should signal its support for the AIIB, for example by granting its staff diplomatic privileges under the International Organizations Immunities Act, as it does for other development banks.⁷⁵

To prevent the AIIB from providing Beijing with more soft power, the U.S. and its partners should make clear that

their support for the bank is based on its adherence to transparency and good governance. Western public diplomacy should emphasize the profound differences between the AIIB and the BRI, highlighting the dangers of the latter while celebrating rules-based multilateralism.

2. Addressing Subsidies in Procurement Processes

The U.S. can help address the problem of subsidized bids in two ways. First, the Blue Dot Network should promulgate a robust set of best practices for identifying and rejecting bids that benefit from unfair subsidies. The Blue Dot Network is already aggregating governance best practices from MDBs, the private sector, civil society and international bodies such as the G20. By focusing on practices that specifically address government subsidies and procurement, the Blue Dot Network can improve governance standards worldwide and equip not just Tbilisi but governments around the world with proven tools for addressing foreign subsidies.

The U.S. government should also investigate companies (not just Chinese ones) that are receiving subsidies and using them to win contracts related to physical infrastructure. Conducting lengthy investigations once bids have been submitted slows progress on important projects, and not all governments have the resources to carry out such investigations. By prospectively investigating the worst offenders and publishing information about them and the subsidies they receive, the U.S. could help Georgia quickly identify and reject problematic bids.

3. Fund Georgian Infrastructure

Georgia's security and economic prosperity depend on significant foreign investment in new infrastructure, especially a deep-water port like Anaklia. If it cannot raise the money from Western institutions, governments and private markets, Georgia's government may well turn to China. Large loans from the CDB or the Export-Import Bank of China pose a far more serious threat to Georgia's governance and sovereignty than subsidized bidders or Chinese soft power. The best way to ensure that Georgia does not seek such loans is to attract investors from the West.

The DFC can provide some of this funding directly using the expanded lending capacity it was given by the BUILD Act. Establishing a regional office in Tbilisi, as DFC officials and the Georgian government have discussed, would also send a positive signal.⁷⁶ Meeting all of Georgia's infrastructure needs, however, will require private capital along with the continued involvement of MDBs and the DFC. The Blue Dot Network, which is designed to attract private investors to infrastructure projects, is a promising tool for Georgia. The DFC should find quality infrastructure projects in Georgia to showcase Blue Dot Network certification and, when necessary, cajole the Georgian government into meeting the network's standards. Ideally, a deep-water port in Georgia should be one of the network's first and highest-profile projects. Turning Georgia into a poster child for the Blue Dot Network can attract badly needed investments, deepen ties between Georgia and the U.S., and help repair the reputation of Georgian projects among Western investors.

Endnotes

- 1 Georgia GDP based on 2018 data from the World Bank, Vermont GDP's according to U.S. Bureau of Economic Analysis.
- 2 Georgia's economy is expected to shrink by 5% in 2020. See Sophiko Megrelidze, "Georgia's ruling party claims victory in parliamentary vote," Associated Press, October 31, 2020, <https://apnews.com/article/virus-outbreak-ukraine-georgia-tbilisi-elections-df12d18874fbc05ce1e0e025d98fca7>.
- 3 "The EBRD and the coronavirus pandemic," European Bank for Reconstruction and Development, <https://www.ebrd.com/what-we-do/coronavirus>.
- 4 Megrelidze.
- 5 A group of leading MEPs described the elections as free and competitive. See "Georgia elections: statement by leading MEPs," European Parliament, November 1, 2020, <https://www.europarl.europa.eu/news/en/press-room/20201101IPR90601/georgia-elections-statement-by-leading-meps>.
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