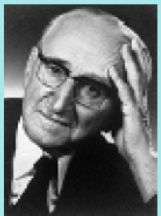




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Ralph M. Wrobel

**The Chinese Belt and Road Initiative between Economics and Geopolitics:
Consequences for Armenia**

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The Chinese Belt and Road Initiative between Economics and Geopolitics: Consequences for Armenia

Ralph M. Wrobel

Abstract

Armenia has already signed some agreements with China to participate in the BRI project while no concrete measures are financed by the initiative. But what are the economic advantages and disadvantages of the BRI? While funding of some for Western financiers unattractive projects by China is a good chance for some participating countries a resulting “debt trap” is dangerous for them. Additionally, it can be shown easily that China’s investments have mostly some geopolitical aspects which make the projects more advantageous for China than for the participating countries themselves. Especially, when in the BRI participating countries cannot pay back their debts a transfer of natural resources respective of infrastructure like ports or pipelines to China may be the consequence. Therefore, Armenia is in a dilemma between strengthening cooperation with China and benefitting from that, on the one hand, and the risk of losing economic as well as political independence, on the other hand.

Keywords

Belt and Road Initiative, Armenia, Geopolitics, Debt-Trap

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The Chinese Belt and Road Initiative between Economics and Geopolitics: Consequences for Armenia

1. Introduction

The Chinese Belt and Road Initiative (BRI) is a huge project divided into two sections, the Silk Road Economic Belt, using several land channels, and the Maritime Silk Road for the sea channels. The project shall cover more than 60 countries in Europe, Asia, and Africa, about two thirds of the world population, and a quarter of all internationally traded goods and services in the world. (Löchel / Nawaz, 2018, 6) Already in 2013, the BRI was announced by president Xi Jinping. As Chinese statements point out: *“The BRI is probably the grandest inter-national economic initiative proposed by China for taking greater responsibility to support the world economy by responding to continuous calls from other emerging economies, especially under-developed ones.”* (Jin / Shen / Jiang, 2021, 219) But observers are also talking about a revival of the ancient silk road updated to fit in China’s 21st century *“to create external conditions favourable to its rise”*. Then, global aims are to secure energy resources for China, to weaken terrorist threats, to strengthen the country’s influence, and to counter US presence in Asia. (Kim 2022, 21) So, obviously the Chinese Belt and Road Initiative is located somewhere between economics and geopolitics. That makes an analysis from both perspectives necessary.

Also Armenia, a small and landlocked country in the South Caucasus region, is already affected by this Chinese initiative. In 2015 a *“Memorandum on Promotion of Cooperation in Building the Silk road Economic Belt”* was signed by Armenia. In 2018, China became Armenia’s 3rd largest trade partner – after the EU and Russia. And in the same year a *“Chinese-Armenian Friendship School”* was built in Yerevan, financed by China spending about USD 12 mill. for the project. (Bergmann 2019) At the moment, Armenia has only one large infrastructure project in progress, the *“North-South Road Corridor”* which connects Iran in the South with Yerevan and Georgia in the North. But this project is financed by the Asian Development Bank with USD 60 million, mainly. (ADB 2021, VII)

On the one hand, Armenia has to think about taking advantage of possible funds from the BRI to promote this project. But on the other hand, there are also disadvantages of further integration into the BRI. Mainly, the so-called *“debt trap”* has to be mentioned. Additionally, also in the Caucasus region BRI seems to be a more geopolitical than economic project. Therefore, in this paper economic advantages and disadvantages of participating in the BRI structure will

be analysed briefly. Then, it will be shown how important geopolitics is compared to economics for China in the BRI structure. By the way, it will be worked out what are possible chances for Armenia and what are the challenges to participate more in the BRI.

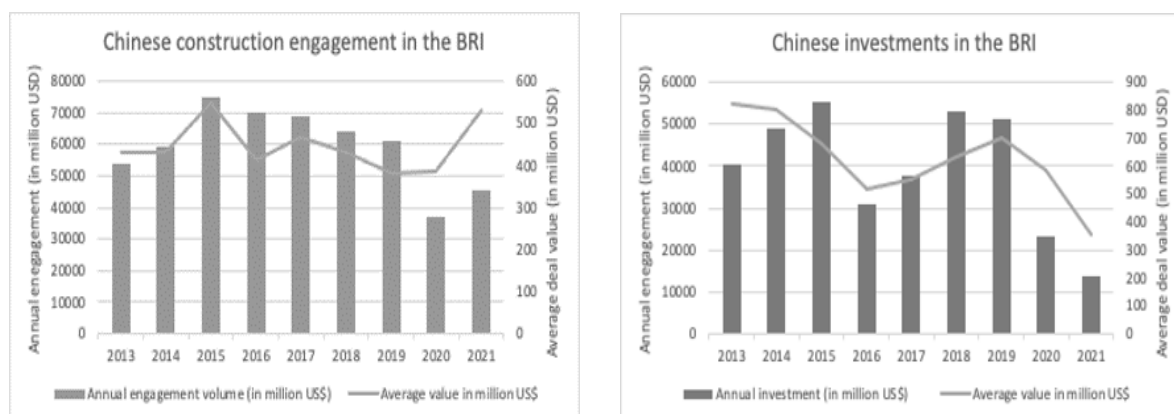
2. Economic Aspects

2.1 Advantages and Disadvantages

The official “five goals” of the BRI are (1) policy coordination, (2) facilities connectivity, (3) unimpeded trade, (4) financial integration, and (5) people-to-people bonds. (Lorenzo 2021, 592) That sounds great! Also, concrete numbers of Chinese investments are impressive. While China spent in 2020 about US\$ 60.5 billion and in 2021 about US\$ 59.5 billion for BRI projects, the cumulated BRI projects value even exceeds US\$4 trillion in September 2021. (Shira 2021) First of all, infrastructure projects in poor LDCs were financed giving chances of development and economic growth to the recipient countries. But at the same time, it becomes obvious that mainly two sectors are affected by BRI projects: the energy sector with 40.2% and the transport sector with 22.9% of cumulative BRI engagement from 2013 to 2021. (Green Finance & Development Center, n.d.) Additionally, about 60% of energy sector loans by Chinese development banks and more than 90% of Chinese energy sector investments from 2014 to 2017 were in fossil fuels. (Nabiyeva 2019, 4) One can gather from it a special focus of BRI funds on projects in the interest of China. Especially the energy sector and persistent flow of energy resources to China are an obstacle for the Chinese economic development as well as for the rise of the new political superpower China.

Additionally, observers point out an imbalanced circle of development for in BRI participating countries. First, there is no trickle down for the local population because of use of mainly Chinese workers. Secondly, there are no direct positive effects on local business cycles because the projects are given to Chinese enterprises, mainly. And, in the end a so-called “debt trap” – consisting of public and hidden debts – may violate the independence of the recipient countries.

Fig. 1 & 2: Chinese Construction and Investment Engagement in the BRI 2013 - 2021



Source: Wang 2022, 8.

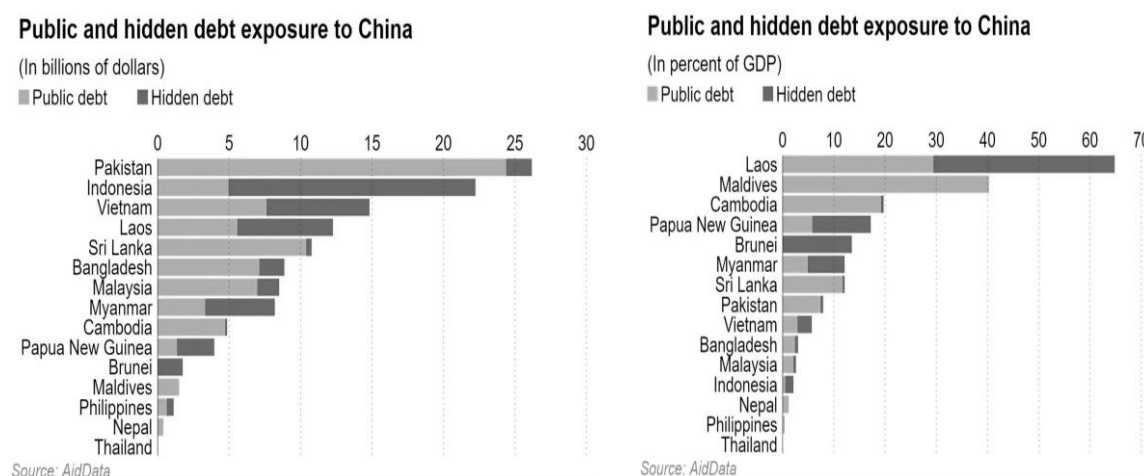
In concrete, often no trickle down to the local population occurs because Chinese workers are used for the BRI projects. Host countries usually seek to increase the proportion of local hires but Chinese firms seek to keep labour costs down. Therefore, importing Chinese labour for BRI projects is advantageous rather than relying on local workers for them. For instance, railroads in Laos and pipelines in Myanmar have been constructed with a predominant Chinese labour force. However, this leads to a limited skill transfer into the recipient countries and has no positive effects on employment. Only Cambodia is a well-known exemption with about 20,000 new jobs for locals created by BRI projects. But mostly, the reactions of local population are frustration or unrest including violence against Chinese workers. (Hillmann / Tippet 2021) Additionally, also Chinese data show the dominance of Chinese companies involved in BRI construction projects in 2021, for instance. In that year, the five most important companies PowerChina, China Communications Construction, Sinopec, China International Trust and Investment and China Railway Construction accounted for more than two thirds (67.1%) of the Chinese BRI investments. (The Green Finance & Development Center, 2022, 18) As a result, in the recipient countries no direct positive effects on business cycles can be expected by the investments.

But Chinese loans are attractive for some less developed countries. In contrast to Western financial assistance for Chinese loans there are no conditions on political and economic reforms like strengthening human rights, good governance or economic liberalization. As a result, in the recipient countries high levels of corruption, weak checks of the executive branch, and lacks of transparency are accepted by the Chinese. (Nabiyeva 2019, 5) But the main problem for recipient countries is the so-called “debt-trap”. At all, China’s loan agreements are subject of an intense controversy. Some observers have suggested *“that Beijing is deliberately pursuing ‘debt trap diplomacy,’ imposing harsh terms on its government counterparties and writing contracts that allow it to seize strategic assets when debtor countries run into financial*

problems”, while others have emphasized the benefits of China’s lending. (Gelpern et al. 2021, 4)

However, the circle of monetary flows in the BRI projects is sometimes very unfavourable for the recipient countries. In an “official monetary circle” the money is given by the Chinese ExIm-Bank – for instance – to the project hosting country which is securing the debt with its own natural resources or the infrastructure project itself. In practice, the money remains in China – flowing directly from ExIm-Bank to Chinese State Owned Enterprises (SOEs) in the construction sector. In the end, the recipient country owns some infrastructure like a harbour, a railroad or a street – but without side effects on local employment or education. If the project is not profitable in the middle run the recipient country cannot pay back the credit to China and has to hand over its resources respective the infrastructure.

Fig. 3 & 4: Public and hidden debt exposure to China in 2017



Source: Aamir (2021).

In the case of China’s lending “official debts” and “hidden debts” have to be distinguished. Hidden debts are not picked up by official statistics of the IMF, World Bank or others, but they account for about 50% of China’s lending. (Horn et al. 2019, 4) In concrete, the term refers to the entire set of loans to host country SOEs and state-owned banks as well as limited liability companies set up for specific projects with some degree of host government ownership but without state guarantees. (Brautigam / Huang 2021, 1- 2) As can be shown in fig. 3 and 4 in 2017 highest indebted to China were Pakistan, Indonesia, Vietnam, Laos, and Sri Lanka. While in three cases the so-called “hidden debts” were overwhelming in Pakistan and Sri Lanka public debts were accounted to be larger, only. In percent of GDP mainly Laos, the Maldives, Cambodia and Papua New Guinea are highly indebted to China. Especially the cases of Pakistan with a debt exposure of more than USD 25 billion and of Laos with a debt exposure of

more than 60 percent of GDP are dramatic but also Sri Lanka is an interesting case study as will be shown in the next chapter. Some governments have already recognised this problem. For instance, Malaysia cancelled a number of China-funded infrastructure projects due to concerns about the country's debt. (Hung 2021, 4) Participation in BRI projects are double-edged, at least.

2.2. Four Examples from Asia: “win – win” or “win – lose”?

The following four examples are chosen to show the theoretically described problems with BRI projects a little bit more in detail respective illustrative:

Example 1: Gwadar Port and China Pakistan Economic Corridor

In Pakistani publications Gwadar Port and the China-Pakistan Economic Corridor are emphasised as a typical win-win project within BRI. For instance, Gholizadeh et al. (2020, 335) emphasised: *“Gwadar Port’s development could enhance the economic security of both China and Pakistan. With the opening of Gwadar Port, oil and energy in the Middle East will be imported directly to China through Pakistan’s oil pipeline. This is not only oil but also goods from Central Asia, and even Europe and the USA will land from Gwadar Port and enter China through the China–Pakistan Economic Corridor (CPEC). The development of Gwadar port under the CPEC program could also dramatically increase the capacity of Pakistan’s maritime trade while reducing its dependence on the current largest port, Karachi, near the India border.”*

As this shows, the main purpose of the China-Pakistan Economic Corridor is to build a connection linking Kashgar in China’s landlocked Western province Xinjiang with the Arabian Sea. (Rafiq 2022, 59) Gwadar port was constructed between 2002 and 2021 in several phases. But already in 2013, when the BRI was announced, the operation was handed over to a Chinese SOE “China Overseas Port Holding Company”, in 2015 some parts of the port were leased to a Chinese company for 43 years as “Gwadar Special Economy Zone”, additionally. (Khetran 2014/15, 71 – 72) Problem was the practical implementation of the project. The port with a maximal depth of 12.5m was constructed for small-size tankers respective cargo vessels, only. Also, the proposed oil pipeline via Himalaya was and is economically unsustainable. The whole project was financed by Chinese investments of USD 63 billion for the infrastructure. Nowadays, Pakistan has no cash to implement further plans but to keep the harbour running more Chinese lending is required. (Jaybhay 2020) The further development of the project is quite open at the moment, but its long-term profitability is questionable. An economic perspective of the project is not obvious, therefore.

Example 2: Hambantota Port in Sri Lanka

In 2016, the hope of a positive development of the Hambantota project in Sri Lanka were huge. In a report the authorities wrote: *“Port of Hambantota [...] proposed development is directed to develop a major industrial and service Port with an attached industrial zone. It is still at its initial stages of operation and has shown great potential of being an industrial and service hub in the region of South East Asia.”* (Sri Lanka Ports Authority 2016, 2) Already in 2007, Sri Lanka signed a loan agreement with China’s ExIm-Bank. From 2008 on the Hambantota port was constructed by the SOE *“China Harbor Engineering Company”*. In 2013 the project was officially incorporated into BRI and expected to play a key role in the BRI structure. Main problem of the project was a major port in Colombo as competitor. Therefore, Hambantota port could not generate enough revenues and Sri Lanka was unable to pay its debts back to China. Therefore, in 2017 the country leased the port to the SOE *“China Merchants Group”* for 99 years. (Hung 2021, 1 – 2) As a result, China owns an own port in Sri Lanka now. This is economically worthless but may have some geopolitical implementations. In contrast, at the end of 2017 Sri Lanka had debts totalling USD 47 billion, more than 50% of its GDP. (Hung 2021, 6) The country is caught in China’s “debt trap”.

Example 3: China-Laos Railway

The Lao-China Railway is running from Lao’s capital Vientiane to the town of Boten at the Lao-Chinese border. It is a segment of the China-Indochina Peninsula Economic Corridor (CICPEC). Its purpose is to expand the trade network from Kunming in China via Laos, Thailand and Malaysia to Singapore. On the one hand, the Lao-China Railway has the potential to increase the country’s attractiveness as an investment destination, if Laos is able to improve business, investment, and trade environment, too. (World Bank 2020a, 14 - 16) On the other hand, at the same time there are clear disadvantages respective risks. The Lao-China Railway was financed by China ExIm-Bank. The railroad was constructed by *“Lao-China Railway Company”* (LCRC) between 2016 and 2021, reportedly with a predominantly Chinese labour force. The whole project is valued at USD 5.9 billion, what accounts for one third of Lao’s GDP. Therefore, the project is of high risk for Laos. First, there is uncertainty about Thai completion of the railway as well as uncertainty about cargo respective passenger volume. But all these risks are taken by the government of Laos while the profit flows by 70% to Chinese SOEs. The project was funded exclusively with hidden debts accounting for about 35% of Laos’ GDP. (Malik et al. 2021, 49 – 49) At all, the project is too large for Laos and the risk too high. Also here, a geopolitical intention of China can be imputed.

Example 4: The Trans-Asia Gas Pipeline

Main contractor of Turkmenistan's "*Trans-Asia Gas Pipeline*" is the Chinese SOE CNPC, the main financier the China Development Bank. The costs of the project are estimated between USD 14 and 20 billion. The construction was done in three phases, 2008, 2009, and 2014. (Aminjonov 2021) The main purpose of this project is obviously China's energy security while there are some risks respective disadvantages for the Central Asian countries. First of all, the whole project is suffering from a lack of transparency and a high corruption level. Secondly, for Turkmenistan it creates a huge dependency from one gas customer only, China. For instance, already in 2017 China took 94% of Turkmen gas exports, representing 90% of the total value of Turkmenistan's exports. Additionally, the control over the region's energy infrastructure has shifted from Russia to China. If the Turkmen income from gas exports shrivels the country with the world's fourth-largest natural gas reserves and a 750-kilometer border with Afghanistan may collapse. (Hedlund 2019)

As one can see, all four projects have some advantages for China but the advantages for the recipient countries are questionable. In some cases, geopolitical interests of China seem to be more important for investment decisions than economic aspects. Therefore, it must be asked if the investment decisions of these examples can be explained by geopolitics.

3. Geopolitical Aspects

3.1 BRI and the Comeback of Geopolitics

While economics and geopolitics have been seen as mainly separate domains in the last decades, the rise of China and its growing rivalry with the US have brought this era to an end. With the Western failure of believing in the convergence of economic and political systems – especially in political changes in China because of the economic rise – geopolitics has turned back. (Pisani-Ferri 2021) Nowadays, all major powers in the world as well as scientific observers are learning to combine both approaches, again.

Already in 1904, Halford Mackinder formulated his thesis of the "*pivot area*", later better known as "*heartland theory*". As he pointed out: "*Who rules East Europe commands the Heartland; who rules the Heartland commands the World-Island; who rules the World-Island commands the world.*" (Mackinder 1919, XVIII) From Mackinder's point of view the traditional Russia as well as Central Asia are the "*heartland*", an area in the world with a geographic structure which could shield it from attacks by sea powers, which could sustain large populations, and could produce some of collective identity.

Fig. 5: The “World Island as it soon will be, by railways, and by aeroplane routes”



Source: Mackinder (1919), p. 81.

While the “World Island as it soon will be, by railways, and by aeroplane routes” (fig. 5) reminds of nowadays Central Asia with its BRI financed railroads, streets and pipelines, an alternative theory about the “Rimland” by Spykman (1944) focusses on the UK, the US and Japan as sea powers with geographical advantages to the “heartland”. In concrete, Spykman emphasized that sea powers of the “rimland” could become superpowers according to their access to the sea and would develop better because of greater contact with the outside world. As a result, his central geopolitical statement is “*who controls the Rimland rules Eurasia, who rules Eurasia controls the destinies of the world*”. (Spykman 1944, 43) Both approaches are discussed also nowadays, again. (Chen / Fazilov 2018, 2) For instance, from an Anglo-American point of view the rimland can be seen as the World Island’s “*inner crescent*”, which rules Eurasia. (Ahmed / Lambert 2022, 58) Spykman’s approach of the rimland is also able to explain the dominance of the US in the South and Southeast Asian area. In detail, his approach of “*encirclement*” (Spykman 1944, 19) – in a modern version – can help to understand China’s geopolitical situation, surrounded by allies of the United States, Japan, South Korea, Taiwan and Singapore. Opening up this circle seems to be of highest interest for China. The best way to achieve this is to become a sea power itself.

3.2 A New Competition of Systems and its geopolitical implications

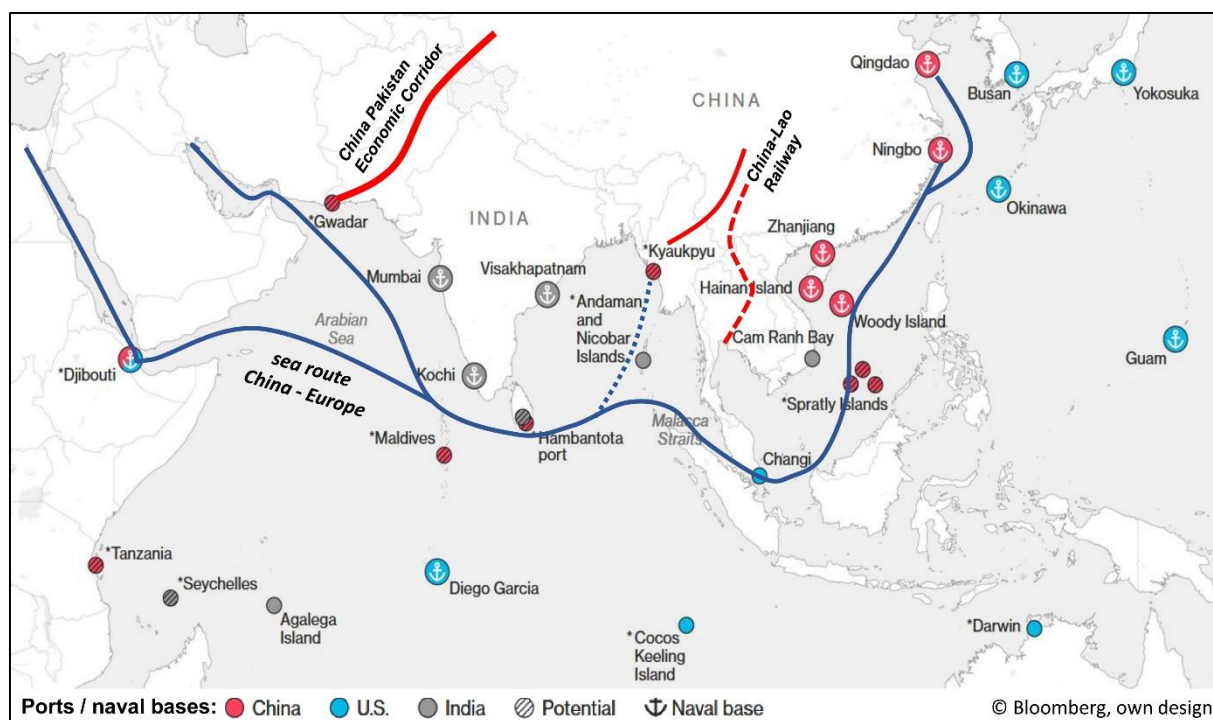
In the beginning 21st century the world faces a new competition of systems – between democracy and autocracy – as well as between the sea power US and the new world power China. On the one hand, the US and its allies – the EU, Japan, South Korea, India, Australia etc. – are supporting the democratic development as well as market economy in the world, while on the other hand, China, Russia and their allies – e.g. Belarus and North Korea – are standing for autocracy and state-led economic systems. Especially after the invasion of Russia into the Ukraine the threat of these systems for the liberal West are obvious. While Russia is already more or less isolated from the Western economic systems Western countries maintain cooperation with China. But also here a change is visible. Broken supply chains in China are forcing investments into European industries – like the semiconductor sector for instance. These are first steps of a decoupling of Western and Eastern economies.

In 2017, the BRI was incorporated into Chinas constitution. The clear objective was to create a revised global order securing China's interests as well as matching Beijing's worldview until the mid of the 21st century. (Seidt 2022, 14) Therefore, it makes sense to analyse the Chinese BRI investments also from a geopolitical point of view. Nowadays, the volume of sea transport is much higher than the volume of land transport. Additionally, the costs are much lower. Therefore, the "*Maritime Silk Road*" is actually more important than the land route crossing Central Asia and the Caucasus. As figure 6 shows the sea routes across the Indian Ocean as well as the Western Pacific are of highest importance for China. On the one hand, it is the sea route for exported goods to Europe, on the other hand the main import route for natural resources – mainly crude oil – from the Middle East to China. But both routes are passing through the Strait of Malacca, which is under control of the US (Singaporean Changi Naval Base). (Löchel / Nawaz, 2018, 7) Additionally, the US have naval bases in Japan (Yokosuka and Okinawa), in South Korea (Busan) and in Guam in the Pacific as well as Diego Garcia and Djibouti in the Indian Ocean. Some Indian naval bases can be added. This shows that the US are a typical sea power, controlling the rimland. To counterweight this naval power in East and South Asia China tried to occupy the Spratley Islands in the last decades and erects alternative transport corridors for natural resources and merchandise goods. By the way, China acts as land power as well as sea power at the same time.

The first corridor to circumvent the Strait of Malacca is the "*China Pakistan Economic Corridor*" starting with Gwadar port and ending in China's western Xinjiang province. To build a highway and an oil pipeline from Gwadar to China has high geostrategic importance for China while the economic advantages for Pakistan will remain small. Only, Pakistan's geostrategic interest of a second harbour far away from the Indian border must be mentioned. (Gholizadeh et al., 2020, 341) The same Chinese purposes can be assumed for the corridor through Myanmar starting

in Kyaukpyu and the China-Lao Railway. Instead, the port of Hambantota in Sri Lanka can be seen as China's strategic station in the Indian Ocean which is currently controlled by India, an ally of the US. The same purpose has the naval station in Djibouti which is neighboured by a US naval base. (Alam / Asef 2020, 277 - 278) As becomes clear by this analysis all three BRI projects – Gwadar port and China-Pakistan corridor, Hambantota port, and China-Lao Railway – have geopolitical importance for China. Economic profitability is secondary. But by these investments China is on the way to become a sea power, too.

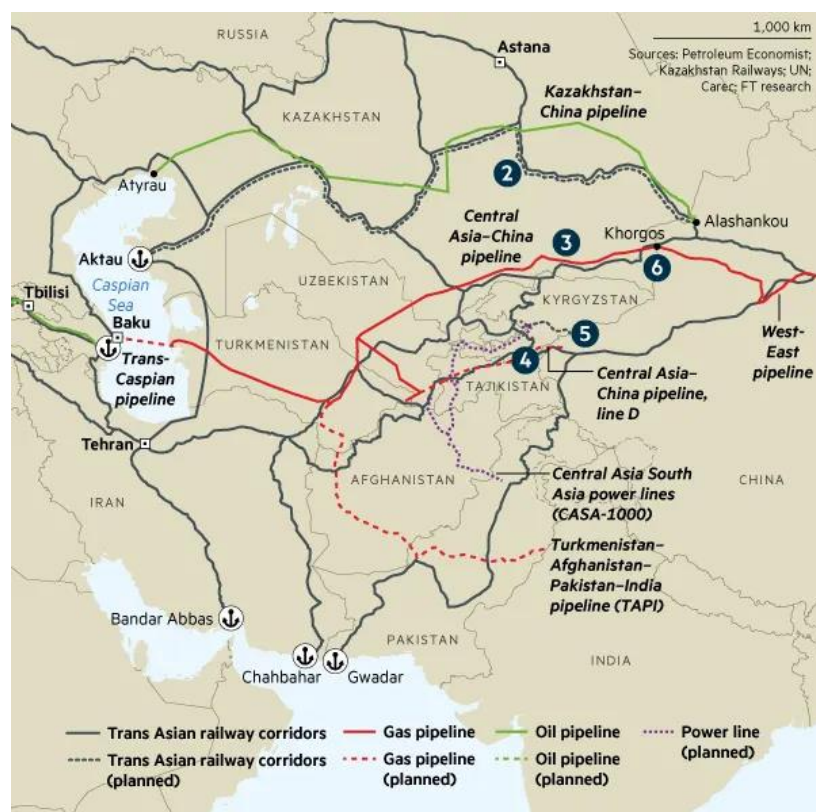
Fig. 6: Sea routes and naval bases in the Indo-Pacific



It is the same story in Central Asia where China is playing a “*New Great Game*” with Russia and the US for dominance in the region. Here Russia has to be considered as China's main rival. Traditionally, Moscow understands geopolitics in terms of spheres of influence. Therefore, Russia mainly accepts China's influence in East Asia. But regarding the post-Soviet space – Central Asia and the Caucasus – Russia considers the region to be its own traditional sphere of influence. Until now, China's economic penetration into the region has not done any substantial harm to Russian interests. (Lukin 2022, 33) Russia still has remarkable influence in several aspects, e.g. serving as military stabilizer while also having some political and economic influence. Until now, it can be emphasized that the Central Asian states have been able to maintain a balance between the external players. Also in the long run, they are interested in retaining Russia as a counterbalance to Chinese influence. (Taliga 2021, 9)

But China's influence is on the rise. As well the railways as the pipelines in the region have the purpose to circumvent the Strait of Malacca, providing oil and gas to China from the region and connecting China directly with its Western customers. Shipping goods overland from China to Europe by train takes 25% to 50% of time than it takes to send them by ship. Also train shipping costs up to 65% less than shipping by air. Especially the growing sectors of high-tech and high-end fashion need this fast and cheap alternative to the traditional shipping routes. (Chen / Fazilov 2018, 8) Also here the geopolitical aspect of investments is obvious. Nowadays, during the Ukraine crisis 2022 and after the takeover of power by the Taliban in Afghanistan in 2021 the West lost a lot of influence in the region. The approach to continuously check Russian and Chinese ambitions in the region by involvement failed. While Russia still can be seen as a remaining military power in Central Asia China is the "new soft hegemon" which controls the construction of oil and gas pipelines from Central Asia to China as well as the expansion of Eurasian Railroads to transport goods from China to Europe. Therefore, also BRI investments in Central Asia have a strong geopolitical component while the economic benefits for the Central Asian countries remain small.

Fig. 7: Railway Corridors and Pipelines in Central Asia



Source: Financial Times (2016).

4. Consequences for Armenia

Therefore, at all BRI projects must be seen as geopolitical projects, first of all, benefitting mainly China and not the recipient countries. All BRI measures clearly reflect the interests and concerns of a rising great power. In concrete, China depends on the imports of raw materials and the export of manufactured goods. (Seidt 2022, 15) Of course, there is also an economic dimension. On the one hand, infrastructure and policy gaps hindering trade and FDI can be closed by BRI based projects. BRI transport projects can reduce trade costs, expand trade, increase FDI and reduce poverty in the recipient countries. Therefore, at all cooperation with China as BRI member can bring benefits. (Turan / Aytekin 2021, 385) But on the other hand, high costs of some investments can further increase the risk of rising public debt (“debt trap”) because sometimes new infra-structure costs can overweight earnings from the projects. And, economic dependence from China can reduce political national independence. At all, the Asian countries are facing similar dilemmas with China’s rise. It is not easy to cooperate with Beijing to get economic benefits while maintaining strong security or policy ties with the US or other Western countries. (Kim 2022, 22)

At the moment, current BRI infrastructure projects in the South Caucasus are avoiding Armenia, e.g. the “*Trans-Caspian International Transport Route*” (TITR) which is the shortest railway route from China to Europe as well as the proposed “*Trans-Caspian Gas Pipeline*”. (Babyev / Ismailzade 2020, 4) But Armenia’s “*North-South Road Corridor*” may become more attractive in the near future. Some German logistics enterprises already announced to suspend temporarily land, air and sea transport via Russia because of the war in the Ukraine. (Hutson 2022) Therefore, Armenian politicians have to think about the “*North-South Road Corridor*” as part of BRI. Perhaps, an acceleration of construction is possible. As the World Bank (2020b, 1) pointed out “*the country may still benefit from the BRI and those benefits can be enhanced if the implementation of complementary policies accompanies infrastructure improvements*”. But at the same time, it demands stronger regional cooperation in the South Caucasus region. Additionally, it is emphasized that Armenia’s fiscal policy allows only a small rise of public investments. Therefore, also a cost-benefit calculation for every concrete project is necessary. Will the construction work be done by Chinese firms and workers? Also, the risk of a “*debt trap*” must be taken into consideration.

And finally, Armenia has to decide to which part of the world it will belong in the future. At the moment, Russia cannot support Armenia in its conflicts with its neighbours Turkey and Azerbaijan because of the conflict in the Ukraine. The mullahcracy Iran is suffering from Western sanctions, too. Therefore, the communist dictatorship China with its Belt & Road Initiative became an important trade partner, already. Its attractiveness will rise in the future, too. But will Armenia become part of the Eastern bloc of the world?

Better would be to balance the power of China and the West to remain as functioning democracy in the Caucasus region – maintaining good relationships with China and the West at the same time.

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