How has COVID-19 Affected BRI Projects in Malaysia?

by

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Of the many pervasive effects of COVID-19 globally, its impact on the Belt and Road Initiative[3] ('BRI') projects — the BRI itself already sweeping in its cross-border reach — has been keenly felt across all economic sectors.[4] Below, we summarise COVID-19's impact on BRI projects in Malaysia. We then highlight the risks and opportunities for current and prospective BRI players presented by the changed landscape thrust upon us by COVID-19.

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3 The Belt and Road Initiative ('BRI'), announced by President Xi Jinping in 2013, is a combination of two other initiatives, the Silk Road Economic Belt and the 21st Century Maritime Silk Road.

4 Bee Chun Boo, Martin David, Ben Simpfendorfer, 'How will COVID-19 affect China's Belt and Road Initiative?' (*World Economic Forum*, 4 May 2020).

BRI PROJECTS IN MALAYSIA POST-COVID-19

Phase	Nature	Scope	Pace
Phase 1 (Infrastructure)	Energy, railways, ports, roads and industrial parks	Previously, leading Chinese contractors, often Chinese State-Owned Entities ('SOE'), had secured numerous infrastructure projects in Malaysia, such as CREC, CSCE and CCCC. These projects are expected ultimately to reach fruition.	Domestic and foreign lockdowns have delayed many infrastructure BRI projects in Malaysia, casting the limelight on force majeure clauses in infrastructure contracts.

Phase 2 (Knowledge and Logistics)	Technology, financial institutions,[5] real estate, and logistics	For private Chinese corporations like Alibaba (Lazada) and Tencent (Shopee/WeChat) scouting for opportunities to further penetrate overseas markets, BRI countries already charted by Chinese SOEs may present greater assurance, especially with the greater uncertainty of the post-pandemic world.	Technology companies are typically better equipped not merely to weather, but to thrive amidst the challenges of a pandemic.[6] Heightened demand for cloud services and increased spending on other digital work tools have been forecast to remain.[7] Pre-pandemic, 2019 had already witnessed collaboration between Alibaba Cloud and major Malaysian corporates to expedite their digitalisation and inculcate technology at their core.[8] Malaysia was also the first foreign country to enable WeChat Pay in local currency (Ringgit Malaysia).[9] With greater demand for online retail and cashless payment methods post-pandemic, growth is likely to accelerate further still.

5 'China Construction Bank opens branch in East Malaysia's Financial Hub' (*Belt & Road News*, 26 October 2019).

6 Based only on the share prices of Alibaba, Tencent, and Xiaomi.

7 Deloitte, 'Understanding COVID-19's impact on the technology sector' (25 March 2020).

8 Edwin Yapp, 'Malaysian state investment fund adopts Alibaba Cloud' (*ComputerWeekly.com*, 1 August 2019); 'Alibaba Cloud expands its footprint as Malaysia's digital transformation journey accelerates' (*The Edge Markets*, (23 September 2019); Manirajan Ramasamy, 'Alibaba Cloud to help banks upgrade services with big data' (*Free Malaysia Today*, (31 July 2019).

9 Tan Zhai Yun, 'Bringing WeChat Pay to Malaysia' (*The Edge Markets*, (13 May 2019).

Future BRI Projects	Production lines are tipped to be shifted to countries across Southeast Asia. This change in the global supply chain is an opportunity for Malaysia to serve as a key regional hub in Southeast Asia.	Like many governments globally, the Malaysian government's present financial focus is on managing both COVID-19 itself and its economic consequences. In this climate, and as the BRI grows in scale, Chinese contractors will need to adopt a more competitive, market-based approach to secure projects and resolve disputes, instead of depending on government initiatives.	Outbound Chinese investment activity has continued, albeit at a slower pace. The current expectation is that key strategic deals will continue to move forward. Commentators have suggested that China faces pressure to extend or even write off loans to countries participating in the BRI because of the COVID-19 pandemic.[10] The importance of cash flow to progress in construction and infrastructure projects, at the heart of the BRI, is inescapable. As a net export country with abundant natural resources, Malaysia should be able to handle the debt burden of BRI commitments if the government exercises prudent fiscal discipline.

COMMON DISPUTE RESOLUTION MECHANISMS

Domestic Courts

Whilst hitherto uncommon, there have been instances of Phase 1 BRI disputes between Chinese private entities and Malaysian corporations coming before domestic courts. The paucity of such examples is likely because enforcement through local court proceedings of a foreign court's judgment is less straightforward than enforcement of an arbitral award. Crucially, Malaysia and China do not currently share any reciprocal arrangements for the enforcement in one of a judgment of the other's courts.

10 Weizhen Tan, 'China under pressure to write off loans as countries struggle to repay debt during coronavirus crisis' (*CNBC*, (10 May 2020).

Jurisdiction	Reciprocal Enforcement Partners
Malaysia[11]	United Kingdom, Hong Kong, Singapore, New Zealand, Sri Lanka, India, Brunei
China[12]	Brazil, France, Italy, Russia, Ukraine, Spain, Poland, Romania, Belarus, Bulgaria, Lithuania, Bosnia and Herzegovina, Kazakhstan, Turkey, Cyprus, Kazakhstan, Cuba, Tunisia, Peru, Algeria, Ethiopia, Kyrgyzstan, Hungary, Tajikistan, Uzbekistan, Mongolia, Vietnam, Laos, Morocco, Egypt, UAE, Kuwait, Hong Kong

International Arbitration

Instead, major infrastructure projects in Malaysia, whether they adopt bespoke contracts or FIDIC standard forms, almost always specify arbitration as their final dispute resolution mechanism. The arbitral process is largely independent of domestic court systems. Especially in a cross-border context, arbitration substantially mitigates perceptions of any form of 'home court advantage' and difficulties in international recognition and enforcement that domestic court judgments may entail.

Similar thinking likely underlies the Chinese judiciary's efforts to promote arbitration for the resolution of international commercial disputes,[13] with amendments to China's Arbitration Law imminent. Both China and Malaysia — like the majority of BRI participating countries — are contracting states to the New York Convention,[14] which streamlines the cross-border enforcement of international arbitration awards.

In Malaysia, arbitration clauses generally refer disputes to the Asian International Arbitration Centre ('AIAC') under its own AIAC Arbitration Rules. An alternative is arbitration under the PAM[15] Arbitration Rules. Sadly, the late AIAC Director passed in March 2020 and his successor has yet to be appointed. This has led some players to opt for the PAM Arbitration Rules to

11 Reciprocal Enforcement of Judgments Act 1958 (Act 99).
12 Articles 281 and 282 of China's Civil Procedure Law and Interpretations of the Supreme People's Court on Applicability of the Civil Procedure Law Zhu Shi [2015] No 5.
13 Big Data Research Report on Cases of the Beijing Fourth Intermediate People's Court Involving Judicial Review of Arbitration and Standardization Guide for Adjudication of Cases Involving Judicial Review of Arbitration. See also Peter A. Neuman, Lili Jiang, 'Arbitration Reform in China: Keeping up with the Beijing Fourth Intermediate People's Court' (*Kluwer Arbitration Blog*, 8 August 2020).
14 The New York Convention on the Recognition and Enforcement of Arbitral Awards 1958 (New York Convention).
15 Pertubuhan Akitek Malaysia, or the Board of Architects Malaysia.

avoid procedural steps which involve the AIAC Director.

China's New Belt and Road Courts

On 29 June 2018, the Supreme People's Court established two branches of the China International Commercial Court ('CICC'), one in Shenzhen and the other in Xi'an. The Shenzhen Court is to preside over BRI Maritime Road disputes, whereas the Xi'an Court will handle overland Belt disputes. The CICC's judges are current judges of the Chinese courts, assisted by an International Commercial Expert Committee ('ICEC') of foreign legal experts. Proceedings are in Chinese. The CICC offers a 'one-stop shop' dispute resolution mechanism, spanning mediation, arbitration and litigation.

Since December 2018, the CICC has presided over several international commercial disputes, none specifically related to the BRI. Insofar as BRI projects are concerned, the CICC has yet to gain traction, but should gain long-term legitimacy and credibility with greater usage and internalisation.[16]

LESSONS LEARNT FROM PHASES 1 AND 2 OF BRI PROJECTS IN MALAYSIA

Business Intelligence and Due Diligence

Chinese companies looking to invest in foreign BRI countries must consider the applicable competitive, regulatory and investment landscape, at both a macro and micro levels. This is especially important when investment takes the form of acquiring a local firm. Whilst accelerated market penetration is valuable, it must be carefully and realistically weighed against the risks of misaligned attitudes to business ethics, corruption, fraud, IP infringement and market manipulation.

Many BRI countries do not have an existing pipeline of projects filtered through a rigorous selection process. To avoid committing to projects with significant delay risks, particularly in frontier markets, it is essential that Chinese contractors undertake their own due diligence of prospective investment targets and partners.

16 Lance Ang, 'International Commercial Courts and the Interplay Between Realism and Institutionalism: A Look at China and Singapore' (*Harvard International Law Journal*).

Political Risks

The scale of infrastructure projects means that they tend to be susceptible to changes in government in the middle of their life cycles. For instance, the change in the Malaysian government in May 2018 led to the suspension and renegotiation of numerous major BRI projects. This underscores the importance of conducting an objective assessment of local and political risks. Chinese companies should avoid heavy reliance on government relations, and instead pursue the benefits of collaborating with experienced, reputable local partners.

Legal Systems

The legal systems of BRI countries span the entire gamut of common law, civil law, Islamic law or some mixture of them. As it is the law of a country that gives meaning to a contract, investors' initial due diligence must include an assessment of a country's legal environment and enforcement mechanisms. We have seen Chinese companies struggle to manage and perform projects efficiently because of an insufficient understanding of a foreign country's legal system and regulatory requirements. Of course, the onus falls also on a country's government to eradicate the barriers to investment of an undeveloped legal system and any instances or perception of corruption.

REWARD AND RISK

There is no reward without risk, not least when it comes to a vision of the BRI's colossal scale. With the added challenges of COVID-19 and its economic consequences, the need for enterprising strategies to be grounded on astute due diligence becomes even more pronounced. With or without COVID-19, foreign players looking to venture into Malaysia (or indeed any other foreign country) should ensure that their risk assessments cover not only specific projects themselves, but also the cross-border effectiveness of a country's available dispute resolution methods and forums. These best practices will provide foreign players a solid, lasting foundation to reap the rewards of their investment in the BRI.