Rapidly Growing BRI Tech Hubs within the Digital Silk Road

While much has been written about major non China based tech hubs and their related ecosystems in Silicon Valley, London, Berlin, Israel and India, this article focuses on the emerging presence of tech hubs with a focus on FinTech along the rapidly expanding BRI. It also examines the drivers underlying this activity and links into the digital Silk Road, first launched in 2015.

The map below (Figure 1) plots tech hubs outside the ones noted above, both existing and planned, as well as FinTech investments by Chinese investors during the first three quarters of 2018 across countries within the BRI as well as those still outside the BRI.

Figure 1: BRI Tech Hubs/2018 BRI FinTech Investments

Leading BRI FinTech Hubs
Emerging Tech Hubs in BRI countries
Future Planned Tech Hubs in BRI countries

Investments:
BRI countries
Non BRI countries

You will note that most of the hubs on the map are clustered in Asia and in Africa. In Asia, we highlight leading FinTech hubs in Hong Kong and Singapore, as well as Bali (Indonesia), Bangkok (Thailand), Kuching (Malaysia) and Ho Chi Minh City (Vietnam).

In Africa, we highlight existing hubs in Lagos (Nigeria), Cape Town (South Africa), Nairobi (Kenya) and Cairo (Egypt).

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Other BRI countries planning either planning to launch or rapidly grow tech hubs, which are mostly focussed on FinTech include the UAE, Moscow (JV with TUS Holdings), Kazakhstan, Ethiopia and Lithuania, which sees itself as a regional hub for the 16+1. Austria, which has not yet signed the BRI MoU, but which has longstanding relationships across the CEE region and Portugal which hopes to be at the intersection of an extension of the inland Economic Belt and a maritime Silk Road, are also keen to become meaningful FinTach hubs.

Not surprisingly, Chinese outbound FinTech investments in 2018 through 30th September are mostly aligned with the Asian regional BRI tech hubs in Hong Kong, Singapore, Thailand, Indonesia and Malaysia. However there were also investments into other BRI countries in Pakistan, Bangladesh and Turkey.

Outside the BRI there were FinTech investments into Japan, Korea, India, Australia, Sweden, Ireland, Germany, Spain, Switzerland and Brazil.

Key Drivers

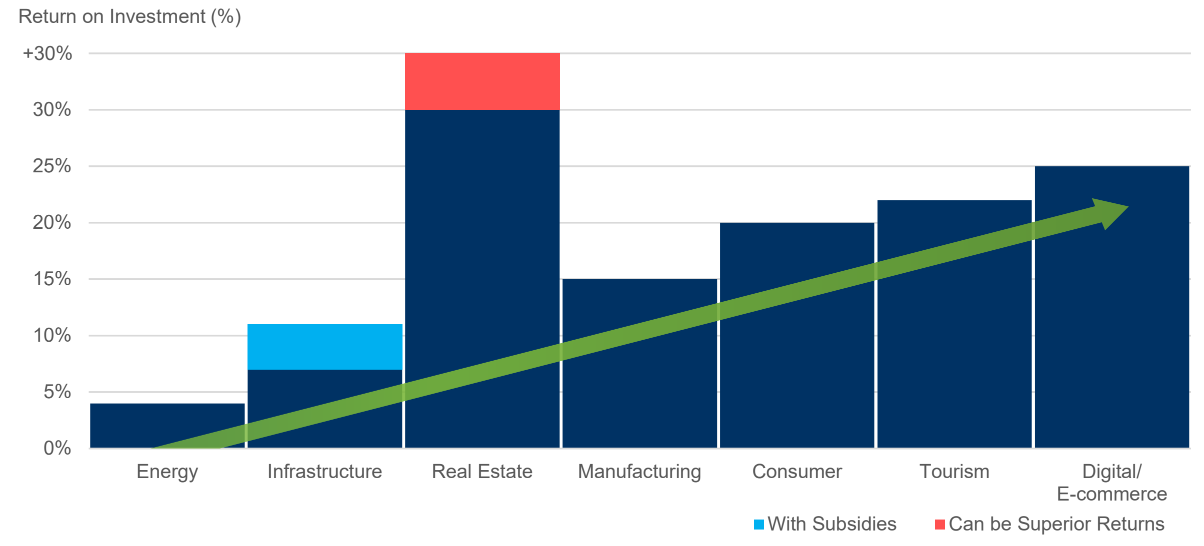
There are numerous strategic reasons for both the building of tech hubs along the BRI and the resulting investment which mostly mirror these hubs.

Economic Growth

Most of the economic growth relating to BRI countries in manufacturing, industrial and consumer is dependent on having adequate energy to power the countries. This is a problem across many of the BRI countries. Such infrastructure takes considerable time to build, frequently produces negative cash flows until the projects are on stream and the financial returns in these components are not as good as financial returns in other components until the country has been adequately powered.

The table below (Figure 2) based on China's own experience demonstrates this:

Figure 2: Exporting the Chinese Economic Growth Model



Building a FinTech sector does not have the long lead times or cost disadvantages of building industrial or manufacturing sectors. It also provides retail customers and SMEs access to previously unavailable financial services (especially in Southeast Asia, Africa and CEE), thus accelerating economic growth.

In 2017, Bain &Co published a study stating that the numbers of digital customers in Southeast Asia increased by 50% to 200 million during 2016, which has helped the region's internet economy grow to more than $50 billion. In its 2018 research, Bain noted that the region's digital economy accounted for only 7% of the region's GDP, versus 16% in China, 27% in Europe and 35% in the USA.

It is fair to expect similar future growth rates in Africa, where average ages are even lower than across Southeast Asia: Nigeria 17.9 years, Kenya 19.0 years, Egypt 23.9 years and Ethiopia 25.1 years. Future GDP increases will also raise employment in this high growth segment.

China FinTech Market Now Mature

While China did not really have a powerful FinTech sector until the early 2000's, some 25 years after Chairman Deng Xiaoping opened up China, it is now the world's leader in FinTech. There was a FinTech boom during the period of 2011-2013, during which a number of now major Chinese competitors were formed. This led to a period of high growth, especially in peer to peer (P2P) lending driven by non-bank lenders offering credit on competitive terms underwritten using data and funded in part from international capital. During the period of 2014-2017, Chinese FinTech companies raised circa $20 billion of fresh capital. During H1 2018, Asian FinTech companies raised another $16.8 billion, including $14 billion alone for Ant Financial.

The Chinese payments market is becoming saturated while P2P lending is facing recent curbs, thus these firms are now focused on taking their expertise internationally by investing in many of the BRI countries as shown in Figure 1. In doing so, they are able to gain access to local markets for e-commerce, including providing supply chain finance to SMEs as well as provide payment mechanisms for visiting Chinese tourists.

An excellent example of this expansion and its effects on important BRI countries are the two acquisitions Alibaba has made in Pakistan in 2018. It's initial acquisition of a 45% stake in Telenor, Pakistan's leading branchless microfinance bank, enabled Telenor to leverage the on-line banking and credit expertise and credit rating system within Alibaba.

Roughly two months later, Alibaba announced the acquisition of Daraz, Pakistan's largest e-commerce platform. In addition to Pakistan, Daraz also operates in Bangladesh, Myanmar, Sri Lanka and Nepal. These markets are home to 460 million people, 60% under the age of 35.

These two acquisitions also helped bring FDI into Pakistan which is facing current account constraints.

Aligned with the Digital Silk Road

The Digital Silk Road was first proposed in July 2015 in Brussels, although it had previously been designed in China with input from NDRC and MOFCOM. The near term goal of this project is to address the low percentage of internet usage in many BRI countries such as Sri Lanka, Bangladesh, Cambodia and Laos to name just a few. Longer term the goal of the digital BRI is to help redirect many of the economies of many countries along the BRI from natural resources and industrial to consumer.

As such communications are the key including mobile phones as well as access to global communications networks.

In 2017, Huawei and Pakistan signed an agreement to build a 8,800 kilometre cable linking Pakistan to Kenya via Djibouti which could then be extended north to Egypt and south to South Africa. China is also considering a fibre-optic cable across the Arctic Circle, linking Finland, Norway, Russia and Japan – as part of the Polar Silk Road. In May 2018, China installed the first cable linking West Africa (Cameroon) to Latin America (Brazil).

It is therefore not a surprise to see many of China's FinTech companies playing an important role in payments, e-commerce and logistics (an industry in which China invested $37 billion alone in 2017) to facilitate cross-border trade in many of these countries.

Thus, for all of the reasons set out above, expect many of these well capitalized Chinese based FinTech companies to continue their investment surge along the BRI throughout the foreseeable future as jointly building tech hubs is an important component of the digital Silk Road and very helpful to countries along the BRI in preparing for the next industrial revolution and for China to continue to build an innovation nation.