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The New Silk Road

How a Rising Arab World is Turning Away from the West and Rediscovering China

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Revised and updated edition

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To Julia and Alex

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Preface

“China is the world.” This is what Mohammed, an Egyptian trader, says to me while we sit in a Turkish cafe. The cafe is in Guangzhou, a large Chinese city neighboring Hong Kong. And it is full of Arab and Turkish traders meeting with their Chinese colleagues. Mohammed has lived in China for the past decade. He has apartments in three different cities and shuttles between each for work, buying goods for export to the Middle East.

Mohammed thinks China is the world because it has provided him with an opportunity to make money and create a better life for himself. He travels easily between China and the Middle East, faced by fewer visa restrictions than he would in Europe or the United States. China’s thirst for oil has also pushed oil prices to record highs, leaving his Arab customers with plenty of cash to spend. I have heard countless stories similar to that told by Mohammed.

The East is catching up to the West. And the change is most obvious in China and the Middle East, from the gleaming skyscrapers of Shanghai to the wealthy investors in Abu Dhabi. The result is a rise of two historic economic powers, and a rebalancing of the world’s center of economic gravity.

This story is increasingly familiar to readers of the *New York Times*, *Financial Times*, or any of the major international dailies. Less familiar is how China and the Middle East are reaching out to each other. It used to be that the two sold their consumer goods and crude oil mainly to the West. But they are increasingly looking closer to home, in the East. The economic crisis has only accelerated the changes taking place as a fast growing East contrasts with a slow growing West.

However, the changes are hard to observe. It is individuals, rather than governments, that are the driving force. Take the Syrian textiles trader who has established an office in Shanghai, or the Chinese entrepreneur who has constructed an exhibition building outside Damascus. They are part of a tapestry that weaves the new Silk Road together. But their stories are not easily uncovered while reading the international dailies. They are happening 1,000 feet below the surface.

Since the book's hardback edition was published, I have maintained a blog, titled the Silk Road Economy, keeping track of events in the Arab, Chinese, and English media. I have also travelled constantly between the two regions, speaking with traders, bankers, and CEOs, among others, about the changes taking place. I had fears that the economic crisis might initially disrupt the strengthening linkages of these two great powers. But, in the event, it has only reinforced them.

Chinese traders have started talking about "oumei," shorthand for Europe and the United States, as fading markets, and instead focus on "jiao dian," or hot spots, primarily in their own domestic market and the Middle East. They have good reason to be excited. Chinese exports slowed briefly during the crisis, but are now higher than they were pre-crisis, having grown to $60 billion.

There are some important, and well-observed, reasons for the increase. China entered the World Trade Organization in 2001, resulting in a drop in the import duties the Middle East imposed on Chinese-made goods. Massive outsourcing by Asian electronics factories to China also produced a sharp increase in the latter's exports of electronics goods, from DVD players to notebook computers, over the past decade. The surge in oil prices has meanwhile fuelled the Middle East's own demand for consumer goods.

Yet there are other equally important, but less well-observed, reasons. Visas remain an important explanation for the growth in trade. Europe and the United States tightened visa restrictions on Arab nationals after September 2001. They have since relaxed them only modestly and the number of Arab nationals receiving visas to the United States, for instance, remains below its pre-2001 levels. China, meanwhile, relaxed its own visa policy, recognizing that visiting Arab traders buy goods and create jobs.

And so Yiwu, the small Chinese coastal city and a virtual Arab market town, continues to flourish. I have visited the city on several occasions since the hardback edition was published, and the number of Arab restaurants and Arabic-speaking translators is still impressive. Worried that Arab traders might be hesitant to visit Yiwu, as the economic crisis and oil prices plummeted, the city's traders set up shop once a year in Dubai itself, at the China Sourcing Fair. They even created a Yiwu-city logo to advertise their participation.

It was not a surprise then when China overtook the United States in 2008 as the world's largest exporter to the Middle East, having overtaken Germany in 2006 and the United Kingdom in 2002. It was a symbolic changing of the guard. Sure China's exports to all parts of the world grew quickly during the period. But its exports to the Middle East have grown at faster rates than its exports to either Africa or Latin America, two equally important emerging markets.

And what does the Middle East think of a flood of cheap Chinese consumer goods? They are certainly welcomed by the region's growing middle-class. I recall shopping for a digital camera with a Syrian friend in Damascus. "If it wasn't for China I wouldn't be able to afford this," he said. He looked delighted at his new purchase, and spent the next week showing me the camera's many features and newly taken pictures of his family.

However, not everyone is happy. The Palestinian city of Hebron has a large textiles industry. It produces Keffiyehs, the black and white checkered scarves so popular among the Palestinians and made famous by the former Palestinian leader Yasser Arafat. But Hebron's textile industry employs just 5,000 people today, down from 15,000 a decade ago. Cheap Chinese imports have undercut local producers. Palestinian men, in their conflicts with Israeli soldiers, are now covering their faces with made-in-China keffiyehs.

While the Middle East's political problems grab media headlines, the region's economic problems are just as damaging. The Middle East has a large youth population of 177 million, or 56 percent of the total population. It is an astonishing figure, the product of high birth rates over the past two decades. Unless they are put to work, these youth will become frustrated and risk turning to crime or violence. And if China's exports to the Middle East continues to grow unchecked, resulting in factory closures, the odds of such an outcome will grow.

Nevertheless, there is an alternative trajectory. Chinese manufacturers, the type that produce the cheap clothing and microwave ovens that fill shelves in Walmarts and Carrefours around the world, are starting to look abroad in response to rising production costs and transport costs at home. They are also looking abroad for fear that rising protectionism will deny them access to Europe, their largest market. If sustained, the development is of huge importance. Whereas China once received factories from the rest of the world, it might start exporting them.

It is typical to focus on countries such as Bangladesh and Vietnam as an alternative to China. But countries such as Egypt are also compelling. Not only does it have a cheap labor force, but Egypt is also situated closer to Europe. This is a boon as oil prices rise to over $80 a barrel and transport costs surge. Moreover, Egypt enjoys preferential market access, having earlier signed a free-trade agreement with the European Union. In 2009, two Chinese air conditioner manufacturers built factories outside of Egypt for just this reason.

An increase in cross-investment would be welcome. China and the Middle East boast some of the world's largest wealth funds. Their public wealth is measured in trillions and they have not been shy to put the money to work as asset prices, especially in Europe and the United States, tumbled during the crisis. The rise of the region's wealth funds is among the most potent symbols of the transfer in wealth from West to East. And it is not surprising that Western bankers fill flights to Beijing and Abu Dhabi as they pitch for funds.

But China and the Middle East have so far invested little in each other. They are good reasons for this; the Middle East's energy assets are largely not up for sale, while it remains too difficult to buy majority stakes in China's established companies. Still, the restrictions will ease in time, especially as controls on foreigners buying domestic stocks are eased. The wealth funds are also increasingly active, such as the joint-venture agreement signed between the China Investment Corporation and the Qatar Investment Authority in late 2009. But more work needs to be done to spur cross-investment.

The Silk Road, of course, was never just about trade and capital. It was also about ideas. One of the best examples was the export of Islam eastwards and Buddhism westwards. China's rise has equally provided the Middle East with an alternative way to think of the world.

Take a study trip made by the governor of Syria's Hasakah province to China's Hunan province in early 2008. He was there to learn more about Hunan's economic reform experience. It made sense. The two provinces are largely poor and agricultural. They both export migrant labor to wealthier coastal cities. They both certainly have more in common they did with the policy planners in Washington who more often gave theoretical, rather than practical, advice. And Hunan's 12 percent average economic growth over the past 10 years must have given hope to the Hasakah's governor.

I also recall watching Song Hongbing, the author of the Chinese-language book, *Currency Wars*, appear on the Arabic-language news channel Al Jazeera in early 2009. He was invited by Bila Hudood, one of the news channel's more popular talk shows. Song's book argued that the West uses its currency policy to prevent the rise of the East. His themes might be considered conspiracy theory, but they were popular among Chinese officials, and they also resonated in the Middle East, especially among the region's former colonies.

Islam is also one of the Silk Road's more important links, but its role is often misunderstood. China's 20 million Muslim population, according to official figures, ranks it alongside Syria and Saudi Arabia. It is tempting to assume that relations between China and its Muslim population are poor because of tensions in the country's western provinces. And, as a result, China's relations with the mainly Muslim population of the Middle East will also face major challenges. But this is a superficial reading of the situation.

Certainly, China's relations with its Uyghur Muslim population are strained. Yet, the Uyghur account for 8 million of the 20 million Muslim population. The Hui Muslim minority make up 10 million.

Who are the Hui? They are the original descendents of Silk Road traders, and the later converts to Islam. They have largely assimilated with the Han Chinese majority and are indistinguishable from the average Chinese national, especially when compared to the Uyghur who share more in common with their Turkic ancestors. The Hui are more geographically diverse, living across the country rather than only in the western provinces. They speak Mandarin Chinese and hold senior positions in government. They are also, most importantly, a useful ally in China's strengthening relations with the Middle East.

Neither is China afraid to play its Muslim card. Take a speech delivered by Prime Minister Wen Jiabao at the Arab League Headquarters in late 2009. Typically, such a speech would stick tightly to a script about bilateral trade and investment relations. But this time Wen started by emphasizing China's historical relationship with the Muslim world. He spoke about the 35,000 mosques in China and the fact that public institutions are legally required to provide Halal food, suitable for the country's Muslim minority.

With the global economic crisis not yet over, what next for China's relations with the Middle East and a historical rebalancing in the world's center of economic gravity?

If there is one city that sums up the potential in the relationship, it is Dubai. The small emirate has received a great deal of bad press as a result of its credit problems. Yet, its foundations remain strong. Dubai was eliminating duties, dredging deep water ports, and building international airports decades ago, long before it embarked on the more glitzy construction projects that have since created such problems for the emirate's rulers. China is already starting to see Dubai's promise as its global reach extends.

What is that promise? Dubai has the type of geography money cannot buy. It lies in the center of three great continents: Asia, Africa, and Europe. This is important to China. For instance, while China's trade with Africa has captured media attention, over 35 percent of that trade is with North Africa, a region that shares strong cultural, historical, and religious ties with the Middle East. And it makes sense for Chinese companies with large business activities in North Africa to set up regional headquarters in Dubai, rather than a city in Africa.

No surprise then Chinese companies are already making a stand in Dubai. The city already hosts 200,000 Chinese nationals, with nearly 50,000 of them traders. Chinese banks are also increasingly active, lending to construction projects in the emirates. In time Dubai will learn to pitch itself more aggressively to China so as to encourage such activity. And Chinese companies will help to fill empty office buildings, some left by exiting Western companies, in another small sign of the changes at work in the global economy.

Chapter 1

The New Silk Road: The Arab World Rediscovers China

Yiwu is a small city by Chinese standards. It has fewer than a million people and lies in the shadow of its wealthy neighbors, Shanghai and Wenzhou. But Yiwu is special. It claims the world's largest wholesale market for consumer goods and is a Mecca for foreign traders. I had heard about the market from a Syrian trader, having asked him if there were many Arab traders in the city. He laughed and replied, "Not *many* Arab traders. *All* Arab traders are in Yiwu." Intrigued, I decided to find out for myself. It was winter when I arrived and the city was gripped by a chill wind. I hustled out of the small airport into the warmth of a taxi. We sped along a newly built freeway to the city's outskirts. From the outside, the exhibition hall looks like a large American mall. But, from the inside, it looks like a riotous collision of every retail shop, city market, and roadside stall in the world.

There are 18,000 individual stalls. Most are less than ten feet wide and staffed by a single stallholder. Each is stuffed with product samples and sell wholesale only. The literature claims there are 320,000 products for sale. Multiply each sample by the thousands of identical products filling warehouses elsewhere in the city and you start to arrive at the sheer volume of goods that Yiwu ships to the rest of the world. It was a mind-numbing experience to walk past a hundred stalls displaying inflatable toys, another hundred stalls displaying plastic flowers, and yet another hundred stalls displaying cutlery. Yiwu's exhibition halls are a massive temple to the twin-gods of consumerism and globalization that have captured the imagination of traders from around the world.

Even the Chinese are impressed. When the Chinese Commerce Minister Bo Xilai visited the city he was awed enough to suggest that the municipal government create an index to survey the city's trade in small consumer goods.[1] Bo recognized that Yiwu was so important to the entire country's trade in small consumer goods that the index would accurately reflect the health of that sector of the economy. The city's municipal government sensibly agreed to his suggestion; after all, Bo was a senior Communist Party leader, the son of one of the "Eight Immortals" responsible for the country's post-Mao transition. A walk through the city's exhibition halls today reveals bronze plates identifying which shops participate in the survey. The Yiwu index takes the temperature of the world's demand for small consumer goods.

Yiwu isn't widely known in the West. The city only started to make its fortune from the early 2000s, whereas Wenzhou, a three-hour drive north, was already an export dynamo in the early 1990s. But Yiwu is different. It sells mainly to individual traders, rather than to large retail conglomerates such as Wal-Mart and Carrefour so the city hasn't grabbed the Western media's attention. Yiwu is also better known in the developing world than in the developed world. As I walked through the city's exhibition halls, I met traders from Cairo, Lagos, and Budapest, among dozens of other cities. It is a true global village. Traders traveled in groups of two or three, accompanied by translators. Most were visiting the city for just a few days before returning to their home countries. All had caught the Yiwu bug.

What makes Yiwu special? It focuses on selling the type of cheap consumer goods that can be purchased for a few dollars. Vendors are also happy to sell in small volume, ideal for developing-world traders who are generally stocking their own street stalls back home and prefer to buy just a few hundred, rather than a few thousand, of any single item. And so, Yiwu has found a niche. But its timing is also fortuitous. The developing world is booming. A surge in commodity prices had injected cash into many economies even as governments have opened their domestic markets to foreign imports. It is an explosive combination and the sudden flood of traders to Yiwu represented the cutting edge of a consumer boom across large parts of the developing world. Forget selling DVDs to America and shoes to Europe. Yiwu is making its fortune selling gifts, toys, and hardware to the developing world.

At one point I found myself in a little stall selling religious icons. A Romanian trader was shopping for pictures of Christian saints while the Chinese shopkeeper stood attentively at his side. The pictures were painted in the fourteenth-century Italian style and depicted a single Christian saint robed in dark cloth and crowned by a golden halo. But these pictures were made from cheap plastic, sold for less than a dollar, and were destined for the walls of homes in Eastern Europe. A few saints had small electric bulbs inserted into their halos that flashed like Christmas tree lights. The Romanian trader was amused by this and pulled a sample from the shelf for closer inspection. I turned away to investigate the rest of the shop and found the opposite shelves filled with pictures of Islamic religious images made from the same cheap plastic. This is the genius of Yiwu. It is the world's largest consumer goods market because it is prepared to sell to anyone in the world, regardless of faith or nationality.

Thomas Friedman alluded to this in his book *The World Is Flat* when he wrote how many festival lamps for sale in Egypt are now made in China. There is a good chance the lamps were from Yiwu. An Egyptian trader had likely spotted the Chinese-festival lamps for sale in Yiwu's exhibition halls and been struck by their similarity to the Egyptian festival lamps. The trader would have asked the Chinese stallholder to modify the design to suit the Egyptian market and placed an order for several thousand. The stallholder would have produced twice that amount hoping to sell the same lamps to other Egyptian traders. If successful, other Chinese stallholders might copy the lamps for sale in their own stalls. In short time, Egyptian festival lamps will have sprouted throughout the city's exhibition halls. It's not just Egyptian festival lamps either, but a multitude of goods sold to all parts of the developing world.

The rise of Yiwu is matched by a surge in arrivals to China. In 2000, China received 445,000 visitors from Africa, the Middle East, and Latin America. By 2008, the number had risen almost five times to reach 2,395,000.[2] The biggest increases are posted in October each year when trade fairs are held in Yiwu and the southern city of Guangzhou.[3] These fairs are popular among traders who lack the sophisticated purchasing networks enjoyed by global retail giants such as Wal-Mart and Carrefour as they are an opportunity to meet wholesalers and inspect a large range of goods. The number of arrivals jumps by tens of thousands as traders flock to the two cities echoing the traders in the bazaars of the old world.

This makes the flight from Guangzhou to Yiwu an experience. It is the only flight in China I can recall on which foreigners regularly outnumber Chinese. No easy thing. I was once seated next to a group of elderly Romanian women dressed in black, their teeth capped gold. They didn't speak either Chinese or English, but we managed to communicate by drawing pictures on the airline's in-flight magazines. On a later flight, I was seated next to an Egyptian shoe manufacturer, a Christian Copt who was wearing a necklace with a heavy gold cross. He owned a factory outside of Cairo, but it was empty, and he now imports all his shoes from Yiwu. "What can I do?" he said with palms raised upwards. "I have to make a living and it's cheaper to import from China than to manufacture locally." He visits the city four times a year to meet with manufacturers and place new orders. I have met many others like him on the flight to Yiwu, all with similar stories to tell.

* * *

It was the Arab traders who first discovered Yiwu shortly after September 2001. These traders had found it increasingly difficult to travel to America due to visa restrictions. There were anecdotal stories of traders detained at customs when their names mistakenly matched those on a "terror watch list." The number of Arabs traveling to the United States stood at over 250,000 in 2000. By 2009, the figure had fallen to 197,000.[4] The average American household might feel safer knowing that Arab visitors are less likely to visit Atlanta or Chicago. But the world has changed. Arab traders might have stayed at home when faced with visa restrictions; today, they travel to Yiwu, China.

It was unfortunate timing for the West. The Arab traders had money to spend for the first time in almost a decade. Oil prices have hit record highs and the Arab economies were booming. Average economic growth was an impressive 5.3 percent, between 2004 and 2009 versus 2.5 percent in the developed