

China's External Economic Model in the South Caucasus: Interests, Instruments, and Challenges for Armenia, Georgia, and Azerbaijan

Executive Summary

This article analyzes China's external economic engagement in the South Caucasus, focusing on Armenia, Georgia, and Azerbaijan, within the framework of geoeconomics and state-led capitalism. It argues that the region occupies a secondary but functionally relevant position in China's Eurasian strategy, driven primarily by connectivity and risk diversification rather than large-scale economic integration. China's approach is characterized by selective, country-specific engagement, with Azerbaijan emerging as the most relevant partner, Georgia facing geopolitical and regulatory constraints, and Armenia remaining limited to niche cooperation. The study highlights a persistent asymmetry of expectations between China and the South Caucasus states and concludes that sustainable benefits from cooperation with China will depend on institutional capacity, realistic strategic planning, and improved regional coordination.

1. Introduction

Over the past decade, China's external economic strategy has undergone a significant transformation, increasingly emphasizing connectivity, infrastructure development, and the diversification of trade and investment routes across Eurasia. The Belt and Road Initiative (BRI) has become the central framework through which Beijing seeks to expand its economic presence beyond traditional markets, mitigate geopolitical risks, and secure long-term access to global supply chains. In this context, regions previously considered peripheral to China's core economic interests have gained renewed importance, including the South Caucasus.

The South Caucasus—comprising Armenia, Georgia, and Azerbaijan—occupies a strategically sensitive position at the intersection of Europe, Central Asia, the Middle East, and the Black Sea region. While the region does not represent a major market in terms of size or consumption, its geographic location grants it potential relevance

as part of alternative trans-Eurasian transport corridors, particularly amid growing uncertainties surrounding traditional routes through Russia and the Suez Canal. As global trade patterns adjust to geopolitical fragmentation, sanctions regimes, and supply chain reconfiguration, Beijing has shown increasing interest in diversified and politically flexible connectivity options.

Despite this growing attention, China's engagement with the South Caucasus remains uneven and frequently misunderstood. Public discourse in the region often oscillates between inflated expectations of large-scale Chinese investments and concerns about political dependency. In practice, China's approach is more cautious and selective, shaped by pragmatic economic considerations rather than ambitions of political dominance. To conceptualize this engagement, the article adopts a theoretical and analytical framework combining **geoeconomics** and **state-led capitalism**.

2. Theoretical and Analytical Framework: China's External Economic Model

China's external economic engagement is best understood through the combined lenses of **geoeconomics** and **state-led capitalism**, which together explain the strategic use of economic instruments beyond market-driven investment logic¹. In this framework, trade, infrastructure financing, and outward investment are not autonomous commercial activities but tools embedded in broader state strategies aimed at enhancing strategic autonomy and managing external vulnerabilities.

From a geoeconomic perspective, economic instruments are deployed to shape the external environment in ways that reduce exposure to geopolitical pressure and systemic shocks. Connectivity projects, transport corridors, and logistics networks function as mechanisms for **risk diversification**, enabling China to mitigate dependence on single routes, markets, or political actors.² This logic has become

¹ MERICS. *China's Belt and Road Initiative after a Decade*. 2023.
<https://merics.org/en/report/chinas-belt-and-road-initiative-after-decade>

² OECD. *Connectivity and Global Value Chains*. 2024.
<https://www.oecd.org/industry/global-value-chains/>

increasingly salient amid sanctions regimes, supply-chain disruptions, and intensifying great-power competition.

The Belt and Road Initiative (BRI) institutionalizes this geoeconomic approach by prioritizing **infrastructure, connectivity, and trade facilitation** as strategic enablers rather than as purely commercial ventures.³ While early interpretations of the BRI emphasized expansion and scale, more recent assessments highlight a shift toward **selectivity, financial sustainability, and risk control**, reflecting both internal policy recalibration and lessons learned from host-country constraints.⁴

At the same time, China's external economic model is shaped by the structural features of **state-led capitalism**, in which state-owned enterprises (SOEs), policy banks, and regulatory authorities play a central coordinating role.⁵ Outward economic engagement is supported by institutions such as the Export–Import Bank of China and the China Development Bank, which provide long-term financing aligned with state priorities. This institutional architecture allows China to pursue projects that may offer strategic value even when short-term commercial returns are limited.

However, state-led capitalism does not imply uniform or unlimited engagement. Empirical evidence indicates that Chinese outward investment has become more cautious, with increasing emphasis on **project feasibility, host-country governance conditions, and debt sustainability**.⁶ This evolution challenges simplistic interpretations of China's external economic activity as either purely strategic or purely commercial, suggesting instead a hybrid model that balances strategic objectives with pragmatic risk assessment.

Within this analytical framework, China's engagement in peripheral yet strategically positioned regions—such as the South Caucasus—can be understood as

³ Asian Development Bank. *Asian Economic Integration Report 2023: Trade, Supply Chains, and Connectivity*.

<https://www.adb.org/publications/asian-economic-integration-report-2023>

⁴ Springer. *Hotspot Geopolitics: Political Economy of the Belt and Road Initiative in the South Caucasus*. 2025.

<https://link.springer.com>

⁵ OECD. *State-Owned Enterprises and the Global Economy*. 2023.

<https://www.oecd.org/corporate/soe/>

⁶ Ministry of Commerce of the People's Republic of China (MOFCOM). *Statistical Bulletin of China's Outward Foreign Direct Investment 2023*.

<https://fdi.mofcom.gov.cn/EN/Statistics/Statistics.aspx>

function-driven rather than integration-driven. The objective is not comprehensive economic incorporation but the creation of optionality, redundancy, and limited exposure. This perspective provides a conceptual foundation for analyzing why China's presence in the South Caucasus remains selective, differentiated, and closely tied to connectivity and logistics considerations rather than broad-based investment or political alignment.

3. The South Caucasus in China's Eurasian Strategy

Within China's broader Eurasian strategy, the South Caucasus occupies a **functionally relevant but structurally secondary position.** Its importance derives less from domestic market potential and more from its geographic role in facilitating alternative east–west connectivity, notably through the Middle Corridor linking China to Europe via Central Asia, the Caspian Sea, the South Caucasus, and Turkey.⁷

From Beijing's perspective, the Middle Corridor represents **one of several possible routes rather than a substitute for existing pathways.** Compared to the Northern Route through Russia, the Middle Corridor remains more costly and fragmented, requiring multiple border crossings and maritime segments across the Caspian Sea. In contrast to southern alternatives, including routes involving Iran or the International North–South Transport Corridor, the South Caucasus offers political flexibility but lacks scale and infrastructural depth.⁸ These comparative constraints explain why China treats the region as a **supplementary option that enhances redundancy rather than a primary logistics artery.**⁹

⁷ European Institute for Asian Studies (EIAS). *The Middle Corridor: Where Europe and Asia Meet*. 2024.

<https://www.eias.org/publications/the-middle-corridor-where-europe-and-asia-meet/>

⁸ Asian Development Bank. *Asian Economic Integration Report 2023: Trade, Supply Chains, and Connectivity*.

<https://www.adb.org/publications/asian-economic-integration-report-2023>

⁹ OECD. *Connectivity and Global Value Chains*. 2024.

<https://www.oecd.org/industry/global-value-chains/>

China, therefore, approaches the South Caucasus with an emphasis on **incremental improvements, feasibility-oriented projects, and bilateral cooperation** instead of comprehensive regional integration. Engagement is shaped by concerns over infrastructure fragmentation, regulatory heterogeneity, and geopolitical risk, as well as by China’s broader recalibration of the Belt and Road Initiative toward sustainability and risk control.¹⁰ Against this strategic backdrop, China’s involvement takes **differentiated forms across Armenia, Georgia, and Azerbaijan**.¹¹

To contextualize the relative scale and structure of China’s economic engagement in the region, Table 1 presents selected indicators of trade, investment, and sectoral focus across Armenia, Georgia, and Azerbaijan.

Table 1. China–South Caucasus Economic Engagement: Selected Indicators

Country	Trade with China (approx.)	Chinese FDI Presence	Key Sectors of Engagement	Strategic Relevance for China
Azerbaijan	Moderate	Limited, project-based	Logistics, transport, energy-related	Medium–High (Trans-Caspian)
Georgia	Moderate	Limited, selective	Logistics, ports, trade facilitation	Medium (Black Sea access)
Armenia	Low–Moderate	Small-scale	Light manufacturing, IT, renewables	Low (non-transit)

*Source: MOFCOM; OECD; UNCTAD; author’s compilation. ^{*12}

¹⁰ MERICS. *China’s Belt and Road Initiative after a Decade*. 2023.

<https://merics.org/en/report/chinas-belt-and-road-initiative-after-decade>

¹¹ Springer. *Hotspot Geopolitics: Political Economy of the Belt and Road Initiative in the South Caucasus*. 2025.

<https://link.springer.com>

¹² UNCTAD. *World Investment Report 2023: Country Factsheets*;

Ministry of Commerce of the PRC (MOFCOM). *Statistical Bulletin of China’s Outward Foreign Direct Investment 2023*;

OECD. *FDI Statistics by Partner Country*.

<https://unctad.org/publication/world-investment-report-2023>

4. Country-Level Analysis

China's economic engagement with the South Caucasus is highly differentiated, reflecting variations in connectivity, economic structure, and geopolitical positioning across Armenia, Georgia, and Azerbaijan. Rather than pursuing a unified regional strategy, Beijing tailors its involvement to country-specific conditions, prioritizing functionality and risk mitigation.

4.1 Azerbaijan

Azerbaijan occupies the most prominent position in China's South Caucasus engagement due to its role in **Caspian logistics**, relative political stability, and strategic location within the **Trans-Caspian segment of the Middle Corridor**.¹³

While Azerbaijan is not a major energy supplier to China, cooperation in the energy sector carries **symbolic and strategic value**, reinforcing Baku's broader strategy of diversified external partnerships.¹⁴

China's primary interest in Azerbaijan lies in **transport infrastructure, logistics services, and contractual projects** linked to rail and port connectivity.¹⁵ Chinese companies are more active in **construction, engineering, and service provision** than in equity investment, reflecting a cautious approach toward long-term exposure in a geopolitically sensitive environment.¹⁶ For Azerbaijan, cooperation with China

<https://fdi.mofcom.gov.cn/EN/Statistics/Statistics.aspx>

<https://www.oecd.org/investment/statistics.htm>

¹³ European Institute for Asian Studies (EIAS). *The Middle Corridor: Where Europe and Asia Meet*. 2024.

<https://www.eias.org/publications/the-middle-corridor-where-europe-and-asia-meet/>

¹⁴ Asian Development Bank. *Asian Economic Integration Report 2023*.

<https://www.adb.org/publications/asian-economic-integration-report-2023>

¹⁵ Georgian Foundation for Strategic and International Studies (GFSIS). *China's Activities in the South Caucasus*. 2024.

<https://gfsis.org/publications/view/chinas-activities-in-the-south-caucasus>

¹⁶ Ministry of Commerce of the People's Republic of China (MOFCOM). *Statistical Bulletin of China's Outward Foreign Direct Investment 2023*.

<https://fdi.mofcom.gov.cn/EN/Statistics/Statistics.aspx>

offers opportunities to strengthen its **transit role across the Caspian Sea** and diversify partnerships beyond traditional energy markets. However, the country's **hydrocarbon-dependent economic structure** limits the spillover effects of transit-oriented cooperation and constrains broader industrial diversification.¹⁷

4.2 Georgia

Georgia's strategic relevance for China is anchored in its **Black Sea access** and long-standing ambition to function as a **transit hub between Europe and Asia**.¹⁸ The **bilateral free trade agreement with China** has enhanced Georgia's profile as a potential gateway for Chinese goods, while Chinese interest has focused primarily on **logistics, transport infrastructure, and trade facilitation**.¹⁹

At the same time, Chinese engagement in Georgia has been shaped by **geopolitical sensitivities and regulatory constraints**. Alignment with **European Union standards**, combined with domestic political debates surrounding major infrastructure projects, has generated uncertainty and delayed implementation.²⁰ As a result, Georgia's cooperation with China remains characterized by **unrealized potential rather than large-scale transformation**.²¹ The Georgian case illustrates the tension between openness to Chinese economic cooperation and the constraints imposed by existing geopolitical and regulatory commitments.²²

¹⁷ UNCTAD. *World Investment Report 2023: Country Factsheets – Azerbaijan*. <https://unctad.org/publication/world-investment-report-2023>

¹⁸ European Institute for Asian Studies (EIAS). *The Middle Corridor: Where Europe and Asia Meet*. 2024.

<https://www.eias.org/publications/the-middle-corridor-where-europe-and-asia-meet/>

¹⁹ Ministry of Commerce of the People's Republic of China (MOFCOM). *China–Georgia Free Trade Agreement and Trade Statistics*.

<https://fta.mofcom.gov.cn/topic/en/chinageorgia.shtml>

²⁰ Springer. *Hotspot Geopolitics: Political Economy of the Belt and Road Initiative in the South Caucasus*. 2025.

<https://link.springer.com>

²¹ Georgian Foundation for Strategic and International Studies (GFSIS). *China's Activities in the South Caucasus*. 2024.

<https://gfsis.org/publications/view/chinas-activities-in-the-south-caucasus>

²² OECD. *Trade Policy Implications of EU Regulatory Alignment*. 2023. <https://www.oecd.org/trade/topics/trade-policy/>

4.3 Armenia

Armenia remains on the **periphery of China's external economic engagement** due to limited connectivity, landlocked geography, and persistent security challenges.²³ Unlike Azerbaijan and Georgia, Armenia does not function as a transit corridor within China's Eurasian strategy, significantly reducing its **functional relevance** for connectivity-oriented engagement.²⁴

Chinese cooperation with Armenia has therefore concentrated on **niche sectors**, including light manufacturing, information technology, and small-scale industrial projects.²⁵ These initiatives reflect **pragmatic assessments of Armenia's economic scale and comparative advantages** rather than ambitions of strategic integration. Structural constraints—including **limited market size, infrastructure gaps, and regional instability**—continue to restrict Armenia's role within China's broader connectivity-oriented external economic model.²⁶

5. Comparative Analysis and Asymmetric Expectations

A comparative assessment of China's engagement with Armenia, Georgia, and Azerbaijan reveals a persistent **asymmetry of expectations**. While South Caucasus states often perceive China as a strategic development partner capable of delivering large-scale investment and economic transformation, Beijing approaches the region pragmatically, prioritizing **feasibility, connectivity, and risk avoidance**.²⁷

²³ OECD. *Connectivity and Global Value Chains*. 2024.

<https://www.oecd.org/industry/global-value-chains/>

²⁴ European Institute for Asian Studies (EIAS). *The Middle Corridor: Where Europe and Asia Meet*. 2024.

<https://www.eias.org/publications/the-middle-corridor-where-europe-and-asia-meet/>

²⁵ Ministry of Commerce of the People's Republic of China (MOFCOM). *Outward FDI Statistics by Country*. 2023.

<https://fdi.mofcom.gov.cn/EN/Statistics/Statistics.aspx>

²⁶ UNCTAD. *World Investment Report 2023: Country Factsheets – Armenia*.

<https://unctad.org/publication/world-investment-report-2023>

²⁷ MERICS. *China's Belt and Road Initiative after a Decade*. 2023.

<https://merics.org/en/report/chinas-belt-and-road-initiative-after-decade>

This asymmetry is rooted in differences in **economic scale, institutional capacity, and strategic priorities**. For China, engagement with the South Caucasus serves primarily to enhance **flexibility and optionality** within its broader Eurasian strategy.²⁸ For regional states, cooperation with China is frequently framed as an opportunity for **diversification, development, and greater geopolitical autonomy**.²⁹ The resulting mismatch amplifies frustration and limits the transformative impact of economic cooperation.³⁰

Comparatively, Azerbaijan's logistics role aligns most closely with China's functional priorities, while Georgia's ambitions are constrained by **geopolitical and regulatory factors**. Armenia, facing **structural and security limitations**, remains marginal to China's engagement.³¹ These differentiated outcomes underscore the importance of **realistic expectations and capacity-driven strategies** in shaping China–South Caucasus economic relations.³²

6. Challenges for the South Caucasus States

The primary challenges facing South Caucasus states in their engagement with China include limited bargaining power, infrastructure sustainability risks, fragmented regional connectivity, geopolitical constraints, and institutional capacity gaps. As relatively small economies, Armenia, Georgia, and Azerbaijan face structural asymmetries when negotiating with a major global economic actor.

²⁸ OECD. *Connectivity and Global Value Chains*. 2024.

<https://www.oecd.org/industry/global-value-chains/>

²⁹ Georgian Foundation for Strategic and International Studies (GFSIS). *China's Activities in the South Caucasus*. 2024.

<https://gfsis.org/publications/view/chinas-activities-in-the-south-caucasus>

³⁰ Asian Development Bank. *Asian Economic Integration Report 2023*.

<https://www.adb.org/publications/asian-economic-integration-report-2023>

³¹ European Institute for Asian Studies (EIAS). *The Middle Corridor: Where Europe and Asia Meet*. 2024.

<https://www.eias.org/publications/the-middle-corridor-where-europe-and-asia-meet/>

³² UNCTAD. *World Investment Report 2023: Country Factsheets*.

<https://unctad.org/publication/world-investment-report-2023>

Ensuring project sustainability, strengthening governance mechanisms, and improving regional coordination are critical for maximizing potential benefits. Overestimating China's developmental role without parallel domestic reforms risks unmet expectations and suboptimal outcomes.

7. Conclusions and Outlook

China's engagement with the South Caucasus reflects a broader pattern of pragmatic, risk-conscious geoeconomic behavior. The region is unlikely to become a central pillar of China's Eurasian strategy but retains relevance as a supplementary corridor. Sustainable benefits for Armenia, Georgia, and Azerbaijan will depend on institutional strengthening, realistic expectations, and regional coordination rather than the scale of Chinese involvement alone.

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<https://merics.org/en/report/chinas-belt-and-road-initiative-after-decade>

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