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SEP • 2019 | No. 29

THOUGHT LEADERSHIP BRIEF

KEY POINTS

- The Chinese Debt Trap (CDT) is a conspiracy theory that reflects a US-led counter-mobilization against China's Belt and Road Initiative.
- No CDT exists anywhere, including in Sri Lanka, the case ubiquitously cited by media.
- Sri Lanka's Chinese-built and leased Hambantota International Port (HIP) is not part of debt trap, not a white elephant, not a debt-for-equity swap, and not a violation of sovereignty.

This research project is funded by the Strategic Public Policy Research Funding Scheme from the Central Policy Unit of the HKSAR Government.

The "Chinese Debt Trap" and its Sri Lanka Example

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Issue

"The Protocols of the Elders of Zion" was an influential 20th Century conspiracy theory spread by the Russian secret police, based on a 1903 forgery that purported to record Jews detailing the varied means they use to seek world domination. Protocol 21: Loans and Credit reads "We [Jews] have taken advantage of the venality of administrators and slackness of rulers to get our moneys twice, thrice and more times over, by lending to… governments moneys which were not at all needed by the States."

A Chinese Debt Trap (CDT) notion now similarly portrays China as lending to corrupt and inept foreign rulers to build useless infrastructure, expecting the borrowers to default. China can then seize state assets and further its drive to world domination. US elites aggressively promote this conspiracy theory: Vice President Pence and Secretary of State Pompeo accuse the Chinese of being predators who lend to deprive countries of their sovereignty, a charge that echoes those long made against Jews.

US liberal Democrats also back the CDT notion, as do US allies India, Japan and Australia, and some European leaders. The CDT however is, like the Protocols, a fantasy. Western media accuse Chinese of entrapping almost every developing country, but often focus on the example of Sri Lanka's Hambantota International Port (HIP). It in no way shows the existence of a CDT however.

Assessment

HIP is not a Chinese-plotted debt trap. Sri Lankans had, since the 1920s, talked about building an HIP next to the major Indian Ocean shipping lanes. In 2006-2007, the Government of Sri Lanka asked India and then Japan to finance it. They declined: India did not want to build a competitor to Indian ports and Japan was already Sri Lanka's biggest bilateral creditor.

The Government then had to actively persuade China to finance and build HIP, from 2007-2012. The Sri Lanka Port Authority (SLPA) initially managed it, but HIP, like many new ports, did not make as much money as expected. In 2016, the Government decided to lease out HIP and again approached India and Japan, who again declined. The Government then lobbied hard to attract a Chinese firm. Hong Kong-based China Merchants Port Holdings (CMPort), together with SLPA, agreed to take a 99-year leasehold.

The lease did not result from a pressing debt to China. Because of its long civil war and lower middle-income status, Sri Lanka by the mid-2000s could get few concessional loans, other than from China. Instead, it had to secure high-interest commercial loans, mainly from US and UK banks, and issue expensive international sovereign bonds (ISBs), mostly bought by Americans and mainly used not for infrastructure projects, but to cover general government expenditures.

About two-thirds of the Government's loans from China – to build HIP, railways, roads and power plants – are concessional, averaging 3.2% interest, and are mostly repayable over 20 years. By 2016, only 9% of Government external debt or 15% of all Sri Lanka public entity external debt was owed to China. It did not figure in any debt crisis: the SLPA could use profits from its Colombo Port to make HIP loan payments, some $67 million per year in 2016 and 2017. Meanwhile, the Government needed billions to repay ISBs and commercial bank loans held by Westerner investors.

HIP's lease is not a debt-for-equity swap. CMPort put up $1.12 billion, much more than HIP's then valuation, to receive less than a 70% share of the lease. While SLPA got more than a 30% share, plus a right to buy 20% more in ten years and the remainder thereafter. China does not own HIP and did not erase the HIP loan debt.

HIP is not a white elephant. Ports usually take one to two decades to become profitable. HIP aims for that in 4-8 more years. CMPort is China's biggest port operator, with 36 terminals in 18 countries. CMPort's Colombo International Container Terminal (CICT) became profitable within a year of opening in 2014. It now handles 38% of Colombo Port's container traffic using only 17% of its workforce. CICT says it contributes $2 billion in revenues to local entities every five years. The success of CICT is likely one reason the Government decided to lease HIP to CMPort.

When it took over HIP operations at the end of 2017, CMPort pledged to spend $400-600 million more for improvements, including bunkering (fuel provision) and, eventually, container terminals, to take up Colombo Port's overflow of transshipments. A planned industrial park is already attracting enterprises. Hambantota is Sri Lanka's poorest district, but with a railway and highway arriving, it seeks to become like China's Shekou, a booming port-park-city model.

Figure 1: Chinese Loans to Build HIP (Chamber of Young Lankan Entrepreneurs figures)

Year	US Dollars	Interest Rate	Term	Grace Period
2007	306.7m	6.4%	15 years	3 years
2011	144m	2%	20 years	5 years
2011	65.1m	2%	20 years	5 years
2011	600m	2%	20 years	5 years
2012	150m	2%	20 years	5 years

Figure 2: Interest, Principal Paid to China Exim Bank for HIP Construction Loans (up to time of lease)

Year	Interest	Principal
2010	$7.5m	$0
2011	$18.3m	$0
2012	$21.7m	$0
2013	$25.4m	$0
2014	$31.3m	$30.8m
2015	$34.7m	$33.8m
2016	$33.7m	$33.8m
2017 H1	$16.2m	$16.9m

HIP's 99-year lease does not infringe Sri Lanka's sovereignty. Like any sovereign, the Government can renegotiate or take back HIP and it forbids using the port as a foreign military base. Long leases are moreover not uncommon for investments that require high-value improvements. Australian states have leased out a half-dozen major ports for 99 years, to entities of varied nationality – local, UAE, Canadian, Indian, and Chinese. India allows its ports to be leased for 99 years and Canada has permitted leasing a Nova Scotia port for that long.

Recommendations

Analysts should call out CDT as an illogical conspiracy theory. Debt entrapment would alienate developing states from China and diminish their capacity to be its customers. There is no evidence that Chinese inveigle countries to build infrastructure or foreclose when they cannot repay loans. Our interviews in African states and Sri Lanka show that Chinese- financed infrastructure projects are almost always a local idea and require host state adoption. No national asset anywhere outside China has been forfeited to Chinese lenders. Recent studies in the US, UK and Germany, by the Rhodium and Oxford China Africa consultancies, the Center for Global Development, and University of Kiel scholars, show China has restructured loans for scores of debtor states, rather than pressing countries that have difficulties. In contrast, the Paris Club of largely developed country lenders seldom restructures debt.

It should be acknowledged that the CDT notion is a political instrument and reflection of racist ideology. It is part of the ongoing US counter-mobilization against China's investment and infrastructure-building Belt and Road Initiative. The BRI is seen as challenging US interests in developing states. US allies can be enlisted in the counter-mobilization through the rationale that Chinese use debt trap deceptions to victimize developing countries. Moreover, opposition forces that want to discredit a BRI country's ruling party can invoke the CDT when the government seeks Chinese loans, making these forces more apt to support the anti-BRI campaign.

Figure 3: Major Australian Ports Leased Out, 2010-2017

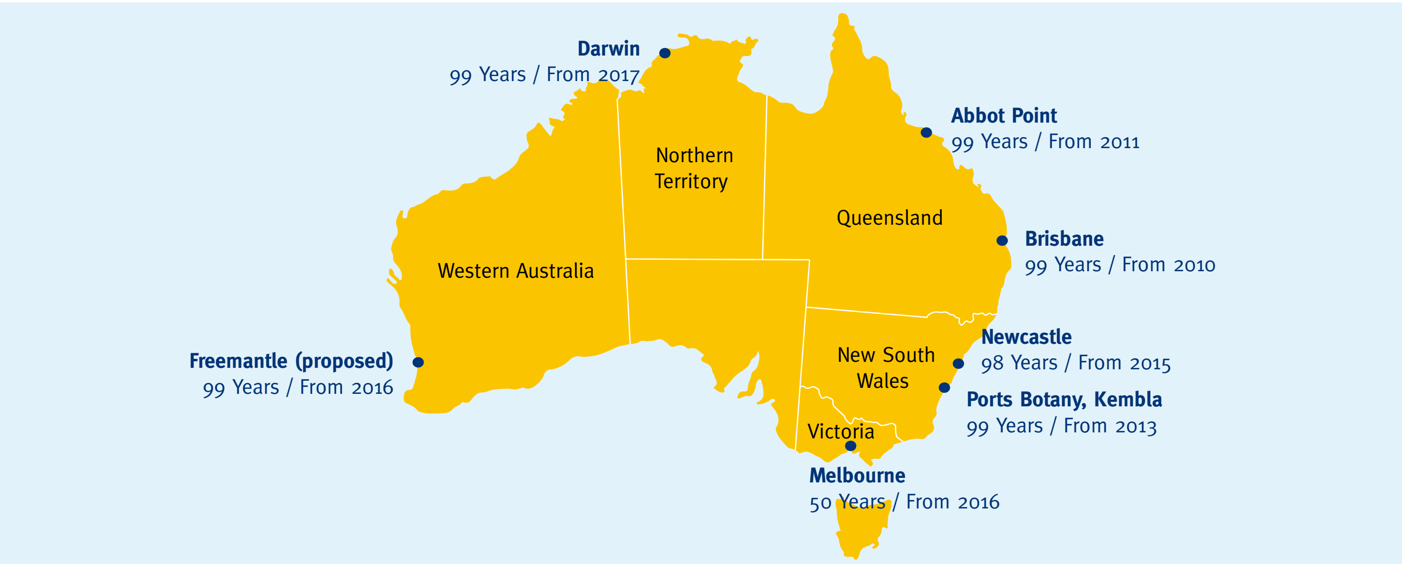
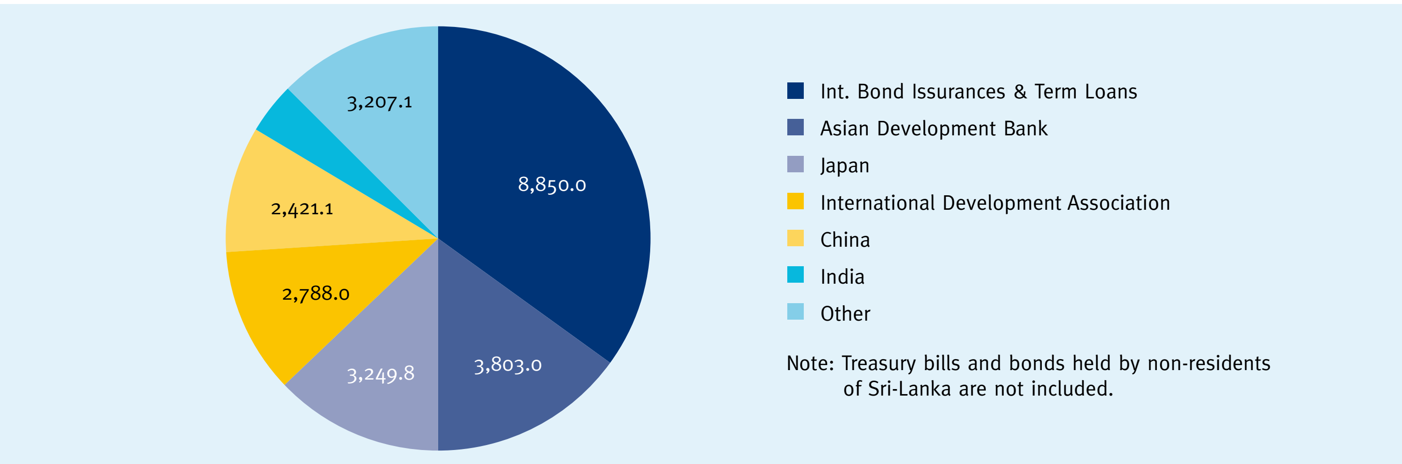


Figure 4: Total Government Foreign Debt Stock at the end of 2016 (in USD mn)



Source: Sri Lanka's External Debt Months Before the HIP Lease

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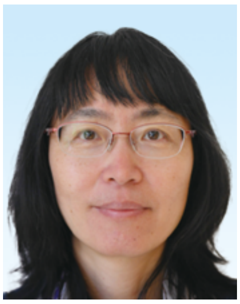
State Department Policy Planning chief Kiron Skinner has underlined that China "poses a unique challenge... because the regime in Beijing isn't a child of Western philosophy and history" and is, supposedly, the first "great power competitor that is not Caucasian." Classic Yellow Perilism posited that Chinese seek world domination. The same is said today by Trump advisors, such as John Bolton and Peter Navarro, and by US Republican and Democratic politicians, such as Senators Marco Rubio, Mark Warner and Gary Peters and House Committee on Homeland Security Chairman Michael McCaul. The historian of US/China relations Michael Schaller has observed that such claims are also analogs of "classical anti-Semitism."

Yellow Perilism then and now has represented China and Chinese as using infiltration, corruption, pollution, infection and addiction to ensnare countries. In the original Yellow Peril iteration, Chinese were accused of literally addicting others, to opium. That charge has been updated in the US with the opioid fentanyl, even though it mainly is produced domestically. At the same time, the CDT is presented as a metaphorical addicting of peoples, to debt, most prominently by Grant T. Harris, the Obama Administration's former chief Africa specialist.

Active repudiation of the CDT notion should be encouraged. That the CDT idea is embedded in a racist stereotype makes it difficult to dislodge, as does its association with a large authoritarian state. Yet, even as the CDT notion is spread by politicians and media, it is increasingly rejected by those specialists in China's overseas relations who have studied it. Wider circles should be encouraged to repudiate the CDT as logically and empirically flawed and a dangerous addition to the globalization of racism.

Barry Sautman is Professor Emeritus of Social Science at HKUST. He is a political scientist and lawyer who is a leading expert on China in Africa and has spent extensive time conducting research on Chinese investments in Zambia, Ethiopia, Kenya, and other African countries, with a particular focus on the relationship between Chinese employers and African workers. He has also conducted research on the Belt and Road Initiative in Sri Lanka.



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