



Connectivity Models in the Indo-Pacific: An Indian Perspective

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ABSTRACT

China's Belt and Road Initiative (BRI) is often sold as a project that aims to meet the infrastructure deficit in many underdeveloped parts of the world. However, Chinese projects under the BRI come with features that have negative short-term and long-term implications for the host countries in question. Chinese project financing almost uniformly lacks transparency, including about the terms of this financing, and is accompanied by uncertainty about local benefits such as employment and by poor standards. This paper begins by highlighting some key features of Chinese infrastructure projects under the BRI, before it examines, in detail, the financing of these projects, particularly in South Asia. The article concludes by stating that China's success in pushing the BRI – despite its several problems – is the result of the inability of democratic nations to come up with feasible alternatives that respect local sensitivities and conditions in the countries in need of infrastructure development. India, especially, has much to reflect upon in respect of its own methods and approaches towards its neighbours and towards overseas development assistance in the wake of China's BRI.

KEYWORDS

infrastructure development; connectivity; Belt and Road Initiative; project financing; employment; South Asia; Chinese foreign policy

Without doubt, it is the Belt and Road Initiative (BRI) – comprising the Silk Road Economic Belt¹ and the 21st Century Maritime Silk Road Initiative² – that is, today, the preferred Chinese framework for building connectivity with China's neighbours and the wider world.³ Such connectivity is often understood as an attempt to move excess infrastructure capacity existing in China to parts of the world where it is more urgently required, as well as to provide greater returns on investment.⁴ This would be unremarkable, were it not for the fact that this exercise comprises much more than meets the eye and does not come without both explicit and hidden costs to host or participating countries.

Problems with Chinese Physical Infrastructure Connectivity Models

Despite the hype and some obvious benefits, China's BRI⁵ is marked by several features of concern over both the short and long term.

First of all, as will be examined in detail in the next section, Chinese infrastructure development does not come free or even cheaply. What China offers to BRI host countries is mostly loans and not grants. And as Pakistani parliamentarians, asking rather pointed

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questions of their government, have discovered, Chinese loans often come at higher interest rates than those from other international lending agencies. The experience of Sri Lanka, which had to lease out its Hambantota port to the Chinese for 99 years because it was unable to repay Chinese loans, is instructive.

Second – and this is closely related to the first feature – more often than not, Chinese money from Chinese banks goes directly to Chinese companies, usually state-owned enterprises (SOEs), which then ship the necessary equipment to the target country. The host, however, has to pay the loan back with interest. In effect, as the case of the China–Pakistan Economic Corridor shows, there will be a net outflow rather than inflow of capital.⁶

Third, much of the technology that the Chinese ship to BRI countries is old and outdated, which is another way of saying it is also polluting. While in the case of Pakistan, Chinese technology for power plants is coal-driven and actually helps reduce Pakistan's costs by cutting down its fuel imports,⁷ there is a price to be paid in terms of both pollution and water usage, in a country that is water scarce.

Fourth, Chinese projects more often than not involve Chinese labour. Such projects are executed rapidly largely because the project managers bring in experienced workers from China.⁸ This, in turn, undermines local hopes for direct employment in BRI projects.⁹ Therefore, economic prosperity, if it comes at all, will probably come only over the long term – that, too, assuming that the projects come to fruition and operate properly – and perhaps from some ancillary activities developing around the BRI projects run by locals, such as transport logistics, security services (as in Pakistan, for example), supplies to restaurants, etc.

To be fair to the Chinese, the African experience has been that the longer a Chinese company stayed in a country, the greater the proportion of local labour employed, because the latter would, over time, be trained to operate and take up skilled work and responsibilities in the company.¹⁰ However, more recent anecdotal evidence from Africa suggests that ever since the BRI came into effect, Chinese companies have “clammed up” in respect of offering news or details of their projects and work.¹¹ This might, then, indicate that given the drive to create “national champions” (i.e. Chinese enterprises that are at the top of the field domestically and then promoted to achieve the same abroad) and China's own political global ambitions, even this positive spinoff might soon disappear.

Fifth, – and related to the fourth point – the lack of transparency in respect of details of China's BRI projects does not lend itself to creating confidence in quality control, financial accountability or environmental accountability in host countries – unless, of course, China is able to influence the media, or operates in countries where it has good ties with the local ruling and political elites who can control the media. Where China has operated large BRI projects in countries with democratically elected governments, an independent media, or some reasonable quality of parliamentary oversight as in Sri Lanka, Nepal or Pakistan, BRI projects have been objected to or even cancelled as more exact details came to light (further details follow).

Sixth, in many instances, the quality of Chinese infrastructure and equipment is poor, generating complaints and concerns in the BRI host nations.¹² This poor quality of Chinese infrastructure adds costs, especially over the longer term, to what might in the immediate present appear to be cheap or worthwhile projects.

Seventh, Chinese BRI projects are infused with a heavy dose of propaganda, which makes their political objectives – viz. countering US influence and power, and pre-empting potential challengers to China’s rise and hegemony – markedly clear. Of particular concern for India, and many Asian nations, too, is the fact that the Chinese narrative on the “new Silk Road[s]” is based on false interpretations of history, and on denigrating or dismissing the contributions of other peoples and civilisations.¹³

While by no means purporting to be a complete account of the nature of the Chinese model of physical connectivity projects under the BRI,¹⁴ the foregoing aspects certainly constitute some of its most prominent features.

While it is inconceivable that politicians in BRI host countries are completely unaware of the infirmities and consequences of Chinese projects outlined above, their acceptance of these projects is reflective of the uneven nature of economic development across the globe, of access to capital and aid, and the degree of political exclusion that smaller, weaker countries generally suffer from within the international system. In combination, the effect of these shortcomings and inequalities is such that politicians in BRI host countries end up welcoming Chinese infrastructure development and political support, despite the costs.

Nevertheless, the financial implications of BRI projects deserve closer attention if for no other reason than the significance of their immediate impact and the near-term consequences that they generate. The following section, therefore, examines the question of Chinese financing in greater detail, with particular focus on South Asian examples.

Financial Implications

Amidst the political crisis in Maldives, brought about by the imposition of a state of emergency in the island nation, in early February, by President Abdulla Yameen, the former Maldivian president Mohamed Nasheed offered a comment on his country’s debt to China. In an interview with the Japanese news outlet Nikkei, published on February 13, 2018,¹⁵ he commented that the debt Maldives owed to China amounted to between US \$ 1.5 billion and US\$ 2 billion and that the final interest stood at more than 12% per annum. This, he said, Maldives would have to start repaying in 2019 or 2020. In Nasheed’s view this was an impossible task, since the monthly revenue of Maldives was a mere US\$ 100 million. He further stated that most of the debt was accrued on account of the building of roads and bridges, including one to Malé airport, which he described as “wasteful infrastructure development”.

Chinese Interest Rates

It is difficult to find information on the actual interest rates that China levies on its loans to other countries, and there is some doubt about whether the figures that Nasheed has quoted are, in fact, accurate. The issue might be examined from several angles.

To begin with, it has been largely – if not always – the case that the only sources (within the public domain) in respect of information on interest rates applicable to Chinese loans are the host countries of the BRI projects, and not the Chinese themselves. However, in the case of Nasheed, a genuine question can be raised about the veracity of his information, since he has been out of power for quite some time, having been deposed in a coup in

2012. That said, it is also a fact that Maldives is a small country with under 400,000 inhabitants and there are very close links between the political and governing elites, including family ties. As such, it is quite possible that Nasheed has sources amongst these elites.

Further, as a Chinese Foreign Ministry spokesperson pointed out in a press briefing, “When Mr Nasheed was the president, China also offered assistance and conducted practical cooperation with his country, which led to enormous outcomes”.¹⁶ What this implies (among other things) is that Nasheed himself has direct experience in dealing with the Chinese and their terms of contract, in which case there might well be some truth in the figures he has indicated.

Secondly, there are other examples from around South Asia where Chinese projects have racked up severe debt for the host nation. Take for instance Sri Lanka, where in 2017 the Sri Lankan government leased out its southern port of Hambantota, and also about 15,000 acres in the immediate proximity of the port for an industrial zone, to the Chinese state-run China Merchants Port Holding Company, for a period of 99 years. The deal, worth US\$ 1.1 billion,¹⁷ will help to partly repay debts to China incurred by Sri Lanka during the previous Mahinda Rajapaksa presidency. These debts, amounting to some US\$ 8 billion, were incurred on account of several large infrastructure projects such as the Norochcholai coal power plant, the Colombo Port South Terminal, the Hambantota port itself and the Colombo Port City project. In other words, China has forced Sri Lanka to surrender equity in exchange for debt relief. In this context, Nasheed’s concerns about his country are mirrored by those of the erstwhile Sri Lankan Minister for Ports, Arjuna Ranatunga, who warned that the project “could undermine national sovereignty”.¹⁸

Another example comes from Pakistan, the site of the BRI’s “flagship project”, the China–Pakistan Economic Corridor (CPEC). In March 2017, the Planning and Development Committee of the Pakistan Senate found that China was providing loans and grants for only 3–4% of the CPEC sums reported and that the terms of financing, including interest rates, were higher than what China was offering other countries like Myanmar. The Senate Committee specifically charged that Chinese banks were, in fact, levying upon Pakistan higher rates of interest than any other international bank.¹⁹ A more recent Pakistani report notes that China is extending loans to Pakistan at the London Interbank Offered Rate (LIBOR) plus 2–2.5%.²⁰ While these are considerably lower than the figures Nasheed quotes with respect to the Maldives, concerns over the incurring of unsustainable debts, owing to Chinese loans, have remained quite strong in Pakistan.²¹

Thirdly, more general inputs available on how Chinese loans work suggest that Nasheed’s figure might be correct. Japanese specialists on the Chinese economy, for instance, argue that a 12% rate of interest is possible from both financial and bureaucratic viewpoints.²²

On the financial side, if the rate of interest for a loan is normally calculated as a function of the risks involved in a particular project, then it must be acknowledged that the Maldives is risky for a number of reasons. A late 2017 Moody’s report noted that credit negative factors in the island nation included:

- (1) a meaningful deterioration in fiscal and debt metrics and worsening debt affordability;
- (2) an escalation in domestic political tensions that hinders effective policy making or undermines growth; and
- (3) a shock to the tourism sector that results in a sharp fall in growth.²³

While gross domestic product (GDP) growth has been supported by Malé's focus on large infrastructure projects, these have also increased the debt burden over the medium term. And now, with President Yameen's action, the latter two scenarios could also play out. Moreover, if the borrower cannot pay back and asks the lender for a renewal of the contract, the interest rate will rise higher still, in the fresh contract. The Chinese, therefore, seem to have anticipated a crisis in the Maldives, given their own increasing experience in other difficult parts of the world – Venezuela, for example²⁴ – and it makes sense that they are charging the high rates of interest that Nasheed claims they are.

On the bureaucratic side, it has been pointed out that Chinese banks are actually beginning to enforce stricter standards in disbursing loans. The two major Chinese banks involved in the process, the China Development Bank and the Export–Import Bank of China, have thus far employed poor methodology for loan disbursements, owing to a variety of factors.

The first of these is that Chinese banks are fairly new at the business of providing international loans, and their previous bureaucratic leaders are also not entirely qualified to deal with their tasks. Secondly, the banks could not ignore the political rationale that underpinned many of the decisions to disburse loans. Over time, however, and with growing experience, sections within the Chinese government appear to be concerned about not being seen as wasting Chinese money in risky investments in foreign countries. The higher interest rates for projects deemed risky are, possibly, the result.²⁵

Geopolitics at the Core?

Here, however, several points occur as a counter. The point about the changes within the Chinese bureaucracy is important – there seems to be a clear generation gap between the older and younger generations of Chinese bureaucrats specialised in the financial sector. But this then begs the question that if the BRI is now part of the Communist Party of China (CPC) constitution,²⁶ how is it that Chinese officials can continue to ignore what is effectively Xi Jinping's express directive to ensure the success of BRI projects? Do (Can?) officials define "success" differently from the leadership? Or does the definition of "success" include financial viability, too?

If economic profitability is going to be secondary to Chinese political necessities or foreign policy goals, as represented by BRI projects, we then come to the question of what China's true intentions are.

A point raised by a former Sri Lankan minister is germane here. Even as they were aware that Sri Lanka was going to be unable to repay the debt it was taking on for its infrastructure project, Chinese companies did not ask questions about Sri Lanka's ability to repay. Thus, according to Wijeyadasa Rajapakshe, the former Minister of Justice in the Maithripala Sirisena cabinet – sacked for his criticism of the Hambantota port lease²⁷ – Chinese intentions were never above board.²⁸

The same issue arises in the case of the Maldives. Is the real Chinese intention to ensure that the Maldives is indebted in such a way that it has to repay China by way of parting with equity? Indeed, one Indian news report has a much more cynical take on the view that Chinese bankers are now enforcing stricter conditions, suggesting in the specific context of Pakistan that this was only a Chinese stratagem to avoid criticism of the financing of its BRI projects.²⁹

Whatever Beijing's intentions, if the protests against the Hambantota deal in Sri Lanka are any indication,³⁰ then China either completely lacks the ability to anticipate potential risks or has extraordinary confidence in its ability to deal with the consequences.

It would seem that the Chinese have moved away from their traditional approach to foreign aid and, indeed, from their ubiquitous rhetoric of “win-win” relationships, to the other extreme of looking at economic investments in poorer countries only from the point of view of their own interests. From the point of view of the receiving country, however, such Chinese projects with exorbitant rates of interest – even if they come in areas where nobody else is willing to offer them loans – are hugely problematic deals that send the receiving country down a debt spiral and create huge resentment against China where none existed previously.

It could be argued that the Chinese banks and enterprises are not taking into account geopolitical considerations. What if the receiving country decides it does not want a Chinese loan and realises that the Chinese are just as greedy as Western donors or institutions?

This has already happened in India's neighbourhood. Three instances should suffice to illustrate the point being made.

In November 2017, Nepal terminated its Memorandum of Understanding (MoU) with the China Gezhouba Group Corp (CGGC) for the joint construction of the 1200 MW (US \$ 2.5 billion) Budhigandaki Hydroelectric Project, with the then Nepalese Deputy Prime Minister and Energy Minister Kamal Thapa declaring the agreement was “marred by irregularities” and, therefore, rejected by a parliamentary committee.³¹ Gezhouba, meanwhile, has defended itself³² while a Chinese news report has speculated that Nepal acted under Indian pressure.³³

Even in Pakistan, just a few days after the Nepalese decision, the government in Islamabad felt compelled to turn down the idea of including the Diamer-Bhasha dam, in Pakistan-occupied Gilgit-Baltistan, within the ambit of the CPEC, because as its Water and Power Development Authority chairman, Muzammil Hussain, put it, China's conditions for funding were “not doable and against our interests.”³⁴

Last but not least, in January 2018, the Bangladesh government cancelled the Dhaka-Sylhet road expansion project that had been awarded to the China Harbour Engineering Company Ltd (CHEC) and, in fact, blacklisted the company for bribing a Bangladesh official. CHEC is a key actor in China's BRI projects elsewhere and, what is more, this was not the first instance of the company attempting bribery in Bangladesh.³⁵

Conclusion

We would thus appear to have a situation where while there is significant geopolitical intent in Beijing's infrastructure-development projects under the BRI, the complexities of both the global environment and China's own domestic situation mean that China is still “crossing the river by feeling the stones”.

Nevertheless, Chinese confidence in pushing their BRI projects, despite the many problems that have been highlighted, might stem from the fact that Western – and Indian – institutions are bound by practices of development assistance and considerations that are not adequately sensitive to the interests of and conditions in the poorer countries, which require such assistance in the form of infrastructure development, or other public goods

such as health or education. Many BRI host countries thus accept Chinese projects and development largesse simply because they lack alternatives.

It is not the point here that good governance and accountability are not necessary, but rather that democracies have, despite their rhetoric, failed to provide acceptable or feasible alternatives to poorer countries in Asia and elsewhere, which are now being targeted by China's BRI. In fact, it might even be too late, in some instances. Pakistan, for example, in February 2018, turned down a Japanese offer for a loan to a CPEC project even though it was cheaper than that being offered by the Chinese.³⁶

While India has long held that there is an infrastructure gap in Asia that needed to be filled and has been at the forefront of transnational connectivity projects since well before the BRI came on the scene,³⁷ its big problem has simply been the inability to "walk the talk". In other words, New Delhi is seldom able to follow up its grand projects with timely implementation. It is also unlikely that the West can be expected to come to the aid of Asian and other Third World nations for long, given their own economic problems and evolving domestic dynamics, including, in many cases, an inward-looking turn.

Therefore, it is only India that has the potential to effectively challenge China by helping erase development and technological deficits in poorer countries while simultaneously ensuring democratic accountability. However, for this to happen, India must seriously reconsider its own systems of governance and foreign policy doctrines, including what its ambitions are, for both its own people and the rest of the world. Such introspection might well reveal that in these respects, India does not hold itself up to the high standards enshrined in its own constitution. By way of contrast, while China might be an authoritarian state, those doing business with it through the BRI apparently have no illusions as to its intentions. With India, on the other hand, the same countries have higher expectations given its identity as a democratic, liberal republic. When India falls short, therefore, the disappointment of its neighbours and countries farther afield is all the greater.

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