

Policy Brief

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BRI: Current Status, Lending Terms and Issues

A. Introduction and Background

The Belt and Road Initiative (BRI) is a debated topic with strong opinions on both sides. Western countries often focus on the potential downsides of BRI, while China emphasizes its goals and potential benefits. Nepal signed a BRI agreement in 2017 but hasn't made much progress yet. There's a lack of understanding about BRI within Nepal, even among many policymakers.

To best participate in BRI, Nepal needs to be aware of its advantages and disadvantages, the different ways BRI projects can be implemented, and how to negotiate deals that benefit Nepal's democracy and development.

This report, based on review of literature and interviews with Nepali experts, offers information on the global status, trends, and ongoing issues surrounding BRI to help Nepal approach the initiative in a well-informed way.

B. BRI and its Status

According to the State Council Information Office of PRC, BRI is “the Silk Road Economic Belt and the 21st Century Maritime Silk Road proposed by Chinese President Xi Jinping in 2013.” The initiative aims at promoting five pillars, namely, “policy coordination, facilities connectivity, unimpeded trade, financial integration and people-to-people bond in the international community [1].” So far, more than 150 countries and over 30 international organizations have signed Belt and Road cooperation agreements.

During the third Belt and Road Forum in 2023, Chinese President Xi Jinping outlined “eight major steps” to support BRI [2]:

- building a multidimensional Belt and Road connectivity network,
- supporting an open world economy,
- carrying out practical cooperation,
- promoting green development,
- advancing scientific and technological innovation,
- supporting people-to-people exchanges,
- promoting integrity-based Belt and Road cooperation, and
- strengthening institutional building for international Belt and Road cooperation.

Xi also said “small yet smart” livelihood projects will be carried out along with big signature projects. For this, the two Chinese policy banks would finance about USD 48.75 billion and about USD 11 billion would be financed through the Silk Road Fund [3].

World’s largest creditor

China has always been an active international lender (since the foundation of PRC in 1949), although there was a slowdown from the 1970s to 2000. Recipients of Chinese official finance are close to that of the US. In terms of the total amount, China is now the world’s largest creditor.

A decade after its launch, the Belt and Road Initiative (BRI) has surpassed USD 1 trillion in total engagement. This includes USD 634 billion (60%) in construction contracts and USD 419 billion (40%) in investments. In 2023, there were 212 deals worth USD 92.4 billion, an increase of 22% from 2022 [4].

Currently, China is the world’s single largest source of international development finance; its aid and credit (ODA and OOF) commitments to low and middle income countries (LMICs) are around USD 80 billion a year [5]. The USA and the G7 have ramped up their development financing in recent years. The US now provides about USD 60 billion to LMICs, but G7’s ability to compete with China in the long term is uncertain [6].

Growing investments and private sector involvement

While the average deal size of investments is growing, the deal sizes of construction projects is getting smaller. Experts believe the emphasis on “smaller or beautiful” projects and the sovereign debt risk management strategies explain this shift [7]. While most of the investments involve China’s private sector, construction involves China’s SOEs.

In 2023, China’s private enterprises were bigger players than Chinese SoEs. Among the major players for BRI investments in 2023 were—contrary to most years before—not exclusively Chinese SOEs, but private enterprises [8].

Revamped BRI

In recent years, China has suffered more soft-power setbacks than gains compared to the US [9]. However, China actively seeks to establish its reputation where opportunities arise [10]. China is taking several measures to reduce its exposure to debt distress in the developing world:

- ramping up RMB denominated emergency rescue lending;
- using state-owned commercial banks (eg, ICBC and Bank of China) in place of policy banks (C-Exim and CDB), which are exposed [11];
- outsourcing risk management to Western financial institutions;
- putting in place stringent safeguards [12];
- stronger penalties for late repayments (currently around 8.7% interest).

BRI projects on loan and grants are implemented very quickly—the average time is 3 years. AidData’s study also shows that after 2018, China has put strong ESG safeguards in place; about 57% of projects in LMICs have strong ESG safeguards in place, at least on paper and they do not need longer time to complete [13].

Types of Chinese loans

Chinese official loans are of three types:

1. Highly Concessional loans: These loans are interest-free and highly concessional with zero interest rate, 20-year maturity and 10 year grace period. These loans are provided by China’s central government or Ministry of Commerce, which oversees foreign aid. These loans constitute only about 0.5% of China’s official foreign lending.

2. Concessional loans and credits: China Export-Import Bank provides Concessional Government Loans and Preferential Export Buyer Credits. They are subsidized and carry interest rates of 2 to 3%, 20 year maturity, and a 5 year grace period. Until 2017, they constituted about 15 % of all Chinese commitments.

In low income countries China’s loans typically have interest rates of 2 to 3%. This is in contrast to the typical low income developing countries (LIDC) loans or grants by multilateral creditors, which tend to be interest-free. Chinese official loans to emerging markets and middle-income countries are about 7%.

3. Commercial Loans: They are provided by China Export-Import Bank, China Development Bank and state owned commercial banks and enterprises. They carry an interest rate of 5%, the maturity period is 13 years, and the grace period is 4 years. More than two-thirds of Chinese loans are of this type.

C. Issues

China’s grant giving and lending activities to low and middle income countries is not transparent, so it is difficult to analyze the costs and benefits of participating in BRI [14]. Some of the major issues associated with BRI are:

- Debt (debt-to-GDP ratios, and balance of payments crises, hidden contingent liabilities)
- Poor return on investment
- Threats to land and livelihoods of indigenous communities
- Impact on environment
- Setbacks due to poor quality of construction
- Chinese workers and subcontractors displacing local supply
- Beijing’s bailout conditions are tougher than that of IMF, therefore BRI countries are opting for bailouts from the IMF rather than China

Perception

Globally, China is perceived as the most active development partner and has been the number one partner of choice in infrastructure development, while the US is perceived as the partner of choice, by a large margin, in environment, social sectors and governance [15].

Benefits of Chinese finance were perceived to be fewer conditions, more favourable financial terms, greater alignment with national priorities and fewer delays. The disadvantages were considered to be lack of transparency, less transfer of capacity to local partners, and lower quality [16].

Experience in Southeast Asia

Southeast Asian countries' experience with BRI has been largely positive, with a few exceptions like the Philippines. However, there have been persistent concerns about financial viability, impact on environment, society and governance, including transparency and accountability. In many countries, BRI has helped buttress the political legitimacy of governments but potential risks, including reputational risks, of BRI continue [17].

BRI as a strategy?

Bennon and Fukuyama (2023) argue that China's initial BRI motivations are to [18]:

- Help Chinese companies make money abroad,
- Keep China's construction sector afloat,
- Preserve the jobs of Chinese workers, and
- Achieve foreign policy and security goals, including gaining political influences, and in some cases, securing access to strategic facilities.

In South East Asia, actual Chinese investments and contracts have receded gradually since 2018, but Chinese commitments remain substantial (eg, more than USD 20 billion in 2023) [19].

Although BRI is touted as a strategic plan, according to *The Economist*, "no grand plan is apparent" and Chinese SoEs and private sector are rushing to make money [20]. Despite mixed results, ASEAN countries continue to better negotiate with and court China [21].

China normally invests in projects that have financial viability. The only exceptions are the two strategic sectors: transport infrastructure (strategic rail and road links) and resource backed deals (oil, gas pipelines) [22].

Security Focus?

According to an IISS assessment, BRI investments have slowed down since 2018, allowing space for Western alternatives. In recent years, the assessment claims, China's strategic interests (and thus its BRI focus), has shifted to South East Asia and South Asia, and from hard infrastructure to digital infrastructure. Another important trend is towards an attempt to promote "Chinese-centric norms of security, development and digital governance." It implies that China may seek to convert BRI into "useful influence [23]."

BRI's success in South Asia, as a project of connectivity, depends on India's "acquiescence," which is unlikely in the short term. Some scholars argue that since the US "cannot match the investment and infrastructure scale of the BRI," it should support India-led BRI alternatives, help reduce risks of BRI, and promote a stable South Asia.

Debt distress and overhangs

BRI has led to concerns about not only "debt trap diplomacy" but also "debt overhangs" or the inability of countries to service existing loans and secure financing for future projects [24]. By the end of 2021, China had to carry out 128 rescue operations in 22 countries worth USD 240 billion (USD 185 billion from 2016-2021). By 2022, about 60 percent of China's overseas lending portfolio supported countries in distress. However, most of these "bailout operations" were kept "largely out of public sight [25]."

Currently, about 80% of China's lending is to countries which are under financial distress; as a result, debt default is increasing. Similarly, the number of projects financed by China with significant environmental, social, or governmental (ESG) risk is increasing [26], forcing China to step up ESG risk mitigation efforts.

In some recent International Monetary Fund (IMF) loan agreements, countries got relief on their national debts, but their state-owned businesses still had to repay loans from the Belt and Road Initiative (BRI). According to Bennon and Fukuyama (2023):

"To avoid that dire outcome—and to avoid spending Western taxpayer dollars to service bad Chinese debts—the United States and other countries should push for broad-based reforms that would make it more difficult to take advantage of the IMF and other international financial institutions, imposing tougher criteria on countries seeking bailouts and demanding more transparency in lending from all their members, including China [27]."

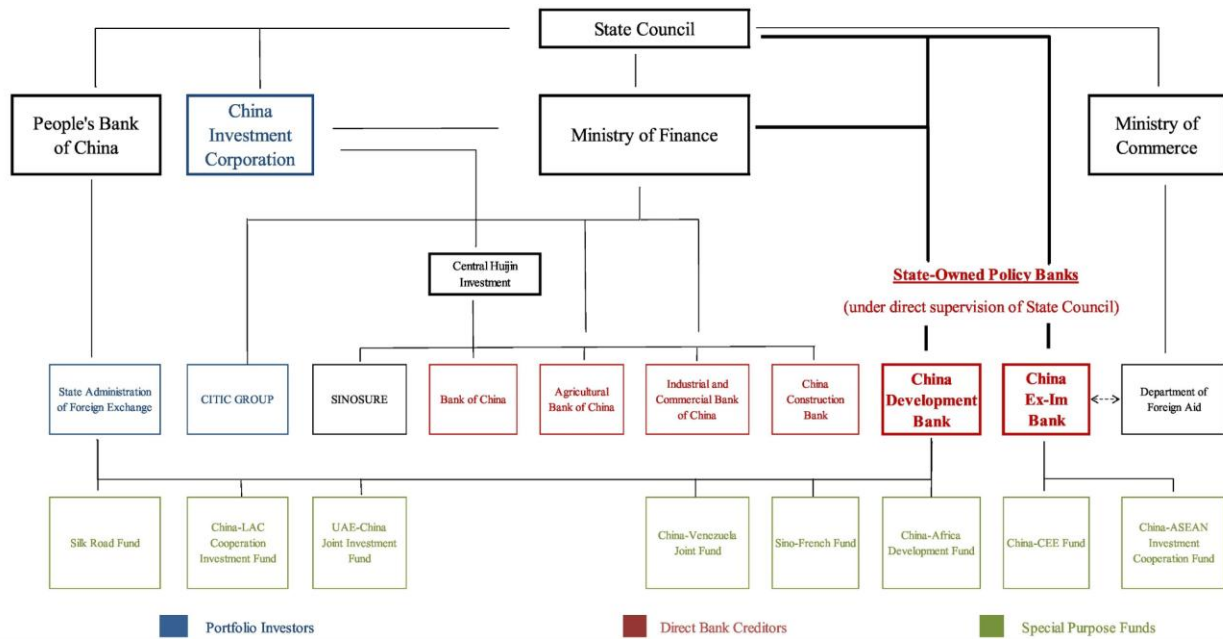
Over two dozen countries are now heavily indebted to Chinese state-owned creditors, with their debts exceeding 10% of GDP. The largest creditor is China Development Bank (CDB) followed by China Export-Import Bank (C-EXIM); they account for over 70% of China's international lending.

Debt restructuring

According to Horn et al. (2022), "defaults or restructurings of Chinese overseas debts have four key features [28]:

- They remain largely "hidden [29]."
- Chinese debt restructurings are more common than those with private lenders or Paris Club creditors.
- Restructurings with Chinese state-owned creditors often follow extended defaults and payment arrears.
- Limited debt relief from China leads to prolonged periods of high debt (debt overhang) and repeated restructurings.

Annex 1 Chinese Official Creditors



(Source: Horn et al. 2021).

Endnotes:

- [1] Xinhua (2024). *Belt and Road*. The State Council Information Office of China (SCIO).
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https://docs.aiddata.org/reports/belt-and-road-reboot/Belt_and_Road_Reboot_Full_Report.pdf.
- [6] Ibid.
- [7] Wang, C.N. (2024). China Belt and Road Initiative (BRI) Investment Report 2023 – Green Finance & Development Center. *Green Finance & Development Center*. <https://greenfdc.org/china-belt-and-road-initiative-bri-investment-report-2023/>.
- [8] Ibid.
- [9] The indicators of soft-power, in this case, being public opinion, media sentiment, and elite support.
- [10] Parks, B. C., Malik, A. A., Escobar, B., Zhang, S., Fedorochko, R., Solomon, K., Wang, F., Vlasto, L., Walsh, K. & Goodman, S. (2023). *Belt and Road Reboot: Beijing’s Bid to De-Risk Its Global Infrastructure Initiative*. Williamsburg, VA: *AidData at William & Mary*.
https://docs.aiddata.org/reports/belt-and-road-reboot/Belt_and_Road_Reboot_Full_Report.pdf.
- [11] C-Exim and CDB are currently channelizing less than 22% of lending. See Parks et al. 2023
- [12] One example of such safeguard is cash collateral and escrow accounts of borrowers, from which China can draw cash unilaterally. See Parks et al. 2023.
- [13] Parks, B. C., Malik, A. A., Escobar, B., Zhang, S., Fedorochko, R., Solomon, K., Wang, F., Vlasto, L., Walsh, K. & Goodman, S. (2023). *Belt and Road Reboot: Beijing’s Bid to De-Risk Its Global Infrastructure Initiative*. Williamsburg, VA: *AidData at William & Mary*.
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- [14] Malik, A.A., Parks, B., Russell, B., Lin, J., Walsh, K., Solomon, K., Zhang, S., Elston, T., and S. Goodman. (2021). Banking on the Belt and Road: Insights from a new global dataset of 13,427 Chinese development projects. *Williamsburg, VA: AidData at William & Mary*.
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- [16] *ibid.*
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- [20] *Ibid.*
- [21] *Ibid.*
- [22] Wang, C.N. (2024). China Belt and Road Initiative (BRI) Investment Report 2023 – Green Finance & Development Center. *Green Finance & Development Center*. <https://greenfdc.org/china-belt-and-road-initiative-bri-investment-report-2023/>.
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- [26] For example, in 2021, some 1,693 projects worth USD 470 were under ESG risk. See Parks et al.

2023

[27] Bennon, M. and Fukuyama, F. (2023). China's Road to Ruin The Real Toll of Beijing's Belt and Road. *Foreign Affairs*. <https://www.foreignaffairs.com/china/belt-road-initiative-xi-imf>.

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www.aeaweb.org/articles?id=10.1257/pandp.20221002.

[29] According to Horn et al. (2021), about 50% of Chinese loans (around 5% of GDP of recipient countries) are not reported to the World Bank (ie, are hidden) and are excluded from officially reported debt statistics. After 2016, the number of countries in default is more than 10%.

