September 2020

BRI Pulse

Turning the Tables on China??

The BRI is frequently criticized for the debt burden that it is said to inflict on the nations that host many China led BRI projects, while both Japan and the USA have complained about unfair competition in this area.

We would like to address each of these components with Q3 developments:

1. *Chinese "Debt Trap" Allegations debunked*
2. *Japan's largest single policy loan package to date to a single country*
3. *US EXIM Bank – "We have a new mandate to take on China throughout the world"*

Chinese "Debt Trap" Allegations debunked

Finally, in Q3, there were two studies released, both by Western organizations, confirming there were no signs of "debt trap" diplomacy by China along the BRI; in fact they found that in most cases the recipient country erred in its own calculations.

In July, Johns Hopkins University (USA) launched its China-Africa online/interactive database of Chinese loans into Africa (2000-2018) totalling $148 billion commitments, built by SAIS-CARI. This database also includes data from the World Bank's DSSI database (40 African countries) and the AID data (from William & Mary). This study did not produce any evidence of debt trap and found that only 3 of Africa's 54 countries have any Chinese debt issues, and only one of these is significant.
https://chinaafricaloandata.org

In August, Chatham House (UK) released a study *"Debunking the Myth of 'Debt-trap Diplomacy' How Recipient Countries Shape China's Belt and Road Initiative"*. They examined Chinese loans at selected BRI countries, which have been recipients of Chinese loans. One of its conclusions was "Malaysia has been portrayed as both a victim of China's debt-trap diplomacy and as leading a backlash against the BRI. Neither narrative is accurate".

https://www.chathamhouse.org/publication/debunking-myth-debt-trap-diplomacy-jones-hameiri

Our firm, which has been tracking Chinese policy bank loan data since 2008 globally, reached this conclusion years ago and has consistently stated this across numerous media, lectures and other presentations for the past several years.

Japan: a threatened country or a BRI beneficiary? A Bangladesh example

In early July, the financial press reported that the Bangladesh Government approached China requesting support, including financing, for a package of 9 infrastructure projects totalling $6.4 billion. This approach was made via the Investment Cooperation Working Group with China, formed in 2019.

On 12th August, Bangladesh and Japan (JICA) signed the largest-ever loan deal of $3.2 billion loans under a single package. Key loan terms were 0.65% interest rate, 20 year maturity with a 10-year grace period. Bangladesh stated that it plans to use the funds to implement seven major infrastructure projects.

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Later in August, it was reported that China agreed to a loan of circa $1 billion for the Teesta river management project (Teesta is the fourth-largest trans-boundary river in Bangladesh). As this document is written, we can find no formal confirmation of this loan facility commitment.

USA Challenges BRI: "We have a new mandate to take on China throughout the world"

Also in August, we saw the first multi-billion direct loan by the re-launched US EXIM bank. This 86 year old organisation was dormant during 2012-2016 after the US Senate failed to renew its charter in 2012. The Trump administration reconstituted the board quorum in May 2019, with the mandate to fulfil the Trump's Prosper Africa initiative, an economic effort launched in 2018 to increase two-way trade and investment between the United States and Africa. In an interview earlier this year, The President & Chairman of USA EXIM publicly stated that Africa and Sub-Saharan Africa are an absolute priority (surprising in light of Trump's prior comments on Africa countries and their leadership).

Mozambique's "tuna bond default", highly publicised within Washington DC circles during the 2018 World Bank/IMF meetings, seemed to attract investor attention to Mozambique's two major LNG discoveries (Block 1 and Block 4). In 2019, Andarko Petroleum (USA), was acquired by Occidental Petroleum (USA). As part of the transaction, Andarko, the owner of the more desirable Block 1 assets, located in the Cabo Delgado Province, sold these assets to Total (France), which in turn created a consortium; Total (26.5%), Mitsui (Japan – 20%), ENH (Mozambique – 15%), Bharat Petroleum (India – 10%), PTT (Thailand – 8.5%) and Oil India (10%). Most of the LNG developed from this operation was contracted to be purchased by Japan, India and Thailand – which represented nearly 50% of the consortium shareholders.

After previously attempted closings, in July 2020, Total announced that it had secured financing commitments of $14.9 billion, led by loans from USA EXIM ($4.7 billion), JBIC (Japan – $3 billion), Thai Eximbank ($150 million) and ADB ($400 million) as well as loan guarantees from NEXI (Italy – $2 billion), UKEF (UK – $1 billion), SACE (Italy – $950 million) ECIC (India – $850 million) and Altradius (Netherlands – $604 million). Twenty-one banks were involved in the facility.

At the time of the closing, US EXIM claimed that its $4.7 billion loan will support exports of US goods and services for the supply of American equipment that will be used for the production of LNG, add 16,700 new jobs over 9 states from 68 U.S. suppliers before any follow-on sales to lead to additional jobs growth over a 5 year construction period.

While many of the world's press have lauded the Trump Administration for its success in leading this consortium of its allies, producing new jobs for USA (and other countries) and for assisting future Mozambique GDP growth, there are large risks associated with this project. These include security risks related to growing insurgency and deaths by ISIS in Cabo Delgado. On 29th September, it was reported that the USA, in a phone call between U.S. Assistant Secretary for African Affairs Tibor Nagy and Zimbabwe Foreign Minister requested Zimbabwe's assistance in settling ISIS on this region, which is likely to be the recipient of up to $60 billion of investment, led by the USA and implicity supported by its allies.

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There are also substantial economic risks regarding Mozambique, one of the world's poorest countries, which had a 113% debt/equity ratio in 2019 (up from 54% in 2013) and which is expected to have negative GDP this year.

I am also not convinced that employees of UK companies (many of which have avoided investing in or even sending legal staff to Pakistan due to possible violence) and employees from 68 USA based companies will want to operate on a project in a region in which Mozambique's Foreign Minister has requested international military assistance to settle ISIS in the area of the project.

Did USA Beat China on winning this deal?

It is our understanding that China was well aware of the investment opportunities within both Block 1 (above) and the less attractive Block 4 – where CNPC is a minority investor with Exxon (the majority owner) for a number of years. Indeed, we believe that China met with Total (and others) experienced in developing such finds years before US EXIM involvement. It is also important to note that since 2017/ 2018 China has been focussed on funding the rapidly developing Russian LNG as part of the Arctic Silk Road (on which we published).

In 2019, three of China's major energy firms (CNPC, Sinopec and CNOOC) were merged into a new company, PipeChina, China's new state-owned pipeline operator. At the end of 2019, the Power of Siberia I pipeline, which is designed to pump 38 billion cubic metres of gas (bcm)/year from Russia to China became operational. In March 2020, President Putin approved the Power of Siberia II, which, when operational, is designed to pump up to 50bcm/yr, nearly double the volume in the original MoU, to China. In July 2020, PipeChina began construction of the southern portion of the Power of Siberia system.

The markedly above average summer temperatures across Siberia during both 2019 and 2020 have led to rapid ice melt along the Northern Sea Route (NSR), which was ice free by mid-July 2020, and thus saw substantially increased sea traffic over the past several months.

It is very clear that Russian LNG has a substantial CIF price (Cost, Insurance and Freight) advantage as well as reduced shipping risk for China, Korea and Japan, the world's three largest LNG importers – over Mozambique, Australia or USA LNG. As such, maybe what the USA (and its UK friends) really "won" by funding this project was to invest/lend $6 billion of USA and UK taxpayer monies to fund to their allies to operate in an area of growing ISIS insurgency, requesting international Government military assistance, as well as to implicitly link USA allies to the larger ($30 billion) and much more complex Block 4 project.

As we say in the banking world... it is difficult to build a profitable loan book when you are the last lender to enter a market…

The Guardian reported that UKEF's contribution involves $300 million loans to UK companies working on the project plus guarantees of UK bank loans of $850 million. In September, Friends of the Earth confirmed it was seeking a judicial review of UKEF's decision to help finance the project – to date the UKEF declined requests to make its review public.