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The Philippines in China's BRI

The Road So Far

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The shift in Philippine-China relations under President Rodrigo Duterte has resulted in numerous bilateral cooperation agreements and billions (in USD) worth of projects backed by Chinese funding. One of the major components in this rapprochement is the Philippines' participation in China's Belt and Road Initiative (BRI).

This particular development is expected to boost the country's "Build Build Build" (BBB) program, which aims to address the perennial issues of poverty, economic growth, and industrial development by increasing public spending on infrastructure, as the influx of Chinese investments will provide the necessary financial support for such an expansive domestic infrastructure project.

However, observers have raised concerns on the implications of being heavily indebted to China. Much of the speculations involve the Philippines falling into a "debt trap" or a "debt-for-equity" scenario.[2] That similar cases have occurred in Sri Lanka and in Ecuador further validate the need for a risk assessment to avoid the likelihood of the Philippines from suffering the same fate.[3]

This policy brief looks into the challenges and opportunities of the BRI for the Philippines. The following sections provide an overview of the framework within a domestic context and discuss what considerations for policymaking can be made to maximize the possible gains of the Philippines from its participation in the BRI.

Understanding the BRI

The Belt and Road Initiative ("一带一路") is regarded as "one of the most ambitious infrastructure projects ever conceived," owing to its massive geographical coverage across Asia, Africa, and Europe.[4] Launched in 2013, the BRI envisions an interconnected trading network that extends via land (the Silk Road Economic Belt) and sea (the 21st Century Maritime Silk Road). In 2018, China also announced another component to the BRI—the Polar Silk Road—which extends the network all the way to the Arctic and is expected to provide China access to energy, commercial, and geopolitical resources.[5] The BRI as a regional framework is anchored in creating a "sphere of confluence" of both "hard […] and soft infrastructure[s] through loans, grants,

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[2] Brahma Chellaney, "China's Debt-Trap Diplomacy," *Project Syndicate*, January 23, 2017, https://www.project-syndicate.org/commentary/china-one-belt-one-road-loans-debt-by-brahma-chellaney-2017-01.

[3] Kai Schultz, "Sri Lanka, Struggling With Debt, Hands a Major Port to China," *New York Times*, December 12, 2017, https://www.nytimes.com/2017/12/12/world/asia/sri-lanka-china-port.html; Nicholas Casey and Clifford Krauss, "It Doesn't Matter if Ecuador Can Afford This Dam, China Still Gets Paid," *New York Times*, December 24, 2018, https://www.nytimes.com/2018/12/24/world/americas/ecuador-china-dam.html.

[4] Andrew Chatzky and James McBride, "China's Massive Belt and Road Initiative," Council on Foreign Relations, January 28, 2020, https://www.cfr.org/backgrounder/chinas-massive-belt-and-road-initiative.

[5] Jane Nakano, "China Launches the Polar Silk Road," Center for Strategic and International Studies, February 2, 2018, https://www.csis.org/analysis/china-launches-polar-silk-road.

and investments."[6] Projects classified under the BRI receive financial support from various sources, including China's state-owned banks, commercial banks, and international multilateral banks.[7] China-backed projects can also be funded by a special Silk Road Fund,[8] by state-owned enterprises administered by the central and local governments, and by private enterprises.

A potential starting point to unpack the BRI is by looking into China's foreign policymaking process. A 2018 study on China's foreign policy suggests that the way by which the BRI operates is based on various dimensions of cooperation—policy coordination, facilities connectivity, unimpeded trade, financial integration, and people-to-people bonds—which reflect the guiding principles of China's foreign policy under Xi Jinping, such as open consultations, joint contribution, and mutual benefit.[9]

Another study posits looking at China's internal and external considerations to determine possible motivations behind the BRI.[10] Internally, the BRI can be seen as a development strategy "to empower China's less developed regions, promote Chinese industries through linkages [economic and trade cooperation agreements] with overseas markets, and tackle overcapacity issues."[11] Externally, it can be regarded as a containment strategy, or more specifically, as "a response to the 2011 US Pivot or Rebalance to Asia" by diversifying the movement of trade "to accelerate the shift in the locus of economic activity through new access routes, maximize the stakes of conflict, and offer great disincentive for military action or political disruption, whether against China or other countries in the Belt and Road region."[12]

BRI and the Philippines: The Road So Far

The Philippines is more likely to benefit from the maritime component of the BRI. Also known as the 21st Century Maritime Silk Road, this is expected to link the north and south portions of Manila in the Philippines to the provincial cities of Ningbo and Qingdao and Shanghai in China.[13] According to the Xinhua-Baltic International Shipping Centre Development Index Report, establishing a shipping network in these identified seaports is such that "the route's biggest advantage is the provision of direct services from Qingdao to Manila and rapid service from Central China to Manila."[14]

The Philippine government is positive that the country will benefit from its participation in the BRI given its congruence with the Duterte administration's BBB.[15] A report in 2019 likewise identified the Philippines—along with Pakistan, Bangladesh, and Malaysia—as the countries that are expected to gain from the BRI through "increase in investments, trade, tourism, and integration."[16]

According to the Philippine's finance department, there is "significant progress" on the ongoing China-

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6 Aaron Jed Rabena, "The Complex Interdependence of China's Belt and Road Initiative in the Philippines," *Asia and the Pacific Policy Studies* 5, no. 3 (2018): 685, https://doi.org/10.1002/app5.257.

7 China One Belt One Road Network, "问答丨"一带一路"投资生产，网友关注这些问题" [Q & A 丨 "Belt and Road" investment and production, netizens are concerned about these issues], Belt and Road Portal, July 24, 2017, https://www.yidaiyilu.gov.cn/ghsl/cjwt/55898.htm.

8 Silk Road Fund, "Overview," Silk Road Fund, http://www.silkroadfund.com.cn/enwap/27363/index.html.

9 Meiting Li, "China's Foreign Policy in Xi's Era: Change and Continuity" (UP CIDS Discussion Paper 2019-05, UP Center for Integrative and Development Studies, Quezon City, 2019); The State Council of the People's Republic of China, "Full Text: Action Plan on the Belt and Road Initiative," March 30, 2015, http://english.gov.cn/archive/publications/2015/03/30/content_281475080249035.html (inaccessible as of October 2020).

10 Rabena, "The Complex Interdependence," 685.

11 Ibid.

12 Ibid, 686.

13 Richard Ghiasy, Fei Sui, and Lora Saalman, *The 21st Century Maritime Silk Road: Security Implications and Ways Forward for the European Union* (Solna: Stockholm International Peace Research Institute and Friedrich Ebert Stiftung, 2018), http://library.fes.de/pdf-files/iez/14860.pdf; China Economic Information Service and Baltic Exchange, *Xinhua-Baltic 2018 International Shipping Centre Development Index Report*, (Beijing and London: China Economic Information Service and Baltic Exchange, 2018), https://safety4sea.com/wp-content/uploads/2018/07/Baltic-Exhchange-Xinhua-ISCD-Index-Report-2018_07-min.pdf.

14 China Economic Information Service and Baltic Exchange, *Xinhua-Baltic 2018 International Shipping Centre Development Index Report*, 65.

15 Cai Ordinario, "DOF Chief: PHL Has Everything to Gain from China's Belt and Road Initiative," *Business Mirror*, September 17, 2019, https://businessmirror.com.ph/2019/09/17/dof-chief-phl-has-everything-to-gain-from-chinas-belt-and-road-initiative/.

16 Craig Chan, Euben Paracuelles, and Sonal Varma, "The Belt and Road Initiative: Globalization, China Style," *Nomura*, April 2018, https://www.nomuraconnects.com/focused-thinking-posts/the-belt-and-road-initiative-globalisation-china-style/.

funded infrastructure projects under the BBB as of last year.[17] This includes the Binondo-Intramuros and Estrella-Pantaleon bridges, spearheaded by the Department of Public Works and Highways under a USD 63.13 million grant, and concessional loans to finance the Chico River Pump Irrigation and New Centennial Water Source–Kaliwa Dam projects worth USD 62.09 million and USD 211.21 million, respectively.[18]

The country's participation in the BRI, however, is not just limited to infrastructure development and connectivity. A 2018 study shows that both countries have also made headway on other forms of BRI cooperation.[19] There have been efforts for *policy coordination* through the signing of various agreements to "gradually harmonize mutual development goals and interests within the BRI framework" and "to facilitate business-matching activities and industrial linkages."[20] China remains *among the country's top trading and investment partners* and has benefitted both Philippine and Chinese firms.[21] In 2018, the Philippine Central Bank launched the peso-yuan spot market to facilitate *financial integration* by lowering the transaction costs of doing business between Philippine and Chinese banks; while Chinese tourists have been granted visa-upon-arrival in the Philippines to promote *people-to-people exchange* between the two countries.[22]

Opportunities and Challenges

Given its massive scope, it comes as no surprise that the Philippines' participation in the BRI has been mired with mixed views, particularly concerning its implications. The success of this regional framework is considered crucial for contributing to growth and increasing productivity. This is perhaps what makes participating in the BRI appealing for countries like the Philippines, where infrastructure deficit has stunted economic performance over the past decade.[23] The BRI also presents an opportunity for Philippine enterprises to access a bigger market and an "an expanded source of financial channels"—factors that are necessary in making a domestic economy more globally competitive.[24] Increase in Chinese investments for large-scale infrastructure projects under the BBB was expected to create around two million jobs, especially in the construction industry.[25]

Turning all these opportunities into concrete outcomes is not without its potential risks and controversies. Speculations of the Philippines at risk of falling into a "debt trap" emerged as loans from China to fund major projects under the BBB continue to add to the country's national debt.[26] The ambiguity, lack of transparency, and/or inaccessibility of the fine print involving BRI-related or Chinese-funded projects only serve to fuel doubts that the Philippines may have entered into agreements with unfavorable terms.[27]

The Duterte administration has conducted a review of its infrastructure projects in late 2019 in a move to shift against reliance from foreign loans by encouraging public private partnerships.[28] Two China-funded deals were reportedly "shelved" from the new list, though the Philippine government

17 Department of Finance, "Dominguez Cites Significant Progress in China-funded Infra Projects," March 20, 2019, https://www.dof.gov.ph/index.php/dominguez-cites-significant-progress-in-china-funded-infra-projects/.

18 Ibid.

19 Rabena, "The Complex Interdependence," 689.

20 Ibid.

21 Ibid.

22 Daxim Lucas, "Yuan-Peso Trade Platform Launched," *Philippine Daily Inquirer*, October 30, 2018, https://business.inquirer.net/259764/yuan-peso-trade-platform-launched; Rabena, "The Complex Interdependence," 692.

23 Yuwa Hedrick-Wong, "Philippines' Richest 2019: Chinese Infrastructure Investments Could Inject Much-Needed Growth," *Forbes*, September 25, 2019, https://www.forbes.com/sites/yuwahedrickwong/2019/09/25/philippines-richest-2019-chinese-infrastructure-investments-could-inject-much-needed-growth/#41529f3b25fa.

24 Rabena, "The Complex Interdependence," 689.

25 Ibid.

26 Anders Corr, "New Philippine Debt of $167 Billion Could Balloon to $452 Billion: China Will Benefit," *Forbes*, May 13, 2017, https://www.forbes.com/sites/anderscorr/2017/05/13/new-philippine-debt-of-167-billion-could-balloon-to-452-billion-china-will-benefit/.

27 Kenneth Cardenas, "Duterte's China Deals, Dissected," *ABS-CBN News*, May 8, 2017, https://news.abs-cbn.com/focus/05/08/17/dutertes-china-deals-dissected; Siegfrid Alegado and Ditas B. Lopez, "Philippines Looks to Calm Growing Fears of a China Debt Trap," *Bloomberg*, March 27, 2019, https://www.bloomberg.com/news/articles/2019-03-27/philippines-looks-to-calm-growing-fears-of-a-china-debt-trap.

28 Cliff Venzon, "Duterte Shelves Chinese Projects But Still Pushes 'Build, Build, Build,'" *Nikkei Asian Review*, November 15, 2019, https://asia.nikkei.com/Economy/Duterte-shelves-Chinese-projects-but-still-pushes-Build-Build-Build/.

remains optimistic that these "could [still] be pursued sometime in the future."[29]

A recent study on the expansion of Chinese investments in the Philippines also warned against the "dark side" of Chinese capital as it "bypasses and transforms preexisting procedures, concentrates profits in specific groups, and strengthens existing and generates new patronage networks."[30] This "corrosive" aspect is evident in the surge of Philippine offshore gambling operators (POGOs), where many Chinese workers are employed to cater to Chinese offshore gamers.[31] "The gambling industry, for instance, preys on innocent recruits and thus encourages the migration of illegal workers. [It] is also not taxable, as these gaming companies are, on paper, based in another country, allowing them to escape taxes on goods and services, the 5-percent franchise tax, among others, resulting in as much as Php 3 billion in lost revenues each month."[32] An official from the Bureau of Internal Revenue has confirmed in a Senate Labor Committee hearing that majority of licensed POGOs have failed to remit their withholding income and franchise taxes in 2019—resulting in an estimated loss of Php 50 billion in government revenue.[33]

Key Insights for Policy Development

While there is no question with regard to the abundance of opportunities that the BRI offers, its caveats suggest the need to develop new strategies or rethink existing ones for the Philippines to maximize its possible gains without sacrificing its constitutional mandate to safeguard national interests.

One consideration for policy development has to do with ensuring that the Philippines is not building up more debt than it can repay. Observers have often criticized that loans from China comes with a higher interest rate—between two and three percent—compared to Japan whose rates go between 0.25 and 0.75 percent.[34] An article from the *East Asia Forum* counters that Chinese interest rates were found to "still [be] lower than commercial rates" and that "Chinese loans are more flexible and expedient than those under Western aid…can be used for riskier projects, require less scrutiny and depend on the host state's political relations with Beijing."[35] This is not to say that concerns about interest rates of such loans are not valid. On the contrary, the same article warns that these conditions can actually "perpetuate rent seeking and encourage irresponsible borrowing."[36]

In light of these scenarios, previous studies have suggested reviewing existing policies on infrastructure funding such that these mechanisms should be specifically designed to mitigate excessive debt accumulation.[37] For its part, the Philippine government has so far taken steps towards this direction and assured that financing terms with regard to Chinese funding have been reviewed by national agencies in charge appropriately.[38]

Another recommendation raised is integrating national infrastructure development projects with regional connectivity programs, particularly for plans on ports management.[39] This involves reassessing priority infrastructure projects outside simply catering to domestic needs; its intended impact should also be rooted in reaping long-term benefits and establishing

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29 Ibid.

30 Stratbase ADR Institute, "Chinese Investment Surge: Caution on the Dark Side," Stratbase ADR Institute, March 19, 2019, https://adrinstitute.org/2019/03/19/chinese-investment-surge-caution-on-the-dark-side/.

31 Ibid.; Ralf Rivas, "How China's online gambling addiction is reshaping Manila," *Rappler*, October 9, 2018, https://www.rappler.com/newsbreak/in-depth/212443-how-china-online-gambling-addiction-reshaping-manila.

32 Stratbase ADR Institute, "Chinese Investment Surge."

33 Christia Marie Ramos, "Majority of Licensed Pogos Failed to Pay P50B in Taxes in 2019—BIR Official," *Inquirer.net*, February 11, 2020, https://newsinfo.inquirer.net/1227277/majority-of-licensed-pogos-failed-to-pay-p50b-in-taxes-in-2019-bir-official.

34 Alito L. Malinao, "Beware Those Chinese Loans to PH" (Commentary), *Inquirer.net*, August 4, 2018, https://opinion.inquirer.net/115119/beware-chinese-loans-ph.

35 Alvin Camba and Kuek Jia Yao, "China's Belt and Road Initiative Paved with Risk and Red Herrings," *East Asia Forum*, June 26, 2018, https://www.eastasiaforum.org/2018/06/26/chinas-belt-and-road-initiative-paved-with-risk-and-red-herrings/.

36 Ibid.

37 Darlene V. Estrada, "China's Belt and Road Initiative: Implications for the Philippines," *FSI Insights* 5, no. 3 (March), http://www.fsi.gov.ph/chinas-belt-and-road-initiative-implications-for-the-philippines/.

38 *CNN Philippines*, "Malacañang Denies That Chinese Loans Have High Interest," March 3, 2019, https://cnnphilippines.com/news/2019/03/02/Malacanang-Chinese-loans-high-interest.html.

39 Raphael P.M. Lotilla, "Policy Suggestions on Ensuring the Sustainability of the Belt and Road Initiative," Powerpoint presentation, Philippine Institute for Development Studies, https://pidswebs.pids.gov.ph/CDN/OUTREACH/maritime_beltroad_ppt-pids-1.pdf.

a wider network that would encourage better movement of goods and services at a regional level.[40]

The increasing presence of POGOs, meanwhile, has emphasized the need to rethink existing policies or to create new ones that would better regulate their business operations, including mandates that specifically cover taxation and labor and employment, among others.

As with any national modernization agenda, observing a transparent and participatory process is crucial to ensure accountability in the planning and execution of projects—both from the part of domestic and international stakeholders. This especially considers the opportunities and risks involved in a program as massive as this administration's BBB. That uncertainties about China's intentions remain prevalent among Filipinos only underscore the need to define explicitly and to discuss more openly the technicalities and nuances surrounding the Philippines' participation in the BRI.[41]

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[40] Ibid.

[41] *Philippine Daily Inquirer*, "44% of Pinoys Doubt China's Intentions for PH," April 7, 2019, https://newsinfo.inquirer.net/1104012/44-of-pinoys-doubt-chinas-intentions-for-ph.

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