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More Chinese loans to Pacific islands but no debt forgiveness

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Earlier this week, Chinese Vice Premier Wang Yang pledged increased assistance to eight Pacific island countries at the 2nd China-Pacific Islands Countries Economic Development and Cooperation Forum in Guangzhou. There were similarities with the first such forum held seven years ago in Nadi, Fiji. Both forums were attended by leaders from China and the Pacific. Both saw a commitment by China to increase trade and share expertise in areas such as healthcare, education, tourism and disaster relief. And both meetings saw a substantial commitment to provide financing to the region.

The most significant outcome of the forum was the announcement of up to US\$1 billion in concessional finance, to be provided over four years. This substantial figure builds on Premier Wen Jiabao's commitment at the 2006 forum to provide US\$492 million (RMB 3 billion) in concessional finance to Pacific island countries. The Chinese government has stated that these new loans will be used to 'fund big productive, infrastructure and public welfare projects'. This is a broad ambit, to say the least, and raises questions about what exactly such loans will be used for.

The lack of detail about these loans is consistent with previous Chinese assistance to the region. In the past, even loan contracts between Pacific island countries and the Export-Import Bank of China (Exim Bank) have been vague, stating that disputes are to be settled in 'a friendly manner' without providing details normally included in loan agreements.

The same approach for these new loans can probably be expected. Exim Bank loans to the Pacific have been used to fund both productive as well as less-productive infrastructure, ranging from investment in rural roads to grandiose government buildings. There has typically been limited economic analysis of such projects. Funding of ongoing costs related to operation and maintenance of infrastructure has also not been considered, resulting in the rapid deterioration of some infrastructure.

The controversial nature of some past loans in the Pacific highlights a key challenge for China. The Chinese aid program is avowedly apolitical, and is often said to reflect the wishes of Pacific island governments. However, government priorities are by their very nature political. Loans can become controversial as a result. This was evident recently in Vanuatu, when a new government sought to modify the previous government's request for China to fund the Pacific's largest convention centre. Similarly in Tonga, the use of an Exim Bank loan to fund an extension of the Royal Palace resulted in considerable criticism. The loan had been approved by parliament for reconstruction work in Nuku'alofa.

Also significant at the China-Pacific Forum is what was not announced. A number of Pacific island delegates attended with an expectation that debt forgiveness would be on the table. It was not. In fact, debt was the elephant in the room at the forum. Several Pacific island governments are struggling with record debt, and

have established 'no new loans policies' to deal with the issue (see budget statements for [Tonga](#) and [Samoa](#)). In the case of Tonga, Exim Bank loans account for 64 per cent of its external debt stock, which is 39 per cent of GDP. For such countries, there will be no benefit from the new loans announced by China. Indeed, whether the full amount of US\$1 billion will ever actually be lent is questionable, given limited absorptive capacity in the region.

The failure to discuss debt at the China-Pacific Forum represents a missed opportunity. It makes planning difficult for Pacific island governments with high debt levels. In Tonga, repayments of Exim Bank loans were to have begun this financial year, and would have costed over 17 per cent of government revenue in 2014–15. China has agreed to defer repayments, but for only five years, and the maturity of the loans will not change. This means that repayments will be larger still when they start in 2018.

In other countries, the issue of debt is likely to become increasingly important as up to US\$1 billion in concessional finance is made available. There are likely to be more and more calls for debt relief, mirroring what has occurred recently in Tonga (and as raised by this [paper](#) from the [Pacific Institute of Public Policy](#)). Like it or not, the Chinese government will be forced to address such issues in the coming years. It could make a start now by being more proactive in ensuring that agents such as Exim Bank lend responsibly and operate transparently. For their part, Pacific island governments will need to be cautious when taking on new debt.

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