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Philippine-China Relations and China's Belt and Road Initiative*

Introduction

In 2013, President Xi Jinping announced the Belt and Road Initiative (BRI), which aims to centralize Chinese capital in the hands of the Chinese Communist Party (CCP), expanding trade, infrastructure, and connectivity of East-Southeast Asia, sub-Saharan Africa, and Europe.[1] The BRI's emergence initiates one of the most crucial debates in development studies in decades: Is China the savior of, or the new colonizer in, the developing world?

In the Philippines, previous executives were constrained by domestic politics or foreign policy positions. During Gloria Macapagal-Arroyo's administration (2001-2010), the Philippines and China embarked on a joint maritime venture in the South China Sea and expanded political-economic relations. But despite growing political ties with Beijing, Arroyo's administration eventually canceled the two biggest Chinese foreign direct investment (FDI) projects – the Northrail and ZTE Corporation's proposed National Broadband Network.

Approximately 20 other projects were canceled. Similarly, tense bilateral relations under former President Benigno S. Aquino III (2010-2016) explain the absence of major Chinese official development assistance (ODA) and development finance projects during his administration. At the start of Aquino's term, Chinese foreign investment was targeted to fund

* Paper based on a presentation given at the "Forum on Philippines-China Relations: Geopolitical Perspectives and Realities," organized by the Philippine Association for Chinese Studies (PACS) and the Department of International Studies, Miriam College and held at the Little Theater, Miriam College, Quezon City on November 8, 2018.

[1] O'neill, Daniel. (2018). *Dividing ASEAN and Conquering the South China Sea: China's Financial Power Projection.* Hong Kong: Hong Kong University Press.

more than 10 major investment and aid projects. Aquino himself visited Beijing in 2011 and acquired the commitment of the Chinese government to provide more US$13 billion worth of aid and investments.

However, the Scarborough Shoal issue led to the triumph of an anti-China coalition in Aquino's own cabinet, which limited Chinese development finance and loans in the Philippines. In contrast, President Rodrigo Duterte's presidency opened the country to a greater amount and scope of funding from the BRI. His 2016 visit to China brought an earmarked $24 billion worth of Chinese FDI and ODA for the Philippines.

This essay explains what China's Belt and Road means to the Philippines. It argues that the Belt and Road cannot be fully understood using the lens of geopolitics, which paints BRI as a security threat or as China's benevolent gift to the developing world. Rather, the BRI enables host countries to borrow foreign capital to fund infrastructural development, which is crucial to build up a country's productive base and pursue medium to long-term economic strategy. The BRI's success or failure is not predetermined but depends on host country features.

The paper is structured as follows. First, it will discuss the dominant interpretations of the Belt and Road in the policy and media circles. These interpretations could simply be narrowed down to the hawkish and benign interpretations of the BRI, which are limiting and tend to obfuscate more important issues. Second, this paper points to five key nuances that both interpretations understate in their analysis: host state features, elite politics, multiple Chinese actors, relative autonomy of the SOEs, and host state actors. And finally, the paper discusses how the Belt and Road is an opportunity for the Philippines to expand infrastructure spending on key projects that have been ignored by multilateral development banks (MDBs) or other financiers. Since the Philippines is attempting to catch up and compete with other regional competitors, acquiring funding outside the Western funders and capital markets can better enable the Philippines to compete in the 21st century.

Dominant Interpretations of the Belt and Road

There are two dominant interpretations of Belt and Road. On one hand, security studies and foreign policy think tanks situate the BRI within China's geopolitical ambitions, often linking the Communist Party's strong political and financial hold over Chinese state-oriented enterprises and the high interest rates of Chinese policy banks to the "debt trap." From Patrick Mendis and Joey Wang's "soft budget constraints,"[2] to Deepak Lal's grim assessment of the developing world.[3] While some concerns merit consideration, more popular ones tend to be exaggerations or distortions built upon stereotypes of China. Such depictions draw attention away from the actual limitations of BRI, which the paper enumerates below.

In their views, Chinese economic capital – FDI, development finance, and other forms of official finance – is inherently tied to economic statecraft and security issues. These views carry over to Western news outlets which often treat China as a corruption-inducing and resource-seeking player. For instance, the *New York Times* reported that "China is worsening the climate crisis" by funding 50 new coal plants across Africa. These cases, wherein reporters typically misinterpret and sensationalize the data, are common among major newspapers, which show how Western media tend to be unfair in getting the empirics right and capitalizing on historically entrenched stereotypes to unfairly describe China and the developing world.

This is not to say that the Belt and Road is without any project problems. China has relied on importing massive inputs of resources to fuel its manufacturing economy.[4] In the early 1990s, Chinese FDI and development finance targeted these natural resources in the developing world, propagating deindustrialization, natural resource dependency, and socio-environmental disruptions in the developing world.[5] Furthermore, Chinese engagements generated political and security concessions for Beijing, such as recognizing the One-China Policy, votes in the United Nations on human rights or multilateral interventions, or support against The Hague arbitration's ruling on the South China Sea.

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[2] Mendis. Patrick, and Wang, Joey. (2018). "Belt and road, or a Chinese dream for the return of tributary states? Sri Lanka offers a cautionary tale." *South China Morning Post.* Retrieved on October 24, 2018 from https://www.scmp.com/comment/insight-opinion/article/2127415/belt-and-road-or-chinese-dream-return-tributary-states-sri.

[3] Lal, Deepak. (2018). "Beijing is creating debt traps to turn countries into vassal states." *The Nassau Institute.* Retrieved on October 24, 2018 from https://www.nassauinstitute.org/chinas-belt-and-road-initiative-is-becoming-a-massive-debt-trap.

[4] Ho-Fung Hung. (2015). *The China Boom: Why China Will Not Rule the World.* New York: Columbia University Press.

[5] Gallagher, Kevin, and Porzecanski, Roberto. (2010). *The Dragon in the Room: China and the Future of Latin American Industrialization.* Stanford: Stanford University Press. Retrieved from https://www.sup.org/books/title/?id=20122.

On the other, the Chinese state, pro-China think tanks, and media organizations portray the Belt and Road in a completely positive light,[6] ignoring the negative socio-environmental disruptions and potential negative spillovers. They have painted BRI as completely benign since as early as the Hu Jintao era. Across the world, the Chinese media apparatus, Confucius institutes, and other pro-China organizations echo these depictions. However, these depictions must coincide with China's increasingly alarming after the 2010 financial crisis, which led to the economic slowdown and the leadership transition to Xi Jinping. Indeed, since China has emerged to be an important investor and financier, new geo-economic considerations and other political considerations have exacerbated the conditions for China's foreign capital export.

Beijing altered the direction of Chinese economic capital to help rebalance from export-led manufacturing to consumption-driven growth. Chinese foreign investments, construction contracts, and development finance now target a broad portfolio of strategic and non-strategic assets across a variety of sectors. Indeed, Chinese ownership or equity can be found in ports, railways, and e-commerce across different countries. China has become less forgiving of debts and loans that developing countries accrue, which is a stark departure from its behavior in the early 2000s.

For instance, Beijing has recently decided to acquire equity returns in Sri Lanka, Djibouti, and Pakistan.[7] These actions point to the CCP's greater desire to accord political and security considerations to Chinese economic capital. As the future of US leadership in the Asia Pacific Region remains unclear under the Trump administration and with more economies relying on Chinese economic capital, the BRI appears to be a bid to compete for power and influence across a rapidly changing world.

It should be noted that BRI is not a new policy but instead evolved from China's Going Out policy. However, unlike the BRI, the Going Out Policy grew out of China's decentralized approach to the role of Chinese state

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[6] Mulvaney, Brendan S. (2015). "One Belt, One Road includes benefits for all." *People's Daily Online.* Retrieved on October 24, 2018 from http://en.people.cn/n/2015/0331/c90780-8871690.html.

[7] Camba, Alvin. (2017). "China's Port Acquisitions in Sri Lanka and Djibouti: Lessons on Chinese Development Finance for the Philippines." *Stratbase ADR Institute for International Studies.* Retrieved on October 24, 2018 from https://www.researchgate.net/publication/320170328_China's_Port_Acquisitions_in_Sri_Lanka_Djibouti_Lessons_on_Chinese_Developmental_Financing_for_the_Philippines.

oriented enterprises (SOEs) within China's own borders.[8] The Going Out policy was highly decentralized and it gave power to a variety of competing actors in China's borders.

In the early 2000s, China's inevitable economic growth and increasing welfare gains among its population led to Chinese capital exports to various destinations in the developing world. At this time, China also increasingly engaged in various overseas development assistance practices under the programs facilitated by the Chinese policy banks – the Chinese Export-Import Bank, the Chinese Development Bank, and the Big-Four Banks. China started to grant government concessionary loans, preferential buyers credited, loan interest loans, revolving credits, and aid. These grants became available not only to Chinese companies or investors seeking to profit in the developing world or enact the Chinese state's goals but also to host state companies who work with Chinese actors. In contrast, the Belt and Road concentrates the decision-making power of infrastructure in the hands of the Chinese state and the recipient government.

There is a broader context to BRI's appeal. Western development agencies increasingly began to shift their funding from infrastructure spending and economic productivity to social welfare and human component expenditure, which limited the ability of the developing world to increase their capacity in the value chain.[9] Available Western funding for infrastructure in commercial banks and other sources often require longer time horizons and demand higher interest rate payments. A comparison between China's funding and Japan is more appropriate. China's funding is more expensive than Japan in the long-term, but Japanese loans are often more expensive in the short-term due to insurance premiums.

What Explains the Impact of the Belt and Road

Dominant scholarly and policy discourses around the BRI revolve around China's security considerations and geopolitical significance. Nonetheless, the developmental impact of BRI depends on other factors which vary across different host countries.

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[8] Ho-Fung Hung. (2015). *The China Boom.* p. 187.
[9] Brautigam, Deborah. (2009). *The Dragon's Gift: The Real Story of China in Africa*. Oxford: Oxford University Press.

First, the impact of BRI's infrastructural funding and loans vary across different parts of the world. An important and often understated aspect is host state features, which would increase or decrease the risk brought by BRI's financing. These features include the credit rating of countries, currency reserves, state capacity, local politics, and social context. Indeed, the Center for Global Development published a systematic study of the BRI, arguing that 23 out of 65 countries will face debt risk due to their unfavorable host state characteristics. This more nuanced take accepts that BRI does generate risk, but the degree varies across countries and partly come from the receiving country's end.

Second, internal politics matter to the decision making and implementation of BRI projects. Project commitment and progression depend on a domineering national political elite, a "strongman," or centralized governments who are positively predisposed towards Beijing and can redirect the host state's development strategy toward BRI financing. For instance, Malaysia's Najib Razak, Philippines' Rodrigo Duterte, and Indonesia's Jokowi Widodo represent such committed national political elites. However, after project commitment, project progression, implementation, and eventual completion are shaped by the nuances of host country politics. Highly politically centralized regimes enable the strongman or national political party to close ranks, whereas more decentralized regimes constrain the strongman's ability to punish defecting local elites.

This contrast could easily be seen when Razak spearheaded the East Coast Railway's (ECRL) construction with little opposition from regional-local elites, the Sultans, or political parties.[10] In the Philippine case, Duterte's attempt to expedite the Bicol South Railway Project (South Rail) was hindered by a coalition of regional-local elites who were competing for rail station to ensure their family's dominance in the provinces for centuries to come. Understanding the nuances of the host state would unravel the determinants and actual developmental implications of BRI projects.

Third, international relations scholarship has often treated China as a unitary actor when it comes to foreign policy. While some scholars agree with the SOE's relative autonomy, they assign greater analytical weight

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[10] Hurley, John, Morris, Scott, and Portelance, Gailyn. (2018). "Examining the Debt Implications of the Belt and Road Initiative from a Policy Perspective." *Center for Global Development.* Retrieved on October 24, 2018 from https://www.cgdev.org/article/chinas-belt-and-road-initiative-heightens-debt-risks-eight-countries-points-need-better.

to the party-state because of government's guaranteed financing and political influence.[11] The CCP does have the power to appoint the leaders of the SOE, but the actual operations and direction of these companies operate with some significant degree of relative autonomy. In other words, instead of a top-down relationship between the CCP and SOEs, the actual decisions depend on negotiations, compromises, and shared governance.[12]

Indeed, it has often been argued that the CCP has the power to make major, path breaking decisions, but the actual governance of everyday operations are left to the SOEs. This argument comes from the broader literature on the political economy of Chinese development, which emphasizes decentralized governance and competing local-level actors. This characterization of a fragmented and often less coordinated Chinese state contradicts the often unitary and homogenous treatment from international relations scholarship.

Fourth, there are multiple Chinese actors engaging in the host state. There is variation among Chinese investment activity in terms of asset specificity, sectoral distribution and investment size. There is no singular characteristic "Chinese investor." Instead, there is a multiplicity of national and regional state-owned enterprises, provincial entrepreneurs and private investors. The varying histories of the host state prefigure how SOEs have entered the region. For example, China's support of numerous anti-colonial struggles during the Cold War paved the way for Beijing's strong involvement in sub-Saharan Africa. Stronger ties between the African political parties and the CCP go back to their Cold War origins. Southeast Asia's own Chinese population and the historical Kuomintang (KMT) networks have worked with PRC SOE and private capital. Indeed, PRC investments in mining and offshore gambling often have Taiwanese KMT and Macau partners.

Even illicit activities, such as smuggling of drugs in the Philippines, are not simply pushed by PRC investors but by the broader KMT networks as well. In contrast, PRC's engagement with Latin America emerged in the late 1990s. Latin America's "second stage" of neoliberalism required a massive market for natural resource export. China also became a major

[11] Shambaugh, David. (2013). *China Goes Global: The Partial Power.* Oxford: Oxford University Press.

[12] Chih-shian Liou. (2014). "Rent-seeking at home, capturing market share abroad: the domestic determinants of the transnationalization of china state construction engineering corporation." *World Development,* vol. 54, pp. 220-231.

investor of development finance and loans in Peru, Bolivia, and Brazil.

And finally, the BRI narrative understates the role of SOEs and recipient countries in shaping project outcomes. Indeed, SOEs, private Chinese firms, and host state companies matter to BRI projects. In the former, Chinese firms compete to acquire PRC financing to fund overseas projects in order to profit from the guaranteed material sourcing. For instance, a World Bank black listed Chinese company made a bid for Marawi's reconstruction and got the approval of the Philippine government. While the PRC started to limit outbound outflows without government approval and take money laundering seriously, many PRC actors still evade their country's regulation.

Patrick Ho, a member of the CEFC China Energy-backed China Energy Fund Committee, was recently arrested by the US Fedral Bureau of Investigation on charges of allegedly bribing the government officials of Chad and Uganda.[13] In the latter, regional and local firms use their national government networks to get Chinese funding. In turn, PRC partners agnostically go along with the operation. These types of cases tend to occur in countries with significant local government deregulation. These projects become overpriced, economically less viable, or at worse, can illegally operate for profit. For instance, Kenneth Cardenas (2017) argued that the initial group of Chinese consortiums that President Duterte brought have partnered up with questionable Philippine companies.[14] In these cases, both the Chinese state and host state national governments do not gain from the project's completion due to the enormous overhead costs and negative social impact.

What Does It Mean for the Philippines?

During the Aquino administration, infrastructure financing was largely conducted using the Private-Public Partnerships, which relied on

[13] Lum, Alvin. (2018). "Patrick Ho's lawyers accuse US authorities of using 'illegally' obtained evidence in charges for US$2.9 million corruption scandal." *South China Morning Post.* Retrieved on October 24, 2018 from https://www.scmp.com/news/hong-kong/law-crime/article/2142504/patrick-hos-lawyers-accuse-us-authorities-using-illegally.

[14] Cardenas, Kenneth. (2017). "Duterte's China Deals Dissected." *Philippine Center for Investigative Journalism*. Retrieved on October 24, 2018 from https://pcij.org/stories/dutertes-china-deals-dissected.

Philippine conglomerates to build, plan, and fund the project. Drawing from capital markets that experienced a huge influx of US dollars because of the US Federal Reserves' quantitative easing, the Philippine conglomerates experienced huge spurts of growth during the Aquino administration.

However, medium- to long-term planning to increase Philippine competitiveness and alleviate quality of life concerns were placed at the back burner in favor of macroeconomic stability and maintaining a positive credit grade rating. When quantitative easing ended in 2015, most of the hot money placed in Philippine conglomerates left the region in favor of the recovering American markets. These occurrences hampered Philippine development, which needed an influx of capital to facilitate infrastructural development, increase competitiveness, and diversify economy sources.

If used and facilitated correctly, the BRI can increase the competitiveness of the Philippine economy. This list of approved projects will likely be used to offset increasing shortages and sustain economic growth in the Philippines. While the Chico River Dam Project aims to supply water to 8,700 hectares of agriculture land and 4,350 farmers across 21 barangays, the Kaliwa Dam can generate 600 million liters of water per day to Metro Manila.[15] Both projects were initially proposed in the 1970s during the Marcos administration and even slated to be funded by the World Bank but ultimately shelved because of civil society and local opposition as well as the lack of urgency during those times. However, the likelihood of water defiance in Metro Manila, Bulacan, Cavite, and Tanay, and low agricultural productivity across the country, make both projects urgent in the short-term and necessary for long-term growth.

Infrastructure deficiency has also constrained economic growth and quality of life.[16] The Subic Clark Railway Project, a 70-km cargo rail, seeks to increase the movement of goods between the Subic and Clark freeports, which have been major areas of growth and employment in Northern Luzon. While the project endeavors to include transportation to Clark International Airport and then New Clark City, the initial project aims to reduce reliance on trucks and increase connectivity in the special

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[15] Cal, Ben. (2017). "P12.2-B Kaliwa Dam project to augment Metro Manila water supply." *Philippine News Agency.* Retrieved on October 24, 2018 from http://www.pna.gov.ph/articles/1053324.

[16] Chua, George. (2015). "Economic effects of traffic in Metro Manila." *BusinessMirror.* Retrieved on October 24, 2018 from https://businessmirror.com.ph/2015/03/12/economic-effects-of-traffic-in-metro-manila.

economic zones.[17] With the success of Subic Port as an alternative port of entry in the Philippines, a projected exponential growth of ship entry and traffic in the region is anticipated. As Subic and Clark have been clusters of chip assembly, import entries, and employment generation outside Metro Manila, the construction of a cargo train that increases movement and eases traffic will contribute to economic growth.

Unlike Northern Luzon, Bicol and the whole of Southern Luzon have lagged in economic development. In this context, the Chinese-funded PNR South Rail involves a highspeed rail across nine stations: Manila, Los Baños, Batangas City, Lucena, Gumaca, Naga City, Legazpi City, Sorsogon City, and Matnog. From Manila to Bicol, the reliance on bus transportation and the increasing amount of vehicle traffic in the across the provinces shows that the growing internal demand. For instance, business process outsourcing (BPO) expansion in Laguna has increased vehicular use in the province.[18] Similar issues have occurred in Southern Luzon and Bicol provinces. The China-funded bridge projects, free under the current plans, target long-term traffic and predict likely growth. While the positive impact of the two bridges on traffic is debatable,[19] analysis on current vehicle usage ignores the fact that population and vehicle growth will most likely continue for decades. In other words, acting only when the problems occur instead of meeting these challenges ahead largely contributed to traffic congestion.

Furthermore, the current composition of projects makes a debt trap unlikely. According to the current list of approved and pipeline (grant, loans) projects in the Philippines, more than half are funded by the Japanese International Corporation Agency and the Asian Development Bank (40 projects). Indeed, in the list of currently approved China projects, there are currently two China grant projects for bridges, which would be free under the scheme, and two development finance projects.

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[17] Navales, Reynaldo. (2018). "Angeles council endorses Subic-Clark Railway Project." *SunStar*. Retrieved on October 24, 2018 from https://www.sunstar.com.ph/article/1768072.

[18] Orellana, Faye. (2018). "DPWH: Brace for heavy traffic in San Pedro, Laguna with repair of bridge." *Philippine Inquirer*. Retrieved on October 24, 2018 from https://newsinfo.inquirer.net/1001073/dpwh-brace-for-heavy-traffic-in-san-pedro-laguna-with-repair-of-bridge.

[19] Schuengel, Frank. (2018). "Why rebuilding the Rockwell Bridge makes no sense." *Visor*. Retrieved on September 24, 2018 from https://visor.ph/traffic/why-rebuilding-the-rockwell-bridge-makes-no-sense.

While there are 16 more China projects in the list, two of these are the discussed train projects, some are interprovincial roads, and most are the China grant bridge projects. Some of these might not come to fruition given the difficulties of already existing projects and vetting system. Indeed, Duterte's $24 billion package in 2016, most of the FDI and aid projects were canceled because of the stringency of the bureaucracy, infighting among host state partners, or findings of feasibility studies. In sum, the Chinese-funded projects have a growing internal demand to meet, making it more likely for the Philippines to generate enough growth to pay for the project costs and sustain long-term economic development

Conclusion

This article discussed what and how BRI can help the Philippines. It suggested that geopolitics or international relations couldn't fully account for the impact of BRI. Taken from a political economy perspective, the BRI increases the options for the developing world to pursue infrastructural development. BRI can bring foreign direct investment, construction contracts, and development loans to host country projects.

The paper also argued that numerous factors have shaped China's economic capital and BRI projects, particularly host state foundations, elite politics, multiple Chinese actors, and the relative autonomy of SOEs and host state firms. The article also examined the key projects that BRI has initially targeted in the Philippines. While there are dangers and risks to the Chinese loans, these projects make sense given the Philippine economy's internal demand for services.