POLICY BRIEF

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Debt Relief with Chinese Characteristics

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POLICY POINTS

Different types of lenders provide different types of loans, and different types of debt relief.

China carefully considers requests for restructurings based on a loan-by-loan, project-by-project basis.

Chinese officials have emphasized that debt relief, including the G-20 debt service moratorium, will be negotiated bilaterally.

JOHNS HOPKINS SCHOOL of ADVANCED INTERNATIONAL STUDIES

AS THE COVID-19 CRISIS CONTINUES WORLDWIDE, African economies are facing unprecedented challenges. According to the IMF, almost 20 African countries are in debt distress or at high risk of debt distress. It is clear that another debt crisis is in the works.

In 2017, according to the World Bank's *International Debt Statistics*, China accounted for about 17 percent of African public and publicly-guaranteed debt. China has joined other G-20 countries in pledging a moratorium on principal and interest payments for 77 eligible low-income countries through 2020, but faces calls for further debt relief.

In order to shed more light on how China is likely to handle COVID-19 related debt relief beyond the moratorium, researchers at SAIS-CARI compiled and analyzed an original dataset of past Chinese debt relief actions in Africa. Between 2000 and 2019, Chinese lenders cancelled US$ 3.4 billion in loans, restructured approximately US$ 7.5 billion, and refinanced another US$ 7.5 billion.

CHINA AS A LENDER

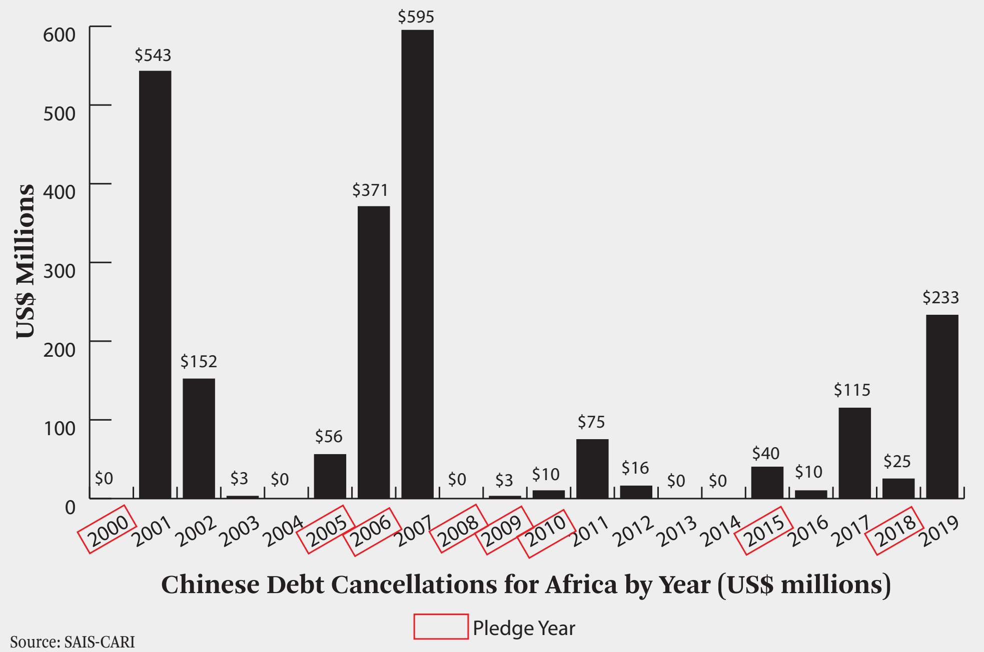
CHINA MADE ITS FIRST LOAN TO AFRICA IN 1960. The early years of China's foreign aid program included mostly grants and zero-interest loans (ZILs) from China's central government. The Export-Import Bank of China (Eximbank) was established in 1994, and began providing concessional foreign aid loans and other commercial credits in 1995. Since then, China's lending to Africa has expanded dramatically. Lenders have signed US$ 148 billion worth of loan commitments between 2000 and 2018, and include China's two policy banks (Eximbank account for US$ 86 billion; China Development Bank, US$ 37 billion), seven commercial banks, and over 20 companies.

When countries have trouble paying back their loans, China typically offers debt relief, which can take a number of forms. *Debt cancellation*, sometimes referred to as a debt "write-off," is when a debt is cancelled outright. *Debt restructuring* (including "rescheduling" and "reprofiling") is when the terms (e.g. interest rate, grace period, maturity, or various fees) related to a disbursed – or partially disbursed – loan are renegotiated. *Refinancing* can also offer debt relief: a new loan is issued to pay off an old loan, extending the amount of time a borrower has to pay the debt, possibly with a lower interest rate.

PRE-2000 DEBT RELIEF

IN THE MANY LOAN AGREEMENTS for ZILs signed in the first decades of China's foreign aid program, one can frequently find this phrase: "if there is difficulty to repay when the loan is due, the repayment period can be extended after consultation between the two governments." These discussions and extensions happened often in the ensuing decades, particularly as the African continent descended into economic crisis in the "lost decades" of the 1980s and 1990s. By one estimate, only 14 percent of these loans were ever repaid.

Figure 1: Chinese Debt Cancellations for Africa by Year



Source: SAIS-CARI

DEBT CANCELLATION

IN 2000, CHINA MADE ITS FIRST DEBT cancellation pledge, which only included African countries. Since then, China has made seven debt cancellation pledges that included African countries. China's debt cancellation pledges generally promise to cancel only the overdue part of governmental ZILs that were maturing in a particular year.

Zero-interest loans are offered by China's Ministry of Commerce (MOFCOM) as part of intergovernmental Economic and Technical Cooperation Agreements. They average about US$ 10 million per loan, and make up less than five percent of China's overall lending to Africa from 2000-2018. Importantly, the funds for zero-interest loans are accounted for in China's annual foreign aid budget rather than raised from capital markets, which means that MOFCOM does not rely on ZIL repayment to balance their books.

This, coupled with the standardized nature of ZILs, make debt cancellation negotiations relatively simple. Cancellations are negotiated bilaterally, but follow a standardized process whereby eligible countries apply, and a committee led by China's Ministry of Finance with delegates from MOFCOM then approves or rejects the cancellation request.

Between 2000 and 2019, China has cancelled at least US$ 3.4 billion of debt, almost exclusively overdue ZILs.[1] Our data includes 94 cases of debt cancellation in Africa (each case can represent multiple loans). Two thirds of these cases were from 2000-2007, with distinct peaks in 2001 and 2007. This represents the "mopping up" of old debts that had accumulated in the 1980s and 1990s. Although China never

Box 1: Debt Restructuring cases show a wide range of treatments

Treatment	Reprofiling of debt service payments within original maturity	Short Maturity Extensions (e.g. 3-7 years)	Longer Maturity Extensions (e.g. 10-20 years)	Maturity Extension and Interest Rate Reduction	Specific Details Unknown
Cases	Mozambique (2017) Cameroon (2019)	Cameroon (2002) Zimbabwe (2007, 2010, 2012) Niger (2018)	Ethiopia (2018)	Zimbabwe (2003, 2004) Seychelles (2011) ROC (2019) Djibouti (negotiations ongoing)	Benin (2004) Sudan (2012) Chad (2017) ROC (2018)

Box 2: Debt Restructuring & Refinancing - Three Key Cases

Angola	Niger	Republic of Congo
Approximately US$ 7.5 billion borrowed from China Development Bank (CDB) by Angola's state-owned company Sonangol between 2010 and 2014 was refinanced through a line of credit CDB extended to the Angolan government. Angola used US$ 10 billion from this credit line to recapitalize Sonangol, the majority of which was used to pay off the SOE's debts to CDB.	In 2008, Niger and China National Petroleum company formed a JV for the SORAZ refinery, and borrowed US$ 880 million from Eximbank (40% guaranteed by Nigerien government). After the refinery had a rocky start with slow cash flows, Niger asked for refinancing at a concessional interest rate, although this never happened. Refinery conditions improved, Niger is on schedule to repay the loan by 2023 after being granted a 4-year maturity extension in 2018.	After experiencing an economic crisis induced by the downturn in oil prices, the ROC initiated restructuring negotiations with creditors in 2017. In 2018, China Machinery Export Corporation agreed to reschedule US$ 116 million of arrears. In 2019, China Eximbank agreed to restructure US$ 1.6 billion of outstanding debt from loans signed by the ROC between 2010 and 2014, extending the maturities by 15 years and reducing the interest rates

formally coordinated its debt relief with the programs negotiated by the Paris Club, the World Bank, and the IMF, the timing of China's early 2000s cancellations roughly parallels the heavily indebted poor countries initiative (HIPC), which began in 1996 and entered a second phase in 2006.

DEBT RESTRUCTURING AND REFINANCING

AS MENTIONED IN THE PREVIOUS SECTION, cancellation-eligible ZILs make up less than five percent of China's lending to Africa. When countries seek debt relief from other types of loans, they must instead seek restructuring or refinancing. We identified 16 cases in 10 African countries where creditors worked with borrowers to restructure loans, and one case of refinancing between 2000 and 2019.

Restructured loans include commercial loans, concessional loans, export buyer's credits, and supplier's credits. Unlike small zero-interest loans, which come only from MOFCOM, these loans often involve much larger sums, and can come from a variety of sources. Concessional loans and preferential export buyer's credit are offered by China Eximbank, for example, while supplier's credits are offered by Chinese companies. Also, unlike ZILs, which are funded by the state budget, funding for bank loans is raised on debt markets, which means that creditors take a loss if they are not repaid. Commercial loans of all kinds usually require insurance from Sinosure. As a result, debt restructuring is complicated, and takes different forms depending on the lender, the type of loan, the borrower, and the related project.

In the period from 2000 to 2012, rescheduling generally involved the same relatively small debts that were characteristic of the early years of Chinese lending, averaging US$ 52 million per case (again, cases can include multiple loans). We identified nine cases of restructuring totaling US$ 415 million in five countries in this period.

After the commodity price collapse of 2015, countries' requests for restructuring have accelerated, and those that have been concluded involve far larger sums, averaging approximately US$ 1 billion per case. We identified seven cases totaling US$ 7.1 billion in six countries between 2015 and 2019. We also identified one case of refinancing in this period, which involved approximately US$ 7.5 billion worth of loans in Angola.

KEY FINDINGS & POLICY RECOMMENDATIONS

AFTER EXAMINING 94 CASES OF CANCELLATION, 16 cases of restructuring and one of refinancing between 2000 and 2019, we make the following policy recommendations:

1. Know your lenders, know your loans: Different types of lenders provide different types of loans, and different types of debt relief. MOFCOM ZILs can be cancelled, while loans from Eximbank and Chinese companies can be restructured. CDB is the only bank we have seen offer refinancing. We have seen no cases of restructuring from Chinese commercial banks. Borrowers should keep in mind that Chinese loans other than ZILs have almost never been, and likely will never be, considered for cancellation, and they should by no means see China as a "free money machine". They should be ready to negotiate separately with policy banks and with Chinese companies.

2. **Manage your expectations:** China carefully considers requests for restructurings based on a loan-by-loan, project-by-project basis. Loans for projects that face demonstrable (and reasonable) cash flow difficulties are more likely to be granted restructuring. While debt relief is a pressing issue, negotiations are complicated, and can take a long time. Most cases take at least a year to negotiate. In some cases, China Eximbank has halted disbursements on new loans during negotiations, and, like the IMF or World Bank, it has required arrears to be paid before restructuring is agreed. Furthermore, debt restructuring cases show a wide range of restructuring outcomes. The debt relief that is requested may not always be the debt relief that is granted.

3. **Be ready for bilateral negotiations:** Chinese officials have emphasized that debt relief, including the G-20 debt service moratorium, will be negotiated bilaterally. This may be because it isn't entirely clear which loans qualify as official bilateral credits. This is in contrast to the Paris club multilateral negotiation process. But it does appear that multilateral rules can influence these talks. For instance, IMF policies on lending to countries with unsustainable debt and sovereign arrears influenced the restructuring negotiations between the Republic of Congo and China.

4. **Know your worth:** China's relationships with its African partners are an important part of its foreign policy, and are especially important to Chinese companies seeking foreign contracts. We have seen no cases of arbitration in courts over loan repayment or asset seizure, and China is unlikely to jeopardize relations by pursuing these methods in the future.[2] If a need for debt relief is clear, Chinese lenders will likely be flexible. ★

ENDNOTES

1. This figure is calculated from China's official figure for debt cancellation from 2000-2012 (US$ 3 billion), and SAIS-CARI figures for debt cancellation from 2013-2019 (US$ 422 million).
2. The widely touted Hambantota case of asset seizure has been debunked (see Umesh Moramudali, "The Hambantota Port Deal: Myths and Realities," *The Diplomat*, January 20, 2020, https://thediplomat.com/2020/01/the-hambantota-port-deal-myths-and-realities/). Partial privatizations on the other hand, do remain an option for governments.

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