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Policy Note

Chinese Loans and the Infrastructure Program of the Duterte Administration

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How can foreign loans be sustainable under an administration that favors foreign borrowing, particularly from the People's Republic of China? The basic premise is that a debt is sustainable if the benefits of the project to which the loan proceeds are applied exceed the cost of borrowing. As an alternative, this article offers a framework on sustainability with the essential element of good governance, among other components. It focuses in detail on four infrastructure projects which are funded through loans from various foreign sources. To determine whether these loans are sustainable, the loan agreements between the Philippines and foreign funders were examined in terms of whether the provisions in the agreement were onerous or one-sided in favor of the lender, and/or disadvantageous to the borrower. The terms and conditions of the Chinese loans were also compared with those of other foreign sources in order to determine which sources offer better terms for the Philippines and ensure that no one source is unduly favored. By looking also at the experiences and lessons from abroad, policy recommendations are drawn to enhance debt sustainability in the Philippines.

The pivot to China by the Philippines had its antecedents under President Ferdinand Marcos who established diplomatic relations with the People's Republic of China in the early 1970s. Following that was President Gloria Macapagal-Arroyo (2001-2010) who first recognized the "clear and inevitable role" of China in the global economy (Camba, 2017, p. 7). Arroyo conducted several bilateral talks in Shanghai that resulted in the signing of agreements related to tourism and opening of the country to Chinese investments. Arroyo's administration was, however, involved in a corruption scandal exposed by Congress that culminated in the cancellation of a telecommunications project funded by China.

Under President Benigno Aquino III (2010-2016), closer relations with China initiated during the Arroyo administration were reversed. The Philippines filed a case in an international tribunal in The Hague, Netherlands against China to contest the latter's sweeping territorial claims on the South China Sea. The Philippines won the case, with the decision coming immediately after the

end of Aquino's term. But when Rodrigo Duterte became President in mid-2016, he set aside the Hague ruling (as the international court's decision has come to be known) favoring the Philippines and instead pursued a foreign policy that is closely aligned with China, touted by his supporters as "independent" but widely perceived as being subservient to China. Duterte's "pivot to China" was defined by unconditional reliance on Chinese loans to finance an ambitious infrastructure program popularly known as "Build, Build, Build" (BBB).

Indeed, under Duterte China's presence in the Philippines expanded exponentially. Chinese nationals became one of the most numerous and ubiquitous tourists in the country, doubling, according to the Bureau of Immigration, from just over 600,000 in 2016 to over 1.2 million in 2018. There has also been an increasing number of Chinese workers, with those seeking special work permits jumping from 15,000 in 2016 to 200,000 in 2018. Mostly employed in the construction and gaming sectors, some of these workers arrived on a tourist visa without the required work permits; a few have been apprehended and deported back to China.

No less than four official trips were made by Duterte to China during the first half of his six-year term alone; Chinese President Xi Jin Ping reciprocated with one visit to the Philippines. On a number of occasions, Duterte has effusively and unabashedly professed admiration for China, even boasting that the Chinese government is not going to let him be overthrown by domestic opposition. All of these official and personal relations were happening amidst the rising tensions in the South China Sea/West Philippine Sea caused by China's aggressive island-building and military fortification activities inside the Philippines' exclusive economic zone (EEZ).

The flow of Chinese workers and tourists was accompanied by the large inflow of Chinese capital in the form of investments, aid, and loans. The Chinese invested heavily in online gaming enterprises in the Philippines catering mainly to Chinese nationals.

In light of these developments, this article examines the issue of Philippine-China relations. The article aims to answer the following questions:

1. What is debt sustainability?

2. Is the country's debt to China sustainable?

3. What are the implications of the strategy of relying on Chinese loans on the pursuit of the "good life" in the Philippines?

In exploring these issues, the article takes note of the rapid increase in Chinese loans under the Duterte administration; offers a model of good governance

and debt sustainability; examines the record of the Philippines in servicing its foreign debt obligations; discusses the different institutions and processes involved in loan negotiations, packaging, and implementation; compares four foreign loans from different sources using selected evaluation criteria; and examines the experience of countries which extensively relied on Chinese loans to finance their infrastructure programs and/or projects. The final section concludes and makes some policy recommendations for enhancing debt sustainability.

Build, Build, Build and Chinese Loans

Good infrastructure is a *sine qua non* to a nation's competitiveness, economic growth, and development. It facilitates the flow of people and goods, connects and unites the different parts of a country, and reduces transport and distribution costs. Poor infrastructure has been blamed for the generally sluggish economic growth of the Philippine economy compared to neighboring countries. While countries at a similar level of development as the Philippines have been investing 5% or more of their GDP on infrastructure, the Philippines has in the past invested only around 2%.

The growth of Chinese loans and grants to the Philippines under the Duterte administration has been phenomenal. In 2016, the first half-year of the Duterte administration, there was only one Chinese project worth only USD1.56 million. In October of that year, Duterte visited China and entered into 13 cooperation agreements worth USD$24 billion in pledges, of which USD$15 billion were business-to-business contracts and USD$9 billion were official development assistance (ODA). By 2017, China's ODA increased to PHP10.857 billion. As of 2019, the BBB program included 75 priority infrastructure projects, of which 16 projects worth PHP672.4 billion were to be funded from Chinese loans. These projects are shown in Table 1.

Table 1
Infrastructure Projects to be Funded from Chinese Loans and Grants

Project	Amount of grant/loan (in billion pesos)
1. North-South Railway Project-South Line (long haul)	175.3
2. Subic-Clark Railway Project	57.2
3. Ambal-Simuay River and 4. Rio Grande de Mindanao River Flood Control Project	39.2
5. Davao City Expressway Project	25.6
6. Panay-Guimaras-Negros Island Bridges	97.3
7. Cebu-Bohol Link Bridge	56.6
8. North Expressway East Project	44.6

9. Dinagat (Leyte)-Surigao Link Bridge	47.4
10. Luzon-Samar Link Bridge,	57.6
11. Camarines Sur Expressway Project	2.3
12. Pasacao-Balatan Tourism Coastal Development Program	4.7
13. Safe Philippine Phase I.	20.3
14. Chico River Pump Irrigation Project	4.7
15. New Centennial Water Source Kaliwa Dam Project	12.2
16. Pasig-Marikina River and Manggahan Floodway Bridges Construction Project	27.4
TOTAL	**672.4**

Source: NEDA (2019); Department of Finance (2019); Punongbayan (2019)

As of July 2019, the approved infrastructure loans and grants from all sources indicated that loans sourced from Japan as well as from ADB/Japan accounted for more than three-fourths, while the Chinese loans amounted to 19%. Excluding the share of the Philippine government and private sector loans, the respective shares of China, Japan, and Japan/ADB increased to 22%, 28%, and 46%, respectively. At the rate Chinese loans were increasing in both number and amount under Duterte, Chinese loans would supersede loans from other sources.

Debt Sustainability Defined

When is a debt sustainable, and when is it not?

The key word is "sustainable." We start with the Brundtland Commission's definition of sustainable development as "meeting the needs of the present without compromising the ability of future generations to meet their own needs" (1987, p. 16). Initially used in connection with the environment, the concept has since been applied to other areas—thus, sustainable production, sustainable consumption, sustainable tourism, sustainable manufacturing, sustainable debt etc. Implied in the concept is a future state of affairs that is as good as, if not better than, the current state.

A debt is sustainable if a loan-financed project's income stream is sufficient to pay for the principal plus the interest when these are due. The opposite, unsustainable debt, is thus one where, at the micro or project level, the revenue streams of the project are insufficient to pay for the combined principal and interest. At the macro or economy-wide level, debt is unsustainable if the totality of a country's debt obligations—public and private, domestic and foreign, short-term and long-term—are high and expected to remain as such relative to the country's gross domestic product (GDP), export earnings, international

reserves, tax revenues, and other incomes. Unsustainable debt can lead to debt restructuring if the problem is lack of liquidity or to debt default if it is insolvency.

What was discussed is debt sustainability in the narrowest sense. We argue in this article that there is a broader concept of debt sustainability that takes into account not only the ability of the borrower to pay its debt obligations when these fall due, but also the process involved in contracting the debt, the manner of implementation of the debt-financed project, and the impact of the debt on the country's development goals. In the context of developing countries, a debt's development impact refers to increased income and employment, alleviation or reduction of poverty, and preservation and protection of the environment and the nation's patrimony resulting from the debt-financed project. On the other hand, the process and the manner of contracting and implementing the loan-financed project refer to these principles of good governance: transparency, accountability, rule of law, absence of corruption, and public participation. Taking all these into consideration, we can broadly define sustainability as the capacity to pay the loan plus good governance. It is argued in this article that, in the long-run, debt sustainability is a function of good governance.

Sustainability and Good Governance

One of the reasons for the low quantity and poor quality of infrastructure in the Philippines and other developing countries is corruption. Corruption takes many forms. For instance, steel bars that are under-sized, but which carry the price tag of larger bars, may be bought and used in building or road construction. The resulting building or road infrastructure is almost certain to be substandard, and may soon have to be repaired or replaced, thus making the project more expensive. Although examples of official corruption in infrastructure projects are plenty, hardly anyone gets prosecuted or punished, and the few big ones who are caught and jailed are soon set free, like what happened to the legislators and executives who were jailed for corruption by the administration of President Benigno Aquino III.

Thus, an essential element of good governance is the deterrence of corruption in the negotiation, approval, disbursement, and implementation of loans. The World Bank, the Japanese Government, and the Korean Government all contain a clause requiring the reporting of any corrupt or fraudulent practices as well as protection from retaliation to any person or agency reporting such practice(s).

Transparency and public participation contribute to public acceptance and ownership of a project, thus enhancing its chance of success and continuity beyond the administration that initiated it. Islam et al. (1997) show that projects that are characterized by active citizen participation (even in the form of demonstrations and other forms of protest) and civil liberties are more likely to be successful than

those where these are absent. All too often, however, details of loan contracts are opaque and hidden, and the public gets to know (if at all) about the details only after these contracts have been signed and the projects are already underway.

Clear lines of authority and accountability are also important, so that in the event that something goes wrong with a project, someone is held liable or accountable. Absent such clarity, endless finger-pointing could ensue, jeopardizing the project.

Finally, the rule of law, including a functioning judicial system, is an important safeguard against arbitrary decisions or abuse of authority. Under non-democratic regimes, institutions that serve as checks and balances such as an independent legislature and functioning courts are either non-existent or powerless. Without checks and balances, a government in power may enter into transactions and activities of dubious legality and propriety, and get away with it. This happened abundantly during the Duterte administration and the Marcos regime.

Principles Governing International Agreements

In conducting trade and commerce as well as people-to-people interactions, nations observe certain norms and codes of conduct. The most basic of these are mutual respect, fairness, and tolerance. This principle is anchored on the recognition of the unique history, culture, and socioeconomic condition of a country as well as the character of its people. It behooves then that a country in need of financial support from another country should be treated with generally accepted behavior and standards, in order to avoid distrust and conflicts. This principle also applies to negotiations between countries for the purpose of crafting a loan agreement, which is the financial instrument by which a country agrees to secure financing for specific projects or development activities. Under generally accepted international practices, a loan agreement must abide with clarity and specificity to the terms and conditions of the loan. Both parties, the borrower and the creditor, must clearly understand and accept the terms of the loan.

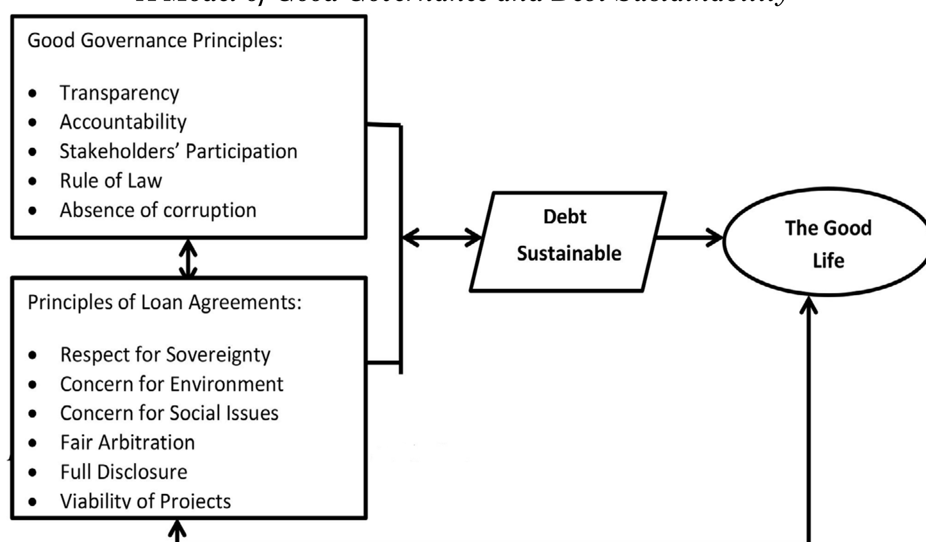
How can mutual respect and fairness be achieved in a loan agreement? In international practice, the loan agreement must disclose fully the terms; ensure that they are fair and not onerous; that the parties treat each other as equals and as sovereigns; and the parties abide by international laws and practices, including arbitration in a neutral setting. Some loan agreements contain provisions on the protection of the natural environment, on climate change mitigation, the protection of human rights (including those of indigenous peoples and minorities), and equal opportunities in employment and contracting.

A key point in negotiating and concluding a loan agreement is the promotion and protection of the sovereignty of the loan-seeking country and

ensuring that there is no duress and imposition by the lending country. A loan agreement should be transparent, with full disclosure of the terms, and no quid pro quo consideration. Anything not spelled out in the loan instrument that is not germane to the agreement should not be enforceable. Most loan agreements do not contain confidentiality clauses that prohibit the disclosure of the agreement or parts thereof.

The foregoing discussion can be summed up as follows: debt sustainability depends upon good governance and adherence to the principles and practices of international relations. It can be represented in Figure 1, which serves as the framework of this study.

Figure 1
A Model of Good Governance and Debt Sustainability



Source: Authors' own construction.

Recent Philippine Experience in Borrowing

When it comes to servicing its foreign debt obligations, the Philippines has had a fairly good record. The one major exception was in 1983, when the Marcos administration defaulted on its loans amidst the economic and political legitimacy crises that engulfed the country. After EDSA 1, there was a clamor to repudiate the foreign loans contracted by the Marcos administration, especially tainted ones like the loan for the Bataan Nuclear Power Plant, which never became operational but whose amortization the Philippine government religiously continued paying until recent years. President Cory Aquino and her successors chose to honor all the country's debt obligations, probably one reason why the country has maintained a favorable credit rating abroad.

In recent years, the ability of the Philippines to service its debt steadily improved, especially under President Benigno Aquino III. The debt-to-GDP ratio and the debt-service burden steadily declined from over 40% during the Arroyo administration to just over 30% towards the end of the Aquino III administration. The decline under Aquino III is the combined effect of the high GDP growth rate and the low level of foreign borrowing, the latter partly due to the preference for the public-private partnership form of financing. But the downward trend in the debt-to-GDP ratio was arrested during the first two years of the Duterte administration; there has in fact been a noticeable upward trend since, probably the effect of more foreign borrowing and lower growth rates.[1]

The Loan Process in the Philippines

Normally, projects requiring foreign loans are initiated or proposed by any government agency, public corporation, local government, or other government entities. Project proposals are subject to review and approval by the National Economic and Development Authority (NEDA) through the Investment Coordination Committee (ICC). Once projects are vetted and qualify under the ICC guidelines, they become part of the ODA portfolio. The requirements for such projects include submission of plans and documentations, review and endorsement by their respective Regional Development Councils as applicable, compliance with the equitable distribution and use of ODA funds, and meeting the required economic internal rate of return (IRR) of 15%. Since foreign loans normally require foreign exchange for their payment, the Monetary Board of the Bangko Sentral ng Pilipinas (BSP) also approves foreign-funded projects.

The Philippine Constitution mandates NEDA to review foreign-funded projects in order to prevent a repetition of the excessive foreign debts incurred by the Marcos administration. In 1996, Congress further empowered NEDA to monitor the use of foreign grants and loans. However, this primary function and independence of NEDA had been eroded in subsequent administrations. President Arroyo began this process of weakening NEDA "through administrative reorganizations or the creation of ad-hoc administrative groupings."(Desierto, 2009, p. 77). Attempts were also tried to lower the 15% threshold for the IRR of projects. The Duterte administration energized the ICC through the formation of an ICC-CabCom (Cabinet Committee) where foreign funded projects are now deliberated and approved instead of by NEDA.

In June 2017, the ICC-CabCom raised the project cost threshold for ICC approval from PHP1 billion to PHP2.5 billion. As directed, four exceptions to this rule were made, including one which reads: "2.4 All proposed projects for funding with the Chinese Government, regardless of amount" (ICC, 2017, p. 2). The change also gave a proponent agency the power to approve and implement a project under its own authority.

The function of the ICC thus became merely ministerial. The effect on the mechanism for approving project proposals by NEDA has been to dilute the process, and is tantamount to "a classic constitutional violation" (Desierto, 2009, p. 103).

Comparison of Four Loan-Financed Projects

To get a better perspective on the nature of the various foreign loans secured by the Duterte administration, four infrastructure projects funded from three sources, namely, Japan (1), the World Bank (1), and China (2) were selected for detailed study. These projects were selected because these were approved and signed under President Duterte; their loan documents were available; and there were in fact on-going construction activities. The authors requested the Department of Finance (DOF) for more loan documents but we were given access to only four. NEDA also declined to provide data on the loan agreements, stating that under current protocol, the DOF is the official depository of the documents. The four projects are:

a) **North-South Commuter Railway Extension Project**. Funded by Japan through the Japan International Cooperation Agency (JICA), it will construct a 50.7 km railway extension from Malolos, Bulacan to Clark International Airport in Angeles, Pampanga and a 56.5 km extension railway from Tondo, Manila to Calamba, Laguna. The project aims to ease traffic congestion in Metro Manila.

b) **Clean Technology Project**. Funded by the World Bank, it includes a Metro Manila Rapid Bus Transit project on Quezon Avenue.

c) **Chico River Pump Irrigation Project**. Funded by China, it is a pumping station and other facilities to irrigate 8,700 hectares of farms from Cagayan to Kalinga.

d) **New Centennial Water Source-Kaliwa Dam Project (NCWS-KDP.** Funded by China, it is expected to supply 600 million liters per day (MLD) of water to Kaliwa Dam and a 2,400 MLD capacity raw water conveyance tunnel. The water will be supplied to Metro Manila.

The four projects were examined closely according to eight (8) criteria, which are in line with the principles of good governance and international agreements: economic viability, interest rate, length of maturity, respect for national sovereignty, fair arbitration, full disclosure of the loan terms, presence or absence of anti-corruption provision(s), and due regard for social/environmental issues.

Table 2
Comparison of Four Loan Agreements

Lender Terms	JICA	IBRD	CHINA	CHINA
Project Name	North South Railway	Clean Technology	Chico River Pump Irrigation	New Water Source Kaliwa Dam
Date signed	1/21/2019	2/14/2019	4/10/2018	11/20/2018
Loan amount	JPY167.2M	USD23.9M	USD62.09M	USD211.2M
Interest rate (annual)	0.1%	¾ of 1% plus .18% mgt. fee	2% +.3% mgt fee. .3% com.fee	2% plus .3% mgt. fee, 3% com. fee
Maturity	40 Years	18 Years	20 Years	20 Years
Respect for sovereignty	Yes	Yes	No	No
Environment/ Social issues	Yes	Yes	No	No
Fair arbitration	Yes	Yes	No	No
Full disclosure	Yes	Yes	No	No
Anti-corruption	Yes	Yes	None	None
Viability of projects	Yes	Yes	Yes	Yes

Interest Rate and Maturity of Loans. The interest rates charged on the Chinese loans are many times higher than those charged on both the International Bank for Reconstruction and Development and Japanese loans. Both Japan and the IBRD charge less than 1% while China charges at least 2% for each of its two loans, with a 3% management fee. In terms of maturity, the picture is mixed. The JICA loan has the longest maturity at 40 years, followed by the two China loans at 20 years each, while the World Bank loan has the shortest maturity at 18 years.

It would seem, though, that a loan's maturity has something to do with the nature of the project financed by the loan. Thus, an infrastructure project such as a railroad has a long maturity, since the returns from a railroad project, which is characterized by stable technology, are realized over a long period of time. Meanwhile, an environmental project, which uses a new technology and hence has a high risk, should realize its returns within a relatively short period.

Viability of Projects. On their face value, the four projects that are funded by three foreign sources are all economically viable since they have passed the review of the NEDA, the CabCom, and the DOF. The four projects presumably passed the required IRR (15% or better), and are therefore all financially viable. However, one other important requirement, which is the geographic dispersal of projects to provide spatial parity in the use of public funds, has apparently not been met. It is significant to note that three of the four projects are concentrated

in Metro Manila. One is intended to ease traffic congestion and the other is intended to provide adequate potable water, both for the benefit of residents of Metro Manila. All projects are located in Luzon.

Respect for Sovereignty. As previously mentioned, a fundamental principle in international relations, and in particular among the parties involved in transacting a loan, is mutual respect and recognition of the sovereignty of each country. Japan and the IBRD seem to fully abide by this principle. The terms and conditions of the two Chinese loans are almost identical, except for the provision on sovereignty. Article 8.1 on the Waiver of Immunity for the New Centennial Water Source-Kaliwa Dam Project was changed; *the exceptions to the waiver provision were deleted*. The Chico River Pump Irrigation Project loan agreement originally provided that

> "Notwithstanding the foregoing, the Borrower does not waive any immunity of its assets which are 1) used by a diplomatic or consular mission of the Republic of the Philippines, 2) of a military character and under control of a military authority or a defence agency of the Republic of the Philippines, or 3) located in the Philippines dedicated to a public or governmental use (as distinguished from patrimonial assets and assets dedicated for commercial use)" (Republic of the Philippines, 2019 as cited in Rivas, 2019, para. 17).

This particular provision of the loan agreement was at the core of the alarm raised by former Supreme Court Associate Justice Antonio Carpio when he argued that the waiver in the Kaliwa Dam project in case of loan default endangers the West Philippine Sea oil and gas deposits, which a joint Chinese and Philippine Marine Seismic venture found during the time of President Arroyo to hold oil and gas reserves of 17.7 billion tons (compared to Kuwait's 13 billion tons), thus making the Philippine oil and gas reserves the fourth largest in the world. These reserves may be seized by China if the Philippines defaults on its debt obligation. There is enough experience elsewhere to warn the Philippines of such a danger.

Fair Arbitration. Both the World Bank and JICA observe international law and resort to international institutions to settle conflicts or disagreements in the process of project implementation. In Japanese loan-financed projects, it is specifically provided that arbitration is to be undertaken through a court of competent jurisdiction. In the IBRD, there is no specific clause on arbitration, but there is a provision to the effect that changes made by the borrower require World Bank approval. However, in the case of the two China loan agreements, there are provisions that give the lender the upper hand. Both Chinese loan agreements provide that in arbitration, China's laws are to govern and that there will be a three-member arbitral panel whose composition ensures a Chinese majority. There are specific provisions to the effect that the Chico River Dam Project will be arbitrated by a Chinese commission, while that on the Kaliwa Dam will be handled by a Hong Kong-based center. In both cases, the Chinese creditor clearly has the upper hand.

Full Disclosure. In general, information about loans is available upon request. But the Chinese loans have a specific clause prohibiting the public from having access to information on the loans in the form of a confidentiality clause to be observed by both the Philippine and Chinese governments. On the other hand, both the JICA and the IBRD loan agreements have no such confidentiality clauses or non-disclosure provisions on their loan agreements, demonstrating transparency.

Anti-Corruption. The Chinese loan agreements are silent on the issue of corruption and the pursuit of anti-corruption measures, whereas Japan and the IBRD are very emphatic in their disapproval of corruption. Both also provide guidelines for reporting corruption in the course of project implementation.

Concern for the Environment and Other Social Issues. The JICA and World Bank loan agreements contain specific provisions that highlight the need for a sustainable environment and orderly resettlement of displaced populations when infrastructure projects disrupt not only human habitations but also entire ecosystems of flora and fauna. On the other hand, the Chinese loan agreements do not have provisions for the protection of the environment and the orderly relocation or resettlement of people affected by the projects.

Public Participation. Participation of the citizens in the process of contracting loans and implementing loan-financed projects is also important, although it is not included in Table 2. It is conspicuously absent in the loan agreements entered into by the Philippine government with China mainly because of the non-disclosure provision. Without information, the public cannot meaningfully participate in governance.

It is surmised that one of the reasons for the current lack of access to information, and consequently the lack of public participation, is that institutions of governance such as the legislature and the courts may have been muzzled or have abdicated their active roles in a democracy. Only a small sector of the Philippine press is keeping the torch alive, and even that small opening may be fast closing up.

The Experience of Other China-Indebted Countries: The Angola Model

The comparison of the four projects indicates that loans from sources other than China are more advantageous to the Philippines. Thus, one is led to ask: if Chinese loans are an alternative to the more traditional loan sources such as Japan, Asian Development Bank, and the World Bank, should the loan terms offered by China be at least at par with if not better than those offered by the

traditional sources? The more varied the loan sources are, the more advantageous it should be for the borrower, because competition among the creditors drives down the borrowing rates and improves the other terms of a loan. So, why have Chinese loans been favored by the Duterte administration?

The answer, we believe, is that compared to other lenders, China is more tolerant towards corruption and "democratic deficits" (e.g., authoritarian rule and violation of political, and human rights) in the borrowing countries. The Chinese have shown that they are willing, or are more willing than other creditors, to offer incentives to malfeasant officials in order to push their loans in the borrowing country, especially resource-rich but poor countries. The same conclusion has been made by Yoon, who observed that weak and compliant Asian countries "allow China to prevail through threats and/or inducements," even as China pays little regard to "institutional constraints on infrastructure investment in host countries" (2018, pp. 19-20).

Experience also shows that foreign loans contracted under such conditions are likely to be unsustainable, resulting in debt default or, worse, loss of sovereignty. In Sri Lanka, China took over the management and control of the strategic Hambantota Port when the government of Sri Lanka could not pay its debt. In Kyrgyztan, a Central Asian country close to China, a large piece of the country's territory was ceded to China to satisfy the Central Asian country's debt obligation—this was understandably denied by a high-ranking Kyrgyz official (Punongbayan, 2019; Rivas, 2019).

All these are consequences of the adoption by less-developed countries of what has come to be known as the "Angola model." The model takes its name from the country in the southern part of Africa which is rich in mineral and other natural resources, but, like many other countries in the same continent, is poor and underdeveloped. Part of the reason why Angola was economically backward was the poor state of its infrastructure, the legacy of a civil war that lasted for more than a decade and tore the country apart.

When the Angolan civil war ended in the early 2000's, the country was faced with the enormous task of physical and economic rehabilitation. Having just emerged from a period of political instability, Angola was a poor credit risk and did not have access to loans from the traditional sources. That was when Angola turned to China, which had been offering aid and loans at attractive terms. Chinese loans were not only readily available; they did not carry the usual conditions to the borrowing country attached by Western and multilateral banks, such as transparency, accountability, the rule of law, anti-corruption, and other governance principles. For China, the attraction of Angola was the presence of mineral resources that China needed badly to fuel its rapid industrialization. And so, China extended loans to Angola, with the latter's oil resources as collateral (Yun Sun, 2014; Beattie, 2010).

What could happen did happen. Unable to meet its maturing loan obligations, Angola's revenues from its oil/mineral assets were sequestered by China to ensure the repayment of the loans extended to the country. What happened in Angola —the oil or minerals-for-loans exchange—became the template for Chinese economic relations with other African countries, and subsequently with other countries in Asia and Latin America.

By owing China USD25 billion in loans, Angola became the most heavily indebted African country. But Angola is just one of more than 30 countries in Africa, Latin America, Asia, and Oceania that have borrowed from China. As of mid-2019, these countries owed China a staggering USD700 billion to finance power, transport, and infrastructure projects. These China-indebted countries have something in common: they are low- to middle- income countries, many of them with abundant natural resources, especially oil and minerals. Many of these countries are also under authoritarian rule, have "democratic deficits" and corrupt leaders. All or most of the loan-financed projects are implemented by Chinese contractors who use materials made in China and employ Chinese workers. As a result, most of the loan proceeds go back to China.

Summary, Conclusion, and Policy Recommendations

On the narrow definition of sustainability, the Chinese loan agreements entered into by the Duterte administration appear to be sustainable, but on a broad definition that takes into account the core principles of good governance (transparency, accountability, public participation, and absence of corruption) and international principles governing loan agreements and international relations in general (mutual respect, equality, and respect for sovereignty), the Chinese loans and a development strategy that relies heavily on them may be unsustainable.

What, then, is to be done? Kapoor et al. (2019) proposed five alternatives to the unsustainable debt strategy being pursued by some African countries:

1. reduce reliance on risky and volatile debt sources and instead rely more on PPP (public private partnership), securitization of infrastructure assets, and privatization;

2. increase the maturity of external debt, to at least 30 years;

3. use more flexible countercyclical and state contingent debt instruments, such as commodity hedging or GDP-indexed instruments;

4. develop safe domestic assets; and

5. apply greater transparency in debt management, including commitment by government to release in real-time data on old and new debt from all sources.

All five alternatives are relevant to the Philippines, although we believe that alternatives 1, 2, and 5 are particularly applicable.

As an alternative to foreign borrowing, PPP and privatization reduce the fiscal burden of government and thus enable it to use its funds for other important public services. Projects funded by PPP are usually undertaken by domestic businessmen and industrialists; they provide employment to Filipino workers (not to workers from the lending country); they do not deplete the country's foreign reserves (unless a project has a large import component); and they do not saddle future generations with potentially unsustainable foreign debts. The disadvantage for the public is that they may have to pay users' fees.

The second alternative, negotiating for longer debt maturity as well as lower interest rates, should be the aim of every negotiator who has the interest of the country at heart. Philippine officials should take advantage of the fact that there are now more sources of loans, some with more advantageous terms for the country other than the Chinese loans.

As for alternative 5, officials should make no advance commitment to award a project before the terms of the loan agreement are known. Such a commitment was made by Duterte to Chinese officials for the third telecommunications (telco) player when he visited China in 2017, a commitment that was subsequently repeated to a Chinese official who visited the Philippines in 2018. The bidding for the third telco that subsequently transpired was thus a sham, a clear case of *lutong makaw*.[2] The same recipe of *lutong macaw* applies to the Chinese loan contracts, thus revealing the pre-concocted and dubious agreements entered into by the Duterte administration.

Another option is to cancel patently onerous and one-sided loans. This was the strategy pursued by Prime Minister Mahathir Mohamad of Malaysia upon assuming office after the former Prime Minister was voted out of office on allegations of widespread corruption. Although Mohamad's initial hardline stance subsequently softened, a renegotiation of the Chinese loans gave Malaysia more favorable terms.

The Philippines can learn a lesson from the experience of Angola and other countries that borrowed heavily from China and ended up surrendering to the lender control of some of their assets. Government officials should be more circumspect in entering into loan agreements with China in particular and in dealing with China in general. Even if Chinese loans appear to be generous,

Filipinos should be on guard against "Greeks bearing gifts." These loans could be the Trojan horse for foreign domination and control of the Philippines.

The question that stares us in the face is: Why is borrowing from China the preferred development strategy of the Duterte administration when it could borrow elsewhere at better terms for the Philippines? These alternative loan sources offer lower interest rates and longer maturities, rely on and use Filipino instead of foreign workers, are more transparent, employ an impartial arbitration process in case of dispute between the parties, and are not tainted with corruption.

This brings us also to the related political-economy issue of why foreign borrowing seems to be a favored strategy of authoritarian rulers like Marcos and Duterte. One would expect that, being strong, these rulers should be able to extract more taxes from internal sources, rather than rely on foreign loans.

The reason for this behavior of authoritarian rulers is that they are also "populists," in the sense that they derive legitimacy for their repressive rule by depending on "freebies," such as free college tuition, free irrigation and fertilizers, subsidized commodity price control and cash dole outs. They ignore the long-term social and economic consequences of their actions which can be potentially disastrous to the country. Consequently, the monitoring of the loan agreements with China deserves closer attention primarily by NEDA and DOF beyond performing their narrow scope and technical guidelines. These agencies need to exercise due diligence in crafting loan agreements and be more conscious of the value itself of serving the nation. In addition, future policy studies may be directed towards an evolving framework described in this paper that elevates the accepted standards of cost-benefit ratio and internal rate of return in the design and execution of foreign loans. The impetus of such studies should be geared to how these loan agreements adhere to the model of good governance and debt sustainability. The fundamental considerations in this model are transparency in the loan agreements, fairness and competitions in the bids for projects, priority to hiring of Filipino contractors and workers, safeguarding the rights of cultural minorities and indigenous people in the affected project areas, fostering public participation, consultation and review, and safeguarding the environment and natural resources of the country. Above all protecting the national patrimony and sovereignty is paramount when the welfare, dignity, and interests of the Filipino people are involved.

Endnotes

[1] Note that the upward trend under Duterte preceded the COVID-19 pandemic by many years.

[2] "*Lutong Makaw*" is literally translated as "cooked in Macau (China) style". The dish is prepared in advance, with the ingredients already cut and ready to be cooked. In Philippine usage, *lutong makaw* means a rigged bid with a predetermined outcome.

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