

China, as the Sovereign Creditor of Emerging Markets and Developing Economies

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SUMMARY

The study's three main questions are: 1. What trends can be observed in Chinese sovereign lending? 2. How does the contractual setup differ from the Western one? 3. What proposals have been made to mitigate the related risks, and which ones seem feasible? The research relied on recently established databases and regulatory materials. China is the world's largest sovereign creditor at the moment. Its credit expansion began as early as 2008, well before the official announcement of the intention. Several conditions in its contracts differ from those of the West, which pose a risk relevant to an international debt settlement. Their purpose is twofold: to make a profit secured by strong collaterals and, if necessary, "soft power" influence. On the other hand, China does not use "debt-trap diplomacy". Any global reform in sovereign debt management needs the involvement of China, but in the longer term, Chinese lending conditions should also ease.¹

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The indebtedness of the states is higher and higher internationally. The financial crisis beginning in 2008–2009 and the shock caused by the COVID–19 pandemic pointed out the (not new) requirement of more uniform international procedures related to the management of sovereign bankruptcy. In this process, China, aiming at world market dominance more and more prominently in the past fifteen years, plays an outstanding role on the creditor side.

The internal economic and political stability of the People’s Republic of China (hereinafter: China) and its external global economic and political power went through a spectacular change in the past seventy years. Its lending to foreign countries also showed an increasing tendency. Sovereign lending by China may be divided into several groups; the fundamental categories are loans directed to developed and developing economies (Balla, 2020). The data sources of the former are somewhat better, partly because the developed economies or economies with high income publish statistics themselves. A classic example of such countries is the United States of America, which publishes detailed statistics on the distribution of its sovereign bonds. The strategy of China in this category is mainly directed at the primary or secondary market government bond purchases. They hold American, German and British government bonds in the largest quantities, of which China has been the biggest holder for a good while (Horn et al., 2021a). The issue raised most frequently in relation to the USA is global disequilibrium (Gábor, 2009).

Chinese loans are disbursed to developed economies via other channels, too, among others, via sovereign funds (Csoma, 2015; Dani – Törös, 2011). At the same time, loans extended to developed economies and economies with high income are not really problematic in sovereign debt management,

as the majority of these countries did not struggle with payment difficulties in the category of sovereign bankruptcy during the past one hundred years or only struggled with them very rarely. However, this problem is significantly more frequent in emerging markets and developing economies². In our research, we concentrated on the latter. The topic is relevant from a Hungarian aspect, too, as the loan related to the Budapest-Belgrade railway line is also disbursed by the Export-Import Bank of China, presumably under the ‘usual’ conditions also analyzed in this study.

We examine three key questions in the study. Firstly, we examine how big may the real volume and proportion of the sovereign loans extended to the emerging markets and developing economies by China bilaterally and otherwise be. It is an important issue as it is not easy to gain information about it. Secondly, we examine the main tendencies in disbursement, geographical distribution and above all, non-payment. Our second question regarded the unique condition system of the Chinese sovereign loans. Our purpose was to assess the additional risks in the conditions of contracts that had become known. The third question was about the proposals made to mitigate the related risks and what could be feasible from these proposals.

Despite China being the largest sovereign creditor now, we faced significant data problems. In the first research question, we largely leaned on a database (Horn et al., 2021b) that had attempted to establish a uniform database in the academic literature for the first time, using official and unofficial data (preparing an estimate of hidden debt): this in itself was an extraordinary task for the authors. Our other database was the sovereign bankruptcy database of the Bank of Canada and the Bank of England (Beers et al., 2021), which had been available until 2020. Although this database calculates from far less precise official

data – more precise data are not available – it is still possible to draw a conclusion on a trend as the sample is representative. The source in the second question was provided by the available contracts and their analyses (e.g. Gelpert et al., 2021), from which we attempted to give an overview of the main and more risky clauses. In the third topic, we summarised the academic literature regarding the publicly available solution proposals and drew our own conclusions as well.

THE SOVEREIGN LENDING ACTIVITY OF CHINA IN EMERGING MARKETS AND DEVELOPING ECONOMIES

The so-called ‘soft power’ has been in the foreground of the foreign policy of the superpowers, too, since the second half of the 20th century (Winkler – Nye, 2005), and instead of the traditional force (‘hard power’), it has relied on an approach related to the economic and cultural values. Some of its fairly important tools are sovereign and private lending as well as granting aids, which may be performed directly or via development banks.

China is a leading country in this: already in the course of the economic and political changes following the 2008–09 crisis (Csanádi et al., 2009; Szilágyi, 2015), the Chinese central bank launched a significant credit growth programme among the state-owned commercial banks (Lentner, 2016), only domestically at that time. Foreign expansion was officially indicated by the announcement of the so-called One Belt, One Road (OBOR) programme, which is also called the new Silk Road (Shambaugh, 2014). It was launched in 2013 (Szilágyi, 2018). One tool was the Asian Infrastructure Investment Bank (AIIB), founded in 2015, although China also lent via other multilateral institutions. The name of the programme changed to Belt and Road Initiative

(BRI) in 2017 (Berlie, 2021), and the number of countries concerned was approximately one hundred and forty in 2021 (BRIX, 2021). To one end of the ‘intergovernmental financial cooperation scale’ related to the emerging markets and developing economies, we may place approximately three thousand aids, while around two thousand sovereign loans would occupy the other end.

The estimation of the loan portfolio extended by China is not an easy task from several points of view; the main reason, however, is that China does not report these to the international databases. The role of debt ‘hidden’ is significant (Alfaro – Kanczuk, 2019). Although it is in partnership with the Paris Club that rallies bilateral state creditors and has been operating since 1956, China is not part of it and neither it is subject to the related informing obligation. China is not a member of OECD either; therefore, Chinese data is not incorporated in its databases, although a partial data supply is operating already. The Chinese central bank is a member of the Bank for International Settlements (BIS); however, very limited data is available. Although there is relevant data in the database of the World Bank (The World Bank, 2022), it is extremely incomplete. Transparency on the receiving side is prevented by the confidentiality clauses built into the contracts (Gelpert et al., 2021). A further problem is that the lending process is performed via several institutions (AIIB, central bank, different state institutions, state-owned banks, etc.).

The study of *Horn, Reinhart and Trebesch* (2021) made probably the most thorough attempt to prepare a uniform estimate of the period between 1949 and 2017 from the existing rather limited data. Because of the above difficulties, even the latest updates (2021) only provide a clear picture of the 2017 data. Nine different official and unofficial data sources were used for the summary, and

several studies were examined for the historical details, from which a uniform database was created. From this, it is evident that the foreign lending of China shows an increasing tendency; moreover, based on the estimated data, China is presently the largest bilateral creditor in the world. We will mainly use data from this database in the following sections of our study.

Figure 1 shows the trends of the state debts of emerging markets and developing economies to China between 2008 and 2017. It can be clearly seen that the increase did not begin with the official announcements of 2013 but already in 2008. Exploiting the 2008–09 financial crisis and the sovereign debt crisis following it (the case of Ecuador, for example, see Vidovics–Dancs, 2015), China significantly

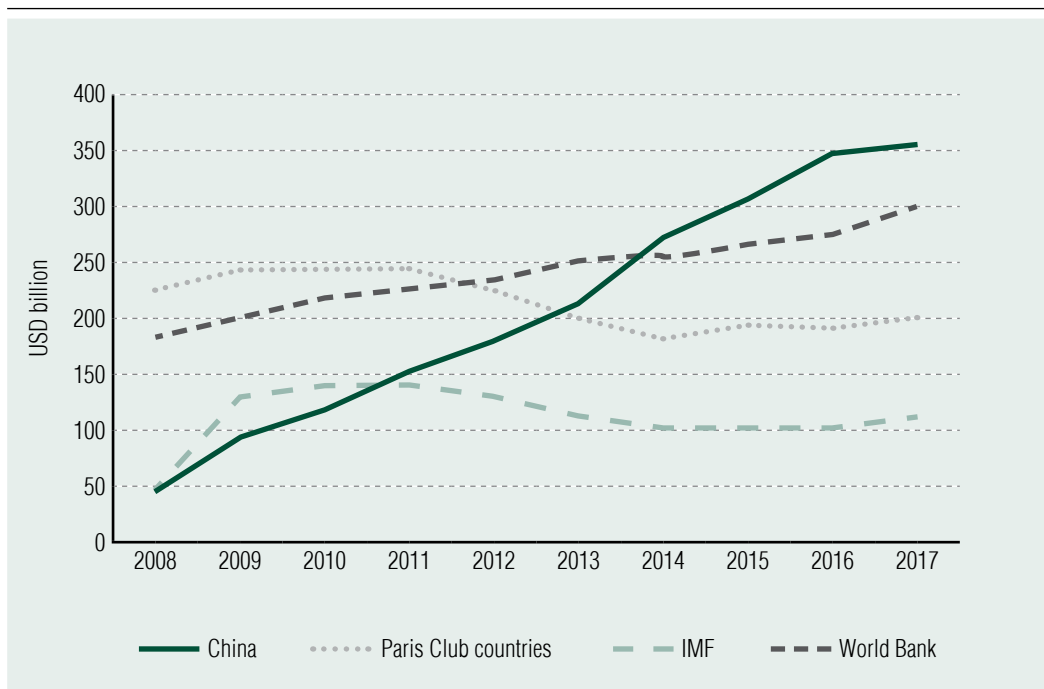
strengthened its position when it did not make its intention public yet; moreover, the majority of the institutional system established for this particular purpose was still missing.

It can also be observed that while in the period of 2010–2013, the portfolio of the countries of the Paris Club and the World Bank decreased significantly, that of China grew dynamically, which meant that after an aggressive market acquisition, China was the largest creditor in these countries when it announced OBOR.

Already in 2017, there were over twenty countries with state debts to China exceeding 10% of the country’s GDP. The regional distribution in 2017 is shown in Figure 2. Although it is the most important initiative, BRI means only 55% of the total outstanding

Figure 1

COMPOSITION OF LOANS EXTENDED TO EMERGING MARKETS AND DEVELOPING ECONOMIES ACCORDING TO CREDITORS (2008–2017, USD BILLION)



Source: Horn et al. (2021b)

Figure 2

DISTRIBUTION OF EXTERNAL DEBTS TO CHINA ACCORDING TO REGIONS (2017)



Source: Horn et al. (2021b)

debt, according to the estimates. Before 2017 the focus was on the Central Asian, Sub-Saharan African and Latin American regions. The portfolio of loans extended to emerging markets was 72%, and the portfolio of loans extended to countries with low income reached 28% (Horn et al., 2021b). The problem is that these states run severe sovereign and country risks on their own, too, and many of them were already seriously indebted (Li et al., 2021; Yue – Nedopil Wang, 2021), which has become visible in recent years in non-performance (Beers et al., 2021). We may only suspect the main trends after 2017 from other reports and studies based on non-public data (Yue – Nedopil Wang, 2020). Unfortunately, we do not have data series that would be as reliable as the databases mentioned above.

Approximately 10% of the loans after 2013 are ‘hidden’, i.e. unreported disbursements not included in public databases. That was a significant item mainly in the African and Central Asian countries, and according to the suspicions, it was mostly in connection with some raw materials (e.g. crude oil, rare earth metal), too (Horn et al., 2021b).

At the same time, when the role of China grew in the past one and a half decades in the field of sovereign lending flowing to emerging markets and developing economies, the subjects of sovereign bankruptcy management and restructuring were also pushed to the foreground. Taking into account that China is outside the usual Western institutional system, it is not a member of any creditor club, this aspect is particularly interesting. Luckily, the Canadian and English central banks maintain

a database of such events that is more up-to-date than the previous one (BoC-BoE Sovereign Default Database); therefore, there are available data until 2020 (Beers et al., 2021).

The disadvantage of this database is that non-bilateral, non-official loans and lending in the commercial category are not included (as opposed to the previous database); however, the main trends may still be read from the data. Another disadvantage is that there is no separate data series for the emerging markets and developing economies; however, as the percentage of non-payment is insignificant in developed countries, we may still use them – as a kind of proxy – in practice.

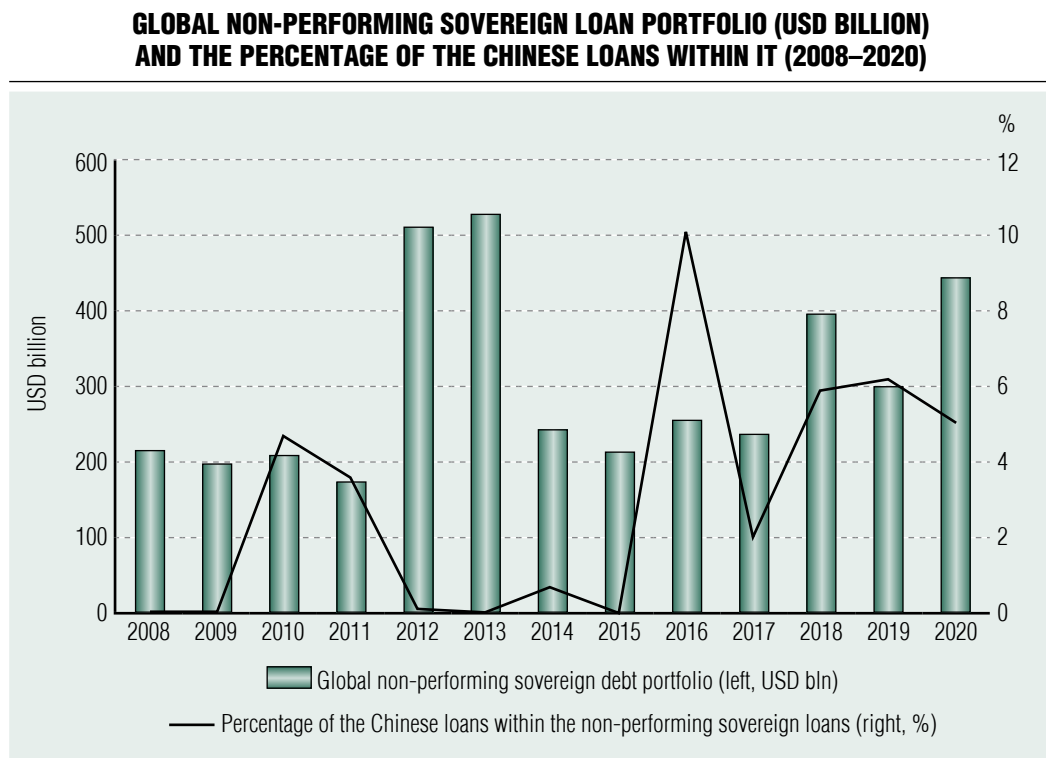
Figure 3 presents the global non-performing sovereign loan portfolio and the percentage of

the Chinese loans within it. It is visible that the surge until 2013–14 caused problems in the Chinese loans, too, in the following years, while in 2012–13, the sovereign crises culminating then did not concern them relevantly.

While the proportion of non-performing Chinese sovereign loans may not be considered outstanding in volume within all defaults, as far as the numbers are concerned (the number of sovereign loans failing to perform to China), the situation is already different: by 2020, nearly 25% of all sovereign defaults affected Chinese loans, and the tendency showed an increase (Beers et al., 2021).

We examined the ratio of Chinese volumes and the number of sovereign loans within all defaulted or restructured loans until this point. Figure 4, however, shows the percentage

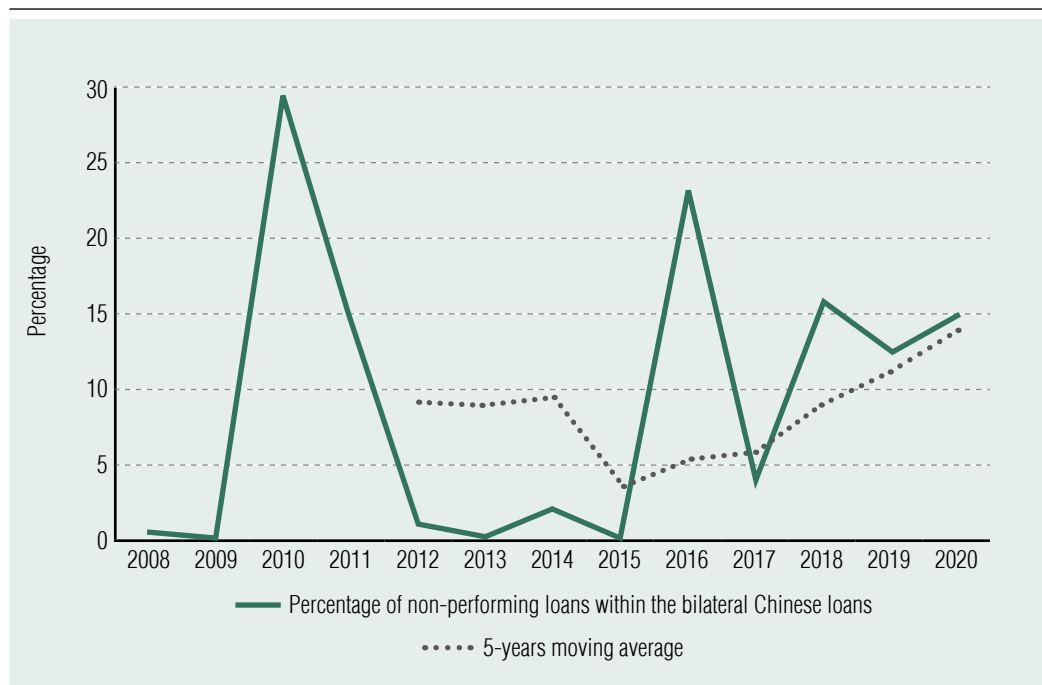
Figure 3



Source: Beers et al. (2021)

Figure 4

**PERCENTAGE OF NON-PERFORMING LOANS WITHIN THE BILATERAL CHINESE LOANS
(2008–2020, %)**



Source: Beers et al. (2021)

of non-performing bilateral Chinese sovereign loans. It is important to note that the bilateral transactions are only one part (approximately one third) of the Chinese sovereign lending (Horn et al., 2021b).

It is assumed that the relatively high percentage in 2010 is related to the not exceptionally high total volume of that time; however, it may be repeatedly observed that the trend is increasing, which is prominently demonstrated by the five-year moving average.

Thus, having exploited the opportunities provided by the crisis of 2008, the Chinese state consciously began its expansion on the international sovereign loan market already five years before the official announcement, with great success. By 2014–15 it became the biggest sovereign creditor in the world. Its role is so significant that in most World

Bank reports, the lending figures are already provided with ‘excluding China’ notes (World Bank, 2021).

Having analyzed the default statistics of recent years, after the early boom, we can see that even if the volume is not significant yet, there are more and more default events related to the Chinese loans, and – at least regarding the bilateral loans – the non-performing portfolio began a trend-like increase in the past four-five years. Based on the relevant reports, it also seems probable (Yue – Nedopil Wang, 2021) that the COVID–19 pandemic of 2020 deteriorated this situation.

The condition system of Chinese loans differs significantly from the Western norms, which fact – due to the deteriorating non-payment statistics – may even carry significant risks in international sovereign lending, and,

to make matters worse, China has not become part of the Western institutional system. In the following chapter of the study, we will examine the typical contractual conditions and restructuring experiences, which have become known to date as well as their potential risks.

THE LEGAL FRAMEWORK OF CHINESE SOVEREIGN LOANS AND THEIR RISKS

The analysis is made rather complicated by the fact that the contents of the Chinese contracts are rarely available to anyone, but the direct participants and they are strengthened by strict confidentiality clauses, and – as it was explained earlier – there are only estimates available of the total portfolio of the loans.

In the section below, we will summarise the characteristic features of the condition systems of the Chinese loans, their differences from the Western standards and the types of risks they carry. The authors of the key study on the subject (Gelpern et al., 2021) worked relying on the contract database of the AidData research workshop operating at the William and Mary private university. The database was built based on available official data. The total number of Chinese loan contracts exceeds two thousand, of which a sample of one hundred contracts considered representative was examined in full text with particular attention given to the contractual conditions, and this was compared with a standard Western sample of 142 contracts and the official contract template of the Loan Market Association. Our analysis builds on the database established this way.

The total loan value of the revealed contracts amounts to USD 36.6 billion; therefore, while the sample represents approximately 5% of the number of contracts, it is slightly larger in its volume. 84% of the contracts were contracts of the China Development Bank, and the Export-Import Bank of China concluded with

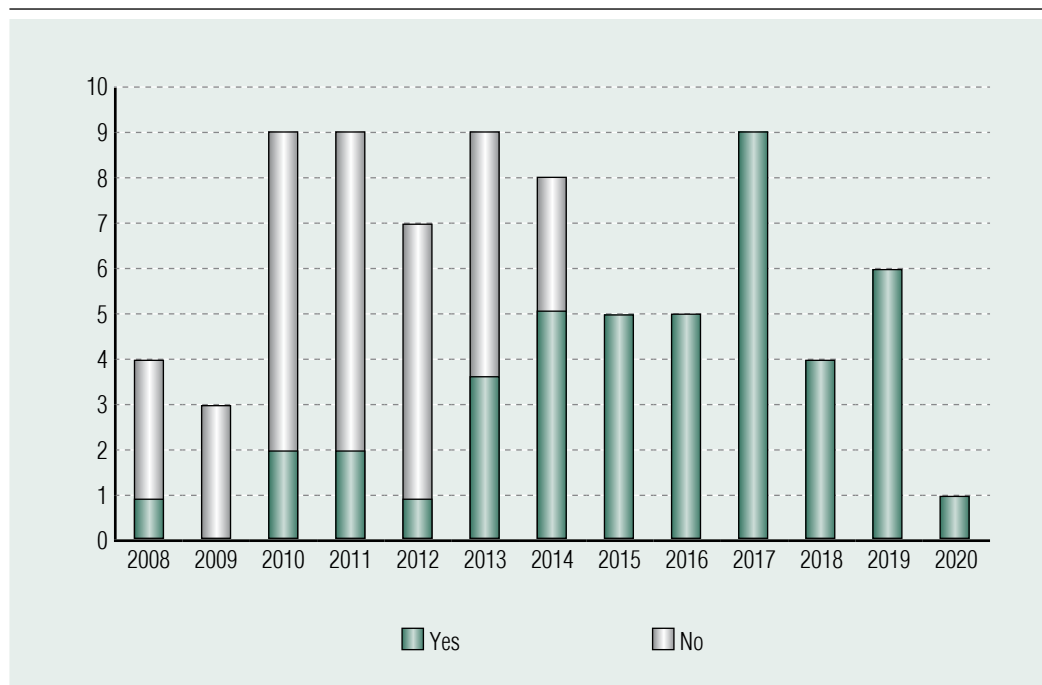
twenty-four partner countries. According to our current knowledge, the multitude may be deemed representative geographically. The researchers summarised and analyzed all the contractual conditions (e.g. principal, interest payment, currency, maturity, collateral, guarantees, bankruptcy events, priority order, termination, other clauses) and compared them with the Western samples. The key differences were the following.

Every contract concluded after 2014 (*Figure 5*) included a stringent confidentiality clause binding on the debtor. In several cases, the very fact of the loan was also covered by this clause. There are such clauses in Western contracts, too; however, they are not interpreted as tightly, and they are not binding on the debtor but the creditor (generally in connection with the pricing and termination). The risks of lack of transparency to such extent are obvious: neither the citizens of the given state nor the other partners can assess the creditworthiness, indebtedness of a country precisely; therefore, all this may significantly distort and render both the collective debt settlement and the potential domestic political consequences more difficult.

30% of the contracts (55% of the volume) required the debtor to open a special bank account ‘approved by the creditor’ as security of the repayment. A particular revenue of the debtor (e.g. oil or bauxite) or the income of a project financed from Chinese loans was often allocated to this bank account. In some instances, the creditors may block the debtor’s access to this account or may even gain repayment from this account, which may be kept even at an off-shore financial institution. That may directly channel specific cash flows away from the debtor and significantly reduce the transparency. There were altogether three analogous conditions in the Western contract templates. Such conditions significantly strengthen the creditor’s collateral positions

Figure 5

**CONFIDENTIALITY CLAUSES IN THE CHINESE SOVEREIGN LOAN CONTRACTS
IN THE SAMPLE, 2008–2020**



Source: Gelpern et al. (2021)

and considerably reduce the debtor’s margin, which is a clear risk when multilateral restructuring is performed.

Nearly three-quarters of the contracts included ‘No Paris Club’ clauses, which expressly exclude the debt from the debt settlement procedures of the Paris Club (and any other similar organization); therefore, these clauses effectively provide seniority to the Chinese creditor. There is obviously no such clause in any of the Western contracts. One of the most significant risks is that the process in the case of the given country may be practically blocked until it comes to an agreement with China. The seniority of the Chinese loans also has a kind of exclusion effect, as if a given country accumulates significant Chinese debt, it may take out loans from the international market later either

with more difficulties or more expensively as the creditors must also compensate for the Chinese creditor’s advantage.

Incidentally, these clauses are in contrast with the Chinese obligations undertaken within the framework of the 2020 Debt Service Suspension Initiative (DSSI)³ announced by the G20 (in which China is also a member) in November 2020 in connection with the difficulties caused by COVID–19, as DSSI effectively created a special environment similar to the Paris Club. Many emerging market debtors of China (e.g. Russia) are not in the programme as these are not countries with low income. Several countries concerned did not join the programme being concerned about the deterioration of their credit rating resulting from their participation becoming public (Stiglitz – Rashid, 2020). Moreover,

DSSI concerns official lending only because China changed the status of its state-owned banks and most of its development banks to non-official (commercial) in 2020, probably to avoid the inclusion of these portfolios (Yue – Nedopil Wang, 2020).

In approximately half of the Chinese sample, there were ‘default events’ (‘cross-default clause’) not related to repayment in themselves, which concerned government measures conflicting Chinese economic interest in the broader sense (covering actions from disappropriation, changes in economic policy and conflict of interest specified completely in general). The costs of the changes in economic policy are also transferred to the debtors, connected perhaps with an acceleration condition, which means a payment obligation preceding the deadline incorporated in the contract. Such conditions are also widespread in the Western sample, but with not so general wording; they, therefore, significantly extend the creditor’s toolbox. The termination of diplomatic contacts with China, for example, was a termination event in every Chinese contract

There has been no comprehensive study about the meeting of the contractual conditions and the legal disputes; most pieces of information come from a couple of case studies (e.g. Bon – Cheng, 2020), reports (e.g. CABRI, 2021; Yue – Nedopil Wang, 2021) and anecdotal sources. It may be said, in any case, that the majority of the contracts stipulate Chinese law and courts for legal disputes (Jia, 2022); however, for example, English law prevails in the contracts of the China Development Bank. The contracts of the Western sample most frequently stipulate London or New York law and courts, which is not surprising; however, there are few direct experiences about the operation of the Chinese legal authority for apparent reasons: this is another uncertainty.

The previously described contractual ‘over-insurance’ also indicates that China uses the tool of debt relief most rarely, even in the case of emerging markets and developing economies. Data on this subject is also rather deficient. Between 2018 and 2020, we know 96 such debt relief actions, which, based on the estimates, concerned 2% of the volume, and it was only used for interest-free loans (Acker et al., 2020; Yue – Nedopil Wang, 2020). According to another summary, the Chinese creditor, in most cases, does not reduce the entire principal debt (it is not a so-called ‘haircut’); it only waives arrears and repayments in default (Bon – Cheng, 2020). China does not have an official debt relief procedure (which the Paris Club has); therefore, debt reliefs are always performed bilaterally on an ad-hoc basis (often applied not to a creditor but a debt only). All in all, interest-free loans of the 15 least developed African debtors were waived in October 2020 (Yue – Nedopil Wang, 2021).

China also makes certain attempts to develop the fiscal sustainability of the debtor countries: In 2019, the Ministry of Finance of the People’s Republic of China issued a recommendation to its institutions titled ‘Debt sustainability framework for countries participating in the Belt and Road Initiative’ wishing to strengthen the analysis of sustainability and risk management (Ministry of Finance of the People’s Republic of China, 2019). Based on the presently known case studies and data, with the exception of a few cases (e.g. Hambantota International Port in Sri Lanka) China has not really resorted to direct asset seizure (see e.g. Acker et al., 2020). The issue of the so-called ‘sovereign immunity cause’, namely that if a state suffers sovereign bankruptcy, it might have to relinquish its economic sovereignty to China, was raised regarding the case of Nigeria in 2021. However, it is rather the case of giving up immunity

before the courts in special cases (the given country becomes enforceable) (Igwe, 2020). The most powerful tool used by the Chinese creditors to date was that they did not disburse additional amounts to continue projects. Although China's behaviour in restructuring actions may be considered a relatively grey zone, presently, there is no generally accepted proof of an outright hostile approach, a 'debt-trap diplomacy' – intentionally rendering the repayment of loans more difficult for political advantages (Chellaney, 2017).

Loans extended to emerging markets and developing economies by China, therefore, serve a twofold purpose: to make a profit, which is deemed a usual creditor intention, on the one hand – even if it is performed in a manner more detailed, stricter, 'more secured' than it is usual in the West – and, on the other hand, it allows applying political pressure, 'soft power'. Therefore, we cannot state that China uses the 'debt-trap diplomacy' and, based on the case studies, it does not seem to be a malicious partner in the debt settlement proceedings either.

It is certain, in any case, that the condition system explained in this chapter, the lack of transparency to this extent, and the very strong collaterals do not support more uniform international debt settlement procedures. It has been, of course, already recognized by the academic literature. The following chapter will summarise the proposals to solve the problem and present our perspective.

KEY PROPOSALS TO MITIGATE THE RISKS

The dispute related to sovereign risk management arose again in connection with the debt portfolio caused by the fiscal stimuli following the COVID-19 pandemic and the growth in the percentage of non-payment.

According to the calculations of IMF, 60% of the developing economies with low income may face serious problems already in 2022 (Georgieva – Pazarbasioglu, 2021); therefore, the issue is acute. The main problem is still the lack of a uniform global framework for the management of sovereign risks. Several proposals were made under the aegis of IMF in the past decades for the establishment of a uniform institution system, with moderate success to date, maybe also because of a lack of interest on the part of superpowers (Bethlendi, 2018).

This latter is also typical of the Chinese behaviour, as the lack of a rule system and the status quo established along the crumbliness of the governing processes is actually in their interest for the time being. Several proposals were nevertheless made to draw the Chinese and Western institution systems closer; moreover, China also took steps in this direction. The BIS membership of the Chinese central bank, partial data provision to OECD, and not too intensive cooperation with the Paris Club are among these steps (Gelpern et al., 2021). The DSSI participation of China is already a clear step forward; however, its extent will only be seen in practice.

The – principle level – proposal for the solution, which seems to be the simplest for the uniform sovereign debt management framework, was made by the United Nations back in 2012 and had outstanding importance, as China is also a member state and approved it. The United Nations Conference on Trade and Development (UNCTAD) elaborated the principles of responsible sovereign lending (Principles On Promoting Responsible Sovereign Lending and Borrowing, UNCTAD, 2012).

Based on the UNCTAD principles and the unfavourable experiences of that time (e.g. the case of Greece or Argentina), the UN established the principles of restructuring

processes (Basic Principles on Sovereign Debt Restructuring Processes) and adopted them by the resolution of its General Assembly No. A/RES/69/319 (10 September 2015) (United Nations, 2015a). These principles essentially resonate with the UNCTAD document highlighting transparency, the equality of creditors (in fact, the ban on preferential treatment, seniority), sovereign immunity and qualified majority decision making. Collective compliance with the principles would eliminate most of the risks related to Chinese sovereign lending. Practical implementation, of course, was not detailed by the materials; therefore, only the theoretical framework was set up. It is particularly interesting regarding the resolution that China – already aggressively into market acquisition – voted yes, and the six countries voting no (United Kingdom, Israel, Japan, Canada, Germany, USA) were the dominant sovereign creditors of the Western world. They reasoned that the approved principles would increase economic uncertainty (United Nations, 2015b). The principles have not been applied in practice since then.

Several proposals were made to align Chinese lending with the Western system in the indebtedness wave caused by the COVID–19 pandemic. One of the first proposals was made by the International Institute of Green Finance operating in Beijing (Yue – Nedopil Wang, 2021), with green aspects considered, resulting from the nature of the Institute. In the opinion of the Institute, China should perform a certain volume of debt relief (in the form of a ‘haircut’, quasi debt write-off) for the countries in trouble, in exchange for which it would expect the greening of the given projects and climate protection targets. Furthermore, the Institute proposes closer cooperation with the Western institution system (IMF, World Bank, G20) and a significant increase in transparency.

A position was taken up in one of the key issues, aligning with the Paris Club, on behalf of The Stimson Center think tank (USA) (Rieffel, 2021). The author emphasizes the DSSI initiative of G20 from which a permanent framework should be established; in his opinion, China would follow the rule system of the Paris Club without joining it formally. The qualification of the loans of the China Development Bank and the Export-Import Bank of China as official instead of commercial loans would be essential (although China transformed them in connection with DSSI precisely to avoid its loans being subject to the initiative). Finally, it is interesting that it urges the leadership of the USA to join the financing of the countries in debt to China and in trouble (bilaterally and via IMF) as a kind of ‘soft power’ fight. The conclusion is that China is unlikely to become a member of the Paris Club in the foreseeable future; however, it could be urged to align by making the G20 initiative permanent (and with the pressure of the USA on the other side).

The latest relevant proposal package with nine concrete proposals was received from the sovereign debt working group of the Bretton Woods Committee (Bretton Woods Committee, 2022), and it focused on the (data and procedural) issues of transparency specified by many in connection with the crisis (e.g. Stiglitz – Rashid, 2020; OECD, 2021). In the working group’s opinion, the primary issue would be the establishment of a worldwide uniform sovereign loan database. To this end, the first step would be to agree on a minimum reporting requirement system based on consensus (the material provides a concrete proposal concerning this). The debtors could be encouraged to report with some positive or negative tool: e.g. potential debt relief or some kind of a fine for reporting failure. They find the involvement of China inevitable. As the IMF and the World Bank already have an

existing database, the development could be integrated into one of these.

Our opinion is that any uniform framework may only be established realistically with China, the largest creditor involved. In this case, it is probable that not only the Western processes and solutions will be implemented, but the Chinese interests will also be taken into account. One solution in law enforcement could be cooperation with some forums of the UN (once the principles of 2015 were already approved), for example, with the United Nations Commission on International Trade Law (UNCITRAL), Working Group III: Investor-State Dispute Settlement Reform), aligning the Chinese practice with the Western standards (UNCITRAL, 2022). The enforcement of the 2012 (UNCTAD, 2012) and 2015 principles (United Nations, 2015b) would also be an essential step.

The issue of transparency is of primary importance, as the database currently deemed most precise was set up based on nine other databases and their own estimates. That is an issue to be solved in any case; the proposals of the Bretton Woods Committee should be followed in this respect. China should ease on the presently stringent, overinsured contractual framework, and in the international cooperation, it should align with the Paris Club along a certain extended DSSI (regarding not only the countries with low income), although in respect of the international sovereign lending system the best solution would be joining with a compromise – which move is certainly not expected in the short run.

CONCLUSIONS

We asked three questions in the study. The first was about the key features and trends of China's sovereign loans to emerging markets and developing economies bilaterally and

in other constructions. Our main finding is that having exploited the opportunities provided by the crisis of 2008, the Chinese state consciously began its expansion on the international sovereign loan market well before its official announcement, with great success: by 2014–15, it became the biggest sovereign creditor of the world. It disburses the loans via several rather intransparent channels, and the majority go to the emerging markets and countries with low income. After the early boom, an increasing number of non-performances is related to the Chinese loans in the recent years, and the non-performing portfolio began a trend-line increase in the past four-five years, which deteriorated further by the COVID–19 pandemic.

Our second question examined the differences between the conditions of the Chinese sovereign loans and the usual Western ones, as well as the related additional risks. Analyzing the different conditions of the loans, we may state that there are significant differences: confidentiality is significantly stricter than the usual on the part of the debtors, revenues channelled away by special security accounts, 'No Paris Club' clauses, termination rules interpretable as a blanket rule (e.g., cross-default), and the seniority of the Chinese debtor. The purpose is twofold: to make a profit secured by strong collaterals in line with the usual creditor intention and, if necessary, "soft power" influence. China does not explicitly use 'debt trap diplomacy', and based on the case studies, it does not seem to be a malicious partner in the debt settlement proceedings either. Despite that, these differences from the Western tradition mean serious risks in multilateral debt settlements, they could even block settlements in the worst case and make a sovereign bankruptcy wave more serious.

Finally, we examined the proposals made to mitigate the situation and analyzed which

could be used. We believe that any uniform sovereign debt management framework may only be established realistically with China, the largest creditor involved, with the Chinese viewpoints also considered. The already approved UN principles could help in this, for which China also voted yes, should ‘only’ be adhered to. The issue of transparency is of primary importance; the uniform minimum reporting requirement system of the proposals of the Bretton Woods Committee could work

under the aegis of IMF, the World Bank or even the OECD. China should ease its apparently overcollateralized contractual clauses, and in the international cooperation, it should align with the Paris Club via a certain extended DSSI (regarding not only the countries with low income), and it should even join the Paris Club. Unfortunately, we do not see either that or the establishment of the above-mentioned global sovereign debt management framework probable in the near future. ■

NOTES

- ¹ The publishing of the study was supported by the Kálmán Széll Public Finance Research Group of the University of Public Service.
- ² To define this country group we use the ‘Emerging Market and Developing Economies (EMDE)’ concept of the IMF and the World Bank, similarly to the database of Horn et al. (2021),
- in which interpretation the term of ‘developing economies’ means developing countries with low income.
- ³ Within the framework of DSSI the suspension of the debt service payments of bilateral government loans became possible for seventy three countries with low income (World Bank, 2021b).

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