

# China's Overseas Lending: From Boom to Bust

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# This lecture is based on my work with Sebastian Horn and Christoph Trebesch

Horn, Reinhart, Trebesch: **China's Overseas Lending**, NBER WP 25060, July 2019 published in *Journal of International Economics*, November 2021

Horn, Reinhart, Trebesch: **Hidden Defaults**, *AEA Papers & Proceedings 2022a*

Horn, Reinhart, and Trebesch **China's Overseas Lending and the War in Ukraine**, VoxEU, April 2022b.

Horn, Parks, Reinhart, Trebesch: **China as an International Lender of Last Resort**, WB Policy Research Working Paper 10380 forthcoming in *AEA Papers & Proceedings 2023*

I also refer extensively to:

Gelpern, Horn, Morris, Parks, Trebesch: **How China Lends**, *Economic Policy*, 2023

# A vast research and surveillance gap

While China's dominant footprint in world trade and global output is well known, its expanding role in international finance is poorly understood. Apart from its massive scale, the most notable feature of China's capital exports is its opacity. Data are scarce and the process of lending is not transparent. This helps to explain why relatively little work exists on China's large-scale cross-border investments. In the past five years, we have helped fill this gap.

# China's overseas lending

- The Chinese government and Chinese state-owned entities have provided record amounts of loans to finance infrastructure and energy projects along the Belt and Road
- This lending boom has transformed China into the world's largest official creditor, and into one of the most important players in international debt renegotiations
- The academic literature has previously focused primarily on Western creditors (bondholders & the Paris Club). China's growing financial footprint has created important knowledge gaps:
  - Magnitudes and drivers of lending
  - How does China lend?
  - How does China deal with debt distress?

# Roadmap for this lecture

## 1) China's overseas lending boom (focus will be on South-South loans rather than South-North portfolio flows)

- Drivers, magnitudes and recipients
- How China Lends: Loan terms
- Confidentiality clauses and the rise of **hidden debt**

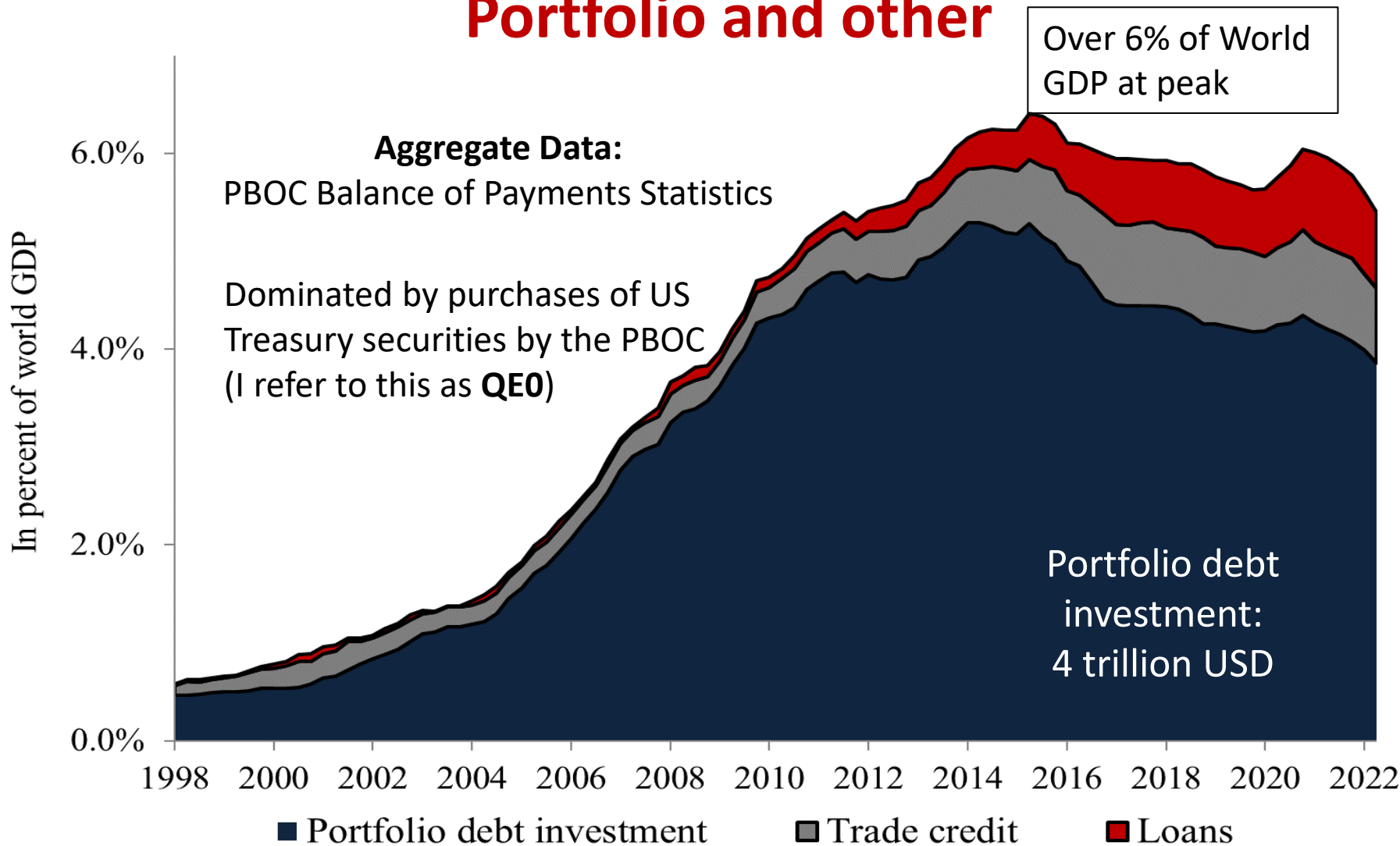
## 2) The lending bust (where we are now and where we are heading)

- Debt distress in developing countries and the **sudden stop** in Chinese lending
- China's approach to debt restructuring
- China as an international lender of last resort

# **CHINA'S OVERSEAS LENDING BOOM**

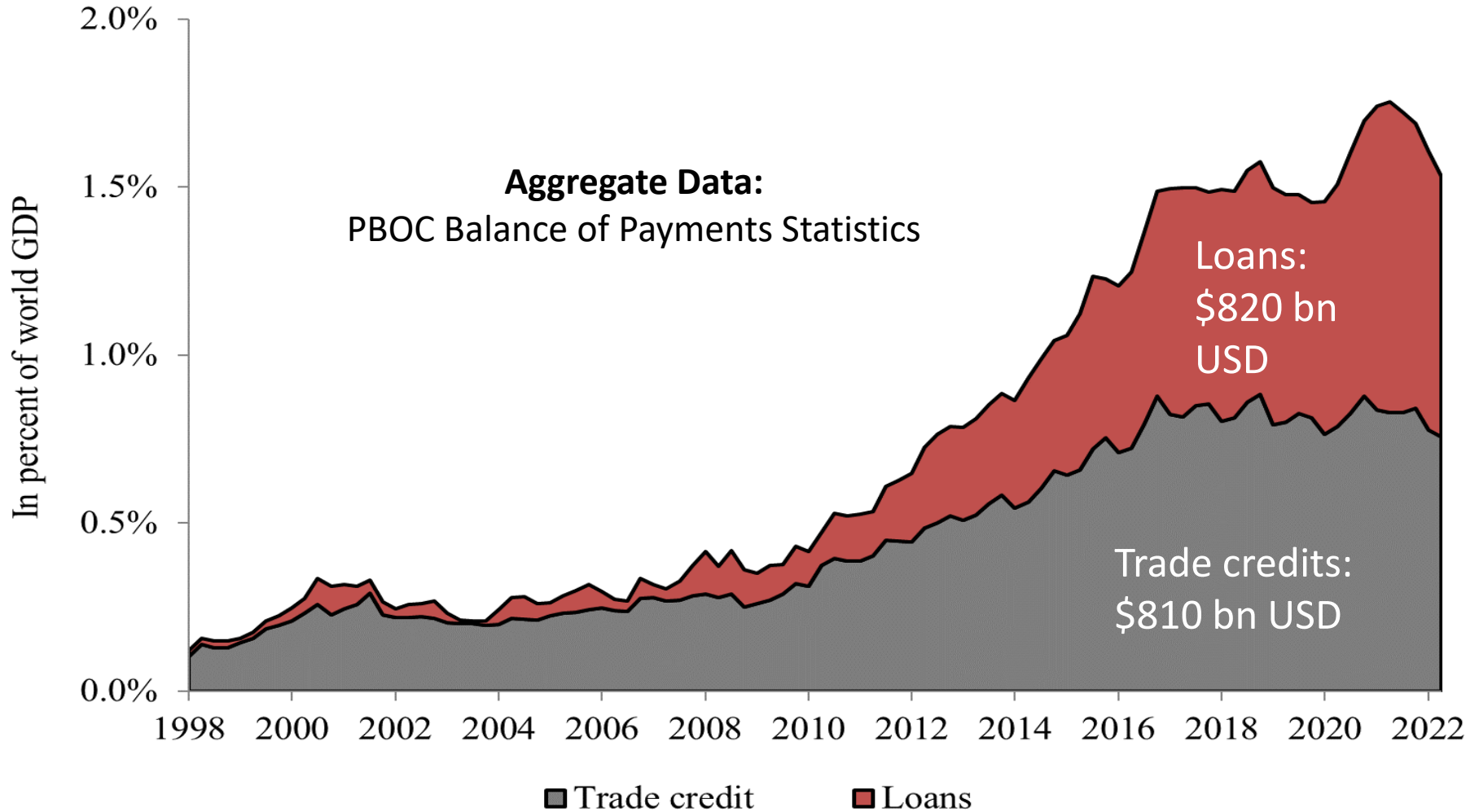
**Horn, Reinhart, and Trebesch (2019 and 2021)**

# China's overseas lending boom: Portfolio and other



Source: Horn, Reinhart, and Trebesch (2019 updated)

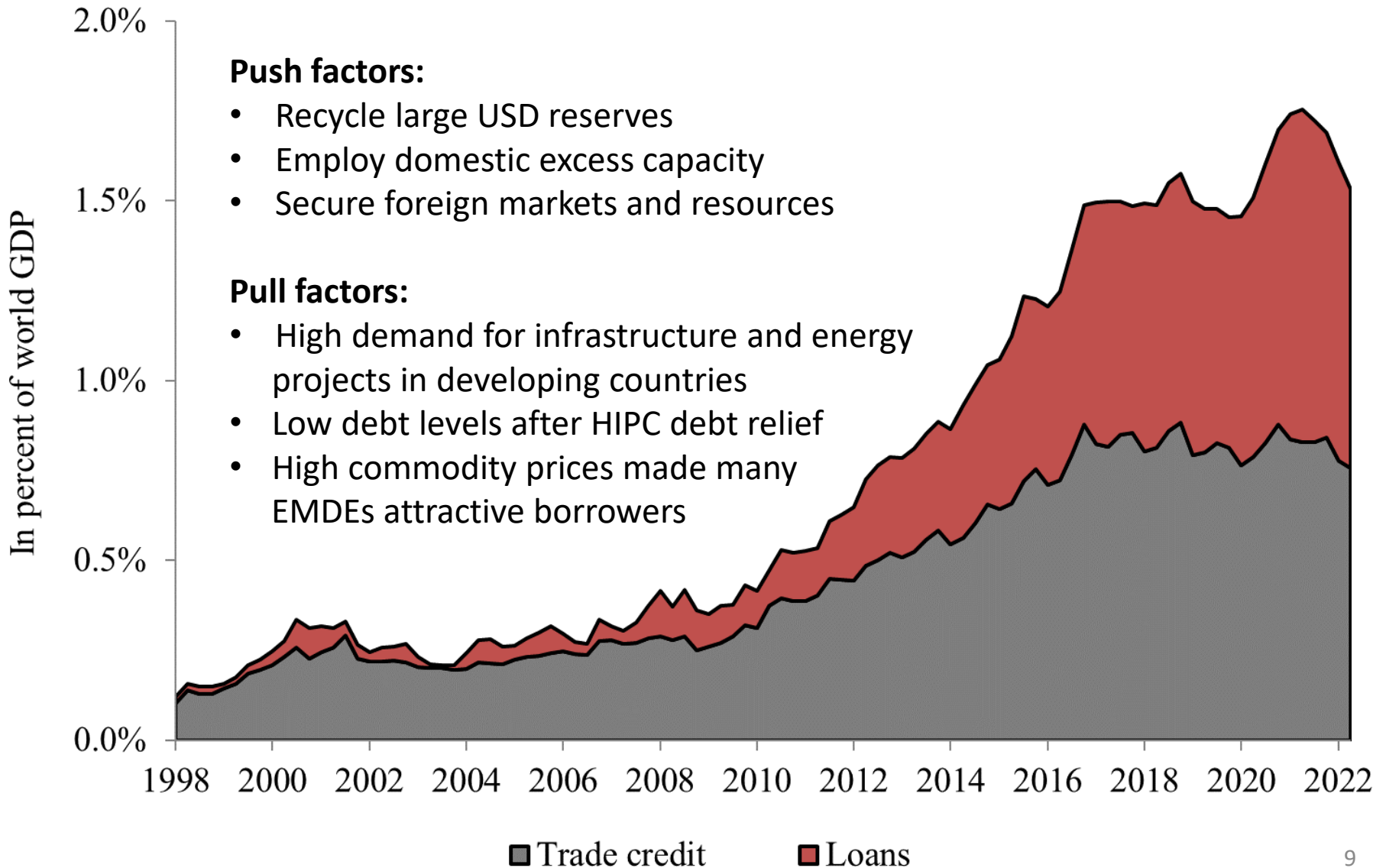
# China's overseas lending boom: South-South



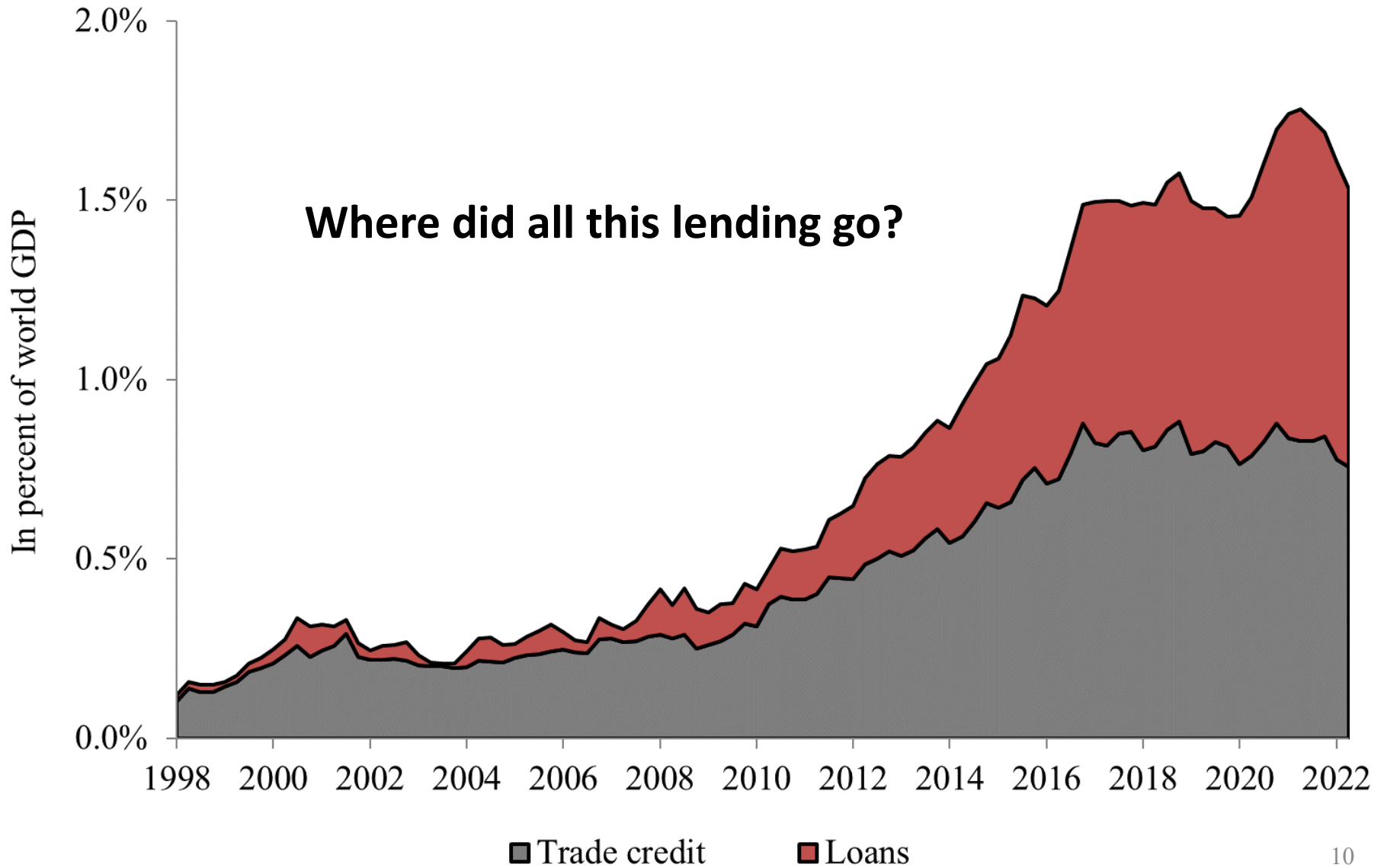
Source: Horn, Reinhart, and Trebesch (2019 and 2021 updated)



# China's overseas lending boom: The drivers



# China's overseas lending boom



# We created a micro-level dataset of Chinese lending

## Existing data sources

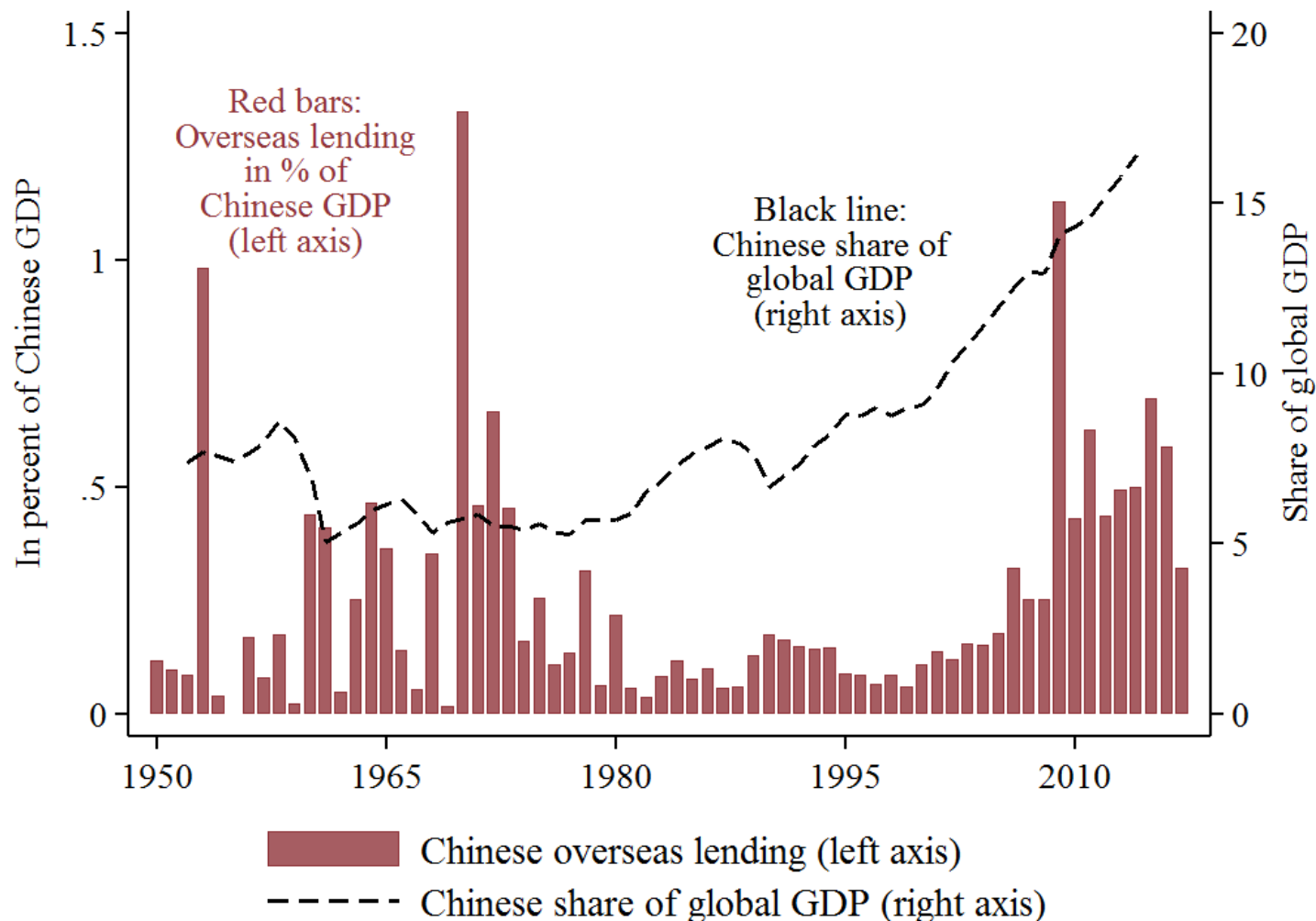
- William & Mary AidData:
  - Chinese Official Finance Dataset
  - Chinese Diplomacy in Asia Data
- Inter-American Dialogue Database
- Johns Hopkins China-Africa Research Initiative
- BU China Global Energy Finance
- Lowy Institute:
  - Chinese Aid in the Pacific
  - Pacific Aid Map
- Dozens of debtor and creditor-specific resources
- Dozens of sources for pre-2000 Lending

→  
Clean  
&  
Merge  
→

## Our merged database

- **5000 Chinese official loans and grants from 1950 to 2020**
- **700 billion USD total volume**
- Gathered terms of lending, repayments schedules & currency denomination

# China has always lent abroad ...but it was not such a large economy



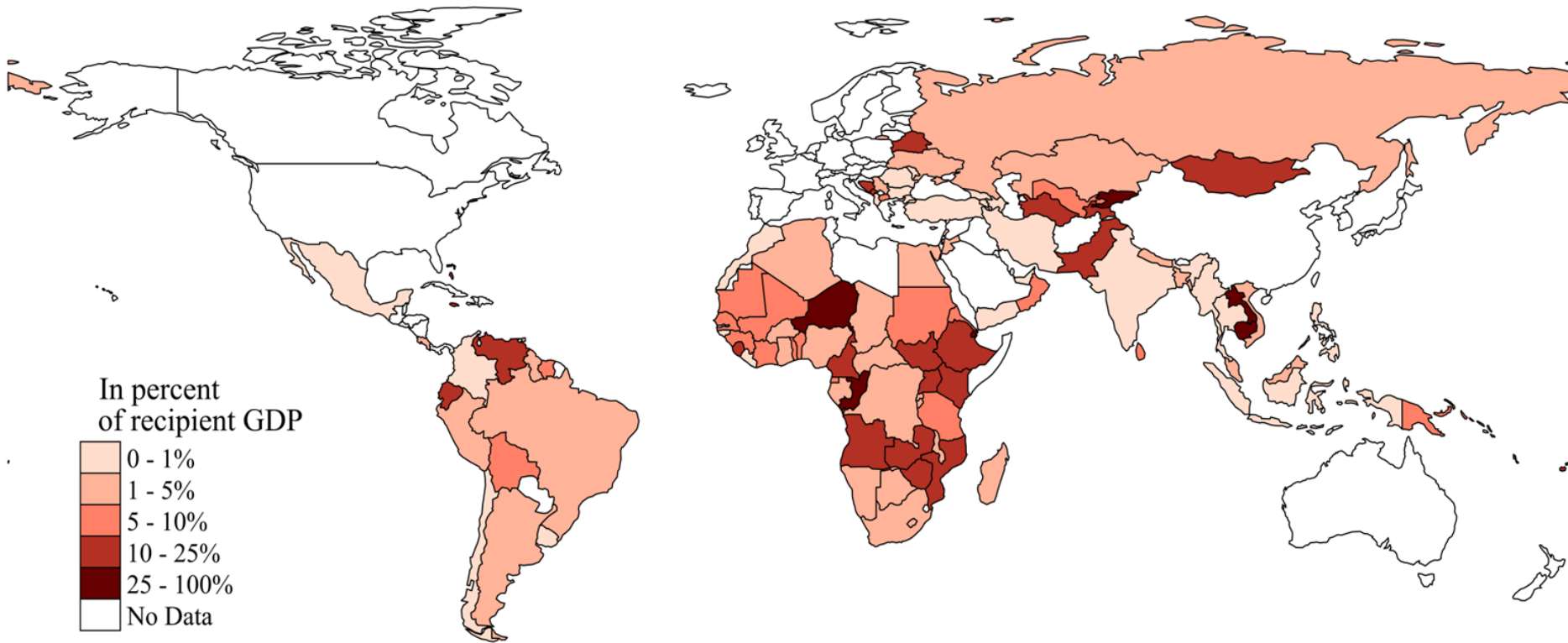
Source: Horn, Reinhart, and Trebesch (2019 and 2021)

# ...and it did not lend on such a global scale



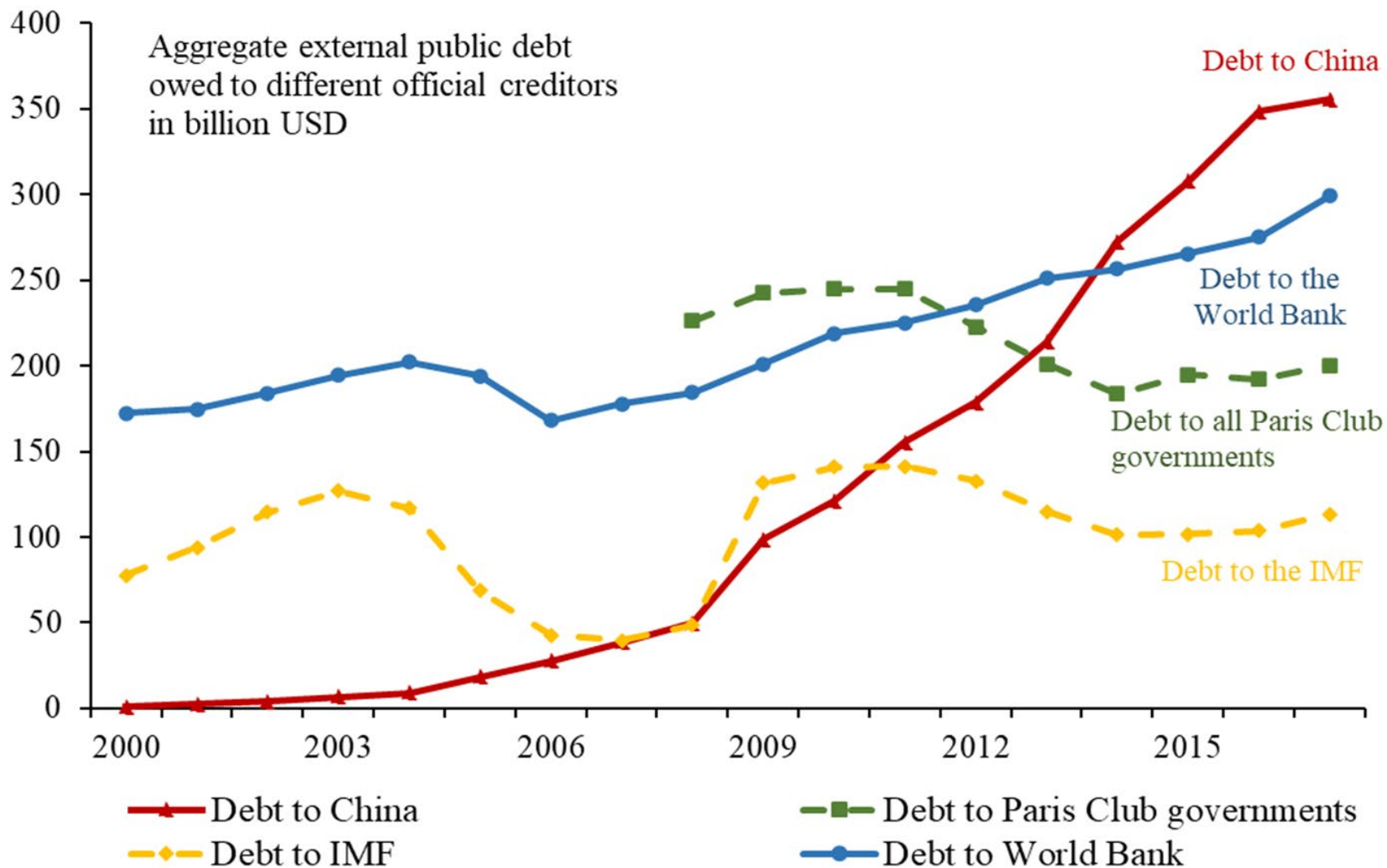
Source: Horn, Reinhart, and Trebesch (2019 and 2021)

# Debt owed to China as a percent of GDP



External public and publicly-guaranteed debt in percent of debtor GDP  
Source: Horn, Reinhart & Trebesch 2021

# China is the world's largest official creditor



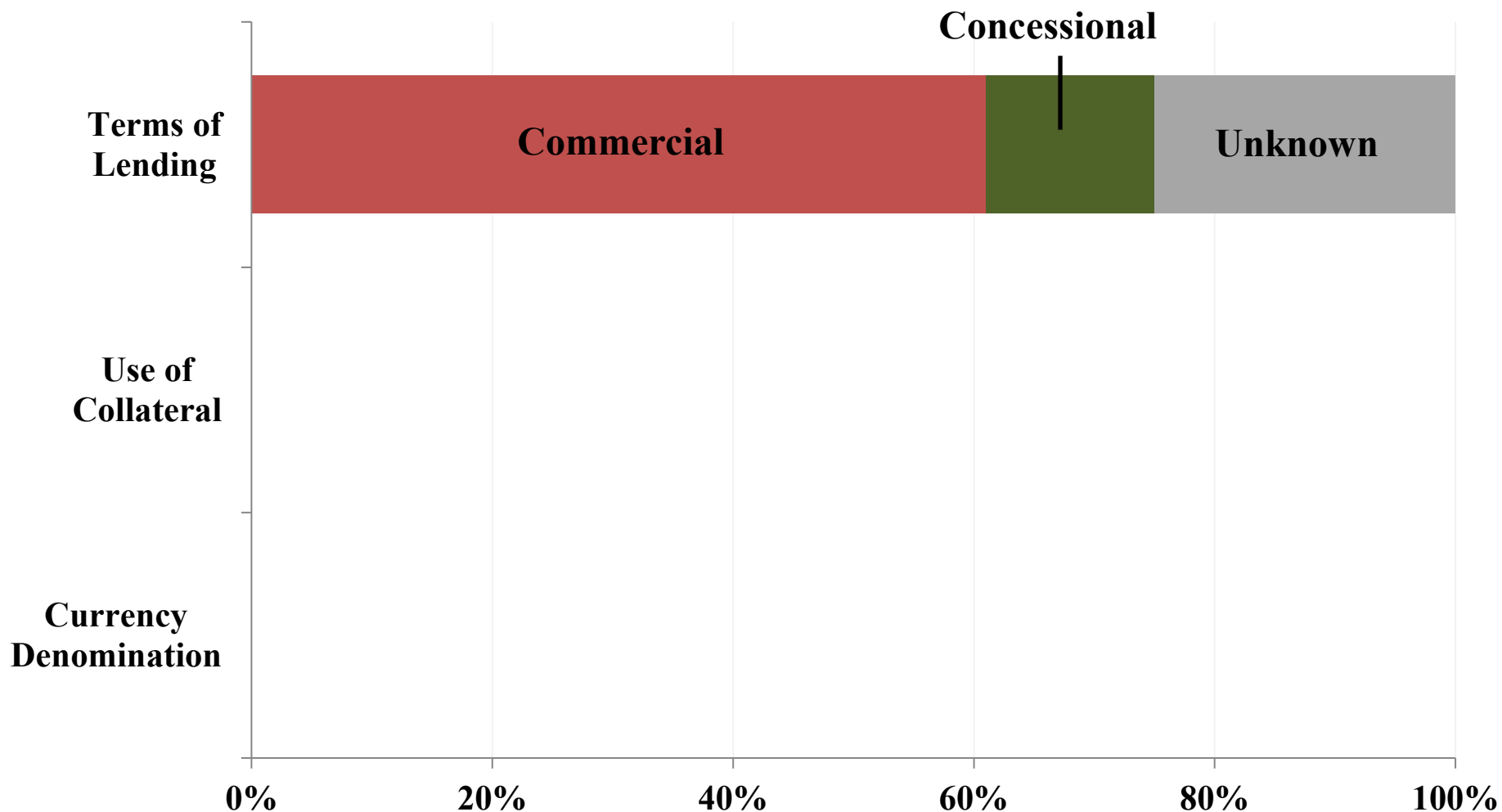
Source: Horn, Reinhart, and Trebesch (2021).

## **HOW CHINA LENDS**

**Like no other official creditor (since the 19<sup>th</sup> century)**

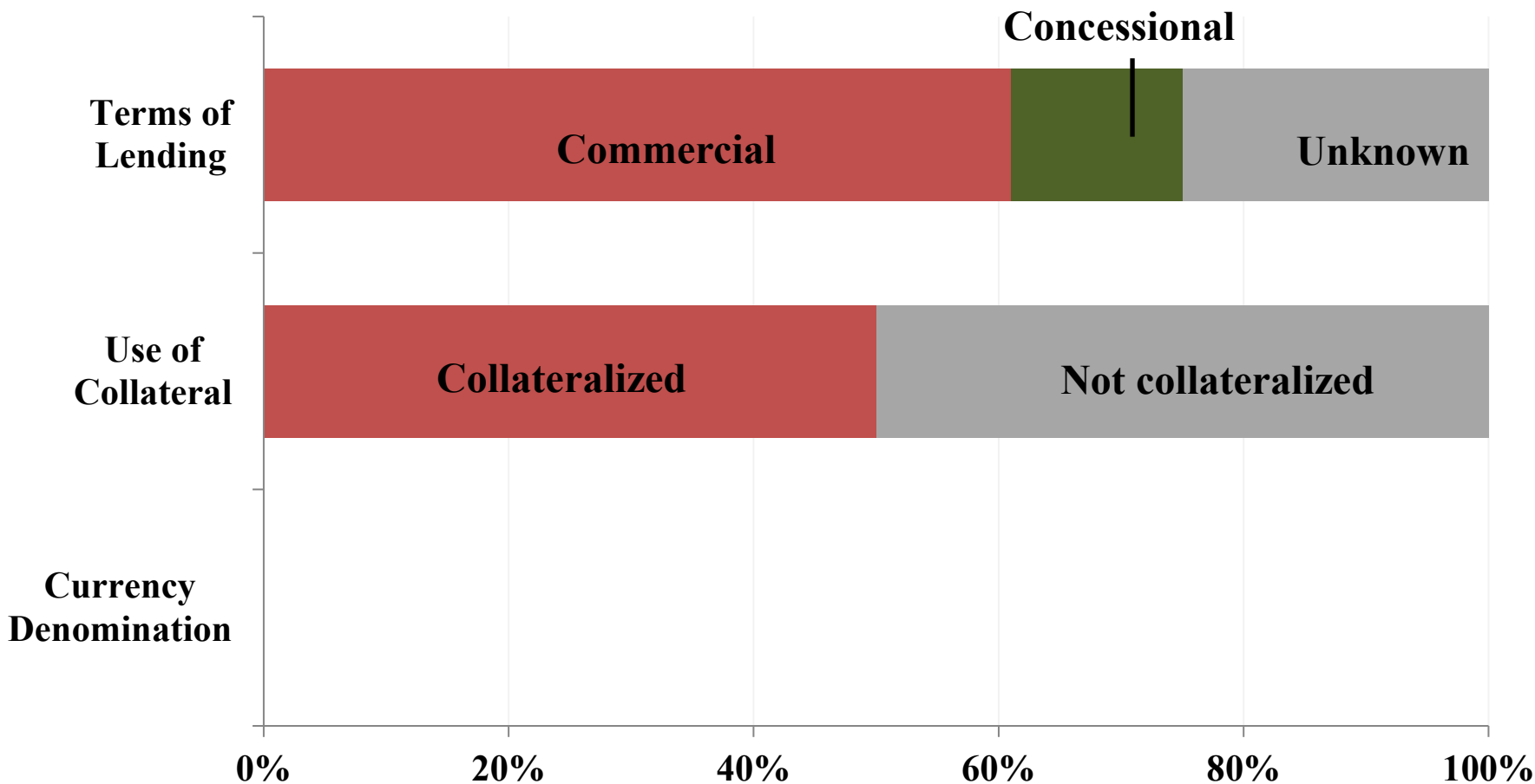


# Unlike other official creditors, Chinese official lending is mostly on commercial terms

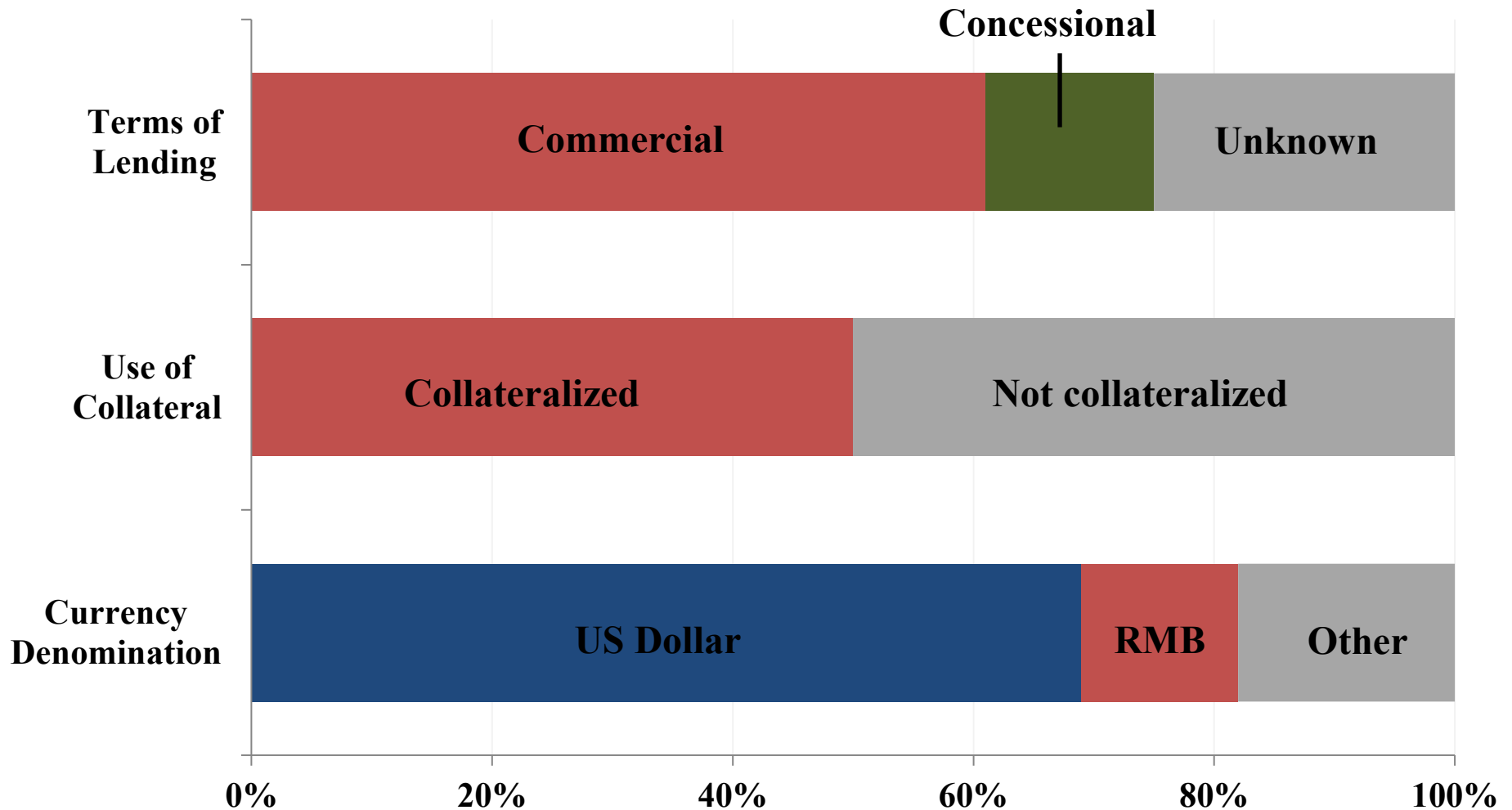


Horn, Reinhart and Trebesch (2021); Bräutigam & Gallagher (2014); Gelpern et al. (2021)

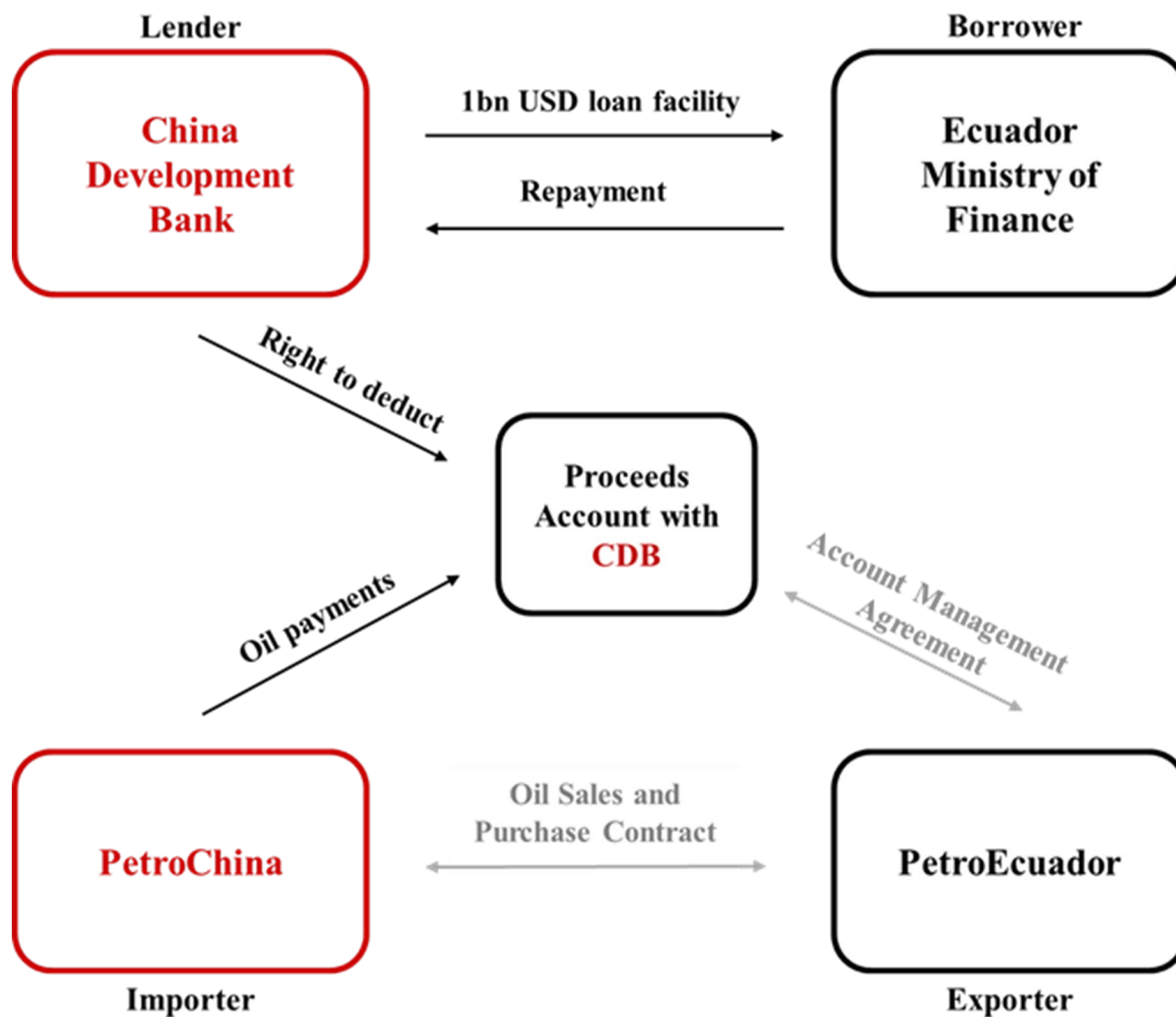
# Unlike other creditors (official and private), around 50 percent is collateralized...



# ... and most loans are denominated in USD



# Collateralization through off-shore bank accounts: Ecuador example



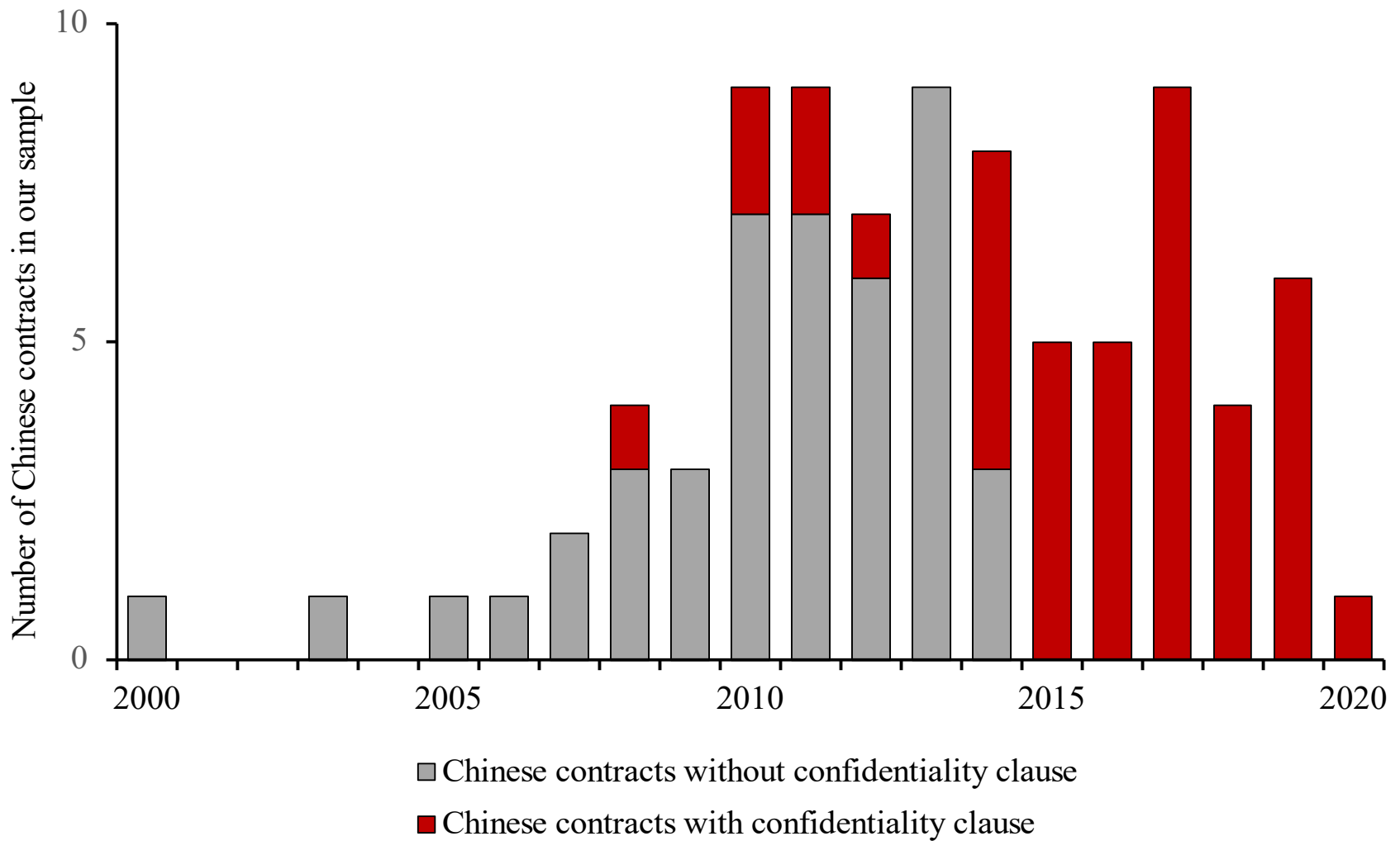
Source: Gelpern et al. (2021)

## Unlike other creditors', Chinese contracts include broad confidentiality clauses

### Typical China EXIM Bank clause:

*“The Borrower shall keep all the terms, conditions and the standard of fees hereunder or in connection with this Agreement **strictly confidential**. Without the prior written consent of the Lender, the Borrower shall **not disclose any information** hereunder or in connection with this Agreement **to any third party unless required by applicable law.**”*

# Secrecy increased markedly since 2013



Source: Gelpern et al. (2021)

**Which is why the international community has  
been facing**

**THE ISSUE OF HIDDEN DEBT**

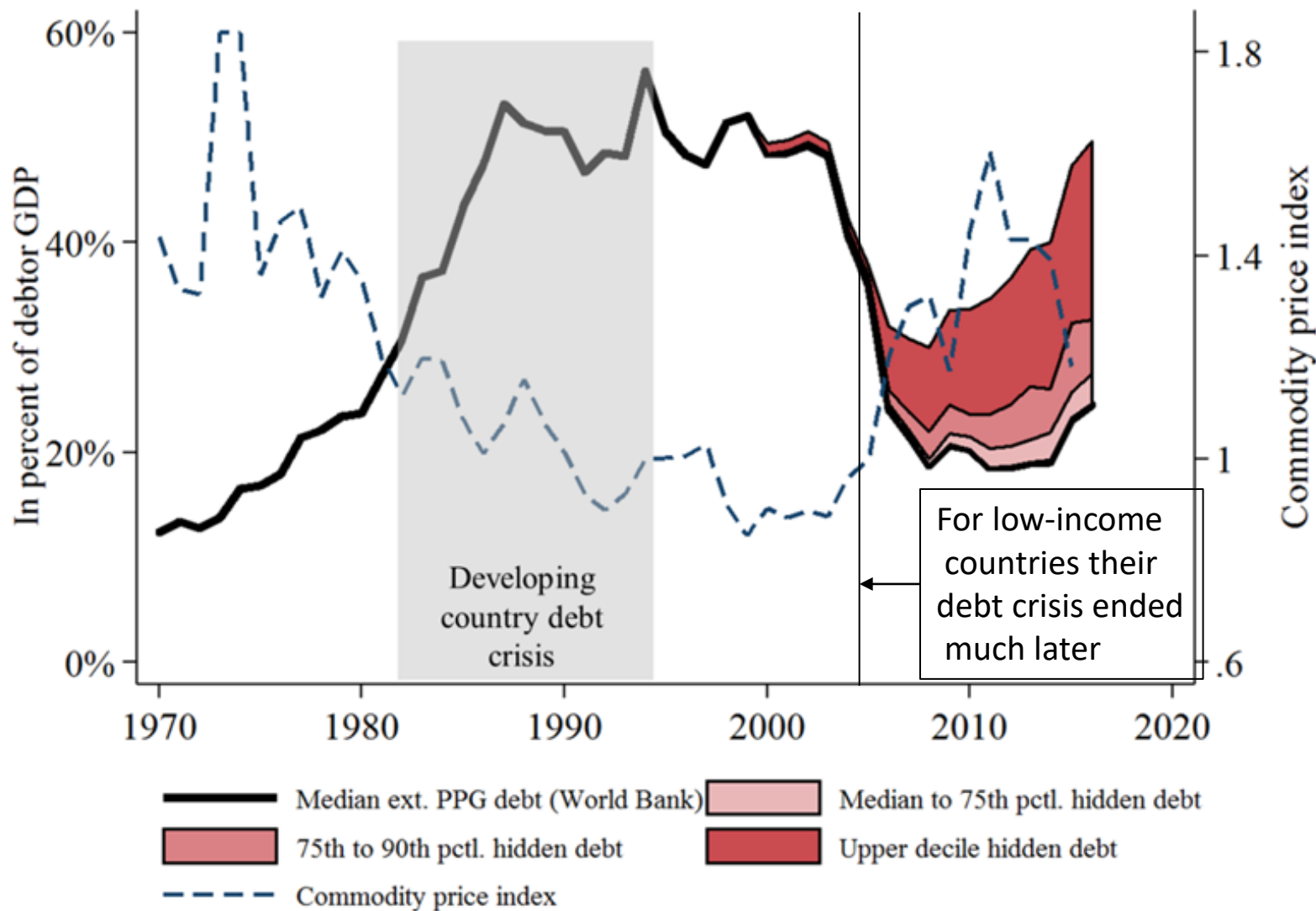
# Quantifying “hidden” debts: Horn, Reinhart, and Trebesch (2019 and 2021)

## How large is the under-reporting problem?

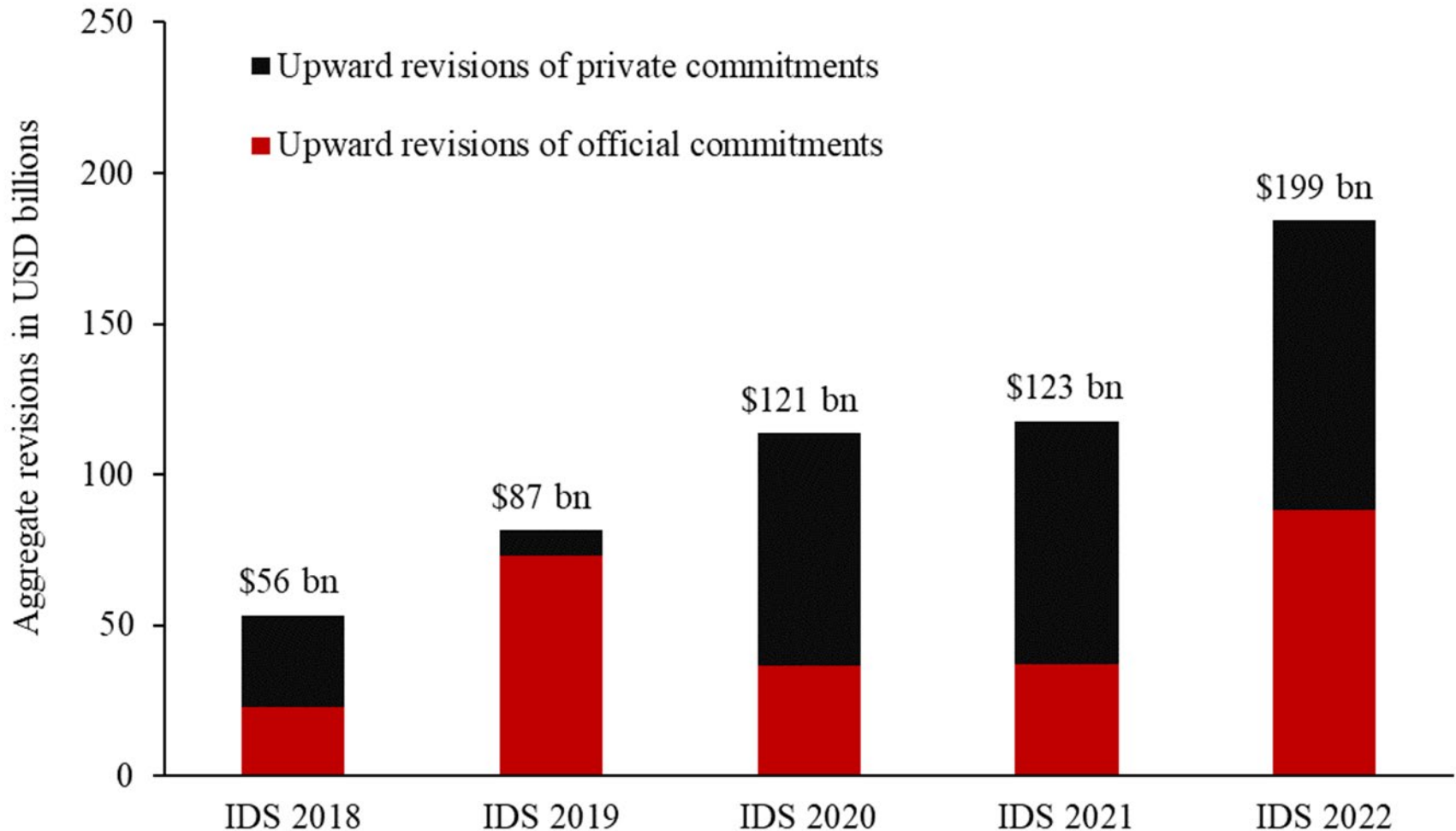
- **Debtor side:** Chinese lending coincides with reporting gaps in official debt statistics (loans to state-owned enterprises (SOEs), disbursement through contractors & funds)
- **Creditor side:** China not a member of OECD or the Paris Club; confidentiality clauses are strictly bilateral. Because it is “official” debt, it is off the radar screen of major credit rating agencies
- **Compare our loan data to those of World Bank Debtor Reporting System (DRS; IDS 2018)**



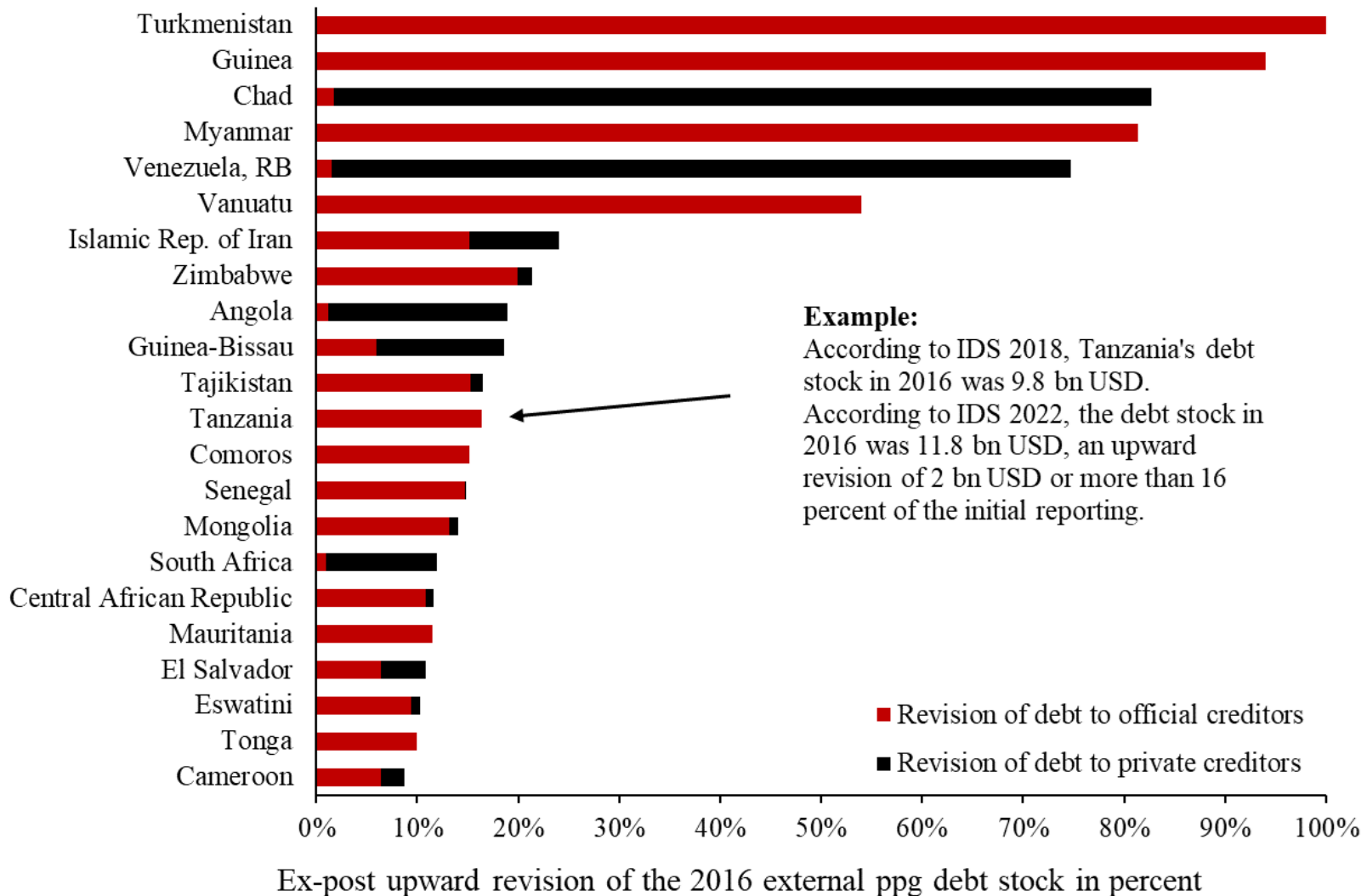
# 50% of Chinese lending during the boom years went unreported (HRT, 2019, 2021)



# ... the extent of *hidden debt* in the official databases has only been revealed very recently...



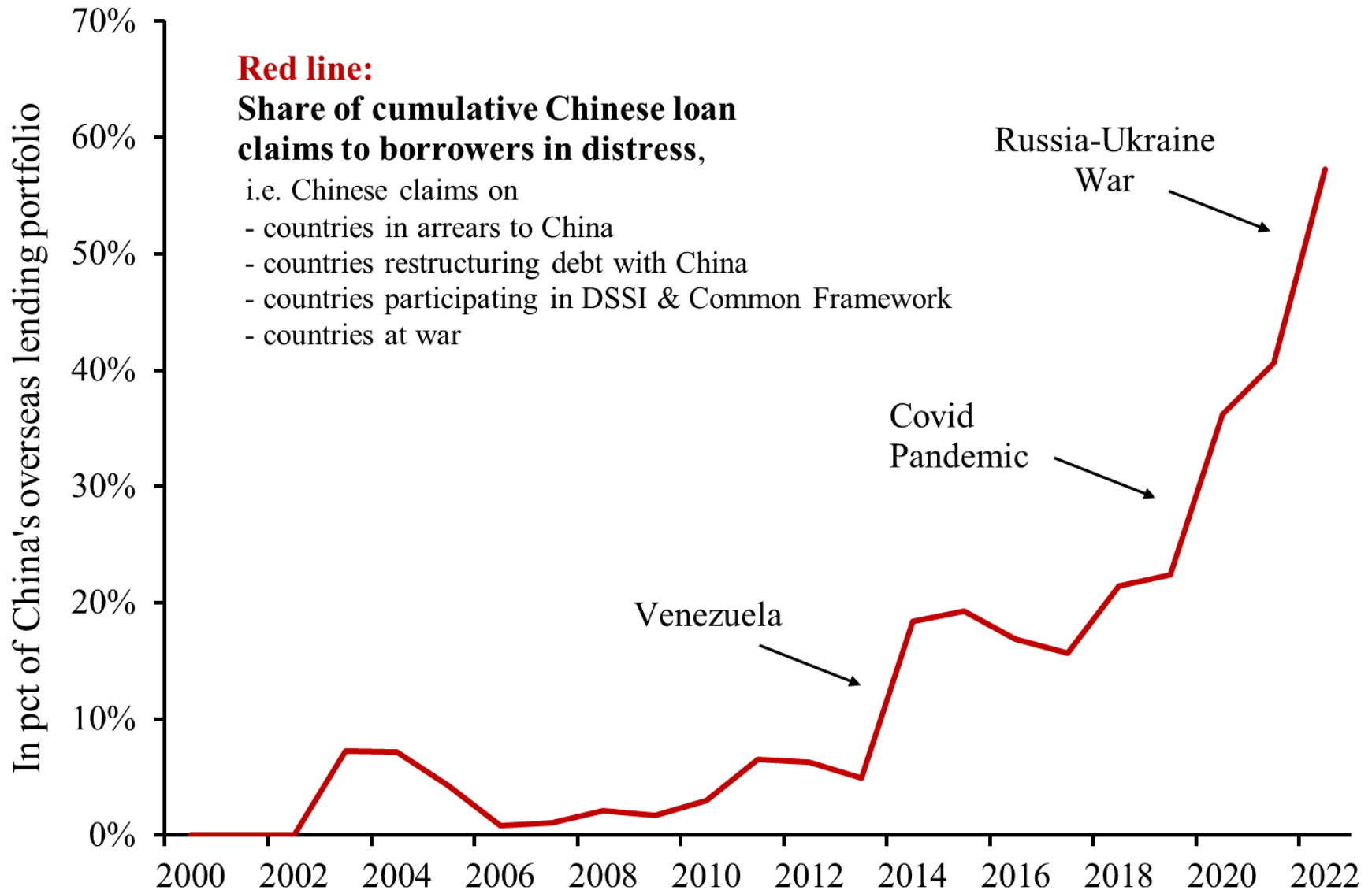
# ... leading to large ex-post upward revisions of debt statistics in recipient countries—often in the midst of a debt crisis and an IMF program



**The unfolding debt crisis in a rapidly growing  
number of EMDEs**

**FROM LENDING BOOM TO BUST (AGAIN, SEE  
REINHART AND ROGOFF, 2009)**

# The bust: Many debtor countries are now in debt distress...



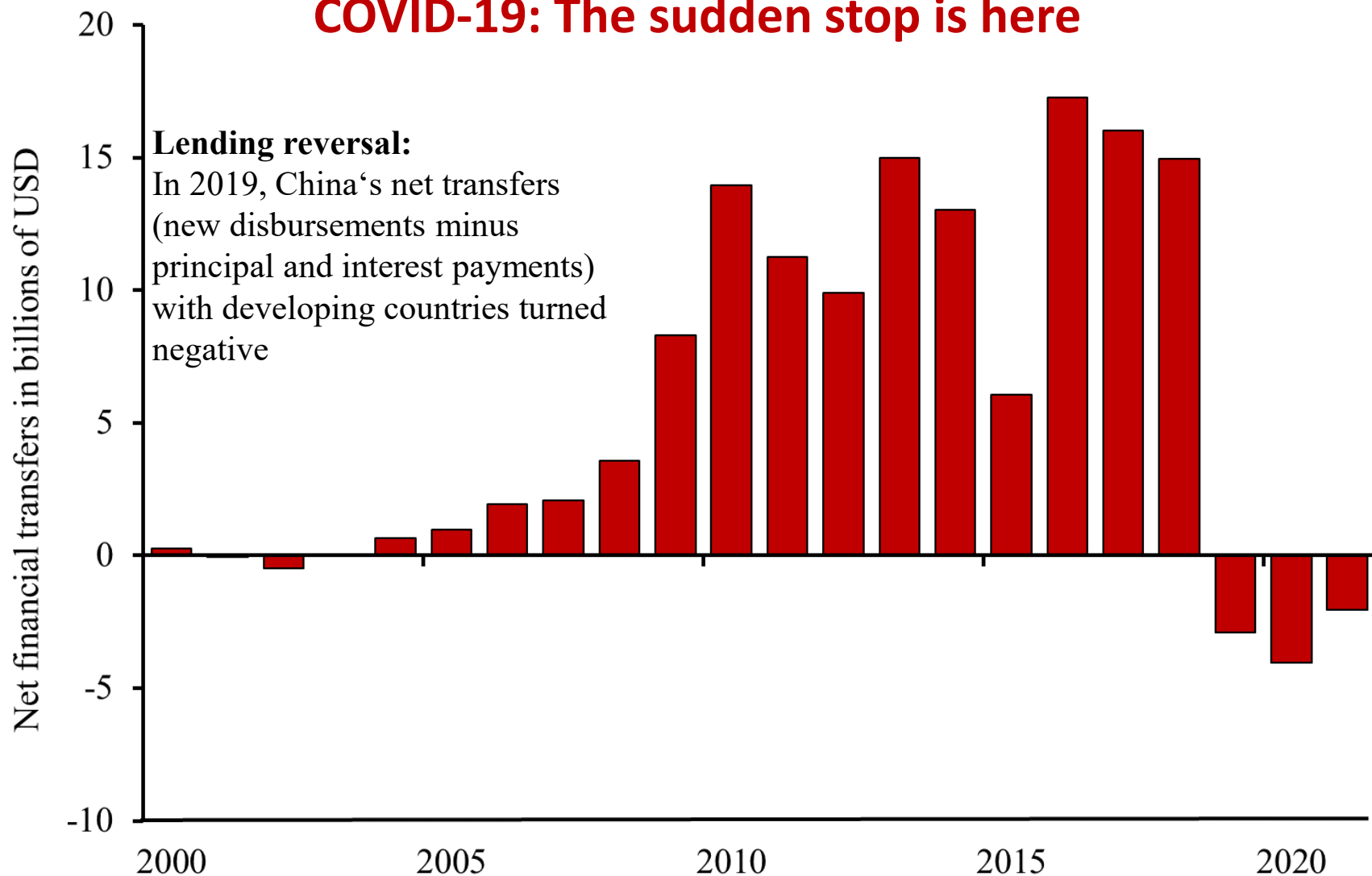
Source: Horn, Reinhart, and Trebesch (2022b)

# The loan portfolio of Chinese creditors is increasingly suffering from acute rating downgrades



Source: Horn, Reinhart, and Trebesch (2022b).

# New lending by Chinese official creditors declined even before COVID-19: The sudden stop is here



Source: Horn, Parks, Reinhart, and Trebesch (2023)

# Hidden defaults: Horn, Reinhart, and Trebesch (2022)

## **Loans to distressed borrowers are not necessarily in default:**

- Chinese banks use innovative contractual designs  
e.g., collateralization through foreign escrow accounts
- Repayment may occur “in kind” through commodities

**But some certainly are!** Yet, there is no systematic data on payment defaults or debt restructuring agreements with Chinese creditors

**Why do we know so little?** (i) not tracked by rating agencies. (ii) China not a member of the Paris Club, (iii) confidentiality clauses

→ **There are many “hidden” defaults and credit events (restructurings).** This is not unique to Chinese creditors, as opacity is also a feature of other non-Paris Club lenders (Saudi Arabia, UAE, among others )

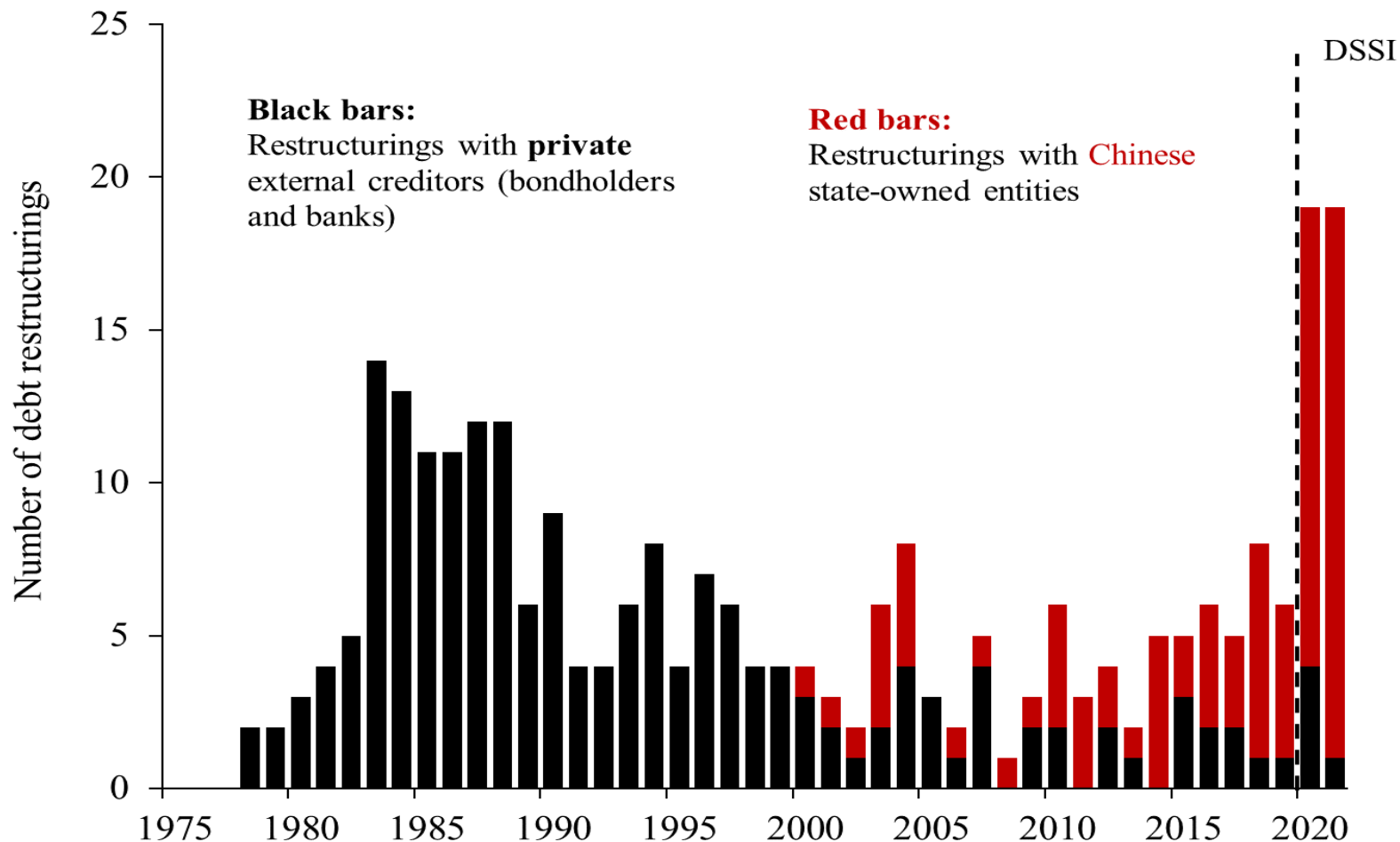


# How do Chinese creditors deal with debt distress in EMDEs?

## Main insights from Horn, Reinhart Trebesch:

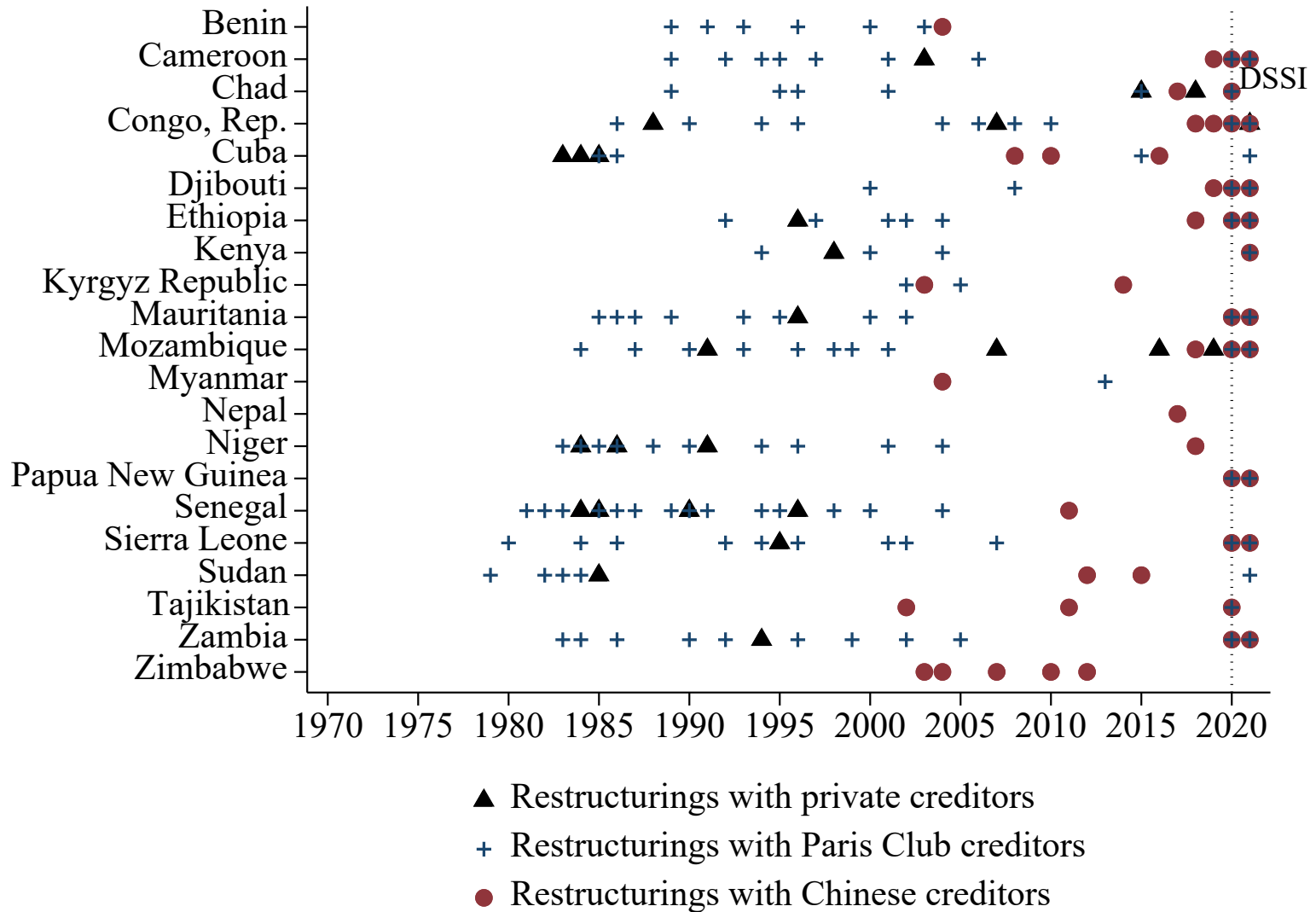
- Debt restructurings, when stakes are low (mainly LICs):
  - Debt restructurings with Chinese creditors now more frequent than with private creditors
  - Maturity & grace period extensions, hardly any nominal debt write-offs
- Rescue lending, when stakes are high (mainly EMs):
  - Liquidity support through PBOC swap lines
  - BOP loans from state-owned policy and commercial banks
- Approach reminiscent to Western creditors in 1980s and 1990s (“kicking can down the road”) and to recent Eurozone bailouts

## Sovereign debt restructurings with Chinese creditors are now more frequent than restructurings with private creditors



Source: Horn, Reinhart, and Trebesch (2022a)

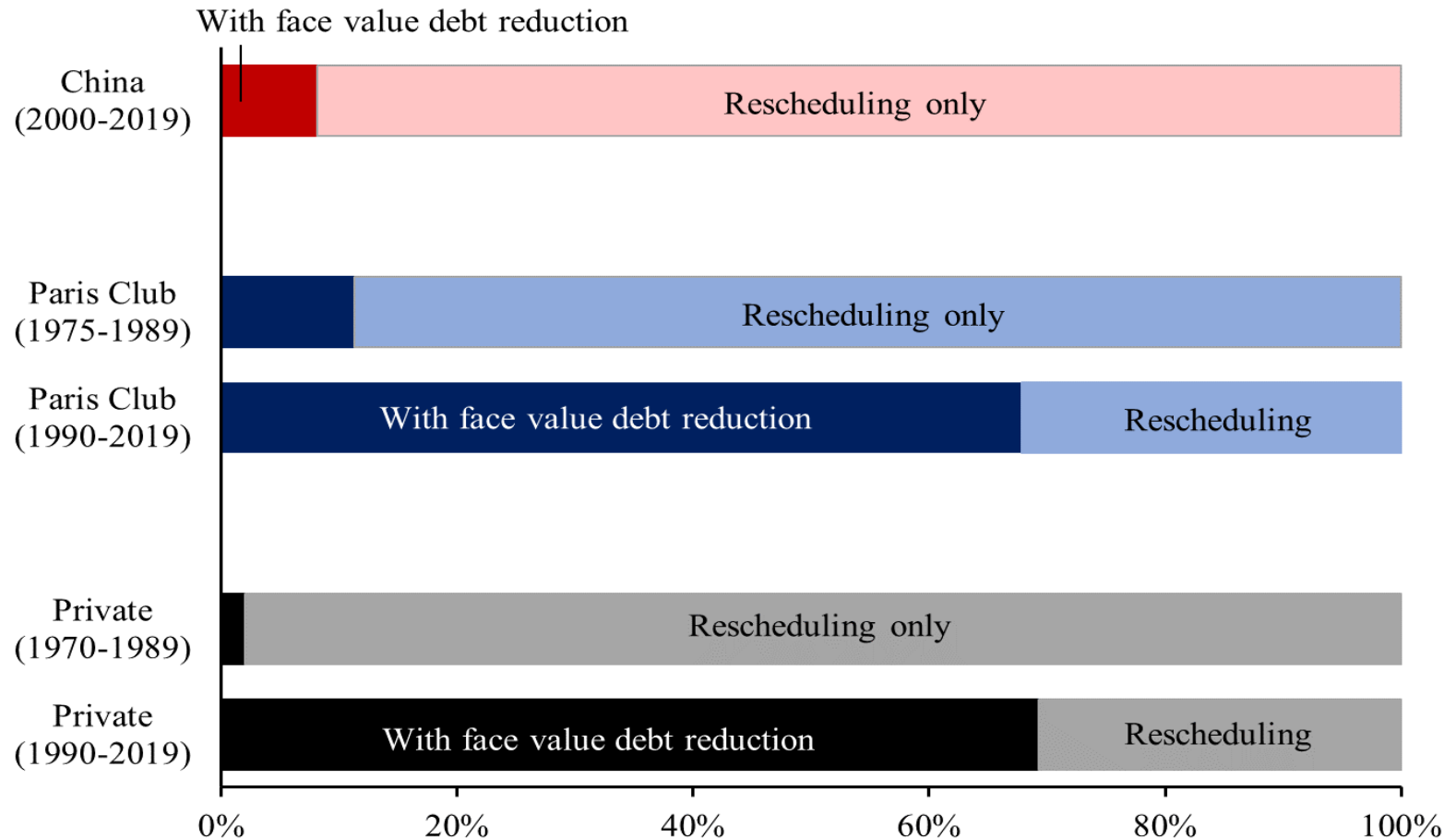
# Serial restructurings: Private, Paris Club and Chinese creditors, 1970 - 2021



Source: Horn, Reinhart, and Trebesch (2022a).

Note: Selected developing countries, see paper for all developing and emerging country timelines

# No face value debt relief: China's approach today resembles Western creditors in 1980s and early 1990s



Source: Horn, Reinhart, and Trebesch (2022a)

# China as a Lender of Last Resort

## Horn, Parks, Reinhart, and Trebesch (2023)

When the stakes are high, China has also extended rescue loans (“bailouts”):

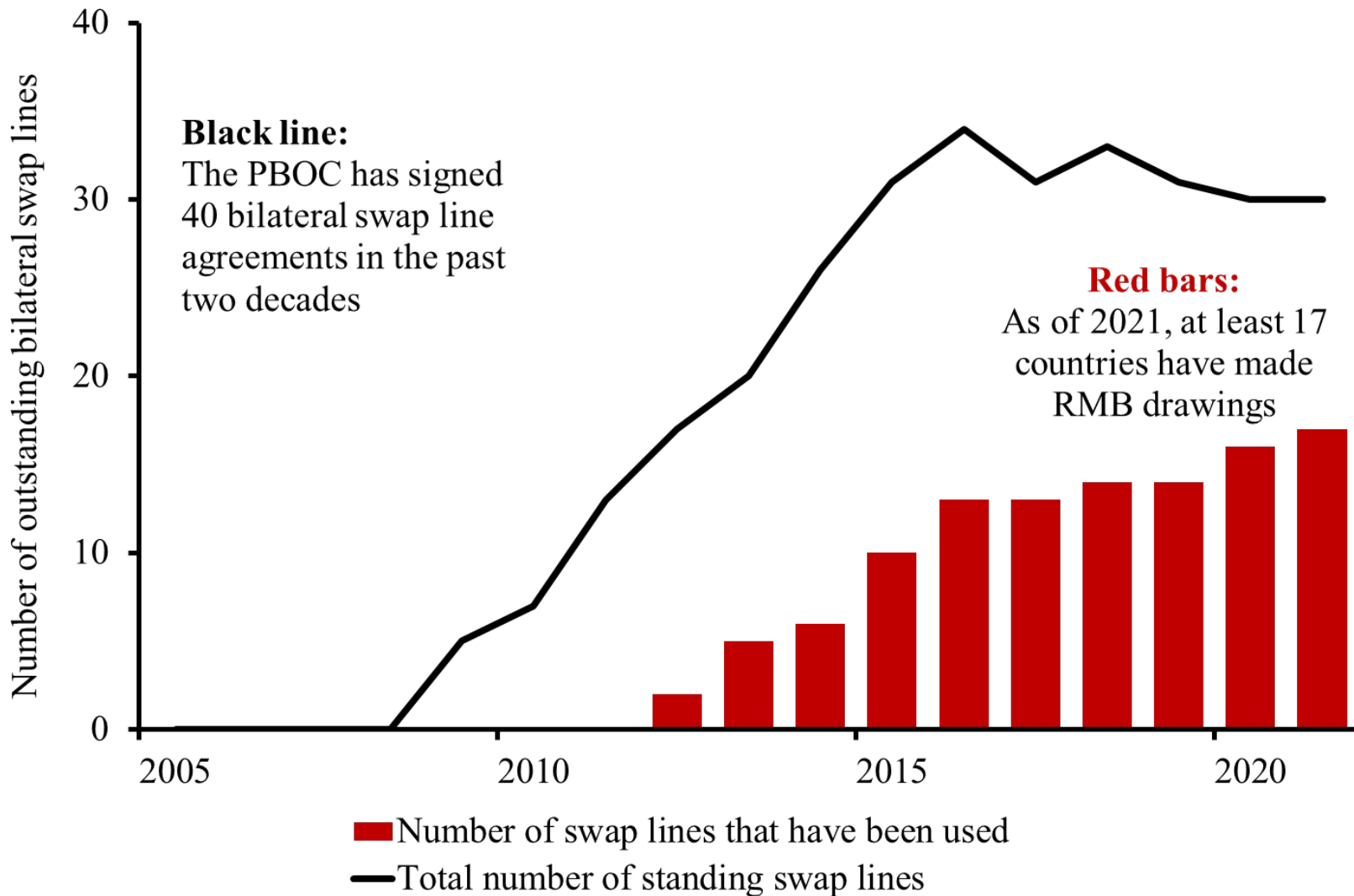
### 1. PBOC liquidity support through RMB swap line network

- The PBOC has extended 40 bilateral swap agreements with foreign central banks (McDowell 2019; Perks et al. 2021; Bahaj and Reis 2022)
- **Our contribution:** We quantify for the first time which central banks made drawings, in what amounts and when

### 2. Liquidity support by Chinese state-owned banks and enterprises

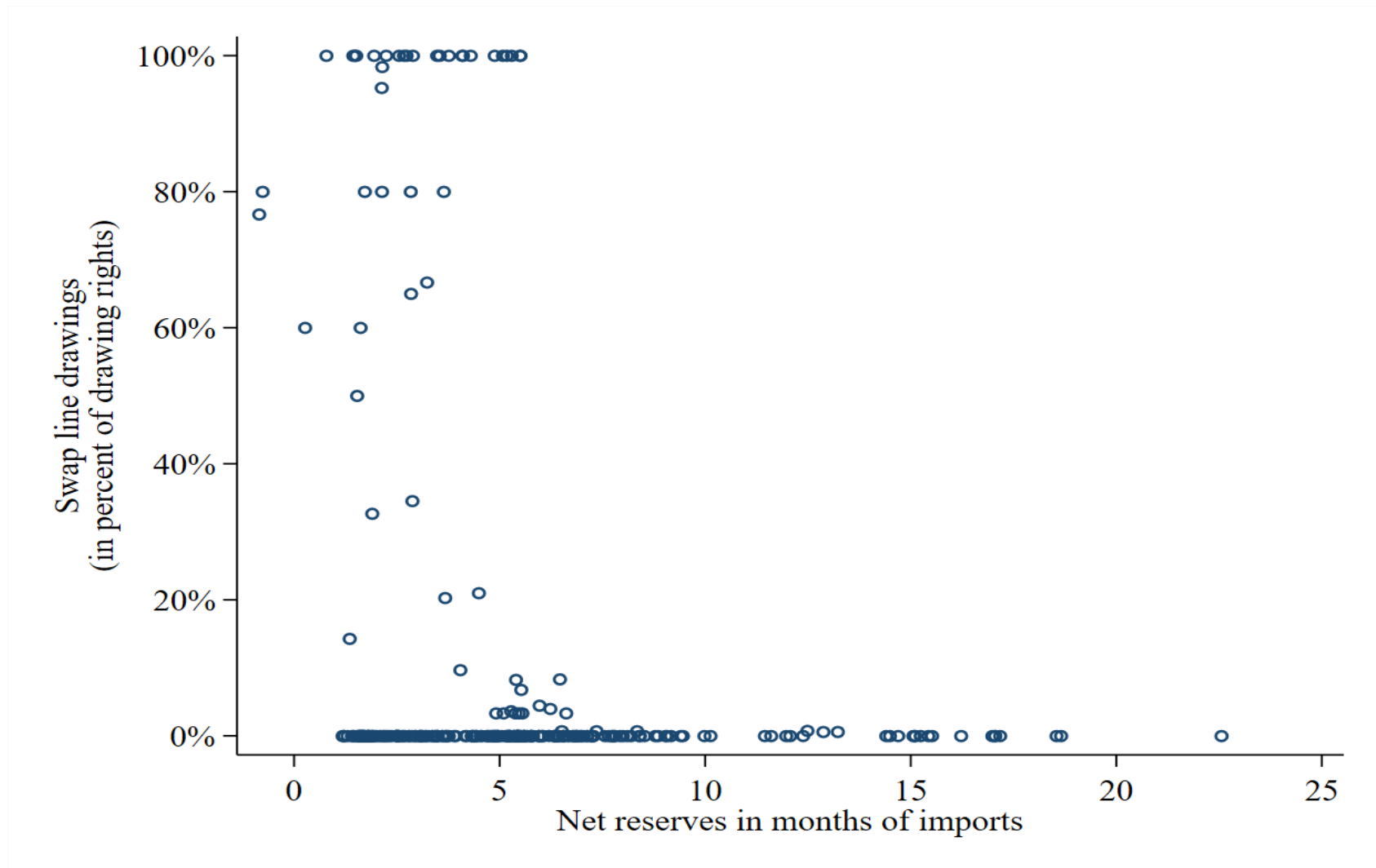
- General purpose loans by Chinese state banks
- Term deposits at foreign central banks
- Commodity prepayment facilities by state-owned energy companies

# The PBOC swap line network is gaining traction...



Source: Horn, Parks, Reinhart, and Trebesch (2023)

## ... and the swap lines are mainly activated by countries in debt distress

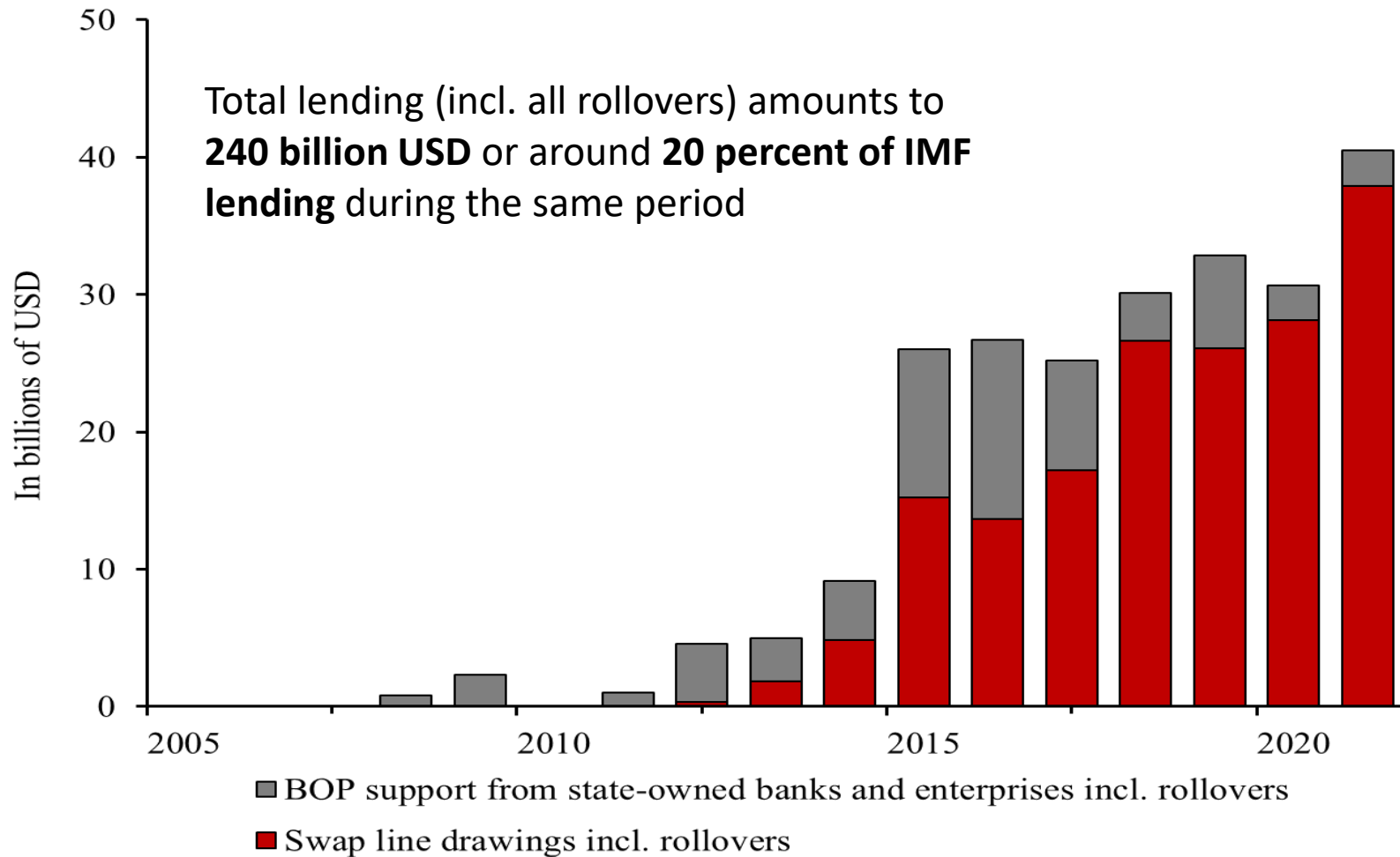


Source: Horn, Parks, Reinhart, and Trebesch (2023)



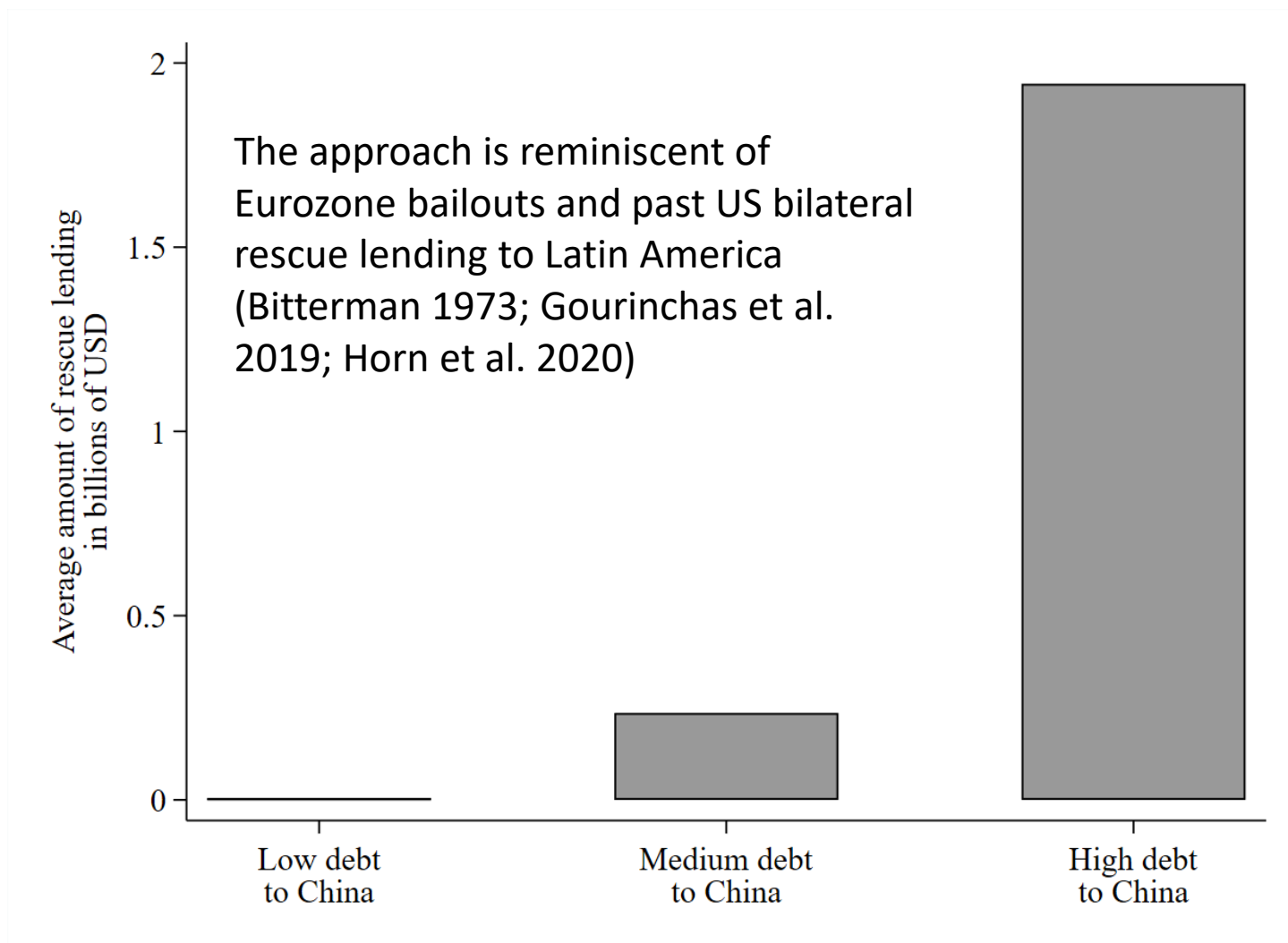


# China's BILATERAL rescue lending



Source: Horn, Parks, Reinhart, and Trebesch (2023)

## Rescue lending is targeted at countries with high debt to Chinese banks and enterprises



Source: Horn, Parks, Reinhart, and Trebesch (2023)

# Final thoughts

- Chinese state-owned banks are the world's largest official creditors and among the most important players in the unfolding sovereign debt restructuring efforts for many EMDEs. They are larger than the Paris Club creditors combined.
- China's lending boom (and bust) show many parallels to past lending booms, in particular the 1980s debt crisis (see Reinhart and Rogoff, 2009).
- There are important knowledge gaps. Limited data on lending, debt and default present severe challenges for country surveillance work, but much scope for future research!
- The issues extend beyond China to other important non-Paris Club creditor powers (Arab states, India). There is a growing shift to a more opaque, fragmented and multipolar international financial architecture.
- If history is any guide, the unfolding debt crisis in many EMDEs will take years to resolve. The G20's Common Framework may be necessary but it is unlikely that it will prove sufficient to deliver a better outcome than in the previous debt crisis.