

China's Belt and Road Initiative: Opportunities and Challenges for Economic Growth in Sri Lanka

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Abstract

Sri Lanka is an upper middle income country, with a population of 21 million, situated in an extremely important strategic location for security and international trade in the Indian Ocean at the center of the East-West maritime trade and mobility route belonging to the South Asian region. Sri Lanka's economic growth has always been sluggish during the post-independence period. Sri Lanka has also witnessed a thirty-year separatist conflict and a serious impact by the Indian Ocean Tsunami in 2004 that devastated the country. While China has assisted Sri Lanka by aid and loans in the process of rebuilding the economy devastated by Tsunami and separatist conflict, China itself has embarked on a global mission of intense bilateral economic cooperation by formalizing its bilateral economic relations through the Belt and Road Initiative. The geographical scope of BRI spans from the East Asia through South Asia, West Asia, and Africa to Europe, and Sri Lanka has become a bilateral partner of China in the BRI. Since the BRI is designed to enhance cooperation and assistance on policy coordination, trade and investment cooperation, and cultural exchange, Sri Lanka stands to gain by being a partner of the BRI while being confronted with many challenges. The BRI has created a complex web of bilateral economic relations covering three continents of the world that includes nearly 80% of the world population. Given the global significance, the BRI tends to generate both opportunities and challenges for Sri Lanka. This paper examined the opportunities and challenges of BRI for Sri Lanka in its efforts to achieve development goals that are aimed at escaping from the middle income trap. The paper argues that Sri Lanka has gained/will gain significant economic benefits from BRI while being compelled to face challenges which can be overcome through appropriate policy regimes and policy cooperation and coordination.

Keywords: Belt and Road Initiative, Chinese Investment, Economic Growth

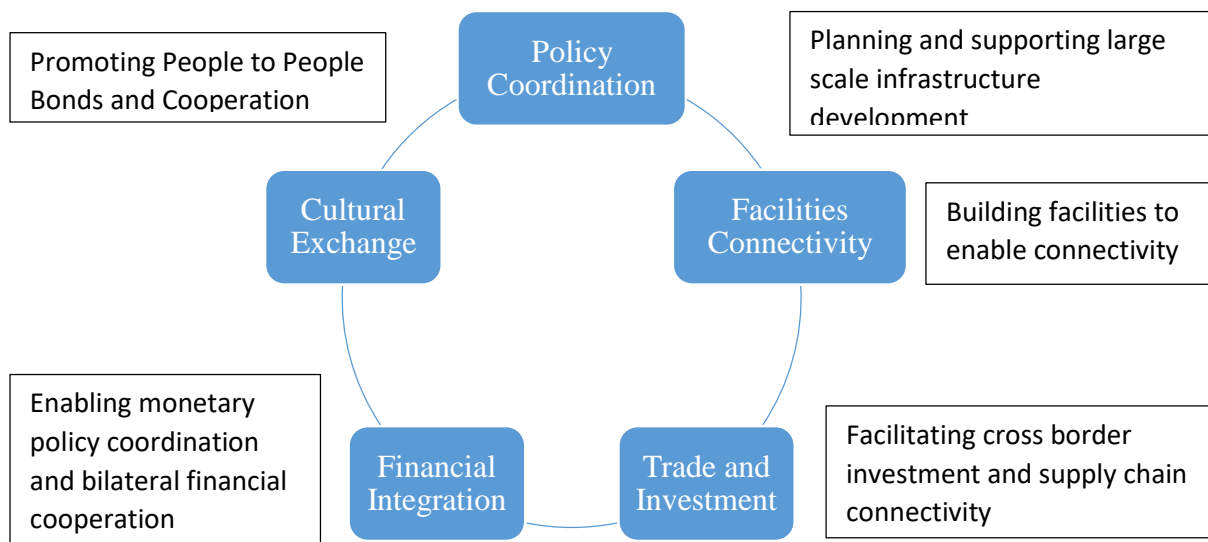
1. Introduction

The world has witnessed a new growth miracle in China during last three decades. Chinese economy transformed from a poorer economy into an upper middle income one becoming the second largest economy in the world. Moreover, China's economic presence as well as its international influence in the global economy and individual countries grew rapidly in recent times. China's economic presence in Sri Lanka has also grown very rapidly since 2005 with various development projects funded by China either through loans, grants or direct investment. Cultural relations have also increased. Chinese tourists have made the largest contribution to total tourist arrivals in Sri Lanka during the last few years. With increased Chinese economic presence in Sri Lanka and with a unilateral internationalization scheme, China is seemingly creating opportunities for economic growth in Sri Lanka while also posing a number of economic, foreign policy and political challenges.

In terms of total land area, China is the world's 4th largest country. China is the largest country in the world in terms of population. Its population rose from 981 million in 1980 to 1400 million in 2017. China is the 2nd largest economy by GDP in the world, USA being the 1st, as China made rapid economic development since it adopted open economy/market economy in 1978 under President Deng Xiaoping. China's GDP per capita rose from US\$ 194 in 1980 to US\$ 8827 in 2017. China's poverty has reduced from 863 million persons (88%) in 1980 to 74 million persons (9.1%) in 2017. China's foreign reserves rose from US\$ 2.2 billion in 1980 to US\$ 3993 billion in 2017 (www.worldbank.org). As a result of China's rapid growth and increase of international trade and investment, as well as accumulation of huge amount of foreign exchange reserves, China has been able to successfully invest in different countries to enhance its economic presence and increase trade and investment. China has become an economic superpower that is able to penetrate any market in the world due to its competitiveness and technological lead. The Belt and Road Initiative emerges in this context.

In 2013, China decided to formalize its global economic cooperation by a unilateral scheme named the Belt and Road Initiative (BRI). The Chinese President Xi Jinping founded the initiative of jointly building the Silk Road Economic Belt and the 21st-Century Maritime Silk Road (Belt and Road Initiative). The initiative is designed to increase trade and investment opportunities among approximately 60 countries within the Eurasia region. The Silk Road Fund was established with US\$40 billion to finance the Belt and Road Initiative to invest mainly in infrastructure and resources, and in industrial and financial cooperation. Later it was re-established as the Asian Infrastructure Investment Bank (AIIB).

Chart 1: Opportunities in Five Key Areas of BRI



Map 1: Belt and Road Initiative in a Map



China-Sri Lanka economic cooperation and relations have increased and strengthened significantly during the past two decades with China becoming the major lender to Sri Lanka. Economic partnership with loans and investments in the area of infrastructure development have been extremely vital for post-Tsunami and post-conflict economic reconstruction and development efforts. Sri Lanka-China economic relations improved prior to BRI and further strengthened after the introduction of BRI. With the increased and intense Chinese projects in Sri Lanka, the BRI appears to have generated both opportunities and challenges for Sri Lanka.

In this context, this paper is an effort to examine and evaluate opportunities and challenges of BRI for ‘economic growth’ in Sri Lanka.

Why do we give priority focus on economic growth in this discussion? Economic growth means increase of overall capacity, national income, national expenditure, and economic power of a country. Economic growth with a system for distributional justice enables a country to increase consumption of goods and services and to raise the living standards. Economic growth is, therefore, seen as the cornerstone of development of a nation. Economic growth is the means through which development can happen, but without economic growth development is not possible. Economic growth can help development in many ways. First, economic growth helps reduce absolute poverty in that increased national output means households can enjoy more goods and services. For countries with significant levels of poverty, economic growth can enable vastly improved living standards. For example, in the nineteenth century, absolute poverty was widespread in Europe, a century of economic growth has lifted nearly everyone out of this state of poverty. Moreover, China's economic growth during the last three decades has helped it to reduce poverty 863 million persons to 74 million persons. Economic growth is particularly important in developing economies. Second, economic growth tends to reduce unemployment. A stagnant economy leads to higher rates of unemployment and the consequent social misery. Economic growth leads to higher demand and firms are likely to increase employment. Third, economic growth tends to improve public services and welfare including ability of a government to take measures to maintaining distributional justice, as growth tends to increase government's tax revenue thereby its capacity to spend. Higher economic growth leads to higher tax revenues (even with tax rates staying the same). With higher growth, incomes and profit, the government will receive more income tax, corporation tax and expenditure taxes. The government can then spend more on public services, welfare and schemes to reduce income inequality. Finally, economic growth reduces public debt and make economic development sustainable. Economic growth helps reduce debt to GDP ratios. In the 1950s, the UK had a national debt of over 200% of GDP. Despite very few years of budget surplus, economic growth enabled a reduction in the level of debt to GDP. Therefore, countries must give priority in their economic development efforts for enhancing economic growth while having a proper system to maintain distributional justice. All newly industrialized economies such as South Korea, Singapore, Hong Kong, Taiwan and fast growing emerging economies such as Malaysia and China have given the highest priority for maintaining rapid economic growth with the aim of developing the economy. In this context, this paper attempts to examine the opportunities and challenges of BRI on economic growth in Sri Lanka.

2. Economic Growth and Middle Income Trap

In 1960, Sri Lanka, Singapore, South Korea, Malaysia, Hong Kong and China enjoyed the comparable levels of economic prosperity. During the last half a century, Singapore, South Korea, and Hong Kong have reached the high income status becoming industrialized economies, and Malaysia and China have been getting close to escaping from the upper middle

income category, while Sri Lanka has just entered the upper middle income category (see Tables 1 and 2). Per-capita GDP of Sri Lanka was approximately US\$ 4065 in 2017.

Table 1: GDP per-capita

Country	1960	2017
Singapore	427	57,714
Malaysia	234	9,944
Hong Kong	429	46,193
United States	3007	59,531
China	90	8827
South Korea	158	29,742
Sri Lanka	143	4,065

Source: World Development Indicators

In order to understand the opportunities and challenges of BRI for economic growth in Sri Lanka, we need to examine the current growth status with surrounding economic conditions and make a growth forecast so that the relevance, opportunities as well as challenges can be understood.

Table 2: World Income Categories

Threshold	GDP per-capita in US\$
Low-income	< 1,005
Lower-middle income	1,006 - 3,955
Upper-middle income	3,956 - 12,235
High-income	> 12,235

Source: www.worldbank.org

Table 3: Recent Growth Rates of GDP per-capita in Sri Lanka

Year	Annual GDP Per capita Growth Rate	Average GDP Per capita Growth Rate
2010	7.3	6
2011	7.7	
2012	8.5	
2013	2.5	

2014	4	3
2015	4	
2016	3.2	
2017	1.9	

Source: Central Bank of Sri Lanka

Table 4: GDP Per-capita Forecast for Sri Lanka

Assumed Growth Rates of GDP per-capita	Projected GDP Per-capita		
	2020	2025	2030
3.2%	4349	5091	5960
5%	4661	5949	7593
6%	4841	6479	8670
7%	5026	7050	9888
8%	5217	7666	11264
9%	5413	8329	12815
10%	5614	9042	14563

Source: Authors computations based on compound growth equation.

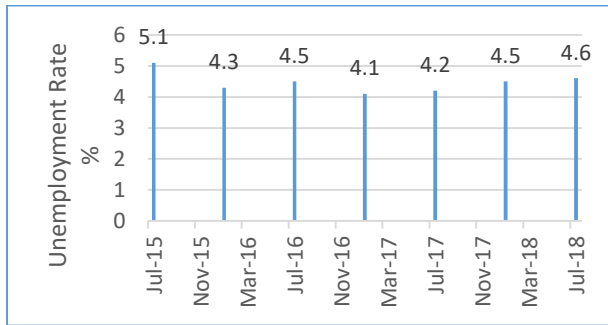
It is noteworthy that Sri Lanka's economy has recorded a sluggish growth during the post-conflict period indicating that the average performance of the economy does not show a significant difference between the conflict and post-conflict periods (see Table 3). Further, in order to examine the opportunities and challenges of BRI, it would be important to have a forecast of GDP per-capita based on the most recent growth performance. We use a compound growth equation to estimate the predicted GDP per-capita up to the year 2030. The GDP per-capita of 2017 in Sri Lanka is taken as the base year GDP per-capita and population growth rate is assumed to remain at the current rate of 1.1% until 2030 as there is no reason to assume that growth rate of population will change during this period due to fertility rates. The predicted GDP per-capita for different growth rates is given in table 4. Estimations show that in order for Sri Lanka to escape from the middle income trap by 2030, Sri Lanka will have to maintain annual growth rate of GDP per-capita of more than 8% for the next decade. The role of BRI in achieving these growth objectives of Sri Lanka appears to be vital.

Sri Lanka is currently locked in the middle-income trap (MIT) which is the situation in which Sri Lanka's growth has slowed/does not accelerate after reaching middle income levels so that the transition to high-income levels seemingly becomes unattainable. Sri Lanka reached the lower middle income category decades ago and GDP per-capita has only moved just above the

lower middle income category. Why do countries including Sri Lanka get into the middle income trap? First, in the country, the pool of transferrable unskilled labor is exhausted so that productivity growth due to shifting additional workers to industry from agriculture and from technology catch-up is diminishing. Second, international competitiveness of the country is eroded and output and growth slow or do not accelerate. Finally, the first stage of growth from low to middle income is factor driven (labor and capital) based on abundant labor supply and high rates of investment financed mainly by foreign aid. In the first phase, production is based on low-technology and the country is locked in to a persistent low technology trap. As a result, middle-income countries, and Sri Lanka, are squeezed between the low-wage poor-country competitors that dominate in mature industries and the rich-country innovators that dominate in industries undergoing rapid technological change. Sri Lanka has been in this predicament for last two decades locked in the middle income trap. In order to overcome from the middle income trap, Sri Lanka needs to invest heavily on new high-tech industries and services, investment on R&D and generate innovations, improve quality of education/skills development, increase infrastructure investment thereby reduce transaction costs and improve competitiveness. It needs to also facilitate FDI by allowing foreign owned firms to come in and/or start joint ventures (agro-based industries and services sectors) and improve investment climate. The BRI is seen to make a big push in investment and productivity growth for escaping from the middle income trap.

In order to understand the importance of BRI, it is also important to examine the extent and structure of unemployment in Sri Lanka. National unemployment rate in Sri Lanka at present is the smallest during the post-independence period remaining at 4.1% in December 2018 while it has remained around 4% for the last three years (Chart 2). However, unemployment is seemingly a serious issue among age groups of 18-30 (Table 5) and among educated youth in Sri Lanka (Table 6). Unemployment among least educated youth appears to be even below a possible natural rate of unemployment implying that there is a labour shortage in unskilled and labour intensive industries, and agriculture and services. Sri Lanka is faced with a peculiar situation of serious shortage of unskilled and semi-skilled labour while there is a surplus of educated labour.

Chart 2: Unemployment Rates in Sri Lanka



Source: www.cbsl.gov.lk

Table 5: Gender and Unemployment in 2017

Age Group	Total	Male	Female
Sri Lanka	4.1	2.7	6.5
15-24	18.5	15.6	23.1
25-29	8.0	3.9	15.5
30 and above	1.6	0.8	2.9

Source: www.cbsl.gov.lk

Table 6: Education and Unemployment in 2017

Level of Education	Total	Male	Female
Sri Lanka	4.1	2.7	6.5
Less than GCE (O/L)	2.4	1.7	3.9
GCE (O/L) Passed	5.7	4.7	7.5
GCE (A/L) Passed	7.8	4.9	10.5

Source: www.cbsl.gov.lk

Unemployment among educated youth, in general, and educated females in particular demands growth and expansion of economic sectors that are able to attract educated labour/skilled labour. At present, the absorption capacity of educated labour in the economy is weak as industries and services are dominated by low-skilled and low technology industries. Moreover, jobs growth depends on economic growth.

Table 7: A Growth Decomposition

Factors	Percentage Contribution to Rate of Growth of GDP

Source: Authors' computations

Labour Growth	14%
Physical Capital Growth	74%
Human Capital Growth	7%
Productivity Growth	5%

Much of Sri Lanka's recent growth has come from investment in physical capital and labour growth (Table 7). Contribution of human capital and productivity growth to economic growth has been around 12% indicating that there is a serious need of transforming education system to produce skilled workers while raising investment on R&D and allowing technology transfer. Increased investment inflows need to accompany rapid productivity growth which is possible only if there is technological progress and innovations. Foreign Direct Investments seems to play a significant role in this as FDI is expected to transfer technology.

In the above context, Sri Lanka is faced with a severe shortage of investment funds to achieve projected growth rates of the economy to escape from the middle income trap. Investment to GDP rate in 2016 was 31.5%. Average capital depreciation rate in 2016 (approximately), that is the investment required to maintain the existing capital stock in the economy, was about 12%. Incremental Capital Output Ratio in 2016 (approximately) was 5, while the same was 2.5 in USA. These statistics helps us to compute the warranted growth rate of GDP and GDP per-capita in Sri Lanka in 2016. According to this data, the investment that could generate growth was about 19.5% considering the rate of depreciation. As a result, the warranted growth rate of GDP from this rate of investment given the ICOR of 5 is 4%. Hence, achieved 3% growth of GDP per capita given the 1% population growth in 2016 was not surprising. Given the ICOR of 5 and a sluggish rate of productivity growth, Sri Lanka needs to have around 40% rate of investment and higher productivity growth to escape from the middle income trap. As the national savings rate is around 25%, Sri Lanka needs to receive foreign investment amounting to 15% of GDP in order to achieve 8% rate of growth of GDP which is the minimum rate of growth required to escape the middle income trap by 2030.

3. Opportunities Created by BRI for Economic Growth in Sri Lanka

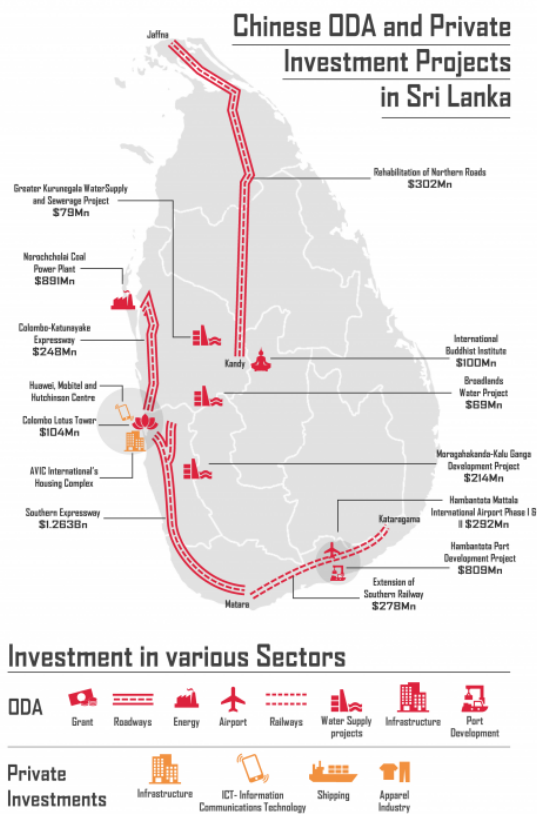
The preceding analysis show that the BRI can play a vital role in raising the rate of investment and contribute to productivity growth in Sri Lanka which will enable Sri Lanka to upscale economic growth in the long run, and escape from the middle income trap. Provided that BRI is used intelligently and with due diligence including measures to prevent possible negative

effects, Sri Lanka stands to significantly gain from the BRI. In the past two decades, Chinese investments have been instrumental in meeting the shortage of investment funds in Sri Lanka. China's contribution in post-Tsunami and post-conflict reconstruction and development was also significant.

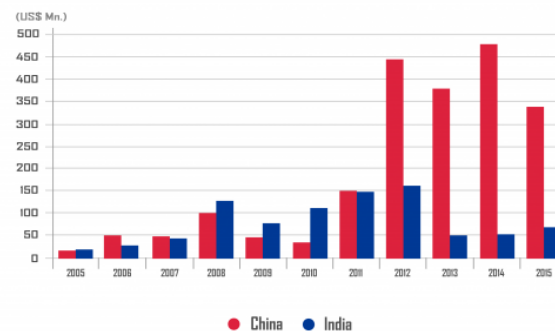
China has invested about US\$ 15 billion in Sri Lanka as grants, loans and direct investment in various sectors. As a result, China has emerged as the leading source of Official Development Assistance (ODA) and Foreign Direct Investment (FDI) in Sri Lanka. Most of the US\$15 billion funds flew to Sri Lanka was ODA in loans and grants –roughly US\$12 billion - in sectors like energy, infrastructure and services. There is private Chinese investment amounting to about US\$2 billion. These project-specific loans, grants, and direct investment directly contributed to economic growth, as they not open unspecified loans to finance budget deficit that would have been subjected to diversion to various government activities that may not necessarily contribute to economic growth. As a result, China has been the largest investor in Sri Lanka (Tables 8 and 9) since 2005. China being a world's leading green energy producer (solar technology), Sri Lanka stands to gain if Sri Lanka facilitate Chinese direct investment in green energy (i.e., Solar technology) as Sri Lanka provides a strong potential for generating solar energy strengthening the Chinese investments that have been taking place in energy sector in Sri Lanka.

In July 2017, Sri Lanka's government and China Merchants Port Holdings (CMPH) signed a Public Private Partnership for US\$ 1.12 billion for Hambanthota Harbour. Second, the government has also proposed developing 15,000 hectares of land surrounding the Hambanthota port into an industrial zone which has unfortunately been hampered by partisan politics which has been a hallmark of recent political economy model of Sri Lanka. Finally, a tripartite agreement was signed in July 2017 between the Ministry of Megapolis and Western Development, the Urban Development Authority, and the China Harbour Engineering Corporation to develop the Colombo Port City. This agreement revitalized the Colombo Port City project and rebranded it as the Colombo International Financial City (CIFC). These arrangements have helped Sri Lanka to increase direct investment and reduce the debt burden due to debt to equity swaps.

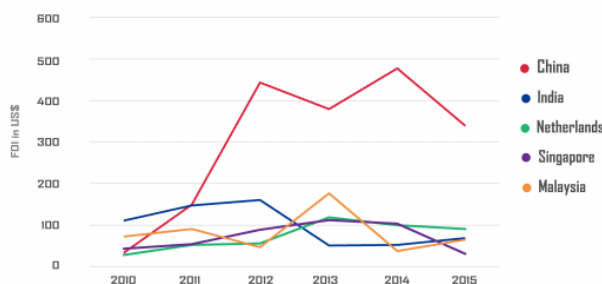
Table 8: Chinese Investment in Sri Lanka



FDI from China and India



Top Five FDI Sources (2010 -15)



Source: www.gatewayhouse.in

The BRI and connected private investment in Sri Lanka would be catalyst for overcoming the low technology trap by contributing to productivity growth. China is providing grants to institutes in Sri Lanka, for instance US\$200 million grant to establish a water testing laboratory on kidney disease in the University of Peradeniya, providing higher education opportunities in China, and providing specific technical assistance on request for various projects. Further technical assistance is possible in green energy generation as China is a leader in solar technology through joint ventures for energy production. Since the BRI has also partnered with international organizations such as the World Bank, International Monetary Fund, United Nations ESCAP, Asian Development Bank for technical assistance BRI partner countries, Sri Lanka stands to gain through technical cooperation arrangements with these institutes in relation to the BRI. Through these efforts and mechanisms, the BRI is expected to make an important contribution to technology transfer and resultant productivity growth thereby fostering economic growth in Sri Lanka.

Table 9: Chinese Projects in Sri Lanka

	Project Title	Amount (US\$ Millions)	Nature of Investment
1.	Norochcholai Coal Power Plant	1342	Loan
2.	Colombo-Katunayake Expressway	248	Loan

3.	Huawei, Mobitel, Hutchinson Center	71	Loan
4.	Colombo Lotus Tower	104	Loan
5.	Southern Expressway	1263	Loan
6.	Rehabilitation of Northern Roads	362	Loan
7.	International Buddhist Institute	100	Grant
8.	Broadlands Water Project in Kitulgala	82	Loan
9.	Kaluganga Development Project	241	Loan
10.	Mattala Airport	292	Loan
11.	Hambanthota Harbour	809	Loan
12.	Extension of Southern Railway	278	Loan
13.	Hambanthota Port Debt-Equity Swap	1120	Direct Investment
14.	Galle-face Shangri-la Hotel	500	Direct Investment
15.	Central Expressway Phase I	1100	Loan
16.	Avic International Housing Projects	250	Direct Investment
17.	Colombo Port City Debt-Equity Swap	1400	Direct Investment
	Total		

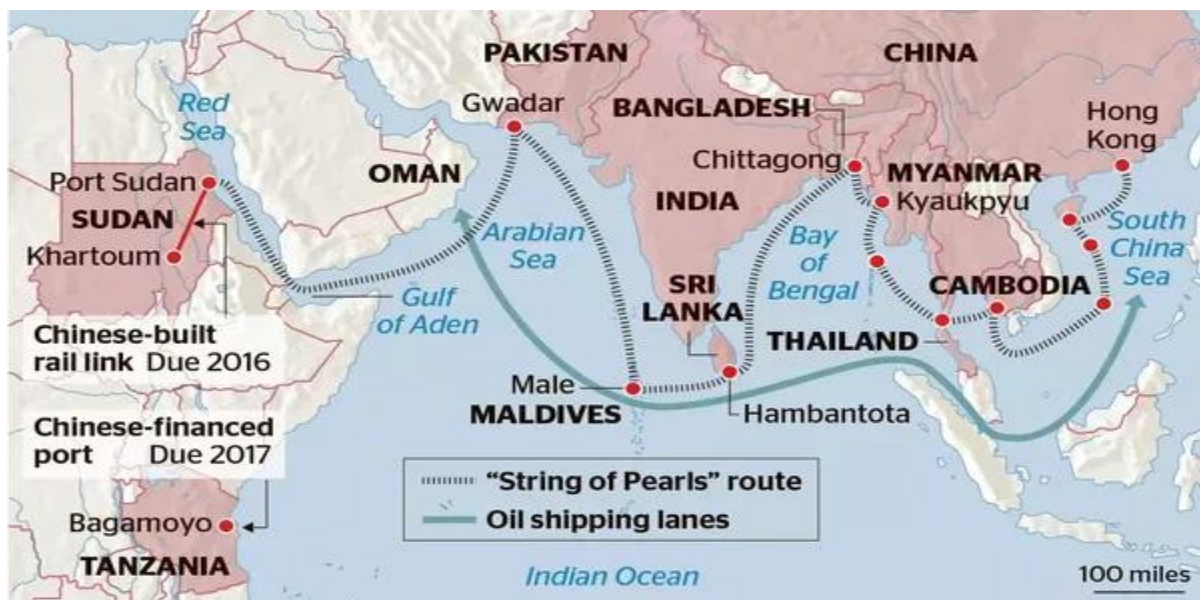
Source: www.gov.lk

It is expected that the BRI would help Sri Lanka to improve its connections to global supply chain. In order to improve the connectivity to global supply chain, four main infrastructure pillars are essential such as transport, energy, telecommunications, and special economic zones. The BRI includes provisions for all these components and China has already invested in all these areas in Sri Lanka (Table 9). The BRI also includes various territorial corridors that would provide the basis for improving connectivity to the global supply chain and that Sri Lanka would mainly benefit by being partner of the BRI to improve trade through these corridors if bilateral arrangements are developed and if Sri Lanka enhanced economic diplomacy. Sri Lanka is strongly connected to the maritime route or the Blue Economic Passage, which is the main international trade route busiest in the world positioned through the Indian Ocean. Moreover, Sri Lanka is expected to benefit from BRI's other international trade corridors such as the New Eurasian Land Bridge, China-Mongolia-Russia Economic Corridor, China-West Asia Economic Corridor, China-Indo-China Economic Corridor, Bangladesh-China-Myanmar Economic Corridor, and China -Pakistan Economic Corridor as these corridors will allow Sri Lanka to improve trade in goods and services. However, improving the access to Chinese markets through bilateral efforts will be essential to improve the supply chain connectivity, which requires preferential treatment for Sri Lanka's exports by China through a bilateral economic partnership arrangement.

4. The Challenges of BRI

The BRI has been a new international development paradigm initiated and propagated by China with its increasing dominance in the world economy. This has also been seen as an alternative arrangement to existing international economic order. With heightened attention on China's increasing web of bilateral economic relations involving South Asia, Africa and Europe, and with international organizations, some scholars have raised concerns of different kind.

Map 2: The 'String of Pearls' Proposition



Source: www.gatewayhouse.org

First, the BRI has been seen as a threat to security and strategic interests of India as BRI appears to encircle India through various trade corridors. It is also thought to weaken the position of west in the global economy. The proposition that the BRI encircles India endangering its security and strategic interests has been known as the “string of pearls theory” (Map 2).

The String of Pearls is a situation in which the BRI is seen to threaten the security and strategic interests of India and others as China is seen to heighten potential Chinese geopolitical intentions in Indian Ocean region. It refers to developing military and commercial facilities in BRI partner countries by China enabling it to influence on the geopolitical matters of those countries, especially in Sri Lanka, Maldives and Pakistan. It is seen as a threat to India's security, its power projections, trade, investment and territorial integrity, especially due to China-Pakistan trade and investment corridor (Brewster 2014, Firzli 2015, Khurana 2008, Prabash 2017, Sibal 2014, Tiezzi 2014). Due to these concerns, Sri Lanka is caught in the power struggle between China, India, and Pakistan. Sri Lanka is constrained to attract Chinese investment, especially direct investment, due to these concerns raised by India. It is also noteworthy that USA or Canada has not raised serious concerns about BRI. In order to address

these concerns, Sri Lanka needs to have an open and transparent foreign policy based on its own interests grounded on economic diplomacy. Taking measures to improve India-China relations and trust and the constructive role that Sri Lanka can play in such an effort is also crucial for this. It is important to make everybody in the world known that Sri Lanka needs to pursue its economic interests and it has to harvest foreign investment, attract foreign technology and develop new areas of collaborations with countries that are economically beneficial to Sri Lanka including China. It is ironic that India can have nuclear bombs as deterrent to other countries which is also a threat to Sri Lanka, and it had adopted a “weaker and poor neighbors policy”. There is no need of Sri Lanka to succumb to the India’s concerns as Sri Lanka’s efforts are not geared towards making any other country insecure as Sri Lanka is a sovereign state which has to pursue the economic interests of its people and it is empowered to control any country that is attempting to use Sri Lanka as a cat’s paw to advance their own security and strategic interests. It is extremely tragic that India is trying to destroy Sri Lanka’s development efforts in an attempt to secure themselves. India appears to have a “weaker and poor neighbors policy” in that weaker and poorer neighbors as a strategy to safeguard their own security and strategic interests. It is time that Sri Lanka develops diplomatic relations with all countries that are economically important to it including India and voice open and resolute protests against India for their attempt to undermine Sri Lanka’s process of economic development. Such a foreign policy should be grounded on the principles of economic diplomacy. It is noteworthy to state here that China’s investment in Sri Lanka will have no impact on India as Sri Lanka has no interests in interfering with the affairs of other countries. Concrete measures need to be taken to develop India-Sri Lanka-China economic relations possibly through a tripartite economic partnership agreement.

Second, it has been noted that there is a general lack of economic viability of some Chinese projects in Sri Lanka as productive economic activities have not been properly planned with the infrastructure investment. The Mattala International Airport has generated significant losses. Despite being of an international standard and at a strategic location on the Maritime Silk Route, the Mattala Airport has been operating at a loss in which losses incurred by the end of 2016 were estimated at US\$ 112.9 million. Moreover, the Hambantota Port Development Project has also resulted in losses. Phase I of the project that was completed in 2011 accumulated an estimated loss of LKR 46.7 billion, with an annual loan repayment of LKR 9 billion until 2016 (www.cbsl.gov.lk). As the port incurred heavy losses making debt repayment difficult, in 2016, the government entered into a debt-equity swap agreement in which 80% of the port was supposed to lease in a debt-for-equity swap to the China Merchants Port Holding Company (CMPort), who was to invest US\$1.12 billion to revive the port under a public private partnership. It was decided that under the agreement, CMPorts had to divest 20% of its shares

to a Sri Lankan company within ten years. The CMPort had to spend at least US\$700-800 million or more to bring the port to profitable operational level. In July 2017, the agreement was signed, but leased only 70% of the Port to CMPort instead of the initially proposed 80% (www.cbsl.gov.lk).

Third, Chinese loans are seen to contribute to worsening Sri Lanka's external debt burden. External debt in Sri Lanka increased to US\$53.4 billion in 2018 from US\$ 44.5 billion in 2012 (Table 10). Chinese debt to Sri Lanka was US\$ 8 billion (12.3% of total outstanding external debt of Sri Lanka) in 2017. Total debt service payments of Sri Lanka increased to US\$2.56 billion in 2018 from US\$1.4 billion in 2010. The government is on record to make the highest debt servicing of about US\$ 2.6 billion in mid-2019. It is also noted that a 77% of the total debt is on the maturity of loans obtained prior to 2015. While total external debt to GDP remains at 59.5%, total government debt to GDP is 77.6% (www.cbsl.gov.lk). This trend has been observed in the context that exports to GDP ratio has been falling making it difficult to finance debt, and that remittances of workers and debt roll-over have been the main sources of debt servicing. These data indicate that Sri Lanka is in dire need to shift from foreign debt to foreign direct investment to find investment funds to finance economic growth. It is also noted that since loans are given mostly for infrastructure development projects, they will have growth effects in the long run only if there is resulting growth of productive economic activities by way of new industries and service institutions.

Table 10: External Debt Situation in Sri Lanka

Year	External Debt (US\$ billions)	Debt Service (US\$ billions)	Forex. Reserve (US\$ billions)
2010	17.44	1.40	7.1
2011	17.97	1.30	6.7
2012	22.81	2.00	7.1
2013	26.87	2.10	7.5
2014	33.67	1.45	8.2
2015	41.00	2.03	7.3
2016	44.80	1.81	6.0
2017	45.10	2.42	7.8
2018	53.40	2.56	8.0

Source: www.cbsl.gov.lk

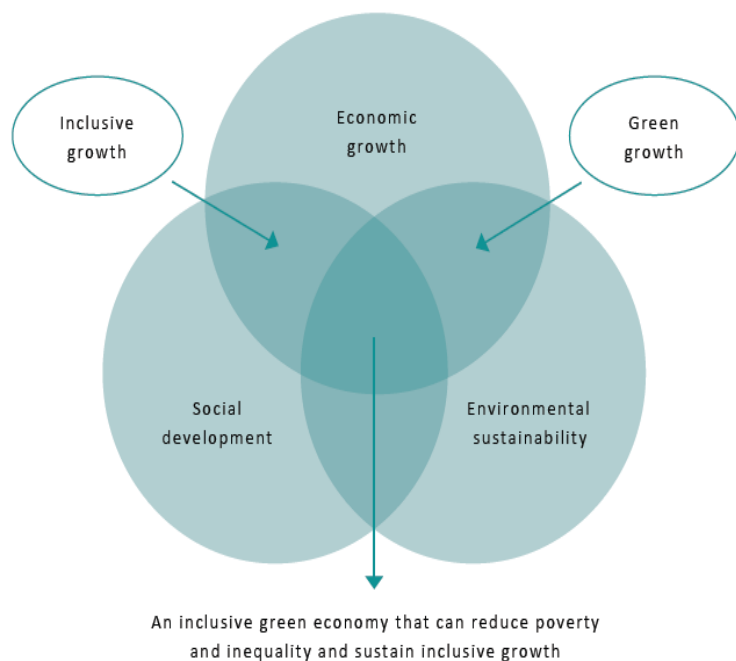
Fourth, since the BRI has been creating a complex web of bilateral economic relations with Chinese investments in terms of loans, grants and direct investment, one would see BRI as an alternative mechanism which is seemingly threatening and undermining global economic order, as it will clash with agendas of multilateral and plurilateral arrangements and established norms of international economic order. The BRI can sometimes be recognized as a mechanism that has the potential to undermine the role of multilateral financial institutions as lending through AIIB would provide an alternative platform for lending and grants for developing countries. The BRI may also undermine international capital markets as countries may seek to borrow from AIIB rather than financing from open capital markets. The BRI may also undermine the global trading system as it promotes bilateralism as against multilateralism. As Cheney (2018) states “the Belt and Road Initiative (BRI)—also known as One Belt, One Road—while promoted as an economic development initiative, will have important implications for the global and regional international orders. As China finances large-scale transportation, energy and digital infrastructure projects across the globe, it seeks to expand its influence and alter the current global order. Through infrastructure investments, China could hasten its rise as a regional hegemon and global superpower by increasing its economic connections and influence. Financial investment in underdeveloped nations will result in governments supporting Chinese interests and, in some instances, becoming financially beholden to Beijing through predatory lending”. In order to redress these concerns, the BRI partner countries will have to have an open and transparent policy and agenda of actions to prevent any negative effects on the health of the global order.

Fifth, does BRI of China inadvertently protects rogue regimes and weaken democratization of nation states? One would tend to argue that since China is not interested in democracy, good governance or human rights of BRI partner countries as its declared policy is non-interference in domestic affairs of partner countries, it may inadvertently help protect ‘crony capitalism’ and ‘rogue regimes’ as it provides lending for government projects which may strengthen corruption, and it would allow undemocratic countries to perpetuate their actions and policy regimes unhindered as there is no external pressure (Cheney 2018, Balding 2018). Conditions on good governance, democracy or human rights are not attached to Chinese grants and/or loans. It should also be noted that political class in Sri Lanka appears to prefer foreign loans as against foreign direct investment inflows possibly because of the fact that loans are channeled via government institutions for government spending which would provide ample opportunities for the political class and bureaucrats to engage in rent seeking activities and advance their political interests.

Finally, one can be skeptical, and foresee, that the BRI projects in partner countries and China's efforts for relocating its industries in other countries in BRI corridors including in Sri Lanka would increase environmental risks. In a rigorous analysis in relation to Europe, Trace *et al* (2016) states that "the initiative will create new environmental risks across the entire Eurasian continent, especially in countries with predominately poor records of environmental governance, including the former Soviet republics and Russia. Concurrently, on the domestic front, the Chinese Government has launched a new policy paradigm, 'ecological civilization', to dramatically improve environmental regulations, reduce pollution, and transform industries by adopting new green technologies and higher environmental standards". The similar concerns can be raised in relation to Sri Lanka. In order to overcome these environmental concerns, the individual countries will have to strengthen their national environmental protection bodies to act diligently including new environmental legislations where such laws are not available. However, since Sri Lanka has developed the required environmental legislations and have established relevant bodies and mechanisms, Sri Lanka is equipped to handle any environmental concerns emerging from the projects of BRI.

In order to overcome these challenges, Sri Lanka needs to adopt an inclusive green development strategy (Chart 2) which is economic development that is environmentally and socially sustainable with an open and transparent foreign policy grounded on economic diplomacy. Inclusive green growth needs to encompass three components. First, Sri Lanka needs to have a strategy for rapid economic growth supported by the BRI and other private investments. It needs to increase the rate of investment through FDI and raising savings. The BRI will be vital for Sri Lanka to fill investment funds shortage and raise productivity growth through R&D and innovations. The inclusive green growth strategy should also include mechanisms and policies for social development, especially to maintain distributional justice, in that Sri Lanka will be compelled to continue with existing subsidy schemes, free education and free healthcare system. Further, a universal social security system will have to be established. Finally, an inclusive green growth strategy should also include mechanisms and actions to create environmental sustainability by switching to green energy sources, especially solar technology, and locating industrial zones in less environmentally damaging areas in the country.

Chart 2: Inclusive Green Growth



Source: www.oecd.org

5. Concluding Remarks

The BRI can be seen as the 21st Century Marshall Plan as it has all the ingredients of the post second world war Marshall Plan and resultant Bretton Woods System that created a new world order dominated by the policies, decisions, and actions of the western economic powers that was aimed at rebuilding the countries devastated by the war. In spirit and actions, the BRI is seemingly creating an alternative world order that is not completely an alternative to the existing one. The BRI constitutes a complex web of bilateral relations with individual countries in South Asia, West Asia, Africa, and Europe as well as agreements with many international organizations such as the World Bank, International Monetary Fund and Asian Development Bank. In order to understand the role of BRI in economic growth in Sri Lanka, this paper examined the current state of economic growth in Sri Lanka and difficulties in escaping from the middle income trap as there is a serious shortage of investment funds, the economy is at the low technology levels, skills levels of the economy are poor, there exists a sluggish growth of productivity, and the issues with competitiveness. Given the importance of infrastructure investment and possibility for direct investment in services and industries, the BRI's role in improving Sri Lanka's connectivity to global supply chain, we find that Sri Lanka stands to significantly gain from the BRI. It was also observed that the BRI tends to pose certain challenges for the Sri Lankan economy including; addressing concerns on India's security and strategic interests, increasing external debt burden of Sri Lanka due to soft Chinese loans, safeguarding Sri Lanka's plurilateral and multilateral commitments in the context of BRI's

heightened bilateral commitments, addressing possible negative effects of BRI's funding on good governance and democracy in partner countries, and possible environmental risks of BRI projects. In order to reap the benefits and face the challenges of BRI, Sri Lanka needs to adopt an inclusive green development strategy that encompasses concrete measures for rapid economic growth, maintaining social and environmental sustainability, as well as an open and transparent foreign policy grounded on economic diplomacy to safeguard and achieve Sri Lanka's economic interests.

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