

**China in Sri Lanka: Is it a ‘debt trap’? Analyzing the Belt and Road Initiative  
(BRI) in Sri Lanka**

By

**DIAS, Galagama Sachini**

**THESIS**

Submitted to

KDI School of Public Policy and Management

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For the Degree of

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## ABSTRACT

The 'Belt & Road Initiative (BRI)' is the 21<sup>st</sup> century grand strategy of China which envisages the construction of massive industrial corridors and connectivity networks across land and sea. Expanding from China to Europe via South East, South and Central Asia, this policy initiative has brought forth significant transformations to the political, economic and strategic aspects of the global power order, re-emerging China as a revisionist power and re-surgings the centuries old Asian order. In response, there has been a growing interest in the existing literature to analyze the context of BRI through diverse concepts and frameworks.

The debt trap which implies the 'debt to equity' transfers is one such debatable concept which has been used by the growing body of literature to interpret the context of the BRI. The Indian Ocean island nation, Sri Lanka has been widely narrated in the literature and policy circles as a victim of Chinese debt trap.

In this backdrop, the purpose of this research paper is to quantitatively and qualitatively analyze Sri Lanka's BRI project profile, investments and debt profile in order to identify as to whether the BRI in Sri Lanka resembles a debt trap. This paper also attempts to identify the implications and possible tendencies of the BRI in Sri Lanka, re-examining the question of why do the policy makers in the developing world need to rethink China's approach.

Traversing on the interpretative and evaluative case study method of qualitative research paradigm, this research paper concludes that BRI in Sri Lanka is a greater economic and development opportunity which has supported the country to fulfill its infrastructure gap in diverse sectors in

Sri Lanka. Although the study identifies that several BRI projects as economically non-viable initiatives, based on the statistical evidences, this paper concludes that the debt crisis of the country as a long preceding structural issue of the economy made by Colombo, not an intended trap of China, counter arguing that the China in Sri Lanka as not a debt trap.

**Key Words:** Belt and Road, Debt Trap, Silk Road, China, Sri Lanka

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## **List of Abbreviations**

BRI - Belt and Road Initiative

GDP - Gross Domestic Productivity

OBOR - One Belt One Road

GDP - Gross Domestic Productivity

FDI - Foreign Direct Investments

PPP-Public Private Partnership

IMF - International Monetary Fund

CICT - Colombo International Container Terminal

SEZ - Special Economic Zone

SOE – State Owned Enterprises

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## 1.0. INTRODUCTION

### 1.1. Background of the Study

In 2013, China launched the Belt and Road Initiative (BRI), the lynchpin of the signature foreign policy of new China. This initiative envisaged constructing massive industrial corridors and connectivity networks across the land and sea, which expanded from China to Europe via Asia and Africa.

This grand strategy has been postulated on the ideology taken from the ancient Chinese Silk Road, a commercial network established more than two thousand years ago, during the expansion of the Han Dynasty in China. (Figure 01). President Xi Jinping's Belt and Road Initiative (BRI) is also identified as the more assertive second version of the <sup>1</sup> Going Global Strategy, the investment push policy launched by Jiang Zemin in 1997. (Miller, 2017; Jenkins, 2019)

As declared by President Xi Jinping, this US\$ 4 trillion policy alternative focuses on partnership, equal footing and inclusive global affairs rather than alliance, aimed to achieve the 'Socialism with Chinese Characteristics for a new era' (Economy, 2018 ; Islam, 2021) which are resembled by the core values of Chinese foreign policy, such as strategic trust, non-interference, discarding hegemonism, multi-polarity, mutually benefited cooperation, etc. (Sarwar, 2017).

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<sup>1</sup> Going Global Strategy or Go Out Policy is the investment policy adopted by China in late 1990s with the aim of increasing Chinese investments abroad. (Sang-Hyung, 2011)

[https://www.posri.re.kr/files/file\\_pdf/71/271/2825/71\\_271\\_2825\\_file\\_pdf\\_1457058703.pdf](https://www.posri.re.kr/files/file_pdf/71/271/2825/71_271_2825_file_pdf_1457058703.pdf)



Figure 01-Silk Road (Old vs New)

Source: The Economist

Expanding over 70 countries in the world, covering sixty percent of the total world population and representing one-third of the global GDP, at present, BRI has become a decisive element in the effort of reemerging China as a core economic and revisionist power in the world. Furthermore, this initiative has played a pivotal role in shifting the global power paradigm towards Asia (Jenkins, 2019; Dunford & Liu, 2019; Dunford, 2021), through the resurgence of the centuries-old Asian Order.

However, in response to this increasing assertiveness of China in the contemporary global politico-economic context, there has been a growing interest in the existing literature to interpret and identify the implications of BRI by applying diverse of theoretical and hypothetical frameworks, which has also attempted to project future trajectories of this initiative and its possible policy implications on the existing power ‘order’ in the Indian Ocean

The 'Debt Trap' is one such conceptual framework that has been widely used in the recent body of literature in order to interpret the implications of BRI to the global politico-economy. In spite of Beijing's proclamation that BRI is a benevolent policy initiative aimed at win-win diplomacy and global cooperation, among scholars, policymakers, think tanks and media, it has been widely portrayed as an illiberal form of geopolitical strategy wrapped with debt trap diplomacy.

Sri Lanka, the Indian Ocean island has been extensively used in the media, literature and policy circles as a classic example of Chinese debt-trap diplomacy (Bräutigam, 2020). As one of the key annexed countries of BRI, Sri Lanka has partnered with China in a number of infrastructure and other development initiatives. However, some scholars argue that the Chinese projects in Sri Lanka as economically non-viable, unsustainable projects which aimed at increasing the debt burden of Sri Lanka aimed at initiating debt to equity transfers (Chelleney, 2017).

Some scholars argue Chinese debt trap in Sri Lanka as a tool to increase its leverage potential in political and strategic domains in the country (Economy, 2018; Abeyagoonasekera, 2021). The case of the Hambantota Sea Port which was leased to China in 2017 to ninety-nine years is often portrayed in the literature and policy circles as a debt to equity transfer (Abi-Habib, 2018). However, there are certain scholars that claim debt trap diplomacy as a political rhetoric and a myth (Carrai, 2021; Jones & Hameiri, 2020). Furthermore, some scholars claim China in Sri Lanka as a greater economic and commercial opportunity (Kelegama, 2014).

Against this dichotomous background, this research paper attempts to contribute to the previous studies on the Belt and Road Initiative, China-Sri Lanka relations and Debt Trap Diplomacy by reanalyzing contemporary context of BRI within the Sino-Lanka relationship trajectory.

Traversing on this dilemma, this research paper concludes that BRI in Sri Lanka is a greater economic and development opportunity which has supported the country to fulfill its infrastructure gap in diverse sectors in Sri Lanka, though the China has been motivated by geo political and geo-economic aspirations. The study also identifies that several BRI projects as economically non-viable initiatives, based on the statistical evidences, this paper concludes that the debt crisis of the country as a long preceding structural issue of the economy made by Colombo, not an intended trap of China, counter arguing that the China in Sri Lanka as not a debt trap.

## **1.2. Significance of the Research**

From a public policy perspective, understanding the ‘context’ of the BRI in Sri Lanka would be significantly important for the policymakers to strategically revise, divert, redirect or continue the existing institutional and policy frameworks, in particular, this study will be of use in the aspects of foreign relations, diplomacy, development studies, Asian studies and economy. This research paper is an attempt to serve this purpose.

## **1.3. Purpose of the Research**

The purpose of this research paper is to quantitatively and qualitatively analyze Sri Lanka’s BRI project profile, investments and loans under BRI in order to identify as to whether the BRI in Sri Lanka resembles a debt trap. This paper also attempts to identify the implications and possible

tendencies of the BRI in Sri Lanka, re-examining the question why do the policy makers in developing countries need to rethink China's approach.

#### **1.4. Research Questions**

This research study will be guided by following research questions.

- 1) What are the impacts of BRI to Sri Lanka?
- 2) Is BRI in Sri Lanka a debt trap?
- 3) What are the policy implications and tendencies of BRI in Sri Lanka?
- 4) Why do the policy makers in developing countries need to rethink China's approach?

#### **1.4. The Outline of the Research Paper**

The remaining part of this research paper consists with three chapters.

The Second Chapter is the literature review which focuses on describing, analyzing and evaluating the existing literature on BRI, China -Sri Lanka relations and Dept Trap aimed at identifying the existing research gaps.

The Third Chapter describes the research methodology which will be undertaken to conduct this study.

The Fourth Chapter is the analysis of the Belt and Road Initiative in Sri Lanka. This chapter evaluates the BRI project profile in Sri Lanka, its impact to Sri Lanka and impact of BRI in Sri Lanka to China. The Fifth Chapter focuses on two case studies, they are the cases of Hambantota Port and Colombo Port City. The Chapter Six analyses debt profile of the country. The main purpose of 04-06 chapters is to evaluate the impact of BRI in Sri Lanka and to derive an evidence-

based answer to the main research question, Is China in Sri Lanka a Debt Trap? The Seventh Chapter of the paper aims to provide an interpretation to the contemporary China—Sri Lanka relations. The Eighth Chapter is the public policy perspective which aimed at identifying the policy implications and possible tendencies of BRI in Sri Lanka answering the question why policy makers in developing countries need to rethink China’s approach while recommending the possible policy initiatives to cope with the challenges of the context. The last chapter of the paper is the conclusion which aimed at providing a summary of the research findings and policy recommendations.



## **2.0.LITERATURE REVIEW**

In the growing body of literature, there are number of studies that have been conducted on Belt and Road Initiative (BRI), China-Sri Lanka relations and Debt Trap diplomacy. The purpose of this literature review is to describe, analyses and evaluate the content and findings of some of those studies to identify the research gap of the subject arena.

### **2.1. Belt and Road Initiative**

In the growing array of literature, there is an ongoing debate concerning China's contemporary approach of Go Out Policy or the Belt and Road Initiative. The Belt and Road Initiative is considered as the most prominent ploy of the 'third revolution' of China, led by the current Chinese President Xi Jinping (Harding, 2006).

Some scholars define the Belt and Road Initiative as the re-incarnation of the historical Chinese Silk Road (Tobin, 2018). As the rise and decline of ancient China has been linked the rise and decline of Silk Road, scholars claim the BRI as a strategically carved pathway to regain the ancient glory and imperial power of China along the Silk Road (Harding, 2006; Lei, 2018). Some scholars further argue that the BRI which is presently unfolding, resembles a reconstitution of the China centric old tributary order, where countries along the silk road and neighborhood had volunteered to join as sub-states of this system to gain the access to trade with China (Zhao, 2006; Kissinger, 2014; Oosterveld et al, 2018).

According to Harding (2006), China is massively 'going global', starting from the late 1990s as a part of its state policy to ensure the energy security and safeguard the interest of natural resources,

raw materials and technology through numerous investments and long-term contracts of Chinese State-Owned Enterprises (SOEs) with foreign countries. The BRI projects in certain parts of the world are massively driven by the need of China to secure energy and raw materials to control the strategic world markets, e.g. Extraction of Rare Earth Elements (REEs) in Africa (Oosterveld, et al, 2018).

Providing examples from the BRI projects related to security and strategic domains, some scholars argue the BRI as a geo-strategic tool which aimed at increasing the strategic and maritime dominance of China in the Indian Ocean and beyond (Luft, 2017; Tobin, 2018). This initiative today covers approximately 900 projects worldwide, out of which more than 80 percent have been contracted to State Owned Chinese firms or SOEs. These projects are not only limited to infrastructure development, but also to some security related projects. For instance, in Pakistan, they develop a video and internet surveillance system which is much similar to the system in Beijing. Therefore, some scholars claim the BRI as an opening for China to advance its military purposes. In addition, at present, Chinese SOEs run around seventy-six Sea-Ports and Port-Terminals around thirty-four BRI annexed countries. It is also an important factor that in certain Ports, China has performed the visits of military vessels. e.g. Greece, Pakistan, and Sri Lanka (Economy, 2018).

As further argued by Economy (2018), through initiatives abroad, illiberal China is trying to establish dominance in the liberal world order. As suggested by Oosterveld et al (2018), using the going out policies, China is standing itself as an authentic alternative to the Washington-dominated

order, to establish 'Beijing Consensus', being an alternative development partner, aid provider and infrastructure developer.

Some scholars argue that the BRI resembles the approach of colonialism which aimed to increase the political influence of China over BRI annexed countries. Some scholars argue these Chinese initiatives abroad as a form of neo-colonialism. (Larmer, 2017-b) As argued by Chan (2018), although African countries have benefited through the economic and infrastructure development activities under going global and BRI, China exhibits some neo-colonial tendencies, revealing some potential to challenge the sovereignty of African countries. The establishment of special arbitration courts for BRI projects is also a declared plan of Beijing, that aimed to promote alternative legal systems in BRI annexed countries which is possibly underpinned by Chinese rules (Economy, 2018). Giving the example of Hambantota Port of Sri Lanka, which has been leased to China for ninety-nine years, some scholars claim the Chinese approach as similar to the imperial strategies that British Empire imposed on Qing China with Hong Kong in the nineteenth century (Green, 2021).

Against this backdrop, the following section of the literature review focuses on describing and analyzing the evolution and current context of the China-Sri Lanka relations and the role of BRI in reshaping this relationship trajectory.

## **2.2. China-Sri Lanka Relations**

Ancient Sri Lanka had been considered as one of the emporiums or trading hubs of the ancient silk road (Rivers, 2004). Shared cultural values of oriental civilization, common religious linkages based on Buddhism and silk road trade relations were important elements of historical China-Sri

Lanka relations (Bastiampillai, 1990; Dewaraja, 2006). Sri Lanka was one of the first few countries that accepted new China through establishing formal diplomatic relations. Sri Lanka (then Ceylon) and new China quickly established strong economic relations with Sri Lanka. e. g. Sino-Sri Lanka Rubber-Rice Pact of 1952 (Kelagama, 2014). Sri Lanka also became a trustworthy mediator in the Sino-Indian conflict resolution and peace negotiation process (Zreik, 2018) in 1962. China provided military assistance during the last stages of the Sri Lankan civil war (Jaiswal & Bhatt, 2021) in 2007/2008. China also played an important role as a regime ally, providing an unconditional diplomatic support at the United Nations Security Council (UNSC) against the international allegations, preventing Security Council resolutions against Sri Lanka (Hein, 2017). This new relationship provided the basis for the resurgence of China-Sri Lanka relations in the past decade. China quickly stepped in as the main development partner for Sri Lanka by filling the lacuna of western investments into the country (Wheeler, 2012) in the aftermath of the conflict.

There are a number of theoretical frameworks in the literature that explain the contemporary China-Sri Lanka bilateral relations. As suggested by Abayagoonasekara (2021), deteriorating economic circumstances with multiple miscalculated strategic choices have weakened the state capacity of Sri Lanka, making it bandwagon with China. He further claimed BRI in Sri Lanka as a strategically carved path of China to extensively expand its scope of influence in the natural sphere of influence of India (Abeyagoonasekera, 2021). Analyzing the evolution of Sino-Lanka relations, Singh (2018) argues that China has never forgotten the historical blunder of unequal treaties during European colonialism and their implications to its economy and society, and is now repeating the same with other smaller and weaker countries, through creating new 'unequal treaties' with promises of investment and development. However, the reality is in the long run,

these ‘unequal treaties’, e.g. BRI in Sri Lanka could be a way for China to increase its influence over the weaker territory (Singh, 2018).

By contrast, according to Kelagama (2014), Chinese presence in Sri Lanka is a greater economic and commercial opportunity with the essence of China’s domination in the global economy as a rising power. Furthermore, analyzing the geo-economic and geo-strategic dimensions, Mendis (2012), claimed that, as a part of the new Silk Road network, Beijing’s expectation is to secure the pearls of its ‘string of Pearls’ naval strategy as strategic economic arteries. He further claimed Sri Lanka as the ‘crown jewel of the string of pearls’ anchored to the center of the new silk road which runs all the way from Persian Gulf to the South China Sea. Wheeler (2012) argued that though some are tempted to see China’s presence in Sri Lanka as a directed and planned offensive geo-strategic ploy of Beijing in order to encircle the South Asia, which is the natural sphere of dominance of India, China’s recent interest on Sri Lanka seems more as a strategic approach owing to the geo-strategic location of Sri Lanka which is vital important for China to hedge against the risks for its energy security along the east west maritime route (Wheeler,2012).

Debt trap is another conceptual dilemma which is being interested in the growing array of literature to interpret the Chinese BRI. Following section will focus on an in-depth analysis of literature that has described the concept of debt trap and Chinese debt trap diplomacy.

### **2.3. Debt Trap**

According to the definition of Oxford Lexico dictionary, the term debt trap refers to “a situation in which a debt is difficult or impossible to repay, typically due to high interest payments which prevent repayment of the principal.” (Lexico, n.d). However, the term dent trap diplomacy was

first coined and popularized by Indian geo-strategist, Brahma Chellaney in 2017 through his article ‘China’s Debt Trap Diplomacy’ which described the predatory lending practices of China in which poor countries would be overwhelmed with unsustainable debts and forced to cede strategic leverage to China (Chellaney, 2017).

Afterward, the term has been widely used among policy makers, media and scholars, particularly in the West in order to interpret the projects of BRI and its far reaching geo-political implications to the contemporary global order. US political elites and diplomats have been often seen using the term debt trap against BRI and China. Peter Navarro, Director of the United States Office of Trade and Manufacturing Policy, criticized Chinese investments in developing countries as an approach of debt-trap financing (Ferchen & Perera, 2019). In 2017, then U.S Secretary of State Rex Tillerson (2017) claimed that Chinese loans for infrastructure projects as a form of ‘predatory economics’, which results in ‘financing defaults and the conversion of debt to equity’ (Jones & Hameiri, 2020). The US Secretary of State Mike Pompeo has also warned on Chinese debt trap to African and Latin American countries claiming “predatory economic activity” (Ferchen & Perera, 2019). In 2020, during a state visit to Sri Lanka, former US State Secretary Michael Pompeo (2020) also dubbed China as a ‘predator’ (US State Department, 2020)

In 2018, The New York Times published an article titled, ‘How China Got Sri Lanka to Caught Up a Port’, analyzing the debatable dilemma of China-Sri Lanka relations, through ‘debt trap diplomacy’. After that, Sri Lanka became one of the most widely narrated examples for exerting influence through providing loans. According to the article, Hambantota Sea Port, which was constructed through the Chinese loans under BRI became a white elephant project without any real

time economic viability. Although the port is located a few miles away from the world's busiest international shipping lane, the port could draw only thirty-four ships in the year 2012. Therefore, with the inability of the government to make debt repayments to China, the government had to hand over the Port to the China Port Merchants Holding, a State-Owned Chinese firm to 99 years of lease. This debt to equity transfer has given an opportunity for China to control a territory just a few hundred miles away from India, and also a strategic base close to a strategic maritime route (Abi-Habib, 2018).

However, debunking the argument of debt trap, Jones and Hameiri (2020) claim that the debt crisis of Sri Lanka was not created by Beijing, but by Colombo. Analyzing the debt and repayment figures, they further argue that debt trap in Hambantota Port, and the Chinese loans in general as a clearly absurd claim (Jones and Hameiri, 2020; Wheeler, 2020). Weerakoon & Jayasuriya, (2019) also claim that although Sri Lanka has been engulfed by a debt trap, that is not created by China but has been created by Colombo and Western dominated financial institutions (Wignaraja et al, 2020). Some scholars claimed debt trap diplomacy as a rhetoric claim and a conspiracy theory which do not based on any evidence (Sautman & Yan, 2019).

Some scholars claim the debt trap as an unintended consequence of inappropriate project implementation of BRI (Rana et al, 2019). Some scholars further argue debt trap as a by-product of by state to state negotiations which is often carried out by political elites driven by political motivations without a proper policy evaluation process (Rana et al, 2019). Partially countering the concept of Chinese debt trap diplomacy, some scholars argue the debt trap as not a state-led strategy of China but a strategy of Chinese firms driven by earning profits through deals which are

built on much-needed infrastructure in the developing countries, exploiting the lack of infrastructure financing of these countries and lack of proper governance mechanism to regulate development policies. Therefore, instead of debt diplomacy, some scholars claim BRI as an approach to crony diplomacy (Akpaninyie, 2019).

#### **2.4. Research Gap**

As to above literature, it can be concluded that historically China had played a pivotal role, as an imperial power along the silk road, in which ancient Sri Lanka (then Ceylon) had been an important subordinate. The BRI is considered as the re-constitution of the ancient power relations along the silk road. This approach has brought forth a number of socio-economic transformations and chain reactions in the contemporary global order and thus has created a contentious dilemma in the existing literature and policy circles. In this context, scholars have made a number of efforts to describe and analyze the BRI through diverse conceptual and theoretical frameworks.

The debt trap diplomacy is one such debatable dilemma which is being often narrated with the BRI. Most of the recent literature has extensively used Sri Lanka as a classic example to demonstrate the implications of China's BRI to the global south, in particular to the debt trap diplomacy. Similarly, there are a number of arguments in the existing literature that counter the debt trap diplomacy in Sri Lanka. However, it is also imperative to note that most of the existing research that claims China in Sri Lanka as debt trap has used a case by case approach. For instance, most of the literature has used the Hambantota Port as an example to show the Chinese BRI in Sri Lanka as a tool of debt trap diplomacy.



Against this background, the literature review of this paper identifies a lack of evidence-based research that has analyzed the overall BRI framework in Sri Lanka to identify as to whether BRI resembles a debt trap or not. Building on this gap in the existing literature, this research paper will serve as an attempt to reanalyze the dilemma of ‘debt trap’ in regard to the context of the overall BRI framework in Sri Lanka in order to contribute to the existing literature of the subject arena.

### **3.0.RESEARCH METHODOLOGY**

Having established the purpose of this research paper, this chapter aims to outline the research methodology that is being undertaken in this research.

As described in the Chapter 01, this paper aims to conduct an in-depth and holistic study on China-Sri Lanka relations in regard to the ‘Belt and Road Initiative’ and ‘Debt Trap’, through analyzing the Sri Lanka’s project profile, investments and loans under BRI. Within this context, having understood the need of a comprehensive detailed analysis on the relations of two countries, this research has undertaken a combined method of ‘interpretive and evaluative case study’ under qualitative analysis as the research methodology.

“A case study is an empirical study that investigates a contemporary phenomenon within its real-life context when the boundaries between phenomenon and context are not clearly evident and in which multiple sources of evidence are used.”

(Yin ,1994)

“An interpretive case study is often used to interpret the data by developing conceptual categories, supporting or challenging the assumptions made regarding them. An evaluative case study aims to go further by adding the judgement of the researcher to the phenomena found in the data.”

(McDonough, J & McDonough, S., 1997).

Under the methodology of the interpretive and evaluative case study, this research includes both quantitative and qualitative data collected through secondary sources such as government and non-government reports, journal articles, newspaper articles and interviews, analyzed through the content analysis approach.

However, as the methodology of this research is the qualitative case study method, it is also important to understand that the study could include natural limitations of subjectivity which could be impacted by the experiences, observations, ideologies and perspectives of the author.

#### **4.0. ANALYSIS OF BELT AND ROAD INITIATIVE IN SRI LANKA**

The purpose of this chapter is to understand the anatomy of the BRI and to showcase how do the diverse BRI projects in Sri Lanka has contributed to the economic and social development of the country through a brief assessment of the key BRI projects in Sri Lanka. This chapter also focuses to evaluate the Chinese perspective on the BRI in Sri Lanka.

##### **4.1.The Belt and Road Initiative (BRI)**

In the year 2013, Chinese President Xi Jinping unveiled the official launch of silk road economic belt and 21<sup>st</sup> century maritime silk road, the most ambitious economic and geo-political initiative of new China. This strategy was first named as ‘One Belt One Road’- (OBOR) and composed of building connectivity and industrial corridors, to connect China to Europe via South East Asia, South Asia, Central Asia and Africa.

According to the government of China, the purpose of this massive initiative is,

“To promote the connectivity of Asian, European and African continents and their adjacent seas, establish and strengthen partnerships among the countries along the Belt and Road, set up all-dimensional, multi-tiered and composite connectivity networks, and realize diversified, independent, balanced and sustainable development in these countries.”

(National Development and Reform Commission, Ministry of Foreign Affairs, and Ministry of Commerce of the People's Republic of China, State Council authorization,2015)

The OBOR has been later renamed as ‘Belt and Road Initiative’, abbreviated by BRI, in which the term belt represented the oceanic wing of the project and road represented the territorial wing of the project.

Although, BRI is widely spoken due to its infrastructure development and connectivity projects, it is a multi-faceted initiative that has focused on cooperation of political, trade, finance, development and socio-cultural aspects among the partner countries. The Belt and Road Initiative is based on five priority elements. They are; i). policy coordination, ii). facilities connectivity, iii). unimpeded trade, iv). financial integration, v). people-to-people exchanges.

The anatomy of the Belt and Road Initiative (BRI) is composed of two major wings. (Figure 02)

They are,

- Silk Road Economic Belt – Territorial Wing of BRI
- The 21st Century Maritime Silk Road-Oceanic Wing of BRI

The territorial wing is composed of six key development corridors.

- New Eurasian Land Bridge Economic Corridor (NELBEC)
- China – Mongolia – Russia Economic Corridor (CMREC)
- China – Central Asia – West Asia Economic Corridor (CCWAEC)
- China – Indochina Peninsula Economic Corridor (CICPEC)
- Bangladesh – China – India – Myanmar Economic Corridor (BCIMEC)
- China – Pakistan Economic Corridor (CPEC)

The oceanic wing of BRI or the 21st century maritime silk road is composed of developing sea ports and canals to connect China to Southeast Asia, South Asia the Arabian Peninsula, Africa,

Central Asia and Europe, encircling the South China Sea, Strait of Malacca, Indian Ocean, Gulf of Bengal, Arabian Sea, Persian Gulf and the Red Sea.

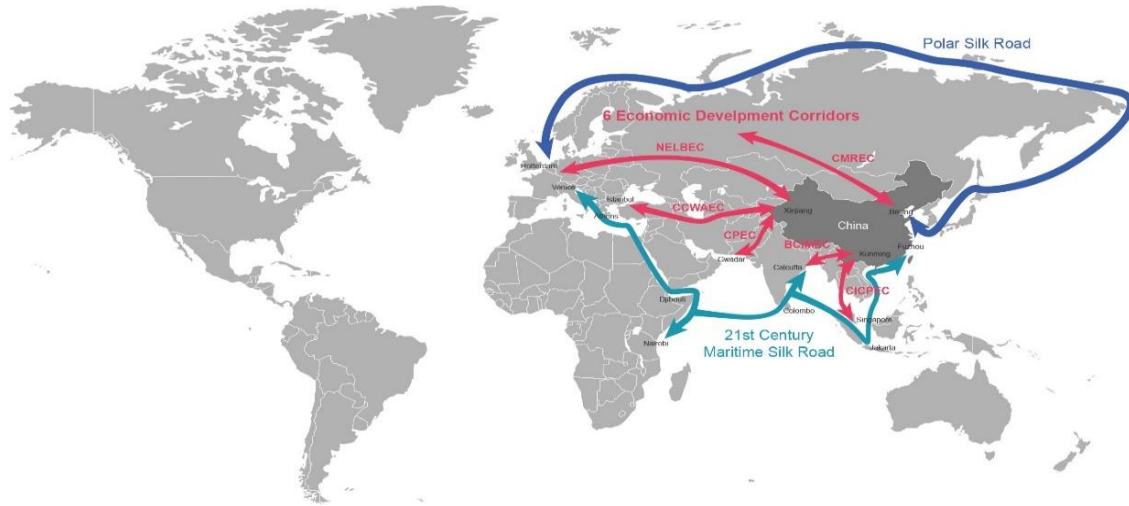


Figure 02-Anatomy of BRI

Source: Belt and Road Portal(2021)

#### 4.2.BRI Project Profile of Sri Lanka

Sri Lanka was among the first group of countries that openly supported the BRI in 2013. However, development assistance of China to Sri Lanka runs back to 1970s. Since then, there have been number of Chinese funded infrastructure development and industrial projects in Sri Lanka. Although the BRI has been officially announced in 2013, since the end of the civil war in 2008, China has started to hugely invest in Sri Lanka.

The Colombo Port City project is considered as the first official project announced under BRI profile in Sri Lanka. However, a number of other development initiatives started before 2013 also today considered under the profile of BRI. For instances, Hambantota Sea-Port, Mattala Mahinda Rajapaksa International Airport, Southern Lanka expressway are few such projects which has been

initiated before the official launch of BRI in 2013. However, later on, all these projects were taken under the BRI profile in Sri Lanka. It is also important to note that the BRI profile in Sri Lanka does not limited to connectivity and industrial development initiatives, but comprised a wide scope, expanding through multi-dimensional aspects of the socio-economic development of the country. (Table 01).

| Category                   | Description   | Key Projects   |
|----------------------------|---|--|
| Transport                  | This includes the building and reconstruction of roads, expressways, rail ways, seaports and airports                                 | <ul style="list-style-type: none"> <li>- Southern Lanka Expressway</li> <li>- Colombo-Katunayake Expressway</li> <li>- Central Expressway</li> <li>- Colombo outer circular highway</li> <li>- Hambanthota Sea-Port</li> <li>- Mattala International Airport</li> <li>- Colombo International Container Terminal of Colombo Port (CICT)</li> </ul> |
| Urban Development          |   | <ul style="list-style-type: none"> <li>- Colombo Port City Project (Colombo International Financial City)</li> </ul>   |
| Energy                     | This includes the projects that aims extraction of natural resources, renewable and non-renewable energy generation and transmission. | <ul style="list-style-type: none"> <li>- Norocholai coal power station</li> <li>- Hybrid renewable energy systems in Sri Lankan islands located in the Palk Bay. (cabinet approval received for the project)</li> </ul>  |
| Water                      |   | <ul style="list-style-type: none"> <li>- Kandy North Pathadumbara water supply project</li> </ul>  |
| People to people exchanges | This includes hard infrastructure investments related to culture, religion, tourism, health education etc.                            | <ul style="list-style-type: none"> <li>- Nelum Pokuna Auditorium in Colombo</li> <li>- The Lotus Tower</li> <li>- Mahinda Rajapaksa Convention Centre in Hambantota</li> <li>- China-Sri Lanka Friendship National Nephrology Specialized Hospital in Polonnaruwa</li> </ul>   |
| Telecommunication          |   | <ul style="list-style-type: none"> <li>- The Lotus Tower</li> </ul>  |

Table 01-Scope of BRI project profile in Sri Lanka

Data Sources: Central Bank of Sri Lanka, Ministry of Finance, Board of Investment

Although some of the projects have been called into question due to the lack of very economic viability and sustainability, most of these projects have been identified as economically viable initiatives. In addition to the economic viability, the most of the development projects has brought forth number of transformations, reducing the urban-rural development gap and enhancing the decentralization of development paradigm and socio-cultural development.

According to Asian Development Bank (2014), the Southern Expressway project is considered as a financial sustainable and socio-economically viable BRI project, which has connected the southern part of the country to Colombo, the commercial capital, reducing the journey time into just 1.5 hours. The Colombo-Katunayake expressway which has been connected to the central Colombo and to outer circular highway of the southern expressway has provided the direct, safe and easy access to southern part of the country from the international airport.

The development of the Colombo International Container Terminal (CICT) is another key BRI project in Sri Lanka. This project is a joint venture between China Merchants Port Holding Company and Sri Lanka Port Authority bound under a 35-year Build Operate and Transfer agreement. The construction of CICT has increased the annual throughput of the Colombo Port by 15% and the total volume by 38%. This contribution of CICT has upgraded the Colombo Port to the 11<sup>th</sup> best connected Port in the world. The CICT terminal is also considered as the only deep-water terminal in South Asia which is capable of handling the largest vessels afloat (CICT, 2021). The Norocholai coal power station, which is the biggest power plant of the country records for 31% of total installation capacity of the all the power plants owned by the Ceylon Electricity Board. In the year 2018, it has been recorded that the total power generation of the plant as 33%



of country's total power generation (Ceylon Electricity Board, 2021). The construction of the power plant has been financed by the EXIM bank of China (Ministry of Power-Sri Lanka, 2021). The China-Sri Lanka Friendship National Nephrology Specialized Hospital in Polonnaruwa, which has been constructed with the Chinese grant of US\$ 60 million is said to be the largest nephrology care hospital in South Asia. The hospital is a specialized facility to treat kidney ailments, a prevalent and recurring disease among the farming community of the north central part of the country (Sirinivasan, 2021).

Against this context, that it is apparent that the BRI projects in Sri Lanka has not confined to particular arena, but has expanded over various development aspects. Following the project profile analysis through a socio - economic perspective, it could be concluded that majority of the BRI projects in Sri Lanka has already generated a significant economic benefit to the economy, countering the argument in the existing literature that BRI projects are economically non-viable and unsustainable.

In addition to the direct socio-economic impact of BRI projects in Sri Lanka, it is also important to note that these projects carry a long-term prospect of bridging the significant infrastructure financing gap in the country whilst increasing the domestic and global connectivity. China's BRI approach became a greater and timely opportunity for Sri Lanka, to cope the much challenging infrastructure and development gap of the country, followed by a three decade long civil war. According to the Asian Development Bank (2017), South Asia has been identified as one of the highest infrastructure needed regions in the world. According to World Bank (2014), by 2024, South Asia requires US\$ 2.5 trillion investment to bridge its existing infrastructure gap. According

to calculations of Wignaraja et al (2020), current infrastructure financing gap in Sri Lanka has been estimated as US\$ 36 billion, which is around 40% total national GDP of the country. Furthermore, according to the data of World Economic Forum (2019), overall infrastructure performance of Sri Lanka lies well below the other upper middle-income countries. Sri Lanka's infrastructure performance ranks 61 out of 141 countries in the world implying a greater gap and need of infrastructure financing for multiple sectors. Therefore, the socio-economic benefit of BRI projects initiated with the fulfilment of the much-needed infrastructure financing gap of the country (World Economic Forum, 2019). This could also enhance the link of local markets with that of sub-regional, regional and global value chains increasing the long-term trade and investment opportunities for the country (Wignaraja et al, 2020)

#### **4.3.China's Perspective on BRI in Sri Lanka**

The Indian Ocean Region is considered to be highly decisive in terms of the energy security and strategic dominance of China (Singh, 2021). As the top oil exporter of the world, China's oil import from the Middle East region, which at present accounts for nearly 53% of the crude oil imported by China (General Administration of Custom in China, 2021), is categorically dependent on the international maritime route passed through the Indian Ocean. Simultaneously, export of Chinese products to Africa and Europe, which accounts for 20% of Chinese GDP (The Economic Times, 2020), are mainly dependent on the sea lines of communication which lie in the Indian Ocean region. More importantly, there are certain maritime choke-points along this sea line of communication, where shipping could be funneled. The most vital choking point for China in the Indian Ocean is the Strait of Malacca located between Singapore, Malaysia and Indonesia. With the basements in the Andaman and Nicobar Islands which are located very close to this narrow

water way, the Indian navy has a perfect opportunity to block the energy supply to China and exports from China in the event of a war. Therefore, from a Chinese perspective, it is vital for China to protect their raw material and export passage from the threats in peacetime as well as war time.

In addition, the increasing presence of the United States in the Indian Ocean region is also a critical factor for China's more assertiveness towards securing dominance in the Indian Ocean. The engagement of United States with Indian Ocean countries like India, Australia and Japan through its QUAD or Quadrilateral Security Dialog (Pal, 2021 ; Singh, 2021) and recent US initiative of AUKUS with Australia and United Kingdom to strengthen Australian naval power (US State Department, 2021) are viewed by China as a prospective alliance against the rise of China in the global political economy (Pal, 2021). Furthermore, historical tensions between China and India over territorial borders and increasing geo-strategic competition between these two countries to dominate its neighborhood have become decisive elements for Chinese perspective to ensure its strategic security in the Indian Ocean. Simultaneously, the strategic partnership of India and the US, which could also be viewed as a part of 'Off-shore Balancing' strategy of the US has also compelled China to secure its dominance in the Indian Ocean.

According to some analysts, China is encircling India through constructing Sea-Ports in its immediate neighborhood, which is called the 'Chinese String of Pearls', a geographical theory used to interpret the Chinese interest in the Indian Ocean Region (Marantidou, 2014; Ashraf, 2017). This strategy includes construction and developments of Sea-Ports at Chittagong in Bangladesh, at Karachi and Gwadar in Pakistan, at Colombo and Hambantota in Sri Lanka

etc. (Figure 03). This strategy has helped China to exert its power in the Indian Ocean Region as a ‘resident power’ not merely as an ‘extra regional power’ (Brewster, 2016).

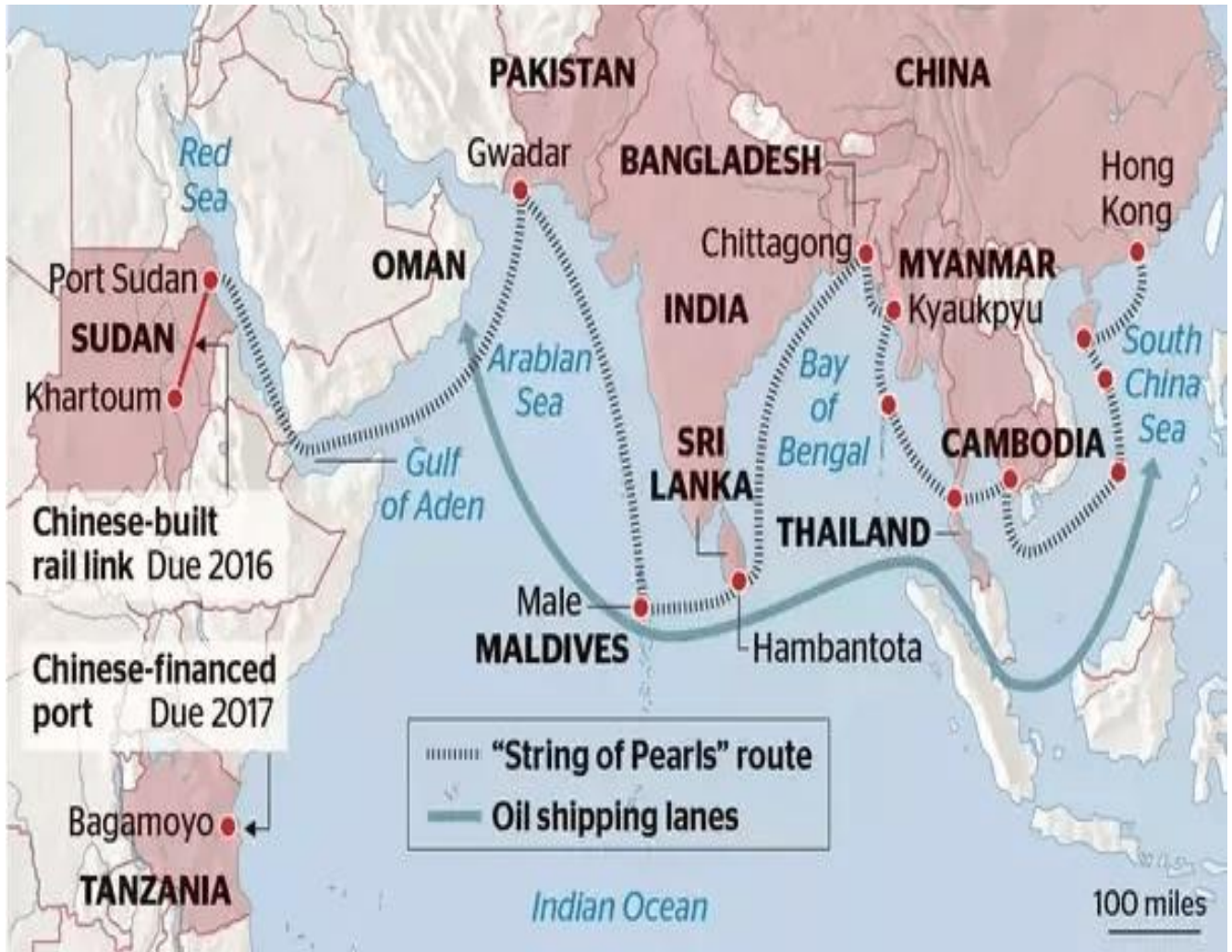


Figure 03-Chna’s string of pearls

Source: Global Village Space (2017)

In this context, analyzing China’s interest and growing presence in Sri Lanka, it needs to be viewed through the need of China to secure its energy security and geo-political competition with the US and India. Sri Lanka is located five to ten nautical miles away from the East West international sea line of communication. Therefore, Sri Lanka has been categorically identified as one of the most

appropriate location for a major navel military base to monitor the Indian Ocean and the world's busiest East-West maritime shipping lanes. Compared to the location of Sri Lanka, the locations of its South Asian neighboring countries are not able to cope with the geographical advantage of Sri Lanka. For instance, although the Pakistan, Bangladesh, and Maldives also possesses a unique geo-strategic importance, from a naval strategic perspective, Sri Lanka has been able to reap a competitive advantage (Awad & Todkar, 2021). On the construction of Hambathota Port, Robert Kaplan, the well-known geo-political analyst has said, "Because the Indian Ocean is sort of the world's energy interstate and China will have a maritime presence, perhaps even a naval presence in some distant morrow. So, the opening of this port in southern Sri Lanka is of real geopolitical significance" (Kaplan, 2012).

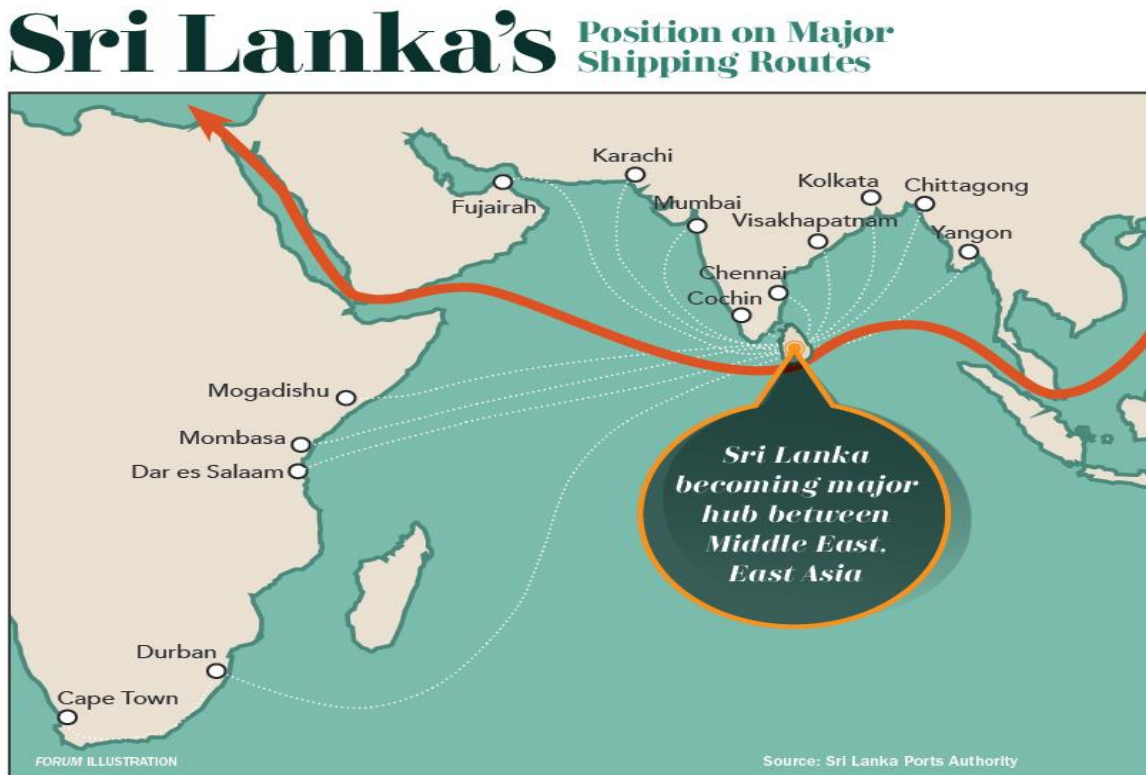


Figure 04-Sri Lanka's Strategic Location

Source: Indo-Pacific Defense Forum, 2018

On the other hand, Sri Lanka is located at the backyard of the Indian sub-continent. Sri Lanka and India are separated by the Palk Strait, which is a narrow water strip of 32 kilometers. (Figure 04) Therefore, it is vital to understand the importance of 'strategic unity' between India and Sri Lanka (then Ceylon) which is a decisive element to gain the dominance in the Indian sub-continent. (Kodikara, 1982).

In this context, it is cognizant that Sri Lanka is a vital element for China in ensuring its energy and raw material security, export security and countering the influence of India in the region. Therefore, from a Chinese perspective, investments and partnerships in strategic assets in Sri Lanka through its BRI, for instance Hambantota Port project, Colombo International Container Terminal (CICT) project, Colombo Port City project and etc. could be geo-politically and geo-economically decisive for China to balance the Indian dominance in the region.

## **5.0. CASE STUDIES**

This chapter aims to descriptively analyze two of the key BRI projects in Sri Lanka in terms of their impact to the politico-economic and socio-cultural aspects in Sri Lanka in order to identify as to whether these cases resemble a Chinese debt trap. First, the Hambantota Port project has been selected for this descriptive analysis due its widespread use in literature and policy circles as an example for the Chinese debt to equity transfer or dent trap diplomacy. This analysis attempts to focus on some of the key factors associated with the construction and lease of Hambanthota Port aimed at identifying as to whether this can be truly an example for Chinese debt trap or not. Second case study is the Colombo Port City Project. This has been selected for the descriptive analysis as it is considered to be the most expensive BRI project in Sri Lanka. Therefore, an analysis on this project aims to understand the economic spillover of the project in order to decide as to whether BRI in Sri Lanka is beneficial to the country or not.

### **5.1.The Case of Hambanthota Port**

Hambathota Port is often portrayed in the literature as a classic example of dent trap diplomacy of China. The project has been financed through the loans from EXIM Bank in China which has accounted US\$1.4 billion. China Harbor Engineering and Sino-hydro Corporation, two state owned Chinese companies became the main contractors to construct the port. (Department of External Resources, Sri Lanka, 2019; Wignaraja at el,2020) The first phase of the project was started with the US\$ 306 million loan from the Chinese bank with the interest of 6.3%. The second phase was started with the US\$ 900 million loan with the interest rate of 2%. Being located just a few nautical miles away from the east west international shipping lane, where daily thousands of

ships are passing, in the year 2012, the port could draw only thirty-four ships. (Abi-Habib,2018) According to the Department of Census and Statistics, Sri Lanka (2017), in the year, 2014 the ships that berthed at the port increased up to 335. In 2015 the number of ships were 295. In 2016, the numbers were 281. In 2017 the numbers were 230. (Table 02)

| Year            | 2012 | 2014 | 2015 | 2016 | 2017 |
|-----------------|------|------|------|------|------|
| Number of ships | 34   | 335  | 295  | 281  | 230  |

Table 02- Usage of Hambanthita Port (2012-2017)

Source: Department of census and statistics, Sri Lanka (2017) & The New York Times (2018)

The port was not able to generate a sufficient income to service the debt payment of the construction project. Therefore, in order to meet the bailout and loan repayment obligations of International Monetary Fund (IMF), the government of Sri Lanka led negotiations with several foreign investors for a joint venture of the port. As a result, the port was leased to China Port Merchants Holdings, a state-owned company in China for ninety-nine years for a price of US\$ 12 billion in 2017 (Reuters, 2017).

The joint venture is not a debt to equity transfer but a fresh Public Private Partnership (PPP) investment by the China Port Merchants Holdings with the Sri Lankan government. It is also reported that, at no time China forced the port deal, but it was a decision of the Sri Lankan government to bail out the port after the heavy financial losses (Wenhong, 2019) . According to the framework agreement signed by the government of Sri Lanka to lease the Hambantota Port under Public-Private Partnership, 20% of shares of the Hambantota Port are managed by the Sri Lankan Ports Authority and 80% of shares are managed by the China Merchant Port Holdings



Company. According to the agreement, the joint venture would be purely commercial (Wijenayake, 2017) and has not conferred any special status of fiscal power or extra territorial authority to China. Sri Lankan security forces, Emigration and Customs have the sole authority to manage all ins and outs of vessels, persons and cargo of the port. The port cannot be used for any military purposes (Wenhong, 2019).

It is also important to note that development of a sea port in Hambantota was not a proposal made by China. The original idea of this port runs back to the 1970s, where D. A. Rajapaksa, a Member of the Sri Lankan Parliament who represented the Hambantota district suggested to build a sea port in the area. (Jones and Hameiri, 2020). Later on, in 2001, then Minister of Ports and Shipping who is also the son of late D. A. Rajapaksa issued the gazette notification for the construction of the Hambantota Port. In 2007, Sri Lanka made an open request for the financing of the construction of the project, to which only China responded positively. According to the reports of the Sri Lankan government, both New Delhi and Tokyo have been directly approached for funding, to which a favorable response had not been received. New Delhi did not want to have a neighboring competitor to their ports whilst Tokyo had already been a biggest creditor to Colombo. (Jones and Hameiri, 2020) However, in spite of having several feasibility reports on the unsuitability of the location, the first phase of the construction of the port was initiated in 2007 with the funding of China. (Wijenayake, 2017).

The port is considered as one of the several other 'white elephant' projects carried out under Chinese loans in order to direct more resources to the home town of the then Prime Minister, Hon. Mahinda Rajapaksa through the greater Hambantota development initiative. (Jones and Hameiri, 2020). In addition to the vacant deep-water port, there is a 35,000-seat cricket stadium and a large

convention hall which were also two of the Chinese funded ‘white elephant’ projects of greater Hambantota development initiative. Furthermore, US\$ 209 million worth second largest international airport of the country was also a part of this development initiative. This ‘white elephant’ airport is also known as “the world’s emptiest international airport (Larmer, 2017-b). However, in 2018, reports came out that the Airport Authority of India (AAI) has planned to take the control of 70 % of the Mattala International Airport under a joint venture with the Government of Sri Lanka for a period of 70 years. (Attanayake, 2018)

Against this background, this section identifies following four important factors that show the narrative of debt trap diplomacy linked with Hambantota Port is an inappropriate concept.

- The open proposal to construct the Hambantota Port was made by the Government of Sri Lanka, not by China.
- Hambantota Port is one of the several other white elephant projects initiated in the Hambantota area, as a part of resource allocation to the home town of then President of the country.
- The ninety-nine-year lease of the port to China was a decision made by the government a request from the China.
- The lease is not a not a debt to equity transfer, but a Public Private Partnership, in which the port has been authorized to use only for commercial purposes.

Therefore, it is pragmatic to interpret that the case of Hambantota Port as a result of ‘mismanaged development policies’ by Colombo, not an intended trap by Beijing.

## 5.2.The Case of Colombo Port City

The Colombo Port City or the Colombo International Financial City is the biggest Belt and Road project in Sri Lanka constructed by the Harbor Engineering Company (CHEC) with an initial investment of US\$ 1.6 billion. (Figure 04) According to the social responsibility report of CHEC Port City, Colombo (2019), the project includes 269 hectares of reclaimed land from the sea, of which 178 hectares will be marketable land with the gross floor area up to 5.73 million square meters and the project intended to fill the lacuna between the international financial centers of Dubai and Singapore, becoming a gateway to South Asia. (CHEC, 2021)



Figure 05-Graphical view of Port City

Source: Daily FT (2021)

The city has been declared as a ‘Special Economic Zone (SEZ)’ through ‘Port City Economic Commission Act No.11 of 2021’ which has been passed by the Sri Lankan Parliament in May 2021. The main purpose of establishing a Special Economic Zone (SEZ) is said to create a single-

window facilitator in order to enhance the ease-of-doing business to attract investment to the city (Panchali & Gunawardhana,2021; Sulthana, 2021).

The project, being a Chinese partnership has been widely criticized as a security threat to the neighboring India. Although, the political elites, media and think tanks based in West and India vividly portrayed the port city project as another ‘predatory economic project’ that increases the strategic leverage of China in the island nation, the claims are still confined to political rhetoric. No evidence based analytical report or any research study has been found by the author in the literature to supplement the rhetoric claims against this project. However, as the key Belt and Road Initiative project in Sri Lanka, the Colombo Port City is intended to generate a vast number of economic and social benefits to the island nation. According to an economic impact assessment conducted by PricewaterhouseCOopers -PWC, a Colombo based consultant firm (2020), economic impact of the port city project has been identified based on five priority areas. They are; i.) employment, ii.) foreign direct investments, iii.) value addition, iv.) balance of payment, v.) government revenue. Furthermore, impact analysis of these five areas have been divided into three stages, they are; i.) reclamation and development stage ii.) construction stage iii.) operational stage.

According to the PwC report (2020), the number of employment opportunities generated during the reclamation and lease stage includes 6400 direct and indirect jobs. The number of direct and indirect man hours generated during the construction stage has been reported as 160 172. The number of direct and indirect employment opportunities that has been estimated to be generated during the operational period include 210 355. This estimation is based on available build up plan and includes skilled, semi-skilled and low- skilled employment opportunities (Table 03)

| Total Employment                              | 100% Development | 85% Development | 60% Development | 30% Development |
|---|------------------|-----------------|-----------------|-----------------|
| Reclamation/infrastructure/lease of land jobs | 6 400            | -               | -               | -               |
| - direct                                      | 1 500            | -               | -               | -               |
| - indirect                                    | 4 900            | -               | -               | -               |
| Construction stage-Man hours                  | 160 172          | 136 65          | 97 489          | 50 459          |
| - direct                                      | 101 375          | 86 492          | 61 702          | 31 936          |
| - indirect                                    | 58 797           | 50 165          | 35 787          | 18 523          |
| Operational stage-jobs                        | 210 355          | 177 097         | 121 698         | 55 181          |
| - direct                                      | 131 827          | 111 14          | 76 685          | 35 312          |
| - indirect                                    | 78 528           | 65 956          | 45 014          | 19 869          |

Table 03- Estimation of employment opportunities of Port City project

Source: PwC (2020)

In addition, the project is intended to attract foreign direct investments (FDIs) of any foreign currency and it is expected that Colombo Port City would potentially fill the gap between Dubai and Singapore to act as a highly desirable trade hub and an international financial center with modern infrastructure facilities (Cader, 2021). According to the PwC economic impact assessment report (2020), US\$ 4.1 billion of FDIs could be attracted during the reclamation, infrastructure development and land lease stage. During the construction stage the amount of FDIs has been accounted as US\$ 5.6 billion. During the stage of operation, annual profit that could be gained after the investment profit repatriation process has been estimated as US\$ 740 million per year. (Table 04 & Figure 06)) Concerning the current figures of FDIs which flow to Sri Lanka, accounting around US\$ 1.0 billion to US\$ 1.5 billion per year, the FDIs that would flow through the Port City project will be a significantly large amount. (Figure 06)

| Stage of the Project  | FDIs in US\$ billions |
|---|-----------------------|
| Reclamation/Infrastructure development and land lease stage | 4.1                   |
| Construction Stage  | 5.6                   |
| Operational Stage (Annual profit)                           | 0.74                  |

Table 04 Estimation of FDIs of Port City project

Source: PwC (2020)

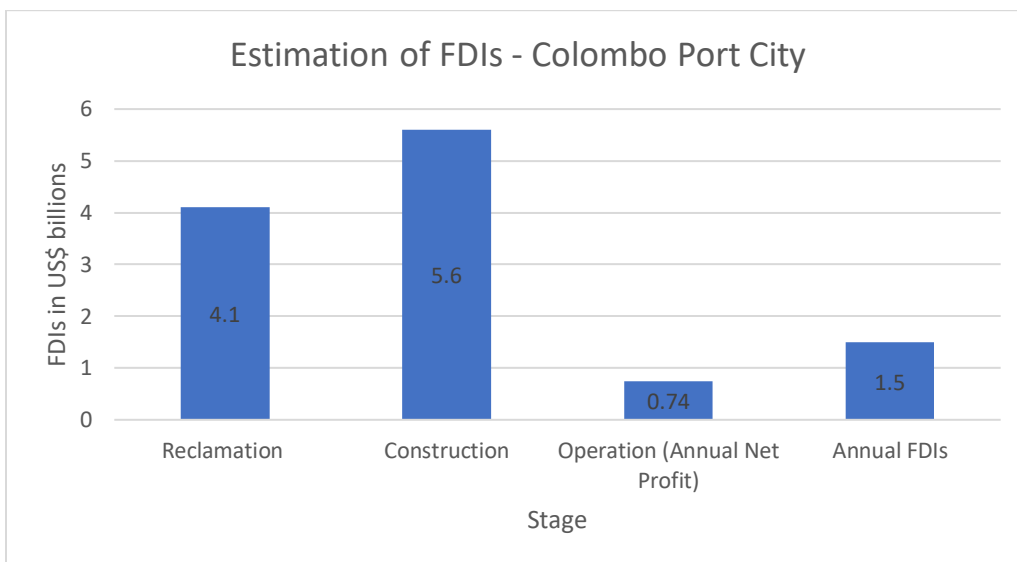


Figure 06- Estimation of FDIs of Port City project

Source: PwC (2020)

Against this trajectory, it is apparent that the prime BRI project in Colombo, the Port City or the Colombo International Financial City project is an economically viable project that could generate a number of commercial opportunities to the island nation, whilst boosting its economy through foreign direct investments, employment and diverse of other direct and indirect elements.

### 5.3. Comparison of Two Projects

For a wider and further understanding, a summary of the findings of this section, comparing above two projects is included as follows.

|   | <b>Hambanthota Sea Port</b>   | <b>Colombo International Financial City (Colombo Port City)</b>   |
|---|---|---|
| Nature of the Project                           | - A Sea Port constructed in the southern part of the country.   | - A special economic zone constructed adjunct to Colombo Port.  |
| Financial Commitment of China (Loan/Investment) | - Loan of US\$ 1.4 billion  | - Investment of US\$ 1.6 billion  |
| Benefits to Sri Lanka                           | - Has been identified as an economically unviable project.<br>- Only 234 ships have been drawn in 2017. | - Has been identified as an economically viable project.<br>- Employment, FDI and Urban development as major economic benefits                        |
| Benefits to China                               | - As a strategic location to control the east-west international maritime route.                        | - In addition to the profit repatriation.<br>- Proximity to India.<br>- As a strategic location to establish as a resident power in the Indian Ocean. |
| Current Status of the project                   | - Public-Private Partnership of Sri Lanka (20%) and China Port Merchant Holdings (80%)                  | - Investment by China   |
| Is it a debt trap?                              | - Evidence does not support the claim of debt trap.   | - Evidence does not support the claim of debt trap.   |
|   |   |   |

Table 05 - Comparison of Hambanthota Port & Colombo Port City

## 6.0. THE DEBT PROFILE OF SRI LANKA

The purpose of this Chapter is to analyze the debt profile of Sri Lanka in order to evaluate the claims of Chinese debt trap in Sri Lanka.

### 6.1. Analysis of the debt profile of Sri Lanka

A deliberate analysis of the debt profile of Sri Lanka could provide a clear and evidence-based picture to the existing literature as to whether the debt crisis of Sri Lanka is linked to the Chinese loans or not. Generally, debt profile of a country includes internal debt and external debt. Internal debt constitutes the borrowings from domestic banks and private sector, whereas the external debt constitutes the borrowings from the foreign lenders (IMF, 2001).

The external debt profile of the country is comprised with multilateral lenders, bilateral lenders and private lenders. (Figure 07)

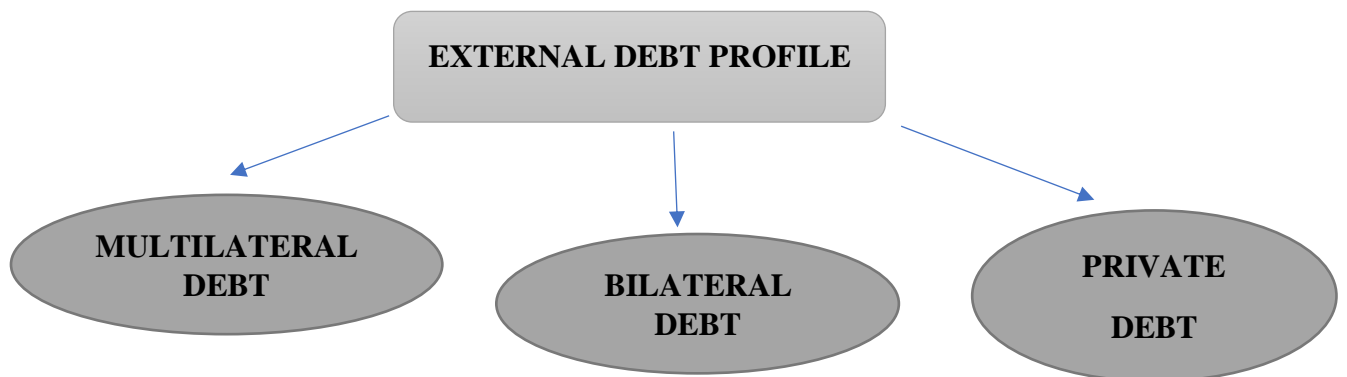


Figure 07 - External Debt Profile

Source: IMF & Department of External Resources, Sri Lanka



The debt profile of a country is often evaluated as a percentage of national gross domestic productivity. According to the Central Bank of Sri Lanka (2021), by the end of 2020, central government debt of Sri Lanka has been accounted as US\$ 81.7 billion whereas the nominal GDP of the country, by the end of December 2020 has been accounted only US\$ 21.8 billion. As a percentage, debt to GDP ratio has accounted for 101.0 % compared to the ration of 97.9 % in the previous quarter. This includes 60.6% of internal debt and 40.4% of external debt. It is also recorded that by the June 2021, this percentage has increased to 104.04%. In the year 2014, the percentage of debt to GDP has recorded as 72.3% which is also the lowest recorded value of the country. However, after 2014, the debt to GDP ratio has continuously increased, but shows a decline of external debt from the year 2018 to 2020. (Table 05 & Figure 08)

| <b>Year</b> | <b>Debt to GDP<br/>%</b> | <b>Total Debt<br/>(Rs.Bn)</b> | <b>External Debt<br/>(Rs.Bn)</b> | <b>Internal Debt<br/>(Rs.Bn)</b> |
|-------------|--------------------------|-------------------------------|----------------------------------|----------------------------------|
| June 2021   | 104.04                   | 16 564.50                     | 6 632 .80                        | 9 931.70                         |
| 2020        | 101.0                    | 15 117.26                     | 6 052                            | 9 065                            |
| 2019        | 86.8                     | 13 032                        | 6 201                            | 6 830                            |
| 2018        | 84.2                     | 12 031                        | 5 960                            | 6 071                            |
| 2017        | 77.9                     | 10 383                        | 4 719                            | 5 664                            |
| 2016        | 79.0                     | 9 479                         | 4 046                            | 5 433                            |
| 2015        | 78.5                     | 8 599                         | 3 544                            | 5 055                            |
| 2014        | 72.3                     | 7 487                         | 3 113                            | 4 374                            |

Table 06- Debt to GDP Percentage in Sri Lanka

Source: Central Bank (2021)

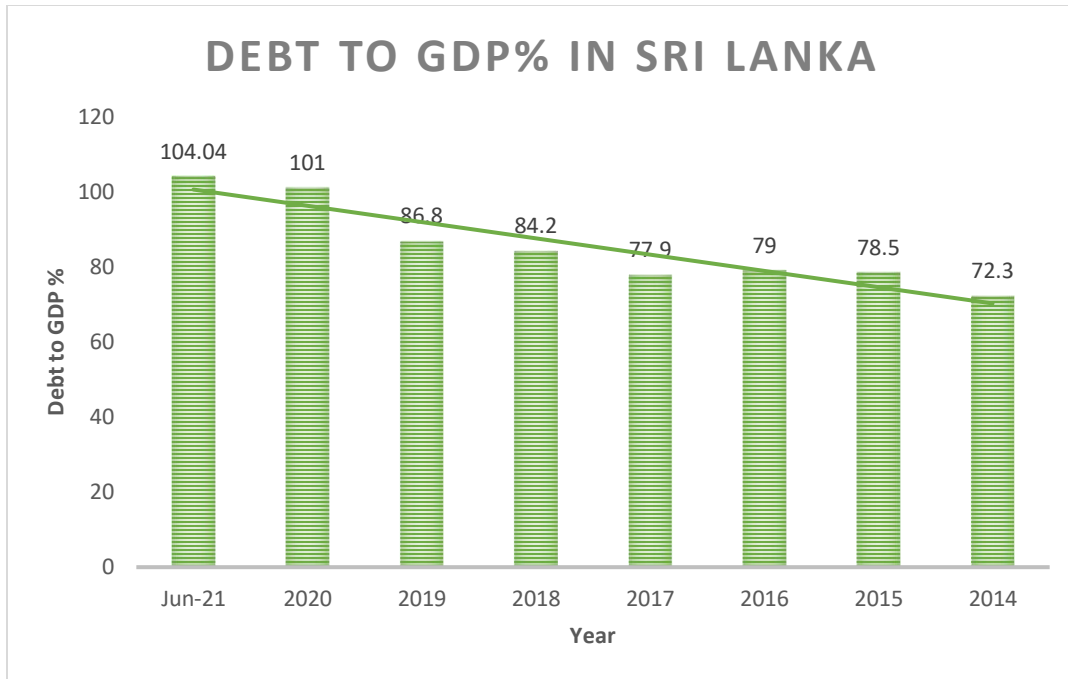


Figure 08– Debt to GDP percentage in Sri Lanka

Source: Central Bank, Sri Lanka (2021)

In addition, according to the data available in the Department of External Resources (2021), Sri Lanka’s total external debt commitment included US\$ 28.6 billion, out of China envisaged only US\$ 4.8 billion, which is nearly 16% of the total debt commitment. By 2017, the total external debt obtained to fund the infrastructure development projects of the government envisaged US\$ 51.824 billion, among which loans obtained from the China has accounted only US\$ 5.5 billion. This accounts nearly 10% of the total debt stock of the country (Central Bank, 2018 ; Carrei, 2018). In 2019 also, only US\$ 3.39 represented the debt commitment to China and this amount was nearly 10% of the total external debt stock of the country (Central Bank, 2020)

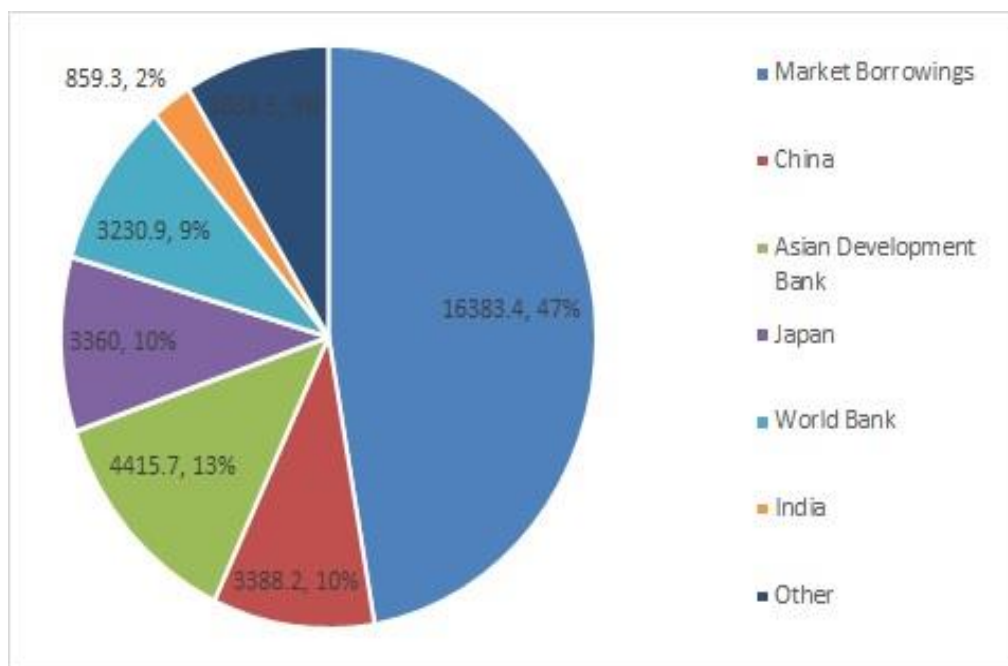


Figure 09- Debt Stock (by Major Lenders, US\$ million)

Source: Department of External Resources, Sri Lanka

According to the latest data obtained from the Department of External Resources, Sri Lanka (2021), by the end of April 2021, the major lenders of the country based on the debt stock include market borrowings, Asian Development Bank, World Bank, China, Japan and India. Around 47% of total debt stock belongs to the market borrowings and 13% of the debt stock belongs to the Asian Development Bank. The World Bank accounts for nearly 9% of total debt stock. China and Japan together account for nearly 20% of the debt stock, in which each country owns 10% of the total debt stock. (Figure 09)

Furthermore, according to the data obtained from the Annual Performance Reports of Department of External Resources, Sri Lanka (2007- 2019), there is an inconsistent pattern of Chinese portion of debt out of total external debt stock of Sri Lanka. In the year 2007, percentage of Chinese debt to Sri Lanka has been accounted as less than 3% of the total debt stock. In 2008, it has been

accounted as 2% of the total debt stock. However, in 2012 and 2013 this percentage drastically increased up to 12% and 13 % respectively. By 2016, percentage of Chinese dent has been further increased up to 17 % and by the end of 2017, it has been decreased to 12%. By the end of 2020, this amount has been further decreased to 10%. (Figure 10)

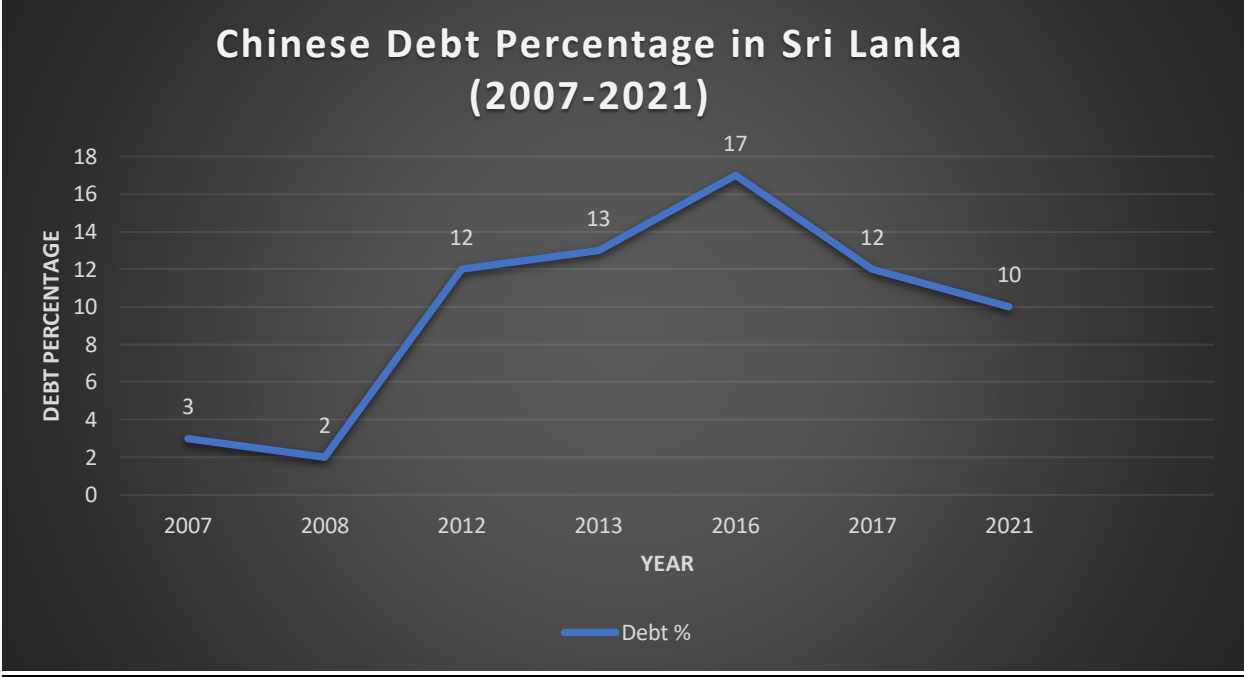


Figure 10- Chinese Debt Percentage in Sri Lanka

Source: Department of Externa Resources, Sri Lanka

Against this context, it is imperative to interpret that debt crisis of Sri Lanka is a structural macro-economic issue which has been proceeding for years. Although the average percentage of Chinese debt has increased with a significant amount (from 2% in 2007 to 10% in 2021), considering the total external debt profile, yet, the value owned by China constitute a comparative minimal value account for around 10%. By contrast, a considerable debt value is owned by multilateral lenders. Therefore, based on the aforementioned evidence analysis, it is pragmatic to conclude that the debt

crisis in Sri Lanka has minimum linked to loans granted by Beijing, but rather linked to loans granted by multilateral lenders.

## **6.2. Is China in Sri Lanka a debt trap?**

Based on the aforementioned analysis on BRI project profile in Sri Lanka and statistical evaluation of investment and debt profile in Sri Lanka, I wish to draw following conclusions.

- Currently, there are number of BRI projects in Sri Lanka, expanded over various development aspects, including urban development, transport, energy, water, telecommunication, people to people exchanges etc.
- Majority of these BRI projects in Sr Lanka has already generated a significant socio-economic benefit to the country.
- The positive impacts of BRI projects in Sri Lanka has been initiated with the fulfilment of the much needed and timely infrastructure financing gap of the country.
- Colombo Port City project is identified as the major BRI project in Sri Lanka, which has been estimated with a significant number of economic benefits including employment and foreign direct investments.
- However, it is also identified that the ‘cost to economic benefit’ of these projects differ from each other, implying that the several BRI projects are categorized as economically non-viable projects.
- The Hambantota Port is identified as one of the economically non-viable BRI project in Sri Lanka.
- It is also identified that unsustainable nature of these projects have been resulted due to the mismanaged development policies of Colombo.

- Also, there is not enough evidence to suggest that the ninety-nine-year lease of Hambantota Port is a debt to equity transfer.
- The evidences show that the lease of Hambantota Port is a Public Private Partnership, initiated by the Government of Sri Lanka, not a forceful deal of China.
- The analysis of debt profile in Sri Lanka clearly shows that the debt crisis in Sri Lanka is a long-proceeded issue resulted due to structural macro-economic issues.
- The debt profile of Sri Lanka shows a minimal contribution of Chinese debt to the debt crisis in Sri Lanka, which accounts only 10% of total external debt stock of the country.

Against this backdrop, this study finds lack of statistical evidence and data to support the claim that China has engulfed Sri Lanka in a debt trap. Therefore, based on the aforementioned conclusions, this study suggests that China's Belt and Road Initiative in Sri Lanka does not imply a debt trap.

## 7.0. INTERPRETATION TO CONTEMPORARY CHINA- SRI LANKA RELATIONS

Having identified the Chinese presence in Sri Lanka not as a debt trap, it is also imperative and pertinent to identify the nature of contemporary China-Sri Lanka relations. From a public policy perspective, this would help policy makers to understand the future tendencies and policy implications of this relationship.

According to the analysis and findings of previous sections, key motivations of China to enter Sri Lanka, through its BRI is based on its geo-strategic, geo-political and geo-economic interest in the Indian Ocean Region. However, by contrast, key motivation of Sri Lanka to be a partner of Chinese BRI is based on its economic development aspirations as a developing country. China and Sri Lanka relations could also be viewed as mutual diplomatic supporters at international levels. In addition, it is also important to consider the structural and functional differences of both countries, as a key element that could shape and direct the relationship trajectory between two countries. (e.g. size of the country, demography, size of economy, political structure, hierarchy in international level etc)

In this context, considering the contradictory primary objectives of both countries, it is imperative to view the current trajectory of China-Sri Lanka relation as an **‘Asymmetric and Imbalanced relation’**. The structural and functional differences between two countries and power relations of both countries at international level could further upsurge the asymmetry and imbalance of this relation.

## **8.0.PUBLIC POLICY PERSPECTIVE**

The purpose of this chapter is to identify the policy implications and possible future tendencies of the China-Sri Lanka relationship trajectory, in particular based on the BRI projects in Sri Lanka. Understanding the policy implications and possible tendencies of this approach will be of use to policy makers in the country in order to strategically divert, re-direct, re-shape or continue the existing policy and institutional framework. Additionally, this chapter focuses on suggesting policy recommendations to cope with the policy implications and tendencies of the BRI context in Sri Lanka.

Although the findings of the previous chapter imply the narrative of debt trap diplomacy in Sri Lanka, in particular the debt trap in BRI as a misapprehension, it is also imperative to understand that there are several other potential negative consequences and transformative effects of this Chinese approach in Sri Lanka. The policy implications of the current context of the Belt and Road Initiative in the island nation envisage a multi-dimensional pathway. The key areas of policy implications include development affairs, debt management, foreign relations, diplomacy, environmental affairs and socio-cultural relations.

### **8.1.Debt Policy**

It is evident that Sri Lanka has been facing a long proceeding general debt crisis, at present accounting for an annual debt stock more than the annual GDP. Increased debt stock to GDP ratio of the country could result in a variety of implications, including declining foreign currency reserves, high inflammation rate, decline of public welfare etc. Continuous borrowings for high



interest rates to service the existing debt installments could also be a possible tendency of a debt crisis.

Although the current debt crisis of Sri Lanka has not been created by the loans obtained from China, it is also important to understand the continuation of the current context could drive the country towards a tendency of a ‘Chinese’ or ‘other’ debt trap. Therefore, it is imperative for Sri Lanka to revise and redirect its debt management strategy towards a more sustainable approach.

To that effect, this study suggests the country should approach assistance from the IMF, as the lender of the last resort for debt crisis management. Also, this study suggests the country should strengthen its fiscal consolidations and economic reforms. Under this, in order to increase the national income, it is imperative to revise tax policies, strengthen the tax collection mechanisms and adopt import control policies of the country to cope with the debt crisis. In addition, it is also vital that the country adopts a ‘diversified debt portfolio’, minimizing the risk of a debt trap of a singular country which could possibly increase the strategic leverage of the lender over the borrower, resulting in compromising political and economic sovereignty of the borrowing country.

## **8.2.Foreign Policy and Diplomacy**

Current BRI context in Sri Lanka has made foreign relations and diplomacy the most pretentious and challenging arena in the country's public policy. The growing influence of BRI projects in Sri Lanka has created diverse political and security implications in the Indian Ocean region. These policy implications are apparently linked to two key aspects of the geographical location of Sri Lanka.

First, Sri Lanka is located a few nautical miles away from the East-West international shipping line which is vital for China, India, US and other key regional and global players to continue their global value chain and energy security. Second, Sri Lanka is located just a few miles away from the southern tip of the Indian sub-continent, within the same maritime security umbrella. These security implications make India concerned about the growing influence of China in Sri Lanka, which is the regional rivalry of India.

It is also imperative to understand the tendency of ‘power grouping’ in the Indian Ocean to counter the rise of China in the Indian Ocean. From Indo-Pacific Strategy to QUAD to the recent AUKUS initiative (US State Department, 2021), these power groupings mainly aimed at countering the rising domination of China in the Indian Ocean. In this context, growing assertiveness of China through BRI could potentially make the foreign and diplomatic relations of Sri Lanka more difficult and challenging. Current tendency of ‘Indo-China Cold War’ in Sri Lankan affairs could increase, resulting in wider political, economic and security implications.

In this background, a deliberate management of the foreign policy and diplomatic relations with China and the rest would be vital. Therefore, this study suggests the policy makers in Sri Lanka to vigilantly consider the existing power relations in the Indian Ocean and the tendency of a more assertive version of ‘Indian Ocean Cold War’ and reshape the existing foreign policy and diplomatic framework.

Although the government of Sri Lanka claims that the underpinning concept of the country's foreign policy is the framework of ‘Neutrality’ (Foreign Ministry, 2020), it is observed that the foreign relations of the country is heavily dependent on the political aspirations of the existing

regime of control. However, as a small island nation surrounded by power relations of big neighbors, it is vital for Sri Lanka to adopt a bi-partisan foreign policy framework based on the framework on Non-Alignment. This study suggests the country should strengthen its relations with both India and China with equal footing. Vigilant implementation of BRI projects focusing more on non-strategic projects and increasing the development partnership with India and other regional neighbors are also suggested as policy recommendations to maintain a balanced relationship with both countries.

### **8.3. Development Policy**

Concerning the ‘cost to benefit’ evaluation of certain BRI projects in Sri Lanka, it is vital that policy makers in Sri Lanka rethink the development policy approach of the country. Chinese loans for infrastructure development projects which have been recipient driven and state to state driven in nature could be a potential future risk of an additional burden of politically motivated ‘white elephant projects’ to a country which has a weak development strategy. Therefore, it is vital for Sri Lanka to develop a strong development policy framework including legally binding elements such as fiscal transparency and accountability.

This study further suggests the development policy makers in the country to formulate the development agenda of the country under a bi-partisan national policy framework, underpinned by a scientific evaluation which could potentially minimize the utilization of development finance to accomplish personal political aspirations. This study also suggests to diversify the development finance agents and sectors, focusing more on export-oriented and high-tech industry development, which could also potentially lead the country towards more long term and sustainable economic benefits. Additionally, this study suggests alternative methods for development loans such

as approaching methods of joint ventures, public private partnerships, build operate transfers and official development assistants.

#### **8.4.Environmental and Social Policy**

From an environmental and social policy perspective, it is imperative to understand the environmental and social implications that could possible arise as a result of the implementation of the BRI projects in Sri Lanka. Failure to meet the environmental impact assessments and feasibility studies could yield long term impacts including environmental pollution, increased threshold of natural disasters, change of the eco-system etc.

Therefore, it is vital to consider the aspect of environmental governance in BRI projects. In this context, this study suggests Sri Lanka to strengthen its existing framework of environmental impact assessment as a legal binding element of the project implementation framework. Additionally, introduction of environmental sensitive, specific tax policies such as ‘polluter pay’ will be useful in the operational stages of projects.

The policy implications of BRI projects to the socio-cultural dimension also need to be taken in to the due consideration as an important element of the BRI in Sri Lanka. In particular, arrival of illegal labour migrants to work in BRI projects, inclusion of Chinese cultural and linguistical aspects to the local society could be possible future tendencies that the government needs to pay attention. In order to prevent the impact of such possible tendencies, it is important to government to introduce new domestic laws to regulate the illegal labour migration etc.

## 9.0.CON CLUSION

This research paper aimed at analyzing the Belt and Road project profile, investment and debt profile in Sri Lanka in order to identify the contemporary Chinese presence in Sri Lanka through the concept of debt trap diplomacy. This paper attempted to answer the debatable dilemma of debt trap of BRI, through the case study of Sri Lanka.

First, the findings of this research identify the approach of BRI in Sri Lanka as a greater economic and development opportunity, although, from the Chinese point of view, Sri Lanka provides a geopolitical and geo-economic opportunity to China, in order to ensure its energy security via Indian ocean and counter the influence of India. According to the findings of the research, BRI has supported the country to fulfill its massive and much needed infrastructure gap in diverse sectors. Although popular literature mainly focuses on the connectivity development aspect of the BRI, this research firmly presents the diversity of BRI projects, which has been expanded through multiple sectors such as transport, energy, water, telecommunication, health, culture etc. The statistical evidence of this research further shows a number of economic and social benefits of key BRI projects in Sri Lanka. e.g. Expressway Projects. Coal Power Plant, Colombo Port Development, Port City Project etc. However, this study also reveals several BRI projects which have been economically non-viable and unsuitable. This mainly include the infrastructure projects carried out in the Hambantota region of the country. Furthermore, manifested firmly on the analysis of this research paper, the author views the China-Sri Lanka relation as an ‘Asymmetric and imbalanced relation’ , mainly due to the contradictory primary objectives of both countries.

e.g. geo-political vs economic. The sustainability of an ‘asymmetric and imbalanced’ relation between two States should be analyzed by further research.

Second, evaluating the case of Hambantota Sea Port and the debt profile of the country, this research identifies the existing debt crisis of the country as a long preceding structural issue of the economy, not a trap by China. Third, manifested by the in-depth analysis of the Hambantota Port deal, it is identified as a public private partnership based on economic purpose, not a debt to equity transfer. In this context, this study argues that the China in Sri Lanka does not imply a debt trap. Additionally, research findings suggest the recipient driven nature of BRI together with the lack of financial governance and political motivations caused for the non-viable Chinese development projects in Sri Lanka, which has a little contribution to the existing debt crisis of the country.

However, though the China in Sri Lanka does not imply an intended debt trap of China, there could be other policy implications driven by the current Chinese approach in Sri Lanka. To this effect, this study identifies several challenges and tendencies in debt policy, development policy, foreign policy, diplomacy, environmental policy and social policy. To cope with these challenges this study suggests the government of Sri Lanka to redirect its debt management policy into a more sustainable approach through consolidating fiscal policies. This study further recommends the government to redirect its development policy, strengthening the existing legal and institutional framework to ensure the financial accountability, transparency and evaluation process of development and investment projects. It is also recommended to approach a bi-partisan development policy to minimize the political motivations of development agendas.

From the foreign policy and diplomatic perspective, this research suggests the government should strengthen its existing bilateral relations with the counter powers of China, moving towards a more balanced diplomatic approach. A vigilant management of a balanced foreign policy within a bipartisan framework would be decisive to prevent the country being a 'field' of global and regional power play. This study further suggests to improve the environment governance of BRI projects by strengthening the legal framework of environmental impact assessments of development projects. This study also suggests the government to consider the possible tendencies of socio-cultural changes due to the increased presence of china in the country and implement appropriate legal framework in order to ensure the socio-cultural security of the future citizens.

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