Dragoman Digest

China set to limit lending to African countries amid growing default risk

Gone are the days when China would unquestioningly shower the continent with billions in loans

As controversy continues over **China**'s loans to African nations, Beijing recently signalled a cut to the amount of lending provided to the region. With pandemic-related economic hardship making the likelihood of default higher, President **Xi Jinping** also revealed that instead of loans for big-ticket infrastructure projects, Beijing will increasingly rely on private sector investment in Africa as well as targeting greener projects and investment in SMEs. Chinese banks currently make up one-fifth of all lending in the region, with the IMF listing more than 20 African countries as being in, or at high risk of debt distress. In addition to exacerbating debt distress, critics allege that China's lending has created clear sovereignty concerns surrounding the management of national assets in **Uganda**, **Zambia**, and **Kenya**.

Though elements of these concerns are based on embellishment and mistruths, some of them have a clearer factual grounding. Entebbe airport in Uganda is one such case. Under the contract (which is governed entirely by Chinese law), the Ugandan Civilian Aviation Authority is required to deposit all revenue into special escrow accounts to guarantee loan repayment to China's Exim Bank. It also has to submit budgets to Exim Bank for approval. The explicit details of the US$200m loan appear to have been negotiated in private, with Uganda's parliament only shown a preliminary version of the contract.

These problematic clauses are not unique to Chinese financiers, with Western lenders also historically imposing harsh adjustment programs on loan repayments. However, though Western lenders also use escrow accounts, the practice is significantly more common with Chinese loans. With the realistic chance of defaults in the next few years, it remains to be seen how Chinese lending practices will evolve.

Regional Comprehensive Economic Partnership (RCEP) swings into action

RCEP is set to accelerate the regionalisation of trade, with Japan and China emerging as the biggest winners

The world's largest free trade deal has come into force, covering approximately 30 percent of the world's GDP and population. **Australia**, **China**, **Japan,** and **New Zealand** are among 10 members who have already completed ratification. **Indonesia**, **Malaysia**, **Myanmar,** and the **Philippines** are set to officially join in February. RCEP is expected to eliminate 90 percent of tariffs on exports between signatory countries across the next 20 years.

Japan is placed to be the biggest beneficiary of the deal, with a US$20.2 billion increase in exports predicted off a 2019 baseline, with China coming in second (US$11.2 billion expected increase). Whilst Japan is the biggest winner in sheer dollar terms, the deal will amplify China's political influence, with regional trade expected to become even more Sino-centric. This is a particular cause of concern for Japan, which is still holding out hope that **India** can be persuaded to join the agreement.

In light of Beijing's increased influence, the **US** has announced plans to develop an Indo-Pacific trade pact. However, the exact details and timeline of this deal are yet to be revealed and it is not clear that it will be legally binding. Failure by the US to develop a material economic alternative will significantly undermine its ability to counter China.

Israel shifts its approach to the US-Iran nuclear deal

New reports signify that Israel is now angling to benefit from any revised nuclear deal between the US and Iran

Despite I**srael'**s initial outspoken concern over the JCPOA – or **Iran** nuclear deal – Tel Aviv's revised assessment indicates that it now views the deal as inevitable, and not necessarily as threatening as it once was. This comes as a surprise given the current deadlock in Vienna, with several sticking points remaining in negotiations between **Iran** and the **US**. Tehran has repeatedly insisted that it wants Washington to provide a legal guarantee that the US will not pull out of the deal again if it is restored – a difficult proposition given President **Biden'**s divided Congress. The timing of sanctions relief and Iran returning to compliance is also another source of friction.

Several factors underlie Israel's changing perceptions. Tel Aviv clearly understands that the US is now angling to reduce its presence in the Middle East to help its renewed pivot to the Indo-Pacific. It also anticipates that President **Raisi** is eager to improve Iran's economy and is less politically vulnerable to attacks undermining his national security credentials than his predecessor, Hassan Rouhani. Biden's renewed willingness to consult allies in the region is another factor that has helped mollify Israel. As part of a new JCPOA agreement, the US has signalled that it would commit to maintaining the military edge of allies – chief of all Israel – over Iran. Military contingency planning is also likely to workshop options, if after the sunset clauses expire, Iran continues to move towards nuclear weapons.

China's growth forecast reduced as Covid-zero policy takes a toll

Major supply chain disruptions anticipated in light of China's continued health policy

With 20 million people in lockdown in **China** and concerns more cities could be affected, current restrictions are now the broadest that they have been since the beginning of the pandemic. There is some talk that a nation-wide lockdown may even be on the cards.

Amid these disruptions, major manufacturers across China are taking a financial hit as testing requirements and lockdowns block ports and furlough workers. Volkswagen, Nike, and Samsung are among key players already encountering delays. Omicron is also weighing on China's growth forecast, with Goldman Sachs this week cutting China's 2022 growth forecast from 4.8 percent to 4.3 percent as the variant continues to spread. Growth of 4.3 percent would be China's slowest growth (with the exception of 2020) since 1989.

Underscoring China's centrality in global supply chains is the case of Ningbo Port. Located near Shanghai, Ningbo is the world's third busiest container port. Just one week's delay at the port could affect trade valued at US$4 billion. With concerns that China's Omicron wave will inevitability spread to more cities, economists warn that Chinese supply chain disruptions will become yet another inflationary pressure in the West.