



Commemorating the 100th Anniversary of the Communist Party of China

**DIALOGUE ON CHINA-SRI LANKA RELATIONS
AND THE BELT AND ROAD INITIATIVE
Critical Success Factors & Challenges**

Pathfinder Foundation & China Reform Forum
March 16, 2021

AGENDA OF THE VIRTUAL DIALOGUE

Main Topic

China-Sri Lanka Cooperation and the BRI in Post-Pandemic Era
(Chinese and Sri Lankan perspectives)

Moderators **Pathfinder Foundation & China Reform Forum**

1:30 pm – 1:50 pm **Welcome by Hosts**

1:50 pm – 2:15 pm **China Reform Forum Perspectives**
(25 minutes. Five speakers x 5 minutes each)

2:15 pm – 2:45 pm **Pathfinder Foundation perspectives**
(30 minutes. six speakers x 5 minutes each)

Speaker 1: Cross-cutting Policy Issues

Speaker 2: Economy and Trade

Speaker 3: Investment Policy

Speaker 4: Tourism

Speaker 5: Apparel

Speaker 6: Real Estate

2:40 pm – 3:20 pm **OPEN FORUM**

3:20 pm – 3:30 pm **Closing Remarks**

REPORT OF THE PATHFINDER FOUNDATION

INTRODUCTION

Relations between the Pathfinder Foundation and China Reform Forum commenced back in September 2019 with plans to conduct a seminar on Sino-Sri Lanka Relations; Sino-Sri Lankan cooperation under the BRI; and Sino-Sri Lankan security and counter-terrorism cooperation, among other topics of common interest. However, this event was cancelled due to the initial outbreak of Covid-19 in China. Following the first wave of the pandemic in October 2020, both organizations signed an MOU and re-commenced their dialogue as part of academic exchanges. The focus of this first dialogue / webinar was China-Sri Lanka Cooperation with regard to the Belt and Road Initiative, where in their specific presentations, each speaker paid attention to success factors as well as risks and challenges that shape relations between the two countries.

Although, with a history of two millennia, in the modern era, the Rubber- Rice agreement of 1952 against the wishes of the Western powers; establishment of diplomatic relations in 1957; Sri Lanka's support for 'One China' policy; steadfast military support extended to Sri Lanka during the separatist war that lasted for nearly 30 years; development of economic cooperation following the end of the conflict in 2009 and the diplomatic support that has been the cornerstone of our relations; when Sri Lanka faced alleged human rights violations in Geneva and at the UN Security Council; were major milestones of our cooperative relationship. 2014 was a watershed year for China-Sri Lanka relations when during the Chinese President Xi Jinping's visit to Colombo, 27 agreements were signed. Highlighted of the visit was Sri Lanka's support of BRI, while the concept was still under formation.

Sri Lanka is a democratic country, with regular elections resulting in change of governments. However, BRI has bi-partisan support, as demonstrated by the support extended in 2014, which was reconfirmed by the new administration at the BRI Summit held in May 2017. Since then, we have witnessed high scope for development of economic relations and investment opportunities. Roads, railways, seaport & airport and power generation projects were some major economic projects undertaken under BRI. Much larger economic opportunities may become possible, if industrial zones as envisaged in Hambantota, become a reality. Consequently, over the years, Chinese companies have gained experience in engaging in business and investment activities in Sri Lanka. The most significant of these is the Colombo Port City project, a 100% a foreign investment by China, which is now ready for infrastructure development.

In terms of challenges faced, politically motivated adverse propaganda internationally, against Chinese investment in Sri Lanka i. e. alleged debt trap, has been a deliberate propaganda campaign against BRI. Another critically important factor is Return on Investment (ROI). Failure to give due weightage to this factor by the lender or borrower may result in failure of the project, creating ill effects on the lending institutions and the good name of China. Global pandemics such as what we are currently facing, economic depressions or meltdowns like what we have experienced during the end of the 20th century and again in 2008 are other risk factors we may have to face in the future. In such an instance, major development projects could get derailed due to such conditions, resulting in economic consequences to both China and other countries relying on BRI. For the relationship to sustain and thrive, we need to address present and potential challenges efficiently.

We are grateful to the Embassy of China in Colombo for recommending the Pathfinder Foundation to China Reform Forum for an engagement of this nature.

OPPORTUNITIES

1. An Investment Agreement will give a strong tailwind to Sri Lanka's pivot from debt to equity. Chinese capital can play a transformative role in the entire Sri Lankan economy built on such landmark projects such as the Port City and the Hambantota Industrial Zone.
2. China is well placed to assist in technological upgrading that has to be an integral part of the government's drive to build a production economy. Huawei's world beating technology can promote Sri Lanka's migration to 5G expeditiously.
3. At present, there is a rapidly increasing number of Sri Lankans enjoying the benefits of training programs in China which is vital in promoting people-to-people contact.
4. The Sri Lankan economy is now focused on "Backward Integration" and value addition with regard to developing the economy. There are plans to establish a US\$ 5.5 billion export generation sector and invites large, Chinese Fortune 500 companies to set up investments in this zone.
5. With international travel most likely to be regional in the upcoming months, Sri Lanka's location and reputation as a sought-after travel destination in Asia will be appealing to Chinese outbound tourists. Online presence in Chinese digital platforms, digital transactions and accessibility will be an advantage.
6. The middle class of China that has benefitted from economic growth will be a market looking for experiences overseas. A majority will opt for an established hotel or resort and as a tech-savvy generation, they are quick to communicate online and a pleasant experience at a destination will be shared with friends and family, creating organic awareness.
7. Joint ventures with Chinese fabric giants, have over the years worked in Sri Lanka and helped localization of fabric.
8. While leading Chinese manufacturers are benchmarked in terms of the best, there is also increased manufacturing technology and capability growing in China, particularly in automation and other areas where Sri Lanka can partner with China to gain expertise in technology transformation.
9. There is much potential for Chinese apparel manufacturers to collaborate and set up operations in Sri Lanka and work together on some of the orders that are moving out of China but can be reclaimed as part of their investments.
10. Due to the restriction on Xinjiang cotton and global brands looking for mitigation of risks, Sri Lanka can be an important location for China given the cultural connectivity as well as the strategic government to government partnerships that can be established and taken further.

11. Colombo Port City is an engineering marvel and sharing of knowledge in reclamation with Sri Lankan engineers who have been working together with Chinese experts on the project. has been invaluable.
12. Job creation – During this phase of construction, CPC has generated over 1400 jobs, a further 130,000 will be created once it is operational.
13. It is encouraging that negotiations are recommencing on the partnership agreement between China and Sri Lanka.
14. Bringing in a world class port operator like China Merchant Port Holdings into Hambantota will not only develop the port but also leverage the networks with shipping companies.
15. People's Bank of China has already provided SWAP arrangements to Central Bank of Sri Lanka and so has China Development Bank. This kind of financing is extremely helpful to create the kind of space needed in the economy.
16. The government is trying to finalise the legal regime applicable to CPC and other investment related legislation including the Inland Revenue Act, the Foreign Exchange Act as well as the Board of Investments Act, in order to make Sri Lanka a much more investor friendly environment, provide security for their investments and also to facilitate repatriation of profits. Multiple initiatives are ongoing to improve the ease of doing business in the country.

RISKS/ CHALLENGES

1. Economic costs of Chinese infrastructure investment to Sri Lanka include rising trade deficits with limited spillovers from Chinese projects. An increase in Chinese projects is associated with rising Chinese imports and poor performance of Sri Lanka's exports to China. Sri Lanka has had limited indirect spillovers such as industrialization, exports or employment from Chinese projects. This is a complex issue related to the enclave nature of some Chinese infrastructure investments.
2. Differences in food and culture and the communication barrier pose a problem during a guest's stay as well as in marketing the destination.
3. Local perceptions and receptiveness
4. Escalating tensions between global powers - Sri Lanka, given its strategic location will face challenges arising from this escalation of tensions amongst major global players.
5. Since 2018, the State Council of China imposed restrictions on overseas investments by Chinese companies in order to restrict capital outflows from China.
6. Perception of the lack of economic opportunity created locally by Chinese projects.
7. Lack of a consistent policy environment in Sri Lanka to ensure continuity of projects and sustain the relationship between the two countries.

RECOMMENDATIONS

1. In the current global and bilateral context, it is important to agree on a trade, investment and tourism framework to facilitate substantial increase in the value of bilateral transactions. Such a comprehensive framework can be built on principles of non-reciprocity and special and differential treatment.
2. Establishment of a technical education Centre will support both Sri Lankan youth as well as Chinese investors in Hambantota and other locations in Sri Lanka.
3. Adhere to the principle of policy coordination which is an important pillar in the BRI. In order to materialize this, it is a necessary condition that both sides study each other's laws and regulations and explore the possibility of harmonization where necessary, particularly by promoting two-way investment, trade and other businesses.
4. The need for rigorous social cost benefit analysis of infrastructure projects, improved infrastructure master planning, and reducing long lags between construction and project operation will result in effective implementation and conclusion of projects.
5. In order to strengthen the debt management system to reduce debt related vulnerabilities and to improve debt transparency with assistance from IFIs, Sri Lanka needs to request a moratorium on interest payment of Chinese debt for 3 years to facilitate overall debt sustainability; and increase its share of infrastructure financing from the AIIB, which offers relatively low-cost infrastructure financing at high procurement and environmental standards.
6. Sri Lankan firms have difficulty exporting to China due to trade barriers, poor market information and language barriers, therefore there is a need to remedy these issues.
7. To maximize benefits, it is suggested that:
 - The Industrial Zone adjacent to Hambantota Port and the Colombo Port City could be attractive to international investors looking to relocate from China and Hong Kong to other parts of Asia.
 - Sri Lanka should step up efforts to attract export oriented FDI from China by better investor targeting, cutting red tape affecting business and ensuring a predictable macroeconomic environment.
 - Sri Lankan firms should develop links with Chinese buyers and become familiar with demands of Chinese consumers and China's Sanitary and Phytosanitary Standards and Technical Barriers to Trade regulations.
8. Sri Lanka's strategic vision for Colombo Port City should be shared by China. The integrated development transcends beyond a piece of real estate and from a strategic point of view, should be seen as a bedrock of hub operation and sits in a key position in the BRI pathway. Large Chinese firms could set up their regional headquarters at CPC so that it will trigger the growth of Colombo city as a regional headquarters hub.
9. It is important that Sri Lanka maintains a visible presence on Chinese digital platforms and search engines such as *Baidu*, which lists websites in Mandarin, as Google is not accessible from mainland China.

10. Facilities to accept and process payments via e-wallets will provide a convenience to Chinese travellers in Sri Lanka.
11. In order to move forward and bring in the growing upper middle class of Chinese society to Sri Lanka, a change in mindset and strategy and data-driven and targeted marketing is important.
12. Backward integration in supply chain and other partnerships can be further enhanced to have more localization in Sri Lanka.
13. Consider bringing sewing technology and capability from China, which would ensure high productivity.
14. Capturing the large Chinese domestic market by setting up joint ventures and collaborations.
15. The mode going forward ideally should be Public Private Partnerships.
16. A reporting system to track economic and social benefits of each of these projects should be implemented.
17. HR mobility and corporate exchange programs could enhance social integration.
18. CPC can be used as a launching pad for Chinese firms in the financial sector to provide its services to South Asia and internalizing the Yuan.
19. The partnership between Sri Lanka and China within the BRI framework could be used in terms of providing bridging finance.
20. Establish a task force with experts and business leaders from both sides, to carry out investigations and identify areas needed towards industrialization of Sri Lanka to work out a map on the future trajectory.

REPORT OF THE CHINA REFORM FORUM

Opportunities and Challenges of the "Belt and Road" International Cooperation Between China and Sri Lanka in The Post Epidemic Era

In 2020, the Covid-19 epidemic ravaged the world, taking millions of lives and crippling economies in the world. This year, with the commencement of the vaccination programme, the end of the epidemic is promising. In the post-epidemic era, economic recovery is a top priority for all countries. China's cooperation with Sri Lanka under the initiative of the "Belt and Road" faces major opportunities, as well as some challenges:

Opportunities and Challenges:

- ◆ The cooperation between China and Sri Lanka under "the Belt and Road Initiative", has opened a window of opportunity for strategic relationship, complementary advantages and win-win results between China and Sri Lanka.

- ◆ The goal of the Belt and Road Initiative is to achieve infrastructure connectivity among countries in the region. Strengthening connectivity, constructing ports and transportation is the common demand of China and Sri Lanka, which is in the fundamental interests and development strategy of both sides. As early as 2010, the Ministry of National Finance and Planning of Sri Lanka issued a national development strategy, setting out an ambitious goal of building Sri Lanka into a maritime, commercial, energy and knowledge hub, linking the East and the West with the construction of the harbour of Hambantota and the Colombo Port City as key projects. In September 2014, during Chinese President Xi Jinping's state visit to Sri Lanka, Sri Lanka's President Rajapaksa said that President Xi's proposal to build the "21st Century Maritime Silk Road" coincided with his vision of building a maritime shipping center in the Indian Ocean. Sri Lanka is willing to work with China to jointly build and operate important projects such as the Hambantota Harbour and the Colombo Port City, strengthen cooperation in economic and trade, energy, infrastructure construction, agriculture, healthcare and other fields, and launch bilateral free trade negotiations".

- ◆ Sino-Sri Lanka cooperation is mutually beneficial and a win-win situation for both sides. Judging from the strategic needs and capabilities of both sides, China's rapidly growing economy can provide Sri Lanka with a certain development dividend; funds, science and technology needed for infrastructure construction; increase local employment opportunities; promote local economic development & livelihood improvement and accelerate infrastructure upgrading. On the other hand, as an important transit station in the Indian Ocean, Sri Lanka plays an important role in the construction of "the Belt and Road", especially in the construction of 21st Century Maritime Silk Road. Located in the east-west shipping lane in the Indian Ocean, Sri Lanka is an important strategic channel for China's maritime cargo and oil transportation. Sri Lanka can provide China with irreplaceable geographical advantages in the Indian Ocean. It also provides a rare opportunity for the development of Chinese enterprises overseas. The two countries have common strategic interests in geopolitics, which is of great significance. This common strategic demand is a

solid foundation for bilateral cooperation as well as a major opportunity for strategic cooperation.

Challenges: Sino-Sri Lanka cooperation also faces some challenges

- ◆ Political risks: Unexpected internal and external events and elements, which may affect the progress of bilateral cooperation. Maintaining policy continuity and a stable social environment are the guarantees for cooperation.
- ◆ Economic risk: Affected by the Covid-19 epidemic, Sri Lanka is facing economic recovery and financial liquidity challenges. The government also faces risks involving currency, interest rates and servicing of maturing public debt.
- ◆ Security risks & terrorist attacks.

The Key Areas of Cooperation Between China and Sri Lanka

China and Sri Lanka are strategic partners. Sri Lanka is one of the first countries to respond to and support Chinese President Xi's "the Belt and Road initiative". Faced with the international situation in the post-epidemic era, China and Sri Lanka should maintain close communication and cooperation to jointly meet the challenges.

- ◆ Maintain high-level exchanges and strengthen strategic communication.
- ◆ Hand in hand to fight the Covid-19 epidemic. Vaccines are a key weapon in the fight against the Covid-19 epidemic. China and Sri Lanka should continue to strengthen prevention and control of the epidemic and share the experience of diagnosis and treatment. China will provide Sri Lanka with additional 600,000 doses of vaccine. We hope that the approval procedures will be completed as soon as possible.
- ◆ Deepen cooperation in various fields. Colombo Port City and Hambantota Harbour are the iconic projects of "the Belt and Road Initiative" between China and Sri Lanka, which are of great significance to the development of Sri Lanka. It is hoped that the Hambantota Special Economic Zone Bill and the Free Port Policy would be introduced to parliament as soon as possible to attract more international investors. China and Sri Lanka should build Colombo Port City and Hambantota Harbour as two engines to promote economic development, seize the opportunities of current adjustment of global and regional industrial supply chain to increase the ability for independent development. Both sides should expand and strengthen shipping logistics and industrial cooperation, promote construction of the International Financial Center at the Colombo Port City and development of the Colombo port. The economic and trade fields are important areas of cooperation between the two countries under the framework of the Belt and Road. Both sides should make great efforts to promote smooth trade and financing, increase economic vitality, realize leapfrog development and accelerate realization of President Gotabaya's "vision of prosperity and glory ". The Sri

Lanka side expressed its desire to strengthen cooperation with China in key areas related to people's livelihood, such as agriculture, science and technology, education & investment, and to promote joint construction of the "Belt and Road" cooperation between the two countries, marked by the comprehensive development of the Colombo Port City and Hambantota Harbour, to achieve more tangible results.

- ◆ Speed up the negotiation process of bilateral free trade zones. The FTA will promote trade and investment cooperation between our two countries. For Sri Lanka, the FTA will provide an opportunity for Sri Lanka to expand its exports to China, help to gradually narrow the bilateral trade deficit, promote the development of small and medium-sized enterprises in Sri Lanka, attract more Chinese investment, and thus add new impetus to Sri Lanka's economic development. For China, the FTA can create convenient conditions for Chinese enterprises and Chinese goods to access Sri Lanka market. The two sides should restart a new round of free trade negotiations as soon as possible and strive to reach a bilateral free trade arrangement at an early date.
- ◆ Strengthen cooperation in the field of security. China will support Sri Lanka in combating terrorism, strengthening anti-terrorism capacity building, and maintaining national security and stability.
- ◆ Expand cultural exchanges, enhance mutual understanding, and lay a solid foundation for deepening bilateral cooperation. In history, China and Sri Lanka had deep religious and cultural exchanges, especially the Buddhist cultural exchanges between the two countries. In the Eastern Jin Dynasty, Chinese monk Fa Xian went to India to study Buddhism and stayed in Sri Lanka for two years. In the Ming Dynasty, Zheng He went to Sri Lanka many times, and brought Chinese gold, silver, silk and porcelain to Sri Lanka. The intersection of the country lies in the communication of the people in each country. China and Sri Lanka should make use of this advantage to strengthen cultural exchanges and enhance understanding. Chinese enterprises should create a good corporate culture, shoulder more social responsibility and create benefit to local people.

THE PATHFINDER FOUNDATION (PF) is a non-profit, non-partisan, research & advocacy think-tank based in Sri Lanka, dedicated to play an important role in public policy, strategic and security related issues. Lately, PF has engaged in ocean affairs focusing on the Indian Ocean in general and the Bay of Bengal in particular. The Foundation has also played a catalytic role in research and analysis aimed at contributing to economic policy reforms in Sri Lanka.

Over the years, PF has concentrated on developing partnerships with institutions in countries having interests in economic, strategic and security issues affecting stakeholders in the Indian Ocean Region. Apart from India and China, countries such as Bangladesh, Iran, Japan, Norway, Singapore, the Russian Federation and the USA have joined these partnerships.

Over the years, PF has established a wide network of partner organisations worldwide, to promote economic, social and political development, in addition to its security and strategic focus. Apart from India and China, countries such as Cambodia, Iran, Israel, Japan, Nepal, Norway, Singapore, the Russian Federation and the USA have joined partnerships.

Serving as a platform to engage in critical thinking and cross-disciplinary analysis, the Foundation aims to increase knowledge and raise awareness of salient issues with relevant stakeholders locally and internationally.

CHINA REFORM FORUM (CRF), as an academic research institution subordinating to Party School of the Central Committee of C.P.C (National Academy of Governance), is committed to organizing domestic and overseas well-known experts and scholars for studies and exchanges about hot topics and difficulties existing in the process of China's reform and opening-up, providing policy suggestions for relevant government departments from the perspective of national strategy.

Founded in 1994, the Forum has conducted a series studies for more than twenty years focusing on China's reform and opening-up and the path of peaceful development, and established dialogue mechanisms with research institutions of over 20 countries such as America, France, Britain, Germany, Russia, India, South Korea and Singapore. With exchanges in multiple forms such as joint studies, international seminars, organization cooperation and personnel visits, mutual understanding has been enhanced and contributions made to China's reform and opening-up cause.

The Forum has a Senior Advisory Committee and Councilors Committee, jointly composed of eminent experts, scholars, former officials and corporate elites from China's strategic circle, academic field, policy research departments and enterprises. In 2014, Mr.He Yiting, Executive Vice President of Party School of the CPC Central Committee, takes the position as Chairman of the Forum. Mr.Li Jingtian, the former Executive Vice President of Party School of the CPC Central Committee is the Director of the Forum's Senior Advisory Committee.