HARVARD | BUSINESS | SCHOOL

9-719-046
REV: JULY 12, 2019

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Chinese Infrastructure Investments in Sri Lanka: A Pearl or a Teardrop on the Belt and Road?

In 2018, as Saliya Wickramasuriya, former head of the Sri Lanka Ports Authority (SLPA), looked over the horizon toward the vast Indian Ocean from the observation deck inside Hambantota Port, he could see the train of container vessels in the busy East-West Indian Ocean shipping lane, 10 nautical miles from Hambantota (see **Exhibit 1** for Indian Ocean shipping map). Back in 2008, then the chairman of SLPA, Wickramasuriya helped secure a loan from China's Export-Import Bank (China Ex-Im Bank) to transform a poor, sleepy fishing village on the southern coast of Sri Lanka into what he called a "niche small port" for non-container cargo and ship bunkering services (or Phase I).[a] Before construction of Phase I was completed, Wickramasuriya left his government post to spend more time with his family.[1] By then, discussion was already underway in the Sri Lanka government for Phase II, comprising mainly of terminals to handle container cargo, which Wickramasuriya said had "no compelling business case" unless the country's main port, in Colombo, were nearing capacity.

During the same week in October 2018, in a major foreign policy speech at the Hudson Institute, a conservative think tank, United States Vice President Mike Pence alleged that China was using "debt trap diplomacy" to expand its global influence by providing infrastructure loans to countries that could not repay them. He also called Hambantota Port a potential "forward military base for China's growing blue water navy." [2]

The Chinese government firmly rejected these allegations, calling them "a gross distortion of facts", adding that China's intention was to make Sri Lanka the logistics hub of the Indian Ocean.[3] Ray Ren, CEO of Hambantota International Port Group (HIPG), said "We want to turn Hambantota into the next Shekou," a reference to a thriving port and free trade zone that his parent company, China Merchant Port Holdings, developed in the Chinese city of Shenzhen.[4]

The fate of Hambantota was closely watched around the world as an early litmus test of China's "Belt and Road Initiative" (BRI): a grand infrastructure initiative to improve connectivity between Asia, Europe and Africa that had the potential to fundamentally change global interactions in decades to

[a] Bunkering refers to ship refueling.

Professor Meg Rithmire and Research Associate Yihao Li prepared this case. Funding for the development of this case was provided by Harvard Business School. HBS cases are developed solely as the basis for class discussion. Cases are not intended to serve as endorsements, sources of primary data, or illustrations of effective or ineffective management.

come. What would Hambantota look like in 30 years? A decaying monument to poor political choices? A bustling center of expert-oriented industry? Or something else?

Sri Lanka

Shaped like a teardrop, Sri Lanka was an island state located in the northern Indian Ocean. Geographically, it was separated from India by the narrow Palk Strait. Sri Lanka had a warm, tropical climate. Sri Lanka in 2012 had a population of over 21 million, of which ethnic Sinhalese accounted for 75% and Sri Lankan Tamils accounted for 11%.[5] Population density – and economic activity – was highest in the Western Province, especially in and around the capital, Colombo.

Formerly known as Ceylon, the island's political history was a study of contradictions. On the one hand, since independence from British rule in 1948, Sri Lanka had enjoyed "a robust, adversarial, democratic, open polity, "said Sri Lanka's central bank governor Indrajit Coomaraswamy.[6] It boasted Asia's first democracy when universal adult suffrage was formally established in 1931,[7] and the world's first elected female head of government, when Sirimavo Bandaranaike became prime minister (PM) in 1960.[8] On the other hand, the country's recent history was marred by a violent 25-year civil war between the government, which was dominated by nationalist leaders from the Sinhalese majority, and the Tamil Tigers, a militant organization that wanted to establish a separate country for the Tamil minority.[9] The Sri Lankan civil war, one of the longest-running in Asia, left around 100,000 people dead and more than 300,000 people displaced, according to United Nations estimates.[10] Despite the war, "we did not have a single day of military rule," added Coomaraswamy.

The war ended in 2009. Mahinda Rajapaksa, who became President in 2005 and led the military offensive, was widely credited for defeating the militant group and regaining control of the entire country. Rajapaksa was re-elected in 2010, receiving 58% of the votes. "The government won the war; they did the impossible. So they had a thumping majority and could do anything," remarked Dushni Weerakoon, executive director of Institute of Policy Studies, a government think tank.[11] (See **Exhibit 2** for Sri Lanka political turnover.)

The end of civil war ushered in a period of economic boom. Sri Lanka's economy grew at an annual average of 6.4% during 2010-2015, and nominal GDP per capita increased by 40% to US$3,891, one of the highest in the South Asian region (see **Exhibit 3** for Sri Lanka's national accounts). Economic growth was led primarily by construction and other non-tradable sectors, as President Rajapaksa embarked on major reconstruction projects across the country to jumpstart economic development.[12] Strong growth had cut the country's poverty rate from 2.4% in 2009 to 0.7% in 2016.[b] Sri Lanka also ranked highly in Human Development Index, with a 93% literacy rate, a 74-year life expectancy, and widespread access to education and healthcare by both male and female.[13]

While construction alleviated some transportation bottlenecks, Sri Lanka still struggled to attract foreign direct investment (FDI), to diversify its export basket beyond rubber, tea and garments, and to integrate into global production chains.[14] A key reason, said the IMF, was Sri Lanka's high trade barriers, restrictive FDI policies and challenging investment climate.[15] "High inflation and high nominal interest rates are not conducive to East Asian-style export-led growth, so we have a current account deficit," explained central bank governor Indrajit Coomaraswamy.[16] In 2017, Sri Lanka regained preferential market access to the European Union under EU's Generalized Scheme of Preferences Plus, which allowed the country to export to the E.U. with zero tariffs.[17]

[b] Defined by the World Bank as living under 1.9 USD per day (adjusted to 2011 purchasing power parity).

At the same time, as social spending increased, the government struggled with a worsening budget deficit. Sri Lanka had one of the lowest tax revenue-to-GDP ratios in the world, after declining from 24.2% in 1978 to 11.4% in 2015. The major causes, said the World Bank, were a small tax base and poor government administration.[18] "We created free education and free healthcare by taxing rubber, tea, and coconut. Then that tax went away because terms of trade (in these sectors) declined. But now we are running out of sectors to tax," added Coomaraswamy. "We got away with living beyond our means for so long because of generous foreign aid, but we graduated from low-income status in 2009 and loans have become mostly commercial. So fiscal discipline is key."[19]

Lastly, inequality remained a challenge, as regional disparities remained wide and income disparity grew. The country's Gini coefficient increased from a modest 0.36 in 2009 to 0.45 in 2016.[20]

China and the Belt and Road Initiative

China's Development in 2018

In 2010, China overtook Japan as the world's second largest economy (see **Exhibit 4** for China's national accounts). 2018 marked the 40th anniversary of the beginning of Deng Xiaoping's Reform and Opening, a suite of policies that introduced markets into Chinese society after decades of centralized planning of production and consumption. Private enterprise was disallowed, and land and firms were owned by the state. In the decades since reform and opening, China had grown from poor, agrarian country with a GDP per capita of $300 in 1978 to an industrialized, high-technology economy with a GDP per capita of $8,827 in 2017.[21]

Deng's reforms famously had no blueprint, but rather were characterized by "crossing the river by grasping for stones"— policy-making through improvisation, experimentation, and learning.[22] The 1980s saw major growth in agriculture and rural industrialization; the 1990s brought financial development, urbanization, growth in FDI, and the privatization of many, but not all, state-owned enterprises (SOEs). In 2001, China formally entered the World Trade Organization, after which its trade balances with developed and developing countries alike grew increasingly imbalanced in China's favor. After the Global Financial Crisis in 2008 generated significant unemployment and imperiled China's export-driven growth model, a financial stimulus of around 4 trillion RMB ($586 billon USD) drove massive investment in construction and infrastructure, much of it undertaken by state-owned enterprises.[23]

Xi Jinping became China's fifth generation leader in 2012. Xi launched the country's most sweeping anti-corruption campaign since the 1950s; low-level officials and central power-holders alike found themselves and their networks under investigation, removed from the party, or jailed. Roderick MacFarquhar, a Harvard specialist on China, argued that Xi had become, "the most powerful leader of China since Mao Zedong died in 1976."[24] By 2018, "Xi Jinping Thought on Socialism with Chinese Characteristics for a New Era" was enshrined in the Constitution, and the term limits on the Chinese presidency (two five-year terms) were eliminated.[25] Under Xi Jinping, the Chinese Communist Party sought a more sustainable path of economic growth, hoping to rely on domestic demand and domestic innovation. The "Belt and Road Initiative" and "Made in China 2025" (a major domestic innovation push) were his signature economic policies. Xi's signature domestic policy was known as the Chinese Dream, and generally signaled the "great rejuvenation of the Chinese nation."[26]

China's Push for Connectivity

Asia in 2018 had a massive and growing infrastructure gap. The Asian Development Bank estimated that between 2016 and 2030 developing countries in Asia would need to spend $26 trillion to build the infrastructure required to "maintain its growth momentum, eradicate poverty, and respond to climate change."[27]

Since the end of World War II, Japanese and American governments had been among the primary donors for development projects in Asia, either through bilateral initiatives with host countries or through multilateral development banks such as the World Bank and Asian Development Bank.[28] But "the demand for infrastructure across Asia and the Pacific far outstrips current supply," said Takehiko Nakao, president of Asian Development Bank.[29] More than half the estimated spending should go to transport and a third to power, according to the ADB, pointing in particular to a lack of ports, railways and highways to link countries to regional and global markets.[30]

In 2013, Chinese President Xi Jinping formally introduced the Belt and Road Initiative (known earlier as One Belt One Road). Xi first announced the Silk Road Economic Belt during a visit to Kazakhstan in September 2013. A month later in October 2013, Xi proposed the Twenty-First Century Maritime Silk Road while speaking at the Indonesian parliament. BRI represented China's effort to revive the ancient Silk Road, a network of overland and maritime trade routes that historians believed played a central role in facilitating the exchange of goods and cultures between Eastern and Western civilizations from around 1st century BC through 18th century AD. [31]

China's focus on infrastructure began at home in the early 2000s, as China focused on developing its western regions. As China's coastal regions flourished in the 1990s, the economic development gap between these areas and the interior and western parts of the country increased. Infrastructure investments, primarily in transportation, were a focus of the resulting Great Western Development Strategy, which was launched under President Jiang Zemin in the early 2000s.[32] Throughout the 2000s, and especially after the global financial crisis in 2008, infrastructure investment was a primary driver of economic growth in China. Soon after, Beijing began to look at connectivity and infrastructure projects beyond its borders to connect China to its neighbors in Asia, through Central Asia to Europe, over land, and through Southeast and South Asia via the sea. Railway, road, and port development had been at the forefront of Beijing's connectivity drive in the region and beyond.[33]

The BRI packaged all these preexisting disparate initiatives into one grand plan, although conversations on the projects with participating nations remained mostly bilateral.[34] The BRI had two components. First, a continental road (or the economic belt) connecting China to Europe through Central and South Asia. Six overland economic belts have been identified as priority. Second, a maritime road aimed to create a sea corridor between China and Europe by way of the Indian Ocean (see **Exhibit 5** for BRI Map). Six priority sectors of infrastructure development included railway, road, port, aviation, pipelines and spatial information technology. In addition to infrastructure development, connectivity also included broader economic policy coordination to facilitate free trade and investment, regional financial integration, as well as environmental, cultural, educational and tourism development at the people-to-people level.[35]

Like Deng's reform, the BRI had no detailed blueprint.[36] The Chinese government stressed that BRI was an open invitation to the entire world and had not released a definitive list of which countries were covered or what projects were included.[37] According to Chinese ambassador to the US, Cui Tiankai, BRI was not intended as China's "solo show", but a "symphony" performed by all participating countries. While the original plan involved only a few dozen countries that straddle the trade routes between China and Europe, by September 2018, some 100 countries and 30 multilateral development banks or UN agencies had signed agreements or memoranda of understanding with China on BRI, and the initiative had expanded to include a "Pacific Silk Road" and an "Arctic Silk Road". "The BRI has been warmly welcomed to an extent that has far exceeded our expectations," said China's deputy foreign minister Le Yucheng.[38]

China was prepared to invest up to one trillion US dollars into BRI projects. By 2018, much of the funding had come from China Development Bank and China Ex-Im Bank – state-owned "policy banks" that channel vast financial resources to government policy priorities in economic development, foreign trade and diplomacy. In 2015, the Chinese government injected $82 billion to three state-owned banks to finance BRI projects. In 2017, China further injected more than $800 billion into various BRI funds in state-owned banks.[39] By November 2018, Chinese banks had issued more than $200 billion in loans to over 2,600 BRI projects, according to vice chairman of China Banking and Insurance Regulatory Commission Huang Hong.[40] China hoped to mobilize more capital from public and private financial institutions from host countries and from the international community.[41]

Critics saw BRI as China's ploy to subject smaller countries in the region to Chinese economic and strategic influence by extending loans to countries that could not repay them, or "debt trap diplomacy".[42] US Secretary of State Rex Tillerson claimed that China "offers the appearance of an attractive path to development. But in reality, this often involves trading short-term gains for long-term dependency."[43] Other critics speculated BRI's real intention was to expand China's overseas military footprint with the construction of strategically located infrastructure, citing the apparent unprofitability of some projects.[44]

China rejected both accusations. "Debt is a neutral term…you cannot develop your economy without the use of debt," said Chinese vice foreign minister Le Yucheng. "The debt burden in some countries is due to complex reasons such as economic fundamentals, historical legacies, changes in commodity prices, interest rates and foreign exchange rates…and not necessarily due to BRI…For countries that cannot repay the debt, we do not press hard on them…we normally take flexible measures." "We have no intention of using BRI as a pretext to set up overseas military bases," said Le. "We rely on host countries to provide security for these investments…I want to point out that China's military presence overseas is much smaller than other major countries. We do not intervene militarily in other countries, nor do we violate their sovereignty and territorial integrity." (See **Exhibit 6** for US overseas military bases.) Mr. Le also dismissed the view that BRI's intentions were similar to those of the post-WWII Marshall Plan, which he described as having "clear geopolitical and ideological objectives to repel the Soviet bloc". In contrast, "the BRI is an inclusive initiative for international economic cooperation and connectivity cooperation."[45]

Traditionally, bilateral and multilateral lenders often imposed strict governance, social and environmental standards, sometimes dubbed the "Washington Consensus", on recipient countries as conditions for the loans. China, on the other hand, extended loans with no such strings attached. BRI projects were often financed by Chinese state-owned banks and built by Chinese state-owned construction companies, which often sent thousands of Chinese engineers and workers overseas for months.[46] Critics said the lack of conditions gave local politicians opportunities for rent-seeking and the extensive use of Chinese labor failed to create jobs for local communities.[47] In 2017, the sovereign debt of 27 countries covered by BRI, including Sri Lanka, were rated as "junk" by major credit rating agencies, and another 17 countries were not rated at all.[48]

China and Sri Lanka

Warm relations between Sri Lanka and China dated to the Rubber-Rice Pact of 1952, when the two countries signed a mutually-beneficial trade agreement to exchange Chinese rice for Sri Lankan rubber amid a challenging external environment for both countries. 1963 saw the signing of a key maritime trade agreement, China's first trade agreement with a non-communist country. During a state visit to Sri Lanka in 2014, Chinese President Xi Jinping called Sri Lanka an "all-weather friend", a term reserved only for a handful of China's most trusted countries.[49] Over the decades, China-Sri Lanka relations were characterized by frequent high-level official visits, mutual support at the United Nations, burgeoning trade and investment ties, growing Chinese aid in health, education and culture, and closer military ties.

As Sri Lanka plunged into civil war in 1983, China offered steadfast support to successive Sri Lanka governments against the separatist Tamil Tigers. Responding to Sri Lanka's concerns of growing Indian support of the rebel groups, Chinese President Li Xiannian reiterated China's long-standing foreign policy principle of non-interference in domestic affairs: "[Sri Lanka] should resist all external inference…Countries big or small, rich or poor should not interfere in the internal affairs of other states."[50] By the 1990s, China emerged as the largest arms supplier to Sri Lanka. Military ties grew even closer with the election of Mahinda Rajapaksa in 2005, who vowed to defeat the Tamil Tigers. Meanwhile, at the United Nations, China helped Sri Lanka fend off efforts by some western countries to accuse the Sri Lankan military of human rights abuses during the war.

China became Sri Lanka's biggest provider of development assistance in 2012, surpassing traditional donors such as Japan, the Asian Development Bank, and The World Bank. The aid relationship started as early as 1964, when Chinese Premier Zhou Enlai pledged a gift of an international conference center in Colombo. In 2017, about 40% of Sri Lanka's public investment was financed through foreign concessional loans and grants.[c] [51] Foreign-funded projects were concentrated primarily in public infrastructure projects in transportation, water and power sectors.

In 2016, China became Sri Lanka's largest trading partner, amounting to $4.4 billion (see **Exhibit 7** for Sri Lanka trade partners), and the two countries started negotiating a Free Trade Agreement in 2014.[52] In addition to economic development loans, China had made significant FDI into Sri Lanka. By 2013, China had become the biggest source of FDI, investing in major infrastructure projects such as Colombo International Container Terminal, Colombo Port City and Hambantota Port. In 2017, China contributed 35% of Sri Lanka's overall FDI inflow of $1.36 billion,[53] a figure the Central Bank believed would increase further as Colombo Port City and Hambantota Port start to attract significant FDI.[54] Still, Sri Lanka's FDI inflow as a percentage of GDP remained low compared to Asian peers at similar income levels.[55]

Hambantota Port

Despite being an island state, Sri Lanka's maritime trade for more than a century had been dominated by the Port of Colombo. Primarily a container port, it handled 6.2 million TEU in 2017.[d] Depending on the year, it ranked between 23rd and 27th in lists of the world's busiest ports by container

[c] Concessional loans are loans that are extended on terms substantially more generous than market loans. The concessionality is achieved either through interest rates below those available on the market or by grace periods, or a combination of these. Concessional loans typically have long grace periods, i.e. the period during which interests do not need to be paid.

[d] TEU refers to Twenty-Foot Equivalent Unit, the standard measure of the capacity of container ships and container terminals.

traffic (see **Exhibit 8** for global container port ranking), the highest ranked port in South Asia.[56] The Port of Colombo rose to regional prominence in the mid-1990s as a transshipment hub for India and the Indian Ocean. "They say the best port in India is Colombo", joked Daniel Stock, a Sri Lanka specialist at Harvard's Center for International Development.[57] Due to inadequate port infrastructure in the region and India's restrictive cabotage laws that barred foreign flagged ships from operating at Indian ports, containers from mega container ships often had to be offloaded in Colombo before being put on smaller ships to India, Bangladesh, and countries in East Africa.[58] Conversely in this hub-and-spoke structure, small feeder ships delivered cargo to Port of Colombo for them to be picked up by large mother ships traveling across oceans. By 2017, Colombo handled a quarter of India's 12 million TEU container trade volume, accounting for about one-third of the Indian Ocean transshipment market.[59]

Rapid growth in container traffic at Port of Colombo in the mid-2000s outpaced growth in handling capacity. Congestion was endemic from the mid-1990s through the late 2000s. But specialists disagree whether the source of the congestion was physical capacity or low operational efficiency.[60] "It is almost as if we have reached an invisible, artificial bottleneck. We are, at current real estate levels, a 4.5 million TEU port. Yet we are feeling the strain at a 3.5 million TEU level," remarked Wickramasuriya in 2007, then head of the Ports Authority.[61] One of the main reasons for congestion in the 2000s was the security-related closure of the North entrance of the port, which effectively made the Port of Colombo a one-way port, as the South entrance was unable to accommodate two ships passing at the same time. [62] In 2006, the ADB estimated that Port of Colombo would reach full capacity by 2010.[63] (See **Exhibit 9** for Port of Colombo capacity and traffic.) Consequently, in 2006, SLPA embarked on a multi-phase Colombo Port Expansion Project that would triple Colombo's container handling capacity to 10.5 million TEU by 2024 by building three new terminals on reclaimed land inside the existing Colombo harbor.

In 2002, developing a second major port in the fishing village of Hambantota in the Southern Province, long a talking point of politicians, formally entered the government's strategic plan.[64] While Port of Colombo was an artificial harbor that had to be periodically dredged to greater depth to accommodate ultra-large container ships, Hambantota was a natural deep-water harbor at the southern tip of Sri Lanka. Moreover, while Port of Colombo was landlocked by the city around it, Hambantota had vast empty land for potential port-related industrial development.[65]

Building a second port to reduce reliance on Colombo Port was a major economic and national security imperative, especially during the civil war. "With 90% of imports and exports of Sri Lanka going through Colombo, anyone who wants to choke Sri Lanka needs only control this port," said Mangala Yapa, former head of Colombo Dockyard and advisor to Minister of Development Strategies and International Trade.[66]

The government also hoped that developing a port in Hambantota would spur economic development in the troubled Southern Province, the poorest in Sri Lanka. Previous attempts by the government to relocate garment factories to the region were hampered by poor transportation infrastructure and radical local politics involving educated unemployed youth in the 1970s and 1980s.[67] The economic imperative to develop Hambantota became even more urgent after December 26, 2004, when a powerful tsunami in the Indian Ocean killed more than 8,000 residents in Hambantota alone and destroyed much of the town. Across Sri Lanka's south and east coasts, more than 30,000 people were killed and 900,000 people were left homeless.[68]

Hambantota was the home to Mahinda Rajapaksa, a long-time member of the Sri Lankan Parliament representing the Hambantota District. After Rajapaksa became Minister of Fishing and Aquatic

Resources Development in 2000, he promised Hambantota residents that one day he would bring big ships to Hambantota.[69] After being elected Sri Lanka's president in 2005, Rajapaksa wasted little time in launching several major infrastructure projects to revitalize the economy of his home district. Hambantota Port, a project first mooted by his father, also a prominent politician, was one of them.

Sri Lanka Ports Authority's initial plan for Hambantota was building a "niche port" to provide bunkering services to passing ships. According to Wickramasuriya, "Hambantota had the potential, in the right hands, to be a source of bunkers in very close proximity to the shipping lane without the detour that Colombo would require for vessels not making cargo calls there." But under President Rajapaksa, the plan was scaled up to become a major container transshipment hub.[70] In the short term, the port was expected to handle non-containerized cargo after completion of Phase I, which consisted of a dry bulk terminal,[e] a liquid bulk terminal, a break bulk terminal, a roll-on/roll-off terminal[f] and ship bunkering and servicing facilities. In the medium term, the port was expected to handle containerized cargo after completion of Phase II, which consisted of several container transshipment terminals, theoretically for container handling for an Export Processing Zone. In the longer term, a Phase III would be for container transshipment, but had yet to be planned or built as of 2018 (see **Exhibit 10** for Hambantota Port plan).

Hambantota Port Phase I

The Sri Lanka government commissioned two feasibility studies for Phase I of the port. In 2003, the first feasibility study was completed by Canadian engineering company SNC-Lavalin, which concluded that the proposed port was not "bankable". But the Sri Lanka rejected the study as "incomplete" as it overlooked certain geological data and potential impact on the country's main commercial port in Colombo.[71] In 2007, a second feasibility study was completed, this time by Danish consulting firm Ramboll. The study reached a more optimistic conclusion. It estimated that dry and bulk cargo would dominate traffic for the port until 2030, and by 2040, Hambantota Port would handle approximately 20 million TEUs.[72]

Based on the feasibility studies, Sri Lanka Ports Authority estimated that Phase I would cost $350 million dollars. "Phase I was entirely commercially manageable, $350 million was a very competitive cost," said Wickramasuriya. "We benchmarked very reasonably against similar port construction projects worldwide." President Rajapaksa's government first asked the Indian and American governments for loans to develop the port, but they declined. Indian companies did not think the project would be commercially viable.[73] "There has hardly been any American or European investment in Sri Lanka since the 1990s," remarked Asanga Gunawansa, a cross-border investment lawyer in Sri Lanka. "My experience was that negotiating large projects with Americans, Europeans and Indians resulted mostly in promises and very little progress, whereas with the Chinese a yes meant yes and no time was wasted," said Wickramasuriya.

In March 2007, President Rajapaksa went to Beijing to seek funds from the Chinese government. The Sri Lankan team first tried to seek a concessional loan from China, but the quota for China's concessional loans to Sri Lanka then had been used for other projects, according to a Sri Lankan official involved in the negotiation.[74] "Given the importance of constructing Hambantota Port Phase I, the Sri Lanka delegation decided to ask for commercial loans. In fact, to get commercial loans as large as 300

[e] Bulk cargo are commodities and goods that are loaded in individually rather than in standard containers.

[f] Roll-on/roll-off (ro-ro) means wheeled cargo that are driven on and off ro-ro ships on their own wheels (such as cars) or using a platform vehicle. This is in contrast to lift-on/lift-off (lo-lo) goods that use a crane to load and unload cargo at a container terminal.

million US dollars during the war was not easy," explained the Sri Lankan official.[75] In November 2007, China Ex-Im Bank agreed to fund 85% of Hambantota Port's Phase I construction costs with a 15-year commercial loan of $307 million with a four-year moratorium. China Ex-Im Bank proposed two interest rate options: a 6.3% fixed rate, based on the benchmark London Interbank Offered Rate (LIBOR) at the time plus 0.75% premium, or a floating rate pegged to LIBOR.[76] Sri Lanka chose the fixed rate of 6.3% because LIBOR was trending higher during negotiations (see **Exhibit 11** for benchmark interest rates).[77]

China recommended China Harbor Engineering Corporation as the construction contractor, which Sri Lanka negotiators gladly accepted. "China Harbor was an acceptable contractor. It had been in Sri Lanka for many years, and done work in fisheries harbors, airports, and roads," said Wickramasuriya. Construction started in January 2008 and by 2009, President Rajapaksa grew impatient. His 65th birthday was approaching in 2010 and he wanted a grand opening of the port to mark the occasion.[78] On November 18, 2010, President Rajapaksa opened the port in an elaborate ceremony and named it after himself. The port was then handed over to Magampura Port Management Company, a government-owned subsidiary of SLPA charged with developing and managing Hambantota Port.

Hambantota Port Phase II

While Phase I construction was ongoing in 2009, President Rajapaksa asked officials to implement phase II of the port ten years ahead of the Ports Authority's original timeline.[79] President Rajapaksa, who had just defeated the separatist Tamil Tigers and ended the civil war in 2009, was reelected for a second five-year term in 2010 "with a strong mandate for reconstruction but huge fiscal deficit due to the war," remarked Dushni Weerakoon of Institute of Policy Studies. She continued: "They went in big for infrastructure, and China was an obvious source of funding. Some of the project selection was decided more on politics rather than economics."[80]

At an estimated cost of $808 million, the expansion focused on building new container terminals that would have a capacity of 2.2 million TEU. In December 2010, SPLA signed a construction contract with an expected completion date in 2015.[81] The original SLPA plan drafted under Wickramasuriya's tenure called for revenue to be coming in before any major expansion.[82]

Hambantota had a slow start in the first years of operation. Due to Magampura Port Management Company's slow procurement of essential equipment to handle cargo, traffic was low but growing significantly, particularly in roll-on/roll-off ships carrying vehicles.[83] (See **Exhibit 12** for Hambantota Port traffic.) In 2012 the Sri Lanka government ordered vehicle carriers bound for Colombo to offload vehicles at Hambantota to jumpstart business there. Sri Lanka Ports Authority had to use profits from Port of Colombo to cover operations cost at Hambantota.[84] In 2012, President Rajapaksa went to Beijing again, asking for $757 million to finance phase II. China Ex-Im Bank agreed to extend the loan at a rate of 2%.[85]

Although Hambantota Port first opened in a limited way in 2010, before Belt and Road Initiative was announced, the Chinese government quickly folded the project into the global program in 2013. In 2014, China Harbor and China Merchants Port proposed to jointly operate the new container terminal.[86] Under the proposed Supply-Operate-Transfer (SOT) arrangement, the two Chinese companies would take 65% equity position in phase II, supply the necessary equipment, operate the container terminal for 35 years, during which 35% of the revenue would repay the overall loan from China Ex-Im Bank, before transferring the terminal back to Sri Lanka Ports Authority after 35 years.[87] In September 2014, an agreement was signed between China Harbor, China Merchants and Sri Lanka Ports Authority in front of President Rajapaksa and visiting Chinese President Xi Jinping.

China Merchants Port Holdings, listed on the Hong Kong Stock Exchange, was a subsidiary of Hong Kong-based conglomerate China Merchants Group, whose core businesses spanned transportation, finance and real estate. Established in 1872, China Merchants Group was fully owned by the Chinese government. China Merchants Port Holdings, which was 62% state-owned as of 2018, was one of the world's largest port developers, investors and operators, with a network of 36 ports in 18 countries, including a 2.4 million TEU container terminal in Port of Colombo.[88] China Merchants Port was known for developing a successful port+zone+city model in Shekou industrial zone in the Chinese coastal city of Shenzhen (see **Exhibit 13** for China Merchants Port Holdings' share prices).

Refinancing the Port

By late 2014, President Rajapaksa had abolished presidential term limits and called for an early election in a bid to win an unprecedented third term. Maithripala Sirisena, who was Rajapaksa's Minister of Health, unexpectedly defected from the party in November 2014 and ran against Rajapaksa. Sirisena ran on a platform to check Rajapaksa's authoritarianism and alleged corruption, warning during his campaign that Sri Lanka would "become a colony, and we would become slaves" if Rajapaksa's policies continued.[89] "The land that white man took over by means of military strength is now being obtained by foreigners by paying ransom to a handful of persons," he wrote in his manifesto.[90] President Rajapaksa was unexpectedly voted out of office in January 2015. The *New York Times* alleged that China Harbor wired as much as $7.6 million USD to support Rajapaksa's reelection efforts.[91] *Reuters* alleged that India's external intelligence agency, the Research and Analysis Wing (RAW), meddled in Sri Lanka's 2015 elections by convincing Sirisena to defect.[92]

Hambantota Port was not the only project that was left idle after it was built under President Rajapaksa. In 2009, China Harbor started building a 35,000-seat Mahinda Rajapaksa International Cricket Stadium in Hambantota, financed with loans of an undisclosed amount. By 2018, the stadium had hosted four games. Also in 2009, China Ex-Im Bank provided the majority loan for the $209-million-dollar Mattala Rajapaksa International Airport, Sri Lanka's second international airport, 18 kilometers from Hambantota.[93] By 2018, all commercial flights had ceased operations due to low traffic volume. In 2011, the South Korean government provided grants to construct $15.3-million-dollar state-of-the-art Magam Ruhunupura International Conference Hall in Hambantota, which had hosted one event in the three years after its opening in 2013.

The newly elected government immediately halted many high-profile infrastructure projects undertaken during Rajapaksa's tenure. It requested that China Ex-Im Bank restructure the Hambantota port loan terms including lowering the interest rate, extending the grace period, and increasing the maturity period. China Ex-Im Bank never responded to the request, and the Sri Lankan Attorney General ruled that SOT agreement had no legal basis, effectively cancelling the agreement signed during President Xi's visit.[94] "China felt stabbed in the back," said Jayanath Colombage, former commander of the Sri Lankan navy.[95]

By mid-2016, the previous government's heavy borrowing had taken its toll. Capital outflows from emerging markets had intensified, triggering a balance of payment crisis in Sri Lanka (see **Exhibit 14** Sri Lanka balance of payment).[96] When it became apparent that Sri Lanka would face difficulty repaying international bond investors, Sri Lanka decided to raise much-needed US dollars by leasing out Hambantota Port, and PM Ranil Wickremesinghe directly appealed to Chinese President Xi to either refinance the loan or to take majority equity in the port. According to Wickremesinghe's Minister of Ports and Shipping, President Xi rejected the idea of refinancing, but committed to helping Sri Lanka find an investor.[97] "The new government went to China in a position of weakness," observed Admiral Colombage.[98]

Nivard Cabraal, who served as Central Bank Governor from 2006-2015 under President Rajapaksa, said in 2018 that Hambantota's repayment terms were manageable and blamed the current government for leasing the port to China. “Rajapaksa never wanted to sell or lease the port to any country,” Governor Cabraal added.[99] Subhashini Abeysinghe, research director at Verite Research, an independent think tank, said: “About 33% of external debt was international sovereign bonds (ISB), which comes at a higher interest rate and shorter maturity periods compared to loans from China, whose share of external debt is 9%, according to data published by the Central Bank of Sri Lanka. Further, unlike in the case of ISBs, which comes with no grace period, the loans by bilateral donors like China has a grace period, and some of the loans as per data published by external resources department, are not up for payment yet.” (See **Exhibit 15** for Sri Lanka’s debt structure.) She diagnosed Sri Lanka with “issues related to project selection, weak macroeconomic management, and poor accountability.”[100]

In 2016, the Sri Lanka Ports Authority invited China Harbor and China Merchants to submit new proposals to develop Hambantota Port. China Harbor proposed to invest $ 740 million to acquire 65% of port equity excluding the container terminal, thus valuing the asset at a sum of $ 1.136 billion. Payment would be made in two tranches: one in 2017 and the other in 2019. Regarding phase II, it proposed to continue with the SOT Agreement with an equity contribution of $ 391 million for supplying container-handling equipment, jointly with China Merchants.[101]

China Merchants proposed to replicate Shekou’s “Port+Zone+City” model in Hambantota. It proposed to invest up to $ 1.12 billion for an 80% equity stake of the Port and to develop the adjacent five-square kilometer (1,235 acres) of land into an economic zone on the basis of an estimated asset value of $ 1.4 billion. It proposed to make the investment in three tranches: 10% within one month, 30% within three months and 60% within six months upon signing the concession agreement – all tranches within 2017. Further, it also agreed to invest in the equipment needed for phase II container terminal.[102]

India strongly opposed leasing Hambantota Port to a Chinese company and raised national security concerns in the negotiation. In 2015, a Chinese submarine docked at a Port of Colombo terminal operated by China Merchants, and India was worried that China would use Hambantota Port as a military output in the Indian Ocean.[103] “It was a routine port call approved by the Sri Lankan government, and it’s not a big deal at all,” remarked Admiral Colombage, adding that India sent the most naval ships to Colombo (85) between 2009 to 2018, followed by Japan with 79 visits (see **Exhibit 16** for naval visits).

But India was not willing to take over the port itself, and negotiations came to a standstill. “The bottom line was we needed the money. And we had to make Hambantota commercially viable. Either we can be dogmatic and talk, or we can be pragmatic and do it,” said Mangala Yapa.” In the end, all parties agreed that the Hambantota Port agreement should include clauses that would prevent Chinese navy from using the port; any military use would require advance approval by the Sri Lanka President. Admiral Colombage said, “If China brings a ship by force, that is an act of war.”[104]

In 2017, Sri Lanka Ports Authority and China Merchants reached a concessional agreement in the form of a Public-Private Partnership. Sri Lanka Ports Authority and China Merchants would form two joint ventures, Hambantota International Port Group (HIPG), which would develop, operate, and manage Hambantota Port for 99 years, and Hambantota International Port Services (HIPS), which would develop, operate and manage common user facilities for Hambantota Port for 99 years. China Merchants accepted an 85% equity position proposed by the Ports Authority, and the final agreement explicitly prohibited any military use of the port without Sri Lanka government approval. To reassure concerned countries, the Sri Lankan Navy's Southern Command would be moved to Hambantota Port to provide security. The SLPA remained the owner of the port, which was leased to the HIPG.

The final agreement stipulated: Within 10 years from the effective date of the concession agreement, Sri Lanka Ports Authority had the right to buy back 20% shares of HIPG on mutually agreed upon terms. After 70 years, SLPA could acquire China Merchants' entire shareholdings in HIPG at a fair value to be determined by an independent company appointed by both parties. After 99 years, China Merchants would transfer all its shareholdings in HIPG and HIPS to the Sri Lankan Government at a token price of $1.[105]

China Merchants appeared confident that it could turn Hambantota Port around. "There is no more land in the Port of Colombo for port-related industrial development. But with Hambantota, we envisage it as an industrial and logistics gateway to the Indian sub-continent by providing marine services and setting up port-related industries inside the port," said Ray Ren, CEO of Hambantota International Port Group.[106] "Hambantota is the only place in the region after Singapore that has port + airport connection," said Dushni Weerakoon of Institute of Policy Studies. "China feels building infrastructure is the first step toward bringing FDI in manufacturing longer term." [107]

Colombo Port City

Since 2014, China Harbor had invested $1.4 billion dollars in equity to reclaim 2.69 square kilometers (1 square mile) of land near Port of Colombo to jumpstart a new city district known as the Port City (see **Exhibit 17** for Port City plan). It was the biggest single foreign investment in Sri Lankan history and government officials hoped it could attract $14 billion more in FDI. According to the masterplan, Port City would become a regional business and financial center, with high-end residential towers, commercial skyscrapers and resorts. The plan included world-class amenities such as a marina, an international school, a well-equipped hospital and convention center, as well as state-of-the-art public transportation. Port City would be developed in phases and was set to be completed in 2041.[108]

The concept of developing real estate on reclaimed land originally came in 2004 from John Keells Holdings, a major Sri Lankan conglomerate, but plans were delayed by the war.[109] A 2003 World Bank report projected that rapid urbanization would see half of Sri Lanka's population living in urban areas by 2010.[110] A 2015 KPMG report estimated that population density in Colombo would grow from 3,417 people per square kilometer in 2015 to 5,722 per square kilometer by 2030, and 100,000 housing units per year would be required.[111] From 2012 to 2018, land prices in Colombo's urban core rose by 16.5% per year on average (See **Exhibit 18** for Colombo urban land prices). In 2009, China Harbor submitted an unsolicited proposal to the government and was awarded the project. [112] Construction started in 2014 during President Xi's visit, but in the 2015 election, issues of sovereignty and environmental impact became political issues. Originally, China Harbor was to receive 0.5 square kilometers of land on a freehold basis, but after strong objections from India over China indefinitely owning territories so close to their borders this was reduced to 0.2 square kilometers.[113]

Immediately after the new government came to power in January 2015, it suspended the Port City project, only six months into construction. One month later, the government backtracked on the suspension and gave the go ahead to the project just before the new foreign minister visited China in order to "avoid any misunderstanding" with Beijing.[114] A month later, just before Narendra Modi became the first Indian PM to visit Sri Lanka in 28 years, Colombo Port City was again postponed.[115] The new government sought Indian investment, but learned that the Indians were not interested. By this time, China Harbor had already filed a lawsuit against the government, seeking $143 million in compensation for the disruption.[116]

By August 2016, all freehold rights were cancelled, and the project was again given the green light after a government study concluded the project was environmentally sound after all.[117] After negotiations behind closed doors, China Harbor would drop the lawsuit and in return, would be allotted additional land, on 99-year lease basis, bringing its total lease holding to at least 1.1 square kilometers.[118]

By fall 2018, master planning was complete and the land reclamation was nearly complete.[119] The government planned to rename the development Colombo International Financial City, in a bid to rival regional financial hubs of Dubai and Singapore.[120] To make the financial city attractive to foreign investors, the government had started drafting a separate legal framework to govern the jurisdiction, with its own laws, courts and arbitration centers.[121] New laws were expected to cover taxation, land ownership, and the international movement of capital and people.[122] China Harbor, for its part, had already started looking for real estate developers and tenants.[123]

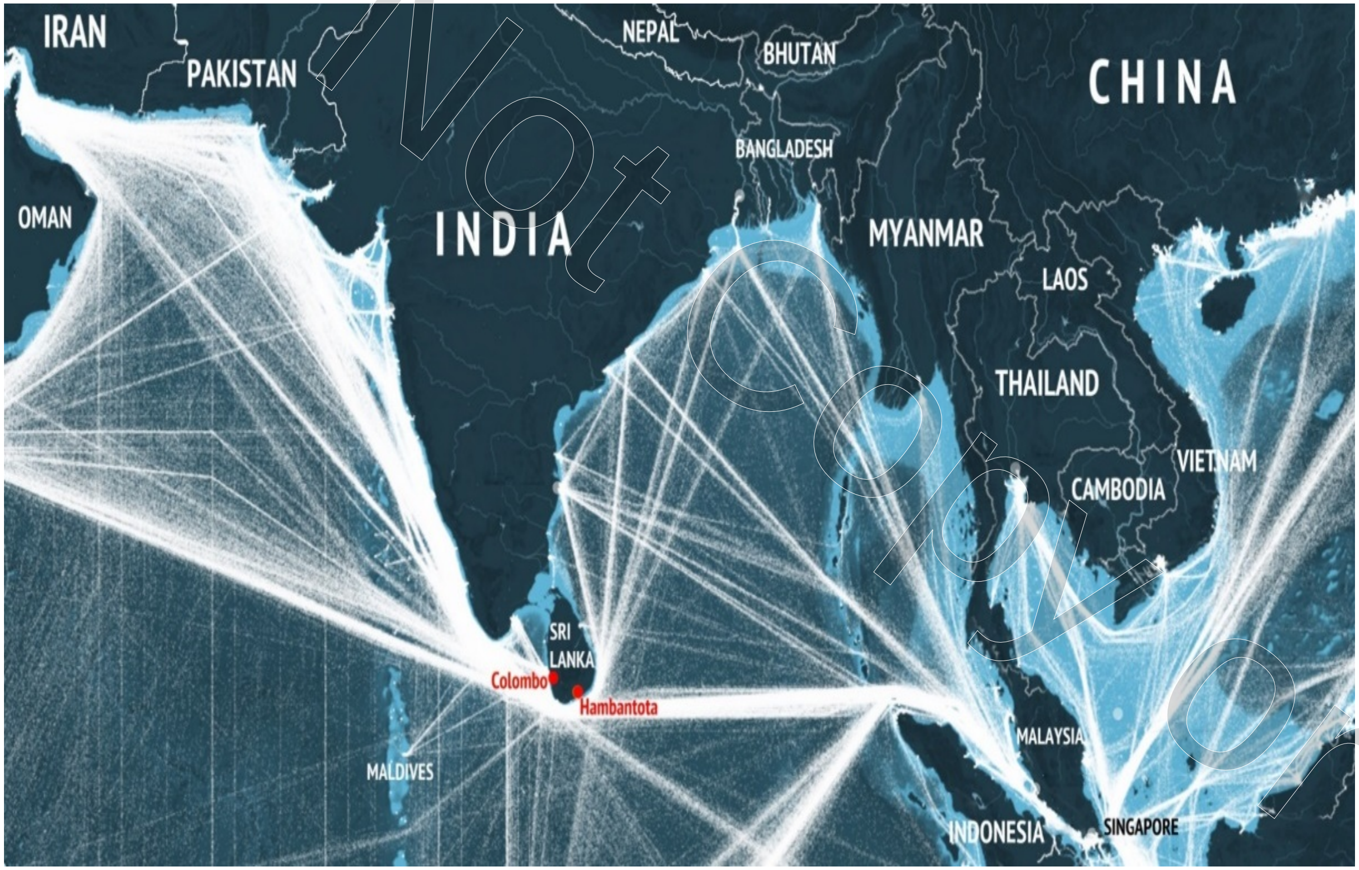
Conclusion

2018 turned out to be a year of uncertainty for Sri Lanka. In late October, President Sirasena surprised his supporters and detractors by suddenly announcing he had "fired" PM Wickremesinghe and swearing in Mahinda Rajapaksa, his former rival, into office as PM. Wickremesinghe refused to depart Temple Trees, the official residence of the PM, arguing that the President did not have constitutional authority to fire the Prime Minister. Sirasena declared that Parliament would take a holiday in advance of a vote of confidence for the new PM, Rajapaksa; many claimed the forced holiday was an effort to give Rajapaksa the time to convert, or buy, the votes he needed. A court stayed the holiday, and Rajapaksa lost the vote in November. The President and Rajapaska, however, refused to accept the vote. The country seemed bound for a political crisis.[124]

While Chinese politics were decidedly more stable, the Belt and Road Initiative itself encountered some uncertainty in 2018. In May 2018, Malaysia became a source of similar pushback against Chinese investments after its dominant party was surprisingly upset in close elections. The new Malaysian government suspended Chinese infrastructure investments and threatened real estate projects; as in Sri Lanka, there were accusations of Chinese funding for ousted politicians.[125] As Xi and others marked the project's fifth anniversary in August, the talk was of a "recalibration" of the BRI, ensuring that its implementation accorded with China's strategic objectives.[126] President Xi was firm in his emphasis on the benefits of the initiative: "The Belt and Road Initiative serves as a solution for China to participate in global opening-up and cooperation, improve global economic governance, promote common development and prosperity, and build a community with a shared future for humanity."[127]

The world watched Sri Lanka's unfolding political crisis with apprehension. Could one of Asia's most durable democracies survive its latest challenge? The world also watched the fate of Chinese investments in the country and, generally, the political conflicts in which China found its BRI enmeshed. Would Xi's vision for a "shared future" prove elusive or were the recent hiccups just obstacles on a very long road?

Exhibit 1 Indian Ocean Shipping Density Map



Source: Adapted by casewriters from www.shipmap.org, accessed November 2018. Map created by Kiln, www.kiln.digital, based on data from the UCL Energy Institute (UCL EI).

Exhibit 2 Sri Lanka Political Turnover

Sri Lankan Presidential Election Results, 1982-2015			
Year	**President Elected**	**Prime Minister**	**Party Affiliation**
1982	J. R. Jayewardene	Ranasinghe Premadasa	United National Party
1988	Ranasinghe Premadasa	Dingiri Banda Wijetunga	United National Party
1994	Chandrika Kumaratunga	Sirimavo Bandaranaike	Sri Lanka Freedom Party
1999	Chandrika Kumaratunga	Ratnasiri Wickremanayake	Sri Lanka Freedom Party
2005	Mahinda Rajapaksa	Ratnasiri Wickremanayake	Sri Lanka Freedom Party
2010	Mahinda Rajapaksa	D. M. Jayaratne	Sri Lanka Freedom Party
2015	Maithripala Sirisena	Ranil Wickremesinghe	New Democratic Front / United National Party

2005 Presidential Election		
Turnout	73.73%	
Candidates	Mahinda Rajapaksa	Ranil Wickremesinghe
Parties	Sri Lanka Freedom Party	United National Party
% of votes	50.29%	48.43%

2010 Presidential Election		
Turnout	74.50%	
Candidate	Mahinda Rajapaksa	Sarath Fonseka
Party	Sri Lanka Freedom Party	New Democratic Front
% of votes	57.88%	40.15%

2015 Presidential Election		
Turnout	81.52%	
Candidate	Mahinda Rajapaksa	Maithripala Sirisena
Party	Sri Lanka Freedom Party	New Democratic Front
% of votes	47.58%	51.28%

Source: Adapted by casewriters from Government of Sri Lanka data, see https://election.news.lk, accessed November 2018.

Exhibit 3 Sri Lanka's National Accounts

	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017
Income										
GDP (billions of current US$)	40.7	42.1	56.7	65.3	68.4	74.3	79.4	80.6	81.8	87.2
GDP growth (annual %)	6.0	3.5	8.0	8.4	9.1	3.4	5.0	5.0	4.5	3.1
GDP per capita (current US$)	2041.3	2095.5	2808.5	3213.9	3350.6	3609.1	3820.7	3842.2	3857.4	4065.2
GDP per capita growth (annual %)	5.2	2.9	7.4	7.8	8.6	2.6	4.0	4.0	3.3	2.0
Composition of GDP										
Private consumption (% of GDP)	70.0	64.4	68.5	71.3	65.2	67.6	67.4	67.4	63.8	62.2
Government consumption (% of GDP)	16.2	17.6	8.5	8.6	7.6	7.8	8.4	9.0	8.5	8.5
Gross fixed investment (% of GDP)	27.6	24.4	30.4	33.4	39.1	33.2	32.3	31.2	35.0	36.5
Exports of goods and services (% of GDP)	24.8	21.3	19.6	20.9	19.8	20.3	21.1	21.0	21.3	21.9
Imports of goods and services (% of GDP)	38.5	27.8	26.8	34.1	31.7	28.9	29.2	28.5	28.7	29.1
Welfare										
% living below $1.9/day poverty line (2011 PPP)	..	2.4	..	..	1.9	..	..	..	0.7	..
Gini coefficient	..	0.36	..	..	0.39	..	..	..	0.45	..
Consumer prices (annual % change; average)	22.4	3.5	6.2	6.7	7.6	6.9	2.8	2.2	4.0	6.6
Gross domestic savings (% of GDP)	13.9	17.9	23.1	20.2	27.2	24.6	24.2	23.6	27.6	29.3
Finance										
FDI, net inflows (current US$)	0.8	0.4	0.5	1.0	0.9	0.9	0.9	0.7	0.9	1.4
Tax revenue (% of GDP)	13.3	12.8	11.3	11.3	10.4	10.5	10.1	12.4	12.3	..
Government budget balance (% of GDP)	-6.1	-8.6	-7.0	-6.2	-5.6	-5.4	-5.7	-7.6	-5.4	-5.5
Public debt (% of GDP)	..	86.1	71.6	71.1	68.7	70.8	71.3	77.7	78.8	77.4
Lending interest rate (%)	18.9	15.7	10.2	9.4	13.3	12.5	7.8	7.0	10.5	..
Deposit interest rate (%)	10.9	10.6	6.9	6.4	8.7	10.2	7.5	6.0	7.1	..
External debt stocks (% of GNI)	41.1	46.9	38.6	39.9	53.2	54.2	54.5	55.9	58.6	59.1
Exchange rate with US$ (average)	108.3	114.9	113.1	110.6	127.6	129.1	130.6	135.9	145.6	152.4

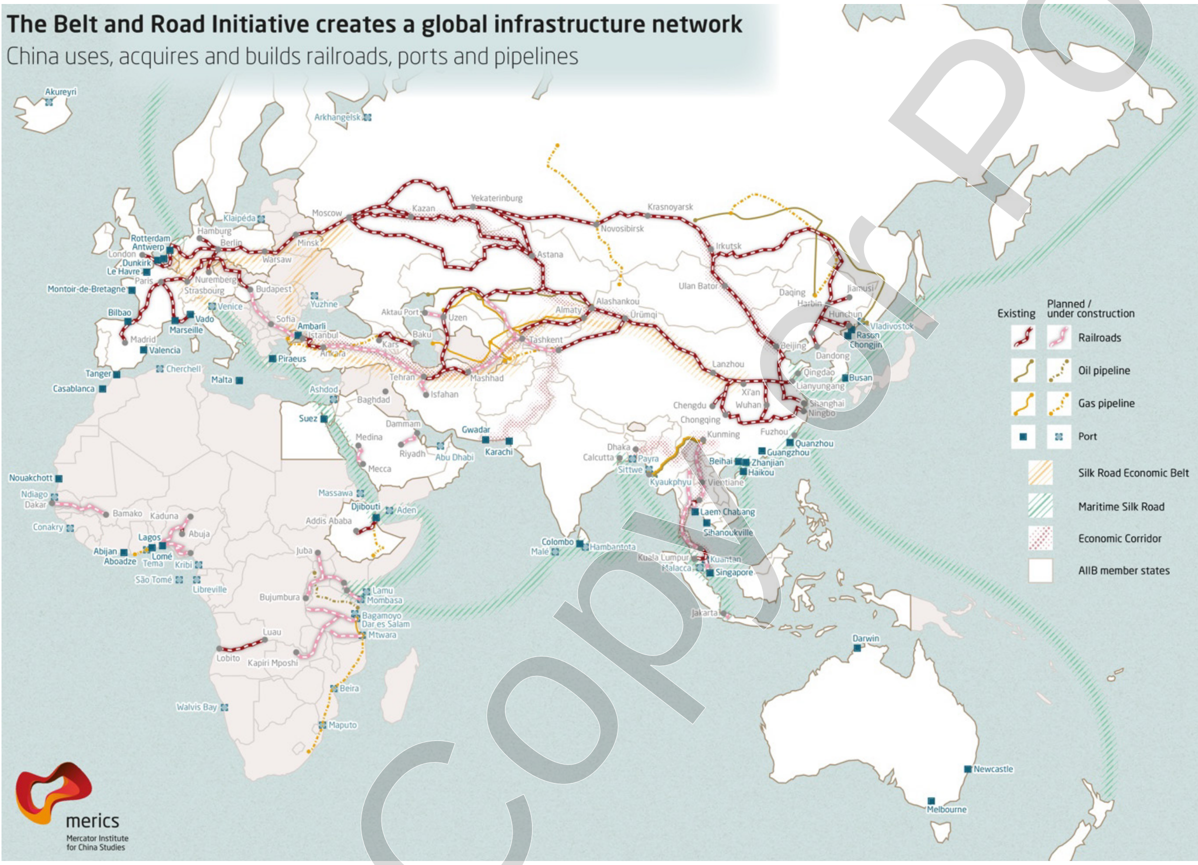
Source: Casewriters' compilation from World Bank data, see https://data.worldbank.org, accessed December 2018.

Exhibit 4 China's National Accounts

	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017
Income										
GDP (billions of current US$)	4,598.2	5,110.0	6,100.6	7,572.6	8,560.5	9,607.2	10,482.4	11,064.7	11,191.0	12,237.7
GDP growth (annual %)	9.7	9.4	10.6	9.5	7.9	7.8	7.3	6.9	6.7	6.9
GDP per capita (current US$)	3471.2	3838.4	4560.5	5633.8	6337.9	7077.8	7683.5	8069.2	8117.3	8827.0
GDP per capita growth (annual %)	9.1	8.9	10.1	9.0	7.3	7.2	6.8	6.4	6.1	6.3
Composition of GDP										
Private consumption (% of GDP)	36.1	36.3	35.4	36.1	36.7	36.9	37.7	38.6	39.5	38.4
Government consumption (% of GDP)	13.2	13.2	12.8	13.2	13.4	13.5	13.3	14.0	14.3	14.3
Gross fixed investment (% of GDP)	43.3	46.4	47.6	47.7	47.2	47.4	47.0	45.4	44.3	43.6
Exports of goods and services (% of GDP)	32.5	24.5	26.3	26.5	25.4	24.5	23.5	21.3	19.7	19.8
Imports of goods and services (% of GDP)	24.9	20.1	22.6	24.1	22.7	22.1	21.4	18.1	17.4	18.0
Welfare										
% living below $1.9/day poverty line (2011 PPP)	14.7	..	11.2	7.9	6.5	1.9	1.4	0.7	..	..
Gini coefficient	42.8	..	..	..	42.2	..	..	..	..	..
Consumer prices (annual % change; average)	6.0	-0.7	3.2	5.6	2.6	1.9	1.4	2.0	1.6	2.1
Gross domestic savings (% of GDP)	50.7	50.5	51.8	50.7	49.8	49.5	49.0	47.4	46.2	47.4
Finance										
FDI, net inflows (billions of current US$)	171.5	131.1	243.7	280.1	241.2	290.9	268.1	242.5	174.7	168.2
Government budget balance (% of GDP)	-0.4	-2.8	-2.5	-1.1	-1.5	-2.1	-2.1	-2.3	-3.8	-3.5
Lending interest rate (%)	5.3	5.3	5.8	6.6	6.0	6.0	5.6	4.4	4.4	4.4
Deposit interest rate (%)	2.3	2.3	2.8	3.5	3.0	3.0	2.8	1.5	1.5	1.5
External debt stocks (% of GNI)	8.2	8.8	12.1	13.9	13.3	15.4	16.9	12.0	12.7	14.0
Real effective exchange rate index (2010 = 100)	97.0	100.6	100.0	102.9	108.6	115.4	119.0	131.1	123.8	120.6

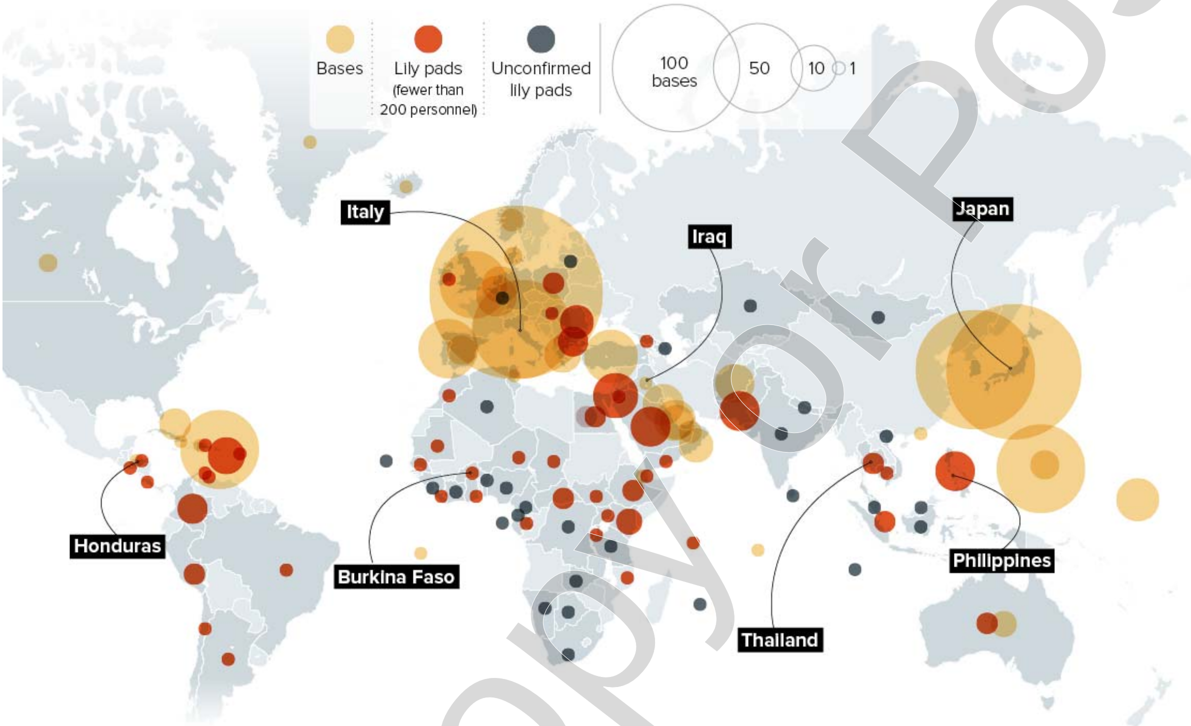
Source: Casewriters' compilation from World Bank data, see https://data.worldbank.org, accessed December 2018.

Exhibit 5 BRI Map



Source: MERICS, "Mapping the Belt and Road initiative: this is where we stand", https://www.merics.org/en/bri-tracker/mapping-the-belt-and-road-initiative, accessed November 2018.

Exhibit 6 U.S. Overseas Military Bases



Source: David Vine, "Where in the world is the US military?", *Politico Magazine*, July/August 2015, https://www.politico.com/magazine/story/2015/06/us-military-bases-around-the-world-119321, accessed November 2018. Graphic by 5W Infographics.

Exhibit 7 Sri Lanka Trade Partners

2012 Exports by Destination		2012 Imports by Origin	
USA	22%	Asia-Other	22%
EU- Other	18%	India	19%
Other	16%	Middle East	15%
Asia - Other	12%	China	14%
UK	11%	EU	9%
Middle East	10%	Singapore	9%
India	6%	UAE	7%
Germany	5%	Other	5%
2017 Exports by Destination		**2017 Imports by Origin**	
USA	26%	Asia-Other	23%
Asia - Other	15%	India	22%
EU- Other	15%	China	19%
Other	14%	Middle East	10%
Middle East	10%	EU	8%
UK	9%	UAE	8%
India	6%	Singapore	6%
Germany	5%	Other	4%

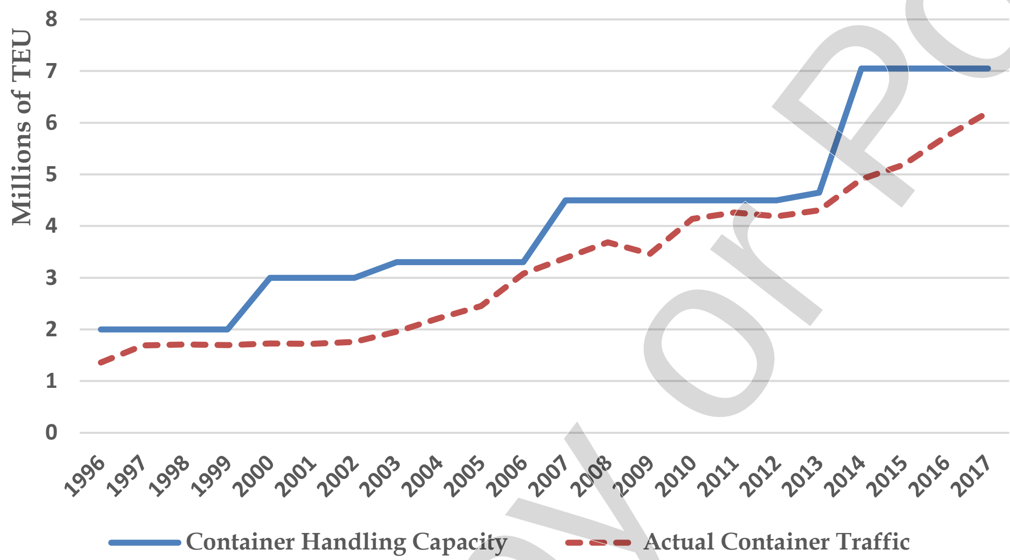
Source: Adapted by casewriters from Central Bank of Sri Lanka 2017 Annual Report.

Exhibit 8 World's Busiest Ports by Container Traffic 2017

Rank	Port	Country	2017 Container Traffic (in thousand TEUs)
1	Shanghai	China	40,230
2	Singapore	Singapore	33,670
3	Shenzhen	China	25,210
4	Ningbo-Zhoushan	China	24,610
5	Busan	South Korea	21,400
6	Hong Kong	China	20,760
7	Guangzhou	China	20,370
8	Qingdao	China	18,260
9	Dubai	United Arab Emirates	15,440
10	Tianjin	China	15,210
11	Rotterdam	Netherlands	13,600
12	Port Klang	Malaysia	12,060
13	Antwerp	Belgium	10,450
14	Xiamen	China	10,380
15	Kaohsiung	Taiwan	10,240
16	Dalian	China	9,710
17	Los Angeles	United States	9,340
18	Hamburg	Germany	9,000
19	Tanjung Pelepas	Malaysia	8,330
20	Laem Chabang	Thailand	7,760
21	Long Beach	United States	7,545
22	New York	United States	6,711
23	Yingkou	China	6,728
24	Colombo	Sri Lanka	6,209

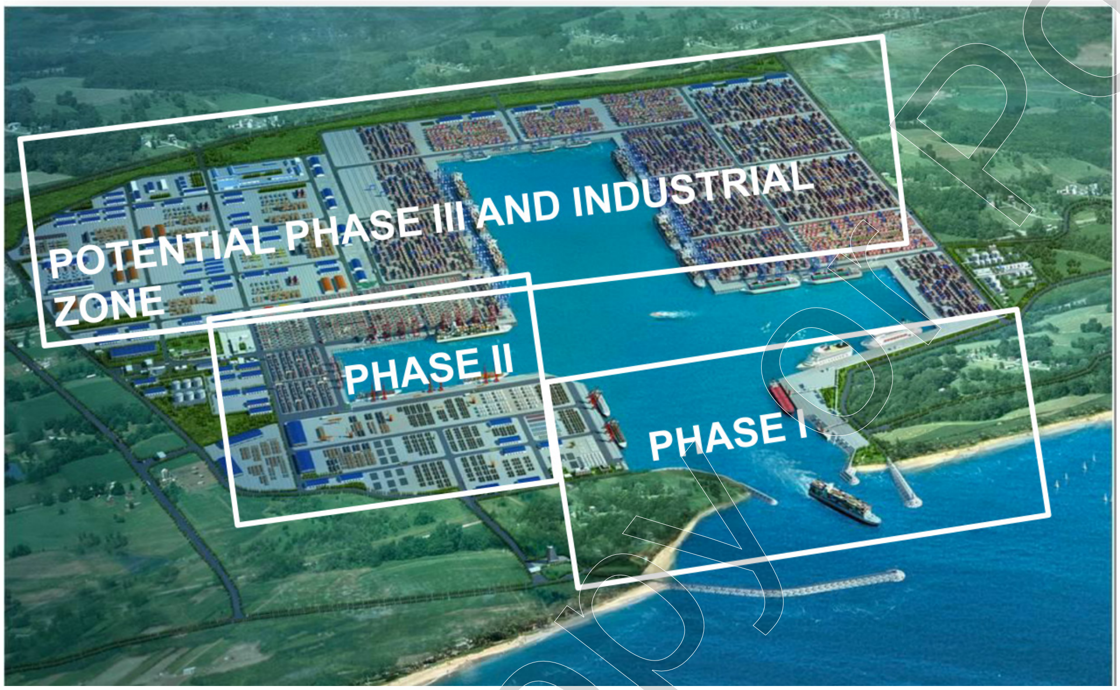
Source: Adapted by casewriters from Lloyd's List of One Hundred Ports 2018, https://maritimeintelligence.informa.com/content/top-100-ports, accessed November 2018.

Exhibit 9 Port of Colombo Capacity and Traffic



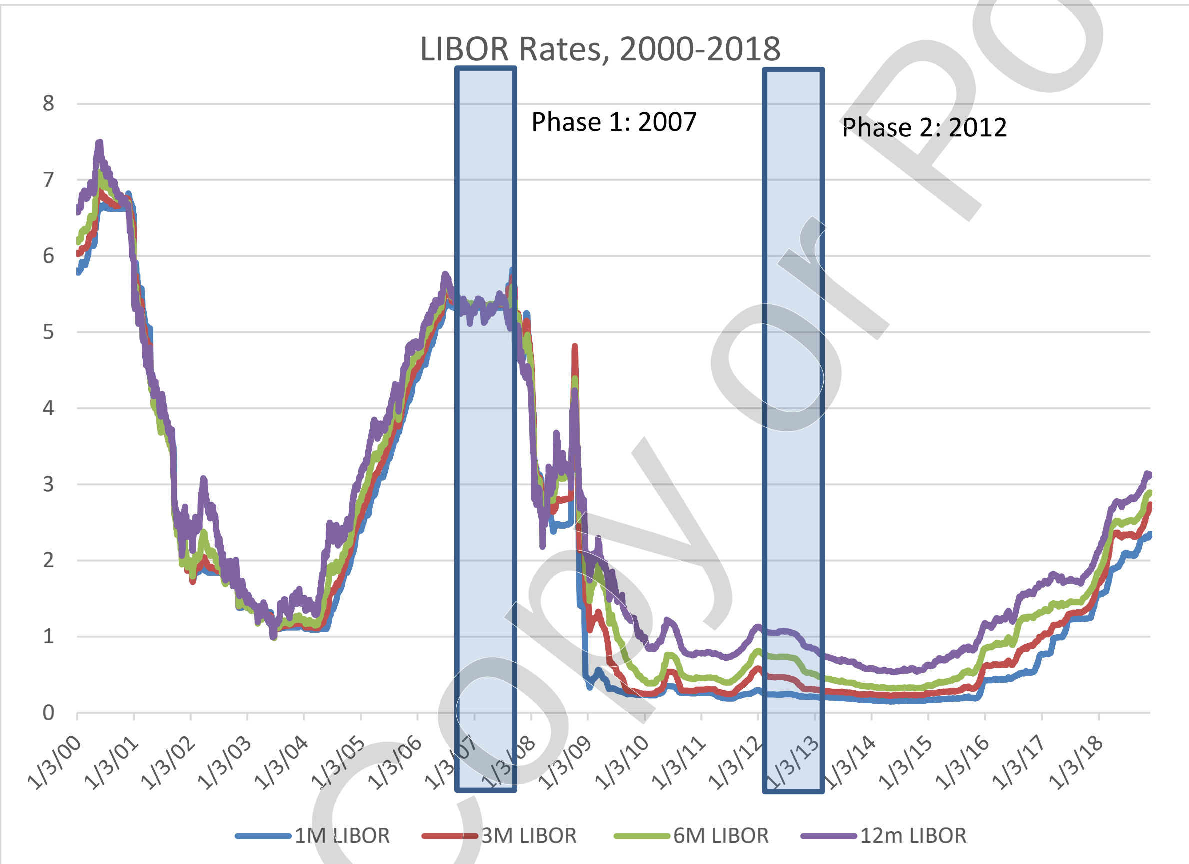
Source: Created by casewriters based on data from Sri Lanka Ports Authority Annual Reports 2013 through 2017 (see https://www.parliament.lk/business-of-parliament/papers-presented?lang=en, accessed November 2018), Asian Development Bank (see *ADB Report and Recommendation of the President to the Board of Directors, Proposed Loan: Democratic Socialist Republic of Sri Lanka: Colombo Port Expansion Project,* February 2007, https://www.adb.org/projects/documents/colombo-port-expansion-project-3, accessed November 2018), Colombo International Container Terminal Ltd., (see http://www.cict.lk, accessed November 2018), and South Asia Gateway Terminals Ltd., (see https://www.sagt.com.lk, accessed November 2018).

Exhibit 10 Hambantota Port Plan



Source: Adapted by casewriters from Sri Lanka Ports Authority, "Port of Hambantota 2016", accessed December 2018.

Exhibit 11 Benchmark Interest Rates



Sri Lanka Treasury Bond Interest Rates in 2007			
	3-year	5-year	6-year
March of 2007	14.10	..	..
June of 2007	..	..	15.04
November of 2007	..	16.00	16.05

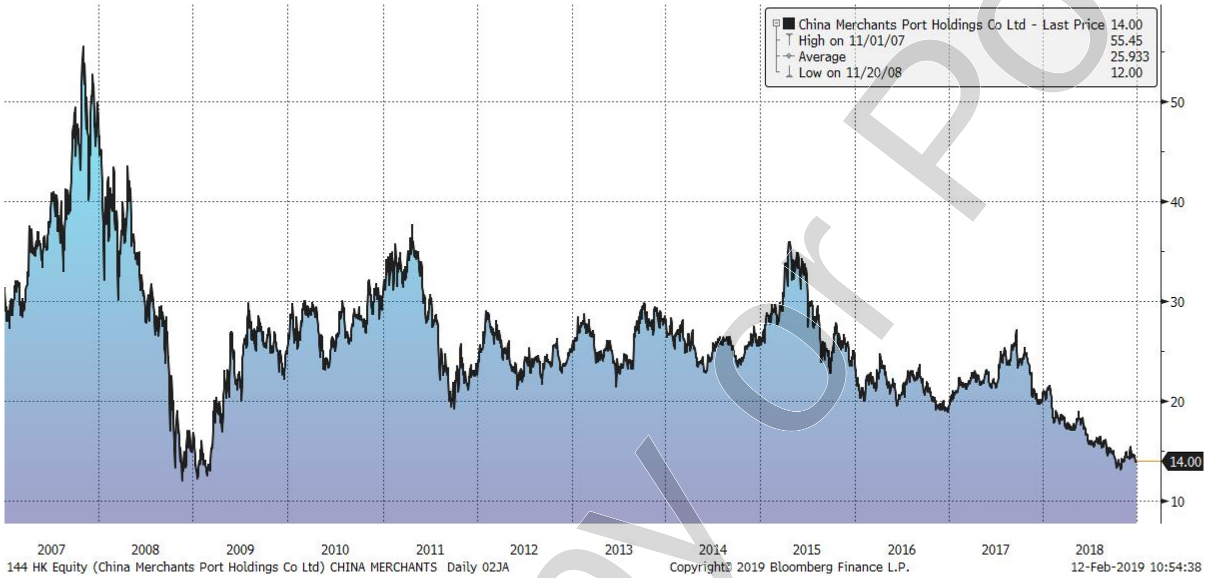
Source: Created by casewriter using data from https://fred.stlouisfed.org/categories/33003, accessed November 2018 and Sri Lanka Central Bank (see www.cbsl.lk/eresearch/, accessed December 2018).

Exhibit 12 Hambantota Port Traffic

Year	2012	2013	2014	2015	2016
Ship Arrivals					
Cargo ships	33	136	269	278	273
Ships for repairs	-	1	-	2	1
Ships for bunkering	-	-	63	7	-
Other ships	1	2	3	8	7
Total ship arrivals	34	139	335	295	281
Cargo Discharged (tones)					
Containerized	-	-	-	-	-
Break bulk	17,081	89,870	201,507	195,061	194,683
Dry bulk	-	-	-	-	-
Liquid bulk	-	-	114,056	-	25,048
Total cargo discharged	17,081	89,870	315,563	195,061	219,731
Cargo Loaded (tones)					
Containerized	-	-	-	-	-
Break bulk	2,635	28,709	103,262	85,056	134,915
Dry bulk	-	-	-	-	-
Liquid bulk	-	-	55,187	12,464	-
Total cargo loaded	2,635	28,709	158,449	97,520	134,915
Vehicles Handled					
Vehicle carrier arrival	31	134	253	276	267
Vehicles handled					
Domestic	6,411	26,458	37,923	69,195	31,519
Transshipment	4,338	38,064	160,502	116,257	150,143
Total Vehicles handled	10,749	64,522	198,425	185,452	181,662

Source: Casewriters' compilation from SLPA Annual Reports 2012 through 2016 (see https://www.parliament.lk/business-of-parliament/papers-presented?lang=en, accessed November 2018).

Exhibit 13 China Merchants Port Holdings Share Prices (in Hong Kong Dollars)



Source: Bloomberg, accessed February 2019.

Exhibit 14 Sri Lanka Balance of Payment (in millions of US$)

	2008	2012	2016	2017
Current Account (net)	(3,886)	(3,982)	(1,742)	(2,309)
Trade Balance	(5,981)	(9,417)	(8,873)	(9,619)
Exports	8,111	9,774	10,310	11,360
Imports	(14,091)	(19,190)	(19,183)	(20,980)
Services (net)	401	1,262	2,879	3,338
Receipts	1,603	3,800	7,138	7,760
Payments	2,004	2,538	4,259	4,421
Primary Income (net)	(972)	(1,219)	(2,202)	(2,355)
Receipts	(32)	142	127	160
Payments	940	1,361	2,329	2,515
Secondary Income (net)	2,666	5,392	6,453	6,327
Capital Account (net)	291	130	25	11
Credit	303	146	56	40
Debit	12	15	31	29
Financial Account (net)	1,483	(4,263)	(2,182)	(2,184)
Direct Investment: Assets	752	64	237	72
Direct Investment: Liabilities	62	941	897	1,375
Portfolio Investment: Assets	548	(10)	…	…
Portfolio Investment: Liabilities	488	2,116	993	1,772
Other Investment: Assets	2,481	363	266	102
Other Investment: Liabilities	1,813	2,384	323	1,981
Reserve Assets	690	760	(472)	2,771
Net Errors and Omissions	728	(412)	(465)	(114)

Source: Adapted by casewriters from Central Bank of Sri Lanka Annual Reports 2008, 2012, 2017, accessed December 2018.

Exhibit 15 Sri Lanka's Outstanding Foreign Debt Ownership Structure (in millions of US$)

	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016
Multilateral	5,531	5,706	5,786	5,969	6,529	6,617	7,000	6,801	7,320	7,395
ADB	2,782	2,933	2,998	3,174	3,468	3,514	3,710	3,613	3,929	3,913
IDA	2,464	2,469	2,471	2,487	2,734	2,743	2,891	2,781	2,879	2,869
…										
Bilateral	5,376	6,153	5,957	6,538	7,623	8,118	6,378	6,075	6,543	6,496
Japan	3,121	3,941	3,713	4,236	4,785	4,291	3,629	3,189	3,367	3,340
India	141	141	156	153	379	614	797	919	1,011	977
China	216	274	406	499	538	528	520	672	863	904
…										
Financial Markets	1,726	1,514	3,573	5,399	6,915	6,952	9,558	10,967	12,223	13,899
China Ex-Im Bank	-	-	-	-	-	-	-	1,120	684	1,665
Other	1,445	1,366	3,535	5,366	6,884	6,925	9,534	9,825	10,782	12,218
ISB	518	522	995	1,963	3,091	3,488	3,546	5,018	7,052	8,386
…										
Total	12,633	13,373	15,316	17,906	21,067	21,687	22,937	23,843	26,086	27,791

Source: Adapted by casewriters from Central Bank of Sri Lanka data (see "Public Debt Management in Sri Lanka: Performance in 2016 and Strategies for 2017 and beyond", *Central Bank of Sri Lanka*, 2016, accessed December 2018).

Exhibit 16 Naval Ship Visits at Port of Colombo (2009-2018)

Country	# of Visits
India	85
Japan	79
China	35
USA	28
…	
Total	430

Source: Created by casewriters with data from Jayanath Colombage, accessed October 2018.

Exhibit 17 Port City Plan

Source: CHEC Port City Colombo (Pvt) Ltd ©.

Exhibit 18 Land Prices in Central Colombo

Average Land Prices in Central Colombo per Perch (in millions of rupees)

	2012	2016	2018
Colombo 1	10	15.5	18
Colombo 2	7	10.5	14
Colombo 3	5	12	15
Colombo 4	4	11	13
Colombo 5	3.5	7.7	9
Colombo 6	3	6.5	8

Source: KPMG, *Paradise Island – Luxury living in the tropics*, *KPMG*, 2018, accessed December 2018.

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