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China's Debt Trap in Indonesia: A Case Study of the Jakarta-Bandung High-Speed Rail Project

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ABSTRACT: Thanks to the Belt and Road Initiative, the rise of China has brought forth new sets of opportunities and challenges for Southeast Asia. Indonesia has become one of Southeast Asia countries that has close economic relations with China. The Indonesia-China High Speed Rail project, which connects Jakarta-Bandung with a 142 km long line, can be seen as one of the biggest projects between Indonesia and China. However, the project faces an overrun of around USD 2 billion. This paper aims to analyze the worst possibility that Indonesia will face, namely China's Debt Trap. This paper uses the literature study method. The results show that Indonesia has the potential to be caught in China's debt-trap if there are no comprehensive economic recovery efforts without relying on foreign loans. State income from loans and debts will only lead Indonesia under the influence of the lender country. This paper suggests that Indonesia needs to reconsider its decision to use APBN funds for a new capital project, namely Nusantara. This can make Indonesia trapped in a debt-trap due to excessive reduction in state assets.

Keywords: China, Debt Trap, High-speed Rail, Indonesia.

INTRODUCTION

The official announcement of China's Go Global strategy, which encourages Chinese businesses to actively pursue internationalization, took place in 2000 (Bellabona & Spigarelli, 2007; Dong et al., 2021). Despite the failure of the Go Global 1.0 strategy, Go Global 2.0 has emerged as China's latest strategy to encourage the expansion of China's foreign direct investment and ensure companies invest abroad more carefully so that China's ambition to become a 'Champion of Free

Trade' and a global actor can be achieved (Bellabona & Spigarelli, 2007; China Policy, 2017; Sun & Lin, 2018). Today's geopolitical expression of the Go Global 2.0 strategy is known as the Belt and Road Initiative (BRI) which launched in 2013 as China's grand strategy for the 21st century. The BRI is geared toward promoting trade, infrastructure, and investment to strengthen the economic interdependence and development throughout the regions: Asia, Africa, and Europe (China Policy, 2017; Kitamura et al., 2022). This grand initiative includes two sub-strategies: the Maritime Silk Road, which encompasses East Asia, South Asia, West Asia, and Africa, and the Silk Road Economic Belt, which focuses on Central Asia (Chang et al., 2022; Z. Yang & Li, 2020; H. Zhang et al., 2022). With 147 partner countries, China and the economies it has partnered with on the BRI have seen increases in their share of the global economy (O.E.C.D., 2018).

Indonesia is one of China's cooperation partner countries in Southeast Asia which has close economic relations with China. The Indonesia-China High Speed Rail project was decided upon by China and Indonesia as a form of BRI's commitment to fund and develop infrastructure around the world. The Jakarta-Bandung high-speed train project is currently 79.9% finished, and operation is expected to begin in June 2023. Jokowi expressed his confidence that the high-speed train connecting Jakarta and Bandung will foster more mobility of people and products, improved competitiveness, and the emergence of new economic growth centers between Jakarta and Bandung (Hu et al., 2023; Li et al., 2023; Nasution, 2017; H. Wang et al., 2021).

A U.S. $2 billion budget overrun for a high-speed rail project funded by Beijing in the first quarter of 2022, however, has been a problem for China and Indonesia (Nasution, 2017; The Jakarta Post, 2022; Yin et al., 2019; A. Zhang et al., 2023). Then, in the third quarter of 2022, the second audit assertion was released with an even higher amount. To address the extra costs brought on by the project delays, this project needs more funding, which is expected to come from a state capital injection (PMN) and a loan from the China Development Bank (CDB) (Desfika, 2017; Henke et al., 2023; The Jakarta Post, 2022; Y. Yang & Han, 2020; Zhu et al., 2020). This problem at first glance looks like what is described by the debt-trap concept which has recently become the focus of analysis among researchers. A growing stigma exists around how China benefits from supporting less powerful developing countries and those that request aid. This phenomenon, when assistance is not always given with good intentions, is known as a debt trap; Such assistance, which at first seems to be a favor, subsequently turns into a debt trap for the receiver and a burden that eventually causes a severe stigma in the economy of the dependent country (Ahuja, 2022; Liu & Zhang, 2021).

This paper aims to analyze the research question: Is the Overrun of Costs on the Indonesia-China High Speed Rail a Form of China's Debt Trap? There is a possibility that the overrun of costs in the Indonesia-China High Speed Rail project is the result of Indonesia's dependence on economic assistance so Indonesia is trapped in China's debt-trap. To answer this question, the author will conduct a literature study regarding the case of budget overruns on the Jakarta-Bandung High Speed Train using the concept of the China's debt trap. The indicators used in this concept are Indonesia's sources of income as a country that borrows, profits obtained by Indonesia, and profits obtained by China as a country that provides loans.

METHOD

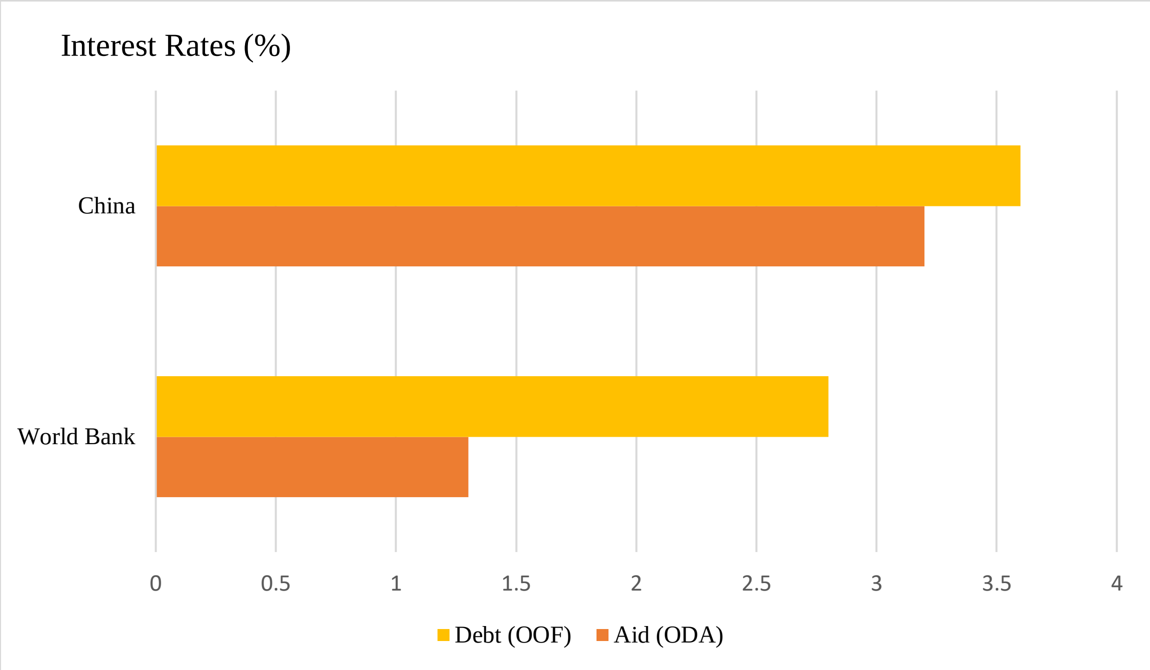
This paper analyzes the Indonesia-China High-Speed Rail using the qualitative method, namely the literature study method. The author uses archive and document-based research techniques by collecting open-source data and previous scientific work from journal articles, referring to the work of Lamont (2015). First, the author collects information about the Belt and Road Initiative from various reliable publication sources. Second, a state of the art analysis is carried out using the Publish or Perish application to see whether there has been previous research on a related topic. Third, the authors conducted a content analysis technique to collect information from journal articles with keywords: China, Debt-Trap, Indonesia, Indonesia-China High-Speed Rail.

The author analyzes the data obtained using the concept of China's debt-trap. To detail the information to be obtained from the analysis, the author determines indicators of the issue of budget overruns in the Jakarta-Bandung Highspeed Rail project: Indonesia's sources of income as a country that borrows, obtained profits by Indonesia, and obtained profits by China as a country that provides loans. This aims to answer the research questions.

RESULT AND DISCUSSION

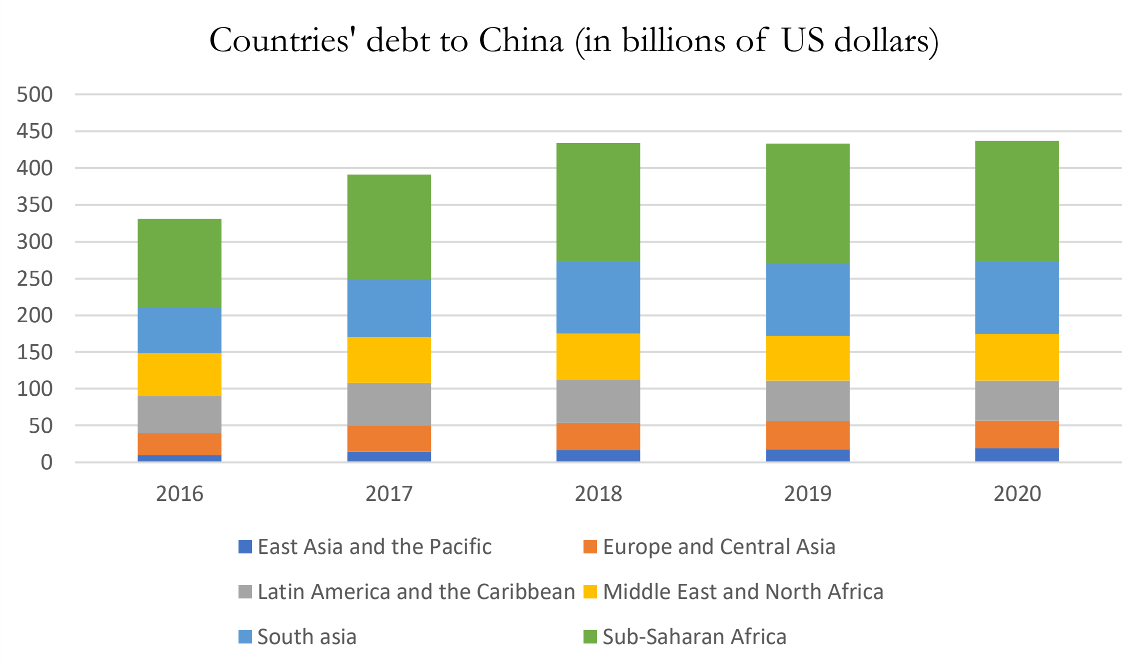
Arguments over the "debt trap" frequently capture the story of China's financing of international development. This is a result of China's development loans in the region, which are mostly financed by debt rather than aid, and which have interest rates that are significantly higher than those of benchmark institutions like the World Bank, hence providing greater returns for Chinese lenders (Cheong, 2022). This narrative is still being debated among scholars. Many latest researches in Europe and the United States demonstrate that there is no proof of the alleged debt trap, leading some to assume that the story of China's debt-trap is "a narrative trap."; There is not a single case in which China takes advantage of others' difficulties in paying back debts to grab assets or resources from other countries. China has a history of keeping information about the funding it provides for international development very secret. Thus, it is challenging to make specific claims about the viability of the "debt trap" theory in the absence of such information. However, some believe that China's debt-trap is not a wrong narrative. China has reportedly provided 150 countries with direct credit and loans totaling up to $1.5 trillion. This amount has exceeded the Organization for Economic Cooperation and Development (OECD), the World Bank, and the International Monetary Fund. Moreover, submit reports to foreign lending institutions and use secretive financing practices (Ahuja, 2022).

Figure 1: A comparison of the loan terms of China's debt-financed and aid-financed loans with the IDA and IBRD loans from the World Bank in Southeast Asia



Source: ISEAS Perspective 2022/88, 8 September 2022

Apart from this debate, several indications of China's debt-trap have emerged in the Southeast Asian region. We can see from the interest rate statistics that China's loans, either supported by aid or debt, are more expensive than those provided by the World Bank. Chinese loans financed by aid typically have interest rates that are 1.5% higher than loans financed by debt, and vice versa. However, previous analyzes regarding the truth of China's debt-trap have only focused on the Middle East region, where analysis in the Southeast Asian region is still general in nature. Going deeper, the discovery that there is a potential for Indonesia's dependence on China in the long term has also become a warning (Azmi et al., 2022). However, an in-depth study of one specific case has not been carried out. The case studies presented by previous researchers have not analyzed the overrun of cost in the Indonesia-China High Speed Rail project which also indicates the existence of China's debt-trap in Indonesia.



Source: BBC News Indonesia (2022)

The table obtained from BBC News Indonesia shows that the phenomenon of increasing countries' debt to China is a global phenomenon (K. Wang, 2022). This shows that there is a relationship of interdependence or dependence between countries and China. This global phenomenon is an early indication of a debt trap. However, determining that a debt trap occurs in a country requires other indicators, such as sources of state income and debt interest.

Indonesia has the potential to be caught in China's debt-trap if there are no comprehensive economic recovery efforts without relying on foreign loans. Criticism was given to Indonesia's decision to expect the CBD to provide financial assistance to Indonesia in covering the overrun cost of the Jakarta-Bandung high-speed rail project. Closing debt through bank loans cannot release Indonesia from economic dependence, which in the long term will make Indonesia remain in this "trap". State income from loans and debts will only lead Indonesia under the influence of the lender country.

Operationalization of the Jakarta-Bandung high-speed rail also requires a massive evaluation in obtaining returns to cover Indonesia's debt swelling to China in this project. First, the price set for the community has the potential for non-return on investment because the price is too high. This requires an in-depth analysis of the possible time for Indonesia to get a return on investment within the time limit stipulated in the Indonesia-China agreement on this project. Second, the project of moving the capital city to Nusantara could also hinder Indonesia's efforts to pay off its debts. Indonesia-China cooperation in building a new capital city in Kalimantan will only exacerbate the swelling of Indonesia's debt to China. Third, transparency in the use of loan funds is still a major problem for Indonesia. One of the main causes of debt swelling in the Jakarta-Bandung high-speed rail project is the non-transparent use of funds from the Indonesian side.

The beginning of Indonesia's foreign debt politics during the New Order era was historically marked by the creation of the IGGI (Intergovernmental Group on Indonesia) (Azmi et al., 2022).

Because per capita income tends to be low, foreign aid is one of the efforts to support economic growth in Indonesia. This foreign loan is used to fulfill the interests of economic growth in various aspects, especially infrastructure. The President of Indonesia, Joko Widodo (Jokowi), included economic diplomacy as a priority for Indonesia's foreign policy, which serves as Indonesia's national interest so that many development efforts are focused on infrastructure development. The Belt and Road Initiative has interests aligned with Indonesia; China seeks to invest in development in developing countries and Indonesia has the ambition to improve the economy through economic diplomacy. From this point on, the common interests between Indonesia and China are the reason why Indonesia agreed to join the Belt and Road Initiative (BRI) in 2016.

The History of Indonesia and the Belt and Road Initiative Cooperation

Indonesia's foreign debt to China was recorded before Indonesia joined BRI. Data shows that in 2015 Indonesia's debt to China began to increase rapidly reaching 73.79 percent. Furthermore, the amount of this debt had decreased in 2017, where it was recorded at USD 18.11 billion. Entering the pandemic in 2020, Indonesia's debt to China reached an amount of USD 20.65 billion dollars. This figure increases in 2021, where Indonesia's debt to China amounts to USD 21.24 billion dollars (Azmi et al., 2022). Recently, there has been an increase in funds in the Jakarta-Bandung high-speed rail project, which of course increases the amount of Indonesia's debt to China.

The Controversies of Jakarta-Bandung High-Speed Rail Project

The rail line has faced criticism about its effects on the area since construction started in 2017 as well as concerns on costs increasing to around $8 billion from the initial estimate of USD 6 billion. (Idrus, 2022). The cost overruns for the project's engineering, procurement, and construction (EPC) were estimated by the KCIC to be between USD 0.6 billion and USD 1.6 billion; for land acquisition, USD 0.3 billion; for financing costs, USD 0.2 billion; for headquarters and pre-operations, USD 0.2 billion; and for other costs, USD 0.05 billion (Idrus, 2022). The initial cost breakdown for the Jakarta-Bandung high-speed rail project included $4.80 billion for the engineering, procurement, and construction (EPC), USD 0.16 billion for HSR management and consultants, USD 0.80 billion for land acquisition, financing costs of USD 0.2 billion, USD 0.03 billion for headquarters and pre-operations, and other costs of USD 0.01 billion. In summary, the project's USD 6.07 billion financial structure was made up of a USD 4.55 billion loan from the China Development Bank (CDB) and USD 1.52 billion in equity, which included USD 0.91 billion in PT Pilar Sinergi BUMN Indonesia (PSBI) equity and USD 0.61 billion in equity from the Chinese consortium.

Due to this increase in funding, the government chose to use the State Budget (APBN) to get involved in the Jakarta-Bandung high-speed rail project. This decision is in contrast to an earlier commitment and regulation in 2015 that restricted any use of the state budget for its development (Suryadinata, 2018). Jokowi opted to permit the government to join the cost of the project in October 2021. A parliamentary panel was informed by the finance minister a month later that the government had chosen to fund the project with 4.3 trillion rupiah (USD 299 million) (Nasution, 2017). The inclusion of State Equity Participation (PMN) in 2021 and the allocation of Rp4.3 trillion for PT KAI (Persero) in 2022 are approved by the government and Commission XI of the House of Representatives (DPR) for the base quality standards of the Jakarta-Bandung high-speed rail project (Nasution, 2017). However, critics of this policy argue that the distribution of project financing could exhaust state coffers and leave Indonesia in a debt trap. Changing policies from what was stipulated in the initial agreement will further endanger Indonesia in the long run. This is due to the capital loan from China for this project which is part of BRI, which has a higher loan interest than the World Bank. Dividing payments in this project is dangerous in terms of APBN fund allocation. Until now, there have been many domestic problems regarding tax payments and public facilities in Indonesia. Efforts to pay off debts focused on raising prices and paying citizens' taxes. Some of the issues that continue to occur are increasing tax prices, removing fuel subsidies, and increasing other costs which in the end tend to make Indonesian people miserable. The Minister of Finance of the Republic of Indonesia, Sri Mulyani, said that Indonesia is able to repay debts if the people pay taxes. In fact, even though the tax amnesty has been held, the trend of taxes is still declining (Azmi et al., 2022).

The problem in closing debt also lies in the effort to return the capital of this fast train project. It is projected that the operation of this high-speed train will not become the main interest of the community because the costs are too high. Suryadi Jaya Purnama, a representative of the Transportation and Infrastructure Commission of the Parliament, issued a warning that many people could not afford to take the train (Nasution, 2017). More than that, the consortium stated that the high-speed rail service was anticipated to turn a profit 40 years after completion - not 20 as originally anticipated - in part because plans to relocate the national capital from Jakarta to Borneo would significantly decrease the number of users. The possibility of sufficient profit to cover debts exceeding 40 years. Therefore, it is necessary to calculate the return on investment from fast train operations to avoid applying for other foreign loans to CDB, where this borrowing of funds will also leave Indonesia trapped in China's debt trap.

CDB Loan as a Solution for Indonesia

Judging from this situation, Indonesia's position is that it has little choice but to negotiate with China. The Chinese and Indonesian sides computed different cost overruns for the most recent audit. The assumptions made by each side vary and the Chinese side's estimate of the cost overrun was smaller since it assumed the network band utilized for railroad communications was unrestricted. Since the project requires additional funding to address the overrun costs incurred due to project delays, the Indonesian government expects that the CDB loan will hasten railway construction. According to the CDB and the consortium of Chinese state-owned enterprises (SOEs), Indonesia looks to be inflating the cost overrun. Both funds cannot be distributed because there is no consensus on the amount of the overrun cost (The Jakarta Post, 2022). This has become an obstacle for Indonesia and China in negotiating a resolution to the problem if transparency is not realized.

China's Debt-Trap is a Real Narrative

Indonesia must also be able to make the rational choice based on cases that have occurred in other countries. The China's debt-trap narrative is not just a false narrative; This phenomenon is true in various countries. Given that criticism of China's debt-trap narrative lies in China's intention to trap partner countries through lending and investment, the argument that can be given is that China does not have data transparency in lending funds. The case of China's non-transparency occurred in Africa, which led to an increase in the state's debt to China. China has significantly overtaken the other "new" donors present in Africa as the continent's largest creditor (Reisen, 2007). China focuses mostly on telecommunications, transportation, and infrastructure for mineral extraction. Financial transparency is challenging to accomplish because business is frequently conducted on a barter basis. Consider the Angola Mode, where money is not directly provided to the recipient state but rather, with the recipient nation's agreement, the Chinese government directs a Chinese construction company (which typically receives support credit from China Exim) to carry out the construction project (Reisen, 2007). The borrowing government will then grant a Chinese company operating in the field of natural resources (primarily oil or minerals) the right to mine those resources through the acquisition of equity stakes in a state oil company or through the acquisition of licenses for production in exchange for the provision of the infrastructure. Therefore, the OECD claims in its report that China still lacks sufficient transparency regarding the volume and rate of commerce (Reisen, 2007).

This lack of transparency makes it difficult for observers to analyze the truth of the debt-trap. More than that, there are indications that many countries have criticized the requirements for borrowing money from China, which are said to provide high interest rates, for example in the case of Tonga, which borrowed to build infrastructure but instead experienced a new crisis at the China Eczema Bank due to high interest rates. A similar case with Indonesia also occurred in Laos. The entire public and publicly guaranteed debt of Laos is expected to exceed 88% of the country's GDP in 2021, according to a World Bank assessment released in April (Bank, 2022; Jiang, 2022). About half of the debt, or $14.5 billion, is owing to China on loans taken out to finance various projects, such as the China-Laos railway (A.N.I., 2022). If the debt-trap narrative were false, similar cases would not occur in many developing countries.

The Projections of Indonesia's Foreign Debt in the Future

Indonesia needs to consider development in Nusantara, Indonesia's new capital which is currently under construction. The construction of the nation's capital could complicate Indonesia's situation in the long run. According to some scholars, China's "debt trap diplomacy" with the Belt and Road initiative has actually "victimised" Indonesia, Malaysia, and Sri Lanka. Given that Indonesia owes Chinese lenders more than US$22 billion for funding the Jakarta-Bandung High Speed Rail project, there are concerns that the growing Indonesia's financial liabilities to China will continue to climb due to the new nation's capital project. This projection is not based on the assumption that China is the project donor. The biggest concern lies in the use of the State Budget to run the project for the new state capital, which will make Indonesia likely to have difficulty paying debts to China. The construction of the first phase of the IKN has started using funds from the state budget, and will last until 2024. The use of this state budget is indeed done to avoid foreign loans from China, even though China has offered investment in the form of infrastructure projects for the construction of a new capital city in East Kalimantan, including cooperation in the energy sector, in 2020. Gezhouba is one of the Chinese companies interested in investing in the development of the national capital (IKN). However, there has been no further information regarding whether Indonesia will accept the investment offer. The IKN Authority Body claims that most of the investments are made by private companies. Private investment – both direct investment and through partnerships with the government – is planned to contribute 80% of project funding worth IDR 466 trillion, around IDR 372 trillion. The Rp.466 trillion project will also continue, even though the world economy is predicted to face a recession. Even though the IMF has predicted a slowdown in the global economy due to the war in Ukraine and rising prices for basic necessities, the Indonesian government will continue to build the nation's capital in Kalimantan.

The step that can be taken by Indonesia to resolve the overrun cost in the Jakarta-Bandung fast train project is a transparent debt calculation. Rahadian Ratry, secretary of PT Kereta Cepat Indonesia China (KCIC), acknowledged that China and Indonesia used different costing methodologies. The assumptions and procedures used were different, which was the fundamental reason for the difference. For instance, China believed that the GSM-R frequencies—used for signaling trains—were unrestricted in China. GSM-R is nevertheless made available in Indonesia through a frequency sharing scheme with Telkomsel, which is not cost-free and requires an investment. Didiek Hartantyo, president director of PT Kereta Api Indonesia (KAI), testified before the House of Representatives in July that the firm had just US$771 million since about September 2022. However, the estimated financial expenditure for the fourth quarter of 2022 was $1.46 billion, which indicated that the project lacked the necessary US$689 million to complete construction by the end of the year. Therefore, dialogue between Indonesia and China needs to be carried out by focusing on the debt analysis.

Second, repayment of the debt burden can be done by putting forward policies that can increase the trend of declining tax payments. The way that can be done is socialization of tax payments to the public. This strategy is carried out to give the right mindset to the community that the taxes they give are for themselves. When people already have a positive outlook, of course they will have the awareness to pay taxes and help increase the trend of paying taxes. This effort must also be accompanied by a productive APBN draft. The government needs to reconsider the draft state budget for the construction of a new state capital so that excess spending does not result in a reduction in state wealth on a large scale.

Third, economic growth that is not accompanied by high per capita income will have an impact on Indonesia's Gini ratio. The government needs to pay attention to inclusive economic development. So far, Indonesia's ambition lies solely in economic growth marked by advances in technology and infrastructure. The similarity of interests between Indonesia and China is indeed tempting for Indonesia. However, this economic cooperation does not look promising in the long run because Indonesia still tends to be unprepared in terms of good governance; there is still a lot of corruption and lack of transparency which exacerbates the amount of Indonesia's debt.

Even if the debt-trap exists, China will not take coercive steps. The economic cooperation promoted by China is always no-string-attached. This means that China is promoting profit-based economic diplomacy, without paying attention to aspects of good governance. In contrast to the United States which is strict on the good governance index, China is more inclusive in implementing BRI. However, it is possible that China has great power in a country because of economic dependencies. Therefore, the debt-trap in Indonesia needs to be a concern of the government.

CONCLUSION

Literature concerned about China's debt-tap has been around for a long time. This analysis sees that the debt-trap narrative is true. Debt-trap occurs when China lends to developing countries in excessive amounts, making it difficult for the recipient country to repay the debt. This phenomenon is evident in various countries in Africa and Asia. The Jakarta-Bandung high-speed train project is clear evidence of China's debt-trap. This argument is based on several similar cases that occurred in various countries, one of which is Laos. Laos is also experiencing an increase in the amount owed to China from the high-speed rail construction project. In addition, the debt-trap is also indicated by a higher interest rate compared to the World Bank. Indonesia, which is not ready in terms of good governance, especially the issue of corruption which is still rife, is a contributing factor in the cause of excess debt. Lack of transparency has also exacerbated this situation, causing fact-finding to be difficult and Indonesia-China negotiations to be hampered. Therefore, lending money to CDB is not a rational choice for Indonesia.

Indonesia needs to reconsider its decision to use APBN funds for a new capital project, namely Nusantara. This can make Indonesia trapped in a debt-trap due to excessive reduction in state assets. Apart from that, Indonesia also needs to recalculate the amount owed by Indonesia to China. Negotiations need to be carried out between the two parties, bearing in mind that China is known for its lack of data transparency in providing foreign debt. Indonesia's ambition to realize rapid economic growth needs to be balanced with an increase in per capita income which can be a sustainable asset for Indonesia. All of these efforts aim to reduce Indonesia's economic dependence on China.

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