CHINESE INVESTMENT IN THE PHILIPPINES: CORROSIVE CAPITAL?

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The Stratbase ADR Institute for Strategic and International Studies (ADRI) is an independent international research organization focused on the in-depth analysis of economic, social, political, and strategic issues influencing the Philippines and the Indo-Pacific region. In the age of geopolitical uncertainties and technological advancements, ADRI gives equal importance to the interdependent nature of states, sectors, and stakeholders in its strategic analyses and solutions design.
Introduction:

Early in his administration, President Rodrigo Duterte announced that the Philippines would pursue a closer relationship with China in order to fulfill his campaign promise of improving the country’s infrastructure and creating jobs for Filipinos. The vision that propelled Duterte’s 2016 electoral campaign just happened to align with that of China’s leader, Xi Jinping: maneuver the Philippines into the fold of the Belt and Road Initiative (BRI). The BRI is China’s global strategy of investing in infrastructure development in order to connect Asia with Africa and Europe via land and maritime networks, ostensibly with the aim of boosting trade and economic growth. Despite its positive mission, the BRI suffers from a reputational burden: many in the international community see the BRI as an instrument of debt-trap diplomacy.

This report will examine how the BRI has unfolded across the Philippines by providing an in-depth analysis of official and unofficial BRI projects. Two are banner BRI projects under Duterte’s Build, Build, Build (BBB) program, which is funded by official development assistance (ODA) loans from China: the Chico River Pump Irrigation Project (CRPIP) which aims to provide a stable supply of water to some 4,350 farmers across 8,700 hectares, and the New Centennial Water Source-Kaliwa Dam Project (NCWS-KDP), which aims to supply some 600 million liters of water per day to nearly 17.5 million people in and around the nation’s capital, Manila. The third and fourth projects are the Safe Philippines Project (Safe Philippines), a video surveillance system funded by a Chinese ODA loan, and the DITO Telecommunity Corporation (DITO), formerly the Mislatel Consortium, the third major telecommunications operator in the country. While Safe Philippines and DITO have not been officially declared BRI or BBB projects, both are embodiments of the BRI’s Digital Silk Road (DSR), which has deployed major Chinese technology companies such as Huawei, China Telecommunications Corporation (ChinaTel), and its subsidiary, China International Telecommunication Construction Corporation (CITCC), to build cell towers and install closed-circuit television (CCTV) in major Philippine cities.

All four projects have generated controversy for the Duterte administration amid widespread allegations of disregard for the rule of law and a lack of both transparency, and accountability.

Governance Gaps

China has long promoted its BRI projects as win-win opportunities for both China and recipient countries. While the Philippines unquestionably needs private and public investment to fuel economic growth, governance gaps must be taken into consideration when assessing the overall benefit of the influx of major investment from China.

This report attempts to assess the corrosive effects of China’s investments on Philippine governance in the following respects: rule of law, public trust in government, and bilateral relations. In addition, this report also makes policy recommendations.
Lack of Transparency

One notable governance gap identified in each of our four case studies is lack of transparency. Loan agreements for the CRPIP and NWCS-KDP, for example, include so-called “confidentiality clauses” that prohibit the Philippines from disclosing any information about the terms of the agreements without the prior written consent of the Export-Import Bank of China (China EXIM Bank). Confidentiality clauses are common in contracts from Chinese lenders, but not contracts from other foreign lenders.

International standards dictate that public procurement documents should be easily accessible, and widely circulated, in order to allow all interested parties to monitor outcomes and results.

While the Philippine Department of Finance (DOF) has argued that the loans for the Kaliwa and Chico dam projects had “standard” provisions, including confidentiality clauses, expert analysis shows that other countries’ ODA loans typically do not contain confidentiality provisions. Even if the documents can be made available upon formal request, as the DOF asserts, the confidentiality clauses and heretofore-unpublished details of the projects serve to deter civil monitoring and degrade overall transparency.

Some Philippine lawmakers have pushed back against the loan agreements, alleging that the terms infringe upon the “constitutional right of the Filipino people to information on foreign loans obtained or guaranteed by the government” and considered “inimical to the national interest.” Section 21 of Article XII of the Philippine Constitution states, in part, that “information on foreign loans obtained or guaranteed by the Government shall be made available to the public.”

In March 2019 the DOF, most likely in response to calls for loan agreements to be made public, posted a copy of the CRPIP agreement on its website, almost a year from the date of signing. Still, there is a dearth of information on the websites of other concerned government entities. An online search for the details and history of the CRPIP yields only basic information, such as the land area affected by the project and the targeted number of beneficiaries. In fact, the language reads as if it were lifted from the same official source—presumably, a press release.

The other two case studies – Safe Philippines and DITO – reveal a similar lack of transparency.

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Little information has been released publicly about the bidding process for Safe Philippines other than the announcement on October 17, 2018 of the start of bidding, and the selection of CITCC on November 16, 2018. The corresponding Department of Interior and Local Government (DILG) feasibility study, credit loan agreement, and bid documentation are not available online. The loan agreement for Phase 1 of the Safe Philippines Project was posted on the DOF website on July 22, 2021.7

Ralph Reco, former Senate president pro-tempore, said DILG not only submitted insufficient data about the project, but failed to independently conduct, or provide copies of, the feasibility study.8 The lack of transparency surrounding Safe Philippines was the main impetus for the 2019 passage by Congress of Special Provision No. 17 of the General Appropriations Bill, which aimed to prevent the use of public funds for surveillance systems but was ultimately vetoed by Duterte.9

The DITO bidding rules evidenced a lack of transparency and clarity about who was qualified to bid. PT&T, which has operated in regions across the Philippines for some 56 years, was disqualified after the NTC declined to certify that the company has been operating on a national scale for the past 10 years. The original ToR, however, require only that bidders carry out the “provisioning, delivery and operation of telecommunications services for a country, or particular regions thereof, as geographically designated by the telecommunications authority of that country.”10 The NTC subsequently amended the terms to stipulate that only foreign telecos could qualify under the regional operations provision.11 In other words, foreign firms with regional operations would qualify, but Philippine firms—such as PT&T—would not. (PT&T would need to operate, too, in the regions of Luzon, Visayas, and Mindanao to qualify as national, not regional, in scale.) PT&T President and CEO James Velasquez characterized the ruling as “discriminatory and, in a way, anti-Filipino.”12

**Loan Agreement Issues**

The CRPIP is financed through an ODA loan from China EXIM Bank with an interest rate of 2 percent per annum and a maturity period of 20 years, including a seven-year grace period. The Philippines signed the loan agreement with China without first securing approval the Monetary Board, the policymaking arm of the Philippine central bank.

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According to Article VII, Section 20 of the Constitution, foreign loans may only be inked “with the prior concurrence of the Monetary Board, and subject to such limitations as may be provided by law.”

The interest rates of loans from China place the Philippines at a significant disadvantage.

The loan agreements with China for both the CRPIP and the NCWS-KDP, when compared to similar contracts for ODA projects signed with Japan and South Korea, feature less favorable interest rates, longer loan repayment periods, and grace periods for loan repayment. The loan for the CRPIP, for example, has an annual interest rate of 2 percent whereas the interest rates of comparable loan agreements with South Korea and Japan are 0.15 percent and 0.25 percent, respectively.

Former Socioeconomic Planning Secretary Ernesto Pernia, then-director general of the National Economic Development Authority (NEDA), justified the decision to accept the 2-percent interest rate as a matter of “trying to diversity” funding and secure “friends” like China to support ambitious infrastructure projects.

The most controversial issue in loan agreements with China is not interest rates, however, but waivers of sovereign immunity. Although such waivers are standard practice in Chinese loans worldwide, the waiver violates the Philippine Constitution, which asserts in Section 3, Article XVI, that “the State may not be sued without its consent.” This waiver exposes Philippine public finances and assets in the event of a default or dispute, spurring fears of a debt trap. Moreover, such disputes would be arbitrated in China, by Chinese arbitrators. This requirement is a departure from arbitration clauses in other foreign loan contracts, such as those with Japan, which specify that an arbitrator must be from a third-party nation.

Many experts and interest groups have questioned the terms of Chinese loan agreements as unfavorable to the Philippine government, and in direct violation of the Constitution.

Circumvention of Procurement Laws

The pre-selection of contractors, and a lack of competition in the tendering process, are recurring themes in all four case studies.

For the CRPIP, the selection of China CAMC Engineering Co., Ltd. (CAMCE) as the primary contractor appears to have violated the Philippines law on procurement, which mandates that preference should be given to domestic contractors. Documents associated with the decision (CAMCE is stipulated in the loan agreement with China EXIM Bank) are not publicly available, in keeping with the general scarcity of information surrounding the CRPIP.

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15 Ibid.
17 Anna Gelpern et al, How China Lends: A Rare Look into 100 Debt Contracts with Foreign Governments
19 Rivas, 2018
The selection process of the contractor for NCWS-KDP raises similar questions. Three firms bid on the contract, as required by law. However, all three firms were Chinese; one was disqualified for failing to meet technical eligibility requirements, and another was disqualified for submitting a bid that exceeded the approved budget (despite being informed, in advance, of the limit). China Energy Engineering Corporation, Ltd. (CEEC), a Chinese state-owned enterprise (SOE), was effectively chosen by default—leading to allegations by observers that the other Chinese bidders participated merely to satisfy Philippine procurement law.

In the case of DITO, two of the three bidders also were disqualified on dubious grounds. The disqualification of the bidders in the ostensibly competitive process meant Mislalat, now DITO, had only to meet the minimum requirements. Philippines-based NOW Telecom filed a lawsuit seeking both a temporary restraining order (TRO) and an injunction in the bidding process. The suit was thrown out by a lower court, and an appeals court subsequently upheld the decision.

This outcome is concerning in light of the Duterte administration’s previous warnings to judges not to interfere with the establishment of a third telecom. Former presidential spokesperson Herminio “Harry” Roque quoted Duterte as saying, “Do not issue any TROs or injunctions.”

Bidding for the Safe Philippines project, too, was controversial. Bid Bulletin No. 1 for the project stated outright that only “legitimate Chinese government-owned corporation[s]” would be eligible to bid on the contract:

An eligible bidder shall be a legitimate Chinese government-owned corporation and a registered manufacturer of quality equipment and product relevant and required in the Safe Philippines Project. Bidding will be conducted in accordance with the applicable procedures as specified in the Government Procurement Reform Act and is open to the three pre-selected bidders as recommended by the Government of the People’s Republic of China, as defined in the Bilateral Agreement.

This clause was controversial for two reasons. First, Philippine law requires that the state give preference to Philippine contractors. (Because the president is empowered to waive or modify this requirement “when necessary,” the law was effectively rendered moot.) Secondly, multiple laws mandate that the bidding process for government tenders be transparent and competitive. Under Philippine law, “competitive bidding” is defined as “open to participation by any interested party.”

Restricting bidding to Chinese SOEs was an apparent violation of Philippine law.

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23 Emphasis supplied

Philippine procurement law also requires the bidding process to include at least three eligible bidders. In the case of Safe Philippines, two of the three Chinese SOEs that bid on the contract (Huawei and CMEC) were disqualified by DILG, which did not reopen bidding. In 2019, the Philippine Commission on Audit (COA) found that Huawei and CMEC participated merely to provide a semblance of competition for a contract that had already been negotiated with the DILG.\textsuperscript{25}

Lawmakers attempted to put a stop to the Safe Philippines project by passing Special Provision No. 17 of the 2019 General Appropriations Bill, which stated that “no amount appropriated herein shall be utilized for any project intended for public video surveillance … with suppliers or service providers that are considered as serious risks to national security or interests.”\textsuperscript{26}

Duterte, however, exercised his line-item veto power to strike down the provision, arguing that it was unconstitutional because it limited the foreign policy powers of the president.\textsuperscript{27}

**National Security Concerns**

National security is a primary concern in the DITO and Safe Philippines projects. On July 8, 2019, DITO became the third and newest major telecommunications provider in the Philippines when it was granted a Certificate of Public Convenience and Necessity by the government, authorizing the company to begin building infrastructure and offering services nationwide. DITO is a joint-venture comprised of Udenna Corporation, Chelsea Logistics and Infrastructure Holdings Corp. (Chelsea), and China Telecommunications Corporation (ChinaTel).

Under the Chinese National Intelligence Law of 2017, ChinaTel—like all Chinese citizens and companies—is required to provide intelligence to the government.\textsuperscript{28} Granting control to a Chinese SOE over parts of the national telecom infrastructure of the Philippines has clear implications for national security.

Already there is longstanding tension between the two countries over the South China Sea and China’s territorial claims, which infringe upon Philippine national waters. China is well-known, moreover, for its extensive use of cyber attacks to gain strategic and economic advantages over its competitors. By ceding some degree of control over cyberinfrastructure, the Philippines—a country already highly vulnerable to cyber attack—could further compromise its ability to defend itself.

Even though the Duterte administration has argued that Safe Philippines will not store national security data, the involvement of CITCC—an affiliate of ChinaTel—raises alarms over the safety of critical Philippine cyberinfrastructure.

Furthermore, the Armed Forces of the Philippines (AFP), the country’s military, has given permission to DITO to co-locate some of its equipment at Philippine military facilities. The AFP insists that DITO will adhere to strict construction standards, and that DITO’s access to military installations will be

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\textsuperscript{25} Commission on Audit, "Audit Observation Memorandum issued to the Metropolitan Waterworks and Sewerage System,” June 10, 2019


carefully controlled. There is precedent for this: similar permissions also have been granted to the two other major Philippine telecoms, Globe Telecom and Smart Communications. But the case of ChinaTel departs from precedent: While Globe and Smart have partnerships with firms from Singapore and Japan, respectively, those firms are not directly linked to the governments of Singapore and Japan.

Privacy and Data Governance Challenges

Online scams rose drastically across the Philippines in 2020. “There were 869 cases reported within a six-month period, which is an increase of 37.3 percent compared to the same period for 2019. Identity theft also increased by 21.47 percent with 362 cases.” Such vulnerability raises concerns over the government’s capacity to secure the system against intrusion by non-state actors—calling into question the decision to build a comprehensive, centralized network.

The Duterte administration has argued that Safe Philippines is not intended to serve as a surveillance system. Yet a key technology in the project is CCTV footage, notably paired facial recognition software, which constitutes “personal information” under the Philippine Data Privacy Act of 2012. Over the past decade the Philippines has taken further measures to attempt to guarantee the privacy of citizens’ personal information and ensure the integrity of the country’s cyberinfrastructure through the establishment of: the National Privacy Commission, the Department of Information and Communications Technology (DICT), and a DICT subordinate agency, the Cybercrime Investigation and Coordinating Center.

Thus far, none of these institutions have issued public statements on Safe Philippines.

Conflicts of Interest

The issue of cronyism is most evident in the case study of DITO. The Udenna Corporation, part of the group that won the project, is the Philippine holding company of the Uy family, members of which contributed heavily to Duterte’s presidential campaign. Dennis Uy, head of Udenna, contributed USD $597,000 (P30 million). Uy’s wife, Cherylyn, the treasurer of both Udenna and Chelsea, contributed USD $19,900 (P1 million). And Efren Uy, a board member of Chelsea, contributed USD $69,650 (P3.5 million).

Many other prominent members of the winning joint-venture also gave significant amounts of money to the Duterte campaign.

There is nothing criminal about being friends with someone who is elected president. And the apparent links between political contributions and crony capitalism are circumstantial; on their own, they do not necessarily constitute graft or corruption. However, the relationships raise questions about propriety and fairness. As early as 2017, Duterte offered China the privilege of a telecom license. ChinaTel then partnered with Dennis Uy to become the only qualified bidder in a process in which fairness was widely called into question.

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Recommendations

The four case studies mapped and identified issues in the pre-implementation stages of the projects. In light of the scarcity of information and documentation surrounding each project, consistent monitoring and evaluation is imperative to further study the corrosive nature of the investments.

Raising awareness of the patterns common to the projects is especially crucial as the current administration nears the end of its term, and a new election cycle begins: Public and media attention already is increasingly focused on irregularities and mismanagement, graft, and corruption in government. Publicizing examples of the links between governance gaps and Chinese foreign investment could again catapult into view projects like CRPIP, NCWS-KDP, and Safe Philippines, helping to ensure they remain of concern to the public.

Increasing public awareness will play an important role in future foreign investment in the Philippines, especially pertaining to projects associated with authoritarian countries like China. Framing the discussion around relevant issues in the Philippines will help both the public and private sectors attract and maximize foreign investment, as well as ensure greater transparency and accountability.

Conclusion

Ultimately, the four projects examined in this report – each linked to, or directly funded by, China – constitute corrosive capital. The evidence-based approach employed by our researchers at Stratbase ADR Institute for Strategic and International Studies (ADRI) has expanded, deepened, and elevated ADRI's anti-corruption and anti-corrosive-capital advocacy.

The projects directly and indirectly violate and undermine established Philippine laws and guidelines, including: the Government Procurement Reform Act (RA 9184); the Guidelines for the Conduct of Community Participation in Procurement issued by the Government Procurement Policy Board; and the general constitutional provisions established in 1987. The threats exposed in the case studies point to the importance of strengthening and promoting constructive capital through fact-based recommendations.

Finally, the case studies illustrate the interplay of internal and external political dynamics in the spread of corruption and corrosive capital. The Duterte administration’s proclivity to appease and condone China is a unique characteristic of the political economy of corrosive capital in the Philippines. Still, the May 2022 elections could deliver new national leadership, and new possibilities, in the fight against corruption and corrosive capital.

By and large, the four projects have compromised not only the economic welfare of the Philippines, but the country’s democratic rules, processes, and institutions. Together, the projects have relinquished the sovereignty of the Filipino people to the government of China.
What is BRI Monitor?

BRI Monitor is a collaborative effort by five civil society organizations in Southeast Asia and the Pacific: the Institute for Democracy and Economic Affairs (IDEAS) of Malaysia, Stratbase Albert Del Rosario Institute (ADRi) of the Philippines, Sandhi Governance Institute (SGI) of Myanmar; the Institute of National Affairs (INA) of Papua New Guinea and the Future Forum of Cambodia to promote transparency and accountability in major infrastructure projects funded through the Belt and Road Initiative (BRI) in the region.

These organizations have studied the regulatory environments governing these large infrastructure projects in respective countries, including public procurement, official development assistance, public private partnership (PPP), and more, to identify regulatory gaps. They have each researched a set of case studies to identify implementation gaps and governance gaps. Each case study assesses the level of transparency based on almost 40 data points, from basic project information to the tendering process to project completion. Last but not least, each organization maps out the structure of the projects in question in order to understand the degree of public financial exposure resulting from each project. (please check our research methodology here).

This website is intended to be a platform for the publication of our research outputs and as a knowledge repository. We also hope that the website can be used as a platform for knowledge sharing and a tool to advocate better governance of major infrastructure projects in the region.

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