



THE RESOURCE-BACKED LENDING MODEL: AN ECONOMIC LIMITATION TO SOVEREIGNTY OF DEVELOPING STATES

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Cite this article:

Ibekwe, E. C., Omidire, K. (2024), The Resource-Backed Lending Model: An Economic Limitation to Sovereignty of Developing States. African Journal of Law, Political Research and Administration 7(3), 80-87. DOI: 10.52589/AJLPRA-NM4UL5T8

Manuscript History

Received: 12 Aug 2024

Accepted: 16 Oct 2024

Published: 21 Oct 2024

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ABSTRACT: *The 21st century developing and under-developed economies are being relegated to the status of neo-colonial states. Developed economies like China, Russia and the United States of America are really in the scramble for more neo-colonial states, mostly in Africa. This has presented itself through the economic relationship among states. The economic relationship under consideration here is taking new turns with emerging global trends and the desire of developing states to alleviate or eradicate poverty. The economic relationship between developed and developing states has grown from exchange of goods and investment to the execution of infrastructure loans on the understanding that the receiving states (borrower in this instance) shall mortgage its local resources to secure the loan. This is clearly the greatest limitation to the sovereignty of developed states under the guise of business agreements. The objective of this article is to examine a number of resource-backed lending systems between developed and developing states, delving more into the business relationship between China and Nigeria; this examination is further related to the relationship between China and states like Angola and Congo. The question sought to be answered is whether this system has proved to be beneficial or detrimental to the sovereignty of developing states is considered in this study. This is done by examining the Nigeria-China Bilateral Investment Treaty and the \$400 million Loan Agreement (“Loan Agreement”) executed by the Ministry of Finance on behalf of Nigeria and the Export –Import Bank of China for the Nigeria National Information and Communication Technology (ICT) Infrastructure Backbone Phase II Project in 2018.*

KEYWORDS: Sovereignty, Developing states, Treaty, Investment, Resource-backed lending.



INTRODUCTION

The foundation of statehood is predicated on the inherent rights of states to have its sovereignty intact.¹ To this end, the inter-relation of state is based on the sacrosanct nature of political independence and territorial integrity of states.² No doubt, the international community is interconnected and no state lives in isolation, an unregulated interrelation will definitely transform the world into nothing but a thin space. The crux of the formation of all kinds of international arrangements has been driven by a desire to preserve the political independence of all existing states against external aggression and respect the territorial integrity of the same.³ Thus, nations and states have always interacted by way of technological exchange, business, trade, sporting activities, education and even the “unjust” industry of colonialism and slavery.

It is imperative to note here that foreign investment and international trade are part of the factors that lead to development in states. Foreign investment comes with the significant potential to transform the economies through productivity enhancement, innovation, creating stable and better paying jobs in the supportive industries and the sector attracting the foreign investments. Growth in the receipt economy increases by increase in the total factor productivity, through the efficient resource usage, beyond the initial macroeconomic stimulus of the actual investments. The experience in Africa and Asia today is that developing economies are heavily relying on foreign investments and bilateral trade to address their economic problems, as such investments help the countries to tackle their socio-economic issues such as balance of payment deficit, unemployment, poor technological ability, foreign exchange scarcity and lack of capacity.⁴

The relationship between developed states and developing states overtime has been in terms of export trade, import trade, Foreign Direct Investment, Infrastructural Development, technological exchange, oil trade and more recently, infrastructural loan agreements. The infrastructural loans have made their way into the inter-relatedness of states owing to the infrastructural deficits noticeable in most developing and under-developed states.⁵

Meanwhile, in the loan relationships, creditor-states usually come up with various recovery means, of these means is the adoption of the Resource-backed lending model especially where the debtor-states have valuable resources needed to achieve the expansionist and economic goals of the creditor-states. Resource-backed loans (RBL) describe the practice of using a country’s natural resources to serve as either a direct source of repayment or as an underlying guarantee of repayment in respect of the loans.⁶ It is clear that the system of RBL introduces a form of collateral loan and as seen in the case of Angola, future earnings from the proceeds

¹ R.G Tătar A. Moși, the Concept of Sovereignty, (2022) Journal of Public Administration, Finance and Law, Issue 24, P. 292.

² For example, Article 4 of the Charter of the United Nations, 1945 provides as part of the purposes and principles of the United Nations that all member states shall refrain from threat or use of force against the territorial integrity of all states.

³ See for example, Article 10 of the *Covenant of the League of Nations, 1919*.

⁴ B Ames, W Brown, S Devarajan & A Izquierdo, *Macroeconomic Policy and Poverty Reduction*, Publication of the International Monetary Fund and the World Bank, 2001.

⁵ Daniel Gurara, Vladimir Klyuev, Nkunde Mwase & Andrea F. Presbitero, *Trends and Challenges in Infrastructure Investment in Developing Countries*, (2018), *International Development Policy*, P. 3.

⁶ D Mihalyi, J Hwang, D Rivetti & J Cust, *Resource-Backed Loans in Sub-Saharan Africa*, Washington DC: World Bank Publications, 2021, P. 1.



which Angola would derive from the sale of its crude oil were used as guarantee for the loan advanced by the Chinese Export-Import bank.⁷

It can be said that this borrowing model is common in Africa, especially as it relates to the relationship between Africa and China, for instance, a World Bank publication published in 2021 reports that between 2004 and 2018, there were many RBLs entered into by African countries and the ones which were made public totaled US\$ 46.5 billion.⁸

The concern in this article relates to whether in entering these RBLs, the sovereignty of debtor-states are not mortgaged. More so, that an external undertaking is given the liberty to enter upon the territory of a “so-called” independent state and control its resources, the agreements would also normally waive the immunity of the sovereign (debtor) state to excuse itself from observing the terms of the RBLs, an example is the provision of Article 8(1) of the \$400 million Loan Agreement (“Loan Agreement”) executed by the Ministry of Finance on behalf of Nigeria and the Export –Import Bank of China for the Nigeria National Information and Communication Technology (ICT) Infrastructure Backbone Phase II Project in 2018. The said Article 8 (1) provides;

The borrower hereby irrevocably waives any immunity on the grounds of sovereign or otherwise for itself or its property in connection with any arbitration proceedings pursuant to Article 8(5), thereof with the enforcement of any arbitral award pursuant thereto, except for military assets and diplomatic assets.⁹

As shall be seen in this Article, provisions similar to the foregoing appears to be in contravention of Article 6 of the United Nations General Assembly Resolution on Permanent Sovereignty over Natural Resources¹⁰ which requires that the exploration of state resources must be done further to ensure the independence of such a state.¹¹

Conceptual Clarification

The concepts which direct the course of this paper are;

- i. Resource-backed lending
- ii. Economic Sovereignty

Resource-Backed Lending Model

Resource Backed Lending (RBL) refers to a borrowing model where all loans provided to a government or a state-owned company is guaranteed by the mortgage of natural resources. Here, the natural resources of a state known as the debtor-state is used as a collateral to secure the loan from the creditor-state.¹² It is usual that these loans are infrastructural loans which are

⁷ Ibid.

⁸ Ibid, P. 8.

⁹ China-Nigeria Loan Agreement, 2018.

¹⁰ United Nations General Assembly Resolution 1803 (XVII) of 14th December, 1962.

¹¹ Article 6, United Nations General Assembly Resolution 1803 (XVII) of 14th December, 1962. Resolution on the Permanent Sovereignty over Natural Resources.

¹² David Mihalyi, Aisha Adam & Jyhjong Hwang, Resource-Backed Loans: Pitfalls and Potential, Natural Resource Governance Institute, 2020, P. 3.



so huge and create fears in the minds of the creditor-states that the debtor-state is likely to default. Some RBLs use natural resources as collateral to mitigate the risk of payment difficulties. In these, the lender can require placement of a resource revenue flow (e.g., a set percentage of oil receipts) in escrow or assign rights to future production (e.g., assign the right to a set number of oil cargoes).¹³ This type of loan is sometimes labeled a “collateralized future commodity receipts arrangement”. In other cases, borrowers set aside a natural-resource-related underground asset as collateral (e.g., security over government ownership rights in a company with assets such as oil or bauxite reserves).

There have been notable examples of this model between China and some African states, where the states that receive lending from China usually contract future revenues from natural resource exports as loan repayment to China.¹⁴ For instance, the first of such lending by China in Africa was initiated in Angola in 2004. A \$2 billion loan from Exim was used to finance the reconstruction of infrastructure damaged in Angola’s civil war.¹⁵ The export revenue from 10, 000 barrels of oil a day over a period of 17 years would be used to repay the loan. In accordance with the loan agreement, 70% of public tenders for the infrastructure projects related to the deal were to be awarded to Chinese construction corporations.¹⁶

In essence, it can be stated that RBLs create a form of collateralized loan with pre-loan agreements which allows the creditor to secure its loan and mitigate the tension of whether or not the loan is recoverable.

Economic Sovereignty

The right and power of a state to make authoritative decisions over its territory without being subject to any higher authority is defined as state sovereignty. It is often carried out by the government, which is defined as a "constitutionally recognized body acting on behalf of the state." Sovereignty grants control over the development of political, economic, social, and cultural systems, as well as formulation of foreign policy. Economic sovereignty may therefore, be seen as the power and authority of a state to make decisions pertaining to its economic concerns without being subjected to any foreign control, it includes the right of a state to explore, exploit and export its resources without being subservient to the power of another state or external bodies.

Chapter II of the *Charter of Economic Rights and Duties of States*¹⁷ was adopted by the *United Nations General Assembly* in 1974, Article 1 asserts that:

Every State has the sovereign and inalienable right to choose its economic system as well as its political, social and cultural system in accordance with the will of people, without outside interference, coercion or threat in any form whatsoever

Article 2 further provides that:

¹³ Ibid, P. 3

¹⁴ See A Vines, C Butler & Y Jie, The response to debt distress in Africa and the role of China, Exploring solutions to African debt distress through multilateral cooperation, (2022), Chatham House Research Paper, p. 5, available at <[2022-12-15-africa-china-debt-distress-vines-et-al \(chathamhouse.org\)](https://www.chathamhouse.org/2022/12/15-africa-china-debt-distress-vines-et-al)> last accessed on 15/3/2023.

¹⁵ Ibid.

¹⁶ Ibid.

¹⁷ *The Charter of Economic Rights and Duties of States: A Resolution adopted by the General Assembly 1974*



Every State has the right (a) to regulate and exercise authority over foreign investment within its national jurisdiction in accordance with its laws and regulations and in conformity with its national objectives and priorities. No State shall be compelled to grant preferential treatment to foreign investment; (b) to regulate and supervise the activities of transnational corporations within its national jurisdiction and take measures to ensure that such activities comply with its law, rules and regulations and conform with its economic and social policies. Transnational Corporations shall not intervene in the internal affairs of a host State. Every State should, with full regard for its sovereign right, cooperate with other States in the exercise of the right set forth in this subparagraph.¹⁸

It will be important to state that the forms of absolute sovereignty as seen in the opinion of Jean Bodin where the sovereign cannot be subject to any law is not totally applicable with regards to International Investment.¹⁹ Meanwhile, this is not to say that the State cannot prescribe the kind of foreign investment or bilateral agreements that comes within its territory, the proper thing is that once a state enters into an International Investment Agreement, the state must afford such level of permissible protection in accordance with the domestic laws regulating such investment, the BITs and IIAs which the state may have entered with the home state of such foreigner (usually some forms of diplomatic instrument based of reciprocal bilateral or multilateral obligations).²⁰

As noted by Al-Adba the state as a party to an investment agreement is in a position of some considerable power to impose conditions that suit its sovereign interests over and above commercial considerations.²¹ Such regulations may include domestic laws which lay down certain requirement, for instance, in Nigeria, foreign participation in any undertaking must be registered in accordance with the *Companies and Allied Matters Act*,²² and other extant laws regulating foreign participation in businesses. It is important to note that the difficulties that may be encountered by foreign investors in developing countries may arise from the stability of state macro-policies which may be in form legislative, economic, and political issues.

¹⁸ Ibid.

¹⁹ J Bodin, Op. cit, p. 35

²⁰ See for example, Article 2 (2), Preamble, Agreement between the Government of the Peoples' Republic of China and the Government of the Federal Republic of Nigeria for the Reciprocal Promotion and Protection of Investment (China-Nigeria, BIT).

²¹ Al-Adba N.M (2014), *The Limitation of State Sovereignty in Hosting Foreign Investments and The Role of Investor-State Arbitration to Rebalance the Investment Relationship* (Unpublished), a PhD Thesis Submitted to the University of Manchester, P. 59, available at <research.manchester.ac.uk/en/studentTheses/the-limitation-of-state-sovereignty-in-hosting-foreign-investment> last accessed on 22/2/2023.

²² Section 78, CAMA, 2020.



Terms of Resource-Backed Lending Model

One of the issues with most of the RBLs is that transparency is lacking in all stages of these deals, and all parties to them contribute to their opacity. Both development and commercial banks publish global lending aggregates on a regular basis. Unfortunately, they rarely make loan-level information such as interest rates, maturity, and resource-security arrangements available to the public. More often, specific RBL deals are mentioned in passing in official bank or company press releases that state only the total amount of the loan and offer vague references to resource-security. Meanwhile, it is glaring that the fundamental terms in most of the deals were that the creditor-state would have the right of exploration and to export certain natural resources belonging to the debtor-state. It is also clear that RBL deals are usually employed in the funding of capital-intensive infrastructural projects and the projects would usually be carried out by the creditor-state domestic companies. Thus, it creates a form of international investment where the debtor-states become the host state and the foreign investor (the foreign company executing the loan agreement from the creditor-state) is protected by the bilateral agreement between the host state and investor-state (creditor). At least, this is the situation with most of the RBLs involving China.

For instance, one of China's infrastructural development undertakings in Nigeria is the development of hydropower construction which is more of a foreign direct investment of Chinese Companies in Nigeria. It is seen that this infrastructure development deal is executed through a loan from China which Nigeria must as a precondition, award the project for which the loan is to be applied to Chinese companies.²³ This manifested in the September 2013 deal with two Chinese firms (China National Electrical Engineering Corporation and Sinohydro) to build the 700 MW Zungeru hydropower plant, this deal is the second major hydroelectric power project awarded to a Chinese firm by Nigeria.²⁴ The government approved funding for 25 percent of the project with the Export-Import Bank of China funding 75 percent via low-interest loans. The project is the largest power project in Africa to be funded with government concessional loans.²⁵ The same position existed between the loan agreement between China and Angola where the export revenue from 10, 000 barrels of oil a day over a period of 17 years would be used to repay the loan. In accordance with the loan agreement, 70% of public tenders for the infrastructure projects related to the deal was to be awarded to Chinese construction corporations²⁶.

Importantly, it will be stated that in the RBL deals, the creditor state will usually be concerned with recovery of its loan in the face of sovereign immunity of states. Since by general principle of international law, a state has immunity from being subjected to the jurisdiction of another state or from having execution levied against its property.²⁷ This principle is premised basically

²³ Available at <www.hydropower.org/country-profiles/nigeria> last accessed on 9/2/2023.

²⁴ Ibid.

²⁵ T. K Yuguda, S. A Imanche, T. Ze, T. Y Akintunde & B. S Luka, Op. Cit. P. 18.

²⁶ Ibid.

²⁷ See V.R Delmon, Sovereign Immunity, Summary and Sample Wording, PPP in Infrastructure Resource Centre for Contracts, Laws and Regulations, 2008, P. 1, available at www.worldbank.org/PPP. Last assessed on 2/12/2023.



on broad considerations of public policy, International law and comity as well as on the dignity, equality and independence of States rather than on any technical rules of law.²⁸

However, this principle can be eroded if the state itself consents to waive its sovereign immunity. This is to say that when a state enters into a contract with another state, the terms of the contract will be binding on the state despite its sovereign immunity. In the case of *Trendtex Trading v Central Bank of Nigeria*,²⁹ the Central Bank of Nigeria (CBN) attempted to rely on the principle of sovereign immunity to avoid the exercise of jurisdiction by the English court in a claim against the bank for payments due in respect of letters of credit issued. In dismissing the claim of sovereign immunity raised by the CBN, it was held inter alia that international law no longer recognize immunity from legal proceedings for a government department in respect of ordinary commercial transactions.

An instance where this principle had been eroded is Article 8(1) of the \$400 million Loan Agreement (“Loan Agreement”) executed by the Ministry of Finance on behalf of Nigeria and the Export –Import Bank of China for the Nigeria National Information and Communication Technology (ICT) Infrastructure Backbone Phase II Project in 2018. The said Article 8 (1) provides;

The borrower hereby irrevocably waives any immunity on the grounds of sovereign or otherwise for itself or its property in connection with any arbitration proceedings pursuant to Article 8(5), thereof with the enforcement of any arbitral award pursuant thereto, except for military assets and diplomatic assets³⁰.

One issue in Article 8 (1) above is that the assets in relation to which Nigeria waives its rights are only military and diplomatic assets, this means that the Republic of China may levy execution on every other asset belonging to Nigeria, this is a wide provision which leaves too much of the discretion to the lender (China) and capable of floating across Nigeria’s vast resources. From the understanding above, it may not be accurate to conclude that the Nigerian government used its sovereignty as a bargaining chip as that goes beyond the scope of a waiver of sovereign or jurisdictional immunity. However, it is clear that economic sovereignty is at stake from the provision above. More prominently is the fact that the African Development Bank and other international bodies have adjudged the Chinese loans to be non-transparent in relation to its terms and conditions³¹. Furthermore, Nigeria had plunged itself into a large indebtedness burden with China; the Debt Management Office (DMO) reports that as at March 31, 2020, the total borrowing by Nigeria from China was USD3.121 billion³².

²⁸ Ibid.

²⁹ (1977) 1 Q.B 529

³⁰ China-Nigeria Loan Agreement, 2018.

31 See ECOFIN Agency, Chinese loans to Africa increased sharply, but a large majority is not transparent (AfDB).

³² See <[FACTS ABOUT CHINESE LOANS TO NIGERIA - Debt Management Office Nigeria \(dmo.gov.ng\)](#)>, last accessed on 15/3/2023.



Most times, and from recent ordeals, the borrowers regret their choices. To cite just few examples³³, on June 25, 2018, *the New York Times* reported the fate of Hambantota, Sri Lanka. With the rate of Sri Lanka's debt ballooning under Mr Rajapaska, Hambantota port was handed over to the Chinese Government and 15, 000 acres of land around it for 99 years in December. Scary too is the 2006 loan to Tonga sought to rebuild infrastructure where from 2013 to 2014, the country suffered a debt crisis. The EXIM Bank of China, to whom the loans were owed, did not forgive them. The loans claimed 44% of Tonga's GDP.

In Zambia, the Chinese Government seeks control over Glencore's Zambian operation Mopani and the country's largest producer, First Quantum Minerals; the Chinese firms are seeking to capitalize on the liquidation of Konkola Copper mines, a subsidiary of London-based Vedanta Resources (Zambia is Africa's second-largest producer of copper). It would appear that the victims could not stop borrowing from China; sad as debt reliefs, renegotiation and restructuring proved abortive as China ever plays hardball.

The questionable motives of China in this RBLs should preach caution to the Governments of states that intend to engage in RBLs and it is to this end that Tillerson, the United States Secretary of State warns African countries against taking the terms of Chinese loans without proper consideration, describing China foreign policy as "debt trap diplomacy"³⁴.

CONCLUSION

Already, the resource-backed lending model which developed countries like China are operating in developing countries allows the developed states to enter the territories of the developing states and receive revenue since the resources of the developing states are staked as collaterals for the loans received by the developing states. This concept is already in operation in the relationship between China and some African countries, for instance, in 2021, China received 72 percent of Angola's oil as part of the repayment for the infrastructure loan advanced by China for the rebuilding of Angola. Also, the construction of railway in Congo via the infrastructure loan was the means by which China secured the mining lease in Congo. The classical situation is that of Zambia where much of the Zambian external debt is to China and the same is secured with copper exports which continues to create national tension in the sense of loss of control and sovereignty to China. This is definitely against the concept of sovereignty under the treaty of Westphalia.

³³ <https://www.google.com/amp/s/www.trtworld.com/africa/is-debt-trap-diplomacy-china-s-neocolonialist-tool-in-africa-27672/amp> (accessed 2/8/2023).

³⁴ See Premium Times Newspaper, 8th March, 2018, available at <www.premiumtimesng.com/newsheadlines> last accessed on 19/9/2023.