China’s Development Cooperation and Patient Capital at work

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April 6 2018
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Outline

I. China’s approach in South-South Cooperation: combining trade, aid and investment

II. China’s dev assistance in health

III. China utilizes Patient equity capital to finance Infrastructure and Private Sector

IV. Prospect of development finance

V. Risks and challenges

Drawing from our joint book on *Going Beyond Aid: Dev Cooperation for Structural Transformation* (Lin and Wang 2017) and a piece at Project Syndicate: A new approach for infrastructure finance, Lin, Halland and Wang: 
Our New Book

Going Beyond Aid
Development Cooperation for Structural Transformation

Cambridge University Press
I. China’s Approach in SSDC: trade, aid and investment

• China combines trade, aid and investment in South-South Dev Cooperation (SSDC)

• China’s aid is not “altruistic”. The government never considers aid as one sided “alms”, but something mutual.

• ... “Do what they know best”, following their comparative advantage in providing South-South Dev. Cooperation (SSDC)

• ”Teach fishing rather than giving fish”, following China’s own experience and building 6 Special Econ Zones in Africa.
China’s ODA: small, with huge potential

The Comparison of ODA as percentage of GNI and GNI per capita between China and OECD-DAC members, 2014

II. China’s dev assistance in health

1. Started to provide aid and dev cooperation since the 1950s.

2. Medical and health care is a major area where China directs its foreign aid.
   - In 1963, China dispatched the first medical team to Africa. Since then China sent 25,000 medical workers to 70 countries and treated 300 million patients.
   - Constructing medical facilities and equipment
   - Brightness trip activities: free eye surgeries
   - Preventive and control of infectious diseases
   - Combating Ebola and other epidemics (SCIO “white papers” 2011, 2014).

3. According to Aiddata.com, total grants in health between 2000-13 was 5.67 billion USD with 531 projects undertaken (Shajalal et al 2017)

3. In Africa, China targeted general health (313 projects), combating malaria (115 projects), and maternal, neonatal and child health (12 projects).

4. Most funding was targeted towards infrastructure and medicine (304 projects) followed by medical teams (189 projects). There is a significant relationship between aid to Africa and Chinese export to Africa. (Shajalal et al 2017)
Southern partners can use 3 Comparative Advantages

• Utilizing comparative advantage (CA, a trade concept) to help each other

• First, China has comparative advantages in building infrastructure: e.g. hydro-power, highways, and high-speed railways

• Second, China has comparative advantage (CA) in 45 out of 97 subsectors in trading goods

• Third, emerging economies have high savings and Patient Capital, which could be a comp advantage to be utilized: (elaborated below)
1. China has Comparative Advantage in Infrastructure and Scale Economy

Average Hourly Labor Cost in Construction, for Site foreman, PPP 2013

2. Declining RCA in China: Labor-intensive sectors have to relocate, creating millions of jobs elsewhere.

China: Revealed Comparative Advantage 1984-2013

III. Utilizing Patient Capital

• What is patient capital?

• “Patient capital”: those capitals to be invested in a “relationship” in which the stakeholder/partner is willing to take a stake in the host country’s development, aiming for a win-win. Countries with “Long Term Orientation” (Hofstede, 1990, 2010) are with “patient capital”.

• They are equity-like investors but willing to “sink” money in the real sector or unlisted projects for a long time—as long as 10 years and above.

• And they are willing and better able to take risks.

• **Net Foreign Asset** is positively and significantly associated with Long Term Orientation index. On the other hand, countries with Short Term Orientation and low savings rates would see their Net Foreign Asset positions deteriorating and their foreign debt mounting. (Lin and Wang 2017b)
Patient Capital (ultra-long term) from China and other EM

Source: Lin and Wang 2017b.
Patient capital 1: Net suppliers of FDI
Outflows minus inflows

Source: Lin and Wang 2017b. Calculated based on UNCTAD data.
2. China utilizes Patient Capital: Outward FDI (OFDI) from BRICKS

Outward Foreign Direct Investment Flows (2000-2016)
Source: UNCTAD Statistics on FDI

#1 China, 183.1
(World Rank #2)

#2 Russian Federation, 27.3

#2 Korea, Republic of, 27.3

#4 India, 5.1

#5 South Africa, 3.4

#6 Brazil, -12.4

Source: UNCTAD data. China’s OFDI reached $183 bn in 2016 surging up 44%.
Chinese Firms Creating Jobs Overseas

Huajian Shoes: A Quick Win in Ethiopia

• Former PM Meles Zenawi went to China in March 2011
• Huajian decided to make the investment in October 2011 and recruited 86 local workers to be trained in China.
• In 4 months, export started in March 2012. **Huajian became profitable in October 2012.**
• Huajian employed 3,500 workers by the end of 2013.
• **See McKinsey June 2017:** “**Millions jobs have been created by Chinese firms in Africa**”
New commitments by China

- China initiates the AIIB, The New Development Bank and the Silk Road Fund (SRF), and several other funds
- Set up a sustainable development fund of $2 billion at UN
- China has set up a $2 billion fund for South-South Cooperation.
- In the FOCAC meeting in South Africa, Xi committed to support Africa transformation by $60 billion dollars in three years, consisting, grants, no interest loans, concessional and non-concessional loans
- China has set up a industrial capacity cooperation fund with a $2 billion dollars
- The Belt and Road Initiative (BRI). How to finance it:
  - **Wide Consultation (共商)**;
  - **Joint Construction （共建）; and**
  - **Shared benefits （共享）。It is a platform for PPP co-investment**
New equity funds led by China

<table>
<thead>
<tr>
<th>Name</th>
<th>Established</th>
<th>Target Fund Size ($bn)</th>
<th>Chinese Investors</th>
<th>Other Investors</th>
</tr>
</thead>
<tbody>
<tr>
<td>China-Africa Development Fund</td>
<td>2007</td>
<td>10</td>
<td>China Development Bank (CDB)</td>
<td>–</td>
</tr>
<tr>
<td>China-ASEAN Investment Cooperation Fund</td>
<td>2013</td>
<td>10</td>
<td>China Export-Import Bank (EXIM)</td>
<td>–</td>
</tr>
<tr>
<td>China-Central and Eastern Europe Investment Cooperation Fund</td>
<td>2013</td>
<td>1</td>
<td>EXIM</td>
<td>Hungarian Export-Import Bank</td>
</tr>
<tr>
<td>Silk Road Fund (SRF)</td>
<td>2014</td>
<td>40</td>
<td>SAFE, CIC, EXIM, CDB</td>
<td>–</td>
</tr>
<tr>
<td>China-LAC Cooperation Fund (Private Equity Fund)</td>
<td>2015</td>
<td>3</td>
<td>EXIM</td>
<td>–</td>
</tr>
<tr>
<td>China-LAC Industrial Cooperation Investment Fund (CLAIFUND)</td>
<td>2015</td>
<td>10</td>
<td>SAFE, CDB</td>
<td>–</td>
</tr>
<tr>
<td>China-Africa Production Capacity Cooperation Fund</td>
<td>2016</td>
<td>10</td>
<td>SAFE, EXIM</td>
<td>–</td>
</tr>
<tr>
<td>China-Russia Regional Development Investment Fund</td>
<td>2017</td>
<td>15.4</td>
<td>15. National Development and Reform Commission (NDRC)</td>
<td>–</td>
</tr>
<tr>
<td><strong>TOTAL</strong></td>
<td><strong>99.4</strong></td>
<td><strong>99.4</strong></td>
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IV. Future Prospect in Dev Financing

- ODA (official development aid) will decline in relative importance in the next decades;
- But OOF and OOF-like loans will grow.
- MDBs accounts for only 1% of global inv on infrastructure (Dollar 2016). They need to better utilize “patient capital”
- Setting up more Multilateral Investment Banks/Strategic Investment Funds (SIFs)
- Expand the definitions of ODA, OOF, OOF-like loans (blended, like AIIB, CDB, EXIM bank), and OOF-like investments (Silk Road Fund, SIFs, and SWF, pension funds, other new funds). [patient/equity capital!]
- UNCTAD recognizes the roles of National Development Banks – and it is ahead of the curve. IFC new study on “leveraging” trillions for Green Dev, but far from it....
Expanding the definitions of development financing

There is a need to expand the definitions of development assistance to include ODA, OOF, OOF-like loans (blended, like AIIB, CDB, EXIM bank), and OOF-like investments (Equity investment, SWF, and Silk Road Fund)

- DF1=ODA
- DF2=DF1+OOF
- DF3=DF2+OOF-like loans
- DF4=DF3+OOF-like investment

Projection of Global Investment 2015-2030

TREND OF GLOBAL SHARES OF INVESTMENT

- Share of developed countries
- Share of developing countries without China
- Share of developing countries with China
More equity capital: What can be done by MDGs and DFIs

- To expand the pool of equity capital available for infrastructure investment. E.g. in October 2017, India’s National Investment and Infrastructure Fund (NIIF) announced a $1 billion deal with a unit of the Abu Dhabi Investment Authority. The agreement will help India finance critical infrastructure upgrades.

- Create more “Fund of Funds” for development.

- MDBs and DFIs can convert assets into “patient equity” by deploying capital through well-performing SIFs. They can 1) provide loans to help governments capitalize their strategic investment funds, 2) capitalize the SIFs directly, or 3) co-invest at the project level.
Patient capital could be 60% of...

Composition of External Financial Flows to Developing Economies, $1.4 Trillion in total, 2016

- Remittances, 28%
- Portfolio Inv, 9%
- ODA, 12%
- FDI, 45%
- Oth inv incl Bank Lending, 6%

In our view, 60% in total is estimated as “Patient Capital Flows”, about $850 bn in 2016.

V. Risk and Issues /challenges

• China’s SS cooperation is not transparent enough, and there is no “foreign aid law”...

• Issues arising on Risk and Debt Sustainability

• Issues on Environmental and Social Safeguards

• How to evaluate your developmental impact (M&E)

• Risks: losing strategic patience – rushing into investment decisions – 失去战略耐心，急功近利

• China will become the largest net creditor in the world. (Dollar 2016) How to deal with ”heavily indebted countries”, and potential default. What rules and conditions for restructuring debt?

• Newly established China International Development Cooperation Bureau. Will it improve transparency and coordination??? 5 Questions on its functions......
Conclusions

• MDBs need to 1) combine trade, aid, and investment like China does; and 2) Utilize Patient equity capital with long term orientation, suitable for enhancing global connectivity for global value chains.

• The WBG (IFC)’s new equity fund (InfraVentures) is a good way forward –to leverage private equity finance.

• China is moving to a new multilateralism with new banks and funds. China is learning to become “a responsible stakeholder” in global affairs by supporting FfD via the New Dev Bank and AIIB and SRF, and more SIF/funds

• The Belt & Road initiative is a platform for PPP co-investment, will create opportunities for all countries, It is a win-win-win multilateral initiative.
References:

• Lin, Justin Yifu, New Structural Economics, 2010.