
China's 21st Century Financial Foreign Policy

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The paper focuses on the main trends of China's financial foreign policy in early 21st century in the areas of foreign currency reserves accumulation, investing capitals abroad, participation in global economic and financial institutions, and yuan internationalization, as well as the policy transition under the impact of the 2008-2009 global financial and economic crisis.

China's growing financial power is one of essential factors of current global development. Especially 2008–2009 global financial and economic crisis promoted increasing China's influence in global finances.

Two main strategies of China's financial foreign policy, according to Ken Miller, include accumulating foreign currency reserves and investing money abroad in the form of direct foreign investments, aid, assistance, and loans [Miller 2010, 97]. The 2008-2009 global financial crisis and post-crisis development contributed to some essential updating the strategy. Simultaneously there is a gradual but visible shift in the wake of the crisis in two other directions: increasing China's influence in global financial institutions and yuan internationalization.

During the global financial and economic crisis China as well as other East Asian nations to a large degree escaped financial turmoil, but it was affected by a sharp fall in its main export markets – the EU and the U.S. While being the main global producer and exporter in early 21st century, since 2008 China has become a leading global creditor and investor.

In 2008 China replaced Japan as the main U.S. creditor. In May 2011 Chinese government possessed 36 percent of U.S. Treasury securities and 16 percent of total U.S. public debt. In August 2011 it amounted \$1 trillion. Such outcome deepens U.S.-China financial interdependency and creates huge potential risks for U.S. and global economy if Chinese banks stop buying U.S. Treasury securities or start selling them in quantity. Similarly American dollar depreciating means huge losses for China's dollar-denominated currency reserves. Financial crises in euro-zone have the same negative impact on euro-denominated Chinese reserves. According to Central Bank of China information, in September 2011 in spite of significant decrease of China's foreign currency reserves in \$60,8 billion they totaled \$3201,7 billion [Транснациональное прямое инвестирование...2011]. Chinese government is forced to search safer ways to protect its foreign currency reserves and to get out of “a dollar trap” it was caught in. The most visible way out is seen in increasing Chinese investments abroad. Some experts argue China should adjust its macroeconomic policy and reject the policies leading to farther foreign currency reserves accumulation [Is it the time for China...2011].

Compared to early stages of China's financial foreign policy when preferred investment areas included foreign governments obligations and gold, a shift to foreign direct investments (FDI), grants, aid and concessional loans, mostly to the governments of Global South nations for certain projects, has occurred since early 21st century. Unlike the U.S. China has given aid to developing nations without any conditions regarding their political systems, domestic policy, human rights and democracy issues. Typical Chinese foreign investment project can combine FDI of state enterprises and concessional governmental loans on favorable terms and Chinese companies' participation in the project realization. FDI of private Chinese companies are not large so far and they also require public approval.

Although China's foreign direct investment policy is a quite recent phenomenon its several stages are visible: 1) late 1980s – late 1990s; 2) early 2000s; 3) since 2008-2009 global financial and economic crisis till now.

Chinese foreign direct investment policy started in late 1980s –1990s with the target to ensure markets for Chinese goods and to provide access to scarce natural resources. It was a time when Chinese public sector was under reconstruction and private one was too weak for significant investments. The major China's foreign investment destination was Hong Kong. In 1980s Chinese companies also tried to establish joint ventures in the Caribbean, especially in textile sector to penetrate into American market. Some investments went to natural resources in Latin America, Africa, Asia - iron ore and oil in Peru (1992-1993), oil in Sudan (1995) etc. With a significant shift in China's regional policy and joining regional groupings since 1996 some important financial initiatives were signed within the frameworks, the first large-scale contracts were reached. Among them \$4, 3 billion China's National Oil Corporation investments into Kazakhstan's oil sector and \$3 billion into Caspian Sea – Xinjiang pipeline construction (1997) [China and the Developing World 2007, 70].

“Going out” strategy was announced in October 2000 in the 10th five-year plan documents. Its realization was accelerated after China joined World Trade Organization (WTO) in December 2001. The first large contracts were signed by Chinese oil companies to explore, produce, and refine oil as well as develop infrastructure in the Middle East (in pre-war Iraq, Iran, Oman) and North Africa (Algeria). After Chinese top leaders visited several African countries and China hosted the first China-Africa business conference in 2003 the country has been involved to much more energy projects in Africa. The fact that China entered global energy market much later than Western nations limited its investment opportunities. So it tried to penetrate to niches not occupied by Western companies, and enter “problem zones” too risky for Western companies with investment and aid packages. For example, after a civil war in Angola in 2002 Beijing granted Angolan government a \$3 billion loan to develop its oil sector and reconstruct its ruined infrastructure. In 2006 Angola was the second oil producer in Sub-Saharan Africa (after Nigeria) and one of China's leading suppliers [Jiang 2006, 7].

A noticeable expansion of China's foreign investments occurred in 2005-2007. Chinese economy needed more and more resources; China's foreign exchange reserves essentially increased; public enterprises recovery enabled their investments abroad. Numerous visits of China's top leaders to African, Latin American, and Asian countries led to large-scaled investment contracts. According to UNCTAD statistics, in 2005 China's outward investments totaled \$12, 3 billion (compared to \$916 million in 2000 and \$ 5, 5 billion in 2004), in 2006 – \$21, 2 billion, in 2007 - \$22, 5 billion [UNCTAD Handbook of Statistics 2009, 367].

Investments into Africa have essentially increased since 2006, called the “year of Africa” in China. This year the first top level FOCAS (Forum of Chinese-African Cooperation, established in 2000) summit gathered in Beijing more than 40 African leaders. Chinese companies had a peculiar interest in energy, mineral resources, telecommunication, and construction sectors. Some large-scaled contracts were signed in oil sector of Libya, Nigeria, Kenya, Angola, and Sudan. While Western nations imposed sanctions against Sudan's regime because of humanitarian or other reasons, China became its largest investor. In 2007 Sudan was the 6th largest China's oil supplier behind Saudi Arabia, Angola, Iran, Russia and Oman. Among the largest infrastructural investments into Africa there was an \$8 billion contract for 20-years period with Nigeria to reconstruct its railways, signed in 2006.

Significant bilateral investment agreements in mineral resources, energy and infrastructure projects were signed with Latin American nations: Argentina, Brazil, Chili, Cuba, etc. The most noticeable Chinese investments flew to oil sector of Venezuela. The cumulative stock of Chinese FDI in Latin America and the Caribbean rose from \$4.6 billion in 2003 to \$11.5 billion in 2005, accounting respectively for almost 14 and 20 percent of China's FDI stock worldwide, though Chinese outward FDI had not been as significant as China's trade flows. At the end of 2006 China's cumulative stock of FDI worldwide amounted to \$73.3 billion, just 0.58% of global FDI stock. Besides, it was noticed that the overwhelming majority of Chinese FDI to Latin America and the Caribbean (almost 96 percent in 2005) went to the Cayman Islands, the British Virgin Islands, and Bermuda, known as tax havens. These three nations were also the major sources of FDI into China, that confirmed the Chinese investors' intention to bring the capital back as FDI to take advantage of preferences given to foreign firms [China's Foreign Policy and "soft power" 2008, 35-36].

The efforts of Chinese companies to gain significant assets in developed countries visible since 2005 often met serious obstacles. For example, the China National Offshore Oil Corporation's (CNOOC) attempt to acquire the California-based Unocal in 2005 failed because of the rise of xenophobia in the U.S. A friendly purchase of American IBM's personal-computer business by Chinese computer producer Lenovo in 2005 (\$ 1, 8 billion deal) was an exception.

Though outward China's investments were still insignificant compared to inward investments to Chinese economy (in 2005 respectively \$12, 3 billion and \$72, 4 billion) even limited Chinese capital had impressive political effect. For example, the alternative created by Chinese investments in Latin America to the U.S. economic ties encouraged Venezuela and MERSOCUR nations to fail the Free Trade Area of the Americas (FTAA) with the U.S. in November 2005.

"Going out" strategy was specified at the 17th CPC Congress in October 2007. Large national corporations were encouraged to turn into multinationals while buying well known brands, pursuing mergers and acquisitions. To promote dynamic public and private outward foreign investments Chinese government established in 2007 a sovereign wealth fund China Investment Corporation (CIC) with initial capitalization of \$200 billion.

A great opportunity to gain assets worldwide appeared during the 2008-2009 global financial and economic crisis. Before the crisis China invested mostly in developing and emerging countries with loans, grants, and aid, combined with FDI, now lack of liquidity in developed countries formed their strong demand for China's capitals, including FDI.

It was a noticeable growth of China's outward FDI in 2008 – \$52, 1 billion (compared to \$ 22, 5 billion in 2007). In 2009 it fell to \$ 48 billion as Chinese government was focused on large-scaled investment into domestic economy. According to Chinese sources, multinationals mergers and acquisitions composed 34 percent of all China's outward FDI in 2009. Among them a significant property gained by CIC and its branch Stable Investment Corp. in the staggering U.S. financial sector (Morgan Stanley, Blackstone Group LP, Reserve Primary Fund) in 2008–2009, which was a new trend in Chinese foreign investment policy. By the end of 2009 12 000 Chinese investors had founded 13 000 enterprises with assets exceeded \$ 1 trillion in 177 countries and regions worldwide. 2009 U.N. global investment report ranked two Chinese companies among top 100 global multinationals, and ten – among top 100 developing nations multinationals [Потенциал развития инвестиций за рубежом...2010].

Some new specified features of China's foreign financial policy are noticeable in the post-crisis recovery period. China's government March 2010 report guarantee more support and autonomy to qualified companies in pursuing mergers and acquisitions abroad. With exception of very large or political sensitive projects which still have to be approved in Beijing, other projects get permit at a local level within one-two months. The specified areas of investment interest include natural resources production and processing, high-tech industry, green energy, well-known brands etc. As a result China's FDI in the first half of 2010 reached \$55, 2 billion. At the end of 2010 China was the fifth largest world investor.

According to regional-based analyses of outward Chinese foreign investments (summer 2010) Africa gained a lead (\$62, 2 billion), the 2nd place went to North America (\$59 billion), the 3rd one - to Australia (\$58, 5 billion), the 4th - to Europe (\$53, 1 billion), the 5th - to Middle East (\$49, 5 billion), the 6th - to Asia (\$44, 9 billion), the 7th - to Latin America (\$19, 2 billion), and the last one - to Russia and Ukraine (\$8,4 billion) [Money can buy love 2010, 101].

In Asia favorable conditions for China's outward investments have been created by the China-ASEAN Free Trade Area since January 2010. China's FDI into Japan are increasing as well, especially in the wake of March 2011 earthquake. In 2010 they amounted to \$200 million, compared to Japan's \$4 billion into China. In the first seven months of 2011 China's investment in Japan, including mergers and acquisitions, soared to \$570 million. Number of Chinese companies invested in Japan reached 661 by July 2011, compared to 233 in 2006. According to Jia Qingguo, associate dean of Peking University's School of International Studies, it's explained by a very attractive buying price for Chinese bidders and a mutual benefit. So the Japanese enterprises get the money they need and a convenient way to enter the Chinese market, and Chinese companies gain brands, technologies and distribution channels [Building on common ground for Asian era 2011].

Investments into the U.S. have grown as well. Though its amount is still relatively insignificant, there is a huge progress compared to previous years. Obama's administration is concerned about a drastic fall of the U.S. share of global FDI over the last decade from more than 40 percent to 17 percent, as well as 11 percent fall of FDI inflows into the U.S. in the first six months of 2011, compared to the first half of 2010. In June 2011 President Obama signed an executive order to create SelectUSA, a branch attached to the Commerce Department, as the first-ever government-wide initiative to attract and retain the U.S. business investments. Chinese FDI are highly welcomed [U.S. vows to attract foreign direct investment 2011].

China's annual investments into Ukraine before the global crisis were about \$11 million, compared to \$ 500 million into the U.S. Ukraine's demand for investments, especially for Euro-2012 infrastructure reconstruction, was one of the main topics of Ukrainian-Chinese talks during the President Yanukovich's visit to China in September 2010. As provided by 13 bilateral agreements signed during the visit Ukraine expects to get \$11-15 billion of Chinese investments annually during next 5-7 years in the fields of energy, shipbuilding, ports and roads infrastructure development, and other infrastructural projects. The main outcome of Hu Jintao's visit to Ukraine in June 2011 was the establishment of bilateral strategic relations between China and Ukraine. Financial issues were discusses as well, mostly developed projects to the amount of \$3, 5 billion, and loans [В Україну прийдуть...2010; Гаврилечко 2011].

Huge domestic investments in 2008-2010 (4 trillion yuan or \$ 586 billion, about 13 percent of GDP) as a response to the global crisis coursed some negative trends

in China's economy (growing inflation, "bad credits" problem, etc.) and urged to accelerate transition to a new "scientific" development model. Balancing of inward and outward investments, GDP and GNP as well as a shift in the foreign trade through increasing export with the help of investments abroad is among the main targets of the 12th five-year plan (2011–2015).

Foreign investment policy gives China mighty tools to solve important domestic problems, stimulates economic growth and job creation, secures its access to energy and mineral resources, technologies and leading financial institutions, serves the goal of China's unification. Simultaneously Chinese capitals flow to developing and emerging nations helps to correct imbalances between Global North and South. Most of Chinese investments are not expected for fast return, so they promote China's "soft power" and contribute considerably to the strategic China's target of a new multipolar political and economic world order construction.

China's participation in the G20, a group of twenty major economies, serves the target as well. The G20 creates a framework for multilateral discussion of financial and economic issues, making major developed and developing nations equal partners in sharing their views on global development. The reform of the International Monetary Fund and the World Bank is on the agenda. Increase of developing and emerging nations' quota in the global financial institutions, promoted by BRICS nations, will strengthen China's power in the global finances, considering its position as a global creditor and investor as well as its image as a leader of developing and emerging nations.

After the head of the People's Bank of China called in March 2009 for the end of using American dollar as the world's reserve currency in the favor of a new currency to be created by the IMF, worldwide discussions about yuan internationalization prospects has been intensified. Experts agree that China's currency internationalization will both strengthen its international financial power and challenge its economy, so it's going to be a gradual and incremental process.

The global crisis and post-crisis development (the EU debt crisis, the U.S. and Japan credit rating drop) accelerated the process. In 2009 Chinese government allowed some economies (Hong Kong, Macao and ASEAN) to use yuan to pay for Chinese import as well as five cities in China to pay for imports into China. In 2011 it was decided to spread the experience on all parts of China, all countries and regions. According to the Central Bank of China statistics, yuan employment in foreign trade increased in the first half of 2011 to 957, 57 billion yuan (about \$149, 62 billion), in 13.3 times compared to the similar period in 2010. China and ASEAN are working on an agreement to use yuan in bilateral trade (supposed to be signed in late 2011 – early 2012) [Work underway on China-ASEAN yuan trade settlement agreement]. Another important shift in the renminbi internationalization is connected with the authorization to use it in foreign investments in China, except financial sector [Транснациональное прямое инвестирование... 2011].

China's financial policy dynamics and trends confirm a new China's global role in the 21st century and a significant shift in the wake of the global 2008–2009 crisis to multipolar economic and political world order, promoted by China.

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