DEMOCRACY AND SOCIETY 18.12.2020 | Kevin P. Gallagher & Rebecca Ray

China takes the lead in development finance

China has provided developing countries extra resources they had long sought from the West. But its lending has to become more sustainable

China has provided many developing countries the additional resources they had long sought from the West. If Chinese lenders align this funding with efforts to ensure financial and environmental sustainability, the world would stand a much better chance of achieving a green and inclusive recovery from the Covid-19 crisis.

According to new estimates, China now finances overseas development at nearly the same level as the World Bank. With countries currently struggling to combat Covid-19, protect the vulnerable, and mount a green and inclusive recovery, this significant increase in global development funding could potentially bring major benefits to the world economy.

But, like any huge influx of capital into the developing world, China's financial assistance also poses large risks – especially regarding debt distress, biodiversity loss, and climate change.

A new interactive dataset from Boston University's Global Development Policy Center tracks the overseas sovereign loan commitments of China's two global policy banks – China Development Bank and the Export-Import Bank of China. Between 2008 and 2019, China's global development finance totalled USD 462bn, just USD 5bn short of the World Bank's sovereign commitments in the same period.

Is China's development finance leading to debt traps?

China's development finance is highly concentrated in infrastructure – a sector with strong potential for spurring economic growth – as well as extractive sectors. The World Bank estimates that China's overseas

investments could lead to an increase in global real income of up to 2.9 per cent by 2030, with recipient economies experiencing real income gains of up to 3.4 per cent. In contrast, researchers using similar modelling techniques estimated in 2016 that the Trans-Pacific Partnership (TPP) trade pact would boost growth in its member countries by just 1.1 per cent by 2030, and globally by 0.4 per cent.

Chinese development finance also poses risks to biodiversity and climate stability.

Moreover, forthcoming research in the *American Economic Journal* shows that each Chinese-financed project has yielded a 0.41-1.49 percentage-point increase in economic growth. The same study found no robust evidence that World Bank projects promoted growth.

But the increase in Chinese development finance has raised concerns about possible debt distress in recipient countries. Although this financing spans the world, 60 per cent of it to date has gone to just ten countries: Venezuela, Pakistan, Russia, Brazil, Angola, Ecuador, Argentina, Indonesia, Iran, and Turkmenistan. Several may now struggle with repayment obligations.

Earlier this year, the G20 established the Debt Service Suspension Initiative (DSSI), which suspended bilateral official loan repayments for 73 of the world's poorest countries through mid-2021 as they struggle to tackle the pandemic and the associated economic crisis. According to the World Bank's DSSI database, debt service owed to China through 2021 is similar to the debts owed to the World Bank and all multilateral creditors combined.

The climate impact of China's development efforts

Chinese development finance also poses risks to biodiversity and climate stability. The new Boston University dataset locates each Chinese-financed project by its longitude and latitude, allowing users to pinpoint their proximity to sensitive regions from the standpoint of biodiversity. Of the 615 projects mapped there, 124 are in national protected areas and 261 are within critical habitats.

Moreover, in a recent article co-authored with Princeton University scientists, we found that between 2006 and 2015, public lending by China's two policy banks financed more additional power-generation capacity globally (59 gigawatts) than the ten largest multilateral

development banks combined (55 GW). Although this Chinese lending helped to increase global energy capacity, 64 per cent of those plants were in the carbon-intensive coal sector and will emit more than 12 gigatons of carbon dioxide over their lifetimes.

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China, its debtors and the international community need to maximise the benefits and minimize the risks of this much-needed global development finance. Over the course of 2021, China will have three major opportunities to spearhead this effort.

Within the G20, China is already the largest participant in the DSSI, having so far suspended over $1.9 billion in debt service. At their November summit, G20 leaders adopted a framework that goes beyond debt suspension and could provide real debt relief for poorer countries. China could take the lead and require that countries benefiting from debt relief use their newfound fiscal space to advance green development goals.

China can lead the way

In May 2021, China will host the Conference of the Parties to the Convention on Biological Diversity, and could pledge to align its overseas development finance with the new global biodiversity goals. This is a principal recommendation made by a body sponsored by the Chinese Ministry of Ecology and the Environment, and it would build on China's domestic biodiversity-protection efforts.

Finally, at the United Nations' COP 26 climate-change summit in Glasgow in November, China could promise to extend its recently announced pledge to become carbon neutral by 2060 to its overseas development financing. China is already a global leader in financing and diffusing solar and wind power domestically; by reorienting its development finance, it could rapidly spread these technologies around the world.

China has led the way in providing developing countries with the additional resources that they had long sought from the West. If Chinese lenders manage to align this funding with efforts to ensure financial and environmental sustainability, the world would stand a much better chance of achieving a green and inclusive recovery from the Covid-19 crisis.



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