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WORKING GROUP ON DEVELOPMENT AND ENVIRONMENT IN THE AMERICAS

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This China-Latin America Economic Bulletin is the third annual note summarizing and synthesizing trends in the burgeoning China-Latin America economic relationship. The goal of the bulletin is to provide analysts and observers handy reference to the ever-changing landscape of China-Latin America economic relations, a landscape where data is not always as readily accessible. Highlights from this year's edition include:

- LAC's trade deficit with China stayed relatively constant in 2015, at 0.6 percent of regional GDP. Behind this unchanged level are increasing volumes of major commodities coupled with falling prices. In effect, LAC spent 2015 spinning its wheels in its exports to China.

- Chinese lending to LAC leapt upward in 2015, to $29.1 billion: more than the World Bank, the Inter-American Development Bank, and the Latin American Development Bank combined. China has emerged as an important source of counter-cyclical finance during economic slumps in LAC, both in the recent financial crisis and now in 2015. What is more, China has established $35 billion in new regional funds with Latin America in infrastructure and industrial development.

- Chinese overseas investment continued to be concentrated in primary materials in 2015. Over the last five years, three-fourths of Chinese mergers and acquisitions in the region were in extractive industries (oil, natural gas, and mining), while three-fourths of other countries' mergers and acquisitions in the region were in services. In new "greenfield" FDI projects, 18 percent of Chinese investment was in agriculture, compared to just two percent of other greenfield investment in the region.

- Movement continued on major Chinese investment and financing projects initiated during the 2015 China-CELAC summit. Feasibility studies began for the Twin Ocean Railway, linking Peru and Brazil, and the *Capital de las Ciencias* industrial park in Mexico. Also, the Nicaragua Canal's environmental impact assessment was published, but met with significant criticism by an independent panel of experts and the Nicaraguan public.

Major Trends in Trade, Finance, and Investment

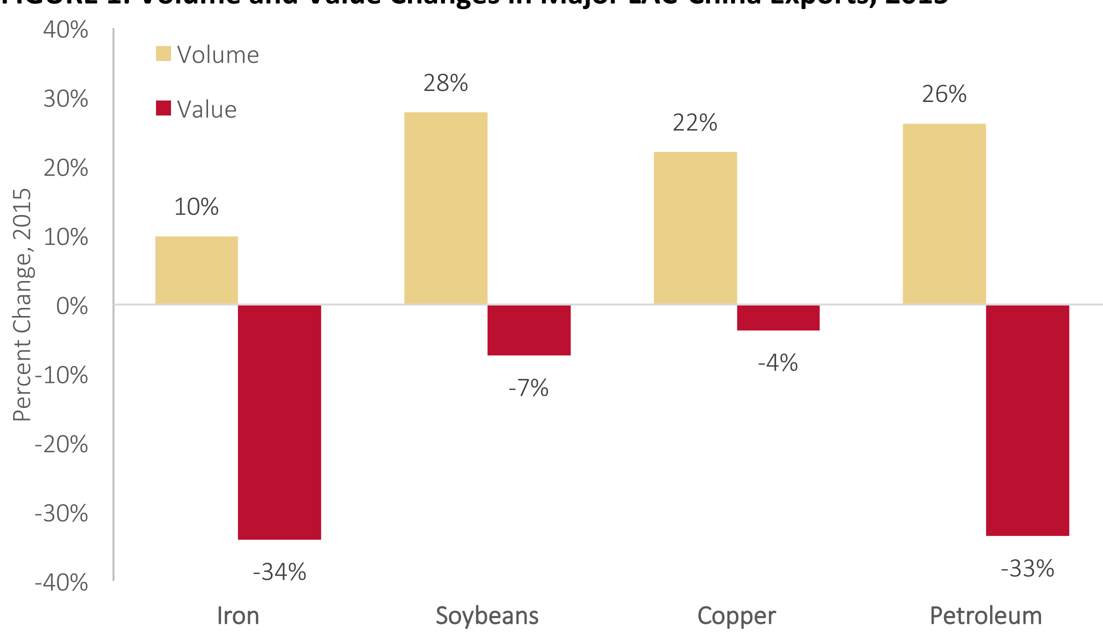
In 2015, LAC exported $109 billion USD in merchandise to China, and imported $139 billion in goods in return: nearly unchanged from 2014. But Chinese lending to LAC rose dramatically in 2015, reaching $29 billion USD: more than the World Bank and Inter-American Development Bank combined. Chinese FDI fell from $10.2 to $4.6 billion USD in new FDI projects ("greenfield" FDI, or GFDI) and $49.9 million USD in mergers and acquisitions (M&As) in LAC.

LAC Trade with China

In 2015, preliminary estimates indicate that LAC trade with China stayed nearly constant in absolute terms: the region exported approximately $109 billion USD to China (up from $108.5 billion in 2014) and imported $139 billion USD from China (down from $143 billion in 2014. LAC's resulting trade deficit also remained constant, at 0.6 percent of regional GDP.

Behind these constant levels were rising quantities and falling prices, which also brought a slump in regional GDP. LAC was essentially spinning its wheels with its exports to China in 2015: the volume of LAC's most important exports to China continued to grow, while the value of those exports fell, as Figure 1 shows.

FIGURE 1: Volume and Value Changes in Major LAC-China Exports, 2015



Source: Authors' calculations using China Customs Information Center and UN Comtrade data.

Together, these four commodities – iron, soybeans, copper, and petroleum – account for over half of all LAC-China exports in recent years. In fact, LAC exports to China have consistently been highly concentrated, with over two-thirds of exports concentrated in just five commodities over the last five years of available data, as Table 1 shows.

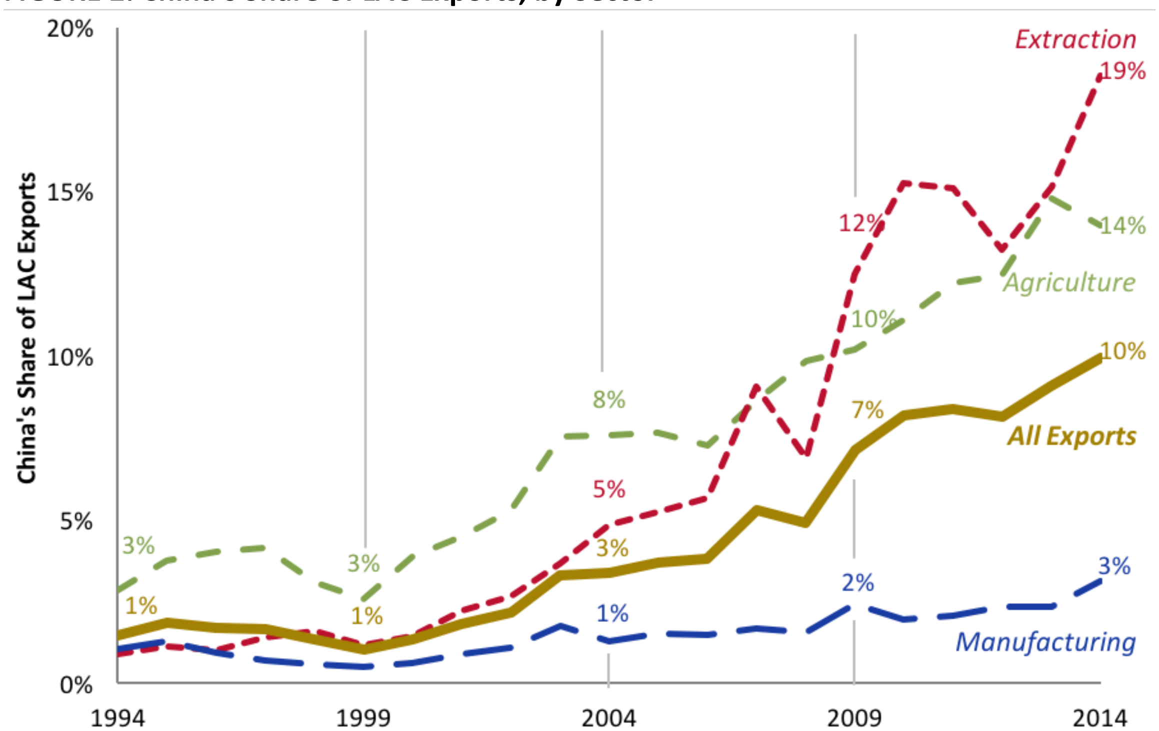
TABLE 1: Top 5 Imports and Exports, 2010-2014

LAC Exports to China		*LAC Imports from China*	
1. Iron ores, concentrates	19.0%	Telecom equipment	9.7%
2. Soy, other oilseeds	18.0%	Data processing machines	3.8%
3. Copper	12.2%	Ships, boats, floating structures	3.3%
4. Unrefined petroleum	11.0%	Optical instruments, apparatus	3.3%
5. Copper ores, concentrates	9.6%	Petroleum products, refined	2.3%
Total, top 5	69.7%	Total, top 5	22.5%

Source: UN Comtrade.

China continues to grow as an export market for LAC, especially for primary goods. Figure 2 shows China's rising importance by export sector. In 2014, the last year of available data, China purchased 10 percent of the region's overall exports, but 14 percent of agricultural exports and 19 percent of extractive exports. LAC has had relatively little success in marketing its manufactured goods to China, however: China purchased just three percent of these exports in 2014.

FIGURE 2: China's Share of LAC Exports, by Sector

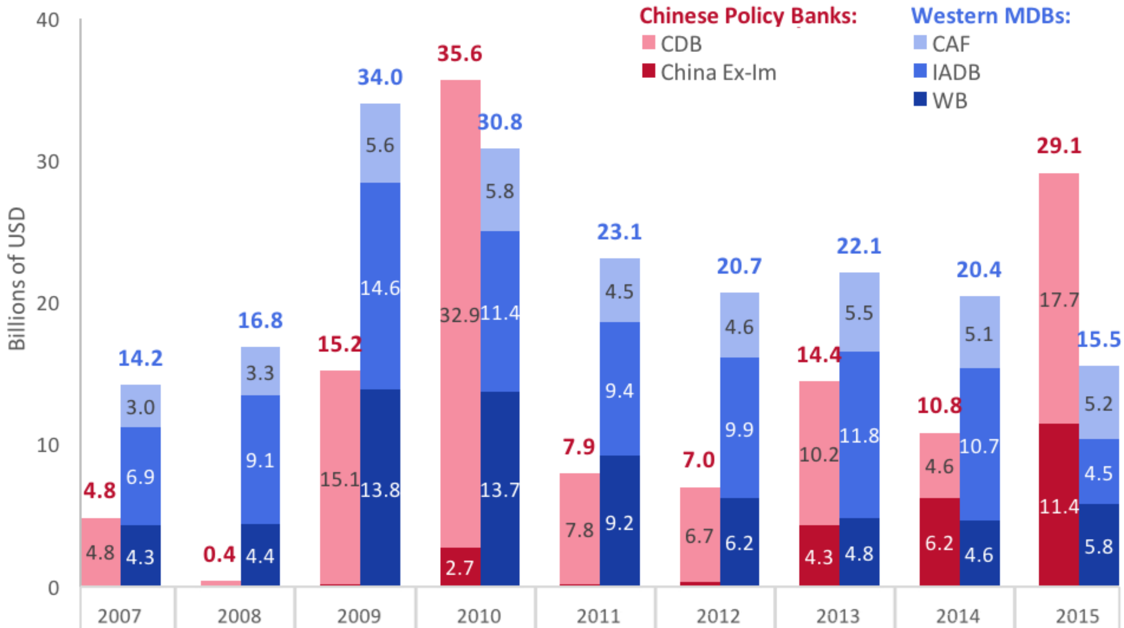


Source: UN Comtrade.

Chinese Lending to LAC

Chinese lending to LAC countries leapt upward in 2015, reaching $29 billion USD: nearly twice as much as the combined totals of all of the Western multilateral development banks (MDBs), including the World Bank (WB), the Inter-American Development Bank (IADB), and the Latin American Development Bank (CAF). In contrast, Western MDB financing has gradually declining over the last several years.

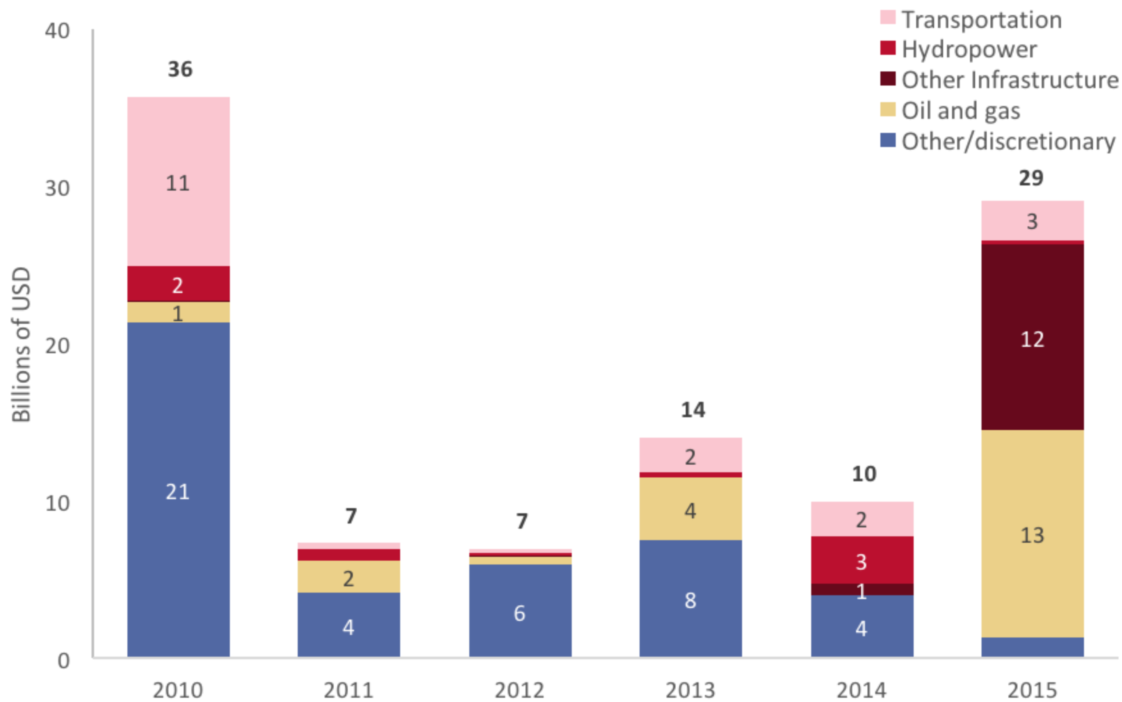
FIGURE 3: Sovereign Lending to LAC, by Source



Source: Gallagher and Myers (2016), Myers et al (2016).
Note: CAF lending for 2015 is a preliminary estimate. CDB refers to the China Development Bank and China Ex-Im refers to the Export-Import Bank of China. Other acronyms are explained in the text.

China has emerged as an important source of counter-cyclical finance during times of regional economic contraction. Over the last decade, Chinese lending to LAC peaked in the two years of faltering regional GDP: 2010 and 2015.

FIGURE 4: Chinese Sovereign Lending to LAC, by Sector



Source: Gallagher and Myers (2016), Myers et al (2016).

In 2010, China lent LAC $35.6 billion USD, most of which was discretionary. In contrast, last year China steered completely away from discretionary lending and channeled its loans into two main sectors: infrastructure and hydrocarbons.

This increase in single-sector lending is likely to continue over the upcoming years, as part of the 2015 China- Community of Latin America and Caribbean States (CELAC) summit agreements. New projects currently undergoing feasibility studies include the Capital de las Ciencias industrial park in the state of Jalisco, Mexico and the twin-ocean railway, connecting Peru, Brazil, and possibly Bolivia.

Another important new development in 2015 was China's announcement of new regional financial platforms. Three funds promise $35 billion in credit for industrial cooperation, infrastructure, and other projects in the region. The China-LAC Industrial Cooperation Investment Fund ($10 billion for phase one) and the Special Loan Program for China-LAC Infrastructure Projects ($20 billion) come from China's State Administration of Foreign Exchange (SAFE) and is administered by CDB. In 2015, China also announced $5 billion in association with the already established China-LAC Cooperation Fund. The China-LAC Cooperation Fund may also be part of the IDB-China Co-Financing Fund for the Latin America and Caribbean Region and a still-pending IDB-Eximbank private equity fund. These funds show a new wave of Chinese finance in LAC into infrastructure and industry.

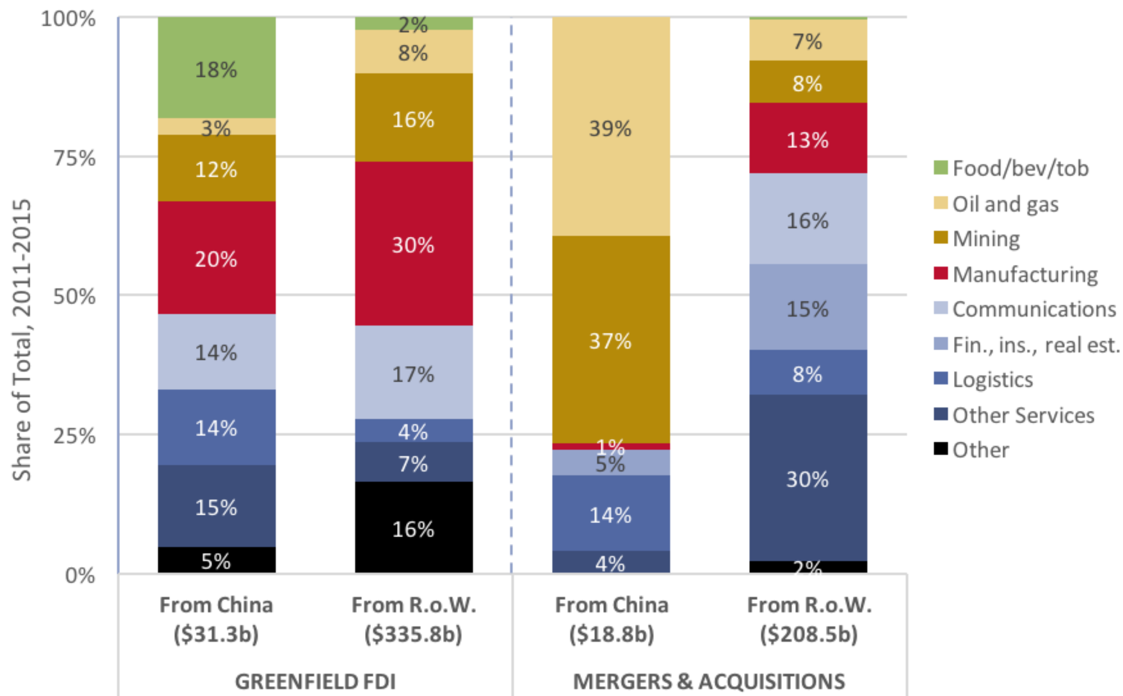
Chinese Investment in LAC

In 2015, China invested $4.6 billion USD in new FDI projects ("greenfield" FDI, or GFDI) and $49.9 million USD in mergers and acquisitions (M&As) in LAC. China is now the second largest source of GFDI projects behind the United States, and the third largest source of FDI through M&As behind the United States and Spain.

In each kind of FDI, Chinese investment is more heavily tilted toward primary sectors than other investment. Among GFDI projects, 18 percent of Chinese investment is channeled into agriculture, compared to just two percent of other GFDI. In its place, other countries invest more in LAC manufacturing, which takes up 30% of total GFDI from countries other than China compared to just 20% of GFDI from China.

Among M&A deals, roughly three-fourths of Chinese investment over the last five years was concentrated in extraction: oil, natural gas, and mining. This stands in stark contrast with other M&A investment in LAC, nearly three-fourths of which has been channeled into services.

FIGURE 5: Sector distribution, FDI into LAC



Source: Authors' calculations based on Financial Times (No Date) and Bureau Van Dijk (No Date) data.
Note: Mergers and acquisitions include only completed deals worth at least $10 million USD.

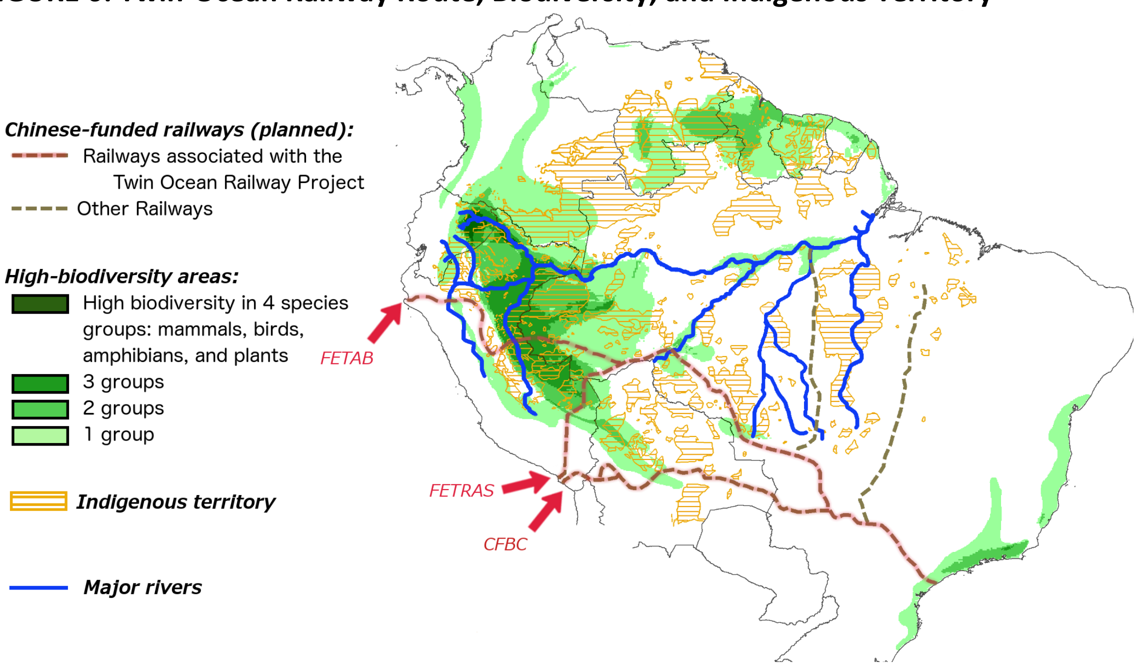
2016 and Beyond: Major Financing and Investment Projects

Looking forward, 2016 is likely to see further development in the first wave of investment projects since the 2015 China-CELAC Summit. Three major projects in particular are discussed below: the Twin Ocean Railway, the Nicaragua Canal, and the Capital de las Ciencias industrial park in Mexico.

Twin Ocean Railway

This past year saw further progress with the proposed Twin Ocean Railway connecting Peru, Brazil, and possibly Bolivia. In May 2015, Chinese premier Li Keqiang visited Lima and announced that a feasibility study would be ready one year later (Rosales Ferreyros 2015). In February 2016, Brazilian lawmakers met with a delegation of Chinese firms interested in participating in the project, and announced that study details would be shared in public meetings along the planned route (Bland 2016).

FIGURE 6: Twin-Ocean Railway Route, Biodiversity, and Indigenous Territory



Source: Ray et al. (2015). Note: potential Twin Ocean Railway routes are highlighted in red. High biodiversity is defined as the top 6.4% of South American land area for species richness. Indigenous territory includes lands with and without official state recognition.

Press reports have stated that the Peruvian route is still undefined, with two potential routes: *FETAB*, through northern Peru and *FETRAS*, through the south of the country ("Empresas chinas" 2014, "Los Intentos de Europa" 2016). Nonetheless, Peruvian President Ollanta Humala has announced a preference for the former route, through "northern Peru, for reasons of national interest" ("Los intentos de Europa" 2016). This choice is highly significant for the potential environmental and social implications of the project, as well as the domestic resistance it may face: the northern route transverses several indigenous territories as well as a highly biodiverse section of the Amazon. The southern route, in contrast, avoids these risks. Ultimately, the choice of route will rest with the next Peruvian president (to be elected in April 2016), and may make the difference between a smooth rollout and a rocky one.

Bolivia has continued to press for inclusion in the route, through a separate spur connecting to the main route in southern Brazil and to the Pacific Ocean in the port of Ilo, Peru. A Chinese delegation is due to visit Bolivia in the spring of 2016 to discuss this Corredor Ferroviario Bioceánico Central (*CFBC*) in more detail (Lazcano 2016).

Brazilian president Dilma Rousseff has shown willingness to study the possibility, noting the importance of facilitating imports of Bolivian natural gas into Bolivia ("Rousseff Open" 2016). Notably, as shown in Figure 6, the potential Bolivian addition avoids sensitive territory, and may face more local acceptance than the Peruvian section of the Twin Ocean Railway, especially if the final route follows FETAB rather than FETRAS.

Nicaragua Canal

Last year's bulletin discussed the Nicaragua Canal, which was announced in 2013 and which began its community consultation work in 2014. HKND, the firm directing the project, published preliminary archeological results in March of 2016, and indicated that further archeological work would continue in the coming months (HKND, 2016).

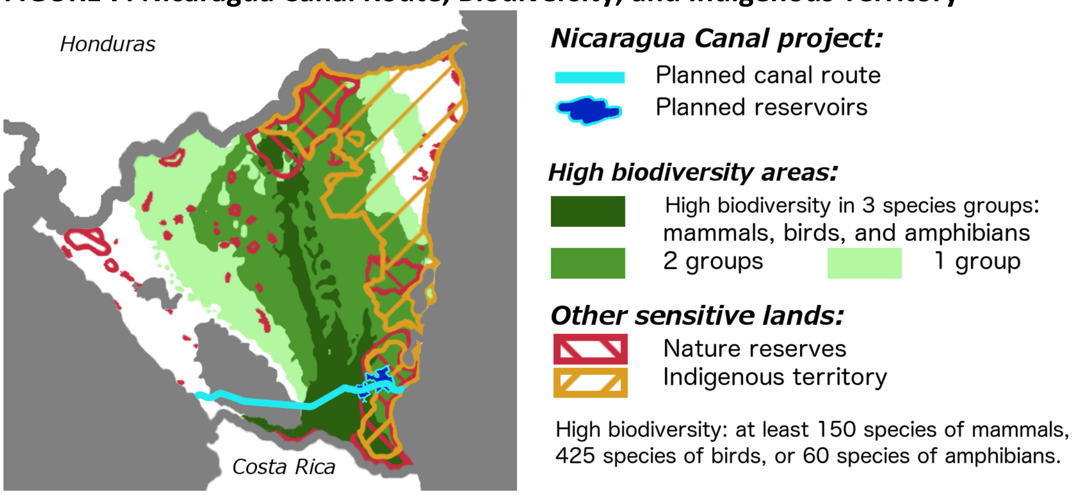
Nonetheless, the project has faced important obstacles that may endanger its future advancement. Wang Jing, its main investor, chairman, and CEO, has lost $9.1 billion of his personal wealth since the 2015 Chinese stock market crash, or 84 percent of the total (Chang 2015). Prior to the crash, he had committed to investing $500 million in the project: a small fraction of his wealth before the crash, but a significant share afterward.

Other obstacles have come from domestic resistance to the project. According to press reports, citizens have held at least 60 marches to protest the canal, with up to 15,000 participants (Miranda Aburto 2016, "Miles Marchan" 2015). Protestors have published a list of complaints and a demand for the canal project to be cancelled (Álvarez 2015). These complaints do not list specific grievances other than general references to rights to private property, life and dignity. The lack of specificity may be related to the lack of information available to citizens. The terms of reference of the environmental and social impact assessment commit to publishing an environmental impact report in the vernacular language (HKND Group 2014b). To date, HKND has published the report in English (HKND 2015), but no such document has been published in Spanish yet.

Nonetheless, 2015 saw work continue on this project. In March, HKND shared several sections of its EIA with an independent panel of experts at Florida International University. Unfortunately, the panel did not respond positively (Covich et al 2015).

Among other objections, the panel focused on one problematic aspect that is likely to accentuate social conflict and delay the project's completion: the choice of route. The executive summary of the EIA acknowledges that HKND selected a route south of Bluefields in order to save money, even though this decision meant crossing through the Cerro Silva Natural Reserve as well as Kriol and Rama indigenous territory, as Figure 7 shows (ERM 2015). The project's independent review panel vehemently objected to HKND's having chosen the route without adequate research into whether other routes, outside of these sensitive territories, would have had lesser environmental impacts (Covich et al 2015).

FIGURE 7: Nicaragua Canal Route, Biodiversity, and Indigenous Territory



Source: Compiled from Anderson et al. (2008), Congreso Mesoamericano de Areas Protegidas (2010), HKND Group (2014a), and León Áviles (2013).

At this stage, it is unlikely that HKND will change the canal route, so the success of the project will hinge upon its ability to diffuse local opposition. At the outset of the project, HKND committed to seven initial "scoping" meetings with key stakeholder groups, as well as focus groups and in-depth "baseline workshops" beginning in 2014, and finally, 11 "town hall" meetings once the project is underway (HKND Group 2014b). To date, HKND has conducted the seven initial meetings. It will be difficult for HKND to address protestors' concerns without catching up on its commitments to publish a Spanish-language EIA and conduct public consultations.

Capital de las Ciencias

In October 2015, during the "México Cumbre de Negocios" Business Summit in Guadalajara, Jalisco Governor Aristóteles Sandoval signed a memorandum of understanding with the Americas chief of the China Communications Construction Company (CCCC), Liu Yueping, for the development of the "Capital de las Ciencias" technological industrial park ("Anuncia" 2015, Graham 2015). The memorandum of understanding will launch a six-month feasibility study for the park, to be published later this year.

According to press reports, the park will occupy approximately 500 hectares (1,235 acres), and divided into three zones: an integrated zone, an industrial park, and a service area (Graham 2015). It aims to support about 100 Chinese and Mexican high technology manufacturing companies ("Concretan" 2015). This is the first of what is slated to be numerous Chinese-sponsored industrial parks across Latin America as part of the CELAC-China Cooperation Plan negotiated in early 2015 between the two entities (Gallagher, 2016).

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