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CHINA'S RISE IN SOUTH AMERICA: THE PARTNER OF CHOICE?

by

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CHINA'S RISE IN SOUTH AMERICA: THE PARTNER OF CHOICE?

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ABSTRACT

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TABLE OF CONTENTS

LIST OF FIGURES

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LIST OF ACRONYMS AND ABBREVIATIONS

ALBA	Alternativa Bolivariana para las Américas (Bolivarian Alliance of the Americas)
BPD	barrels per day
CDB	China Development Bank
CEEC	China Energy Engineering Corporation
C-EXIM	Export-Import Bank of China
CNPC	China National Petroleum Company
CRCC	China Railway Construction Company
FDI	foreign direct investment
FONDEN	Fondo de Desarrollo Nacional (National Development Fund)
IADB	Inter-American Development Bank
IMF	International Monetary Fund
IOC	international oil company
ISI	import substitution industrialization
LAC	Latin America and the Caribbean
MCC	Millennium Challenge Corporation
MERCOSUR	Mercado Comun del Cono Sur (Southern Cone Common Market)
MERVAL	Mercado de Valores (Stock Market Index in Argentina)
NAFTA	North American Free Trade Agreement
NGO	Nongovernmental organization
NIEO	New International Economic Order
NOC	national oil company
OAS	Organization of American States
OBOR	One Belt, One Road
PDVSA	Petróleos de Venezuela, S.A. (Petroleum of Venezuela)
RMB	Renminbi
TPP	Trans-Pacific Partnership
UNASUR	Unión de Naciones Suramericanas (Union of South American Nations)
USAID	U.S. Agency for International Development
USD	United States dollar

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I. INTRODUCTION

A. SIGNIFICANCE OF THE RESEARCH QUESTION

This thesis answers the question, "Are South American countries benefiting from Chinese investment?"

Import substitution industrialization (ISI) was attempted in South America in the 1950s by imposing high tariffs on imports to shield its infant industries, in order to eventually compete with the core's manufacturing capabilities and costs. Argentina's own economist Raul Prebisch taught Dependency Theory or how the core or technologically advanced economies, like the United States, used the peripheral countries to further perpetuate the core's progress. This, in turn, would create a richer center and leave the periphery poorer and enslaved to the core. However, only the larger Latin American economies had success with ISI because their economies created enough demand to make a profit from a large enough quantity of highly inefficient domestically manufactured products. Smaller countries incurred larger losses due to inefficiencies and lower demand for the products.

In the 1980s, the World Bank aided Latin American economies that had not sufficiently benefitted from ISI. Along with the financial assistance came strings attached to implement the neoliberal reforms that the banks demanded in return. After several decades of following orders from the United States, enduring years of U.S. military intervention, suffering from oppressive loans, and tolerating unfair foreign business practices, South American countries once again sought their own sovereignty, political autonomy, and economic independence.

According to Robert Ellis, these occurrences motivated left-leaning governments in South American countries to seek more flexible investment options to fund their projects and programs on their own terms instead of following the dictates of U.S.-backed organizations (e.g., World Development Bank, International Monetary Fund (IMF), or

Washington's policies).[1] China's increased involvement in South America matters greatly, because if it succeeds at displacing the United States politically and economically, there will likely occur significant changes throughout the Western Hemisphere that diminish U.S. power globally.

South America has met China's requests for strategic partnerships by providing China commodities as well as export and foreign investment opportunities. According to Stephen Kaplan, Chinese loans—and subsequent investment—have increased dramatically since the 2008 financial crisis and have supplied South America with "patient capital" as opposed to short-term capital with associated restraints, enabling South America to sidestep U.S. political-economic maneuvers in the region.[2] Consequently, as noted by Harold Trinkunas, Chinese foreign investment in Latin America surpassed that of such traditional sources as the World Bank and Inter-American Development Bank in 2013.[3]

Furthermore, Trinkunas notes that Chinese trade with South American countries has risen significantly, and in many South American countries, it has surpassed levels of trade with the United States.[4] As of 2012, observe Wu Baiyi and Liu Weiguang, some of South America's most successful and influential countries, Brazil and Chile, were among those that now conduct more trade with China than the United States.[5] These examples of rising trade, foreign investment, and cooperation indicate how China and South America both appear to be achieving economic gain while the United States is losing ground.

China's aggressive engagement in global banking—at a time when many South American leaders sought alternative financing—enabled it to gain access to South

[1] Robert Evan Ellis, *China in Latin America: The Whats and Wherefores*, vol. 46 (Boulder, CO: Lynne Rienner Publishers, 2009), 26.

[2] Stephen B. Kaplan, "Banking Unconditionally: The Political Economy of Chinese Finance in Latin America," *Review of International Political Economy* 23, no. 4 (July 3, 2016): 2.

[3] Harold Trinkunas, "Renminbi Diplomacy? The Limits of China's Influence on Latin America's Domestic Politics," *Foreign Policy at Brookings*, *Geoeconomics and Global Issues*, no. 3 (November 2016): 1.

[4] Trinkunas, 5.

[5] Liu Weiguang Wu Baiyi, *China-Latin America Relations: Review and Analysis* (Reading: Paths International, 2012), 98.

America's raw materials and energy markets. Andrew Cooper and Jorge Heine claim that Chinese planners understood China's industrial growth had surpassed its domestic energy and resource production capacity, and that there was an insufficient amount of natural resources and agricultural production in Southeast Asia to maintain its economy and citizenry.[6] This "win-win" financing seems to drive South America's political economy while supplying China the energy and materials needed to feed its domestic industries, resulting in an arrangement that is complementary rather than competitive.

This chapter focuses on the available literature available about Chinese investment in South America and whether it has benefited South America. This is important because if South America is benefiting, it is critical that the United States implement policies that will help it regain the regional title of "partner of choice." Next, potential hypotheses are discussed to understand whether Chinese investment has been beneficial to South America or not. Finally, the research design describes the thesis' approach of analyzing Chinese investment in South America to better understand the dynamics of the new form of global banking and to determine if it is benefitting South America.

B. LITERATURE REVIEW

The literature review focuses on how South America has sought autonomy from the grasp of Washington, benefited from the autonomy, and how South America may be negatively affected. Finally, China's interests in South America are also reviewed to portray how the two have joined together financially to minimize U.S. influence.

1. South America's Pursuit of Fiscal and Political Autonomy from United States

Due to the perception that U.S. policies are unfriendly to Latin American interests, 12 countries from the region formed in 2008 the Union of South American Nations (UNASUR) to begin cutting ties with the U.S. "core." As Jeanne Hey states, "an anti-core policy is . . . the 'new' Latin American Foreign Policy. It is oriented towards the Third

[6] Andrew Fenton Cooper and Jorge Heine, *Which Way Latin America?: Hemispheric Politics Meets Globalization* (Tokyo: United Nations University Press, 2009), 102.

World, promotes the New International Economic Order (NIEO), and seeks autonomy from the U.S.A."[7] Because the United States has been the core, it has used "carrot and stick" approaches for several decades, South American countries have looked to other trading partners to achieve political-economic goals. This further aligns with the view of Hey, who states, "economically dependent states will develop policies that accord with their patrons' foreign-policy wishes."[8] South American leaders have not always agreed with U.S. foreign policy and therefore understand the need to disconnect economically to achieve political autonomy. By finding other countries to provide the same economic benefits without strings attached, South America can more easily implement policies that may counter U.S. interests.

For example, Baiyi et al. suggest that Latin America and China were insulated from the 2008 financial crisis due to fewer financial and market linkages with the United States.[9] On the other hand, Kaplan argues that it was the increase of Chinese loans to South America—patient capital—that helped those countries weather the storm.[10] Less researched is how Chinese investment:

- Helps prop up non-democratic, South America regimes over the long run
- Provides measures to counter U.S. policies
- Creates less transparency both financially and politically

Additional research by Ellis also suggests that because of fewer strings attached to Chinese loans, there is hope for growth in commodity exports to China and China's also acting as a counterweight to offset U.S. influence in the region.[11] Similarly, Ernesto

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7 Jeanne A. K. Hey, "Three Building Blocks of a Theory of Latin American Foreign Policy," *Third World Quarterly* 18, no. 4 (September 1, 1997): 637.

8 Hey, 637.

9 Wu Baiyi, China-Latin America Relations: Review and Analysis, 97.

10 Kaplan, "Banking Unconditionally: The Political Economy of Chinese Finance in Latin America," 17.

11 Ellis, *China in Latin America: The Whats and Wherefores*, 46:24.

Vivares suggests, “Washington no longer determines the equilibrium of world power in a decisive way as it did after the Cold War. There are new and influential players to take account of.”[12] On the other hand, Hey states that pro-core policies are often implemented when a country depends on the core for monetary reasons, political unrest, or simply the prestige of being associated with the core (e.g., the U.S. government, World Bank, or IMF).[13] Because China has offered more loans-for-resources, China has altered the composition of the traditional core and has altered the structure of diplomatic ties in the Western Hemisphere, thus reducing the United States’ traditional hegemonic role with unforeseen consequences.

The literature is abundant but conflicting when it comes to South America’s benefitting from Chinese investment. “While such a pattern may produce more wealth and optimize the allocation of resources globally,” notes Ellis, “it will do so, in part, by propagating income inequality and a lack of well-paying jobs throughout Latin America.”[14] It may create short-term benefits for South America while accelerating the spread of Chinese geopolitical influence in the Western Hemisphere. How? By providing China additional soft power while it continues to grow as a world superpower.

Additionally, Kevin Gallagher states that increasing commodity exports to China has caused currency appreciation, which, if countries are not careful, can destroy domestic industry and employment by suppressing investment in noncommodity industries.[15] This is problematic because the majority of Chinese investment is in the energy sector. Furthermore, because Chinese imports have slowed worldwide, South America’s windfall revenues will recede, and, if governments have not properly invested in other sectors or saved significantly, Chinese investment will have done little for the region.

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[12] Ernesto Vivares, *Exploring the New South American Regionalism* (NSAR) (New York: Routledge, 2016), 50.

[13] Hey, “Three Building Blocks of a Theory of Latin American Foreign Policy,” 634.

[14] Ellis, China in Latin America: The Whats and Wherefores, 46:287.

[15] Kevin P. Gallagher, The China Triangle: Latin America’s China Boom and the Fate of the Washington Consensus (New York: Oxford University Press, 2016), 92.

2. China's Interests in South American Investment

China's economy has grown so quickly that Chinese interests in South America have grown substantially in search of opportunities for natural resource imports and manufactured exports to South America. Chinese interest has also been enticing to South America because of new opportunities for foreign investment other than that with the United States. Ellis states that China has four interests in South America: "acquiring primary products, obtaining markets for Chinese exports, gaining international isolation of Taiwan, and securing strategic alliances as part of China's global positioning as it emerges as a superpower."[16] These four objectives seem to align well with South American objectives because:

1. They dovetail with the Chinese commodity boom.
2. All South American countries except Paraguay have ceased recognizing Taiwan as the Republic of China.
3. Most have enjoyed the maneuvering room afforded by new forms of financing with fewer conditionalities than Bretton Woods institutions imposed.

The Chinese have many political as well as economic reasons for maintaining strong Sino-South American ties. Ellis states that China is building strategic partnerships with Latin American countries that hold significant power in their regions, such as Venezuela in the Caribbean, Mexico in Central America, and Brazil and Argentina in South America, which show more geopolitical influence rather than strictly economic reasons.[17] This creates the Chinese counterweight that is needed to combat the undesirable U.S. hegemony in all three of these regions.

Additionally, Kaplan states, "China's state-led capitalism is an important form of patient capital. Unlike the short-term horizon of private market capital, patient capital is

[16] Ellis, China in Latin America: The Whats and Wherefores, 46:9.

[17] Ellis, 46:17.

characterized by both a long-term horizon and long-term relationships."[18] This "patient capital" as Kaplan calls it, buys South American leaders time to pursue their objectives without short-term investors threatening to pull funds on account of uneasiness about market trends, political environment, and other events. Furthermore, Kaplan states that China is a complementary commodity-trading partner with South America because, unlike the United States, China does not need to protect its agricultural products, as the U.S. government does through subsidies, therefore creating more cost-effective commodity trade for both countries.[19] This makes trade much between China and South America much easier than the conflict-laden agricultural trade between the United States and South America.

Chinese President Xi Jinping pledged $250 billion in overseas foreign direct investment (FDI) to Latin America and the Caribbean (LAC) between 2015 and 2019, some $50 billion a year, according to David Dollar.[20] Although the recipients of these funds have not all been determined, it is evident that the Chinese intend to continue investing funds in the region. Rolando Avendano, Angel Melguizo, and Sean Miner also suggest that Chinese overseas FDI has recently reached $200 billion, shocking many economists because Chinese FDI now accounts for 10% of the world's total FDI, and only a decade ago China accounted for just 2%. This outward flow of investment is highly concentrated in mergers and acquisitions of "higher value companies with technological knowhow, brand value, and strategic assets, such as semiconductor and other advanced manufacturers."[21]

18 Kaplan, "Banking Unconditionally: The Political Economy of Chinese Finance in Latin America," 643.

19 Kaplan, 5.

20 David Dollar, "China's Investment in Latin America" (Brookings, January 2017), 1, https://www.brookings.edu/wp-content/uploads/2017/01/fp_201701_china_investment_lat_am.pdf.

21 Rolando Avendano, Angel Melguizo, and Sean Miner, "Chinese FDI in Latin America: New Trends with Global Implications," The Atlantic Council of the United States and the OECD Development Centre, June 2017, 4–5, http://www.atlanticcouncil.org/images/publications/Chinese_FDI_in_Latin_America_web_0626.pdf.

C. ARGUMENT

The focus of this thesis is to determine whether South America is benefitting from Chinese investment because they are relying less on the United States and other western sources of capital. What seem to be complementary goals between the China and South America will eventually lead to both political and economic non-complementary objectives shared by the two regions.

Chinese foreign investment within South America is a new phenomenon that needs to be analyzed for observers to understand how it is shaping South American political-economic dynamics. Due to China's influence over Chinese firms and state-owned enterprises, South America will likely experience much more pressure from the People's Republic of China as China's role in the world expands.

Additionally, Chinese investment has the ability to prop up regimes that are undemocratic and authoritarian. For example, had the Chinese not pumped billions of dollars of loans-for-oil investments into Venezuela's economy to buy Maduro's regime time to implement economic reforms, President Nicolás Maduro might well have been forced to step down or been thrown out.

D. RESEARCH DESIGN

Chapter II briefly focuses on China's "opening-up" and "going-out" policies and reforms to convey a sense of how the Chinese state-owned banks, under the governance of the Communist Party of China, have been able to accomplish what they have in such a short time. Additionally, the chapter shows where Chinese global investment has been distributed worldwide with an emphasis on growth in South America and why the region has embraced a new source of investment.

Chapters 3 and 4 provide a deeper dive into the political economies of Venezuela and Argentina to explore whether and to what degree Chinese investment is helping these two countries. Although they are but a small representation of the region, they can speak to the practical implications of what other South American countries can expect from similar investment by China. The two case studies are extreme in nature, which best illustrates how politicians' decision-making can dramatically affect the outcomes of increased financial ties with China. Venezuela's economy has become more exposed to the resource curse while Argentina has been attempting to diversify its energy sector and update infrastructure with the increase in foreign investment instead of using funds for political gain through Venezuela's socialist programs.

On the other hand, the case studies are limited because no other South American countries have oil reserves as large as Venezuela's and would not likely be able to attain, let alone shoulder, the hefty debts that China has allowed Venezuela to incur in exchange for oil. In 2015, however, Bolivia relied on oil and gas for nearly 45% of its export revenue and an additional 37% from mining and minerals exports.[22] This places Bolivia in a highly susceptible position to succumb to what its leaders might perceive as attractive loans-for-resources from China. Similarly, many other economies in the region rely on mining and minerals, such as Peru, Colombia, and even Chile, which is one of the strongest economies of the region. Furthermore, Ecuador relies on oil for 30% of its exports. These numbers do not inherently cause alarm, but coupled with populist leaders, large loans, investment ties, and little oversight, they portend the potential for disaster.

Although not all South American countries have the potential for producing and exporting oil, vast amounts of minerals, or such metals as copper and gold, many South American countries such as Argentina, Brazil, Uruguay, and Paraguay can lure China to them with their large production of agricultural and animal products. Therefore, they can still be susceptible to resource curse, or over-reliance on the revenue from natural resources instead of diversifying and developing additional revenue generating sectors. By knowing the results of Venezuela and Argentina's financial decisions, leaders of other South American nations can make more informed decisions, leading to more long-term growth, and avoid potential pitfalls.

These comparative case studies collect, measure, and analyze data to determine the significance of Chinese influence in South America. In particular, research reviewed Chinese investment in Venezuela and Argentina, because China has diversified

[22] "By Country Exports, Imports, and Trade Partners," The Observatory of Economic Complexity, accessed January 30, 2018, https://atlas.media.mit.edu/en/visualize/tree_map/hs92/export/bol/all/show/2015/.

investments in hundreds of countries and it is not feasible in this study to analyze each South American country. The current crisis in Venezuela makes that nation a particularly intriguing case study to understand how China is reacting and possibly foreshadow how China will react to the actions of other countries that find themselves in similar situations.

Argentina, on the other hand, achieved the greatest market growth in the world in 2017 with a 45% rise in its Mercado de Valores (MERVAL) index, a Buenos Aires stock portfolio consisting of 28 large Argentine companies.[23] This growth makes Argentina a good country to analyze being on the opposite spectrum as Venezuela. Additionally, Argentina has a large economy that has gone through cycles of great growth followed by great crisis; the country has sought autonomy from the United States since before World War II and has been heavily involved with the Chinese in the past decade.

Finally, Chapter V focuses on U.S. foreign policy recommendations to help steer the United States toward being able to furnish attractive alternatives for South American countries, and their citizens. For example, in his southern tour to Colombia, Argentina, Chile, and Panama in August 2017, Vice President Mike Pence specified, "'America first' does not mean 'America alone.'"[24] However, the rhetoric alone is not sufficient to gain the traction needed to win favor from South American citizens, and new innovative policies are necessary for America to remain the "Partner of Choice," as the 2017 to 2027 U.S. Southern Command's Theater Strategy seeks to achieve. It is imperative that the United States use every opportunity to regain its hemispheric hegemony and to preclude China from further aligning South America away from U.S. influence as it has during the Chinese decade. This thesis considers whether a Good Neighbor policy for the 21st century is likely to ensure responsible governance in the Western Hemisphere and to remain the "partner of choice" over the rise of China.

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23 "The Best of 2017 in Business," Fortune, December 18, 2017, http://fortune.com/2017/12/18/business-trends-news-2017/.

24 Peter McKenna, "Trump's Abysmal Treatment of Latin America Could Open Up Opportunities for Canada," *Chronicle Herald*, accessed September 1, 2017, http://thechronicleherald.ca/opinion/1496868-mckenna-trump%E2%80%99s-abysmal-treatment-of-latin-america-could-open-up-opportunities-for-c.

II. CHINA'S "GOING-OUT": CHANGING GLOBAL INFLUENCE IN THE WESTERN HEMISPHERE

"Ultimate excellence lies not in winning every battle, but in defeating the enemy without ever fighting"

—Sun Tzu

"Let China sleep; when she awakes, she will shake the world."

—Napoleon, 1817

"The greatest Chinese dream is the great rejuvenation of the Chinese nation."

—Xi Jinping, 2012

To better understand how and why China has been able to engage so quickly in South America, Chinese domestic and foreign policy—driven by the Communist Party of China—need to be understood. This chapter provides the background information needed to better understand what is at stake for the Western Hemisphere if China is successful at being a superior partner of choice. Chinese economic growth and development abroad would not be questioned if investment was highly privatized and detached from heavy government influence and power. However, an authoritarian government is at the helm of one of the largest economies in the world and it is entangled in financial agreements and projects worldwide. This chapter briefly sheds light on China's opening-up and how its reserve accumulation is tied its state-owned bank. Finally, this chapter focuses on China's new "going out" strategy in South America and how South America may be benefiting and where it may be losing.

A. CHINA'S STATE-OWNED "NATIONAL CHAMPIONS" AND THEIR WORLDWIDE INFLUENCE

China began recognizing the inefficiencies of its state-owned enterprise as the Asian Tigers continually developed more quickly and were becoming more and more advanced despite China's exhausting labor practices. Once Mao died in 1976, leaders were relieved of his harsh policy of growth at all costs and were given flexibility to try new reforms. Watching China's economy grow, has given hope to some in South America that the Chinese model may be more beneficial to their economies than what the Washington Consensus has provided them over the past two centuries.

The Communist Party decided to maintain control over the largest and strategic industries permitting the smaller and less significant sectors of industry to either be sold to private industry or shut down. These efforts were known as *zhuā dà fàng xiǎo*, or "grasping the large and letting go of the small," which enabled the party to maintain control over only the largest and selective sectors of state-owned enterprises, allowing the smallest state-owned enterprises to be shut down or privatized to decrease massive inefficiencies. According to Nicholas Lardy, to "grasp the big and release the small," 30 million or two-fifths of state employees were fired in 1995.[25] However, the reform introduced privatization, which encouraged vast amounts of inward foreign investment to enter the country. Foreign investment boosted China's domestic industry while decreasing the amount of inefficient state run businesses and factories. This reform generated efficiencies as foreign companies brought new product ideas to China, enhancing manufacturing capabilities, and thus more savings were possible because of higher profit margins of private industry and domination of the world markets—leading to the vast foreign exchange reserves that China now enjoys.

Despite China's state-owned enterprise reform, the state still owns many powerful industrial sectors. Lardy states that in 2003, the Chinese government formed the State-Owned Assets Supervision and Administration Commission to create "national champions" out of state-owned enterprises. Lardy also notes that the Commission would oversee 200 of the most important state enterprises and "serve as guarantors of Party supremacy."[26] For instance, Lardy's data from 2009 shows that China's two largest state-

[25] Nicholas R. Lardy, *Markets Over Mao: The Rise of Private Business in China* (Washington, DC: Columbia University Press, 2014), 18.

[26] Lardy, 49–50.

owned enterprises generated as much profit as the top 500 private Chinese companies together.[27]

China's state-owned banks run by the Communist Party provide these "national champions" soft-budget loans to invest abroad. An increasing number of these loans, however, are non-performing and have created a moral hazard and have continued to cause inefficiencies in state-owned enterprises and the state. Lardy highlights other concerns about government intervention in business. As he states, "an intimate link between the party and these top state-owned firms perhaps is best symbolized by the red phones on the desks of these firms' CEOs, which provide a direct, encrypted link between the firms and Zhongnanhai, the location of the Chinese Communist Party headquarters in Beijing."[28] Furthermore, Carl Walter and Fraser Howie write that in 2010, half of China's 109 "national champions" had CEOs embedded by the party.[29] These strategic and massive state-owned enterprises are directly linked to the interests, influence, and direction of the Communist Party of China.

Although there has been a big change in the name of ownership, those in charge of the Communist Party still control the economy. For example, Lardy still believes that while the number state-owned enterprises is shrinking, the Communist Party's aspirations are not, and party bosses are willing to tap into its $3.7 trillion reserves to lengthen its control.[30] These reserves create space for the party-state to disregard inefficiencies and instead focus on maintaining power, control, and influence.[31] This data provides little hope for regime change from a single party authoritative system with very deep pockets and power over strategic sectors of industry—both domestically and abroad.

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27 Lardy, 49.

28 Lardy, 52.

29 Carl E. Walter and Fraser J. T. Howie, *Red Capitalism: The Fragile Financial Foundation of China's Extraordinary Rise* (Singapore: John Wiley & Sons, 2012), 167.

30 Nicholas R. Lardy, "Book Review Roundtable: Nicholas R. Lardy's Markets over Mao: The Rise of Private Business in China," *Asia Policy* 20 (July 2015): 148.

31 Lardy, 148.

Private Chinese businesses and large state-owned enterprises—both highly influenced or controlled outright by the Communist Party—are now able to influence hundreds of other countries as financial ties have broadened worldwide. For example, Australia, which conducts a significant amount of trade and has many Chinese studying there, has noticed Chinese influence spreading within its own government. Merriden Varrall claims that politicians are being paid off and the Communist Party of China is releasing communist ads in newspapers to sway public opinion.[32] It is likely that similar occurrences will surface in South America in future years.

B. CHINA DEVELOPMENT BANK IN SOUTH AMERICA

China has the largest foreign exchange reserves in the world, and this enables the China Development Bank (CDB) to project the communist party's agenda due to its being a state-owned enterprise and having direct ties to the party. In December 2017, reserves rose to $3.14 trillion. Although the reserves are not exclusively used by the CDB, the bank is the state's largest foreign exchange lender, is fully owned by the state, and it is able to offer lower interest rates and arrange longer-term limits on its loans than other Chinese banks.[33] The four big Chinese banks have more assets than the CDB, but they are becoming more privatized, less influenced by the central government, and are more focused on making quick returns on shorter investments. On the contrary, Erica Downs states that the CDB is managed by the government and therefore more capable of achieving state agendas, while focusing less on profit maximization—while still very important—but more concerned about long-term strategic objectives, such as energy security.[34]

China directs nearly 40% of its developmental loans to Latin America, which raises concerns for the Western Hemisphere because the Chinese state controls the CDB. Dollar

32 Merriden Varrall, "A Chinese Threat to Australian Openness," *New York Times*, July 31, 2017, https://www.nytimes.com/2017/07/31/opinion/australia-chinese-students.html.

33 "China December Forex Reserves Rise to $3.14 Trillion, Highest Since September 2016," Reuters, January 7, 2018, https://www.reuters.com/article/us-china-economy-forex-reserves/china-december-fx-reserves-rise-to-3-14-trillion-highest-since-sept-2016-central-bank-idUSKBN1EW061.

34 Erica Downs, *Inside China, Inc: China Development Bank's Cross-Border Energy Deals* (Washington, DC: Brookings, 2011), 64.

states, “[Chinese] policy banks lent $118 billion to Latin America between 2007 and 2014: 53 percent went to Venezuela, 18 percent to Brazil, 12 percent to Ecuador, and 12 percent to Argentina.”[35] As the state uses the loans to create strategic partnerships, Chinese state-owned enterprises follow behind the loans to fund additional projects. Figure 1 shows how much of these development funds have gone to LAC compared with the rest of the world. The fact that the world’s largest state-owned bank is focusing investment in Latin America is troubling because most development banks are a conglomeration of multiple states’ collective assets and collaborative ideas for proposed projects. However, China holds extreme volumes of foreign exchange reserves linked to the CDB, which has nearly four times as many assets as the World Bank.

[35] David Dollar, “Yes, China Is Investing Globally—But Not So Much In Its Belt and Road Initiative,” Brookings, May 8, 2017, https://www.brookings.edu/blog/order-from-chaos/2017/05/08/yes-china-is-investing-globally-but-not-so-much-in-its-belt-and-road-initiative/.

Region	$USB
Asia	
Silk Road Fund	40
The Green Silk Road Fund	4.8
China-ASEAN Fund	1
Eurasia	
China-Central and Eastern Europe Investment Fund	4
Russia-China Investment Fund	2
Latin America and Caribbean	
CELAC-China Investment Fund	20
China-LAC Industrial Cooperation Fund	10
China-LAC Investment Fund	5
China-Mexico Investment Fund	2.4
Africa	
China -Africa Development Fund	2
Africa Growing Together Fund	2
China-Africa Industrial Capacity Cooperation Fund Company Limited (CAICCF)	-
Global South	
South-South Climate Fund	3.2
South-South Cooperation Fund	2
Total	98.4

Figure 1. Worldwide Distribution of Chinese Development Banks' Assets ($ billion).[36]

Although most of these development funds are from the CDB, a portion comes from the Export-Import Bank of China (C-EXIM). The direct linkages to the largest foreign exchange reserves, the lowest interest rates, some of the longest-term loans available, and oversight by the Chinese government, enable China to project tremendous political-economic power throughout Latin America. Figure 2 shows how the CDB dwarfs the world's largest development banks and combined with C-EXIM, the Chinese financial footprint is very influential.

[36] Rohini Kamal and Kevin Gallagher, "China Goes Global With Development Banks," Bretton Woods Project, April 5, 2016, http://www.brettonwoodsproject.org/2016/04/20508/.

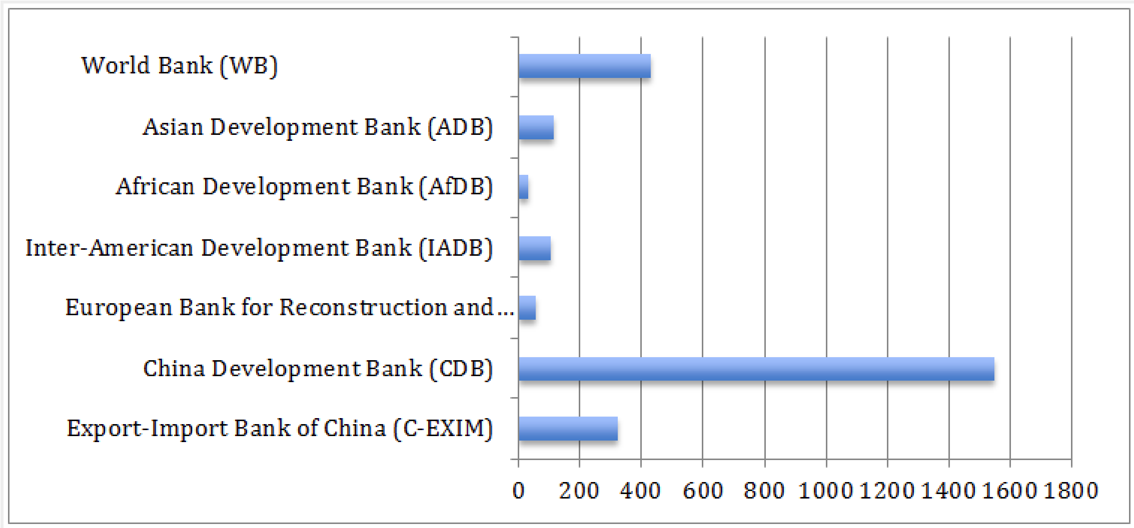

Figure 2. Chinese vs. Western-Backed Development Banks' Assets ($ billion).[37]

The rise of the CDB in South America, as well as the rest of LAC, enables China to greatly influence the region. The drop in oil prices in 2008, along with the financial crisis that soon followed, caused China to reconsider its foreign exchange reserve portfolio. China quickly realized the volatility of investing too heavily in the U.S. market. While many oil producing countries needed foreign investment to stay afloat during the oil bust, China's leaders decided to diversify their use of the country's foreign exchange reserves by investing in energy, according to Downs.[38] China shifting its investments from U.S. treasury bonds towards energy shows how the Chinese government can quickly direct finances to meet its strategic objectives. Furthermore, if financial investments are geo-economic weapons used to influence other countries, a large majority of finance is flowing to Latin America to do just that. Allison defines geo-economics as "the use of economic instruments (from trade and investment policy to sanctions, cyberattacks, and foreign aid) to achieve geopolitical goals."[39] Chinese development abroad is a new phenomenon and the possibility of financial investments being used as geo-economic weapons must not be carelessly ignored.

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37 Kamal and Gallagher.

38 Downs, *Inside China, Inc: China Development Bank's Cross-Border Energy Deals*, 60.

39 Graham Allison, *Destined for War* (Boston—New York: Houghton Mifflin Harcourt, 2017), 20.

China's massive foreign exchange reserves, coupled with the Communist Party's ability to communicate and advance its agenda abroad through the CDB, enable development funds to be earmarked by the state for specific regions, business sectors, and strategic interests. Chinese development loans are also tied to the state's foreign FDI. The Chinese leadership generally establishes strategic partnerships with countries by means of large development loans. Once these loans are in place, Chinese state-owned enterprises enter the arena with additional investment to finance and construct large projects. Figure 3 shows the significant amount of Chinese foreign investment in Latin America.

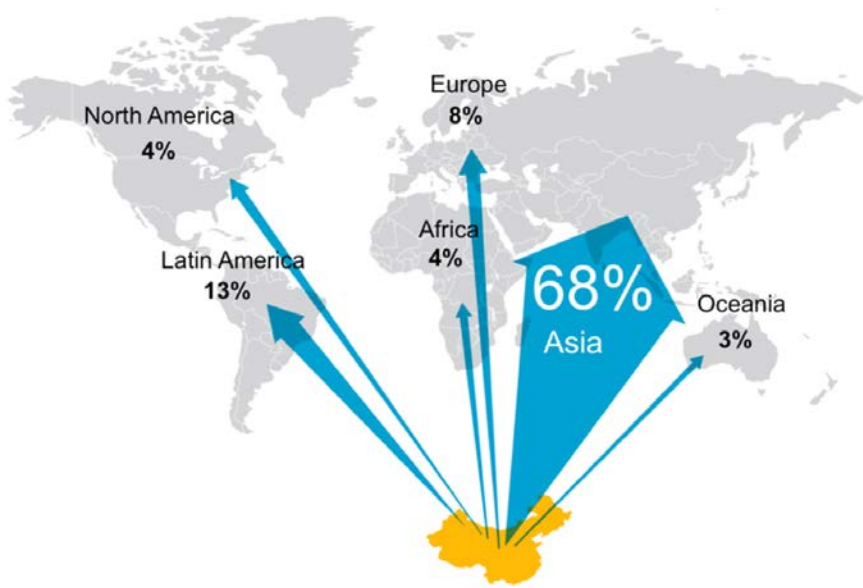


Figure 3. Distribution of Chinese Overseas Foreign Direct Investment Stock (2013).[40]

Figure 3 shows that China has significantly invested in many of its Asian neighbors. However, after Asia, Latin America is the next-largest region for Chinese foreign investment. While the United States was entangled in the 2008 financial crisis, China offered South America alternative FDI in exchange for resources and opportunities to increase market interconnectivity. Considering the hype of China's footprint in Africa,

40 Denise Leung Lihuan Zhou, "China's Overseas Investments, Explained in 10 Graphics," World Resources Institute, January 28, 2015, http://www.wri.org/blog/2015/01/china%E2%80%99s-overseas-investments-explained-10-graphics.

there is over three times as much investment in Latin America compared to Africa. For this reason, it seems necessary to investigate the phenomena.

In 2005, Chinese annual overseas FDI totaled a mere $13.7 billion, or 1.6% of the total world's overseas FDI, which was $843.8 billion, according to OECD's calculations.[41] As of 2016, however, Chinese annual overseas FDI has amounted to $217.2 billion, a 15-fold increase. To put this into perspective, OECD data from 2016 illustrates the world's total annual outflow of FDI as $1.474 trillion; thus Chinese overseas FDI has reached nearly 7% of the world's overseas FDI.

Additionally, David Shambaugh states that China's total accumulated overseas FDI stock reached $1.2 trillion in 2016 and was right on target as A Capital, a consulting firm, had predicted a surge of $800 billion between 2011 and 2016.[42] Figure 4 shows the exponential growth of overseas FDI since China implemented its going-out strategy.

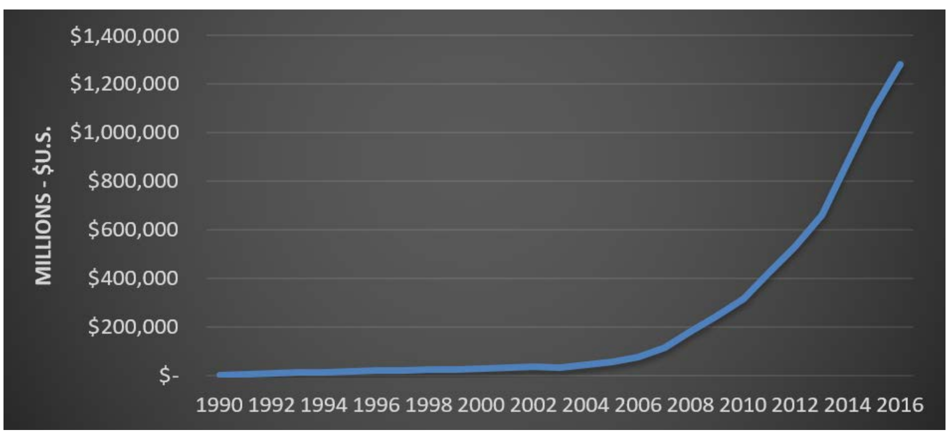


Figure 4. China's Cumulative Overseas Investment (1990–2016).[43]

41 Author based his calculations in this paragraph on data derived from OECD: https://data.oecd.org/foreign direct investment/foreign direct investment-flows.htm#indicator-chart

42 David Shambaugh, *China Goes Global: The Partial Power* (Oxford—New York: Oxford University Press, 2013), 178.

43 "World Investment Report 2017: Annex Tables," United Nations Conference on Trade and Development, accessed January 24, 2018, http://unctad.org/en/Pages/DIAE/World%20Investment%20Report/Annex-Tables.aspx.Note: Author constructed chart from data from United Nations World Investment Report for 2017.

This significant growth in overseas investment correlates with the growth of China's exponential reserve growth. This can be problematic for reasons stated by Robert Blackwill and Jennifer Harris: "Time and time again in modern history hard power has followed where capital leads, flowing from advanced economies to developing nations regardless of religion, culture, and ideology of the home country."[44] Furthermore, China's economy has matured, the country has more buying power, and the Communist Party of China has significantly more potential to influence abroad, including in South America. China's leaders certainly hope that it will not need to abandon its non-interfering approach to protect its investments abroad.

C. POLITICAL-ECONOMIC MOTIVATIONS FOR CHINESE OVERSEAS INVESTMENT IN SOUTH AMERICA

China's current objectives for its overseas investments, according to Katherine Koleski, are to continue importing raw materials while using its indigenous innovation to produce higher-value-added products for export worldwide.[45] South America's desire to trade raw materials complements Chinese aim to import low-cost materials with which to fabricate higher-value-added products for resale at much higher profits. Nevertheless, these are not the only motivators at play.

China is likely using these investments to buy influence while simultaneously achieving its primary goal of securing natural resources. As Robert Gilpin states, FDI is an "overall strategy to develop permanent position in another economy."[46] These patterns of economic behavior suggest that China has long-term objectives for investing in South America. Additionally, Gilpin mentions that multinational corporations do have a political and economic effect on a country because of FDI.[47] Increasing Chinese foreign investment in South America over the next several years will likely strengthen China's political

[44] Robert D. Blackwill and Jennifer M. Harris, *War by Other Means* (Cambridge: Harvard University Press, 2016), 143.

[45] Katherine Koleski, "The 13th Five-Year Plan," n.d., 38, https://www.uscc.gov/sites/default/files/Research/The%2013th%20Five-Year%20Plan.pdf.

[46] Robert Gilpin, *Age of the Multinational* (Princeton: Princeton University Press, 2000), 164.

[47] Gilpin, 171–172.

leverage and give South America financing and business opportunities as projects, mergers, and new business models began to take shape and produce results. Eugene Gholz, Umul Awan, and Ehud Ronn state, "perhaps China is using loans-for-oil to cultivate diplomatic ties, making them a way to 'buy friends,' as foreign aid has often been used in the past."[48]

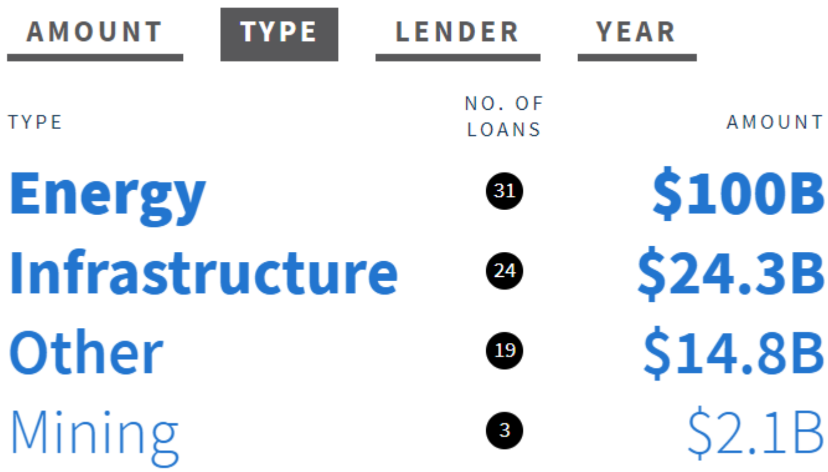
Not only is China seeking new allies and selling its brand abroad, but the country is benefiting from the acquisition of abundant South American raw materials. According to Gallagher, the top four commodity exports from South America are iron ore, soy, copper, and oil.[49] These are essential to keep Chinese factories supplied and workers fed, enabling them to continue producing a large share of the world's products. Gallagher mentions that this new reliance on natural resource exports to China is causing South America to become more vulnerable to the resource curse, as 86% percent of its exports to China are primary commodities instead of diversified manufactured products. On the other hand, Gallagher states that South America averages 56% primary commodities and 40% manufactured goods exported to the rest of the world.[50] This breakdown highlights the potential for atrophy of manufacturing jobs in South America as commodity exports increase. Not only does this create lead to de-industrialization, but commodities are more susceptible to shocks than manufactured goods and can lead to more severe economic downturns.

Further highlighting the potential for South American countries to be susceptible to commodity shocks is the fact that a significant portion of the Chinese loans have gone towards the energy sector—mainly oil. The China-Latin America Finance Database shows, in Figure 5, which sectors have received the most financing.

48 Eugene Gholz, Umul Awan, and Ehud Ronn, "Financial and Energy Security Analysis of China's Loan-for-Oil Deals," *Energy Research & Social Science* 24, no. Supplement C (February 1, 2017): 49.

49 Gallagher, *The China Triangle: Latin America's China Boom and the Fate of the Washington Consensus*, 45.

50 Gallagher, 45.



TYPE	NO. OF LOANS	AMOUNT
Energy	31	$100B
Infrastructure	24	$24.3B
Other	19	$14.8B
Mining	3	$2.1B

Figure 5. Purpose of Chinese Loans in Latin America.[51]

The data shows that 71% of Chinese loans have gone to energy, 17% to infrastructure, 10% to "other," and merely 1% to mining. Downs claims that the focus on energy reinforces the fact that all of CDB's projects must be approved by China's State Council and therefore disproportionately align with the party's agenda to secure long-term energy contracts.[52] Furthermore, it provides Chinese national oil companies (NOCs) with opportunities for exploration and production overseas since domestic reserves are insufficient for China's needs. China also benefits from acquiring and maintaining a technological edge in the oil industry while producing significant oil revenues for the state abroad.

Although oil is only China's fourth-largest import from the region, the country has made its largest loans in exchange for oil and energy security. The growing Chinese middle class will demand more energy to feed new cars and appliances as well as for the production of other goods that a country of 1.4 billion people will come to expect. A common argument is that the Chinese economy's growth rate will slow and oil demand may decrease. Despite China's decline from double-digit GDP growth toward 6 or 7% in 2016, it was four times

51 "Inter-American Dialogue," China-Latin America Finance Database, accessed January 24, 2018, https://www.thedialogue.org/map_list/.

52 Downs, *Inside China, Inc: China Development Bank's Cross-Border Energy Deals*, 80.

the growth rate of the United States. Additionally, Qiang Wang and Rongrong Li claim, "China's oil consumption will continually increase from 10.7 million barrels per day (bpd) in 2020, then to 16.9 million bpd in 2030, and then to 20.0 million bpd in 2040."[53] Figure 6 reaffirms that the country's oil needs have increased 14% since 2016 and are not likely to decrease any time soon.

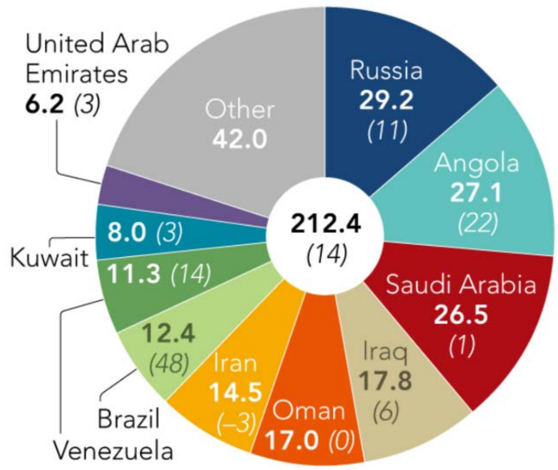


Figure 6. 2017 Chinese Crude Oil Imports (Millions of Tons).[54]

Not only does Figure 6 show the increase in oil imports to China, but it also shows that Middle Eastern shares of oil exports are not growing as quickly as those from South America and Africa. This trend has two implications. First, China is decreasing its dependence on Middle Eastern oil, which is susceptible to wars, blockades of the Strait of Hormuz, and regional confrontations with the U.S. military. Second, and more important to the Western Hemisphere, is the fact that China is using its excess foreign exchange reserves to reduce over-reliance on investments in U.S. bonds. Instead, it is diversifying its

[53] Qiang Wang and Rongrong Li, "Sino-Venezuelan Oil-For-Loan Deal – The Chinese Strategic Gamble?#," *Renewable and Sustainable Energy Reviews* 64, no. Supplement C (October 1, 2016): 818.

[54] Tyler Durden, "De-Dollarization Accelerates: China Readies Yuan-Priced Crude Oil Benchmark Backed By Gold," Zero Hedge, accessed January 24, 2018, https://www.zerohedge.com/news/2017-09-02/de-dollarization-accelerates-china-readies-yuan-priced-crude-oil-benchmark-backed-go. Note: Parenthesis denote oil imports percentage change from 2016 data.

foreign exchange reserves with natural resources in regions where it can use those same funds to both secure resources and build potential strategic partnerships and alliances through long-term loan arrangements.

Not only have some South American countries wanted to shift their investment portfolios from the United States after the 2008 financial crisis, but China also wishes to diversify against its holdings of U.S. bonds. But, Gholz et al. state that China provides subsidized loans in exchange for oil by paying higher-than-market prices for the oil, which would not be a good investment strategy if it were trying to reduce its holdings in U.S. treasuries.[55] It is easy to see why South American countries want to partner with China if they are guaranteed large sums of money over a long period of time and with the assurance that they will be paid near-current-market prices for oil over the term of the loan. Gholz et al. also state, "Chinese officials acknowledge the safety and reliability of U.S. Treasury bonds, where they have invested some $1.16 trillion, but they hope to slowly reduce the proportion of their reserves allocated to U.S. Treasuries."[56] They do not agree, however, that China intends for economic reasons to reduce its holdings of U.S. securities in favor of oil. Instead, it seems that it has adjusted its portfolio for geo-economic reasons, such as to increase trade linkages and to develop new, untapped markets.

Furthermore, the One Belt, One Road (OBOR) initiative is designed to reduce the country's excess capacity and employ thousands of Chinese citizens by building a network of roads to link western China with much of Southwest Asia, the Middle East, and even Europe. Similar to this project are many large projects under way in Latin America to meet Chinese labor demands. These projects also allow it to create trade linkages to regions that are underdeveloped and could mutually benefit from China's excess capacities in steel, labor, and cheap exports. Communist party leadership fears that if they are not able to continue high growth rates, the rising middle class may slump back into poverty, potentially causing widespread rioting across the country and even contestation of the communist party.

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55 Gholz, Awan, and Ronn, "Financial and Energy Security Analysis of China's Loan-for-Oil Deals," 46.

56 Gholz, Awan, and Ronn, 46.

Construction has outpaced demand, indicating that either a) excess capacity was used to create employment at any cost to avoid political unrest or b) China plans to dramatically urbanize more of the country as rural citizens are incrementally allowed by the Communist Party to migrate to these cities. Richard Gray states that the Chinese have built more than 50 cities that are not currently inhabited or being utilized ("ghost cities") and between 2011 and 2013, China used more concrete than the United States used in all of the 20th century.[57] This is further reasoning for China to seek infrastructure projects in Latin America to keep Chinese firms engaged and citizens employed worldwide as its own economy has reached saturation. On the other hand, this phenomenon indicates that China is preparing its cities to continue to dominate the manufacturing and technical industry while relying on raw materials from abroad to supplement urban agricultural and extractive industries.

Ultimately, China is planting deep financial roots in South America that will not likely be uprooted anytime soon. Heriberto Araujo and Juan Pablo Cardenal put it best: "By buying companies, exploiting natural resources, building infrastructure and giving loans all over the world, China is pursuing a soft but unstoppable form of economic domination."[58] Whether China has intentionally funded anti-American regimes in South America or simply meant to purchase more shares of oil, the Communist Party's influence will likely be felt for many years to come. Additionally, if South America enjoys more growth from the Chinese model over the next decade, U.S. influence in the region will be greatly threatened because it failed to perform for South America from the 1980s to the turn of the 21st century.

D. LATIN AMERICA'S INTEREST IN CHINESE INVESTMENT

As left-leaning leaders, such as President Hugo Chavez of Venezuela, President Evo Morales of Bolivia, and President Rafael Correa of Ecuador, teamed up to form the Bolivarian Alliance of the Americas (ALBA), it was evident that South America was

57 Richard Gray, "China's Zombie Factories and Unborn Cities," BBC, February 23, 2017, http://www.bbc.com/future/story/20170223-chinas-zombie-factories-and-unborn-cities.

58 Heriberto Araújo and Juan Pablo Cardenal, "China's Economic Empire," *New York Times*, June 1, 2013, https://www.nytimes.com/2013/06/02/opinion/sunday/chinas-economic-empire.html.

largely detesting U.S. policies. This Bolivarian movement was formed to unite South America by forming the Southern Cone Common Market (MERCOSUR) or the common market of the South. This detachment was additionally favored by President Luiz Inacio Lula da Silva of Brazil and President Cristina Kirchner of Argentina and began further pronounced as the Free Trade Agreement of the Americas failed to launch. Argentina, Bolivia, Brazil, and Venezuela had opposed the free trade agreement that was supposed to mirror that of the North American Free Trade Agreement (NAFTA) due to worries of U.S. agricultural subsidies destroying agricultural jobs in their countries. Additionally, they feared that U.S. multinational corporations would not pay the local citizens their fair share of profits in the region, while exporting raw materials and leaving barren wasteland.[59]

China's reserves came at an once-in-a-lifetime opportunity to fill the Western cash cow's void as the 2008 financial crisis hit and South America sought funding. The cash offerings that China now proposes to the international community have become more appealing to many foreign countries than compared to the Western led Bretton Woods institutions—due to traditional loans having shorter terms, higher interest, and more stipulations. China's going out, coupled with cash, has built many megastructures abroad to further Chinese prestige around the world. Eric Helleiner and Jonathan Kirshner state that monetary power becomes more apparent as a country is able to export sizable capital and provide crisis financing.[60] This occurred post-2008 financial crisis as less developed countries latched onto Chinese loans as the United States focused on fixing their financial mess and restricted their loan process, while China liberally opened their loan floodgates with sizable loans capable of completing almost any task imaginable.

South America was attracted to Chinese investment mostly to attempt something other than what had not been working for them during the Washington Consensus—1980s to the turn of the 21st century. Additionally, Chinese banks became more enticing to the world as China's lack of conditionality and non-interventionist attitude was portrayed to

59 "The World's Largest Trade Zone That Never Happened," The Balance, accessed October 24, 2017, https://www.thebalance.com/ftaa-agreement-member-countries-pros-and-cons-3305577.

60 Eric Helleiner and Jonathan Kirshner, *The Great Wall of Money: Power and Politics in China's International Monetary Relations* (Ithaca—London : Cornell University Press, 2014), 25.

countries that were tired of meeting U.S. demands of maintaining particular levels of democratic processes and deficit reduction policies. The World Bank had increased conditions that recipient countries needed to meet in the 1980s to protect the World Bank's assets as well as ensuring effective outcomes of its loans. In the case of South America, loans were riskier than usual and significant conditions were placed on them. Diego Hernandez claims these efforts were aimed at taming economic imbalances and establishing a foundation for long-term growth.[61] However, long-term growth was usually lacking and thus South America's search for alternative methods.

As economic conditions in South America weakened, with correlating weakening relations with the United States, it is likely that South America witnessed African success stories of Chinese investment. Adrienne Klasa states that in 2015, China was only the ninth largest contributor of capital investment in Africa but more importantly ranked seventh for the number of projects there. The Chinese also created over 14,000 jobs in Africa and more than any other country.[62] These findings will likely continue to give hope to other regions, such as South America, who hope to benefit from more jobs, growth, and infrastructure development.

The China boom, or also known as the "commodity lottery" for Latin America as coined by Gallagher, occurred from 2003 to 2013. It benefited much of Latin America as China's appetite for natural resources and attached infrastructure projects fueled 3.6% average economic growth per year in Latin America. On the other hand, the Washington Consensus was implemented in Latin America in 1982, and for nearly two decades averaged only 2.4% growth per year and ended with the 2008 financial crisis, according to Gallagher.[63] Most of the growth during the China boom was due to the increase in commodity exports, fueled by China's demand for resources and agricultural products.

61 Diego Hernandez, "Are 'New' Donors Challenging World Bank Conditionality?," January 2016, 6, http://docs.aiddata.org/ad4/pdfs/wps19_are_new_donors_challenging_world_bank_conditionality.pdf.

62 Adrienne Klasa, "The Africa Investment Report - 2016," *This is Africa*, 2016, 7, https://www.camara.es/sites/default/files/publicaciones/the-africa-investment-report-2016.pdf.

63 Gallagher, The China Triangle: Latin America's China Boom and the Fate of the Washington Consensus, 2.

China has met South America's financial needs as western banks have been outbid by Chinese banks. Figure 7 shows that the top five Latin American recipients of Chinese loans are all in South America and account for over 95% of Chinese loans in Latin America.

Figure 7. Chinese Loans: Quantity and Amount by Latin American Country.[64]

64 "Inter-American Dialogue."

The data indicates that economic ties are growing deeper with China in South America. Research on China's increase in aid to Africa found that fewer conditions were placed on the same countries, by the World Bank, due to competition with Chinese banks. However, Hernandez states that maintaining transparency, fighting corruption, and increasing democracy were found to be more challenging.[65] Although circumstances in Africa may be different than South America's, there is an argument to be made that South America is more susceptible to corruption and a decrease in democracy and transparency due to less restrictions on loans as Chinese loans have increased competition and lowered conditionality for investment.

Despite South America's excitement for the rapid economic growth during the last decade, it raises the question of how long it will last, as economic growth may be temporary as commodity boom and bust cycles go and come. Gallagher states, "During the Washington Consensus period Latin American governments put an end to high inflation and fiscal irresponsibility. What is more, the period ushered in a return to democracy."[66] It is evident that an authoritarian regression has occurred in Venezuela as Chinese funding boosted Chavismo and now propels Maduro's ambitions to rewrite the constitution and ensure the extension of his power. However, what is yet to be seen is how freedom and democracy will be affected in Argentina as investment shifts, between two completely different forms of government, to finance President Macri's center-right and business oriented administration.

65 Hernandez, "Are 'New' Donors Challenging World Bank Conditionality?," 5.

66 Gallagher, The China Triangle: Latin America's China Boom and the Fate of the Washington Consensus, 5.

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III. VENEZUELA'S TRADE AND INVESTMENT FAILURES WITH CHINA: A CASE STUDY

> "This country will eventually fall into the hands of the unbridled mob, and will proceed to almost imperceptible petty tyrannies of all complexions and races."
>
> —Simon Bolivar

> "It is the devil's excrement. We are drowning in the devil's excrement."
>
> —Juan Pablo Perez Alfonso, former Venezuelan oil minister

Poor relations between the United States and Venezuela, coupled with the 2008 financial crisis, aligned China's state-owned development banks with Venezuela's socialist, anti-American president—Hugo Chavez. This chapter provides the background for Chinese energy security needs and the void the Chinese filled as the anti-American rise occurred in Venezuela. Finally, the last section debates whether or not the Sino-Venezuelan relationship benefits Venezuela.

A. CHINA'S INTERESTS IN VENEZUELA

As President Chavez was cutting ties with Bretton Woods institutions and distancing his country from U.S. influence, China was more than willing to use its influence and economic power to fill the gap. As Christopher Balding states, "China's interests in gaining friends in the Western Hemisphere while securing access to oil overlapped with Venezuela's interest in diversifying its customer base away from the United States."[67] These conditions allowed China to gain a foothold in the Western Hemisphere, while shielding Venezuela from U.S. politics.

China's important financial reserves allow their NOCs to invest in risky regions where private firms are currently not willing to enter or where entry is not possible or even granted. According to Deborah Brautigam and Kevin Gallagher, "in countries without good credit ratings, a resource guarantee increases security and lowers risk, and allows projects

[67] Christopher Balding, "Venezuela's Road to Disaster Is Littered with Chinese Cash," *Foreign Policy*, 2017.

to be financed at a reasonable interest rate."[68] China was convinced that investment risk in Venezuela could be minimized by securing their funding through "resource-secured" financing.

For example, China National Petroleum Company (CNPC) and Petróleos de Venezuela, S.A. (PDVSA) began talks in 2009 and have signed more agreements in 2017, allowing China to build the Nanhai 400,000 bpd refinery that will be located in Jieyang, Guangdong Province, China. The joint venture of CNPC-PDVSA has already teamed up in Venezuela's Orinoco heavy belt to form Petrourica and Petro Sinovensa. Venezuelan heavy crude will be processed in the Chinese refinery and operations are slated to begin upon completion in 2020, according to Robert Brelsford.[69] This benefits the Chinese and enables Venezuela to eventually not have to rely on exporting crude to American refineries, shielding Venezuela from the U.S. economy and sanctions.

Despite China's efforts to tap into the world's largest oil reserves, the Chinese have found it to be extremely difficult, as the United States has experienced, to be profitable in Venezuela. Oil production is at a 23-year low, oil rig counts are decreasing drastically and oil shipments are late. Other investments in railways and infrastructure have been terminated. For example, Simon Romero states that Chavez intended for a 290 mile, high-speed railway to be built and functioning as of 2012 but as of 2017, the Chinese have packed up and left the project incomplete as Venezuela's economy has failed.[70] Additionally, John Perry claims, 350,000 homes have been built between 2011 and 2012, to try and meet Chavez's lofty goal of three million homes by 2019.[71] This accomplishment

68 Deborah Brautigam and Kevin P. Gallagher, "Bartering Globalization: China's Commodity-Backed Finance in Africa and Latin America," *Global Policy* 5, no. 3 (September 2014), https://doi.org/10.1111/1758-5899.12138.

69 Robert Brelsford, "Venezuela, China Advance Plans for Chinese Refinery," *Oil & Gas Journal*, June 12, 2017, https://www.ogj.com/articles/2017/06/venezuela-china-advance-plans-for-chinese-refinery.html.

70 Simon Romero, "China's Ambitious Rail Projects Crash Into Harsh Realities in Latin America," *New York Times*, October 3, 2015, https://www.nytimes.com/2015/10/04/world/americas/chinas-ambitious-rail-projects-crash-into-harsh-realities-in-latin-america.html.

71 John Perry, "Lessons From Latin America: The Case for Public Investment in Housing," *Guardian*, June 6, 2013, http://www.theguardian.com/housing-network/2013/jun/06/public-investment-housing-venezuela.

was applauded back in 2013 but four years later after massive socialist expenditures and low oil prices, the country is in shambles. Daniel Lansberg-Rodriguez claims that China is now trying to salvage its largest loans and investments in Venezuela—China's largest debtor—and hoping that Maduro's replacements are Chavistas, who will not claim odious debt due to unlawful legislation of acquiring it in the first place.[72]

The mere existence of vast quantities of oil in Venezuela makes a complementary arrangement for China and Venezuela to depend on one another. However, poor relations between the United States and Venezuela, coupled with the 2008 financial crisis, further aligned China's state-owned development banks with Venezuela's socialist, anti-American president. Additionally, these conditions enabled China to gain a foothold in the Western Hemisphere, while shielding Venezuela from U.S. politics. Furthermore, Balding states, "China's interests in gaining friends in the Western Hemisphere while securing access to oil overlapped with Venezuela's interest in diversifying its customer base away from the United States."[73]

China's massive financial reserves allow its NOCs to invest in risky regions that private firms are not willing to enter or where entry is not possible. China was convinced that investment risk in Venezuela could be minimized by securing their funding through "resource-secured" financing.[74]

B. VENEZUELA'S INTERESTS IN CHINA

As nationalism rose with the economic decline in the late 1990s, Chavismo was born in 1999. Soon after Chavez's election, he began to expel foreign investment and to give the state larger control over Venezuela's number one revenue source: oil. Venezuela

72 Daniel Lansberg-Rodríguez, "Exit the Dragon: Why China Should Stop Supporting Venezuela," *New York Times*, February 15, 2017, https://www.nytimes.com/2017/02/15/opinion/exit-the-dragon-why-china-should-stop-supporting-venezuela.html.

73 Balding, "Venezuela's Road to Disaster Is Littered with Chinese Cash."

74 Brautigam and Gallagher, "Bartering Globalization: China's Commodity- Backed Finance in Africa and Latin America," 346.

has the largest estimated oil reserves in the world: more than 298 billion barrels.[75] Venezuela relies on oil for 96% of its export revenue.[76] Chavez's efforts were to regain control of its prized commodity from international oil companies (IOCs) because they seemed to primarily benefit U.S. companies. His administration promised to return the profits to Venezuela's citizens. However, Michael Ross states, "IOCs were generally blamed for problems within developing oil countries prior to the 1970s and then most countries nationalized their oil industries in the 19701s but the resource curse and ill effects of oil have not resulted in more efficiencies and these countries that have nationalized are worse off today.[77]

The majority of oil-rich developing countries nationalized their oil sectors in the 1970s, including Venezuela, which nationalized its oil in 1976 and formed PDVSA, according to Matt Smith.[78] Later, according to Mamdouh Salameh, "Venezuela re-opened its upstream oil sector [in the 1990s] to private investment. This policy facilitated the creation of 32 operating service agreements and four strategic associations, each operated by a non-PDVSA entity. In recent years, Venezuela has moved to largely undo most of these initiatives."[79] Because the regime did as much as possible to nationalize the oil industry and force foreign industry out of the country, Chavez also relied on Chinese investment to make possible the transition and "Bolivarian revolution."

As oil prices rose during the early 2000s and the Chavez regime enjoyed a surplus of petrodollars, it was in the regime's best interests to fund a variety of social programs to gain support for his Bolivarian revolution. Chavez set up several Bolivarian Missions and

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75 "The World's Largest Oil Reserves By Country," *WorldAtlas*, accessed October 10, 2017, http://www.worldatlas.com/articles/the-world-s-largest-oil-reserves-by-country.html.

76 "Venezuela Overview," World Bank, May 2, 2017, http://www.worldbank.org/en/country/venezuela/overview.

77 Michael Ross, *The Oil Curse: How Petroleum Wealth Shapes the Development of Nations* (Princeton: Princeton University Press, 2012), 4.

78 Matt Smith, "Venezuelan Oil and Hugo Chavez: A Tangled Tale," CNBC, October 8, 2012, https://www.cnbc.com/id/100373746.

79 Mamdouh G. Salameh, "China's Oil 'Adventure' into Venezuela," *International Association for Energy Economics*, no. Second Quarter (2011): 17.

he launched efforts to develop better public infrastructure that would both benefit the impoverished. One example of the Bolivarian Missions was a program called "Gran Volumen," or Great Volume, which operated under the banner of "Mi Casa Bien Equipada," or My Well-Equipped Home. The program put into the hands of poor citizens such Chinese products as washers, dryers, televisions, DVD players, stoves, and the like, according to Fidel Vasquez I.[80] These initiatives were popular for the masses and boosted support for Chavismo. These Bolivarian Missions also benefitted the Chinese because they increased the flow of Chinese exports to South America as well as provide opportunities for Chinese companies to win contracts to build homes, railways, and other large infrastructure projects.

President Chavez's Bolivarian revolution took full control of PDVSA in the early 2000s, thus channeling PDVSA's revenues to fund his new social programs. In 2004, two-thirds of PDVSA's budget went to these programs. Furthermore, high oil prices in the mid-2000s expedited Chavez's agenda, and Chinese funding further supported his populist programs; whether China intentionally backed them or not, Chinese loans and investments were instrumental in maintaining support for the regime as oil prices plummeted in mid-2008. These windfalls helped feed Chavez's socialist policies and helped him achieve the popularity he needed to stay in power. As Francisco Monaldi states, "the consumption bonanza, allowed by the increasing imports that were fueled by the surge in oil export revenues and the increase in foreign debt, enabled the president to have relatively high levels of popularity and easily win re-elections in 2006 and 2012."[81]

Additionally, the nationalization of PDVSA enabled Chavez to purchase in 2007 a majority share of oil projects in the Orinoco belt for $30 billion, which caused

[80] Fidel E. Vásquez I, "1.200.000 Electrodomésticos Han Sido Distribuidos Por Mi Casa Bien Equipada," Aristóbulo Istúriz, March 16, 2012, http://aristobulo.psuv.org.ve/2012/03/16/canpana/1-200-000-electrodomesticos-han-sido-distribuidos-por-mi-casa-bien-equipada/.

[81] Francisco J. Monaldi, "Is Resource Nationalism Fading in Latin America? The Case of the Oil Industry," Issue Brief, no. 09.03. 14 (2014): 7, https://scholarship.rice.edu/bitstream/handle/1911/91732/F._Monaldi._Columbia._Impact_of_the_Decline_in_Oil_Prices_on_Venezuela_September_2015.pdf?sequence=1.

ConocoPhillips and ExxonMobil to leave Venezuela.[82] Furthermore, in 2010 he seized 11 oil rigs belonging to U.S. company Helmerich & Payne Inc.[83] Oil nationalization seemed to be largely effective due to abnormally high oil prices generating enormous state revenues during the commodity boom, which gave Venezuela more financial freedom from foreign companies than dependence on them.

C. CHARACTERISTICS OF CHINA'S ATTRACTIVE LOANS (THAT LEAD TO INCREASED INVESTMENT)

Despite the oil boom, Venezuela was determined to create a coalition with China that would free it from U.S. influence. Chinese loans began in 2007 and increases in Chinese investment followed after the 2008 financial crisis.

The majority of Chinese loans take the form of loans-for-oil from the state-owned CDB, while others are linked to infrastructure investment in exchange for oil. Venezuela receives the money up front to use as the government pleases and then ships oil to China. China pays for that oil at current market prices and places the revenues in a Chinese state-owned bank and either uses the oil at home or sells it to other lucrative markets. Managers of the Chinese fund deduct payments for loan principal and interest from the oil revenue until its loan to Venezuela is paid in full. Figure 8 shows all of the loans that China has provided Venezuela from the first in 2007 to the latest in 2016. Since 2016, Venezuela has been struggling to meet its debt payments, and, according to open sources, China has made no further loans. Jack Stubbs and Deisy Buitrago argue, however, that Russia has made concessions to Venezuela to restructure debt to ease the burden, and China's foreign ministry has stated that it will treat the debt situation "appropriately."[84]

82 Ross, *The Oil Curse: How Petroleum Wealth Shapes the Development of Nations*, 61.

83 "Factbox: Venezuela's Nationalizations Under Chavez," Reuters, October 8, 2012, https://www.reuters.com/article/us-venezuela-election-nationalizations/factbox-venezuelas-nationalizations-under-chavez-idUSBRE89701X20121008.

84 Jack Stubbs and Deisy Buitrago, "Venezuela Wins Russia and China Backing as It Says It Is Honoring Debt," Reuters, November 16, 2017, https://www.reuters.com/article/us-venezuela-debt/venezuela-wins-russia-and-china-backing-as-it-says-it-is-honoring-debt-idUSKBN1DF2WC.

DATE	TYPE	PURPOSE	LENDER	AMOUNT
November 2007	Energy	Joint Fund - Tranche A	China Development Bank	$4B
April 2009	Energy	Joint Fund - Tranche B	China Development Bank	$4B
December 2009	Energy	Not specified	China Ex-Im Bank	$500M
December 2009	Mining	Mining project credit	China Development Bank	$1B
May 2010	Other	Trade-related credit facility	CDB and Portugal's BES	$1.1B
August 2010	Energy	Joint Fund - Long-Term Facility	China Development Bank	$20.3B
June 2011	Energy	Joint Fund - Tranche A renewal	China Development Bank	$4B
November 2011	Energy	Abreu e Lima refinery	China Development Bank	$1.5B
February 2012	Energy	Purchase of oil-related products	China Development Bank	$500M
August 2012	Energy	Joint Fund - Tranche B renewal	China Development Bank	$4B
June 2013	Energy	Sinovensa production in Orinoco	China Development Bank	$4B
September 2013	Mining	Las Cristinas gold mine	China Development Bank	$700M
September 2013	Infrastructure	Pequiven marine terminal	China Ex-Im Bank	$391M
November 2013	Energy	Joint Fund - Tranche C	China Development Bank	$5B
July 2014	Infrastructure	Joint Fund - Tranche A renewal	China Ex-Im Bank	$4B
April 2015	Energy	Joint Fund - Tranche B renewal	China Development Bank	$5B
November 2016	Energy	Oil sector development	China Development Bank	$2.2B

Figure 8. Chinese Loans to Venezuela.[85]

The majority of the loans are directed towards the energy sector. There are a couple smaller loans involving the mining sector as well as two loans focused on infrastructure. Despite the fact that China was considering cutting financial ties with Venezuela in 2016, PDVSA signed agreements with the CDB again in June 2017 to finance potentially 700 other projects with Venezuela, many being in the oil sector, according to Brelsford.[86] However, all the loans serve the same purpose of extracting resources for China to import them more quickly and efficiently back home.

As far as Venezuelan politics are concerned, much of the loans went into the FONDEN fund or Venezuela's national development fund. According to Antulio Rosales, "Official estimates show that the Venezuelan government has invested over

85 Gallagher, "Inter-American Dialogue."

86 Brelsford, "Venezuela, China Advance Plans for Chinese Refinery."

USD 115 billion through FONDEN in various infrastructure, productive and social projects and, generally, over USD 600 billion have been invested in social spending in the past 14 years of Bolivarian government."[87] He further suggests that FONDEN has been a source of embezzlement and highly difficult for critics to scrutinize. Without the conditions that Bretton Woods institutions placed on loan agreements, Chinese loans make it easy for Venezuela's government to not have to answer to anyone, which can lead a regime to become more authoritarian in nature. Furthermore, Pedro Palma, a Venezuelan economist, argues that "the Venezuelan government feels it has the right to loot resources from the Central Bank and PDVSA" and that the funds "are resources for which the Central Bank and PDVSA receive no compensation at all and end up spent discretionally by the President."[88]

Chinese loans to Venezuela increased dramatically since the 2008 financial crisis and provided Venezuela with "patient capital" versus short-term capital with its associated restraints according to Kaplan.[89] He also states, "Unlike the short-term horizon of private market capital, patient capital is characterized by both a long-term horizon and long-term relationships."[90] Chinese patient capital allows anywhere from 2 to 28.5 year term agreements, which is much longer than Bretton Woods institutions' loan terms and therefore, are more appealing to regimes seeking long-term survival, according to Brautigam et al.[91] This shadow of the future, coupled with fewer stipulations, provides hope for countries, such as Venezuela, to allow projects to mature and come to fruition without fear of intervention by the United States, IMF, or World Bank.

Although loans and investments are distinct, China provides both to Venezuela. Between 2005 and 2016, Chinese investments totaled $20.74 billion piling on top of the

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87 Antulio Rosales, "Deepening Extractivism and Rentierism: China's Role in Venezuela's Bolivarian Developmental Model," Canadian Journal of Development Studies 37, no. 4 (October 1, 2016): 545.

88 Rosales, 565.

89 Kaplan, "Banking Unconditionally: The Political Economy of Chinese Finance in Latin America," 2.

90 Kaplan, 643.

91 Brautigam and Gallagher, "Bartering Globalization: China's Commodity- Backed Finance in Africa and Latin America," 350.

$62.2 billion loan debt. The energy sector had $11 billion of Chinese investment, followed by $2.45 billion in the construction sector, and $1.49 billion in agriculture.[92] With the crisis underway in Venezuela, investments in the energy sector continued to climb to $4.58 billion from 2015–2016. These investments were likely mandated by the Chinese government to ensure its other loans—tied to energy security—would not be lost, as the China Energy Engineering Corporation (CEEC) and CNPC further invested in the troubled economy.

D. RESULTS OF THE SINO-VENEZUELAN RELATIONSHIP

China's loans-for-oil as well as Chinese investments have created an environment that has allowed the situation in Venezuela to deteriorate rapidly due to China's non-interventionist attitude and Venezuela's authoritarian style of leadership, which result in fewer mediums for answering to the voice of Venezuelan citizens. The proper economic controls are not in place to maintain a country where all can benefit in the long-term. On the contrary, short-term windfalls have created patrimonial relationships to win votes and fuel the regime. Safeguards have been eroded as the rewriting of the Venezuela constitution, laws, and makeup of its country have occurred and China does not seem to care that these regressions have occurred.

Chinese resource-secured loans have been the lifeline for the Venezuelan government as crude oil production has plummeted. According to Lucia Kassai and Sheela Tobben, crude production hit a 29-year low in 2017.[93] Chinese financing has further enabled President Maduro to further his ambitious restructuring of the Venezuelan government—while avoiding a coup—even as inflation hit a record high of 800% in December 2016.[94] The military has taken control over scarce food supplies and it seems

92 "Chinese Investment Dataset - China Global Investment Tracker," American Enterprise Institute, July 8, 2015, http://www.aei.org/china-global-investment-tracker/.

93 Lucia Kassai and Sheela Tobben, "Venezuelan Oil Output Heads to 29-Year Low," Bloomberg.com (Bloomberg, November 10, 2017), https://www.bloomberg.com/news/articles/2017-11-10/venezuelan-oil-output-heads-to-29-year-low-as-cash-crunch-grows.

94 "Venezuela Inflation Rate," Trading Economics, accessed February 11, 2018, https://tradingeconomics.com/venezuela/inflation-cpi.

likely that the military will continue to receive the money it needs to remain loyal to Maduro's regime. There is no transparency in the loans, which allows Maduro to channel funds as he deems necessary. As Michael Todaro and Stephen Smith state, "some economists argue that greater openness to trade beneficially affects the subsequent evolution of institutions."[95] As Chinese investment has increased with Venezuela, there is an argument to be made that Chinese styles of governance are also spilling over into Venezuela's government styles.

Not only have funds been used for social projects and to boost the military, but with the intent to gain the popular vote. This suggests that many people were benefiting from Chinese funding during the China boom, since they were sufficiently happy and willing to continue voting for Chavez. However, Jorge Giordani, President Chavez's Planning Minister for 10 years, claims that in order for Chavez to have won his third election in 2012, extreme amounts of money had to be utilized.[96] This new source of revenue has both allowed the Venezuelan regime to prolong their agenda and power, while shaking off the chains of the World Bank. Even though the World Bank has heavy stipulations on loans, there is room for corruption within these fairly transparent loans. For example, Hernandez states, "while the World Bank has the fundamental interest to use conditionality as an instrument to ensure the effectiveness of its projects, the recipient government might turn to the World Bank for financial assistance to remain in office and implement a set of preferred policies while in power."[97] Since Chinese loans have fewer stipulations and less transparency, there is a significant opportunity for increased levels of corruption.

Chinese investment has been an enabler of the populist regime, as development funds have poured into Venezuela at opportune times to boost social programs and populist support. Additionally, the loans have not been adequately used to boost Venezuela's oil industry. Furthermore, it is surprising that the industry is it its current condition given that

95 Michael Todaro and Steven Smith, *Economic Development* (Boston: Addison Wesley, 2008), 87.

96 Rosales, "Deepening Extractivism and Rentierism: China's Role in Venezuela's Bolivarian Developmental Model," 565.

97 Hernandez, "Are 'New' Donors Challenging World Bank Conditionality?," 7.

$3.29 billion of investments have been specifically earmarked for PDVSA.[98] It is the appeal of the long-term, unconditional loans that give Venezuela's populist regime room to maneuver as it sees fit, while leading to disastrous results as the government has done a poor job of managing its crown jewel—PDVSA. The NOC is in shambles. Although Caracas is failing to maintain ageing oil industry infrastructure and failing to provide incentives for qualified oil industry technicians and businesses, China's non-interventionist posture has not benefited Venezuelan citizens. China has too much money at stake to publicly pressure the regime to step down in order to give Venezuelans their voice back. If regime change occurred, Venezuelans would likely claim odious debt and China would be forced to incur large losses.

For example, two-thirds of PVDSA's budget went to social programs in 2004 according to Ross.[99] Although oil prices were high, Venezuela did not invest money back into ageing refineries, rigs, and oil tankers, but spent unreasonably high amounts of the budget in low cost housing, medicine, education, and other similar programs, to boost the popularity of Chavismo. To further demonstrate, as Chavez was seeking a third six-year term, he tapped into the $20 billion Chinese loan to help turn the vote. According to Downs, "Chávez announced on September 21, 2010—less than a week before the legislative elections—that $1 billion from CDB's loan would be used to finance the construction of 25,000 houses for people living in the slums of Caracas, traditional Chávez strongholds where the president's popularity has been waning."[100]

As Venezuela is trying to make loans-for-oil payments back to China, there is less and less of a margin for profit from their oil due to the price collapse of oil in 2014. Rosales states it best: "Venezuela's appropriation of oil rents is changing radically, whereby it is spending today tomorrow's rents."[101] Figure 9 shows how Venezuela is even late on large shipments of oil to China due to a shrinking supply of oil.

98 "Chinese Investment Dataset—China Global Investment Tracker."

99 Ross, *The Oil Curse: How Petroleum Wealth Shapes the Development of Nations*, 61.

100 Downs, *Inside China, Inc: China Development Bank's Cross-Border Energy Deals,* 95.

101 Rosales, "Deepening Extractivism and Rentierism: China's Role in Venezuela's Bolivarian Developmental Model," 573.

REFINED PRODUCTS

COUNTRY	PARTNER	PRODUCT	CARGO VOLUME	TOTAL MONTHLY VOLUME	DELAYED/CANCELLED CARGOES	TOTAL DELAYED VOL
China - Tranch A	PetroChina	Jet fuel	240,000	240,000	11	2,640,000
China	China Oil	Jet fuel	240,000	240,000	10	2,400,000
Russia - Credit line 1	Rosneft	ULSD	240,000	480,000	6	1,440,000
Russia - Credit line 1	Rosneft	Jet fuel	240,000	480,000	5	1,200,000
Russia - Credit line 2	Rosneft	Jet fuel	240,000	480,000	4	960,000
Russia - Credit line 2	Rosneft	ULSD	240,000	480,000	3	720,000
China - Tranch B	PetroChina	Jet fuel	240,000	240,000	2	480,000
China - Tranch A	PetroChina	Fuel oil	500,000	1,000,000	0	0
China - Tranch B	PetroChina	Fuel oil	2,000,000	2,000,000	0	0
China	ZhenhuaOil	Fuel oil	2,000,000	2,000,000	0	0
Russia - Credit line 1	Rosneft	Fuel oil	2,000,000	2,000,000	0	0

CRUDE OIL

COUNTRY	PARTNER	PRODUCT	CARGO VOLUME	TOTAL MONTHLY VOLUME	DELAYED/CANCELLED CARGOES	TOTAL DELAYED VOL
China - Loan I	CNPC	Boscan	800,000	1,600,000	4	3,200,000
China - Loan I	CNPC	Merey 16	1,800,000	7,200,000	0	0
Russia	Lukoil	Merey 16	500,000	500,000	0	0
Russia	Lukoil	Bachaquero/Boscan	400,000	800,000	0	0

Figure 9. Venezuela's Late Oil Shipments to China and Russia.[102]

The data shows that Venezuela's oil refining capability is behind as it is unable to ship its oil commitments to its largest debtor despite being the largest recipient of Chinese loans in the world. Venezuela's late shipments of crude oil are problematic but what is even more worrying is Venezuela's degenerative capability for producing higher value-added, refined oil shipments. Currently Venezuela is late on 23 cargo shipments of refined

102 "Oil Quotas to Venezuela's Allies," Reuters, accessed October 31, 2017, http://fingfx.thomsonreuters.com/gfx/rngs/VENEZUELA-OIL/010031RJ41B/index.html.

crude to China, while only late on four shipments of plain crude. With China building refineries in China as well as their NOCs owning significant portions of oil companies and refineries around the globe, it is likely that China prefers crude oil shipments. This enables its NOCs to further refine the oil and sell it for higher value-added on the world market, while Venezuela loses out in that profitable process.

PDVSA is also unable to pay for parts and maintenance of oil rigs to pump the oil, so few oil rigs are supplying oil to the company—and therefore the regime and country as a whole. According to Figure 10, in September 2015, 74 rigs were supply oil and in June 2017, only 49 were supplying oil. Marianna Parraga and Mircely Guanipa state that workers from PDVSA claim that "the problems have particularly affected crude units as oil has been diverted away from some PDVSA's refineries to pay foreign debts, leaving insufficient feedstock for distillation."[103]

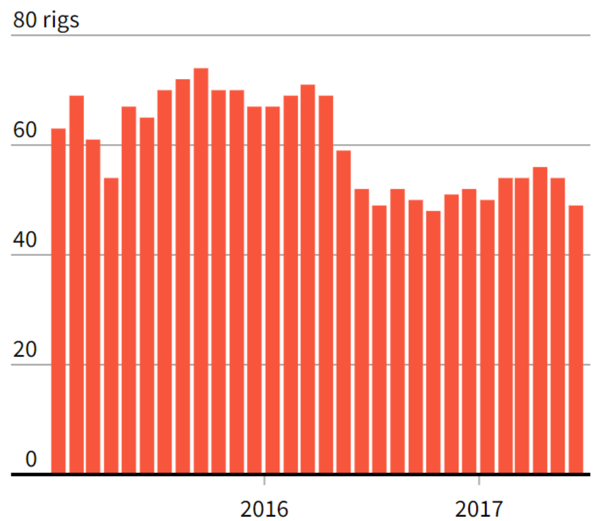

Figure 10. Oil Rigs Servicing PDVSA's Oil Supply.[104]

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103 Marianna Parraga and Mircely Guanipa, "Venezuela's Main Refineries Operating at Record Lows: Sources, Data," U.S. (Reuters, May 10, 2017), https://www.reuters.com/article/us-refinery-operations-pdvsa/venezuelas-main-refineries-operating-at-record-lows-sources-data-idUSKBN18630Z.

104 Marianna Parraga and Christine Chan, "PDVSA's Woes in Four Charts," accessed January 29, 2018, http://fingfx.thomsonreuters.com/gfx/rngs/VENEZUELA-POLITICS-OIL/0100505C0CL/index.html.

Chinese demand for crude is killing Venezuela's domestic oil refining capabilities, as less crude is available to distill domestically. The majority of crude is being shipped overseas before being distilled into a higher value-added product. Venezuela is benefiting from the exports of crude but it would benefit much more if Venezuela refined the crude in Venezuela to produce increased amounts of jet fuel, gasoline, and other fuel oils first, to later be shipped to China as a finished product. This would increase oil profits, create more domestic jobs, and most importantly maintain refineries and domestic expertise. However, domestic higher value-added production is grinding to a halt, while Venezuela's dependence on oil is being amplified. In 1999—the beginning of Chavez's reign—only 69% of total export revenues were oil shares and as of 2014, 96% of export revenues were being generated by oil according to Felix Chang.[105] Venezuela is in need of institutional reform to create an economy less dependent on oil and more open to new technologies and products but it appears that China will continue importing Venezuelan oil while letting the Maduro regime take any and all measures it deems necessary.

In summary, Venezuela's economy is facing severe challenges a decade and a half after Chavismo began. It can be argued that abnormally low oil prices have contributed to the problems. However, many other oil-producing countries have not suffered such severe financial problems following the price drop. Chinese loans directly correlate and contribute to Venezuela's problems, although they are seldom linked to the undermining problems. Venezuela's populist regime has had extreme budget surpluses due to high oil prices, coupled with being the largest recipient of Chinese loans in the world. Chavez was able to use the proceeds to push populist projects (i.e., housing, education, medicine, and appliances), to gain votes. However, Chinese loans and investments have been less helpful to the public than imagined, especially recently as infrastructure projects have failed as resources have dried up. Although many citizens once received some government spending, it has not been enough to compensate for the generally terrible economic conditions today.

105 Felix K. Chang, "Limits of Chinese Friendship: China's Development Loans to Venezuela," Foreign Policy Research Institute, July 5, 2016, https://www.fpri.org/2016/07/limits-chinese-friendship-chinas-development-loans-venezuela/.

E. CONCLUSION

The economic conditions that Venezuelans are facing today are tied to an irresponsible government, coupled with Chinese unconditional loans, further investments from Chinese state-owned enterprises, and China's laissez-faire attitude towards countries it is courting. This neglect by both parties has led to the oil industry falling apart. Logic would lead one to believe that with China's focus on oil, and Venezuela's reliance on oil to boost its regime, oil production would be at an all-time high and Venezuelan oil producing facilities would be state-of-the-art, due to massive Chinese loans and significant amounts of investment. However, such neglect now highlights the losses of the poor policies of the populist regime. Venezuela could easily benefit from increased ties with China but focus would have to revolve around becoming less reliant on oil rents, while shifting efforts towards the diversification of the country's revenues. However, Venezuela's crown jewel oil industry has been grossly neglected as rigs, refineries, and tankers are in shambles and oil production is at a historic low.

It is time that Venezuelan citizens demand that technical expertise be allowed back into the country to fix the broken oil industry without fear of reprisal, demand that Chinese loans made without legislative concurrence be claimed as odious, and begin ramping up efforts to progressively produce more refined products in their homeland to then be shipped to Chinese markets. According to Matt Ferchen, "given how little traction regional and other multilateral efforts to engage with Venezuela have gained, and in light of China's massive loans-for-oil ties to Venezuela, Beijing's role must be more carefully understood and scrutinized."[106] Venezuela's institutions have used oil revenue to bypass the need to tax its people, leading to increased corruption and authoritarian rule. This has led to regimes, driven by popular support of highly demanded social programs, with too much financial power, resulting in increased influence, and the subsequent deterioration of democracy. Institutional changes are the only course corrections that will likely correct the problems.

106 Matt Ferchen, "Can China Help Fix Venezuela?," Carnegie-Tsinghua Center (Carnegie-Tsinghua Center - Carnegie Endowment for International Peace), accessed October 13, 2017, http://carnegietsinghua.org/2017/07/24/can-china-help-fix-venezuela-pub-71564.

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IV. A CASE STUDY OF ARGENTINA'S DIVERSIFIED CHINESE INVESTMENT

"What does President Xi Jinping want? In one line: to 'Make China Great Again.'"

—Graham Allison, 2017

"We are laying the groundwork from which a country can grow. Those were the changes we needed, but no one implemented them because they didn't dare to think long-term. It was easier to see the short term. It's attractive, but in the end it leaves people worse off."

—President Mauricio Macri, 2017

This chapter compares the Chinese investment relationship with Venezuela in comparison with other investors in the region. It also provides the historical context of how Argentina's 2001 economic crisis unfolded and how it led to the courting of China. It then describes the reforms that both President Kirchners' populist left administrations enacted to reverse the crisis, and how these opened the door to Chinese investments in Argentina. Next, as the "pink tide" or left-leaning leaders of the first decade of the 21st century faded, center-right presidents in South America began to pop up. President Macri of Argentina was one of these and is now responsible for balancing the investments of his country. Finally, Argentina's experiences with China are compared and contrasted with Venezuela's previous case study to determine if Chinese investment has benefited Argentina over the past decade and a half. Findings suggest that Argentina's investment diversification with several countries have allowed it to not excessively rely on China but Argentina does need to keep its manufacturing industry in check in order to not become reliant on commodity exports to China.

A. CHARACTERISTICS OF CHINESE INVESTMENTS AND LOANS IN ARGENTINA

Chinese investments, FDI, and loans are very complicated. Sources do not accurately portray where the lines are drawn between each, nor accurately reflect the data. However, this section explains what Chinese investment, in the forms of loans, traditional investment, and construction contracts, are taking place within Argentina. According to

Avendano et al., Argentina makes up nearly $28 billion or nearly 18% of total Chinese investments in South America. On the other hand, Chinese FDI to Argentina, between 2003–2016 was only $5 billion.[107] Argentina receives a large portion of their loans and contracts from China but Chinese FDI appears to be relatively low.

As the Kirchner dynasty grew closer to China, between 2005–2014, Chinese investments amounted to $12 billion.[108] Nearly half of that amount was invested in the energy sector, followed by $2.64 billion in transportation, and finally agriculture, with $1.86 billion invested. President Macri's administration may have had some spillover from the Kirchners but he seemed to ramp up the Chinese investment as $15.62 billion was invested in a relatively short period: 2015–2017. During these three years, energy remained the largest investment sector, receiving $9.79 billion of investments. Transportation remained the second largest sector with $4.1 billion of investments. The third largest sector changed from agriculture to metals, as extractive industries received $960 million in investments.

The World Bank estimates that Argentina's net FDI inflow (current United States dollars (USD)) between 2005–2016, was a total of $88.599 billion.[109] However, the World Bank does not breakdown the FDI by individual contributor country, which makes it extremely difficult to compare FDI flows solely from China. The American Enterprise Institution does have a very helpful database that tracks Chinese "investment and contracts," which amounted to $17.7 billion between 2005–2016. This is equivalent to about 20% of Argentina's total FDI inflows during that period although the two categories,

[107] Avendano, Melguizo, and Miner, "Chinese FDI in Latin America: New Trends with Global Implications," 7.

[108] "Chinese Investment Dataset—China Global Investment Tracker."

[109] "Foreign Direct Investment, Net Inflows," The World Bank, accessed March 2, 2018, https://data.worldbank.org/indicator/BX.KLT.DINV.CD.WD?end=2016&locations=AR&start=2005.

FDI versus "investment and contracts," are not exactly the same but do provide a better understanding of the Sino-Argentina investment relationship.[110]

The Kirchners' investments and contracts with China, according to the China Global Investment Tracker, made up the equivalent of 17% of total FDI inflows from all countries between 2005–2014.[111] On the other hand, the American Enterprise Institute claims that Chinese investments and contracts amounted to $5.39 billion between 2015–2016 under Macri's administration, while the World Bank reported a total of $15.019 billion inward flow of FDI from all countries into Argentina during the same time period. When comparing these two databases, Chinese investment and contracts were equal to 35% of total FDI inflows to Argentina between 2015 and 2016, indicating a recent spike in Chinse investment.[112] However, when comparing the American Enterprise Institute's data with Santandertrade.com's FDI data for Argentina, China does not even appear as a top 10 contributor to Argentina's FDI. Santander Trade is one of the only open sources providing FDI inputs by contributing country, which is why it was chosen to compare the data. Consequently, China is likely contributing more finances to Argentina than any other country as is seen by the relatively significant increase in Chinese "investment and contracts" provided by the American Enterprise Institute from 2015–2016.

Santandertrade.com claims that Argentina's top four largest FDI contributors in 2016 were the United States, Spain, the Netherlands, and Brazil.[113] The United States contributed $1.32 billion, Spain contributed $1.03, Netherlands contributed $689 million,

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110 Author calculated total FDI inflows from the World Bank's data retrieved from https://data.worldbank.org/indicator/BX.KLT.DINV.CD.WD?end=2016&locations=AR&start=2005 and calculated total "investment and contracts" from the American Enterprise Institute's "China Global Investment Tracker" retrieved from http://www.aei.org/china-global-investment-tracker/.

111 Author calculated total FDI inflows from the World Bank's data retrieved from https://data.worldbank.org/indicator/BX.KLT.DINV.CD.WD?end=2016&locations=AR&start=2005 and calculated total "investment and contracts" from the American Enterprise Institute's "China Global Investment Tracker" retrieved from http://www.aei.org/china-global-investment-tracker/.

112 Author calculated total FDI inflows from the World Bank's data retrieved from https://data.worldbank.org/indicator/BX.KLT.DINV.CD.WD?end=2016&locations=AR&start=2005 and calculated total "investment and contracts" from the American Enterprise Institute's "China Global Investment Tracker" retrieved from http://www.aei.org/china-global-investment-tracker/.

113 "Foreign Investment in Argentina," Santandertrade.com, February 2018, https://en.portal.santandertrade.com/establish-overseas/argentina/foreign-investment.

and Brazil contributed $344 million. Although China did not even register on Santanderrtrade.com's top ten list of FDI investors, according to the American Enterprise Institute's China Global Investment tracker, China contributed $1.13 billion to investment and contracts that same year—on par with U.S. FDI to the region. However, in 2017, Chinese investment and contracts jumped to $10.23 billion in a single year according to the China Global Investment Tracker. China National Nuclear invested $4.7 billion in the two nuclear projects, and the China Railway Construction Company (CRCC) invested $4 billion into the railway systems, with other Chinese side investments in real estate, utilities, and metals.[114] From these sources of data, it is evident that China plays a much larger investment role in Argentina than FDI data sources indicate, thus undermining China's influence in the region.

President Cristina Kirchner was the inaugural leader for pioneering Chinese investment in Argentina and she did not hesitate to bind the two countries together. Chinese investments have financed large infrastructure projects, aimed at increasing the health of the entire country as a whole. However, President Macri began his term being more hesitant to hastily move forward with all of the contracts but quickly jumped on board with increasing the strategic partnership.[115]

Chinese investment by themselves are not the only financing taking place within Argentina. Figure 11 indicates the loans that Argentina received from China during President Cristina Kirchner's terms in office—nearly all $15.3 billion came from the CDB. This illustrates best how China does business. The Chinese leadership makes strategic loans in regions of interest that have the energy, transportation, agriculture, and metals potential. Next, many of China's national champions come in, after the two countries' leadership have built strategic partnerships, to tie it all together through further investments made by Chinese state-owned enterprises. For example, on July 2010 a $10 billion loan was made by the CDB towards a railway system and seven years later after talks and loan placement, CRCC made a $2.4 billion construction contract to further complete the railway

114 "Chinese Investment Dataset—China Global Investment Tracker."

115 Patey, "China Made Mauricio Macri a Deal He Couldn't Refuse."

system. Additionally, a pair of energy loans, for the amount of $2.7 billion, were made in 2012 and 2014 by leadership of both countries and after the foundation was set, China National Nuclear came in with an additional $2.7 billion to fulfill the construction contract to build Chinese nuclear reactors.

DATE	TYPE	PURPOSE	LENDER	AMOUNT
August 2007	Other	Export sector development	China Development Bank	$30M
January 2010	Other	Renewal of 2007 loan	China Development Bank	$30M
July 2010	Infrastructure	Train system	CDB and others	$10B
July 2010	Infrastructure	High-speed trains	CDB and CITIC	$273M
March 2012	Energy	Renewable energy projects	China Development Bank	$200M
July 2014	Energy	Hydroelectric dam construction	CDB, ICBC, Bank of China	$2.5B
July 2014	Infrastructure	Belgrano Cargas train line	CDB, ICBC	$2.1B
August 2014	Other	Purchase of cars for metro line A	China Ex-Im Bank	$162M

Figure 11. Chinese Loans to Argentina.[116]

As China saw how the World Bank was not willing to engage with Argentina after it defaulted shortly after the 2001 economic crisis, it filled the void with seven successive loans, totaling over $15 billion in just over a decade. Additionally, as of 2016, China has increased their loans to $25 billion. Besides the hydroelectric plants, nuclear facilities, and railroad upgrades, $1.8 billion is earmarked for the construction of natural gas pipelines, another $1.15 billion will be invested in solar panel projects, and another $360 million is allocated for aqueducts and road construction according to Elizabeth Ingram.[117] The fact

116 Gallagher, "Inter-American Dialogue."

117 Elizabeth Ingram, "China Loans Argentina US$25 Billion for Energy Projects, Including Hydroelectric," HydroWorld.com, August 3, 2016, http://www.hydroworld.com/articles/2016/08/china-loans-argentina-us-25-billion-for-energy-projects-including-hydroelectric.html.

that Argentina is deliberately expending much of the loans towards infrastructure projects, and the government has more democratic checks and balances in place to ensure transparency and accountability, produces circumstances for more promising development than Venezuela.

Regardless of which sectors are utilizing the loans, Argentina still has to pay off the loans and they are not directly secured to resources as they are in Venezuela. Possibly excess electricity can be sold to Brazil instead of energy being subsidized to the domestic economy. Therefore, exporting energy, increasing higher quantities of agricultural products to be exported by train, and constructing more accessible and efficient transportation for Argentine workers, may increase Argentina's ability to pay off the loans. If not, steadily high soy export tariffs—described later in the chapter—and unpopular austerity measures may have to be implemented. President Macri understands this dilemma, but has vowed to progressively lower tariffs as efficiency and productivity rises, in hopes of creating the fewest distortions. Hopefully, Chinese investment will not further entrench Argentina into a raw material exporter. If sound fiscal policy is implemented, the returns on investment will hopefully be significant enough to pay the principal and interest to meet Chinese financial contacts, while simultaneously lowering progressive export tariffs.

Undoubtedly, China has become an increasingly large lender to the region with accompanying investment. As China has shipped nearly 3,000 train cars and associated rails, locomotives, engineers, and other attached goods, Argentina now has long task of paying down the debt. Chinese loans are repaid largely through export tariffs. President Macri hopes to double agricultural exports within four years as well as produce renewable energy and enter the shale gas revolution, while incurring more debt to slowly combat inflation and high levels of debt from the prior administration according to Charlie Devereux and Andres Martinez.[118] However, there is very little literature on how Chinese

[118] Charlie Devereux and Andres R. Martinez, "Argentina at Mercy of Debt Markets to Fund Reforms, Macri Says," Bloomberg News, November 8, 2017, https://www.bloomberg.com/news/articles/2017-11-08/argentina-at-mercy-of-debt-markets-to-fund-reforms-macri-says.

loans and investment have worked with Argentina, but the loan characteristics seem to be more consistent with traditional banking systems.

B. CHINA'S INTERESTS IN ARGENTINA

China is interested in Argentina due to its abundance of natural resources, including a significant amount of soy. China only has 8–10% of the world's arable land but possesses 20% of the world's population. Therefore, China has a great demand for soybeans, which are used for animal feed, vegetable oil, and biodiesel. According to Gonzalo Paz, soy was almost nonexistent 20–25 years ago across the vast farmlands of Argentina, but as world food scarcity and energy security are on the rise, Argentina has been very innovative with its sustainable soy products to capitalize on those export opportunities.[119] Therefore, soybean harvests have increased from 20 million hectares in 1960 to 120 million hectares in 2013 across the globe according to Maria Sly.[120] Argentina is one of the great producers of soy and as of 2016, soy products constituted roughly 31% of Argentina's export market.[121]

China has further showed interest in Argentina's agriculture as China's largest farming company signed a $1.51 billion agreement to lease and develop 300,000 hectares in the Rio Negro province for a five- to 10-year period, according to Shane Romig[122]—maintaining agricultural in China's top three most heavily invested sectors in Argentina. Although China has a great demand for soy, it is extremely selective of what types of soy imports it purchases.

In 2016, China imported 86% of Argentina's plain soybeans, while purchasing fewer amounts of soy meal and oils year to year. For example, from 2003 to 2013—the

119 Gonzalo S. Paz, "Argentina and Asia: China's Reemergence, Argentina's Recovery," 2014, 11, https://www.wilsoncenter.org/sites/default/files/UNCORRECTED%20PROOF-%20Paz.pdf.

120 Maria Jose Haro Sly, "The Argentine Portion of the Soybean Commodity Chain," Palgrave Communications 3 (September 26, 2017): 2.

121 "Products Exported by Argentina (2016)," The Observatory of Economic Complexity, accessed February 2, 2018, https://atlas.media.mit.edu/en/visualize/tree_map/hs92/export/arg/all/show/2016/.

122 Shane Romig, "Hungry China Shops in Argentina," *Wall Street Journal*, June 20, 2011, https://www.wsj.com/articles/SB10001424052702303823104576391621352528138.

duration of the entire China boom—China imported less than a half a percent of Argentina's soy meal and since 2011, China has completely stopped buying soy meal. China chooses to import raw soybeans and build domestic grinding mills in China to provide its large population with domestic jobs, while simultaneously creating higher value-added production lines.

China was originally drawn to Argentine soy oil and had been purchasing between 10–30% of Argentine soy oil during the first 15 years of the 21st century. However, in 2016, China, Argentina's second largest trade partner after Brazil, only purchased .012% of all Argentine soy oil. This indicated China's new domestic capability of making the higher value-added product on its own.

Regardless of China's actions, Argentina remains extremely reliant on vegetable and animal product exports to China—mainly soybean exports, which reached $2.79 billion in 2016—while China is much less reliant on mineral products, textiles, and chemical product imports.[123] Those higher value-added products are to be produced by China to sell for a gain on the world market.

Additionally, China finds Argentina to be attractive because the anti-U.S. Kirchner regime welcomed financing since most Western banks would not provide them with funding since prior loans were still outstanding. This was an opportunity for China to attach its loans to infrastructure projects and further investment opportunities in the region. These loans came with clauses that utilize China's largest state-owned enterprises or "national champions" to provide the materials, expertise, and future supply chains to maintain the finished product. For example, Argentina's $2.4 billion railway modernization loan with China is attached to the CRCC, which is providing the railway materials, train cars, and diesel locomotives to accomplish the project. It does not give Argentina the option of using the loan to pursue other foreign railway companies—or even domestic ones—to complete the task.

[123] "Products Exported by Argentina (2016)."

China is able to make long-term loans because it knows that its own state-owned enterprises will likely profit from the projects. The infrastructure loan will provide markets for Chinese exports in the present, and into the future, as parts will likely be purchased from Chinese railcar manufacturers as the Argentine railways are maintained over the years. Keith Barrow states that the CRCC will supply 3,509 Chinese train cars and 107 Chinese diesel locomotives to Argentina per a contract signed in December 2014.[124] Argentina has already received 2,963 wagons as of May 2017, showing the rapid turnaround from contract to delivery.

The railway modernization loan is a $2.4 billion project to upgrade the 930-mile Belgrano Cargas rail system, or "Train to the Clouds," that traverses the Andes Mountains and crosses into Chile. This railway system would further link Argentina to the Chilean port of Antofagasta, and would be a quick exit point for Argentine exports to reach the Chinese market from the Pacific Ocean. Currently exports travel southward around Cape Horn from the Atlantic Ocean and on to China according to Luke Patey.[125] Another line, the San Martin Line, will be upgraded to increase its 2.3 million ton capacity to 13 million tons by 2024, claims Barrow.[126] This will increase potential shipments of agricultural products by over five and half times. Additionally, future resources inside the vast lands of Argentina will be more easily accessible as the region is further developed and linked to roads, railways, and ports.

The Chinese have also provided Argentina with nuclear technologies to further create energy independence for Argentina and have contracts to build a pair of Chinese nuclear reactors. China currently has four nuclear companies and it appears that the state may try to consolidate them into another national champion. Wan Gang, President of the China Institute of Atomic Energy, stated, "We need a single well known Chinese nuclear

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124 Keith Barrow, "Argentina Receives More Wagons From China," accessed January 23, 2018, http://www.railjournal.com/index.php/central-south-america/argentina-receives-more-wagons-from-china.html.

125 Luke Patey, "China Made Mauricio Macri a Deal He Couldn't Refuse," *Foreign Policy,* January 24, 2017, https://foreignpolicy.com/2017/01/24/china-made-mauricio-macri-a-deal-he-couldnt-refuse/.

126 Barrow, "Argentina Receives More Wagons From China."

brand which can compete with international brands like Areva and Westinghouse."[127] This would be the first Chinese nuclear reactor of its kind in Latin America and possibly the beginning of many more projects to come in the region.

Overall, China's ambitions are to provide new financing opportunities to Latin America. These finance opportunities come packaged with massive projects such as the railway modernization project, nuclear reactor production, as well as the largest Chinese dams to be built outside of China: a reflection of China's Three Gorges Dam, which is home to the largest hydroelectric power generation station in the world. Every piece of the deal is linked to the Chinese communist party through oversight of the CDB's funds, its state-owned enterprises, and diplomatic relations. These initiatives help promote the Chinese model as they have become the largest lender to South America.

C. ARGENTINA'S INTERESTS IN CHINA

Bretton Woods institutions began cutting off financial ties with Argentina after Argentina defaulted twice in the 21st century, once in 2001 after its economic crisis and again in 2014. This led President Nestor Kirchner and his wife, and political successor, President Cristina Kirchner to form the Sino-Argentina relationship. President Cristina Kirchner intensified ties with Venezuela and other anti-American establishments during her two terms. Her administration focused on obtaining infrastructure and energy diversification loans in hopes of lowering energy costs and creating better transportation for the average Argentine.

Near the end of her term in 2013, she raced to complete a loan agreement to have the Chinese build two hydroelectric dams—the largest within Argentina's borders as well as China's largest dam project attempted outside of China, claims Patey[128]—to increase its energy independence. Juan Cardenal states that in her last months in office, she had more

[127] Gao Fu Mao Charles Newbery, "Argentina-China Talks on New Nuclear Plants," *World Nuclear News*, May 8, 2015, http://www.world-nuclear-news.org/NN-Argentina-China-talks-on-new-nuclear-plants-08051501.html.

[128] Patey, "China Made Mauricio Macri a Deal He Couldn't Refuse."

than 30 signed memorandums of understandings signed between Argentina and China.[129] She also subsidized the cost of electricity for citizens due to high energy costs and poor electrical infrastructure, which resulted in the depletion of Argentina's foreign exchange reserves, according to Miner.[130] The CDB was willing to fund $4.7 billion for the dams back in 2014, as other sources of credit were not willing to make large investments in the region due to the aftermath of the severe recession in 2001.[131] This initiative would bring thousands of jobs to the state of Santa Cruz where critics said she has many family and political ties.

On the other hand, the two-mile-wide dam would flood grasslands the size of Buenos Aires and environmental concerns had been raised. Many were worried that Chinese workers would flood the region, but only 150 Chinese engineers have been estimated as potentially working on the project—making up only 4% of total employees, according to Jonathan Watts.[132] Once President Macri was elected, he placed a hold on the project to allow the Supreme Court to reassess the project and environmental impacts. However, as of summer 2017 the project has been allowed to continue for reasons to be explained in further detail later in this chapter. However, he recognizes the need to update the energy sector to increase efficiency and reduce energy costs over the long-term—thus ridding the country of energy subsidies.

The Argentines have been lured by the extensive Chinese nuclear offer because the Chinese would finance the project, transfer nuclear construction technology, source 50–70 percent of the components (eliminating reliance on multiple countries for parts), and

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129 Juan Pablo Cardenal, "Sharp Power: Rising Authoritarian Influence," National Endowment for Democracy, December 5, 2017, 38, https://www.ned.org/sharp-power-rising-authoritarian-influence-forum-report/.

130 Sean Miner, "Why Argentina's Macri Switched Gears on China, Now His Favorite Business Partner," *World Politics Review*, May 23, 2017, https://www.worldpoliticsreview.com/articles/22237/why-argentina-s-macri-switched-gears-on-china-now-his-favorite-business-partner.

131 "Argentina Approves Construction of Chinese-Financed Dams in Patagonia," Reuters, August 28, 2017, https://www.reuters.com/article/argentina-hydro-china/argentina-approves-construction-of-chinese-financed-dams-in-patagonia-idUSL2N1LE0UY.

132 Jonathan Watts, "Argentina Leader Leaves Controversial Legacy With Patagonia Dams Project," *Guardian*, December 1, 2015, http://www.theguardian.com/world/2015/dec/01/argentina-president-cristina-fernandez-de-kirchner-patagonia-hydroelectric-dam-project.

provide 100% of the civil works needed, according to Charles Newbery.[133] Western nuclear companies do not have the means to finance such large projects in developing regions and likely keep a tighter hold on intellectual property rights. Additionally, Santiago Miret claims that Argentina has not prioritized growth in the nuclear sector since the military dictatorships, but with enticing Chinese loans, it completed its third reactor in 2012.[134] Argentina now relies on nuclear energy for 10% of its energy generation capability, with plans for three more reactors and two of those to be constructed by the Chinese.[135]

If the Sino-Argentine nuclear relationship evolves, Argentina plans to be a nuclear hub for Chinese supply in Latin America. According to the World Nuclear Association, "[China and Argentina are] establishing a joint strategic partnership for the purpose of developing and building nuclear reactors in Latin America, so that Argentina becomes a Latin American technology platform, supplying countries with nuclear technology incorporating Chinese goods and services."[136] This could potentially benefit both economies as their supply chains and expertise intertwine and connect with other countries of Latin America.

President Macri has been known for denouncing Venezuela, paying back debts to the United States, and aligning more with U.S. interests. Although President Macri began his presidency questioning Chinese loans and contracts concerning the dam construction, he seems to be supportive of the nuclear and infrastructure rehabilitation projects. Barrow states that in May 2017, he visited Beijing and signed another agreement to increase the $2.4 billion initial investment towards the railway upgrades by another $1.6 billion to further speed up deliveries and connect the vast farmlands to the ports.[137] These

133 Charles Newbery, "Argentina-China Talks on New Nuclear Plants."

134 Santiago Miret, "Nearly Forgotten—Nuclear Power in Latin America," Berkeley Energy and Resources Collaborative, November 5, 2014, http://berc.berkeley.edu/nearly-forgotten-nuclear-power-in-latin-america/.

135 "Nuclear Power in Argentina," World Nuclear Association, February 2018, http://www.world-nuclear.org/information-library/country-profiles/countries-a-f/argentina.aspx.

136 "Nuclear Power in Argentina."

137 Barrow, "Argentina Receives More Wagons From China."

infrastructure initiatives seem to be benefiting the agricultural industry's exports. However, Argentina is de-industrializing as it is becoming more dependent on Chinese industrial imports while exporting higher quantities of agricultural products—mostly basic soy exports.

D. ARGENTINA'S GOVERNMENT DRIVEN BY SOY TAXATION

Chinese loans to Argentina are highly invested in infrastructure and paid for through taxation—much different than the loans-for-resources in Venezuela. This is likely one reason why President Cristina Kirchner dramatically increased export tariffs on soy in 2008, to be able to pay for incurred Chinese loans that began in 2007. For example, in 2016, 63% of Argentina's exports to China were soybean based products and only 8.5% were crude oil exports.[138] Most of the land in Argentina is privately owned so a new popular way for the state to produce income, to pay back its loans, was to increase tax on soy exports.

Argentina's tax system plays a key role in affecting the dynamics of Chinese loans. For example, Venezuela's loans-for-oil provide the government with funding in return for a pre-arranged quantity of oil shipments per month, while Venezuela pays down the principal and interest with each shipment of oil, at previously agreed upon price ranges. In Argentina, the loans are more orthodox, in the sense that the funds are received by the government, utilized per the contracts, and paid back however Argentina decides to—mainly through taxation and trade revenue. Due to the fact that China has a high demand for soy, and Argentina's local economy does not, soy tax rates are more easily taxed at a much higher rate than other commodities being exported from the country. If the export tax rates were equally high for all products, Argentine citizens would be more likely to buy the domestic products due to tariffs insulating domestic prices. However, Argentine's are not seeking to buy soy so the government can hike the taxes on soy easier than other products.

138 "Argentina Exports, Imports, and Trade Partners," The Observatory of Economic Complexity, accessed April 26, 2017, http://atlas.media.mit.edu/en/profile/country/arg/.

Between 2003 and 2007, the Argentine government imposed a 23.5% export tariff on soy, which seemed to revive the economy from the 2001 financial crisis, according to Dowd.[139] However, due to President Nestor Kirchner's "export-oriented populism," he increased soy tariffs to 27.5% in January 2007, and again increased them to 35% in November 2007—just in time for elections.[140] Furthermore, government spending increased more than 54% from 2006 to 2007 as public works and social security spending dramatically rose, supporting the populist movements. Interestingly, the first Chinese loan was also made in 2007 for "export sector development," to speed up the government's ability to export larger quantities of soy. This enabled China to receive more soy and facilitated a way for the populist government to further boost tax revenue.

The actions of Argentina's government were similar to Venezuela's, as government programs increased to appease the lower classes, while using the proceeds of the government's cash cow—in this case soy export taxes—to fund the programs. Dowd claims that critics found President Cristina Kirchner's tax rates to be excessive, as she implemented a soy tax system that dramatically raised soy taxes as soon as she came into power in March 2008.[141] She increased export taxes to 44.1% on soy and the additional revenue was used as a political tool to build support from the poor and much of the working class. By this time, the Kirchner dynasty believed that they did not need the farmers' votes to remain in power and thus radically increased the soy export taxes.

Although the farmers' political votes may not have been important, their voices and actions were. The populist government did not realize the power that the landowners, farmers, and associates had as the agricultural sector began protesting the government's 44.1% export tax. The rural citizens wanted to negotiate a 35% tax instead, and did so by shutting down production and soy exports to force the government, and their urban supporters, to negotiate. For example, as export tariffs skyrocketed, farmers were furious

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139 William Dowd, "Export Taxation: The Case of Argentina," ed. Jeffrey B. Miller (University of Delaware, 2009), 18, http://citeseerx.ist.psu.edu/viewdoc/download?doi=10.1.1.894.8971&rep=rep1&type=pdf.

140 Dowd, 11.

141 Dowd, 39.

and began stockpiling their grain, causing shipments to stop and city protests were launched against President Fernandez de Kirchner's reforms. The middle class feared another economic crisis similar to that of 2001, so they took to the streets with pots and pans, in hopes of pressuring government leaders to lower tax burdens on the agricultural sector. This would give farmers the incentive to supply the markets with soy again, which would employ the working class again, increase tax revenue, and stabilize Argentina—the world's third largest soy exporter. On the other hand, government supporters were told the farmers were causing inflation, poor wages, and that developments would exacerbate to problems witnessed in 2001, if soy exports were not further taxed. Argentina's congress came together in June 2008 to legitimize the 44.1% tax rate but congress voted 37–36 in favor of the 35% tax rate demanded by the farmers.[142]

Taxation was key for allowing citizens to mobilize, as perceptions of unjust reforms were taking place, and allowing their voice to be heard. Farmers' voices were heard in protests and kept a check on Argentina's populist government as soy was unfairly taxed at a much higher rate than any other export. These democratic features have enabled Argentina to maintain balance by preventing the government from overstepping its bounds, as has happened in Venezuela.

Since President Macri was elected, $33 billion in investment has come from the United States, Germany, Canada, Spain, and Brazil.[143] Additionally, Argentina made the top of the list of Fortune magazine's best markets of 2017, as Argentina's MERVAL Index, a portfolio of 28 well-known companies from the Buenos Aires Stock Exchange, reached a 45% run-up.[144] It is likely that increased foreign investment, as well as diversification of the source of investment, has led to the large growth starting in 2014 and rapidly increasing from 2015 to through 2017. Macri's business background and nearly neo-liberal approach has helped transformed Argentina's economy from the populist government of the

142 Dowd, 16.

143 "Factbox: Foreign Investments in Argentina During Macri's Presidency," Reuters, April 11, 2017, https://www.reuters.com/article/us-argentina-investment-factbox/factbox-foreign-investments-in-argentina-during-macris-presidency-idUSKBN17D2T8.

144 "The Best of 2017 in Business."

Kirchners that spanned most of the 21st century. Argentina has paid back past debtors and is once again welcoming foreign investment from all parts of the globe.

Although President Macri has helped foreign investment competition return to Argentina, he has not cut important financial ties with China. He assured China in 2016 that they wanted to continue bilateral ties with China to continue hydroelectric dam projects, continue talks of a $1.5 billion nuclear plant, and finish a Chinese satellite communication station—not claimed to be military related—in Patagonia (which is now operational).[145] However, he has decreased taxes on soy and hopes to further decrease tariffs as the economy becomes healthier.

E. EFFECTS OF CHINESE INVESTMENT IN ARGENTINA

Chinese investment has created a “Commodity Consensus” instead of a “Washington Consensus.” Sly states that many authors use the phrase Commodity Consensus because the Chinese relationship is “completely based on neo-extractivist activities, enormous commercial asymmetries, the loss of food sovereignty, and environmental degradation, among other factors.”[146] As President Cristina Kirchner further increased Argentina’s dependence on China, Argentine exports to China grew 156% from 2003 to 2007, in contrast to China’s 886% export growth with Argentina. Additionally, Argentina’s trade deficit has grown over 700% with China from 2008 to 2014, which was the same period that Argentina began taking on significant debt with China, indicating the linkages to Chinese products as the loans were incurred. Argentina has become more of an agricultural peripheral appendage to the Chinese industrial core as more reliance on primary products—soy and crude oil—have risen, and higher value-added exports, such as Argentina’s prized soy oil, have decreased.

The nuclear deals have come with strings attached as most Chinese projects do. For example, in May 2017 both countries signed a nuclear cooperation agreement that China

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145 “Argentina Reassures China Bilateral Cooperation Remains a Priority for the Macri Administration,” MercoPress, May 20, 2016, http://en.mercopress.com/2016/05/20/argentina-reassures-china-bilateral-cooperation-remains-a-priority-for-the-macri-administration.

146 Sly, “The Argentine Portion of the Soybean Commodity Chain,” 2.

would supply Argentina with two nuclear reactors, valued at $15 billion and China willing to provide loans for 85% of the projects. Although Argentina does not pose a nuclear threat, China once again is increasing its influence and furthering its own economic agenda in the region. For every Chinese nuclear reactor exported, thousands of units of specialized equipment will be needed to maintain them, and hundreds of industries will be needed to manufacture and construct the facilities. This is calculated to produce 150,000 new jobs for Chinese industries that will export the specialized parts, tools, and expertise to Argentina. Furthermore, investments totaling RMB 100 billion throughout the life of the reactor will be generated for the Chinese economy. This could be very lucrative for China if nuclear projects in Argentina are successful and transfer to other South American countries. Chinese manufactures will likely benefit, but Argentine manufacturing will likely be less favorably impacted. However, many jobs will be produced for South Americans if they have the required skill sets and make the proper agreements with China to hire their own labor and produce significant portions of the supplies domestically.

Soybeans remain the staple that keeps China and Argentina held together. However, Argentina once exported soybean oil and soy meal to China, which is a higher value-added product than raw soybeans. Now China has replaced Argentine soybean oil and soy meal with its own domestically created soybean oil and soy meal crushed and processed from Argentina's raw soybeans. This is a prime example of the erosion of Argentina's soy value chain. As China boosts its own soy industry back home, it reduces demand for Argentina's soy mills and soy oil plants, thus making Argentina more reliant on raw materials.

Additionally, Sly claims that China also posed 9% tariffs on soy oil imports to artificially raise the price of Argentine soy oil to allow their domestic soy oil production to grow and develop.[147] Furthermore, she states, "Although [soy] exports increased 84% in terms of volume from 2012 to 2015 [to China], the income in millions of dollars for the same period was 30%." This is due to the volatility of commodity prices. Although Argentine train car tonnage has increased, Argentina now has to export nearly three times as much soy—at current soy prices—to generate the same amount of revenue due to

[147] Sly, 2.

commodity price vulnerability and soy value chain erosion. This is problematic because President Macri wants to double soy exports within four years, but that initiative would not even increase revenue if commodity prices stay low as they did from 2012 to 2015.

Despite China's impressive loans with Argentina, the Sino-Argentina relations have not always been great. Gallagher mentions that Argentina's shoe industry, which consists of 600,000 employees, felt the pressure from China's low cost shoe imports and in 2009, Argentina initiated an anti-dumping case against China.[148] In turn, China increased shoe exports to Argentina to further decrease the cost of shoes and cause Argentina's shoe industry to not be able to compete at such low prices. Argentina fired back with high tariffs on Chinese shoes for five years. China did not back down and knew that Argentina was reliant on soybean exports to China—since it imports 77% of Argentina's soybeans and Argentina's populist government is reliant on high progressive export tax on soy to fund popular programs and keep taxes lower for the working class. Therefore, China reduced Argentine soy imports by 65%, so that only 12% of Argentine soy was being imported by China, thus crippling Argentine farmers and government revenue. Finally, President Cristina Kirchner caved and traveled to China to discuss further developmental plans that would further indebtedness and linkages to Chinese funds for a railroad modernization program (Figure 11 shows the two loans for train projects, which were signed in July 2010 during the same visit to China).

This is a classic case of geoeconomics, as China attacked Argentina's primary export—soy—to achieve its goal of exporting low cost products, while protecting and boosting its own industries, while other countries' high value-added industries are further weakened. This is a foreshadowing of what countries can expect if they attempt to push back against China, who is not about to ratchet back its activity worldwide. As Leslie Gelb states, "Beijing has been playing the new economic game at a maestro level, staying out of wars and political confrontations and zeroing in on business—its global influence far

[148] Gallagher, The China Triangle: Latin America's China Boom and the Fate of the Washington Consensus, 102.

exceeds its existing economic strength. Nations do not fear China's military might; they fear its ability to give or withhold trade and investments."[149]

President Macri finds himself in a difficult dilemma. He must work with China to keep it from withdrawing funding and construction efforts to complete their $20 billion contracts for railroads, dams, and two nuclear plants. For example, President Macri thought that he could count on the Trans-Pacific Partnership (TPP) to create new deals for Argentina with countries such as the United States, Japan, Singapore, Canada, and others, so he made a bold move and halted construction of two controversial dams in Santa Cruz. China in return said that there was a cross-default clause that if one project is stopped, all projects would stop. Furthermore, China began buying less soy to bring Argentina to the negotiating table. President Macri then flew to Beijing, reversed his hardline decision to halt dam construction and further entangled Sino-Argentina relations by signing 16 additional Chinese investment deals.[150] As Macri has tried to cut ties with China, and align more with European and American markets and investment, China has been able to use its soft power to maintain deep financial integration.

As Argentina's government has shifted from a populist regime to a more liberal and outward-oriented market, China continues to remain extremely important for Argentina. President Macri was the first non-Peronist, non-radical Argentine president to be elected since 1916.[151] He attempted to push back against Chinese investment but shortly found that there was not as much maneuvering room as he had hoped as China's cross-default clause threatened to end all projects, if he cancelled the dam construction. President Macri was not willing to forfeit all projects—especially the improved and expanded rail system—over the questionable hydroelectric dams.

Argentina has been able to pull itself out of a severe financial crisis, pay back defaulted loans, and is making great strides to return to its prominence that it achieved at

149 Leslie H. Gelb, "GDP Now Matters More Than Force," *Foreign Affairs*, October 21, 2010, https://www.foreignaffairs.com/articles/united-states/2010-10-21/gdp-now-matters-more-force.

150 Patey, "China Made Mauricio Macri a Deal He Couldn't Refuse."

151 "Mauricio Macri, El Primer Presidente Desde 1916 Que No Es Peronista Ni Radical," Los Andes, November 22, 2015, http://www.losandes.com.ar/article/mauricio-macri-el-primer-presidente-desde-1916-que-no-es-peronista-ni-radical.

the turn of the 20th century. It is too early to tell precisely how Chinese energy diversification investments have benefited Argentina, but the 930 new miles of railway and quintupling of cargo capacity, indicate that infrastructure development has benefited Argentina. It is the linkage between railway modernization that allows more soy, construction materials, and minerals to quickly reach ports and construction sites, thus increasing soy export taxes, and expediting Chinese-led construction efforts.

Therefore, it seems that Chinese investment is not a guarantor for successful economic development but rather dependent on the recipient country's institutions. Douglass North defines institutions as "humanly developed constraints that structure political, economic, and social interaction."[152] As with most successful development transitions, strong institutions have been the key factor for growth, development, and equality. Argentina has had relatively strong democratic institutions in place that have highly scrutinized economic planning, to ensure that citizens do not go through another crisis similar to that of 2001. Although still imperfect institutions, free elections have allowed Argentina to turn the corner from a 12-year populist rule to a center-right administration, ensuring that no single party dominates the political scene for an excessive period, thus increasing opportunities for corruption.

F. CONCLUSION

The new administration has questioned Chinese projects and has diversified its investments with several countries, limiting China's footprint. Additionally, Argentina has used tax revenue to pay debt, which is completely different from Venezuela's oil rents funding the government. The progressive tax on soy exports was the key driver in Argentina's case and seemed to be a plausible way to stay on top of debt payments, while preventing the government from having a monopoly over revenue--such as Venezuela and PDVSA. This gives farmers incentives to find ways to produce more to create larger profit margins, whereas Venezuela's oil industry workers have little to no incentive to ensure

[152] Douglass C. North, "Institutions," *The Journal of Economic Perspectives: A Journal of the American Economic Association* 5, no. 1 (March 1991): 97–112.

rigs, refineries, and tankers are kept in good working condition to increase profits, since PDVSA is not a private firm and nobody owns property rights to any part of the company.

In the case of Argentina, landowners and farmers have leverage to influence the affairs of soy taxation through lobbying, implementing strikes, and storing soy when conditions are unfavorable—thus cutting off soy revenues from the state—if the state's actions are seen as abusive or corrupt or if commodity prices are deemed too low. Therefore, Chinese investment has not caused negative secondary issues by funding corrupt government officials. At times, excessive soy taxation has occurred to increase revenue for the country to meet debt obligations and fuel social programs. However, the voice of the people have been able to keep a proper balance in check.

President Macri has bargained well with FDI from many Western countries that have invested 35% of FDI into manufacturing,[153] bringing capital back to Argentina. This creates a complex diversification of capital with a competitive component to it that has the potential to unlock great economic growth if the foreign investment creates new domestic technology and if it creates new or expanded industry to Argentina. Overall, China appears to have the same strategic partnership with Macri's non-populist administration that it had with the Kirchners', although Macri's administration seems to have added some safety nets to ensure a proper blend of foreign investment diversification. This has likely decreased China's soft power—at least during Macri's administration—but Sino-Argentine policies seem to have remained unchanged and indicate that China is able to penetrate any form of regime in South America.

Chinese investment has been improving Argentina's railways, which will ultimately increase the ability to transfer goods from the state's interior to distant markets at a lower cost, as well as provide better transportation for Argentine workers. It is too early to see how investment in nuclear plants and hydroelectric dams will affect the country. If Argentina's stock market remains strong throughout the construction of the large projects, they will likely finish with much success. Lower energy prices will likely result as well as opportunities to sell energy to Brazil.

[153] "Foreign Investment in Argentina."

Ultimately, Chinese investment can be beneficial for any country as long as good governance occurs. It is when corrupt officials began unwinding democratic processes, fueled by Chinese loans, that the foreign countries and their citizens can become vulnerable to Chinese investment. Argentina is mostly benefiting from Chinese investment but a greater amount of emphasis should be placed on the deterioration of manufacturing jobs. Argentina needs to ensure that Chinese investment highly involves local companies, while building these projects to ensure additional jobs are created domestically, while learning best practices from Chinese firms.

V. SOUTH AMERICA’S GRAVITATION TO THE CHINESE ORBIT: WHAT CAN THE UNITED STATES DO?

> “Who else was there to hold the line against the authoritarians who otherwise would have dominated that century? Who else is there now, at the beginning of the twenty first?
>
> —John Lewis Gaddis

> “Today China is getting a foothold in Latin America. It is using economic statecraft to pull the region into its orbit; the question is at what price?”
>
> —U.S. Secretary of State Rex Tillerson, 2018

This chapter illustrates U.S. foreign investment losses in South America compared with China’s growth in the region. Additionally, it discusses the U.S. National Defense Strategy as it relates to creating allies in the Western Hemisphere while maintaining strategic advantages. Finally, the chapter portrays the urgent need for a Good Neighbor Policy for the 21st century to implement proactive policies in the region. Initiatives for leaders to present at the two summits held in the Americas in 2018 are also presented. One initiative would be to advocate for a “Power America” movement. This would be similar to the “Power Africa” initiative implemented by the Obama administration in 2013 and that continues to this day but would focus resources on our closest neighbors. These initiatives need to be developed with the inclusion of the needs of South American countries but should focus efforts on providing incentives for reducing corruptive, criminal, gang, and drug trafficking activities. No better time exists than now to develop these initiatives, as “the year of the Americas” is unfolding with the G20 and G7 summits taking place this year in Buenos Aires and Quebec, respectively.

A. MIXED RESULTS FROM CHINESE INVESTMENT DUE TO INSTITUTIONAL CONSTRAINTS

As South America has built new partnerships with China over the past decade and a half, the results have been impressive. Chinese loans and other forms of investment have helped many cash-strapped countries find alternative funding that Bretton Woods institutions would not provide or that demanded excessive changes by the recipient country. Throughout the first decade of the 21st century, Chinese financing gave left-leaning governments opportunities to distance themselves from Washington politics. The Chinese commodity boom provided a new windfall of revenue for these governments, as well as inexpensive Chinese products that have been more accessible to the typical South American citizen.

These new Sino-South American ties have created secondary effects that have further changed South America. For example, Venezuela's socialist regime has used the funds to advance its political agenda. This has empowered and benefited the regime but has negatively affected millions of citizens as the regime has become more authoritative.

Given increased investment by China, other South American countries are likely to experience similar effects. If citizens maintain their voice and are given the rights and liberties that they believe are warranted, to control where investments are used, then Chinese ties can be beneficial. If, on the other hand, poor institutions use loosely managed Chinese financing to drive power-seeking initiatives, then increased debt, coupled with corrupt practices, will likely lead those countries down a road to disaster. The Chinese simply want their contracted share of resources and are not concerned with how foreign countries manage their domestic affairs—even if those countries become significantly oppressive as Venezuela has demonstrated.

Although Chinese investment may contribute to distortions in debtor countries' financial affairs and therefore affect those countries' institutions, another concern is that Chinese investment does not focus on the manufacturing industry of South America. As Gallagher mentions in his studies, the China boom was a commodity export boom for Latin America. This did the region no long-term favors. First, manufacturing exports across the region fell from 60% to 35% in 2015. During the China boom, 2003 to 2013, 78% of Latin America's manufacturing industry was not able to compete with the products of equivalent Chinese firms.[154] Furthermore, it is frightening to note that extractive industries only employ 11.6 people per $1 million in exports, while manufacturing jobs employ 71.8 people per $1 million of exports. This is exactly where Latin America is losing. Dilma Rousseff, former president of Brazil, spoke of relations between China and Brazil as needing to evolve "beyond complementarity."[155] There are fewer job opportunities in commodity sectors—China's predominant imports—while the Chinese focus on selling "low cost" manufactured goods to Latin Americans. This ensures job security for the Chinese while almost imperceptibly eroding the manufacturing industry and future job opportunities for Latin Americans.

B. MARKETS, INVESTMENTS, AND RELATIONS INCREASINGLY AT STAKE FOR THE UNITED STATES

If the United States is to remain the partner of choice in South America, policy-makers need to understand what the United States is losing out on and refocus efforts on shoring up relations to remedy the losses. Figure 12 portrays how China has become a substitute for U.S. investment in South America. It is evident that the CDB is already outpacing U.S. foreign investment in the region because it has more foreign investment stock in South America than the United States has.

154 Gallagher, The China Triangle: Latin America's China Boom and the Fate of the Washington Consensus, 96.

155 Ferchen, "Can China Help Fix Venezuela?"

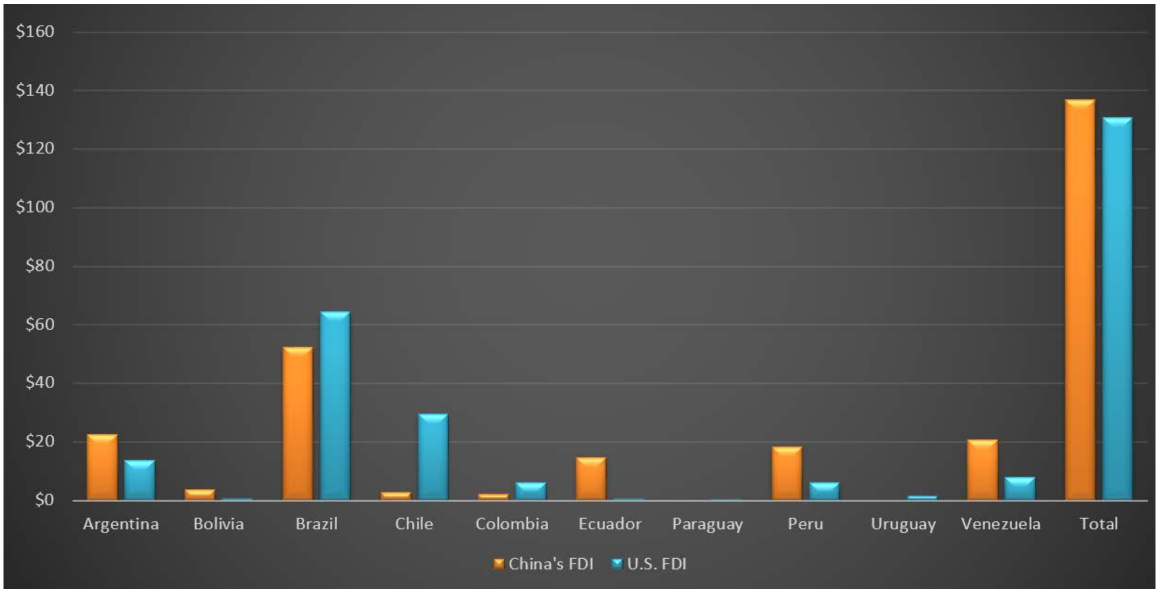

Figure 12. Chinese vs. U.S. Investment in South America (2016)—U.S. $ Billions.[156]

This data illustrates the rapid growth and influence that Chinese investment is achieving in the region as Argentina, Bolivia, Ecuador, Peru, and Venezuela already have more investments from China than the United States. Additionally, Chinese investment stock in South America is currently under $140 billion while China has pledged over $250 billion in investment in Latin America by 2025, according to Miner.[157] This suggests that further investment opportunities will be presented over the next several years. Correlating with this increase in investment are the linkages of trade and commerce, where China is also dominating trade around the globe—with growing influence in Asia and Africa and edging its way further into the Middle East, Western Europe, and now South America. Figure 13 shows how the United States continues to hold 7 out of 12 majority market shares

[156] "Chinese Investment Dataset—China Global Investment Tracker," American Enterprise Institute, July 8, 2015, http://www.aei.org/china-global-investment-tracker/ and U.S. Department of Commerce, BEA, and Bureau of Economic Analysis, "Bureau of Economic Analysis," accessed January 11, 2018, https://www.bea.gov/newsreleases/glance.htm. Note: Author took data from https://www.bea.gov/international/di1usdbal.htm to calculate U.S. investment in South America and http://www.aei.org/china-global-investment-tracker/ to calculate Chinese investment in the region.

[157] Sean Miner, "US Speaks Its Mind on China's Strengthening Relationship With Latin America," *The Diplomat*, accessed February 20, 2018, https://thediplomat.com/2018/02/us-speaks-its-mind-on-chinas-strengthening-relationship-with-latin-america/.

in trade in South America as of early 2016, but that will likely change as China continues to dominate world markets.

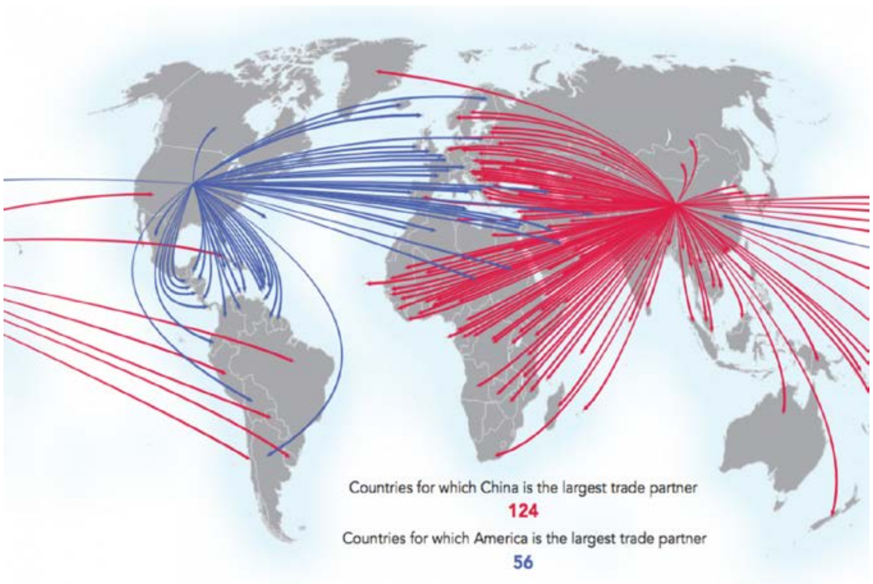

Figure 13. The World's #1 Trade Partner: China.[158]

The Chinese are slowly chipping away at footholds the United States once held. The remaining countries that the United States is vulnerable to losing out on additional trade opportunities—as China crowds it out—are Argentina, Bolivia, Ecuador, Colombia, and Venezuela. They will all likely begin increasing trade with China due to increased investment ties with China, which often come with strings attached in the form of development projects for resource quotas. According to Blackwill et al., "as certain states come to employ geo-economic tools, it can change not only the nature of diplomacy but that of markets as well."[159] For this reason, analyzing imports and exports to better understand how China has influenced South America may show where the United States is losing soft power.

158 Jeff Desjardins, "Four Maps Showing China's Rising Dominance in Trade," *Visual Capitalist*, April 27, 2016, http://www.visualcapitalist.com/four-maps-showing-chinas-rising-dominance-trade/.

159 Blackwill and Harris, *War by Other Means*, 41.

From 2005 to 2017, China accrued $156.44 billion of investments in South America alone—$175.72 billion if the tally includes all of Latin America and the Caribbean.[160] Additionally, China loaned South America $146.65 billion between 2005 and 2017—$150.41 billion including Mexico, Central America, and the Caribbean.[161] Although data for U.S. FDI flows to the region are not available, Figure 14 shows the narrowing gap between Chinese and U.S. FDI outflows on a global scale. Chinese outflows are rising much more significantly than U.S. FDI outflows, and there is no reason to believe that South America would be an exception to the trend.

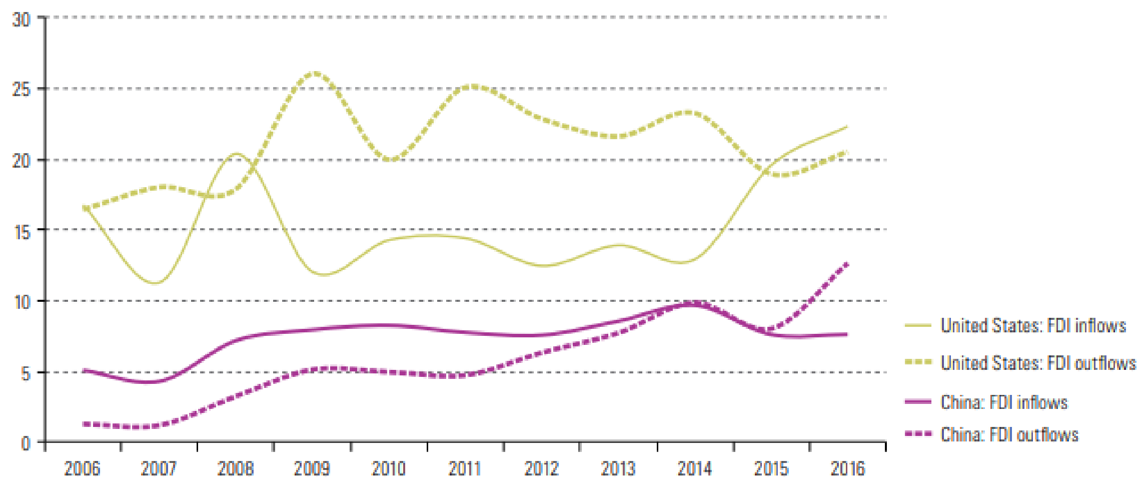

Figure 14. Chinese vs. U.S. Global FDI Inflows and Outflows.[162]

C. U.S. NATIONAL DEFENSE STRATEGY'S NEED FOR A GOOD NEIGHBOR POLICY FOR THE 21ST CENTURY

Current U.S. Secretary of Defense James Mattis understands the need to act in the Western Hemisphere. In the 2018 National Defense Strategy, he stated that the United States must maintain long-term security cooperation with its allies, with an emphasis on

160 "Chinese Investment Dataset—China Global Investment Tracker."

161 Gallagher, "Inter-American Dialogue."

162 *Foreign Direct Investment in Latin America and the Caribbean* (Santiago: Economic Commission for Latin America and the Caribbean (ECLAC), 2017), http://repositorio.cepal.org/bitstream/handle/11362/42024/4/S1700815_en.pdf.

"sustaining advantages in the Western Hemisphere." He stated further that "the U.S. derives immense benefit from a stable, peaceful hemisphere that reduces security threats to the homeland. Supporting the U.S. interagency lead, the Department will deepen its relations with regional countries that contribute military capabilities to shared regional and global security challenges."[163] However, the United States is currently not viewed highly by Latin America and many barriers need to be removed before this can easily be accomplished.

Relations with South America have not always been great, but the United States has been able to meet its strategic objectives on many different occasions. For example, shortly after the Great Depression and prior to World War II, one way the United States gained alliances and increased investment in Latin America was for the U.S. government to implement the Good Neighbor Policy. The United States was able to develop a positive relationship with Latin America through the focused efforts of U.S. President Franklin D. Roosevelt in the 1930s when he delivered his Good Neighbor Policy address. It began as rhetoric in 1933, but was quickly backed by actions, as the U.S. government recognized its poor relations with Latin America as well as its need to solidify the Western Hemisphere against the Axis powers during World War II.

The speech led to a U.S. hands-off policy, which was enticing to Latin America because it was given "a share" of both authority in decision making as well as more shares of wealth from U.S. private owned businesses abroad, according to David Green.[164] By 1939, it had transformed Western Hemisphere relations: a climate that prevailed until the death of Roosevelt 12 years later, as noted by Edward Guerrant.[165] Language from a simple speech, backed by reformed political actions, became tangible reality as the Roosevelt administration bound itself to non-intervention even if it felt obligated to aid American

163 Jim Mattis, "Summary of the 2018 National Defense Strategy," 2018, 9, https://www.defense.gov/Portals/1/Documents/pubs/2018-National-Defense-Strategy-Summary.pdf.

164 David Green, *The Containment of Latin America: A History of the Myths and Realities of the Good Neighbor Policy* (Chicago: Crown, 1971), 38.

165 Edward O. Guerrant, R*oosevelt's Good Neighbor Policy*, vol. 5 (Albuquerque: University of New Mexico Press, 1950), 1.

citizens and to combat nationalism, which was severely tested when President Lázaro Cárdenas of Mexico nationalized the nation's oil industry and seized the assets of several U.S. oil companies, and the U.S. military did not retaliate with force or coercion.[166]

Roosevelt initiated the Good Neighbor Policy to mend U.S. relations with Latin America and to build mutual trust and cooperation in Latin America as a means to help overcome the Axis powers. The United States and South America do not currently have any mutual extra-hemispheric threats to aid Western Hemispheric unification as was the case during World War II, when South America allied with the United States to combat the Germans and Japanese advances. However, in light of America's tarnished image in the region, there is a compelling need for mending relations and increasing cooperation to achieve mutual success in the Western Hemisphere. As Walter Mead stated, "there are real reasons to hope that Americans will rise to the dizzying and daunting challenges of the twenty-first century. . . . Our ignorance of our own past successes impoverishes our foreign policy process today."[167]

To rebuild the Good Neighbor relationship—for the sake of the United States remaining a significant player in the affairs of Latin America and benefiting from trade, investment, and hemispheric security—U.S. policy may need to pivot toward the interests of South America. This includes avoiding replication of past failures and contributing something more than China currently has to offer the region. In the past, this relationship enabled all of Latin America to come together (even, after fervent effort, Argentina) to overcome the Great Depression while jointly combating the evils of World War II. Evident today are similar opportunities for increased cooperation and mutual economic growth and development.

Returning to these same ideas of cooperation and respect could be a solution to enable the United States to return to the South American fold of trust and to push back against Chinese influence in the Western Hemisphere. Consequently, the U.S. government

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166 Guerrant, 5:105, 113.

167 Walter Russell Mead, *Special Providence: American Foreign Policy and How It Changed the World* (New York: Routledge, 2001), 28.

may need to focus on “nation branding” to develop a better image of the U.S. government to more effectively market U.S. trade, investment, and influence among South American countries. Christopher Browning and Antonio Ferraz de Oliveira describe the term “nation branding” as a form of nation building, similar to the efforts of Roosevelt’s Good Neighbor Policy, that attempt to market a nation through good governance and policy around the world to entice others to engage in economic activity.[168] This idea would suggest that the United States could build an appealing label to promote itself better and to sell the “U.S. brand” to South America once again.

The United States may be able to adopt nation branding or a modernized Good Neighbor Policy to create among South Americans a new, better image of the United States, enabling it to compete with China in the Western Hemisphere. Respect, collaboration, and a willingness to reach mutually beneficial agreements go a long way toward ensuring that prosperity and security grows in the Western Hemisphere. This may be the only way to achieve Secretary Mattis’s objective of “maintaining favorable regional balances of power in the . . .Western Hemisphere.”[169]

D. APPROACHES THE UNITED STATES CAN IMPLEMENT TO CREATE A GOOD NEIGHBOR POLICY

The United States government finds itself in a difficult situation as China is gaining an economic advantage in South America, and Latin America’s approval rating of President Trump stands at 16%, according to Miner.[170] Given that negativity, the United States has at least a couple of options. First, the United States can take a passive role in the region and give South American countries the room they needed for self-determination. Second, the United States can take an active role to reshape relations. The active role would have many options within it, but to gain long-term allies and establish successful security cooperatives, it is essential to achieve buy-in from South American countries.

168 Christopher S. Browning and Antonio Ferraz de Oliveira, “Introduction: Nation Branding and Competitive Identity in World Politics,” *Geopolitics* 22, no. 3 (July 3, 2017): 482.

169 Mattis, “Summary of the 2018 National Defense Strategy.”

170 Miner, “US Speaks Its Mind on China’s Strengthening Relationship With Latin America.”

1. Passive Role

If the United States plays a passive role in the region the result might be a larger foothold in the region for China. On the other hand, if China does not reform its South America trade policies, the Sino-South American strategic partnership may lead to similar failed relationships between the region and the United States. For example, South American countries typically remained at the periphery of the U.S. core, leading to path dependency as U.S. companies typically benefited from raw materials to feed their higher value-added industries. This same mercantilist pattern is taking shape between China and the countries of South America. According to Miner, China is in truth more protectionist than the United States, but the rhetoric from Latin America would suggest the opposite.[171]

Therefore, a plausible option for U.S. leadership is simply to say nothing about Sino-South American relations and allow South American countries to follow their own paths with China. In the meantime, the United States could focus on improving relations with Mexico. If the results of a liberal democracy—rule of law and individual rights—lead to superior results than those of an authoritarian global power, it is only a matter of time before South America will turn back to the United States to rebuild mutually beneficial political-economic ties.

For favorable relations to develop with any of Latin America, however, the United States must prevent protectionism from disenfranchising Latin America. The United States can implement protectionism against unbalanced trade relationships, but it is not in the best interests of the United States to repel its southern neighbors through overly aggressive rhetoric, let alone protectionist actions. If protectionism is to be used, it needs to be directed at specific regimes so that all countries do not feel threatened.

The United States should reflect on foreign policy failures in Cuba, from 1898 through the Cuban revolution ending in 1961. As William Williams alludes, "American policy interacted with the politics of the Cuban coalition in a way that strengthened the radicals. It probably also pushed them much further to the left than they had originally

[171] Miner.

hoped or intended to go."[172] He further explains that it was not merely the Cuban revolutionaries who mobilized Cuban citizens to revolt, but it was also the United States' failure to properly use its power in the region and U.S. actions helped propel the revolution.

The United States should avoid further alienating the people of South America. However, it may easily be swayed by political revolutions if the United States' power continues to be negatively viewed in the region. Results from the Cold War in Latin America show that the U.S. containment of the Soviet Union in Latin America yielded long-lasting consequences. For example, Cuban relations remain very cold to this day, because the United States spent years courting anti-communist dictatorships while simultaneously conducting covert operations to overthrow regimes with sympathetic communist ties. Additionally, the United States did not use its power to build up Cuba the way it had built and reinforced its own political-economic structure, a contributing factor of further grievances of the Cuban revolutionaries. Many American companies held valuable, productive properties in Cuba, and when the Cuban government attempted to nationalize or control them, the United States intervened to prevent Cuba's own self-determination, notes Williams.[173] Using the same hegemonic, unilateral Cold War decision-making to contain China's rise in South America would likely lead to similar negative results.

Although Vice President Pence and Secretary of State Tillerson have traveled to South America during the first year of President Trump's administration, their rhetoric has not resonated well with the Latin American population as a whole. For example, Tillerson said, "strong institutions and accountable governments are needed to secure sovereignty against 'potential predatory actors' arriving in their region."[174] Although this is arguably an accurate statement of Chinese policy, much of the time many South Americans also view the United States as a predatory actor. Because U.S. relations with Mexico are

172 William Appleman Williams, The Tragedy of American Diplomacy (New York—London : W. W. Norton & Company, 1972), 4.

173 Williams, 5.

174 "Latin America Should Not Rely on China: U.S. Secretary of State Tillerson," Reuters, February 1, 2018, https://www.reuters.com/article/us-usa-diplomacy-latam-china/tillerson-warns-latin-america-against-reliance-on-china-idUSKBN1FL6D5.

currently quite cold, it is better for the United States to remain silent and let South Americans plot their own course and be their own judges of the Chinese alternative until the United States can resolve issues with its closest neighbor. The United States either needs both feet in Latin America or both feet out. The latter, however, seems more promising.

2. Active Role

Although the China boom has slowed due to Chinese growth rates cooling from nearly 10% to around 7%, it does not appear that the economic trends for trade and investment between China and South America will change much. He Lifeng, chairman of the National Development and Reform Commission, stated to the People's Republic of China's congress held in October 2017, "We expect to achieve the full-year growth target of about 6.5 percent."[175] China has proven to be rather resilient and able to meet the goals it develops in its Five Year Plans, which means that the United States needs to start thinking more strategically if there is any chance of regaining any of the market share and political foothold lost in the region. Secretary of Defense Mattis stated as much in the National Defense Strategy: "Foster a competitive mindset. To succeed in the emerging security environment, our Department and Joint Force will have to out-think, out-maneuver, out-partner, and out-innovate revisionist powers, rogue regimes, terrorists, and other threat actors."[176]

Although U.S. intervention in Latin America has tarnished the nation's reputation, the United States should work multilaterally and aggressively with the nations of South America to help confront their challenges. The American Academy of Arts and Sciences noted in 2014, "If our nation does not act quickly to shore up its scientific enterprise, it will squander the advantage it has long held as engine of innovation that generates new discoveries and stimulates job growth."[177] Not only is South America in danger of

175 Kevin Yao and Meng Meng, "China Still on Track to Hit Growth Target Despite Winter Smog War: State Planner," Reuters, October 21, 2017, https://www.reuters.com/article/us-china-economy/china-economy-on-track-to-hit-2017-growth-target-state-planner-idUSKBN1CQ06R.

176 Mattis, "Summary of the 2018 National Defense Strategy."

177 Allison, Destined for War, 17.

sacrificing technological advancement for increased dependency on raw material trade, but the United States, too, is losing to China its technological and manufacturing edge.

It would behoove the United States to begin working with the members of the Organization of American States (OAS) to negotiate with individual countries to put pressure on China to help mend democratic erosion in Venezuela to which China has partially contributed. If China is unwilling to accept any responsibility or decry Maduro's actions, the United States may need to shine a bright light of condemnation on these disruptive Chinese tactics across the Western Hemisphere. Ferchen states that Argentina, Brazil, and Chile have already expressed concern about President Maduro's intentions to change the constitution.[178] With so many large and powerful South American countries on the same page as the United States, the time is ripe to unite with South America to put pressure on China to assist in fixing the Venezuela mess—or the United States and South American allies should rekindle ties to rewind all that has been undone due to Chinese financing.

However, to effectively push back against China in the region, the United States needs to create a better image of itself. Leveraging the voice of the Venezuelan opposition and allowing it to echo across South America is paramount. The Gallup Poll determined that 37% of Venezuelans approve of the job that President Trump is doing—the highest approval rating in Latin America—much higher than the 16% average across the rest of Latin America.[179] The Venezuelan figure is encouraging, because it suggests that these citizens see hope in the Trump administration's hard stance against the regime of President Maduro and still look to the United States as "a shiny city upon a hill" despite many frustrations. The United States needs to come together with the Venezuelan opposition and

178 Ferchen, "Can China Help Fix Venezuela?"

179 "Outlook Grim in Latin America for Relations Under Trump," Gallup.com, January 24, 2018, http://news.gallup.com/poll/226193/outlook-grim-latin-america-relations-trump.aspx.

the signatory countries of the Lima Declaration, who all demand that Maduro undo the abusive changes he has made to the institutions of Venezuela.[180]

The signatory countries of the Lima Declaration are Argentina, Brazil, Canada, Chile, Colombia, Costa Rica, Guatemala, Honduras, Mexico, Panama, Paraguay, and Peru. As Francisco Monaldi states, "We want hemispheric efforts that are not perceived as a USA-Venezuela confrontation, as President Maduro has always tried to portray it. It's very important that some very significant countries in the region have taken the lead."[181] The agreement about Venezuela provides further opportunities for the United States to mend relationships, because the region can see that some important decisions are not being influenced directly by the United States and that the regional voices matter. This kind of alignment does not weaken the United States but rather strengthens the hemisphere.

If the United States can unite with powerful leaders of South America to accomplish unified goals for resolving the Venezuela crisis, new-found alliances can be built. Western Hemisphere alliances need to press China to start supporting democratic processes in the Western Hemisphere instead of allowing them to crumble and then claim that Chinese policy amounts to "non-intervention." The United States should portray these negative underpinnings, largely perpetuated by China's unwillingness to stand-up for the welfare of the Venezuelan citizens as they have been deprived of their political rights.

In addition to working with Latin American partners to pressure Venezuela, the United States could implement a program similar to President Barrack Obama's "Power Africa" initiative, which began in 2014 when he invited to the White House for talks all but four African heads of state. The program included a $14 billion investment for building

180 "Lima Declaration," Government of Canada, accessed February 21, 2018, http://www.international.gc.ca/world-monde/international_relations-relations_internationales/latin_america-amerique_latine/2017-08-08-lima_group-groupe_lima.aspx?lang=eng.

181 Patricia Mazzei, "U.S. Sanctions 8 More Venezuelans Tied to Maduro Government," *Miami Herald* (Miami Herald, August 9, 2017), http://www.miamiherald.com/news/nation-world/world/americas/venezuela/article166248567.html.

electrical infrastructure in the interior of Africa, according to Doyle McManus.[182] The meeting was held to counter China's growing influence in Africa and the meeting came at a perfect time, as an African-American president was in office to leverage American influence in the African region. One official mentioned, "these projects are a way we can compete with the Chinese for influence. We need to be on the playing field, even if we don't play the same way."[183]

The challenges are likely more difficult in Africa because it is much further from the United States, there are more language barriers, and its culture are even more diverse than the U.S.-Latin American spread. There are many more authoritarian leaders in Africa who find it much easier to cut deals with China than adhering to U.S. requirements to promote human rights and transparency. Therefore, it should be much easier to develop a "Power America" initiative. Although electricity infrastructure is not needed as badly in South America as it is in most of Africa, many roads, highways, railways, and ports need to be built in South America. For example, Argentina has long sought a railway modernization loan. A "Power America" initiative would not necessarily be limited to electric grid projects; such an effort could provide technical assistance, infrastructure development, and innovative technologies to select South American countries. The recipient countries should meet predetermined transparency, human rights, counter-narcotic, and gang and violence levels--or show efforts in curtailing the issues and meeting milestones along the way, in exchange for continued assistance. The U.S. Agency for International Development (USAID) and/or the Millennium Challenge Corporation (MCC) could spearhead the program along with possible partnerships with nongovernmental organizations (NGOs).

Given the Trump administration's hardline stance on protectionism, these initiatives would initially be heavily scrutinized, vigorously attacked, and ultimately subjected to fierce negotiating. Nonetheless, the initiatives would be in the best interests of

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182 Doyle McManus, "President Obama's Troubling Dinner Party," *Los Angeles Times*, August 5, 2014, http://www.latimes.com/opinion/op-ed/la-oe-mcmanus-column-africa-summit-human-rights-20140806-column.html.

183 McManus.

the entire Western Hemisphere, especially if promoted as a means to address the Western Hemisphere's immigration, human trafficking, and drug trafficking issues. The efforts would likely create more jobs and stability in Latin America, which would help reduce immigration issues and potentially keep more people out of gangs and drug trade by having more alternatives within their own country of origin.

Such a program would not only mitigate Chinese influence in South America but boost the United States' tarnished image with its southern neighbors. "You don't promote the cause of peace by talking only to the people with whom you agree," President Dwight Eisenhower once said. "That is merely yes-man performance. You have got to meet face to face the people with whom you disagree at times, to determine whether or not there is a way of working out the differences and reaching a better understanding."[184]

Finally, the World Bank and IMF may need to increase loan limits for countries that meet benchmarks for combating drugs, gangs, and other corruptive activities. There needs to be more dialogue and cooperation between USAID, MCC, the World Bank, and IMF to pool resources for higher levels of funding. The cross-talk would likely facilitate more cooperation and knowledge sharing to effectively reach desired outcomes and give a new name to the World Bank as a leading financial institution in the region, instead of being undermined by the CDB. There are always opportunities for loaning money but loans need to directly benefit Latin America and the United States. Investing in manufacturing would likely lead to the best results as Latin America needs the domestic jobs and China is not bringing this option to the table.

The World Bank and other institutions also need to work more closely with both large corporations within Latin America as well as those in the United States. China's government is set up in such a way that its loans attach to its companies. When China says, "Move," the state-owned enterprises largely enact what the leadership wants. The United States does not have the same mechanism, but the U.S. government can better direct funding to the World Bank, USAID, MCC, and others to ensure it is utilized more

184 John Lewis Gaddis, *Strategies of Containment: A Critical Appraisal of American National Security Policy During the Cold War* (New York: Oxford University Press, 2005), 125.

effectively to fulfill the intent of the National Defense Strategy. Additionally, unlike China, the United States does not have state-owned enterprises to mobilize in South America. However, the U.S. government can incentivize U.S. companies to head projects in these regions. Government incentives could be reformed to provide U.S. private businesses—theoretically more efficient than Chinese state-owned enterprises—with more opportunities to invest in what otherwise might be daunting South American projects by partnering with the World Bank, IMF, MCC, USAID, and others.

Gallagher claims that Chinese and western banks have complemented each other; western banks tend to fund short-term, lower cost governmental and social programs, and Chinese banks try to fill the gap by providing what the West will not, such as massive infrastructure projects.[185] It may be time for the United States to become more competitive with Chinese banks and businesses carrying out very large projects. It has been done before. A prime example is President Theodore Roosevelt's vision to build the Panama Canal, from which Panama has benefited for over a century. Future projects can easily be polled by South American countries to find out what citizens want and see how both parties can benefit by pulling together resources. America needs to be bold again in the way it thinks and acts, and opportunities abound for building ties in the Western Hemisphere.

E. CONCLUSION

Mead stated, "World power does not come with a guarantee. Great powers rise and fall. New technologies, new weapons, and new ideologies have repeatedly overturned existing orders, bringing small peoples out of obscurity into empire and sending great empires crashing down into ruins."[186] It is not too late, however, to take action. This year the Group of Twenty (G20) summit will take place in Buenos Aires and the Group of Seven (G7) summit will take place in Charlevoix, Québec. Secretary of State Tillerson claimed, "in this year of the Americas, the U.S. will continue to be the Western Hemisphere's

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185 Gallagher, *The China Triangle: Latin America's China Boom and the Fate of the Washington Consensus*, 72.

186 Mead, *Special Providence: American Foreign Policy and How It Changed the World*, 338.

steadiest, strongest and most-enduring partner."[187] The Trump administration needs to take advantage of both summits by bringing proposals for South American projects, with a key emphasis on South America to ensure that the region's leaders can provide their inputs and create mutually beneficial projects.

Just as Vice President Pence stated during his southern tour to Colombia, Argentina, Chile, and Panama in August 2017, "'America first' does not mean 'America alone.'"[188] If the administration is serious about making America great again, it is imperative that the United States not work alone over the next three years—as well as during other U.S. administrations in the years to come. Domestic manufacturing can be a priority, which would help the United States promote and help facilitate South American projects, just as President Obama's "Power Africa" is marching onward behind the scenes. There is no reason why a "Power America" project cannot help secure our own hemisphere.

China will definitely bring money to the table with projects in mind. The United States needs to rethink how it provides financing to make its offers more enticing—an attractive, beneficial alternative to China's "Commodity Consensus" that has prevailed over the past 15 years. Government organizations working abroad need to link funding and common goals to help combat China's deindustrialization of South America. It is imperative that the United States use every opportunity to regain its hemispheric leadership and preclude China's further distancing the region from U.S. influence.

[187] Max Greenwood, "Tillerson Cautions Latin America Over China's Influence," *The Hill*, February 1, 2018, http://thehill.com/homenews/administration/371874-tillerson-cautions-against-chinese-influence-in-latin-america.

[188] McKenna, "Trump's Abysmal Treatment of Latin America Could Open Up Opportunities for Canada."

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