Talking point

China – the new financial player in Latin America

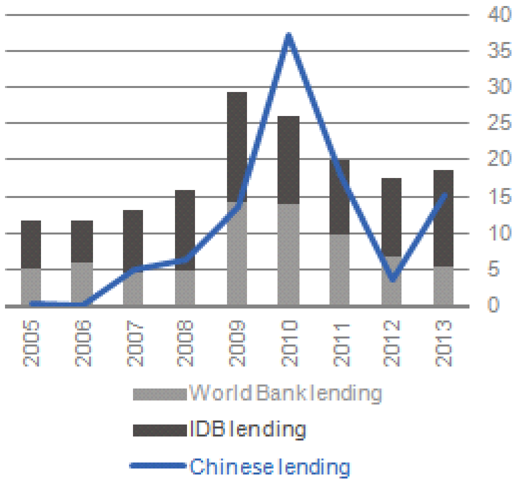
July 29, 2014

Chinese President Xi Jinping just finished a visit to Latin America, which included Brazil, Argentina, Venezuela and Cuba, at a time of rapidly increasing trade and investment ties between China and the region. China is the largest export market for Brazil, Chile and Uruguay, and the second largest for Peru, Venezuela and Cuba. The volume of bilateral trade rose over 20 times from USD 12 bn to USD 288 bn between 2000 and 2013. New Chinese investment in Latin America was around USD 9.2 bn in 2012.[1]

Not only have trade and investment relations reached a substantial scale, but also bilateral lending by Chinese state entities has become an important financing source for some countries in the region. The Inter-American Dialogue,[2] a think tank, estimates that between 2005 and 2013 Chinese state-controlled entities lent an accumulated USD 98 bn to selected Latin American countries. The bulk is loans from China's policy banks China Development Bank (partially in cooperation with other banks) and China Ex-Im Bank. The numbers are substantial compared to combined multilateral lending by the World Bank and the Inter-American Development Bank (IDB) of nearly USD 163 bn over the same period.

Chinese lending surges

New commitments to Latin America & the Caribbean, USD bn



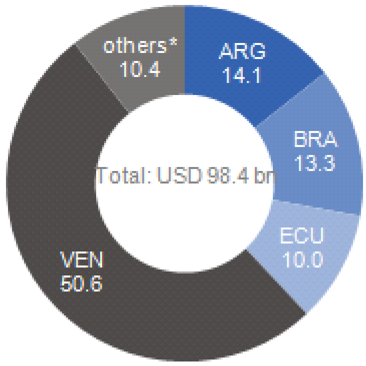
Sources: World Bank, Inter-American Development Bank, Inter-American Dialogue, Deutsche Bank Research

Three of the countries that President Jinping visited are among the largest recipients of these loans. Venezuela is by far the largest borrower of Chinese funds with a total of more than USD 50 bn in 2005-2013. This equals 51% of total Chinese lending to Latin America (chart). During the official Chinese visit, a new credit line of USD 4 bn was announced. Argentina reportedly signed new loans worth over USD 4.7 bn to build two hydro-electric dams and USD 2.1 bn for a railway project. The country already contracted loans of USD 14 bn in the last nine years, mainly funding infrastructure projects in the railway system. Brazil secured two new loans worth USD 7.4 for a large mining company to buy or lease Chinese ship equipment. In absolute terms, Brazil is the third largest borrower of Chinese loans in Latin America, but compared with its large GDP Chinese lending is still relatively small. That is different in Ecuador, where Chinese loans equal more than 10% of 2013 GDP. The majority of these loans (for a total of USD 10 bn) were directed to the state oil company and hydro-electric projects, and some of the funds were used to finance the state budget deficit.

Going by CDS spread levels, three of the four countries mentioned are among Latin America's riskiest for lenders. Chinese banks mitigate the risk they take in lending to Latin American countries mainly in two ways. First, loan contracts often require the purchase of Chinese construction, oil or train equipment or services, opening business opportunities for Chinese companies. Second, some of the loans are backed by future oil shipments. Many of Venezuela's and Ecuador's loan contracts include a clause that requires the countries to ship oil to China, a part of which is deducted to pay interest and amortisation of the loan, at current market prices for the commodity. Thus China secures a continuous supply of oil to its energy-intensive economy.

Chinese loans to LatAm: highly concentrated

USD bn, 2005-2013

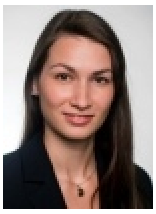


*others: BHS, BOL, CHL, COL, CRI, GUY, JAM, MEX, PER, URY

Sources: Inter-American Dialogue, Deutsche Bank Research

[1] Estimate of the Economic Commission for Latin America and the Caribbean (ECLAC), 2013

[2] Inter-American Dialogue & Global Economic Governance Initiative of Boston University: China and Latin America Finance Database, http://www.thedialogue.org/map_list



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