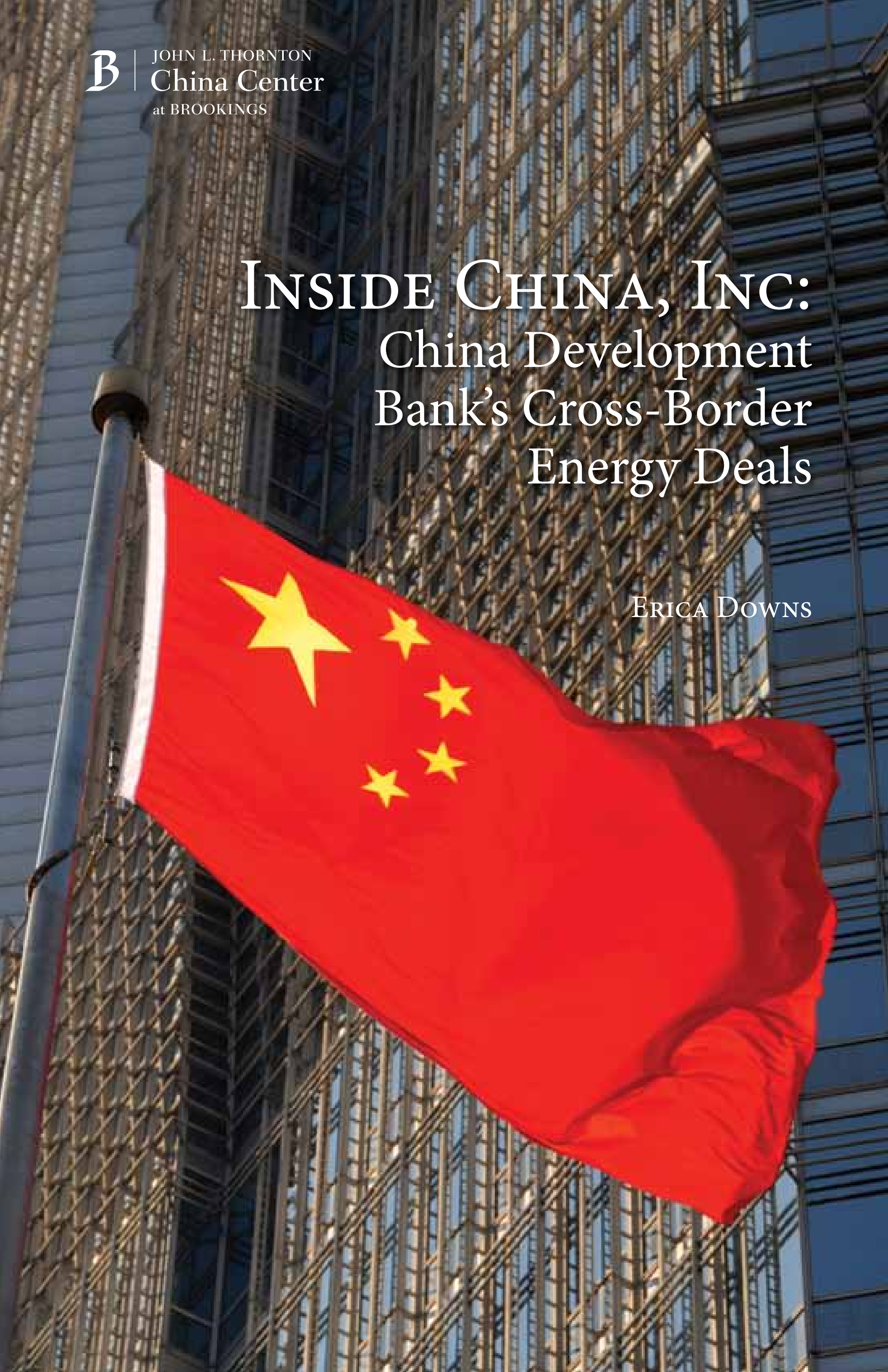

JOHN L. THORNTON
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Table of Contents

Abbreviations

BANDES	Banco de Desarrollo Económico y Social (Venezuela's Bank for Economic and Social Development)
CBRC	China Banking Regulatory Commission
CDB	China Development Bank
CIC	China Investment Corporation
CNOOC	China National Offshore Oil Corporation
CNPC	China National Petroleum Corporation
EBL	Energy-backed loan
ESPO	East Siberia Pacific Ocean
FONDEN	Fondo De Desarrollo Nacional (Venezuela's National Development Fund)
IMF	International Monetary Fund
IOC	International oil company
JIF	Joint Investment Fund
LIBOR	London Interbank Offered Rate
LIC	Local government investment corporation
LNG	Liquefied natural gas
MOU	Memorandum of understanding
NDRC	National Development and Reform Commission
NOC	National oil company
NPL	Non-performing loan
OECD	Organization for Economic Cooperation and Development
ONGC	Oil and Natural Gas Corporation Ltd.
PBOC	People's Bank of China
PDVSA	Petroleos de Venezuela SA
PGS	Petroleum Geo-Services
PSUV	Partido Socialista Unido de Venezuela (United Socialist Party of Venezuela)
SPC	State Planning Commission
WTI	West Texas Intermediate

Introduction

In 2009 and 2010, China Development Bank (CDB) extended lines of credit totaling almost $65 billion to energy companies and government entities in Brazil, Ecuador, Russia, Turkmenistan and Venezuela. The loans are secured by revenue earned from the sale of oil at market prices to Chinese national oil companies (NOCs), except in the case of Turkmenistan, which is delivering natural gas at undisclosed prices. These energy-backed loans (EBLs) are distinguished by their large size (up to $20.6 billion), long terms (up to twenty years), the relatively short period of time in which they occurred (over a period of less than two years), and their availability at a time when many companies were cancelling or postponing major investments in oil and natural gas development because of cash flow problems and virtually no other financial institutions were willing to lend such large amounts of capital for such long terms.[1]

CDB's EBLs demonstrate the increasingly central role the bank is playing in China's "going out" strategy, the international expansion of Chinese firms to secure energy and natural resources, build national champions and acquire advanced technologies. Since the mid-2000s, CDB has participated in some of China's most high-profile cross-border deals, including financing the acquisition of a 9 percent stake in the Anglo-Australian mining giant Rio Tinto by the Aluminum Corporation of China

[1] International Energy Agency, *World Energy Outlook 2009* (Paris: OECD/IEA, 2009), pp. 135-148.

(Chinalco), bankrolling the global expansion of China's telecommunications firms Huawei Technologies and ZTE Corporation, funding the natural gas pipeline that runs from Turkmenistan to China, and managing the China-Africa Development Fund. CDB also purchased a 3.1 percent stake in Barclays when the British bank was attempting to acquire the Dutch bank ABN Amro in what would have been the largest bank merger in history had it succeeded.

CDB's EBLs raise the same question that many outside observers ask about the international mergers and acquisitions of China's state-owned energy and mining companies: to what extent are these deals driven by the strategic interests of the Chinese government versus the commercial interests of Chinese firms? On the one hand, CDB is a wholly state-owned bank with a mandate to advance China's national interests as the State Council understands those interests at any given time. Currently, those interests include supporting the "going out" strategy and improving China's access to energy. Moreover, the bank's chairman and leader for more than a decade, Chen Yuan, serves at the pleasure of the Chinese Communist Party and is the son of Chen Yun, one of the founding fathers of the People's Republic of China. On the other hand, Chen is an ambitious and entrepreneurial financier who operates with a considerable degree of autonomy. He has transformed CDB from a bank created for the explicit purpose of undertaking policy-driven lending into one of the most dynamic and successful Chinese financial institutions. In addition, Chen has a proven track record of advancing CDB's own interests in tandem with those of the Chinese government.

The purpose of this study is to contribute to the debate over the extent to which China's cross-border deals are the product of coordination between Chinese firms and the Chinese government by examining China Development Bank and its EBLs. CDB is a link between the strategic ambitions of the Chinese government and the commercial interests of Chinese firms because the financing it provides to support cross-border deals connects state policy to commercial activity.[2] The bank does this by providing funds to both Chinese companies and entities in energy and resource-rich states. Many outside observers explicitly or implicitly assume that CDB's deals, including the EBLs, are the work of China, Inc.: China's government, state-owned banks and NOCs operating as a coherent entity in a global pursuit of energy.

The main finding of this study is that CDB's EBLs are the result of coordination between government and business but the motive frequently attributed to these transactions—to secure oil and natural gas supplies for Chinese consumers—is just one of the multiple corporate and national interests that drove these deals. CDB, the State Council and China's NOCs worked closely together to structure and execute these transactions. However, this coordination between the Chinese government and Chinese firms must be understood in the context of two important caveats:

First, each of the state-owned firms involved had its own interests, including profitability, to pursue. This conclusion is especially true for CDB, which has a proven track record of advancing its own objectives, including its long-standing commitment to profitability, in tandem with those of the government. The EBLs did not simply further the State Council's objectives of enhancing access to energy, supporting the international expansion of Chinese firms and diversifying China's foreign exchange reserves. They also promoted CDB's own agenda of increasing profits, expanding its overseas business portfolio, and protecting its privileged position in China's banking system. In addition, the loans also dovetailed with the NOCs' strategic priority of expanding their international exploration and production portfolios.

Second, coordination is not synonymous with top-down decision-making. The loans to energy companies in Brazil and

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[2] I thank Arthur Kroeber for this point.

Russia demonstrate that cross-border deals that advance both national and commercial interests can originate with any of these actors. Whereas CDB developed the deal with Brazil, the State Council and China National Petroleum Corporation (CNPC) drove the transaction with Russia.

This examination of CDB's EBLs also demonstrates that cross-border energy deals shaped in part by the strategic priorities of the Chinese government have both positive and negative implications for American interests abroad. Over the past decade, numerous analyses of the implications of China's growing global energy footprint for the United States have focused on how projects that are motivated—or perceived to be motivated—by the strategic priorities of the Chinese government are undermining America's influence and interests abroad, including in the Former Soviet Union and Latin America. CDB's loans have appeared in some of these narratives.

In contrast, this study finds that CDB's EBLs align with some American interests and run counter to others. Evidence indicates the Chinese did not execute these deals to help or harm the United States. Nevertheless, CDB's loans have both positive and negative implications for the United States. On the one hand, the loan to Turkmenistan aligns with some US interests in Central Asia, including bringing incremental energy supplies to the world market and supporting the independence of states in the region by providing them with multiple energy export options. In addition, these deals are not removing oil from the world market and reducing the amount of oil to other consumers. Moreover, the bank's loans to Venezuela, its largest foreign borrower, indicate that CDB, like more established bilateral and multilateral donors, is increasingly concerned about good economic policymaking in recipient nations even if it does not attach the same conditionality to it loans. On the other hand, CDB's loans to Venezuela and Ecuador are empowering anti-American regimes, and CDB's lines of credit may give China's NOCs a competitive advantage over other oil companies, including those domiciled in the United States.

This study is divided into four parts. The first section examines CDB's transformation into one of China's most commercial and international institutions under the leadership of Chen Yuan. It details his success in furthering his own ambitions, which first and foremost included making CDB into one of the healthiest banks in China, while serving the interests of the Chinese leadership. The second section analyzes CDB's EBLs, including their structure and implementation. The third section discusses what the EBLs tell us about the link between national policy and commercial activity in China's cross-border energy deals. It discusses the multiple national and corporate interests behind the deals and the role different actors played in driving different deals. The fourth section examines positive and negative implications of CDB's EBLs for the United States.

Chen Yuan's Transformation of CDB

CDB was one of three policy banks established in 1994 to assume responsibility for supporting government policy objectives, freeing the big four banks (Agricultural Bank of China, Bank of China, China Construction Bank and the Industrial and Commercial Bank of China) to lend on a commercial basis.[3] The other two policy banks are the Export-Import Bank of China (China Eximbank) and the Agricultural Development Bank of China.[4] CDB is the only Chinese bank besides the People's Bank of China (PBOC)—China's central bank—to have full ministerial rank.[5] This status probably reflects the centrality of CDB's mission to China's overall economic development strategy, the provision of large-scale, long-term funding for the construction of infrastructure and industrial projects aimed at breaking the strategic bottlenecks in energy, natural resources and transportation created by China's rapid economic growth.[7] Over the past fifteen years, CDB has evolved from a piggy bank for the government's pet projects to a much more commercially and

[3] Barry Naughton, *The Chinese Economy: Transitions and Growth* (MIT Press, 2007), p. 457-458.

[4] For more on the origins of China's policy banks, see Kaja Sehrt, "Policy banks: the new black hole," *China Economic Quarterly*, Q4 (2000), pp. 32-36.

[5] General Affairs Office of the State Council 国务院办公厅, "国务院厅关于印发国家开发银行机构编制方案的通知" ("Notification from the General Affairs Office of the State Council Regarding the Printing and Publishing of the Structural Plan for China Development Bank"), June 28, 1994, 找法网 (*Findlaw.cn*), <http://china.findlaw.cn/fagui/gj/22/16409.html>.

[6] I thank Albert Keidel for this point.

internationally oriented institution. Not only is CDB arguably the best performing bank in China, but it has a rapidly expanding global footprint and currently boasts the largest portfolio of foreign currency loans of any Chinese bank.[7]

The story of CDB's metamorphosis into one of China's most successful and global institutions cannot be told without mentioning Chen Yuan, who served as governor of the bank from 1998 until 2008, when he became chairman of the board.[8] Chen Yuan is the eldest son of Chen Yun, one of China's "Eight Immortals" celebrated for their role in creating the People's Republic of China. Chen Yun was the second most powerful official behind Deng Xiaoping in the 1980s and the top economist among the old revolutionaries.[9] Like his father, Chen Yuan is extremely public-spirited, and he had the vision, financial acumen, entrepreneurship to reshape CDB into a firm that aims to profitably support government policy objectives at home and abroad, including access to the energy and natural resources China needs for its continued economic rise. Chen Yuan also exploited every advantage granted to him by virtue of being a "princeling"—the offspring of a high-ranking official—to transform CDB.

Chen is often described as a man with a vision, and he arrived at CDB with a plan to use the bank as a vehicle to spur broader

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[7] Yuxin He, "China Development Bank: the best bank in China?" Gavekal Dragonomics China Insight, July 1, 2010; and "Governor's Message" section of China Development Bank, *2008 Annual Report*, http://www.cdb.com.cn.

[8] Telephone interview with Hong Kong-based journalist, October 20, 2009; the comments of Arthur Kroeber in Richard Spencer, "China's big bang on the world stage," *The Daily Telegraph*, April 1, 2008; and Li Ziyou 李子优，"陈元：开发性金融的先行者," ("Chen Yuan: Pioneer of Development Finance"), 当代金融家 *(Modern Bankers)*, December 15, 2008, as re-posted at http://bank.jrj.com.cn/2008/12/1511453069698-1.shtml.

[9] For more on Chen Yun, see Ezra F. Vogel, "Chen Yun: his life," *Journal of Contemporary China*, Vol. 14, No. 45 (November 2005), pp. 741-759; and Nicholas R. Lardy and Kenneth Lieberthal, eds., *Chen Yun's Strategy for China's Development: A Non-Maoist Alternative* (M.E. Sharpe, 1983), pp. xi-xliii.

changes in China that would benefit the country as a whole.[10] Specifically, he sought to transform CDB into a world-class bank and, in the process, contribute to the reform of China's financial sector, which he regarded as critical to China's re-emergence as a global economic power.[11] He viewed American banks, at least prior to the global financial crisis, as the benchmark against which CDB should be measured, arguing that "Chinese banks can be operated as soundly as American banks. China Development Bank is aiming to become a sound top-ranking international bank."[12]

Chen's public-spiritedness is deeply rooted in his pedigree. As the son of a first generation revolutionary, Chen's career has focused on serving the country his father helped found. Several individuals who know Chen personally have noted that he regards himself as having the best interests of his country at heart.[13] Indeed, Chen's career has been characterized by a desire to do good things for China even as he bolsters the privileged position he and other princelings occupy in China.[14]

Chen's ambition to make CDB into a world-class bank is also the product of his financial acumen and travel in international financial circles. Chen is true banker, having served as a vice-governor of the PBOC from 1988-1998. His position at China's central bank brought him into regular contact with foreign banks and international financial institutions.[15] When he assumed the governorship of CDB, Chen solicited advice and ideas from abroad, drawing on many of the contacts he

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[10] Interviews conducted in Beijing in on May 25-26, 2010 and in Washington, DC on December 11, 2009; Telephone interview with a Hong Kong-based journalist, October 20, 2009; and Hu Shuli 胡舒立, Kang Weiping 康伟平 and Chen Huiying 陈慧颖, "访问陈元" ("Interview with Chen Yuan"), 财经 (*Caijing*), No. 5 (March 5, 2004), as re-posted at http://topic.news.hexun.com/detail.aspx?classid=1&id=587998.

[11] See the remarks of Chen Yuan in Li Luyang 李路阳, "陈元印象" ("Impressions of Chen Yuan"), 国际金融 (*International Finance*), No. 10 (2000), p. 7.

[12] Li, "Impressions of Chen Yuan," p. 7.

[13] Interviews conducted in Beijing on May 25-26, 2010.

[14] I thank Barry Naughton for this point.

[15] Interviews conducted in Beijing on May 25-26, 2010.

established while at PBOC. Chen also set up an international advisory council, whose members have included Paul Volcker, former chairman of the U.S. Federal Reserve System, and Andrew Crockett, a former Bank of England official.

Chen's entrepreneurship also contributed to his transformation of CDB. Chen takes great pride in CDB's "blue ocean" strategy—the creation of new market space—at home and abroad.[16] Domestically, CDB pioneered the development of China's bond markets. Internationally, CDB is the dominant financier of the overseas expansion of Chinese firms and the Chinese bank that has been most successful in leveraging China's financial strength to secure energy and natural resources abroad.

One of CDB's most popular innovations, which China's commercial banks adopted, is the use of local government investment corporations (LICs) to finance local infrastructure. The LICs borrow on behalf of local governments, which are not allowed to issue bonds or borrow directly from banks to raise capital. These corporations, which borrowed almost exclusively from CDB until the late 2000s, were initially a very effective vehicle for financing infrastructure projects. However, they became a cause for considerable concern when their borrowing, increasingly collateralized by inflated land values instead of local government fiscal revenues, expanded dramatically during the 2009 economic stimulus program.[17] Victor Shih of Northwestern University estimates that LICs had borrowed RMB 11.4 trillion—34 percent of China's Gross Domestic Product—from state banks by the end of 2009.[18]

Finally, Chen also had the power to make his vision a reality.

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[16] Rui Chenggang 芮成钢，"陈元：建议中国企业去拥有资源和能源的海外地区收购" ("Chen Yuan: Recommending Chinese enterprises make acquisitions in overseas areas with resources and energy"), 经济观察报 *(Economic Observer)*, July 17, 2009, as re-posted at http://finance.ifeng.com/news/hgjj/20090717/956257.shtml#.

[17] He, "China Development Bank: the best bank in China?" pp. 1 and 3.

[18] Victor Shih, "Big rock-candy mountain," *China Economic Quarterly*, June 2010, pp. 26-32.

Chen's status as the eldest son of Chen Yun provides him with enormous political clout. His pedigree undoubtedly played a role in CDB's ability to decline loans to projects championed by local and central government officials and managers of state-owned enterprises and to ensure that borrowers repaid their debts.

Chen Yuan, however, is not an entirely independent actor. CDB's mission is to support the Chinese government's medium- to long-term development strategies and policies.[19] Consequently, the strategic priorities of the Chinese government, as they are understood at any given time, define the parameters in which Chen operates. That said, he has a considerable amount of autonomy in determining how CDB responds to the guidance it receives from above.

The Chinese leadership's domestic and foreign policy agendas provided Chen with both the opportunity and the incentive to transform CDB. When strengthening China's financial system rose to the top of the Chinese leadership's agenda in the late 1990s, Chen saw an opening to make CDB into one of China's healthiest banks. Similarly, the Chinese political establishment's endorsement in 2002 of the overseas expansion of Chinese firms, especially to acquire energy and natural resources in short supply in China, paved the way for CDB to internationalize.

Creating a More Commercial Institution

The high priority that Chinese leaders attached to financial reform in response to the Asian financial crisis of 1997-1998 set the stage for Chen Yuan to change CDB into a more commercially oriented institution. China's banking system was in dire straits by the late 1990s.[20] Non-performing loans (NPLs), largely due to persistent government intervention, were about

[19] See the mission statement in China Development Bank, *2009 Annual Report*, p. 1.

[20] Nicholas Lardy, *China's Unfinished Economic Revolution* (Brookings Institution Press, 2008), pp. 92-127.

40 percent of total outstanding loans.[21] The implosion of the previously dynamic economies of Indonesia, South Korea and Thailand in the fall of 1997 led to concerns in Beijing that a similar collapse of China's fragile banking system, which was sicker than those of its neighbors, might plunge China into economic collapse and political instability.[22] Zhu Rongji, about to begin his tenure as premier, played up the threat posed by the Asian financial crisis to China in a bid to centralize control over the banking sector and bolster his political influence by tackling China's NPL problem.[23]

Chen took advantage of the leadership's newfound resolve to strengthen China's financial system to transform CDB into an institution that profitably supports government policy objectives. He arrived at CDB with a deep appreciation of the threat China's NPL problem posed to China's continued economic development from the ten years he served as a vice governor of the PBOC. As Yuxin He has observed, Chen was much more forward-leaning than the heads of China's big four commercial banks in that he embraced profitability as a top priority much earlier than they did.[24] Indeed, the first goal Chen set for himself as governor of CDB was for CDB to become a "real bank" *(zhenzheng de yinhang)* and not a "government loan distribution machine" *(zhengfu de fangkuan jiqi)*.[25] This objective was paradoxical because CDB had been created to lend to the very types of projects that "real banks" would not finance.[26]

By all accounts, he delivered a stellar performance. The most oft-cited indicator of Chen's success is the dramatic reduction in the bank's NPL ratio that occurred on his watch (see figure

[21] Naughton, *The Chinese Economy*, p. 461.

[22] Victor C. Shih, *Factions and Finance in China: Elite Conflict and Inflation* (Cambridge University Press, 2009), pp. 26-27 and 165.

[23] Victor Shih, "Dealing with Non-Performing Loans: Political Constraints and Financial Policies in China," *The China Quarterly*, No. 180 (December 2004), p. 932.

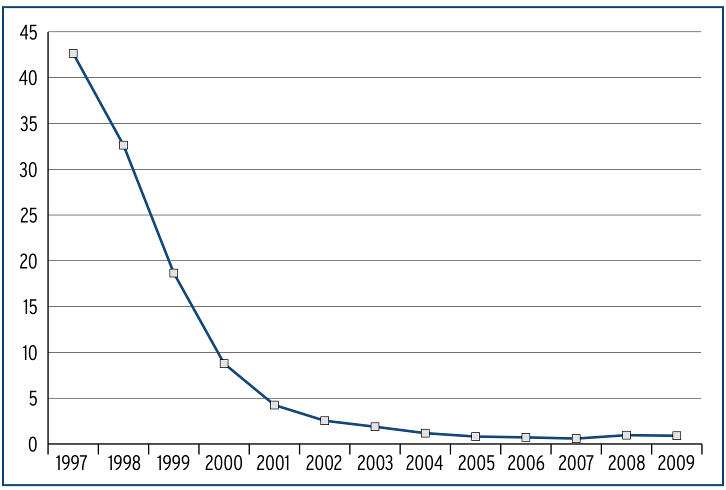
[24] He, "China Development Bank: the best bank in China?"

[25] "陈元：做一个真正的银行家" ("Chen Yuan: Being a Real Banker"), 经济观察报 *(Economic Observer)*, October 30, 2009, as re-posted at http://finance.people.com.cn/GB/10294520.html.

[26] I thank Barry Naughton for this point.

1). In 1997, the year before Chen took charge of CDB, its NPL ratio was 42.65 percent.[27] Four years later, CDB's NPL ratio fell below 5 percent, the international benchmark of economic health.[28] Since 2005, the bank's NPL ratio has been less than 1 percent. The drop in CDB's NPL ratio contributed to the surge in its net profits from 684.5 million RMB in 1999 to 31.9 billion RMB in 2009 (see figure 2). As a result, CDB now has the soundest balance sheet of any major Chinese bank, with a lower NPL ratio than those of the China Eximbank of China, the Agricultural Development Bank and the big four state banks (see table 1).

FIGURE 1: CDB's Non-performing Loan Ratio, 1997-2009

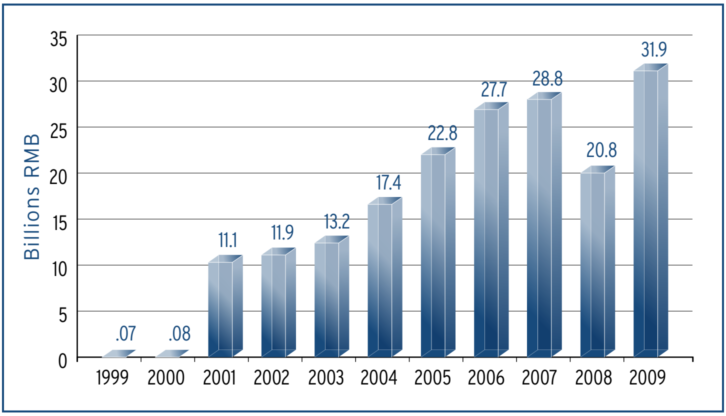


Sources: China Development Bank, annual reports for 2000-2009, http://www.cdb.com.cn; Hu Shuli 胡舒立, Kang Weiping 康伟平 and Chen Huiying 陈慧颖, "访问陈元;" ("Interview with Chen Yuan"), 财经 (*Caijing*), No. 5 (March 5, 2004), http://topic.news.hexun.com/detail.aspx? classid=1&id=587998; and Wang Zhenjiang 王镇江, "从政策性到商业化 国开行大象转型" ("From Policy to Commercialization; China Development Bank's Major Transformation"), 21世纪经济导报 (*21st Century Business Herald*), January 6, 2009, http://www1.21cbh.com/HTML/2009-1-6/HTML_NEDAO0V4CQKK.html.

[27] Wang Zhenjiang 王镇江, "从政策性到商业化 国开行大象转型" ("From Policy to Commercialization; China Development Bank's Major Transformation"), 21世纪经济导报 (*21st Century Business Herald*), January 6, 2009, http://www1.21cbh.com/HTML/2009-1-6/HTML_NEDAO0V4CQKK.html.

[28] Naughton, *The Chinese Economy*, p. 461.

FIGURE 2: CDB's Net Profits, 1999-2009



Sources: China Development Bank, annual reports for 2000 and 2005-2009, http://www.cdb.com.cn.

TABLE 1: Non-performing Loan Ratios of Selected Chinese Banks, 2005-2009 (%)

	2005	2006	2007	2008	2009
China Development Bank	0.81	0.72	0.59	0.96	0.90
Export-Import Bank of China	4.91	3.47	2.45	1.52	1.10
Agricultural Development Bank of China	10.20	7.65	6.29	3.80	3.61
Bank of China	4.62	4.04	3.12	2.65	1.52
China Construction Bank	1.50	2.21	2.60	3.29	3.84
Industrial and Commercial Bank of China	4.69	3.79	2.74	2.29	1.54
Agricultural Bank of China	26.17	23.43	23.57	4.32	2.91

Sources: China Development Bank, *2009 Annual Report*, http://www.cdb.com.cn; Export-Import Bank of China, annual reports for 2005-2009, http://english.eximbank.gov.cn; Agricultural Development Bank of China, annual reports for 2005-2009, http://www.adbc.com.cn; Bank of China, *Annual Report 2009*, http://www.bankofchina.com; China Construction Bank, *2009 Annual Report*, http://www.ccb.com; Industrial and Commercial Bank of China, *2007 Annual Report* and *2009 Annual Results Announcement*, http://www.icbc-ltd.com; and Agricultural Bank of China, annual reports for 2006 and 2009, http://www.abchina.com.

To be sure, Chen Yuan received a helping hand from the government in reducing CDB's NPL ratio. In 1999, the Ministry of Finance created four asset management corporations to take over the bad loans of the big four state banks, the People's Bank of China and CDB. CDB transferred 100 billion yuan of bad loans to the China Xinda Asset Management Corporation in 1999.[29] That year the bank's NPL ratio plummeted by 13.97 percent.

Chen, however, deserves credit for stemming the creation of new NPLs through good management. In particular, he implemented several risk management mechanisms that feature prominently in narratives of the pivotal role he played in transforming CDB. First, Chen sought to depoliticize the lending process and ensure that CDB would earn positive returns by instituting a new system for processing loan applications that separated the individuals who evaluate loan applications from those with the authority to make lending decisions. Loan applications are evaluated separately by four bureaus within CDB which forward their assessments to a lending committee, headed by a vice-governor, which votes on each application by registered ballot. Chen has the power to veto positive recommendations made by the committee but does not have the authority to overturn negative ones.[30] CDB shocked many state-owned enterprise managers and government officials who regarded the bank as a provider of "free lunches" by rejecting their loan applications.[31] CDB even turned down proposals from the National Development and Reform Commission

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29 "Chen Yuan: Being a Real Banker."

30 "国家开发银行防范中长期信贷风险系列报道（七)" ("A Series of Reports on China Development Bank's Precautions Against Medium- and Long-term Credit Risk (7)"), 中国经济时报 *(China Economic Times)*, February 1, 2005, as re-posted at http://www.cdb.com.cn/web/NewsInfo.asp?NewsId=569; Zhong Jiayong 钟加勇 and Ning Nan 宁南, "新国家开发银行" ("The New China Development Bank"), 商务周刊 *(Business Watch Magazine)*, No. 22 (2003), as re-posted at http://qkzz.net/magazine/1009-4865/2003/22/182584.htm; and Kathy Chen, "Giving Credit Where Credit Is Due in China; China Development Bank Turns Around, Rejecting the Powerful, Dispelling Idea It's a Source of Easy Money," *Wall Street Journal*, June 24, 2004.

31 Chen, "Giving Credit Where Credit Is Due in China."

(NDRC), whose predecessor, the State Planning Commission (SPC) had directed much of the bank's lending before 1998.[32]

Second, Chen made local officials his partners in helping CDB avoid accumulating new bad debts by making future lending to local governments contingent upon current borrowers within their jurisdiction repaying CDB.[33] For example, Chen told the Tianjin Party Secretary that CDB would be willing to provide him with 10 to 20 billion RMB for large-scale urban construction and the renovation of older parts of the city if he would assist CDB with the recovery of the 2 billion RMB it was owed by a local car company, Tianjin Xiali. Two years later, CDB had its money back.[34] This strategy was particularly effective for CDB because it is a critical source of funding for local governments through its loans to LICs. The importance of CDB to local governments is reflected by the jingle, "those who are liberated should not forget the Chinese Communist Party; those who have developed should not forget China Development Bank" ("*fanshen buwang gongchandang, fazhan buwang kaifahang*").[35] Moreover, local officials gave Chen their personal assurance that borrowers within their jurisdiction would pay back CDB, so their reputations were at risk.[36]

Third, Chen established a market-based mechanism for CDB to raise funds, which became a form of self-imposed pressure to support profitable projects.[37] When Chen arrived at CDB, the bank funded itself through the sale of bonds, primarily

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[32] For information on the State Planning Commission's role in directing CDB's initial lending, see Nicholas Lardy, *China's Unfinished Economic Revolution* (Brookings Institution Press, 1998), p. 180. For information about CDB rejecting loan applications from the NDRC, see "Chen Yuan: Being a Real Banker"*);* and "陈元接受凤凰专访：中国应抓住能源输出国转向机遇" ("Phoenix TV's Exclusive Interview with Chen Yuan: China should take advantage of the shift in focus of energy exporting countries"), 凤凰卫视 (*Phoenix TV),* August 8, 2009, http://news.ifeng.com/mainland/200908/0808_17_1291577.shtml.

[33] Zhong and Ning, "The New China Development Bank."

[34] "Chen Yuan: Being a Real Banker."

[35] Zhong and Ning, "The New China Development Bank."

[36] Telephone interview with Hong Kong-based journalist, October 20, 2009.

[37] This paragraph is based on He, "China Development Bank: the best bank in China?" p. 2.

to other state-owned banks, at a fixed interest rate that guaranteed CDB a slim margin. Six months into Chen's tenure as governor of CDB, the bank began to sell its bonds on the Chinese interbank bond market, which accounted for more than 75 percent of CDB's funds in 2009 (see table 2).[38] In contrast, China's commercial banks are guaranteed a profit by the gap between the maximum deposit rate and the minimum loan rate. As a result, CDB has had to work harder than China's commercial banks to assess credit risk.[39]

TABLE 2: CDB's Sources of Funding, 2009

	Amount (RMB million)	Share (%)
Bond Issuance	3,188,397	76.62
Subordinated Debts	79,638	1.92
Borrowings from governments and financial institutions	264,637	6.36
Customer deposits	547,345	13.15
Other	81,128	1.95
Total	4,161,145	100.00

Source: China Development Bank, *2009 Annual Report*, p. 42.

Chen's transformation of CDB was motivated by a desire to serve the country his father helped create.[40] Chen, who regarded reforming China's financial system as the key to China becoming a modernized economy, sought, with some success, to make CDB a catalyst for change in China's financial sector.[41] Indeed, the dramatic reduction of China's NPL ratio that occurred under his leadership can be understood as an attempt to spur the reform of China's financial sector. Chen's efforts to make CDB more commercially viable than China's ostensibly

[38] China Development Bank, *2009 Annual Report*, p. 42.

[39] I thank Arthur Kroeber for this point.

[40] Several observers and acquaintances of Chen Yuan stated that he did not view his position at CDB as just a job but as an opportunity to help make China great. Telephone interview with Hong Kong-based journalist, October 20, 2009; and interview with an economist, Washington, DC, December 11, 2009.

[41] For Chen's views on the importance of a strong financial system, see "Chen Yuan: Being a Real Banker."

commercial banks constituted a challenge to China's big four state banks—which, in theory, were supposed to be healthier than China's policy banks—to work harder to clean up their balance sheets. As Chen told the *Financial Times* in December 2006, "we try to be better than other commercial banks. We are one of the best performing-banks in the world."[42]

CDB also contributed to the reform of China's financial sector with its pioneering role in the development of China's bond and securitization markets.[43] One of his first moves in this direction, championed by Zhu Rongji, was to attempt to establish a world-class investment bank under CDB.[44] Although their plan to create China's "Goldman Sachs" suffered defeat at the hands of government ministries intent on preventing the emergence of a powerful competitor to the country's commercial banks, Chen continued to lobby the State Council for permission to issue and underwrite a variety of financial instruments that he maintained would contribute to the development of China's financial markets.[45] His persistence paid off. In 2000, CDB received a license to underwrite corporate bonds. Five years later, CDB was one of the first two banks to gain State Council approval to sell asset-backed securities. Chen's success in expanding CDB's operations beyond development finance to include investment banking activities is an

[42] Andrew Yeh, "Barometer of the communist party's ambitions for the 21st century," *Financial Times*, December 12, 2006.

[43] "The bond builder," *Asiamoney*, November 2006; "China—Developing Debt," *Asiamoney*, November 2006; and "Securitizing China," *Asiamoney*, February 2006.

[44] See the section on "国开行金融控股梦想" ("CDB's dreams of being a majority shareholder") in Liu Xinran 刘欣然 and Li Zhenhua 李振华, "监管三部意见分歧 国开行收购南方证券前途未卜" ("Different opinions exist among the three supervising bodies; the future of China Development Bank's plan to acquire Southern Securities is Uncertain"), 21世纪经济导报 *(21st Century Business Herald)*, December 25, 2004, as re-posted at http://finance.qq.com/a/20041225/000041.htm; Qu Liqiu 曲力秋, "朱镕基的学生们" ("Zhu Rongji's Students"), *21世纪经济导报 (21st Century Business Herald)*, February 2, 2001, as re-posted at http://www.chinanews.com.cn/2001-02-12/26/69578.html; Hu, Kang and Chen, "Interview with Chen Yuan;" and "Why China still doesn't have an investment bank it can call its own," *EIU Business China*, September 13, 1999.

[45] See Liu and Li "Different opinions exist among the three supervising bodies;"and "Why China still doesn't have an investment bank it can call its own."

example of how he combined his ambition and his political connections to realize his vision for CDB.

Despite Chen Yuan's efforts to turn CDB into a more competitive and commercially viable institution, his vision most likely did not include converting CDB to a truly commercial bank. Although Chen runs CDB like a commercial bank, he does not want CDB to be regulated as one.[46] Indeed, CDB has capitalized on its policy bank status and Chen Yuan's entrepreneurship and political clout to successfully vie with the commercial banks for lucrative business opportunities. First, CDB has a historical advantage in financing infrastructure and strategic industrial projects.[47] CDB has funded some of China's largest infrastructure projects, including the Three Gorges Dam, the South-to-North Water Diversion Project, the West-East Natural Gas Pipeline and the Qinghai-Tibet Railway. Second, CDB extends loans with terms substantially longer than those made by the commercial banks. Because it is financed by bonds with terms of up to 30 years rather than short-term bank deposits, long term lending is less risky for CDB than for the commercial banks, whose primary source of funding is the absorption of deposits and borrowing on the Chinese interbank market. Third, CDB is the preferred lender of many local governments because of the LICs that the bank pioneered. These advantages helped CDB stave off competition from the commercial banks for projects such as roads, bridges, railroads, and communications, which became increasingly profitable—and attractive to the commercial banks—in the wake of China's property boom in the 2000s.[48]

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[46] Telephone interview with Hong Kong-based journalist, October 19, 2009.

[47] Sun Wen 孙闻, "国开行商业化转型将加剧银行竞争" ("China Development Bank's commercialization will intensify bank competition"),证券时报 *(Securities Times)*, February 22, 2008, as re-posted at http://bank.hexun.com/2008-02-22/103978072.html.

[48] Sun, "China Development Banks' commercialization will intensify;" and "国开行"商"味渐浓" ("China Development Bank's 'commercial' flavor gets stronger"),中国经济周刊 *(China Economic Weekly)*, August 7, 2006, as re-posted at http://news.xinhuanet.com/fortune/2006-08/07/content_4929270.htm, 2006, http://www.cs.com.cn/csnews/yhwh/03/t20060808_974976.htm.

CDB also ventured into what the commercial banks regard as their territory with its provision of buyer's credit lines to two leading telecommunications equipment manufacturers, Huawei and ZTE, in 2001.[49] In addition, CDB irritated the commercial banks when it began to conduct investment banking activities. As a policy bank, CDB is not bound by China's Commercial Banking Law, which forbids commercial banks from engaging in both commercial and investment banking.[50] Consequently, the commercial banks had to sit on the sidelines while CDB profited from underwriting the corporate bonds of major state-owned enterprises. This uneven playing field prompted the commercial banks to lobby the State Council to commercialize CDB.[51]

The commercial banks found allies in the central government. They included the China Banking Regulatory Commission (CBRC), which sought to gain regulatory authority over CDB and the other policy banks, and several ministries, including the NDRC and the Ministry of Finance, which had grown alarmed by the practice, pioneered by CDB and subsequently adopted by commercial banks, of using rising land values to collateralize loans to LICs to finance public infrastructure.[52] This technique, which allowed CDB to rapidly expand its loan portfolio, tempted local governments to inflate land values and borrow excessively (see figure 3).[53] The proponents of commercializing CDB appeared to secure a victory in January 2007 when Premier Wen announced during the Third National Financial Work Conference that all three policy banks would be converted to commercial banks, beginning with CDB.[54]

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[49] Zhong and Ning "The New China Development Bank;" and "Policy Banks, Commercial Banks Vie for Market Share," *Xinhua Economic News Service*, July 11, 2001.

[50] Zhong and Ning "The New China Development Bank."

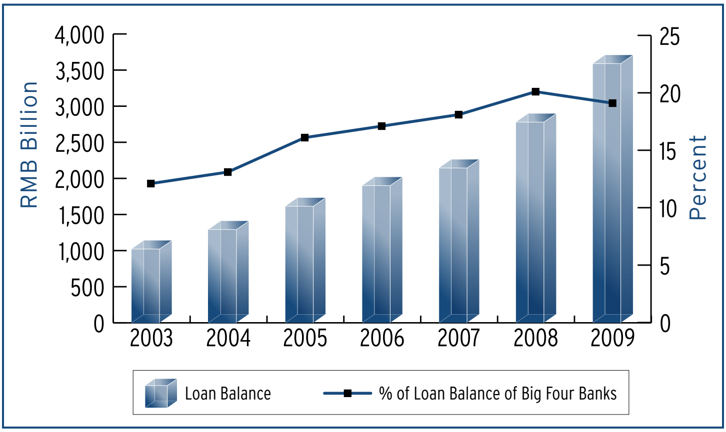
[51] See, for example, "China Development Bank's 'commercial' flavor."

[52] Interviews, Beijing, China, October 19, 2009; telephone interview with Hong Kong-based journalist, October 20, 2009; and He, "China Development Bank: the best bank in China?" pp. 4-6.

[53] He, "China Development Bank: the best bank in China?" pp. 4-6.

[54] "全国金融工作会议在北京召开 温家宝作重要讲话" ("National Economic Work Conference convened in Beijing; Wen Jiabao delivers an important speech"), 人民日报 *(People's Daily)*, January 21, 2010, http://finance.people.com.cn/GB/8215/80348/80351/5539956.html.

FIGURE 3: CDB's Loan Balance, 2003-2009



Sources: China Development Bank, annual reports for 2007 and 2009, http://www.cdb.com.cn; Agriculture Bank of China, annual reports for 2004, 2006 and 2009, http://www.abchina.com; Bank of China, annual reports for 2007 and 2009, http://www.bankofchina.com; China Construction bank, annual reports for 2004 and 2009, http://www.ccb.com; Industrial and Commercial Bank of China, *2009 Annual Results Announcement* and annual reports for 2003, 2005, and 2008, http://www.icbc-ltd.com.

CDB nominally became a commercial bank at the end of 2008. In December, CDB began operating as a joint-stock company, CDB Corporation, with registered capital of RMB 300 billion provided by its two shareholders, the Ministry of Finance and Central Huijin.[55] The central authorities appointed Chen Yuan chairman and Jiang Chaoliang, the former chairman of the Bank of Communications, president of CDB Corporation. (These appointments probably reflected both Chen Yuan's staying power and the Chinese leadership's desire to have a rising star from one of China's top commercial banks help guide the reform of CDB.)[56] These changes prompted the CBRC to declare that CDB was a commercial bank.[57]

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[55] "Reorganization, Changes in Share Capital and Particulars of Major Shareholders" section of China Development Bank, *2008 Annual Report*, http://www.cdb.com.cn.

[56] Telephone interview with Beijing-based businessman, November 13, 2009.

[57] "银监会有关负责人就国家开发银行转制答记者问" ("Responsible officials from the China Banking Regulatory Commission answer reporters' questions about China Development Bank's restructuring"), December 23, 2008, http://www.gov.cn/gzdt/2008-12/23/content_1185268.htm.

Fortunately for Chen Yuan, the global financial crisis provided CDB with an opportunity to undermine the commercialization process by demonstrating its indispensability as a policy bank that China's leaders can rely on to advance their domestic and foreign policy priorities. CDB officials have both privately and publicly lobbied the central authorities to postpone further commercialization reforms.[58] First, the bank's leadership was quick to point out that although China has many large commercial banks, it only has one bank—CDB—that provides the medium- and long-term financing that China needs to complete its urbanization and industrialization processes.[59] Second, they have stressed CDB's centrality to the government's post-financial crisis agenda. In a speech in late 2009, CDB Vice Governor Cai Huaxiang pointed out that CDB has a dominant position in financing the very types of projects that comprised the bulk of the 4 trillion RMB economic stimulus package unveiled by the central government in November 2008, including roads, railroads, airports, irrigation, public housing and the Wenchuan earthquake reconstruction.[60] He similarly highlighted how CDB took advantage of the global financial crisis to advance China's energy strategy by extending EBLs to major energy producers hurt by the collapse in oil prices and the credit crunch in 2009. Third, CDB officials have warned that the elimination of the near sovereign rating of CDB bonds—which the CBRC has announced will be phased out at the end of 2011—will make it more difficult for CDB to serve as the government's first choice for financing national strategic projects that the commercial banks are unable or

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[58] "国开行改制进退" ("CDB's reform is in a fix"), 经济观察报 *(Economic Observer)*, January 9, 2010, as re-posted at http://business.sohu.com/20100110/n269475972.shtml.

[59] *Ibid.*; Xu Ai 徐瑷, "国开行原副行长谈如何破决草根金融难题" ("Former Vice Governor of China Development Bank Discusses How to Eliminate Basic Financial Problems"),南风窗(*Nanfengchuang Magazine)*, August 21, 2009, as re-posted at http://news.sohu.com/20090822/n266152816.shtml; and "蔡华相：国开行不会转型成为传统商业银行" (Cai Huaxiang: China Development Bank will not be transformed into a traditional commercial bank"), 网易财经 *(Netease.com)*, November 5, 2009, as re-posted at http://money.163.com/09/1105/13/5NC2NTHD00253T9E.html.

[60] Cai Huaxiang: China Development Bank will not be transformed."

unwilling to support because such a change will increase the bank's funding costs.[61] Vice Governor Cai has further argued that if CDB has trouble raising funds, then China's economic security and even its social stability will be threatened.[62]

The stalling of the commercialization process in the wake of the global financial crisis indicates that the State Council may have concluded that it needs CDB to continue to function as a policy bank. Some additional reforms that would have made it more difficult for the Chinese leadership to rely on CDB to support their policy priorities have been, or are likely to be, postponed. First, CDB has shelved plans to do an initial public offering and introduce foreign investors, both of which would have made CDB answerable to actors other than the central authorities, complicating the bank's ability to advance the Chinese leadership's policy priorities.[63] Second, the State Council halted the commercialization plans of another policy bank, China Eximbank, in January 2010 when it rejected its capital injection proposal.[64] Third, at the end of 2009, a CDB official told the *Financial Times* that CDB would continue with "business as usual"—supporting government projects and policies, with the international expansion of Chinese firms ranking as one of CDB's most important tasks.[65] Indeed, as discussed below, Chen Yuan seized on CDB's emergence as the main

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[61] "CDB's reform is in a fix;" "Cai Huaxiang: China Development Bank will not be transformed;" and "国家开发银行2010年底前所发债券风险权重仍未零" ("The risk weight of bonds issued by CDB before the end of 2010 will remain zero,") 新华社 (*Xinhua*), February 17, 2009, http://www.gov.cn/jrzg/2009-02/17/content_1233991.htm, and "China: China Development Bank's Bonds To Keep Sovereign Rating Until End-2011," *TendersInfo*, July 12, 2010.

[62] "Cai Huaxiang: China Development Bank will not be transformed."

[63] Zhu Bao 朱宝, "国开行：暂无上市计划" ("CDB" No plans to list for now"), *21 世纪经济导报 (21st Century Business Herald)*, July 30, 2009, as re-posted at http://business.sohu.com/20090730/n265588545.shtml.

[64] Zhang Yuzhe 张宇哲, "进出口行和中信保注资或将减至500亿元"（"The capital injected into the Export Import Bank of China and Sinosure will probably be reduced to $50 billion Yuan"), 新世纪周刊 *(New Century Weekly)*, February 1, 2010, http://finance.caing.com/2010-02-01/100112500.html. I thank Yuxin He for this point.

[65] Jamil Anderlini, "CDB turns away from the path of reform," *Financial Times*, November 2, 2009.

financier of China's "going out" strategy in general and cross-border energy deals in particular as a key reason why CDB should retain its status as a policy bank.

Creating a More International Institution

The Chinese political establishment's endorsement of the "going out" strategy—foreign investment by Chinese firms to secure energy and raw materials, build national champions, and acquire advanced technologies—at the Sixteenth National Congress of the Chinese Communist Party in November 2002 paved the way for Chen Yuan to transform CDB into a global institution. Prior to the Sixteenth Party Congress, then-General Secretary Jiang Zemin had already begun to champion the international expansion of China's NOCs. China had become a net importer of oil in 1993, and by the late 1990s China's leaders had begun to perceive the widening gap between China's oil demand and domestic supply as a long-term strategic problem.[66] In two speeches in early 2000, Jiang advocated overseas exploration and production by China's NOCs as a way to help secure oil for China's long-term economic development, noting that the United States and other western countries were stepping up their efforts to gain control over global oil resources.[67] Although China's NOCs had been investing abroad since the early 1990s, they had done so without much support from the central government.[68] The situation changed after Jiang called for more support for Chinese companies investing overseas in his political report to the Party Congress.[69]

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[66] Bo Kong, *China's International Petroleum Policy* (Praeger Security International, 2010), pp. 44-46.

[67] For information on Jiang Zemin's role in promoting the "going out" strategy, see the following report from the Chinese Communist Party's Central Document Research Institute: Chen Yangyong 陈扬勇, "江泽民"走出去"战略的形成及其重要意义" ("The formation and significance of Jiang Zemin's 'going out' strategy"), 人民网 *(People's Daily Online)*, November 10, 2008, http://finance.people.com.cn/GB/8215/126457/8313172.html.

[68] Kong, *China's International Petroleum Policy*, pp. 44.

[69] "Xinhua carries 'full text' of Jiang Zemin report at 16th National Party Congress," *World News Connection*, November 17, 2002.

Once again, Chen demonstrated his talent for addressing a pressing problem confronting China's leaders. The Chinese leadership had identified the growing domestic shortages of energy and minerals such as iron ore and copper as an increasingly acute threat to the realization of China's long-term development goals, and Chen responded by making CDB a key supporter of the international expansion of Chinese energy and mining companies.[70] Just as he turned CDB into one of China's healthiest banks after the Asian financial crisis catapulted financial reform to the top of the Chinese leadership's agenda, Chen addressed new leadership priorities while expanding the bank's business. CDB's outstanding foreign currency loans expanded from $16.5 billion in 2005 to $97.4 billion in 2009, accounting for 17 percent of the bank's outstanding loans (see figure 4).[71] The following year, the bank's outstanding foreign currency loans reached $141.3 billion.[72] In 2008, CDB surpassed the Bank of China to become the Chinese bank with the largest portfolio of foreign currency denominated loans.[73] Although CDB has not made publicly available the share of its outstanding foreign currency loans dedicated to energy and natural resource projects, one interlocutor from CDB told

[70] For more information on the high priority CDB attaches to energy and natural resources, see "开发性金融合作：发展中国家共同发展之道" ("Development Finance: The Common Development Path of Developing Countries"),中国经济 (*Economy of China*), December 30, 2009, http://www.economyofchina.com/cms/html/zazhi/wangqi/2010nian1yuekan/fengmian/2009/1230/518.html#; Liu Wenfang 刘文芳, Deputy Director, International Financial Department, China Development Bank, "国家开发银行"走出去" '走出去' 情况报" ("Situation Report on China Development Bank 'Going Out'"), Remarks to the China-Africa Business Council, January 7, 2006, http://www.cabc.org.cn/news/2006-1-7/200617141958.html; "官员：国开行支持国内企业收购境外公司的股权" ("Official: CDB supports the acquisition of shares in foreign firms by domestic firms"), 和迅网 *(Hexun Online)*, April 23, 2008, http://news.hexun.com/2008-04-23/105509683.html.

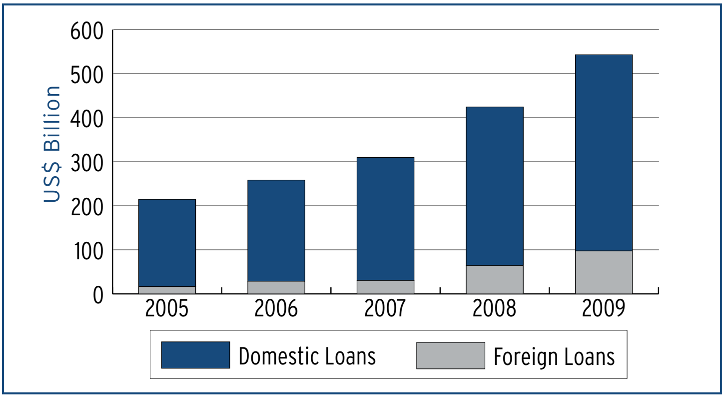
[71] China Development Bank, *2009 Annual Report*, pp. 6 and 57.

[72] Cao Hua 曹华, "国开行去年末外汇贷款余额1413亿美元 国际合作实现又好又快发展" ("China Development Bank's foreign currency loan balance was $141.3 billion last year; international cooperation achieved sound and rapid development"), 人民网 *(People's Daily Online)*, February 14, 2011, http://bank.finance.people.com.cn/GB/13914363.html#.

[73] "Governor's Message" section of China Development Bank, *2008 Annual Report*, http://www.cdb.com.cn.

Caijing magazine that the majority of the foreign currency loans made by CDB in 2009 were for these types of projects.[74]

FIGURE 4: CDB's Foreign and Domestic Lending, 2005-2009



Sources: China Development Bank, annual reports, http://www.cdb.com.cn.

CDB helps China's state-owned enterprises access energy and natural resources abroad in several ways. First, CDB provides financing to Chinese firms for foreign energy and mining investments. As Chen Yuan told the *Financial Times* in 2006, "we follow the biggest market players in China" abroad.[75] CDB's management made the decision to support the overseas expansion of Chinese energy and mining firms in response to both government policy and market needs. Not only did the Chinese political establishment's endorsement of the "going out" strategy create a new national interest for CDB to advance, but the difficulties Chinese state-owned enterprises faced in securing financing for foreign direct investment created a new business opportunity for CDB. According to the bank's annual report for 2004:

"A number of Chinese enterprises have been exploring opportunities overseas and some of the potential projects are

[74] "资源类贷款推高国开行外汇贷款" ("Natural resource loans drive up CDB's foreign currency loans"), 财经 *(Caijing)*, October 28, 2009, http://www.caijing.com.cn/2009-10-28/110296815.html.

[75] Richard McGregor and Andrew Yeh, "China Development Bank Backs Push to Invest Overseas," *Financial Times*, December 6, 2006, p. 1.

relatively large. The high risk inherent in such projects and their relatively large borrowing requirements have made many commercial banks uncomfortable about participating in their funding. Many of the enterprises in search of financing for outbound investment have turned to us. In reality, these projects are typical of the development financing that we typically undertake and we are well-positioned to be of service. We are known to have both the adequate resources to fund these projects and a demonstrated track record of achievement in effectively managing the credit risk."[76]

CDB's first loan to a Chinese company for overseas resource exploration and production went to Sinochem in 2003 to fund its acquisition of Atlantis—a subsidiary of Norway's Petroleum Geo-Services (PGS) with assets in Oman, Tunisia and the United Arab Emirates—initially estimated to be worth about $215 million.[77] Sinochem sought to borrow $413 million to finance the purchase of Atlantis and for exploration and production. China's commercial banks refused to provide a loan because the proposed debt to equity ratio was too high. Sinochem then applied for credit from CDB, which agreed to provide $230 million with a term longer than that of a typical commercial loan.[78] Sinochem subsequently acquired Atlantis for $105 million.[79]

In 2005, CDB joined hands with the NDRC to provide additional financial support for key overseas investment projects,

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[76] "Our Growing Business" section of China Development Bank, *2004 Annual Report*, http://www.cdb.com.cn.

[77] "中化公司石油勘探开发获开发行2.3亿美元支持" ("Sinochem receives $230 million in support from CDB for oil exploration and production"), September 17, 2003, http://www.sinochem.com/tabid/932/InfoID/5863/frtid/930/Default.aspx18, 2003, http://www.sasac.gov.cn/m1180/n1226/n2410/n314274/1222885.html; and Kate Dourian, David Thomson and Winnie Lee, "Sinochem Enters Persian Gulf with Atlantis Buy," *Platt's Oilgram News*, January 22, 2002.

[78] Chen Yuan 陈元, editor, 加强对外合作， 扩大我国能源，原材料来源战略研究 (*Research on Expanding International Cooperation and Expanding China's Strategy for Sourcing Energy and Raw Materials*) (中国财政经济出版社 [China Financial and Economic Publishing House] 2007), p. 279.

[79] "Update 1—PGS seals sale of Atlantis for $105m," *Reuters*, January 24, 2003.

including the development of natural resources. According to the circular released by the two institutions, CDB and NDRC annually draft a plan for financial support for key overseas investment projects, and CDB earmarks a portion of its annual credit budget to bankroll such projects. CDB independently assesses the project applications and will consider providing preferential interest rates on a project-by-project basis.[80]

Other foreign energy acquisitions financed by CDB include CNPC's purchase of Petrokazakhstan for $4.2 billion in 2005, CITIC Group's purchase of the Kazakhstan oil assets of Canada's Nations Energy for $1.9 billion in 2006, and the acquisition of a 97 percent stake in Russia's Udmurtneft by China Petrochemical Corporation (Sinopec) for $3.5 billion in 2006.[81] CDB also extended a five-year loan of $30 billion at a discounted interest rate, which has not been publicly disclosed, to CNPC in 2009 for upstream acquisitions abroad.[82]

Second, CDB finances the development of infrastructure to deliver energy and mineral supplies to China. The bank provided financing for the construction of the Kazakhstan-China oil pipeline.[83] It also contributed $8.1 billion to the syndicate financing the construction of the $11 billion Central Asian Natural Gas Pipeline, which runs from Turkmenistan to China via Uzbekistan and Kazakhstan.[84] In addition, in November 2010,

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[80] "国家发展改革委 国家开发银行关于进一步加强对境外投资重点项目融资支持有关问题的通知" ("Notice of the National Development and Reform Commission and China Development Bank about the Relevant Issues Related to Providing More Financial Support to Key Overseas Investment Projects"), National Development and Reform Commission, Document No. 1838 (September 25, 2005), http://www.cpol.gov.cn/tabid/71/InfoID/541/Default.aspx.

[81] Guo Ying 郭影, "中石油与开行签署长期战略合作协议" ("CNPC and China Development Bank sign a long term strategic cooperation agreement"), September 9, 2009, http://news.cnpc.com.cn/system/2009/09/09/001257466.shtml; and the "Governor's Message" and "Strategic Focus (2)" sections of China Development Bank, *2006 Annual Report*, http://www.cdb.com.cn.

[82] Guo, "CNPC and China Development Bank sign a long term strategic cooperation agreement."

[83] "Strategic Focus (2)" section of China Development Bank, *2006 Annual Report*, http://www.cdb.com.cn.

[84] "Overview of Operations (2)" section of China Development Bank, *2008 Annual Report*, http://www.cdb.com.cn.

CDB agreed to lend the government of Myanmar $2.4 billion, which will be used to finance the construction of a natural gas pipeline from Myanmar to Yunnan Province.[85]

Third, CDB provides credit to foreign energy and mining companies, especially those which offer Chinese firms long-term supply contracts, upstream equity positions or equipment manufacturing contracts. The loans that CDB offered to energy companies and banks in Russia, Brazil and Turkmenistan in 2009 are the most prominent examples. Although national energy companies have been the prime beneficiaries of CDB's largesse, the bank is also open for business with companies that are not state-owned. CDB is a member of the syndicate that loaned $1.1 billion to Australia's Woodside Petroleum in 2009 for liquefied natural gas (LNG) development and the syndicate that provided the $1.95 billion commercial loan to the Exxon Mobil-led consortium, PNG LNG, in March 2010 for an LNG project in Papua New Guinea, three months after the consortium finalized a purchase and sale agreement with Sinopec.[86]

CDB finalized one of its earliest natural resource export revenue backed loans in 2006 with China Minmetals Corporation and Corporación Nacional de Cobre de Chile (Codelco). CDB extended $330 million—and China Minmetals provided $220 million—to Codelco in exchange for the sale of 55,750 tons of copper per year at market prices to China Minmetals over fifteen years. CDB's loan has an 11-year term and a fixed 6.5 percent interest rate. The deal also included an option for China Minmetals to acquire a 25 percent stake in Codelco's Gaby mine.[87]

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[85] Tom Grieder, "China Provides Loan to Myanmar to Accelerate Shwe Gas Pipeline Project," *Global Insight*, December 21, 2010.

[86] Richard Morrow, "Australia's deals of the year: syndicated loan," *Asiamoney*, February 2010; and "PNG LNG to close in March with 50% oversubscription," *Project Finance*, February 2010.

[87] "Codelco, Minmetals Sign Copper Supply Deal," *Platts Commodity News*, February 23, 2006.

Chen Yuan employed the same entrepreneurship that he used to tackle CDB's NPL problem to make CDB the dominant financier of China's cross-border energy and mining deals. First, he reorganized CDB to prepare the bank to internationalize its business. CDB headquarters assigned each of its branch offices responsibility for a different part of the world. For example, the Chongqing branch is responsible for the Balkans, the Henan branch is responsible for five countries in South Africa, and the Sichuan branch covers several countries including Nepal.[88] The branch offices began to dispatch work teams abroad in 2006. The teams, which operate out of Chinese embassies, gather information about the host countries, establish relationships with local officials and businesses, and provide logistical support for visiting CDB officials.[89] One important objective of the work teams is to help Chinese energy and mining companies find investment opportunities.[90] By the end of 2009, CDB had established work teams in 141 countries, including Russia, Venezuela, Turkmenistan, Brazil and 45 of the 53 countries in Africa.[91] Some major energy and natural resource projects financed by CDB including the bank's "loans-for-oil" deal with Brazil resulted from the efforts of the bank's work teams to drum up business.[92]

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88 Zhang You 张友, "国开行分解全球试验" ("China Development Bank's global division of labor"), *21世纪经济导报 (21st Century Business Herald)*, May 15, 2007, http://www.21cbh.com/HTML/2007-5-16/HTML_34K1Q4NIA1ST.html.

89 Shi Jiyang, who was a member of CDB work teams dispatched to Bolivia and Peru, wrote a book about his experience in Bolivia, which provides insight into how CDB's work teams operate abroad. Shi Jiyang 石纪杨, 踏上美洲屋脊 (*Steps on the American Ridge*), (中国金融出版社[China Financial Press], 2010).

90 "中国对外投资稳步提速" ("China foreign investment steadily increases")人民日报（海外版） *(People's Daily (overseas edition))*, October 8, 2008, http://finance.people.com.cn/GB/8215/135583/8146228.html.

91 "Development Finance: The Common Development Path;" and "国家开发银行党委委员，中非基金会董事长刘建平在会上发言" ("China Development Bank party committee member and China-Africa Development Fund general manager Liu Jianping's speech"), July 10, 2009, http://www.iprcc.org.cn/front/article/article.action?id=560.

92 "国开行'以贷款换资源'成功运作一批大项目" ("The successful operation of CDB's 'exchange of loans for resources' yields a batch of big projects"), 人民网 (*People's Daily Online*), September 7, 2009, http://finance.people.com.cn/GB/9998603.html.

Second, CDB's partnerships with foreign financial institutions have facilitated the international expansion of Chinese firms. According to Chen Yuan, the Shanghai Cooperation Organization Banking Union that he initiated helped facilitate investment opportunities for Chinese companies in energy, mining and infrastructure projects in member countries.[93] More recently, CDB signed an agency agreement with Australia's ANZ Bank aimed at furthering CDB's objective of substantially expanding CDB's presence in Australia—where CDB has already financed several acquisitions by Chinese mining firms—and elsewhere in the Asia Pacific region. The memorandum of understanding involves ANZ bringing deals to CDB for financing and acting as its agent in Australia, New Zealand and elsewhere in Asia.[94]

CDB's Foray into Western Financials

CDB's highest-profile cross-border deal—the acquisition of a 3.1 percent stake in England's largest commercial bank, Barclays, in 2007 for £1.5 billion—was also partly aimed at bolstering CDB's ability to help China access energy and minerals abroad. One of the attractions of Barclays to CDB was the British bank's expertise in commodities. The two banks announced a Commodities Strategic Alliance in October 2007, three months after CDB became one of Barclays' largest shareholders, which covers Barclays assisting CDB with the development of commodity projects origination and trading capabilities, the strengthening of its commodities execution and risk management infrastructure, and even providing advice on managing the public relations of purchasing assets in countries where being a Chinese state-owned enterprise can be a liability.[95] As CDB Vice

[93] "Development Finance: The Common Development Path;" and "SCO Banking Union Established with Chen Yuan as President," *Xinhua*, November 22, 2005, as re-posted on http://www.cdb.com.cn/english/NewsInfo.asp?NewsId=1199.

[94] Michael Sainsbury, "ANZ seals banking tie with China," *The Australian*, September 30, 2009, p. 35.

[95] "Barclays and China Development Bank form commodities strategic alliance," *The Asian Banker Journal*, October 15, 2007; and Tan Lu 谭璐, "巴克莱联手国开行 紧盯大宗商品交易" ("Barclays joins hands with CDB, keeps a close watch on major commodity deals")"), *21世纪经济导报 (21st Century Business Herald)*, December 29, 2009; http://www.21cbh.com/HTML/2009-12-30/159753.html.

Governor Gao Jian observed at that time, "Barclays is publicly recognized as one of the top three global commodity banks. China Development Bank is confident that Barclays is the right partner to ensure the long-term successful development of CDB's commodities business capabilities as we evolve into a commercially operated financial institution."[96] In 2009, Chen Yuan highlighted the importance of commodities to CDB's investment in Barclays, noting that CDB's cooperation with the British bank was to a very large extent based on the two institutions' shared views of global mining and natural resource markets.[97]

CDB's investment in Barclays was driven by more than commodities. The acquisition also reflected Chen Yuan's ambition to transform CDB into a more internationally oriented institution. The opportunity to become a major shareholder in Barclays initially looked like it would help Chen achieve this goal. Barclays was trying to take over the Dutch bank ABN Amro when it courted investment from CDB. Had the merger been successful, CDB would have purchased an additional £ 5.1 billion of Barclays' shares, and Chen would have been involved in the largest banking merger in history, further raising CDB's international profile. The Barclays deal apparently whetted Chen's appetite for western banks as he went on to line up investment opportunities for CDB in Citibank and Germany's Dresdner Bank in early 2008. However, the Chinese leadership's loss of confidence in western banks in the wake of the global financial crisis prompted the State Council to call off Chen's plans.

CDB's acquisition of shares in Barclays was one of several ill-timed investments made by Chinese firms in western financial firms in 2007.[98] These acquisitions included the initial

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[96] "Barclays and China Development Bank form Commodities Strategic Alliance," October 10, 2007, http://www.barclayscapital.org.

[97] "Phoenix TV's Exclusive Interview with Chen Yuan," *Phoenix TV*.

[98] "Barclays Issues Shares to China Development Bank and Temasek," August 14, 2007, http://www.barclayscapital.org; and "Barclays Announces Investments of up to €13.4 Billion by China Development Bank and Temasek Holdings, and a Revised Offer for ABN Amro," July 23, 2007, http://group.barclays.com.

investments made by China Investment Corporation (CIC), China's sovereign wealth fund, established with a $200 billion share of China's foreign exchange reserves. Tasked with diversifying China's foreign exchange reserves away from U.S. government debt instruments, CIC first turned to Wall Street in search of solid investment returns, spending $3 billion for a nearly 10 percent stake in the US private equity firm Blackstone and $5.6 billion for almost 10 percentof US investment bank Morgan Stanley.[99] Ping An Insurance Group also purchased a 4.2 percent share of the Dutch-Belgian bank Fortis NV for $2.7 billion, while the Industrial and Commercial Bank of China Ltd., paid $5.5 billion for a 20 percent stake in South Africa's Standard Bank.[100]

The value of these investments plunged as the global financial crisis deepened. Shares of Barclays Bank, for which CDB paid £7.20 ($14.81) per share, closed at £1.54 ($2.24) on December 31, 2008, for a loss of 79 percent. CIC had also racked up huge paper losses on its stakes in Western financial institutions by the end of 2008. The sovereign wealth fund's investment in Blackstone had plummeted by 78 percent, while its investment in Morgan Stanley was down by 66 percent. By the end of 2010, however, CDB and CIC had recouped some of their losses, although their stakes were still worth substantially less than what they paid for them (see table 3).

CDB and CIC were sharply criticized at home for their forays abroad. The Chinese media and internet bloggers publicly excoriated them for the dismal performance of their

[99] Blackstone Group L.P., Form 424B4 file with the U.S. Securities and Exchange Commission, June 25, 2007, available at http://www.edgar-online.com; and Morgan Stanley, Form 8-K, filed with the U.S. Securities and Exchange Commission, December 19, 2007, available at http://www.edgar-online.com; and Jamil Anderlini, "China Wealth Fund's Early Coming of Age," *Financial Times*, December 21, 2007.

[100] "Ping An Buys Stake in Fortis," *Wall Street Journal*, November 29, 2007; and Rick Carew, Jason Loew and James T. Areddy, "China Makes Splash, Again; ICBC Takes 20% Stake in South African Bank; Got Lots of Cash? 'Invest,'" *Wall Street Journal*, October 26, 2007.

TABLE 3: Losses on Investments in Western Financial Institutions

Investor	CDB	CIC	CIC
Investment	Barclays	Blackstone Group	Morgan Stanley
Date of Purchase	July 2007	May 2007	December 2007
Purchase Share Price	720 pence	$29.61	$48.07
Closing Share Price, 12/31/2008	153.4 pence	$6.53	$16.04
Loss from purchase to 12/31/2008	79%	78%	66%
Closing Share Price, 12/31/2010	261.65 pence	$14.15	$27.16
Loss from purchase to 12/31/2010	64%	52%	43%

Sources: "Barclays Announces Investments of up to €13.4 Billion by China Development Bank and Temasek Holdings, and a Revised Offer for ABN Amro," July 23, 2007, http://group.barclays.com; Blackstone Group L.P., Form 424B4 file with the U.S. Securities and Exchange Commission, June 25, 2007, available at http://www.edgar-online.com; and Morgan Stanley, Form 8-K, filed with the U.S. Securities and Exchange Commission, December 19, 2007, available at http://www.edgar-online.com. The closing share prices on December 31, 2008 and December 31, 2010 are available at http://finance.yahoo.com.

investments in global financial institutions. They reserved their harshest words for CIC, accusing the sovereign wealth fund of irresponsible stewardship of the nation's foreign exchange reserves. While some critics attributed the losses to the inexperience of Chinese financial firms in cross-border deals, others suggested that the plummeting share prices might be part of a Western plot against China.[101] The appeal of such

[101] See, for example, Li Qing, "Sovereign Fund: Reputation at Stake," *Caijing*, February 1, 2009, http://english.caijing.com.cn/2009-02-01/110051793.html; Keith Bradsher, "China faces backlash at home over Blackstone investment," *New York Times*, August 2, 2007, http://www.nytimes.com/2007/08/02/opinion/02iht-backlash.4.6962261.html?pagewanted=1&_r=1; and HanTang chizi 汉唐赤子 (Pure Han and Tang Dynasties), "中国金融界最大丑闻: 内鬼洋举杯谈笑间7.5亿美金灰飞烟灭" ("The greatest scandal in Chinese financial circles: insiders and foreigners merrily turn $7.5 billion to dust and ashes"), September 4, 2007, http://hantangchizi.blog.sohu.com/62624828.html.

conspiracy theories is apparently not limited to just the chattering classes. The *Currency Wars*, a bestselling book in China that contends that the financial crisis was the brainchild of American politicians and bankers determined to undermine China's rise reportedly has been widely read by Chinese officials, including members of the Politburo.[102]

The State Council's confidence in western financial institutions dropped along with the share prices of Barclays and Blackstone. In September 2008, Wang Qishan, the vice premier in charge of economics and finance, reportedly told Lou Jiwei, the head of CIC, that his company should not make any more investments in Wall Street firms until CIC had people on staff who could decipher their accounts.[103] Three months later, Lou Jiwei publicly stated that China's sovereign wealth fund was no longer looking to invest in the financial sector. Speaking at a meeting of the Clinton Global Initiative in Hong Kong in December 2008, Lou told his fellow participants that "[r]ight now we do not have the courage to invest in financial institutions because we do not know what problems they may have."[104]

As enthusiasm in Beijing for buying stakes in western financial institutions continued to wane, momentum within the capital for investing in natural resources was building. Numerous Chinese officials regarded the global economic downturn as providing Chinese firms with a "once in one hundred years'" opportunity to purchase commodities such as oil and iron ore at lower prices and with less competition for assets. They encouraged Chinese companies to take advantage of China's $2 trillion in foreign exchange reserves and the col-

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[102] Interview with individual with access to China's top leaders, Washington, DC, October 13, 2009; Grace Ng, "Chinese flip new page in push to be superpower; New wave of bestsellers pressing Beijing to exert its economic influence," *The Straits Times*, April 6, 2009; and Keith Bradsher, "Main Bank of China Is in Need of Cash," *New York Times*, September 5, 2008.

[103] John Garnaut, "Why Canberra Must Not Meddle in the Rio-Chinalco Deal," *Sydney Morning Herald*, February 16, 2009.

[104] Keith Bradsher, "China Shuns Investment in West's Financial Sector," *New York Times*, December 4, 2008.

lapse in commodity prices and the credit crunch to invest in energy and minerals abroad.[105]

CIC had decided natural resources were a good long-term investment bet by early 2009. In March, Jesse Wang, the sovereign wealth fund's chief risk officer, stated that the sovereign wealth fund, spurred by the drop in energy and commodity prices, wanted to diversify its portfolio into these sectors.[106] In 2009, CIC invested almost $9 billion in energy and natural resource companies around the globe, ranging from Kazakhstan's national oil company, KazMunaigaz to Indonesia's PT Bumi Resources and the United States' AES Corporation.[107]

Meanwhile, CDB did not sour on western financial institutions as quickly as the State Council and CIC. In December 2007, Chen Yuan brokered a deal to invest $5 billion in Citibank, which was desperate for capital in the face of huge losses suffered in the US subprime mortgage crisis. Despite Chen's lobbying, the State Council did not sign off on the deal.[108] Undeterred, CDB put together an offer to buy a majority stake in Germany's Dresdner Bank from the German insurer Allianz for $10 billion, which the State Council thwarted by not permitting CDB to make a formal bid before Allianz accepted an offer from Germany's Commerzbank.[109]

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105 "魏建国：金融危机为中国"走出去"带来新机遇" ("The financial crisis brings a new opportunity for China to 'go out'"); 新华网 *(Xinhua)*, July 1, 2009, http://news.xinhuanet.com/video/2009-07/01/content_11633746.htm; Zhang Guobao 张国宝, "当前的能源形势："危"中之"机" ("Opportunities amid risks in the current energy situation"), 人民日报 *(People's Daily)*, December 29, 2008, http://scitech.people.com.cn/GB/8591346.html; and "郑新立：国际金融危机给中国带来四方机遇" ("Zheng Xingli: The international financial crisis brings China a four-faceted opportunity"), 世华财讯（*Shihua Caixun)* December 14, 2008, http://content.caixun.com/NE/01/3p/NE013pa5.shtm.

106 George Chen and Xie Heng, "Update 2—China's CIC sees opportunities in natural resources," *Reuters*, March 4, 2009.

107 Michael F. Martin, "China's Sovereign Wealth Fund: Developments and Policy Implications," Congressional Research Service, September 23, 2010, pp. 5-6, http://www.fas.org/sgp/crs/row/R41441.pdf.

108 Henry Sender, "Up against the Citi limits: How wariness and discord curbed the stakes China has taken in Wall Street Banks," *Financial Times*, May 5, 2008.

109 Jamil Anderlini, Sundeep Tucker, and James Wilson, "Beijing's caution scuppers Dresdner bid plan," *Financial Times*, September 5, 2008.

The State Council's refusal to approve Chen Yuan's plans to invest in Citibank and Dresdner contributed to CDB's decision to abandon, at least temporarily, its efforts to become a world-class bank through the acquisition of stakes in western financial institutions and instead concentrate CDB's cross-border deals on acquiring the natural resources needed to fuel China's continued economic rise. In July 2009, Chen Yuan publicly acknowledged that the Wall Street firms he had once admired had lost their appeal in the wake of the financial crisis, stating that "the lesson we can learn from this is that a world-class bank should not be measured by the standards of Western banks alone."[110] He went on to recommend that Chinese firms seeking to expand abroad amidst the global economic downturn should eschew Wall Street firms in favor of energy and natural resources:

> "The quality of Wall Street assets is very bad; they have many problems. We should think about what China really needs. I've considered this. Natural gas and oil are the resources that China currently has the most pressing need for. So, we should take advantage of the financial crisis. In the past, these energy producing countries could raise capital on the western capital market. But now they are in a difficult situation because they can't raise capital from the West. So, they are shifting their focus to China. Therefore, we should grasp this opportunity to do deals."[111]

The fact that both CDB and CIC decided to abandon investing in financial institutions in favor of energy and natural resources in the wake of the global financial crisis suggests that the Politburo Standing Committee had made a decision that this was the new national policy. After all, it seems unlikely

[110] Rui, "Chen Yuan: Recommending Chinese enterprises make acquisitions."
[111] "Phoenix TV's Exclusive Interview with Chen Yuan." See also Rui, "Chen Yuan: Recommending Chinese enterprises make acquisitions."

that Chen Yuan and Lou Jiwei would independently decide at roughly the same time that they would shift their focus from Wall Street and the City of London to producers of energy and minerals.[112] This apparent decision by the Chinese leadership provided the broader context for CDB to increase dramatically its EBLs.

[112] I thank Barry Naughton for this point.

China Development Bank's Energy-backed Loans

Chen Yuan took advantage of the global financial crisis by stepping up CDB's efforts to leverage China's financial resources to secure the energy China needs for its long-term economic development. The collapse in the price oil (from a high of $147 per barrel in July 2008 to less than $40 per barrel in December 2008 before settling to an average of around $61-62 per barrel in 2009) and the tightening credit markets left major oil and natural gas producers around the world struggling to raise funds to sustain investment programs, refinance short-term debts, and maintain robust social spending. CDB was eager to lend a helping hand. In 2009 and 2010, CDB agreed to provide $65 billion in credit to national energy companies and government entities in Russia, Brazil, Venezuela, Turkmenistan, and Ecuador, often on terms that the borrowers would have had trouble obtaining elsewhere (see table 4). The only major energy-backed loan brokered by Chinese firms that did not involve CDB was a $1 billion loan extended by PetroChina to PetroEcuador in 2009 as pre-payment for oil deliveries of 96,000 b/d over two years.[113] Although the $10 billion that CNPC and the China Eximbank loaned to Kazakhstan's national oil company and development bank in 2009 are often grouped together with CDB's EBLs in the media, the lines of credit extended to Kazakhstan are not backed by an energy supply contract.

[113] Jason Fargo, "Ecuador: Turning to China," *Energy Compass*, July 31, 2009.

TABLE 4: CDB's Energy-Backed Loans, 2005-2010

Date	Country	Borrower	Amount ($ billion)	Term (Years)
2005	Russia	Rosneft	6*	6
2008	Venezuela	BANDES	4	3
2009	Russia	Rosneft	15	20
2009	Russia	Transneft	10	20
2009	Brazil	Petrobras	10	10
2009	Venezuela	BANDES	4	3
2009	Turkmenistan	Turkmengaz	4	NA
2010	Venezuela	BANDES	20.6	10
2010	Ecuador	Ministry of Finance	1	4

* This amount includes funds provided by the Export-Import Bank of China
Source: Author's database

Each of the EBLs made by CDB is secured by revenue earned from deliveries of oil or natural gas to a Chinese oil company. CDB does not have a lien on the oil and natural gas itself but rather on the revenue generated by the sale of these supplies to Chinese firms. The Chinese oil company deposits its payment for the oil and natural gas deliveries into an account held by the borrower at CDB, from which CDB withdraws the interest, principal and other fees it is owed. Some of the deals involve infrastructure projects, contracts for Chinese firms, or the purchase of Chinese equipment.

Russia

On February 17, 2009, after many months of tough negotiations, CDB signed two unprecedentedly large oil export revenue-backed loan agreements with Russian state energy companies. CDB agreed to provide a combined $25 billion in financing to Rosneft, the Russian national oil company, and Transneft, the Russian pipeline monopolist. In exchange, the two Russian firms will supply China National Petroleum

Corporation (CNPC) with twenty years of crude oil deliveries of 300,000 b/d at market prices via a spur from the East Siberia Pacific Ocean (ESPO) pipeline to the Chinese border. The arrangements called for Rosneft to receive 60 percent of the loan and supply 60 percent of the oil and for Transneft to receive 40 percent of the loan and supply 40 percent of the oil.

CDB's loans of $15 billion to Rosneft and $10 billion to Transneft constitute the largest ever trade finance deal between China and Russia. Both loans have twenty-year terms and are repayable in equal installments (after a five-year grace period in which only interest payments are due).[114] The interest rate on the loans is the London Interbank Offered Rate (LIBOR) plus a margin that varies inversely to LIBOR.[115] Rosneft estimates that the interest rate will average 5.69 percent per year and that the total amount of payments made on its $15 billion loan will be $25.9 billion, which would yield CDB gross interest income of $10.9 billion.[116]

Rosneft and Transneft are repaying the loans with revenue from the sale of 300,000 b/d of crude oil to CNPC from January 2011 through December 2030. Rosneft provides 180,000 b/d, and Transneft delivers 120,000 b/d.[117] Transneft, which does not produce any oil, purchases the crude oil from Rosneft under a twenty-year crude oil delivery agreement the two Russian firms signed in 2009.[118] The price of the crude is set

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[114] Rosneft Oil Company, "Rosneft's Board of Directors Recommends a 20% Increase in Dividends to RUB 1.92 per Share," April 29, 2009, http://rosneft.com/printable/news/pressrelease/29042009.html; Rosneft Oil Company, "Information on the major transaction," document prepared for the Annual Shareholders' Meeting of OJSC Rosneft Oil Company, June 19, 2009, http://www.rosneft.com/attach/0/54/72/prepare10en.pdf; and Transneft, "OAO AK Transneft IFRS Consolidated Interim Condensed Financial Statements (Unaudited) for the Six Months Ended 30 June 2009," October 14, 2009, www.transneft.ru/objectdata/WebPageImpl/6283/TN_IFRS_eng_6m2009.doc.

[115] Rosneft Oil Company, "Information on the major transactiontransaction."

[116] *Ibid.*

[117] Rosneft Oil Company, "Rosneft's Board of Directors Recommends a 20% Increase."

[118] For detailed information on the oil delivery agreement between Rosneft and Transneft, including the pricing formula, see Rosneft Oil Company, "Information on related party transactions," document prepared for the Annual Shareholders' Meeting of OJSC Rosneft Oil Company, June 19, 2009, http://www.rosneft.com/attach/0/54/72/prepare09en.pdf.

each month based on the market quotes for Russia's new ESPO blend crude at the Pacific port of Kozmino.[119] CNPC deposits the money it owes Rosneft and Transneft for the oil into accounts at CDB opened on their behalf by OJSC Bank VTB, one of Russia's largest state-owned banks that is acting as an agent for the two Russian firms. CDB has the right to directly debit cash funds from the account to secure repayment of principal, interest and other amounts payable under the loan agreement. In the event of a default, CDB has the right to debit the entire cash balance of the accounts.[120]

The oil whose revenue secures the loans is delivered to China through a spur from the ESPO pipeline to China. The first phase of this pipeline, which runs for 2,757 kilometers (km) from Taishet to Skovorodino, was completed in December 2009. The second phase of the pipeline, which will stretch for 2,100 km from Skovorodino to the Pacific port of Kozmino is currently under construction. The spur to China, which covers the 70 km from Skovorodino to the Chinese border, began commercial deliveries on January 1, 2011.[121] Agreements on the construction of the spur between Chinese Vice Premier Wang Qishan and Russian Deputy Prime Minister Igor Sechin and between CNPC and Transneft were signed as part of the deal.[122] Consequently, CDB's loans helped draw to a close one of the most riveting soap operas in the geopolitics of energy, the fifteen years of bilateral negotiations over building an oil pipeline from Russia to China.

The loans CDB extended to Rosneft and Transneft provided them with desperately needed funds to refinance substantial short-term debts and support large-scale capital projects. Both

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[119] Rosneft Oil Company, "Information on the major transaction;" and Rosneft Oil Company, "Information on related party transactions."

[120] Rosneft Oil Company, "Information on the major transaction."

[121] "Transneft starts commercial oil shipment to China via ESPO spur," *Russia & CIS Energy Newswire*, January 11, 2011.

[122] "Russia, China sign $25 bln loans-for-crude deal," *Interfax: China Energy Newswire*, February 18, 2009.

companies received $10 billion from CDB in 2009, and an additional $5 billion was available to Rosneft in 2010.[123] For Rosneft, the credit from CDB covers the company's refinancing needs from the second quarter of 2009 through the end of 2014, which amount to $14.99 billion.[124] For Transneft, the credit helps meet the company's funding requirements for the ESPO pipeline and supporting infrastructure which may cost as much as US$ 30 billion.[125] Indeed, the loan had been earmarked by the Chinese for the completion of the first phase of the pipeline and the spur to China.[126] A Transneft spokesman also implied that Transneft was not allowed to access the loan until after it began construction of the spur.[127]

It took the Chinese and the Russians four months of tough negotiations from October 2008 to February 2009 to finalize the deal. On October 28, Chinese Vice Premier Wang Qishan and Russian Deputy Prime Minister Igor Sechin signed a memorandum of understanding on cooperation in the oil sector. The document called for the establishment of a joint working group led by Zhang Guobao, then the head of China's National Energy Administration, and Sergei Shmatko, Russia's Minister of Industry and Energy, to work out the terms of the oil supply contracts by March 1, 2010.[128]

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123 "CEO: Transneft fully gets $10 bln loan from China Devt Bank," *Prime-TASS Energy Service*, April 20, 2010; and Rosneft, "Q4 and 12M 2009 US GAAP Results," February 1, 2010, http://www.rosneft.com/attach/0/58/64/Rosneft_Q4_2009_US_GAAP_ENG.pdf.

124 Rosneft, "Q4 and 12M 2009 US GAAP Results."

125 I thank Igor' Danchenko for this estimate based on (Russian only) http://www.oilexp.ru/news/russian_rinok/proektnaya-stoimost-obektov-vsto-2-sostavit-okolo-350-mlrd-rublej/32838/; and (Russian only) http://www.expert.ru/news/2009/02/17/kredit_neft.

126 Chen Zhu 陈竹, "中俄能源谈判前瞻" ("Looking at future China-Russia energy negotiations"), 财经 (*Caijing*), February 20, 2009, http://www.caijing.com.cn/2009-02-20/110071928.html.

127 "Transneft Starts Pipeline Spur to China," *NEFTE Compass*, April 30, 2009.

128 "张国宝：中国石油储备一期完成 未影响国际油价" ("Zhang Guobao: The first phase of China's strategic oil reserve is complete and will not impact world oil prices"), *China News Service*, March 17, 2009, http://news.xinhuanet.com/fortune/2009-03/16/content_11019295.htm; Nadezhda Roumiantseva, "Russia Agrees on Terms for Building Oil Pipeline Spur to China," *International Oil Daily*, October 29, 2008; "Russia to sign oil cooperation memorandum with China – Russian Deputy PM," *China Energy Newswire*, October 27, 3008.

The difficulty of the negotiations reflected the efforts of both the Chinese and the Russians to avoid the problems that arose in their first oil export revenue backed loan agreement. In January 2005, CDB and China Eximbank loaned Rosneft $6 billion through Russia's OJSC Vnesheconombank. The loan was secured with a contract for Rosneft to deliver 48.4 millions tons (about 180,000 b/d) of crude oil to CNPC from February 2005 through December 2010.[129] Rosneft turned to the Chinese because it was having difficulty raising money to finance its $9.4 billion purchase of the former Yukos oil subsidiary Yuganskneftegaz. This acquisition was critical to Rosneft's bid to avoid being taken over by the Russian gas monopoly, Gazprom.[130] As a result, Rosneft hastily agreed to terms that it otherwise never would have accepted and quickly came to regret.

Rosneft came to view the terms of its agreement with the Chinese as increasingly unfavorable in light of rising LIBOR rates and oil prices, and pressured them to renegotiate.[131] The loan initially carried an interest rate of LIBOR+3 percent. However, the dramatic increase in LIBOR rates in 2005 made it much more costly for Rosneft to service its debt. The company successfully persuaded the Chinese to reduce the interest rate to LIBOR+0.7 percent in the first quarter of 2006.[132] The following year, Rosneft began insisting that the Chinese also revise the oil price formula. The original contract price was the monthly weighted-average price of Brent crude oil with a discount of $3 per barrel. However, changes in oil market conditions in 2007 made it more profitable for Rosneft to sell oil to Europe than to CNPC. Rosneft's demands for a

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[129] Rosneft Oil Company, "Management's Discussion and Analysis of Financial Position and Results of Operations for the years ended December 31, 2006, 2005 and 2004," p. 7, http://rosneft.com/attach/0/58/76/MDA_Eng_2006.pdf.

[130] "Russia economy: Rosneft's Chinese gambit," *EIU Viewswire*, February 2, 2005.

[131] This paragraph is based on PFC Energy, "Russia: Breakthrough Deal with China," February 23, 2009, p. 2.

[132] Rosneft Oil Company, "Management's Discussion and Analysis of Financial Position and Results of Operations for the years ended December 31, 2006, 2005 and 2004."

new oil price formula angered the Chinese, who regarded the fixed price discount as a just reward for their generosity toward Rosneft in the company's time of need.[133] A protracted dispute ensued, with Rosneft executives warning CNPC that the company would not extend the supply contract after its expiration in 2010 unless the oil price formula was revised.[134] The threat to not renew the contract was also a threat to not build the ESPO pipeline spur to China because Rosneft had set the signing of a new supply contract as a precondition for the construction of the cross-border pipeline.[135] CNPC eventually agreed to increase the price per barrel by $0.675, reducing the discount to Brent.[136]

The oil price formula was not as controversial in the negotiations over the terms of the second energy-backed loan. The Chinese had wanted a discount to the market price of oil, probably as a concession for once again providing Rosneft with financial assistance in its time of need. However, they eventually gave up this position and agreed to buy oil at the market price with no discount.[137]

The most hotly contested issue in the negotiations in 2008-2009 was the cost of borrowing. The dominant narrative that emerges from Chinese and Russian media coverage of the negotiations over the interest rate is that the Chinese wanted a

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[133] See, for example, Qin Xuanren 秦宣仁 , "中国能源安全与周边环境" ("China's energy security and peripheral environment") 中国经济 *(Economy of China)* (November 2009), http://www.economyofchina.com/cms/html/zazhi/wangqi/2009nian11yuekan/jiaodian/2009/1105/404.html; "CNPC won't agree further oil price hikes under Rosneft contract—source (repeat)," *China Energy Newswire*, January 31, 2008; and "Rosneft and CNPC to discuss 2004 contract price revision—source (part 2)," *Russia & CIS Business and Financial Newswire*, November 15, 2007.

[134] "Rosneft Threatens to Sever Contract with CNPC," *NOVECON: Russia/CIS Energy Digest*, November 15, 2007; and "Rosneft warns China over oil supply post 2010," *Reuters*, September 12, 2007.

[135] Nelli Sharushkina, "Price Dispute Stops Russia and China Agreeing Oil Pipeline Spur," *International Oil Daily*, November 7, 2007.

[136] "Price is sticking point in new Rosneft, CNPC oil contract—source (repeat)," *China Energy Newswire*, March 17, 2008.

[137] PFC Energy, "Russia: Breakthrough Deal with China," p. 3.

floating, market-based interest rate while the Russians wanted a fixed, below market interest rate.[138] However, Zhang Guobao, then the head of China's National Energy Administration and the leader of China's negotiating team, maintains that neither the Chinese nor the Russian positions were as rigid as many media reports portrayed. The Chinese, for example, were willing to consider three options: a fixed interest rate, LIBOR plus a fixed margin and LIBOR plus a margin that varies inversely to LIBOR. The Russians repeatedly indicated that they were inclined to go with the third option, LIBOR plus a floating margin. The difficulty lay in reaching a consensus on how much the margin would fluctuate inversely to LIBOR. According to Zhang, "every fraction of a percent was disputed."[139]

Despite repeated Russian complaints during the negotiations about the high cost of borrowing from the Chinese, the two sides agreed on a market-based interest rate that ended up being favorably viewed by the Russian companies. Transneft President Nikolai Tokarev commented that "it's not easy to get a loan on those terms these days."[140] Rosneft's board of directors was even more enthusiastic, declaring "[t]he value, cost and duration of the loan are unprecedented not only for Russian corporate borrowers but also for the global capital

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[138] "中俄签250亿美元石油换贷款协议 中获俄3亿3吨石油" ("China and Russia sign a $25 billion oil and loans agreement; China will get 300 million tons of oil from Russia"), 21世纪经济导报 *(21st Century Business Herald)*, February 18, 2009,as re-posted at http://finance.sina.com.cn/world/gjjj/20090218/00245867094.shtml; "中俄签署长期原油供销合同等七个能源合作文件" ("China and Russia sign seven energy cooperation documents including a long-term crude oil supply contact"), 财经 (*Caijing*), February 18, 2009, http://www.caijing.com.cn/2009-02-18/110069993.html; Dong Lingxi 董凌汐, "中俄力求3月前完成贷款换石油谈判" ("China and Russia strive to complete the loans-for-oil negotiations before March"), 财经 (*Caijing*), February 3, 2009, http://www.caijing.com.cn/2009-02-03/110052476.html; "OSC Report: Russia, China Unable to Reach Deal on Credits, Oil Deliveries," *Russia, China—OSC Report*, November 19, 2008, *World News Connection*; "Russia, China suspend talks on oil supplies, loans," *BBC Monitoring Former Soviet Union*, November 12, 2008.

[139] "Zhang Guobao: The first phase of China's strategic oil reserve is complete."

[140] "Transneft may refinance Sberbank debt with China Development Bank loan," *Interfax: Russia & CIS Energy Newswire*, June 24, 2009.

markets in general."[141] Indeed, Rosneft may turn a profit on its loan from CDB. According to the Russian media, Rosneft may earn between $23 million and $39.5 million in 2010 alone on the $1.73 billion it borrowed from CDB in the second quarter because of the spread between the higher interest rate for Rosneft's dollar deposits and the lower interest rate on the loan from CDB.[142]

Brazil

On May 19, 2009, CDB completed negotiations with Petrobras, the Brazilian national oil company, for an oil export revenue-backed loan in the amount of $10 billion.[143] The loan has a ten-year term and an interest rate of LIBOR + 2.8 percent.[144] The loan agreement is one of three transactions that comprise the China-Brazil "loans-for-oil" deal. The second is a 10-year crude oil delivery contract for Petrobras to supply Unipec, a subsidiary of Sinopec, with 150,000 b/d in the first year and 200,000 b/d in the subsequent nine years, and the third is a memorandum of understanding (MOU) between the two national oil companies to cooperate in areas of mutual interest, including exploration, refining, petrochemicals and the supply of goods and services.

Although Petrobras has stressed that the loan agreement and the crude oil delivery contract are separate, the two are in fact

[141] Rosneft's Board of Directors Recommends a 20% Increase in Dividends to RUB 1.92 per Share," April 29, 2009, http://rosneft.com/printable/news/pressrelease/29042009.html.

[142] Yekaterina Derbilova, "Rosneft Profiting on Chinese Loan," *The Moscow Times*, August 16, 2010, http://www.themoscowtimes.com/vedomosti/article/rosneft-profiting-on-chinese-loan/412568.html.

[143] This paragraph is based on Petrobras, "Contracting of a Credit Line Worth $10 billion from the China Development Bank," May 19, 2009, accessed at http://www.petrobras.com.br/en/investors/.

[144] Petrobras, "Consolidated Financial Statements December 31, 2009, 2008 and 2007 with Report of Independent Registered Public Accounting Firm," March 24, 2010, pp. 48-49, http://www2.petrobras.com.br/ri/spic/bco_arq/DFPUSGAPP4Q09Ingles.pdf.

linked.[145] Petrobras is using revenue it earns from its oil supply contract with Unipec to secure the loan.[146] According to the Chief Executive of Petrobras, José Sergio Gabrielli, Unipec pays for the oil—purchased at market prices—through an account that Petrobras holds at CDB. Petrobras is required to maintain a minimum account balance equivalent to six months of interest payments.[147]

CDB's credit is helping to fund Petrobras' ambitious business plan, which targets total investments of $224 billion for 2010-2014.[148] It includes the funding required to develop the company's huge oil discoveries in the pre-salt layer of the Santos Basin off the southeastern coast of Brazil. In the first half of 2009, Petrobras raised $31 billion to help finance its business plan. In addition to the $10 billion from CDB, Petrobras also secured $12.5 billion from the Brazilian development bank, $6.5 billion from a syndicate of international banks, and $2 billion from the Export-Import Bank of the United States.[149] Moreover, in 2010, Petrobras netted $26 billion in cash from the world's largest share offering in history.[150]

Both Chen Yuan and Gabrielli have publicly stated that the most difficult part of the negotiations was the issue of how

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[145] See, for example, Petrobras, "Execution of the loan agreement with the China Development Bank Corporation," November 4, 2009, Securities and Exchange Commission, http://www.edgar-online.com; Manuela Zoninsein, "Brazil Turns East: An interview with Petrobras CEO José Sergio Gabrielli de Azevedo," *Newsweek*, June 11, 2009; and "Petrobras CEO Upbeat on China Loan Deal," *Caijing*, May 19, 2009, http://english.caijing.com.cn/2009-05-19/110168560.html.

[146] "Phoenix TV's Exclusive Interview with Chen Yuan;" Zoninsein, "Brazil Turns East;" and "Petrobras Clarifies Loan," *Oil Daily*, May 22, 2009.

[147] "Phoenix TV's Exclusive Interview with Chen Yuan;" "Interview: Petrobras CEO José Sergio Gabrielli on Brazil's Energy Outlook," Americas Society/Council of the Americas, June 23, 2009, http://www.as-coa.org/article.php?id=1719; and "Petrobras Clarifies Loan."

[148] Petrobras, "Business Plan 2010-2014," June 21, 2010, www.petrobras.com.br/ri/Download.aspx?id=10932.

[149] "Interview: Petrobras CEO José Sergio Gabrielli on Brazil's Energy Outlook."

[150] Jonathan Wheatley, "Jubilant mood as country taps foreign reserves," *Financial Times*, November 1, 2010; and "Petrobras Took $26 Billion From Share Sale After Paying Government," *Oil Daily*, October 22, 2010.

to specify collateral for the loan.[151] According to Chen, Petrobras initially was unwilling to use oil export revenue to secure the loan. However, CDB insisted that Petrobras use money it earned from the sale of crude oil to Sinopec to guarantee the loan. As Chen told a television reporter, "if we just made loans to their oil and gas [projects] and to some of their oil and gas companies, we would face a series of risks—for example, the stability of the company, revenues, and this and that. So, in the end, we insisted that everything ultimately be valued in terms of oil. What is ultimately paid back to an account in China is your revenue from oil; we will recover our loans from the money paid for oil received by China and reduce the uncertainty."[152]

Another highly contentious issue in the negotiations was procurement.[153] CDB's preference for tying the loan to purchases of Chinese equipment clashed with the Brazilian government's plan to develop local supply chains for Brazil's oil industry. CDB ultimately prevailed; the final agreement stipulates that $3 billion must be used to purchase oil equipment from China.[154]

Gabrielli, like the Russian energy company executives, was pleased with the terms of his loan from CDB. In an interview

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[151] "Phoenix TV's Exclusive Interview with Chen Yuan;" and Chen Zhu 陈竹, "加布埃利谈中巴石油合作" ("Gabrielli talks about China-Brazil oil cooperation"), 财经 (*Caijing*), May 20, 2009, http://www.caijing.com.cn/2009-05-20/110168728.html.

[152] "Phoenix TV's Exclusive Interview with Chen Yuan."

[153] Ernesto Almeida, Michal Meidan, and Christopher Garman, "Brazil/China: Bilateral ties are more likely to deepen, but hurdles remain," Eurasia Group Note, April 15, 2010.

[154] 中国石油和石油化工设备工业协议 (China Petroleum and Petrochemical Equipment Industry Association) "关于邀请参加中巴石油装备合作洽谈会的通知" (Notification regarding the invitation to participate in the China-Brazil oil equipment cooperation fair), March 6, 2010, accessed at www.cpeia.org.cn; and "Petrobrás negocia empréstimo de US$ 10 bilhões com a China" ("Petrobras has negotiated a new US$ 10 billion loan with China"), *O Estado De S. Paulo*, March 28, 2010, p. B1.

in June 2009, he noted that "the amortization will be on interest rates based on international markets below our cost curve for bonds in the secondary market."[155]

Venezuela

The government of Venezuela is CDB's largest foreign borrower. CDB has agreed to loan Venezuela's Bank for Economic and Social Development (BANDES) more than $28 billion since 2007. These lines of credit include $8 billion to capitalize the China-Venezuela Joint Investment Fund (JIF), which is administered by BANDES, and a separate dual-loan facility valued at $20.6 billion. All of the lines of credit are secured against oil supply contracts.

The governments of China and Venezuela established the JIF to finance the development of infrastructure and social projects in Venezuela.[156] The two countries had deposited $12 billion into the fund, in two separate installations of $6 billion, by the end of 2009. CDB contributed two thirds of the money ($4 billion) and Venezuelan financial institutions provided the remaining one-third ($2 billion) both times. CDB agreed to capitalize the fund in November 2007, when it entered into a credit facility with BANDES for $4 billion. The loan has a term of three years and is extendable for a total of fifteen years.[157] In 2008, CDB made its initial contribution of $4 billion to the fund, and Venezuela's National Development Fund (FONDEN) provided $2 billion.[158] In 2009, after Beijing and Caracas decided to double the fund, CDB granted another loan of

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[155] "Interview: Petrobras CEO José Sergio Gabrielli."

[156] "Venezuela, China Govts Create a $6 Bln Joint Development Fund," *Dow Jones International News*, November 6, 2007.

[157] Bolivarian Republic of Venezuela, "Listing Memorandum with respect to U.S. $2,495,963,000 7.75% Bonds due 2019 and U.S. $2,495,963,000 8.25% Bonds due 2024, October 23, 2009," p. 57, http://data.cbonds.info/emissions/11672/Prospectus_Venezuela_2019_2024.pdf.

[158] Venezuela, China Deposit $6 Bln in Development Fund—Chávez," *Dow Jones Chinese Financial Wire*, February 21, 2008; and Bolivarian Republic of Venezuela, "Listing Memorandum," p. 57.

$4 billion and BANDES and FONDEN contributed a total of $2 billion.[159] According to Venezuela's national oil company, Petroleos de Venezuela SA (PDVSA), projects financed by the JIF include the satellite Simón Bolívar, five metro lines (two in Caracas and one each in Los Teques, Valencia and Maracaibo), the train from Cúa to Encrucijada, and the Gran Mariscal de Ayacucho highway.[160]

CDB's loans to BANDES for the JIF are secured by fuel oil sales from PDVSA to China National United Oil Corporation (Chinaoil), a subsidiary of CNPC. The three-year supply contract that secures CDB's first loan of $4 billion requires PDVSA to deliver 100,000 b/d of fuel oil to Chinaoil.[161] In contrast, the three-year supply contract that secures CDB's second loan of $4 billion stipulates that the volumes delivered to Chinaoil will fluctuate with the price oil from a minimum of 107,000 b/d when oil prices are above $60 per barrel to a maximum of 153,000 b/d when oil prices are below $42 per barrel.[162] PDVSA's fuel oil sales to Chinaoil will range from 207,000 b/d to 253,000 b/d during the period in which the two supply contracts overlap.

The revenue PDVSA earns from fuel oil sales to Chinaoil is used to finance BANDES' loans from CDB. Chinaoil deposits payments for the fuel oil into a collection account held by BANDES at CDB.[163] PDVSA is allowed to deduct the volumes of fuel oil delivered to China from its production tax obligations.[164]

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[159] "Venezuela's development bank and fund to contribute to Chinese Fund," *El Universal*, February 23, 2009, http://www.eluniversal.com/2009/02/23/en_eco_art_venezuelas-developm_23A2234449.shtml; and "Venezuela's Chávez Visits China to Expand Energy Cooperation," *International Oil Daily*, April 9, 2009.

[160] PDVSA, *Informe de Gestión Annual 2009 (2009 Annual Management Report)*, p. 128, http://www.pdvsa.com/interface.sp/database/fichero/free/5889/1049.pdf.

[161] *Ibid.*

[162] *Ibid.*

[163] "China-Venezuela Fund expanded to 12 billion dollars," *Radio Nacional de Venezuela*, February 19, 2009, http://www.rnv.gov.ve/noticias/index.php?act=ST&f=31&t=91081.

[164] PDVSA, *Consolidated Financial Statements, December 31, 2008 and 2007 With Independent Auditor's Report Thereon*, p. 55, http://www.pdvsa.com/interface.sp/database/fichero/free/4968/616.pdf.

On August 23, 2010, CDB, BANDES, Chinaoil and PDVSA finalized a "loans-for-oil" deal worth more than $20 billion at a signing ceremony held at the Diaoyutai State Guesthouse in Beijing.[165] This new deal, which is separate from the JIF, is CDB's largest foreign financing ever.[166] It consists of three agreements: a $10 billion loan to BANDES governed by English law; a RMB 70 billion (US$10.6 billion) loan to BANDES governed by Chinese law; and an oil supply contract between PDVSA and Chinaoil governed by Venezuelan law.[167] The dual credit facility, which has a ten-year term, is secured by revenue earned by PDVSA from the oil supply contract with Chinaoil. Ecoanalítica, an economic consultancy in Caracas, reported in September 2010 that it had been unofficially uninformed that the interest rate on the loans fluctuates between LIBOR+0.5 percent and LIBOR+2.85 percent.[168]

This dual credit facility will finance major infrastructure, social development, energy, mining and agricultural projects in Venezuela.[169] According to the Venezuelan law that

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[165] "Galeria de fotos ceremonia de firma de convenios para el financiamento a gran volumen y de largo plazo entre Venezuela y China" ("Photo Gallery of the Signing Ceremony for the Venezuela-China Agreements on Long-term and High-volume Financing"), August 23, 2010, http://www.venezuela.org.cn/noticias/100823GiordaniGal.html.

[166] "China Development Bank finances $20 billion for projects in Latin America," *China Law & Practice*, August 11, 2010, http://www.chinalawandpractice.com/Article/2649302/Channel/12591/China-Development-Bank-finances-20-billion-for-projects-in-Latin-America.html; and Daniel Cancel, "China Lends Venezuela $20 Billion, Secures Oil Supply (Update2)," *Bloomberg*, April 18, 2010, http://www.businessweek.com/news/2010-04-18/china-lends-venezuela-20-billion-secures-oil-supply-update1-.html.

[167] Andrew Pugh, "Hogan Lovells, White & Case act on China's Venezuela investment," *The Lawyer*, August 6, 2010, http://www.thelawyer.com/hogan-lovells-white-and-case-act-on-chinas-venezuela-investment/1005239.article.

[168] Asdrúbal Oliveros, Maikel Bello, and José Luís Saboin, "The agreement has been finalized: new financing from China is ready," *Ecoanalítica Weekly Report*, No. 36, (Week IV, September 2010), p. 2.

[169] This paragraph is based on "Ley Aprobatoria del Acuerdo entre el Gobiemo de la República Bolivariano de Venezuela y el Gobiermo de la República Popular China sobre Cooperación para Financiamiento a Largo Plazo" ("Law Approving the Agreement between the Bolivarian Republic of Venezuela and the People's Republic of China on Long-term Financial Cooperation") *Gaceta Oficial (Official Gazette)*, No. 39.511 (September 16, 2010); and Oliveros, Bello and Saboin, "The agreement has been finalized."

incorporates the terms of the loan agreement, which the Venezuelan government published in the *Official Gazette* on September 16, 2010, at least $4 billion of the $10 billion and the entire RMB 70 billion will be used to fund projects jointly selected and implemented by both countries. Portions of both lines of credit may also be used to finance bilateral projects in China. The loans also appear to be tied to hiring Chinese firms. For example, China's stated-owned CITIC Group has a contract to build housing units in Venezuela, which will be funded, at least in part, by the loan from CDB.[170]

The role the Chinese will play in determining how to spend the majority of the $20.6 billion is likely a reaction to how the Venezuelans managed the money CDB contributed to the JIF. According to a source in Venezuela, the Chinese "were uncomfortable because $8 billion disappeared without consideration for China."[171] The Chinese insistence on stricter accountability regarding how their loans are used is a form of risk mitigation. CDB is undoubtedly aware that the government of Venezuela may still be repaying the $20.6 billion lines of credit after Venezuelan President Hugo Chávez has left office. Consequently, CDB wants to ensure that its largesse is perceived as benefitting Venezuela as a whole—and not just Chávez—to increase the likelihood that a post-Chávez government will not renege on the loan agreement.[172] Moreover, CDB's concerns about getting repaid by both the Chávez administration and its successor may also explain why the Venezuelan government took the unusual step of incorporating the terms of the loan agreement into a law.[173]

According to the loan agreement, PDVSA will ship escalating volumes of crude oil to Chinaoil to finance CDB's loans of

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[170] Ezequiel Minaya, "Venezuela Signs New Housing Construction Agreement with China," *Dow Jones International News*, January 26, 2011; and "CITIC Group to build 10,000 homes in Venezuela," *Industry Updates*, December 20, 2010.

[171] Lisa Viscidi, "Venezuela: China's Hesitant Relationship," *Energy Compass*, November 12, 2010.

[172] Interview, Washington, DC, October 20, 2010.

[173] "Law Approving the Agreement." I thank Mauricio Cardenas for this point.

$20.6 billion to BANDES.[174] PDVSA will deliver no less than 200,000 b/d in 2010; no less than 250,000 b/d in 2011; and no less than 300,000 b/d in 2012 and until the obligations under the financing agreement have been fulfilled. As is the case with the amortization of CDB's loans to the JIF, Chinaoil will deposit its payments for the crude oil in a collection account held by BANDES at CDB from which the interest, principal and other fees will be deducted. PDVSA deducts these amounts from the taxes and royalties it transfers to the government.[175]

Turkmenistan

On June 25, 2009, CDB finalized an agreement to loan $4 billion to Turkmengaz, the national natural gas company of Turkmenistan, for the development of one of the world's largest natural gas fields, South Yolotan.[176] The loan is secured by natural gas exports to China.[177] The fact that Turkmengaz and CNPC signed a contract for the delivery of an additional 10 billion cubic meters (bcm) per year at the same time that the loan agreement was finalized suggests that Turkmengaz will use the revenue it earns from this supply contract for natural gas as collateral for the loan.[178] Few other details about the terms of the loan, including the price at which the natural gas is sold to CNPC, are publicly available. However, industry sources indicate that Turkmengaz is selling natural gas to China at a price which is lower than what Russia pays and slightly higher than what Iran pays.[179]

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[174] This paragraph is based on "Law Approving the Agreement;" and Oliveros, Bello and Saboin, "The agreement has been finalized," p. 3.

[175] Viscidi, "Venezuela: China's Hesitant Relationship."

[176] John Roberts, "China, Turkmenistan ink loans-for-gas deals; China to lend $4 billion to Ashgabat, to get 40 Bcm/year of gas," *Platts Oilgram News*, June 26, 2009.

[177] Interview with industry expert, Washington, DC, October 22, 2010; and "Majors Play Waiting Game in Turkmenistan," *Petroleum Intelligence Weekly*, December 7, 2009.

[178] Roberts, "China, Turkmenistan ink loans-for-gas deals."

[179] Personal communication from Jen Coolidge, February 16, 2011; and PFC Energy, "Turkmenistan: Complex Geopolitics," August 2, 2010, p. 4.

An explosion on the Central Asia-Center pipeline on April 9, 2009 that disrupted the flow of natural gas from Turkmenistan to Russia—and highlighted the dangers of dependence on a single export route—appears to have prompted Ashgabat to seek financial assistance from Beijing. According to Turkmen authorities, the blast reduced natural gas deliveries to Russia to just 8 percent of the usual rate of 42-50 bcm per year. Exports did not resume until January 9, 2010, costing the government of Turkmenistan as much as $1 billion per month in lost revenue.[180] Ashgabat publicly blamed Gazprom for the explosion, arguing that the Russian state natural gas company failed to provide sufficient advance warning of its offtake reduction, resulting in a buildup of pressure in the pipeline.[181]

The explosion occurred at a convenient time for Gazprom, which had been pressuring Turkmenistan to sell it less gas at lower prices. Gazprom had signed a long-term contract with Turkmengaz to purchase about 50 bcm per year of gas at a fixed price, primarily for onward sale to Europe. However, the global financial crisis reduced natural gas demand and prices in Europe. As a result, Gazprom was caught in a situation in which it was contractually obligated to buy more gas from Turkmenistan than it could sell in Europe and the Ukraine and at higher prices than it could charge its European customers.[182] On April 8, 2009, the night before the explosion, Gazprom reportedly sent Turkmengaz a request to reduce its deliveries to the Russian firm by 90 percent.[183]

Less than two months later, Ashgabat approached the Chinese about buying more gas from Turkmenistan and lending

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[180] "Russia Takes Turkmen Gas After 9-month Gap," *International Oil Daily*, January 11, 2010; and Roberts, "China, Turkmenistan ink loans-for-gas deals."

[181] "Blast Exposes Russian, Turkmen Tensions," *World Gas Intelligence*, April 22, 2009; and Andrew Neff, "Turkmenistan Accuses Gazprom of Irresponsible Actions in Triggering Gas Pipeline Explosion," *Global Insight Daily Analysis*, April 13, 2009.

[182] "Central Asia: Breaking Russia's Grip," *Energy Compass*, June 5, 2009.

[183] "Gazprom wanted 90% cut in Turkmen gas import before blast: source," *Platts Commodity News*, April 9, 2009.

money for the development of the South Yolotan field, which may supply the additional 10 bcm per year to China. Turkmen President Gurbanguly Berdymukhammedov urgently dispatched a delegation headed by Deputy Prime Minister Tachberdy Tagyev to Beijing to hold negotiations on June 1 and 2 about a loan for the development of the South Yolotan field and the terms and conditions of Turmengaz's intended supply of up to 40 bcm per year to China.[184] Three weeks later, when Chinese Vice Premier Li Keqiang visited Ashgabat, the two sides finalized the deal.[185]

The Turkmens are apparently happy with their loan from CDB because they are seeking another one. In August 2010, President Berdymukhammedov ordered energy officials to secure a loan in the amount of $4.1 billion loan from CDB to accelerate the development of the South Yolotan field, which has been hampered by the enormous budget deficit created by the reduction in Turkmenistan's natural gas exports to Russia in 2009.[186] According to a prominent industry publication, the Turkmens are pursuing a second loan from CDB because the terms of the bank's first loan are more attractive than those subsequently offered by Deutsche Bank and Germany's Commerzbank.[187] In March 2011, Vice Premier Wang Qishan and Turkmen Deputy Prime Minister Baymyrat Hojamuhammedov signed a framework agreement for CDB to extend another loan to Turkmengaz.[188]

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[184] John Roberts, "Turkmenistan turns to China for gas funds; Seeks financing for development of giant South Yoloten field," *Platts Oilgram News*, June 2, 2009.

[185] Roberts, "China, Turkmenistan ink loans-for-gas deals."

[186] "Turkmenistan seeks Chinese loan," *FSU Argus*, August 20, 2010; and "Update 3—Turkmenistan welcomes U.S. oil firms, eyes China loan," *Reuters*, August 13, 2010.

[187] "Second Pipeline, Loan to Keep China Tops in Turkmenistan," *International Oil Daily*, October 8, 2010.

[188] "China: Signed Loan Agreement with Turkmenistan Gas Giant," *Dow Jones Chinese Financial Wire*, March 1, 2011; and 廖雷 Liao Lei,"王岐山会见土库曼斯坦总统特使霍贾穆哈梅多夫" ("Wang Qishan meets with the special envoy of the president of Turkmenistan, Baymyrat Hojamuhammedov"), 新华网 *(Xinhua)*, March 1, 2011, http://news.xinhuanet.com/politics/2011-03/01/c_121136475.htm.

Ecuador

On August 31, 2010, CDB signed a loan agreement for $1 billion with Ecuador's Ministry of Finance. The loan has a four-year term with a six-month grace period. It carries a 6 percent fixed annual interest rate and a 1 percent management fee. CDB will also charge 3 percent interest on late payments. The principal and interest will be paid quarterly.[189]

CDB is disbursing the loan in two parts. The first disbursement of $800 million, which the Ministry of Finance received in September 2010, is for the Ecuadorean government's discretionary use. According to Ecuador's Minister of Finance, Patricio Rivera, this money will finance Ecuador's program for infrastructure and other budgetary outlays in 2010 and 2011. The second disbursement of $200 million is earmarked for the development of Ecuador's oil industry.[190]

The loan is secured against oil deliveries of 36,000 b/d of Oriente or Napo crudes or fuel oil from PetroEcuador to PetroChina for four years.[191] The price is calculated on the loading date using a basis of West Texas Intermediate (WTI) minus a differential plus a premium.[192] According to the supply contract with PetroChina, the price of Oriente crude was WTI – $6.69 in September 2010 and WTI – $5.59 in October 2010,

[189] Mercedes Alvaro, "Ecuador Receives $800M Loan from China Development Bank," *Dow Jones Capital Markets Report*, September 29, 2010; and "Decreto Dio Luz Verde Para Credito Del Bano De China A Ecuador" ("Decree Gives Green Light for Credit from the Bank of China to Ecuador"), *Radio Equinoccio*, August 31, 2010, http://www.radioequinoccio.com/index.php?option=com_content&view=article&id=2052:decreto-para-viabilizar-credito-entre-banco-de-china-y-ecuador-&catid=36:ultimas-noticias&Itemid=53.

[190] Mercedes Alvaro, "Ecuador, Development Bank of China Sign $1 Billion Loan," *Dow Jones Chinese Financial Newswire*, September 1, 2010.

[191] Alvaro, "Ecuador Receives $800M Loan."

[192] Richard Capuchino and Winnie Lee, "PetroChina, PetroEcuador ink supply deal," *Platts Oilgram News*, July 28, 2009.

and the price of Napo crude was WTI – $10.19 in September 2010 and WTI – $8.99 in October 2010.[193]

PetroChina pays PetroEcuador through an account that PetroEcuador holds at CDB. According to minutes of meetings held between the Chinese and Ecuadorean negotiators in Beijing in June, 2010, for each interest period, PetroEcuador is required to maintain a minimum balance equivalent to 130 percent of the principal and interest to be paid in that interest period. PetroEcuador may withdraw amounts above this minimum balance for repatriation to Ecuador.[194]

Concerns about China's growing influence in Ecuador, especially in the oil sector, have prompted both the Ecuadorean government and PetroEcuador to publicly defend their deals with CDB and PetroChina. Minister of Finance Patricio Rivera, in an act of hair splitting, has repeatedly stressed that CDB does not have a lien on PetroEcuador's oil production.[195] In fact, the loan is collateralized with the revenue PetroEcuador earns through crude oil sales to PetroChina. Similarly, PetroEcuador's assistant manager for international trade, Nilsen Arias Sandoval, has stressed that the terms of the supply contract with PetroChina are not disadvantageous to Ecuador.[196]

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193 "El convenio con PetroChina registra descuentos más altos" ("The contract with PetroChina recorded higher discounts"), *El Universo*, October 25, 2010, http://www.eluniverso.com/2010/10/25/1/1356/convenio-petrochina-registra-descuentos-mas-altos.html.

194 "Update: Ecuador Negotiating $1 Billion Loan with China, Backed by Oil Sales," *Dow Jones Business News*, July 2, 2010.

195 Alvaro, "Ecuador, Development Bank of China."

196 "Nilsen Arias Sandoval: 'No se peuden comparar los dos contratos de PetroChina'" ("Nilsen Arias Sandoval: 'The two contracts with PetroChina cannot be compared'"), *El Universo*, October 29, 2010, http://www.eluniverso.com/2010/10/29/1/1356/nilsen-arias-sandoval-no-pueden-comparar-dos-contratos-petrochina.html.

Disaggregating China, Inc.

CDB's EBLs involved a fairly high degree of coordination between government and business. CDB, China's NOCs and senior government officials worked together to negotiate the various agreements that comprise the deals with their foreign counterparts. CDB, the bridge between the strategic objectives of the Chinese government and the commercial activities of Chinese firms, functioned as the primary coordinator. A discussion of the China-Venezuela Joint Investment Fund in a volume edited by Chen Yuan describes CDB as the link between government and market, coordinating relations between the engineering contracting companies involved in the infrastructure projects financed by the fund, the oil companies, the borrower, and the credit insurance agencies.[197]

The EBLs appear to have involved more coordination than many of the international mergers and acquisitions of China's energy and metals companies, including two of the highest-profile deals pursued by Chinese firms, the bid by China National Offshore Oil Corporation (CNOOC) for Unocal in 2005, which did not involve CDB, and the attempt of the Aluminum Corporation of China (Chinalco) to purchase an additional 9 percent stake in the Anglo-Australian mining giant Rio Tinto in 2009, in which CDB did participate. In the case of

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[197] Chen, *Research on Expanding International Cooperation and Expanding China's Strategy for Sourcing Energy and Raw Materials*, pp. 280-281.

CNOOC's bid for Unocal, CNOOC and the Ministry of Foreign Affairs failed to develop an international political strategy to support the company's bid for the U.S. firm UNOCAL, despite the fact that they are located across the street from each other in Beijing.[198] After CNOOC withdrew its bid for Unocal, the company chief executive officer, Fu Chengyu, complained about the lack of government support, implying that the relevant government departments should have tried to leverage China's hosting of the six-party talks on North Korea's nuclear program during the week of July 25, 2005, the appreciation of China's currency on July 21, 2005, and Hainan Airlines' purchase of Boeing Aircraft in September 2005 to gain support in the United States for CNOOC's bid.[199] In the case of Chinalco's attempt to purchase an additional 9 percent stake in Rio Tinto, which CDB was prepared to help finance, Chen Yuan has argued that Chinalco's bid should have received the same multilevel government support that CDB's EBLs did.[200] He has also echoed Fu Chengyu's call for closer coordination among China's financial institutions, enterprises and government to facilitate successful cross-border mergers and acquisitions.[201]

The finding that CDB's EBLs were the product of coordination among CDB, China's NOCs and the Chinese government is subject to two important caveats. First, each of the actors involved in these deals had their own interests to pursue. Second, coordination is not synonymous with top-down decision making.

[198] Interview with source close to CNOOC, Washington, DC, April 3, 2007.

[199] Wang You 王佑, "盘点中海油并购败因 傅成玉呼吁政府统一协作" ("Taking Stock of the Reasons for CNOOC's Failed Acquisition, Fu Chengyu Calls for Government Teamwork"), 第一财经日报 (*China Business News*), September 30, 2005, as re-posted at http://news.xinhuanet.com/fortune/2005-09/30/content_3564928.htm.

[200] "Phoenix TV's Exclusive Interview with Chen Yuan."

[201] Rui, "Chen Yuan: Recommending Chinese enterprises make acquisitions."

Multiple Corporate and National Interests at Play

The multi-billion dollar lines of credit that CDB extended to national energy companies and government entities in oil-rich states advanced a variety of corporate and national interests that are difficult to fully disentangle. Although many media reports on the EBLs portrayed them as the quest of a monolithic China to secure oil and natural gas supplies, the reality is that these transactions involved multiple actors and a complex mix of motivations. First, the deals supported CDB's agenda, which included growing profits, demonstrating that China still needs CDB to function as a policy bank, especially in the wake of the global financial crisis, and expanding the bank's international business. Second, the EBLs advanced the State Council's goals of enhancing China's access to energy and diversifying China's foreign exchange reserves. Third, CDB's loans helped China's NOCs further their objective of acquiring exploration and production assets abroad.

CDB's Interests

Growing Profits

Making money is a motive behind CDB's EBLs. This objective is hardly surprising given the strong culture of risk management that Chen Yuan developed at CDB. According to Chen, "at CDB, we are strongly motivated by our desire to align the commercial benefits of a successful and well-managed business with our obligation and commitment to support the State's strategies."[202] Indeed, the bank appears to be applying the same stringent lending criteria to its international projects as its domestic ones. CDB's annual report for 2008 states that the number of nonperforming foreign currency loans had been zero for 25 consecutive quarters, while the bank's annual report for 2009 maintains that "the quality of our international

[202] China Development Bank, *2009 Annual Report*, p. 13.

lending asset base remains sound."[203] In 2010, the NPL ratio for CDB's foreign currency loans was 0.26%.[204]

CDB's focus on generating a positive rate of return from its EBLs is reflected in the market-based interest rates at which the bank is lending money. The interest rates on the lines of credit totaling $45.6 billion that CDB extended to Petrobras, Rosneft and Transneft in 2009 and to BANDES in 2010 are all based on the London Interbank Offered Rate (LIBOR), the average interest rate charged when banks in the London interbank market borrow from each other. However, the spread over LIBOR may be less than what a western bank would require.

The fact that CDB may be lending at interest rates lower that what a western bank might require does not mean that it acts simply as an agent of state policy with no regard to profit.[205] Instead, CDB balances its commitment to profitability and its mandate to advance the policy priorities of the Chinese government. On a straight commercial basis, it may be rational for CDB to accept lower interest rates than western banks because CDB is backed by the Chinese government. Borrowers that abrogate their loan agreements with CDB risk angering not only the bank but also the Chinese government, jeopardizing future deals with Chinese firms.

Making the case the CDB should remain a policy bank

The multi-billion dollar lines of credit that CDB extended to major energy resource holders around the globe also bolstered the argument of CDB officials that the bank's commercialization should be delayed because China still needs CDB to be a policy bank. The EBLs not only demonstrate that the State

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[203] China Development Bank, *2008 Annual Report*, p. 20; and China Development Bank, *2009 Annual Report*, p, 57.

[204] Cao Hua, "China Development Bank's foreign currency loans."

[205] This paragraph is based on comments on an earlier version of this study from Arthur Kroeber, December 27, 2010.

Council can rely on CDB to help advance its global agenda, including access to energy abroad, the overseas expansion of Chinese firms and the diversification of China's foreign exchange reserves. The deals also underscore the point often made by CDB officials that the bank plays an indispensable role in financing China's long-term development goals. As Chen Yuan observed in late 2009, CDB occupies a unique position in China's "going out" strategy because it is the only medium- to long-term credit bank in China that serves national strategy.[206] Indeed, there is arguably no other financial institution in China that possesses the combination of large-scale financial resources, long-term orientation, and freedom of action that enabled CDB to leverage tens of billions of dollars to help secure the energy China requires for its continued industrialization and urbanization.

First, CDB's EBLs indicate that the bank's ability to bankroll major "going out" projects with national strategic value might be constrained if China's Commercial Banking Law were to apply to CDB. The law states that the outstanding balance of loans to a single borrower should not exceed 10 percent of a bank's capital balance.[207] According to Chen Yuan, several of CDB's cross-border energy and natural resource deals related to China's national strategy, such as the $25 billion loaned to the Russian energy companies Rosneft and Transneft, the $8 billion contributed to the China-Venezuela Joint Investment Fund, and the $15 billion extended to Chinalco for its acquisition of a 9 percent stake in the Anglo-Australian mining giant Rio Tinto, may have violated the 10 percent ratio.[208] Chen's comment that there are some conflicts between the execution of major national strategic projects and the commercial and retail banking laws implies that if the central government

[206] "Development Finance: The Common Development Path."

[207] Commercial Banking Law of the People's Republic of China, Adopted at the 13th Session of the Standing Committee of the Eighth National People's Congress on May 10, 1995 by Order No. 47 of the President of the People's Republic of China on May 10, 1995, http://www.china.org.cn/english/DAT/214824.htm.

[208] "Development Finance: The Common Development Path."

wants CDB to continue to finance such projects, then CDB should not be subject to the Commercial Banking Law.[209]

Second, the EBLs also suggest that CDB's ability to quickly execute major cross-border energy deals might be hampered if the bank were to strictly adhere to the commercial bank standards for corporate governance. An article published in *Caijing* magazine, a leading Chinese business publication, implies that CDB's successful execution of its EBLs was due in part to the fact that CDB continued to operate as it had before its conversion to a joint stock corporation—CDB Corporation—in December 2008, directly seeking the approval of the State Council instead of following its new corporate governance procedures and notifying its two shareholders, the Ministry of Finance and Central Huijin, whose involvement in the proposed transactions might have delayed the deals.[210] Indeed, CDB reportedly had sought to institutionalize its circumvention of its shareholders during the drafting of the regulations governing CDB Corporation by proposing the creation of a body outside the board of directors, comprised of high-level CDB officials, to make rapid decisions about major deals. Banking regulators, however, rejected the plan because it did not meet corporate governance standards.[211]

Third, the EBLs also highlight the unique role that CDB plays in China's efforts to secure energy and natural resources abroad. It is unlikely that either China Eximbank or China's commercial banks would have been able to fully substitute for CDB in the bank's EBLs. Although China Eximbank shares CDB's mandates to help ease China's energy and natural resource bottlenecks and to help Chinese firms expand overseas,

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[209] *Ibid.*

[210] Zhang Yuzhe 章宇哲 and Zhang Man 张曼, "开行商业化之困" ("CDB's commercialization difficulties"), 财经 (*Caijing*), March 16, 2009, http://magazine.caijing.com.cn/2009-03-15/110121000.html.

[211] *Ibid.*

it is a much smaller institution than CDB (see table 5).[212] At the end of 2009, for example, China Eximbank's total assets were just 17 percent of CDB's, and its outstanding loans amounted to were 16 percent of those of CDB.[213] Although the total assets and loans of each of China's big four commercial banks exceed those of CDB, they are increasingly independent from the central government because of their international listings and diversified ownership.[214] As a result, China's leaders cannot count on them to advance their strategic objectives. Moreover, the public listings of the big four commercial banks has put them under increased pressure to maximize profits in the short-term, making long-term loans like CDB's EBLs less attractive to them.[215]

TABLE 5: Comparison of CDB and the Export-Import Bank of China, 2009

	Total Assets RMB billion	Loan Balance RMB billion	Net Income RMB billion	NPL Ratio
CDB	4,541	3,708	32	0.94%
China Eximbank	792	592	2	1.1%

Sources: China Development Bank, *2009 Annual Report*, p. 6, http://www.cdb.com.cn; and Export-Import Bank of China, *2009 Annual Report*, http://www.eximbank.gov.cn.

Expanding CDB's International Business Portfolio

Chen Yuan also regards CDB's EBLs as a vehicle for expanding the bank's business abroad. He has explicitly linked CDB's

[212] For more information about China Eximbank's commitment to easing China's energy bottlenecks and helping Chinese companies expand abroad, see Dai Chunning 戴春宁, ed.,中国对外投资项目：中国进出口银行海外投资项目竞选 *(Case Studies of China's Foreign Investment Projects: Selected Overseas Investment Projects of the Export-Import Bank of China)*, (清华大学出版社[Tsinghua University Press], 2009).

[213] China Development Bank, *2008 Annual Report*, http://www.cdb.com.cn; and Export-Import Bank of China, *2008 Annual Report*, http://english.eximbank.gov.cn.

[214] I thank Yuxin He for this point.

[215] Email from Yuxin He, April 12, 2010.

loans to major energy resource holders to his vision for CDB's further internationalization over the next decade.[216] In his view, the bank's EBLs have raised CDB's international profile. According to Chen, "the success of major projects such as the China-Russia and China-Brazil oil cooperation projects have further established CDB's trademark advantage in the execution of major long-term international projects."[217]

CDB's plans to open offices around the globe also involve some of the countries involved in CDB's EBLs. In July 2009, the bank upgraded its Representative Office in Hong Kong to its first overseas branch to help Chinese firms expand abroad.[218] Four months later, CDB opened a representative's office in Cairo, Egypt to facilitate cooperation with African countries in areas including infrastructure, resource exploitation and agriculture.[219] In September 2010, CDB opened an office in Moscow to expand its operations in Russia.[220] CDB also intends to open representative's offices in Brazil and Venezuela.[221]

The State Council's Interests

Enhancing Access to Energy

CDB's EBLs further the State Council's objective of enhancing China's energy supply security. These transactions help China access the energy it needs to fuel continued economic growth by providing China's oil companies with long-term supply contracts and the infrastructure to deliver some of those supplies to China. CDB's loans to Russia are widely regarded in Beijing as the EBLs that have done the most to enhance China's

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[216] Rui, "Chen Yuan: Recommending Chinese enterprises make acquisitions."
[217] "Development Finance: The Common Development Path."
[218] "China Development Bank Opens First Overseas Branch in HK," *Business Daily Update*, July 30, 2009.
[219] "CDB Opens First Egypt Office," *Business Daily Update*, November 13, 2009.
[220] "China Development Bank opens office in Moscow," *People's Daily Online*, September 21, 2010, http://english.peopledaily.com.cn/90001/90778/90861/7146726.html.
[221] Katherine Ng, "CDB Seeks Organic Growth Globally," *The Standard*, July 30, 2009.

energy security by securing a long-coveted oil pipeline and a twenty year supply contract, which will help diversify China's oil imports away from the Middle East and the sea lines of communication.

The Chinese media has praised CDB's EBLs for providing China with long-term security of supply. The oil supply agreements associated with CDB's "loans-for-energy" deals are for unusually long periods of time. The deal with Russia, for example, involves the delivery of 300,000 b/d for twenty years. Most term contracts are much shorter because both buyers and sellers want the flexibility to change who they sell to and by from in response to changing market conditions.[222] The main benefit of these contacts for China's NOCs is that if the exporting companies make the agreed upon deliveries the Chinese firms can count on receiving certain volumes and grades of crude oil for long periods of time. Oil deliveries to China's NOCs from the EBLs will probably peak at almost 1 million b/d in 2012, equal to 19 percent of China's oil imports in 2010 (see table 6).[223]

However, Beijing knows all too well from China's first energy-backed loan to Russia that long-term contracts do not guarantee security of supply. Changes in oil market conditions beginning in early 2007 made it more profitable for Rosneft to sell oil to Europe than to China. The greater profitability of European deliveries not only prompted Rosneft to pressure CNPC to revise the oil pricing formula for their oil supply contract which ran through 2010 but also contributed to the drop in Russian crude oil exports to China from 321,000 b/d in 2006 to 292,000 b/d in 2007.[224]

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[222] I thank Mikkal Herberg for this point.

[223] International Energy Agency, *Oil Market Report*, January 18, 2011, p. 57, http://omrpublic.iea.org/omrarchive/18jan11full.pdf.

[224] Song Yen Ling, "China's Oil Imports Soar," *International Oil Daily*, January 25, 2008.

TABLE 6: Estimated Oil Deliveries from CDB's EBLs, 2010-2014*

1,000 barrels per day					
	2010	2011	2012	2013	2014
Russia (2005)	180				
Russia (2009)		300	300	300	300
Venezuela 2008)	100				
Venezuela (2009)	107-153	107-153	107-153		
Venezuela (2010)	200	250	300	300	300
Brazil	150	200	200	200	200
Ecuador	36	36	36	36	36
Total	773-819	893-939	943-989	836	700

Source: Author's Database

*These are estimates because it is difficult to determine the exact amount of oil China's NOCs will receive in any given year for at least two reasons. First, some of the supply contracts have a built in margin of fluctuation. For example, the supply contracts that Rosneft and Transneft signed with CNPC stipulate that the volumes delivered can fluctuate by +/- 4.1% per year. Second, the volume of oil that PDVSA delivers CNPC to secure CDB's second $4 billion loan to the China-Venezuela Joint Investment Fund fluctuates with the price of oil. See "Information on the major transaction," document prepared for the Annual Shareholders' Meeting of OJSC Rosneft Oil Company, June 19, 2009, p.4, http://www.rosneft.com/attach/0/54/72/prepare10en.pdf; "Items and Resolutions of the agenda," documents prepared for the Annual Shareholders' Meeting of OJSC Rosneft Oil Company, June 19, 2009, p. 7, http://www.rosneft.com/attach/0/54/72/prepare11en.pdf; and PDVSA, *Informe de Gestión Annual 2009 (2009 Annual Management Report)*, p. 128, http://www.pdvsa.com/interface.sp/database/ficherol/free/5889/1049.pdf.

The Chinese government undoubtedly regards the spur from Russia's ESPO pipeline to the Chinese border as the greatest contribution to China's energy supply security made by CDB's EBLs.[225] The spur, which will stretch for almost 70 km from Skovorodino to the Chinese border, will have an initial design capacity of 300,000 b/d which will eventually rise to 600,000

[225] See, for example, You Ran 由然, "中俄原油管道意义深远" (The China-Russia oil pipeline has profound significance"), 中国石油企业 *(China Petroleum Enterprise)*, No. 10 (2009), http://www.cpechina.com/system/2009/11/18/001265097.shtml; and An Bei 安蓓 and Fan Yingchun 范迎春, "中俄原油管道对促进我能源进口多元化有重要意义" ("The China-Russia oil pipeline has great significance for the diversification of China's energy imports"), 新华网 *(Xinhua)*, May 18, 2009, http://news.xinhuanet.com/fortune/2009-05/18/content_11396987.htm.

b/d.[226] Although Russian crude oil exports to China have grown from less than 1,000 b/d in 1995 to more than 300,000 b/d in 2009, the majority of this oil has been delivered by rail. Not only is a pipeline a more cost effective way to ship large volumes of oil to China, but a dedicated pipeline is probably a better guarantee of supply than rail deliveries, which are easier to redirect elsewhere.

This cross-border pipeline will substantially expand Russia's capacity to deliver crude oil overland to China. Russia's current capacity to ship crude overland to China is about 200,000 b/d by rail.[227] The ESPO spur will increase this amount to 500,000 b/d. If the capacity of the spur is doubled to 600,000 b/d, then Russia will be able to deliver 800,000 b/d overland to China. Although Russian exports to CNPC—which currently account for the bulk of the crude oil shipped to China by rail—will be shipped through the ESPO spur en route to CNPC's refinery in Daqing, Sinopec may opt to use the rail capacity freed by the ESPO spur for delivery of crude for its Yanshan Refinery in Beijing.[228]

The ESPO spur is the *pièce de résistance* of Beijing's efforts to diversify China's oil imports away from the Middle East, which supplies half of China's crude oil imports, and the sea lines of communication, through which about 90 percent of China's crude oil imports pass.[229] There is a fairly widespread view in Beijing that pipeline imports are more secure than seaborne ones. However, pipeline imports are actually more vulnerable to sabotage and interdiction than seaborne deliveries.[230]

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[226] Tom Grieder, "Prime Minister Putin Opens Russian Section of Crude Oil Pipeline Spur to China," *Global Insight*, August 30, 2010.

[227] This estimate is based on the fact that Russian rail deliveries to China peaked at 10.3 million tons (206,847 b/d) in 2006.

[228] I thank Matt Sagers for this point.

[229] Tian Chunrong 田春荣, "2008年中国石油进出口状况分析" ("Analysis of China's Oil Imports and Exports in 2008")国际石油经济 *(International Petroleum Economics)*, Vol. 17, No. 3 (2009), p. 34.

[230] Andrew S. Erickson and Gabriel B. Collins, "China's Oil Security Pipe Dream: The Reality, and Strategic Consequences, of Seaborne Imports," *Naval War College Review* (Spring 2010), p. 92.

Moreover, pipelines are unlikely to substantially reduce China's dependence on seaborne oil imports. The combined design capacities of pipelines from Russia, Kazakhstan and Myanmar (currently under construction) to China is 1.1 million b/d, which was 21 percent percent of China's oil imports in 2010 but will be less than 10 percent of the 12.8 million b/d China is projected to import in 2035.[231]

The cross-border oil pipeline is also an especially grand prize for China's leaders because it eluded them for so many years. The signing of the contract for the construction of the ESPO spur ended one of the longer-running and more captivating dramas in the geopolitics of energy in the twenty-first century. Despite the enormous attraction that Russia, the world's largest or second largest oil exporter, and China, the world's second largest oil importer, hold for each other as energy partners, the oil pipeline negotiations dragged on for fifteen years because Moscow and Beijing were not equally interested in starting the project at the same time.

During the 1990s, when oil prices were low, Moscow was the more enthusiastic proponent of the oil pipeline. Indeed, Boris Yeltsin first proposed the idea of a cross-border pipeline in 1994 to help jump start the Russian economy. Beijing, however, was in no hurry to make a binding commitment. China was only importing small volumes of oil, having just become a net importer in 1993, and prices were low, tumbling to less than $15 per barrel in 1998.[232] In the last two years of the twentieth century, there was also reluctance among the Chinese leadership, notably then Premier Zhu Rongji, to invest in transnational pipelines, which made little economic sense given the

231 International Energy Agency, *Oil Market Report*, January 18, 2011, p. 57, http://omrpublic.iea.org/omrarchive/18jan11full.pdf; and International Energy Agency, *World Energy Outlook 2010*, p. 135.

232 *BP Statistical Review of World Energy*, June 2009, p. 16, www.bp.com.

relatively low oil prices at that time.[233] Moreover, the Chinese were intent on taking advantage of a buyer's market to extract maximum price concessions from the Russians.[234]

The rise in world oil prices beginning in late 2002 turned the tables.[235] Beijing, motivated by the unexpected surge in China's oil demand and imports, was finally ready to build the pipeline. In contrast, Moscow's urgency had diminished due to uneasiness about fueling China's growing economic power and dreams of using Russia's increasingly valuable energy resources as a vehicle to restore Russia to great power status. Emboldened by high oil prices, Moscow sought to increase its control over Russian energy assets and leverage them for international economic and political gains. This rise in Russian resource nationalism undermined progress on a cross-border oil pipeline in two ways. First, Moscow's dismantlement of the private oil company Yukos sounded the death knell for the proposed pipeline from Angarsk to Daqing on which the Chinese had originally pinned their hopes. Yukos had championed the project, a move which contributed to Yukos' demise by contributing to worries in Moscow about a private company influencing Russian foreign policy by operating an export pipeline. Second, the intervention of Japan, with its tantalizing promise—but no formal offer—of billions of dollars to support a pipeline proposed by Transneft from East Siberia to the Pacific Coast provided Russia with the opportunity to exploit the competition between China and Japan for its own benefit. Moscow repeatedly put off making a final decision about

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233 Interview with Chinese energy and foreign policy experts, Beijing, China, 4 April 2006 and 11 April 2006; and Xu Haiyan 徐海燕, "俄罗斯 '东向' 能源出口战略与中俄油气合作 – 基于地缘政治经济学的分析" ("Russia's 'Eastern-oriented' Energy Export Strategy") 复旦学报（社会科学版）*(Fudan Journal (Social Sciences))*, No. 5 (2004), p. 104.

234 Andrei Glazov and Doug Rohlfs, "China Doll—China Pipeline Talks Stall Despite State Initiative," *Nefte Compass*, 16 November 2006.

235 This paragraph and the following two paragraphs are based on Erica S. Downs, "Sino-Russian Energy Relations: An Uncertain Courtship," in James Bellacqua, ed., *The Future of China-Russia Relations* (University Press of Kentucky, 2010), pp. 146-175.

the ESPO pipeline and the spur to China in a bid to maximize concessions from both countries. Although the Chinese offered more, notably a $6 billion loan to Rosneft, it was not enough to persuade Moscow, awash in windfall oil profits, to sign off on the construction of the ESPO spur.

The global financial crisis and the collapse in the price of oil suddenly gave China the upper hand in bilateral energy negotiations. The Chinese took advantage of their newfound position of strength to secure the long-coveted spur from the ESPO pipeline to China and a twenty-year supply contract, guaranteed by the Russian state, to fill it. According to a high-level CNPC official who participated in the negotiations, "[t]here has never been an energy project like this one, which experienced so many complications and reversals. The agreements signed before our eyes still changed in the end. If this current economic crisis had not occurred, I don't know for how long we would have discussed this program, and I don't know how it would have changed."[236]

Diversification of Foreign Exchange Reserves

CDB's EBLs also advance the State Council's objective of diversifying China's massive foreign exchange reserves away from low-yielding financial instruments such as U.S. Treasury Bonds to higher-yielding dollar denominated assets. In September 2010, an official from China's State Administration of Foreign Exchange revealed that 65 percent of China's foreign exchange reserves are in dollar-denominated assets.[237] Some analysts estimate that more than one third of China's foreign

[236] Wang Kangpeng 王康鹏, "中俄原油管道：14年啃下"硬骨头"" ("The China-Russia Oil Pipeline: Fourteen years of gnawing a 'hard bone'"), 第一财经日报 *(China Business News)*, July 24, 2009, as re-posted at http://energy.people.com.cn/GB/9716654.html.

[237] "报导：中国外汇储备中美元比重大约65%" ("Report: About 65% of China's foreign exchange reserves are in US dollars"), 华尔街日报（中国）*(Wall Street Journal (China))*, September 3, 2010, http://cn.wsj.com/gb/20100903/bch105839.asp.

exchange reserves are in US Treasury securities.[238] The concentration of China's foreign assets in US government debt instruments reflects both the fact that there are few other investments large and liquid enough to absorb China's rapidly growing stock of foreign exchange reserves and the longstanding view in China that US Treasury markets were a safe place to park China's foreign exchange reserves because of the United States' long and strong tradition of fighting inflation and thus preventing the erosion of the dollar's real buying power.[239]

The US subprime mortgage crisis, however, made senior Chinese officials question the wisdom of investing so heavily in US government debt. They publicly expressed their concerns that Washington's loose monetary policy and heavy deficit spending in response to the crisis would generate inflation and further erode the value of China's dollar reserves. In December 2008, Vice Premier Wang Qishan told Secretary of the Treasury Henry Paulson, "[w]e hope the US side will adopt every necessary measure to stabilize its economy and financial markets, and ensure the safety of China's assets and investments in the United States."[240] In March 2009, Premier Wen Jiabao expressed his anxiety during a news conference at the end of the annual session of the National People's Congress, saying "[w]e have lent a huge amount of money to the United States. Of course we are concerned about the safety of our assets. To be honest, I am definitely a little worried."[241]

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[238] Eswar S. Prasad, "The U.S.-China Economic Relationship: Shifts and Twists in the Balance of Power," U.S.-China Economic and Security Review Commission, Hearing on "U.S. Debt to China: Implications and Repercussions," February 25, 2010, p. 4, http://www.brookings.edu/~/media/Files/rc/testimonies/2010/0225_us_china_debt_prasad/20100225_us_china_debt_prasad.pdf; and Brad Setser and Arpana Pandey, "China's $1.5 Trillion Bet," Council on Foreign Relations Working Paper, January 2009, http://www.cfr.org/china/chinas-15-trillion-bet-understanding-chinas-external-portfolio/p18149.

[239] Email from Albert Keidel, June 28, 2010.

[240] Cary Huang and Al Guo, "US urged to protect China's investments; Vice-Premiers asks Washington to Keep Financial Markets Stable," *South China Morning Post*, December 5, 2008.

[241] Michael Wines, "China's Leader Says He Is 'Worried' Over U.S. Treasuries," *New York Times*, March 14, 2009., http://www.nytimes.com/2009/03/14/business/worldbusiness/14china.html.

Concerns about the safety of China's assets in the United States in the wake of financial crisis intensified the pressure on the managers of China's foreign exchange reserves to invest in assets that would generate higher returns than low-yielding US Treasury bills. One of the ways the Chinese government is seeking to diversify its external portfolio away from US government debt instruments is by encouraging Chinese firms to invest abroad. On July 15, 2009, the State Administration of Foreign Exchange announced that it would loosen control on foreign direct investment by Chinese firms to encourage them to expand overseas.[242] A few days later, during the Chinese Communist Party's 11th ambassadorial conference, which has often served as a venue for new policy announcements, Premier Wen Jiabao endorsed the "going global" strategy as a vehicle for diversifying China's foreign exchange reserves, stating that "we should speed up the implementation of the 'going global' strategy and combine the use of foreign exchange reserves with enterprises 'going global.'"[243]

Chen Yuan has promoted CDB's international projects, especially its cross-border energy and natural resource deals, as a medium for shifting China's foreign exchange reserves away from low-yielding financial instruments into higher-yielding risk assets.[244] According to Chen, investing in energy and minerals is a good way to hedge against a declining dollar and rising commodity prices. In an interview with China Central

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[242] State Administration of Foreign Exchange, "Circular of the State Administration of Foreign Exchange on Issuing the Regulations of Foreign Exchange Administration of the Overseas Direct Investments of Domestic Institutions," July 13, 2009, http://www.safe.gov.cn/model_safe_en/laws_en/laws_detail_en.jsp?ID=30600000000000000,52&type=&id=3; and "China simplifies rules on forex use to boost outbound investment," *Xinhua*, July 20, 2009.

[243] "第十一驻外使节会议召开 胡锦涛，温家宝讲话" ("The eleventh meeting of diplomatic envoys convenes in Beijing; Hu Jintao and Wen Jiabao make speeches"), 新华社 (*Xinhua*), July 20, 2009, http://www.gov.cn/ldhd/2009-07/20/content_1370171.htm; and Bonnie Glaser and Benjamin Dooley, "China's 11th Ambassadorial Conference Signals Continuity and Change in Foreign Policy," *China Brief*, Vol. 9, No.22 (November 4, 2009), p. 8, http://www.jamestown.org/uploads/media/cb_009_61.pdf.

[244] "Development Finance: The Common Development Path."

Television in July 2009, Chen made his oft-quoted statement that "everybody is saying that we should go to the international markets to buy up low-price assets. But I don't think we should go to Wall Street. We should think more about making acquisitions or partnerships in areas with natural resources."[245] The following month, in an interview with Hong Kong's Phoenix TV, Chen explained that China's long-term demand for minerals such as aluminum, copper and iron ore makes these resources a safe long-term investment: "We've thought about the risk. Not the risk of international market fluctuations, but the risk of our own steady development. As long as we have confidence in the ability of China's economy to continue to grow, then the risk is locked in."[246] Another interlocutor from CDB put it even more succinctly, stating that "when your fate is bound to the fate of the country, the risks you bear are lower."[247] (Chen's assessment of the low risk associated with investments in energy and natural resources is shared by Lou Jiwei, the chairman of CIC, who has justified the sovereign wealth fund's recent spate of investments in energy, minerals and commodities in similar terms. In a speech in October 2009, Lou said "bulk commodities are an investment focus for CIC. The main reason is China's rapid economic growth. There is a high correlation between China's economic growth and the price of bulk commodities. We are not allowed to invest in Renminbi exchange zones, but we want to share in the success of China's economic growth."[248])

The NOCs' Interests

CDB's energy loans also dovetail with a strategic priority of China's NOCs, the expansion of their international

[245] Rui, "Chen Yuan: Recommending Chinese enterprises make acquisitions."
[246] "Phoenix TV's Exclusive Interview with Chen Yuan."
[247] Zhang and Dong, "The Lender—China Development Bank."
[248] "楼继伟：中投重点投资大宗商品并用房地产对冲通胀" ("Lou Jiwei: CIC is focusing on investing in commodities and using real estate to combat inflation"), 风凰网 (*Phoenix TV*), October 28, 2009, http://finance.ifeng.com/news/special/qhgllt09/20091028/1398574.shtml.

exploration and production portfolios. China's oil majors have been investing abroad since the mid-1990s for several reasons. First, the NOCs seek to grow their reserves and production, and China's aging oil fields limit the opportunities for China's NOCs to do this within China's borders. Second, China's oil majors are investing abroad to make money. Historically, exploration and production has been the most profitable part of the oil business. This is especially true for CNPC and Sinopec, which have suffered losses in their downstream operations as a result of price controls for crude oil (abolished in 1993) and for refined products (still in place). Third, China's NOCs are expanding abroad to increase their international competitiveness through the development of new capacities, such as ultra-deepwater drilling.[249]

The recipients of CDB's largesse control some of the most important sources of future growth in world oil and natural gas supplies. CDB's generosity has already landed CNPC a role in the development of one of the world's largest natural gas fields in Turkmenistan and undoubtedly bolstered Hugo Chávez's already considerable enthusiasm for the expansion of China's NOCs in Venezuela. CDB and Sinopec also probably expect that the political goodwill generated by its loans will help Sinopec secure upstream projects in Brazil. In the words of Chen Yuan, CDB's cross-border energy deals "have now taken CNPC and Sinopec to places they wanted to go but could not go before."[250]

Turkmenistan

CDB's $4 billion loan to Turkmengaz has helped CNPC secure a role in the development of the South Yolotan natural

[249] For more on this issue, see Erica S. Downs, "Who's Afraid of China's National Oil Companies?" in Carlos Pascual and Jonathan Elkind, eds., *Energy Security: Economics, Politics, Strategies and Implications* (Brookings Institution Press, 2010), pp. 73-102; and Trevor Houser, "The Roots of Chinese Oil Investment Abroad," *Asia Policy*, No. 5 (January 2008), pp. 141-166.

[250] Rui, "Chen Yuan: Recommending Chinese enterprises make acquisitions."

gas field. The UK consultancy Gaffney, Cline & Associates estimates that South Yolotan contains between 4 and 14 trillion cubic meters of natural gas, ranking it among the five largest in the world.[251] Not only is CDB's loan earmarked for the development of South Yolotan, but CNPC is already the dominant foreign player in Turkmenistan's onshore fields. In 2007, Turkmenistan awarded CNPC a production sharing agreement to develop the Bagtiyarlyk field on the right bank of the Amu Darya River, making the Chinese firm the first—and so far only—foreign company to operate onshore in Turkmenistan. According to Murad S. Nazarov, Turkmenistan's Ambassador to China, when Turkmenistan's Deputy Prime Minister Tachberdy Tagiev visited Beijing in early June 2009 to discuss financing for the development of South Yolotan, he said that Chinese companies would be welcome to participate.[252] Six months later, Ashgabat awarded CNPC a service contract worth more than $3 billion to produce 10 bcm per year at South Yolotan.[253]

Venezuela

CDB's loans to Caracas have undoubtedly helped China's NOCs win upstream projects in Venezuela's Orinoco Belt, which has the potential to be an important source of world oil supply growth in the long-term. According to Cambridge Energy Research Associates, the amount of recoverable extra-heavy oil in the Orinoco Belt is about 130 billion barrels, which could be increased to about 260 million barrels.[254] The

[251] Guy Chazan, "Turkmenistan Gas Field is One of World's Largest," *Wall Street Journal*, October 16, 2008, http://online.wsj.com/article/SB122409510811337137.html.

[252] Interview with Murad S. Nazarov in "中国每年接受土库曼斯坦400亿立方米天然气" ("China will receive 40 billion cubic meters per year of natural gas from Turkmenistan"), 21世纪经济导报 (*21st Century Business Herald*), June 24, 2009, as re-posted at http://news.163.com/09/0624/02/5CHQKS2G0001124J.html.

[253] "Turkmenistan dishes deals for South Iolotan," Upstream, January 8, 2010; and Neil Rodova and Geoff King, "CNPC, LG win $10 bn in Turkmen contracts," *Platts Oilgram News*, December 31, 2009.

[254] Enrique Sira, "Venezuela's Extra Heavy Oil Bidding Round: A Sustainable Growth Opportunity?" CERA Decision Brief, April 2009, p. 1.

latter figure exceeds the current reserves of Venezuela (172 billion barrels) and rivals those of Saudi Arabia (265 billion barrels).[255]

Money and friendship have been the keys to securing a foothold in the Orinoco Belt, where PDVSA has awarded blocks to oil companies with cash from countries that have good political relations with Venezuela.[256] President Hugo Chávez has made no secret of his enthusiasm for exchanging Venezuelan oil for Chinese loans. During bilateral discussions about a third $4 billion loan to the Joint Investment Fund from CDB, he announced on state television that "[t]his bank is the one with the most money in the world. It has half the money in the world and is allied with Venezuela."[257] After CDB agreed to provide an additional $20 billion in loans to Caracas, Chávez also gushed about the latest oil export revenue backed loan brokered with the Chinese on state television, declaring: "we agreed on a huge, long-term financing plan. This is a larger scope, super heavy fund. China, the world's second-biggest oil user, needs energy security and we're here to provide them with all the oil they need."[258]

The bilateral energy accords signed on April 17, 2010 include not only the framework agreement for the latest EBL but also another MOU between PDVSA and CNPC for the creation of a joint venture company to develop the Junin-4 block in the Orinoco Belt, which the two companies finalized on December 1, 2010.[259] PDVSA and CNPC plan to develop the

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[255] *BP Statistical Review of World Energy*, June 2010, p. 6, www.bp.com.
[256] Sira, "Venezuela's Extra Heavy Oil Bidding Round."
[257] Steven Bodzin, "Venezuela, China May Sign New Loan-for-Oil Accord," July 3, 2009, http://bloomberg.com/apps/news?pid=20670001&sid=ab3S0C0X1Rdk.
[258] "China lends Venezuela $20b, secures oil supply," *China Daily (Online)*, April 19, 2010, http://www.chinadaily.com.cn/business/2010-04/19/content_9748799.htm.
[259] Juliette Kerr, "Venezuela Seals New Oil Deals with Chinese Companies," *IHS Global Insight Daily Analysis*, December 6, 2010; and "PDVSA and CNPC form a joint venture to produce and improve 400 MBD of crude oil," April 19, 2010, www.pdvsa.com.

block over a twenty-five year period. Production is expected to begin at 50,000 b/d in 2012 and reach the design capacity of 400,000 b/d in 2016, although industry experts have expressed some skepticism that those deadlines will be met.[260] The investment required is estimated at $16.23 billion.[261] CNPC will also pay a $900 million bonus in eight disbursements.[262] The development of the Junin-4 block is part of an integrated project, under discussion for several years, which encompasses the production of extra-heavy oil and the construction of an "upgrader" in Venezuela to process it into a lighter crude blend, which would then be shipped to a 400,000 b/d joint venture refinery to be built in China's Guangdong Province.[263] The December accords also included agreements for Sinopec and PDVSA to develop the Junin-1 and Junin-8 blocks in the Orinoco belt, each of which has a projected production capacity of 200,000 b/d, and for CNOOC to invest in the Mariscal Sucre natural gas fields.[264]

Brazil

Sinopec may get a stake in two deepwater blocks off the northeast coast of Brazil as a result of CDB's $10 billion loan to Petrobras. On April 15, 2010, Sinopec, CDB and Petrobras signed a strategic cooperation agreement aimed at assessing areas of cooperation that developed out of the MOU that Sinopec and Petrobas signed on May 19, 2009. According to the press release on the agreement issued by Petrobras, cooperation in exploration and development includes "the intention of the parties to assess future partnerships, including the possibility

[260] "Factbox—Venezuela development plan for Orinoco oil belt," *Reuters*, October 11, 2010; and Lisa Viscidi, "Venezuela: Friendlier Mood," *Energy Compass*, November 26, 2010.
[261] Kerr, "Venezuela Seals New Oil Deals," *IHS Global Insight Daily Analysis*.
[262] "Factbox—Venezuelan development plan."
[263] Vandana Hari, "China, Venezuela agree two new oil deals; CNPC, PDVSA to develop Orinoco crude, build big refinery in Guangdong Province," *Platts Oilgram News*, May 13, 2008.
[264] "China will pump 40 billion dollars in Venezuela energy," *AFP*, December 3, 2010.

of selling part of Petobras' interest in blocks BM-PAMA-3 and BM-PAMA-8, located in the Pará-Maranhão Basin."[265]

China's NOCs have also expressed interest in playing a role in the development of Brazil's vast oil resources, especially the pre-salt deposits in the ultra-deep waters off the country's southeastern coast that CDB's line of credit is helping to fund. The pre-salt deposits, discovered by Petrobras in 2007, are one of the world's largest oil finds in recent years. The Tupi, Iara and Guara oil fields alone could double Brazil's reserves from 12.6 to more than 25 billion barrels.[266] This newfound oil wealth is not the only reason China's NOCs are seeking a foothold in the Brazilian upstream. China's oil majors are also eager to partner with Petrobras because it is a world leader in deepwater drilling, a capacity that China's oil companies are eager to develop. Although Petrobras signed an MOU with Sinopec to explore upstream cooperation opportunities in conjunction with the Brazilian company's loan negotiations with CDB, neither agreement guarantees Sinopec or its domestic peers a role in tapping Brazil's pre-salt deposits.[267] Their discovery has prompted Brasilia to adopt a more nationalist oil policy for the development of the crown jewels of Brazil's oil industry.[268]

Coordination is not Synonymous with Top-down Decision-making

The mix of national and corporate interests advanced by the EBLs and CDB's status as a state-owned bank with a mission

[265] "Cooperation Agreement with China," April 15, 2010, Securities and Exchange Commission, http://www.edgar-online.com.
[266] Email from TJ Conway, PFC Energy, November 4, 2009.
[267] Petrobras, "Contracting of a Credit Line Worth $10 billion from the China Development Bank (CDB)," May 19, 2009, Securities and Exchange Commission http://www.edgar-online.com.
[268] "Brazil Industry: State-led oil policy sidelines private sector," *EIU Viewswire Select*, September 8, 2009.

to advance the State Council's policy agenda raises the question: who's in the driver's seat? Although CDB has considerable autonomy, it is not an entirely independent actor. All of CDB's international projects require the approval of the State Council. However, not all projects supported by the State Council originate with the State Council. The deals with Brazil and Russia indicate that the relationship between CDB and the central government in developing cross-border energy deals that are also high priority projects for the State Council varies from case to case. The EBL extended to Petrobras is an example of a project that originated with CDB and rose to the attention of the central government, while the EBLs to Rosneft and Transneft an example of a project in which the central government was involved from the start.

Chen Yuan is especially proud of CDB's deal with Petrobras because it grew out of the bank's efforts to develop business abroad.[269] CDB dispatched a work team to Brazil in the mid-2000s to search for financing opportunities, especially in natural resources, infrastructure and agriculture.[270] Chen Yuan visited the country in 2006. CDB made its first loan to Petrobras in 2007, providing it with a $750 million line of credit to finance the construction of the third leg of the Gasene natural gas pipeline by Sinopec.[271] In October 2008, as the global financial crisis deepened and falling oil prices threatened Petrobras' plans to quickly develop its high-cost pre-salt oil resources, CDB approached Petrobras about providing the company with a substantial line of credit in return for a doubling or even

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[269] Rui, "Chen Yuan: Recommending Chinese enterprises make acquisitions," *Economic Observer*; and "国开行 '以贷款换资源' 成功运作一批大项目" ("The successful operation of CDB's 'exchange of loans for resources' yields a batch of big projects"), 人民网 (*People's Daily Online*), September 7, 2009, http://finance.people.com.cn/GB/9998603.html.

[270] China Development Bank, "国家开发银行基本情况介绍" ("An Introduction to China Development Bank"), PowerPoint presentation, August 2008, p. 21.

[271] Petrobras, Form 6-K filed with the Securities and Exchange Commission, December 27, 2007, http://www.sec.gov/Archives/edgar/data/1119639/000129281407003654/pbra20071227_6k.htm.

a quadrupling of the company's oil exports to China.[272] Less than a month later, while Petrobras' CEO José Sergio Gabrielli was in Beijing to attend a biannual summit for national oil company executives hosted by China's three major NOCs, he met with CDB and Sinopec executives.[273] Chen Yuan recalled that "even though he only brought 2-3 people with him, I felt he wanted to cooperate because he brought them."[274]

CDB's plans to extend a large loan to Petrobras gained the support of the Chinese government when it realized that the deal would make a good diplomatic deliverable for Chinese Vice President Xi Jinping's trip to Brasilia in February 2009 and Brazilian President Luiz Inácio Lula da Silva's visit to Beijing in May 2009. The coincidence of the negotiations between CDB and Petrobras with the preparation for the two sets of meeting between Chinese and Brazilian leaders prompted the Chinese government to embrace the deal as a symbol of the growing economic ties between China and Brazil. According to Chen Yuan, "once the Ministry of Foreign Affairs, the Ministry of Commerce, the National Development and Reform Commission and the State Council realized this coincidence, they provided their active support. As a result, this project became a national project."[275] CDB, Petrobras and Sinopec signed memoranda of understanding in Brasilia on February 19, and Gabrielli announced both sides' intention to finalize the agreements by the time of Lula's visit to Beijing three months later.[276] On May 19,

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[272] "Phoenix TV's Exclusive Interview with Chen Yuan;" and "在"走出去"中促发展方式转变—国开行开展国际合作业务纪实,"国际商报 *(International Business Daily)*, March 12, 2010, as re-posted at http://www.cdb.com.cn/Web/NewsInfo.asp?NewsId=3300.

[273] "中石化， 国开行与巴西石油谈判台前幕后的故事" ("The front row and behind the scenes story of the negotiations between Sinopec, China Development Bank and Petrobras"), 第一财经日报 (*China Business News*), May 22, 2009, as re-posted at http://ccnews.people.com.cn/GB/9346336.html; "Update 1—Petrobras in talks with Sinopec for refinery stake," *Reuters*, November 7, 2008, http://www.reuters.com/assets/print?aid=USSP20706220081107; and Takeo Kumagai, "Petrobras, CNOOC to discuss cooperation during Beijing visit," *Platts Oilgram News*, October 29, 2008.

[274] "Phoenix TV's Exclusive Interview with Chen Yuan."

[275] *Ibid.*

[276] "Update 2 – Brazil sells oil to China, expects $10 bn loan," *Reuters*, February 19, 2009.

they concluded the deal at a signing ceremony attended by Hu Jintao and Luiz Inácio Lula da Silva. The two presidents indicated their support for the implementation of the EBL in their *Joint Communiqué Between the People's Republic of China and The Federative Republic of Brazil on Further Strengthening China-Brazil Strategic Partnership.*[277]

In contrast, the Chinese government and, to a lesser extent, CNPC drove the two EBLs to the Russian energy companies, and CDB played a supporting role. The Chinese and the Russians have revealed little information about the development of first deal because of its connection to the controversial sell-off of Yuganksneftegaz. Press reports, however, indicate that discussions about this loan probably originated between Rosneft and CNPC in December 2004 at the Yuganskneftegaz auction.[278] The terms of the agreement were most likely finalized in January 2005, when Rosneft president Sergei Bogdanchikov and Russia's Minister of Industry and Energy, Viktor Khristenko, made a secret trip to Beijing.[279] Chinese and Russian leaders were involved in the development of the second EBL, which was negotiated in a series of intergovernmental meetings in 2008 and 2009. For example, the broad parameters of the deal included in the Memorandum of Understanding on Oil Cooperation signed on October 28, 2008 were hammered out in several rounds of bilateral talks led by Wang Qishan and Igor Sechin—in which Chinese and Russian energy companies and banks participated—before Chinese Premier Wen Jiabao's visit to Moscow at the end of October. A bilateral working group led by Zhang Guobao, then the director of China's National Energy

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[277] Hu Jintao and Luiz Inácio Lula da Silva, *Joint Communiqué Between the People's Republic of China and The Federative Republic of Brazil on Further Strengthening China-Brazil Strategic Partnership,* May 19, 2009, http://www.fmprc.gov.cn/eng/wjdt/2649/t566945.htm.

[278] "China's CNPC may help Rosneft pay for Yuganskneftegaz—report," *Xinhua Financial Network News*, January 19, 2005.

[279] "Platt's—Russia's Rosneft inks 5-year crude supply deal with China – report," *Platts Commodity News*, January 23, 2005; and "China's CNPC may help Rosneft pay for Yuganskneftegaz—report," *Xinhua Financial Network News*, January 19, 2005.

Administration and Sergei Shmatko, Russia's Minister of Industry and Energy spearheaded the negotiations over the specific terms of the agreements that comprise the EBL.

Several factors explain the different roles that the CDB and the Chinese government played in the EBLs extended to Petrobras and Rosneft and Transneft. First, senior Chinese leaders, including Wen Jiabao and Wang Qishan, were intimately involved in the deal with the Russia because, unlike the deal with Brazil, it involves a project perceived to enhance China's national security. The ESPO spur is prized in Beijing not only for diversifying China's oil imports away from the Persian Gulf but also for diversifying China's oil import routes away from the sea lines of communication, where they could be interdicted by various modern navies. This pipeline also has national security implications for Russia. Not only does the Kremlin regard export pipelines as sources of geopolitical leverage but Russian deliberations about the ESPO spur have been colored by anxieties about becoming a "resource appendage" to China. Consequently, decisions about the construction of a cross-border oil pipeline have been made at the apex of the Chinese and Russian political systems ever since Boris Yeltsin first proposed the idea to Jiang Zemin in 1994. Indeed, Zhang Guobao described the decision to build the ESPO spur as a far-sighted strategic decision made by politicians in both countries from a political perspective and for preserving good neighborly relations.[280] In contrast, one of the reasons CDB was able to drive the deal with Petrobras was because it does not involve a cross-border infrastructure project with national security implications.

Second, energy cooperation is more deeply intertwined with politics in China's intergovernmental relationship with Russia. This reflects both the strategic importance that Beijing

280 "张国宝：中俄地区合作符合双方共同利益" ("Zhang Guobao: China-Russia regional cooperation befits the common interests of both sides"), 凤凰网 (*Phoenix Online*), February 3, 2010, http://news.ifeng.com/mainland/201002/0203_17_1536315.shtml.

and Moscow attach to bilateral energy cooperation and the difficulties both countries have encountered in forging closer energy ties. In 1999, China and Russia established the ministerial-level China-Russia Sub-Commission on Energy Cooperation, led by Ma Kai, the minister in charge of China's National Development and Reform Commission and Viktor Khristenko, Russia's Minister of Industry and Energy.[281] This body served as a forum for bilateral energy consultations until May 2008, when Premier Wen Jiabao proposed to Igor Sechin that China and Russia establish a vice premier level energy negotiation mechanism.[282] Wen's initiative reflected both the repeated setbacks the Chinese government and CNPC suffered in their efforts to strengthen the bilateral energy relationship—including the lack of progress on the construction of a cross-border oil pipeline, Russia's insistence on renegotiating the terms of the first deal and the reluctance of Russian energy companies and politicians to allow China's oil companies to invest in exploration and production projects in Russia—and the inability of the Sino-Russian Sub-Commission on Energy Cooperation to make substantial progress on these issues. The Sub-commission's ministerial-level status limited its role in the intergovernmental relationship to a discussion forum because decisions about major projects were made at the highest levels of the Chinese and Russian governments. Moreover, the participants from the Chinese side were all ministerial-level institutions, which made coordination extremely difficult because no single institution had the authority to tell any other institution what to do.[283] The vice premier level energy

281 "中石油集团总理马富才谈中俄及中国与中亚石油合作" ("CNPC General Manager Ma Fucai discusses China-Russia and China-Central Asia Oil Cooperation"), 中国石油报 (*"China Petroleum Daily"*), February 12, 2003, http://news.sina.com.cn/c/2003-02-19/1108913908.html.

282 "中俄启动副总理级能源谈判机制" ("China and Russia launch a vice-premier level energy negotiation mechanism"), 中国青年报 *(China Youth Daily)*, July 29, 2008, as re-posted at http://news.xinhuanet.com/world/2008-07/30/content_8845863.htm.

283 Li Zhonghai 李中海 "中俄能源合作：从山重水复到渐入佳境" ("China-Russia Energy Cooperation: from multiple difficulties to gradual improvement," 领导之友 (*Friend of Leaders*), No. 1 (2009), http://euroasia.cass.cn/news/140630.htm.

negotiation mechanism, by definition, involved more senior officials in negotiations on bilateral energy projects such as the EBLs extended to Rosneft and Transneft.

In contrast, energy cooperation is not as deeply intertwined with politics in the bilateral relationship between China and Brazil. To be sure, the NDRC and Brazil's Ministry of Mines and Energy established the ministerial-level Sub-commission on Energy and Mining of the China-Brazil High-Level Coordination and Cooperation Commission in 2006. But CDB's loan to Petrobras did not originate from this body. In fact, it was precisely the lack of close energy ties between China and Brazil at both the government and firm levels that created an opportunity for CDB to play a pioneering role in strengthening China's energy ties to Brazil.

Finally, Chinese government officials were much more involved in the brokering the deal with Russia than the one with Brazil because Rosneft is much more intertwined with the Russian government than Petrobras is with the Brazilian government. Igor Sechin is both deputy prime minister of the Russian Federation and chairman of the board of Rosneft, a position to which he was appointed by Vladimir Putin, who remains the ultimate arbiter on which export pipelines will be built. As a result, when CDB and CNPC officials interact with Sechin, they are dealing not only with a national oil company executive but also a senior Russian official whose authority over bilateral energy projects exceeds their own. In contrast, when CDB and Sinopec officials meet with Sergei José Gabrielli, they are only engaging with the president of a national oil company.

Implications for the United States

The emergence of state-owned Chinese companies as increasingly active players in international mergers and acquisitions has generated some suspicion in the United States that their business activities may be inimical to American interests because they may be motivated, at least in part, by the strategic objectives of the Chinese government. These anxieties have been most acute in cases where Chinese companies have sought to invest in the United States but they also apply to the expansion of Chinese firms in other parts of the world, including Africa and Latin America. CDB's EBLs, however, demonstrate that cross-border deals by state-owned Chinese firms driven, in part, by the policy priorities of the Chinese leadership have both positive and negative implications for the United States. On the one hand, CDB's loans promote some US goals in Central Asia, indicate that Chinese lenders are likely to become more concerned about good economic policymaking in recipient countries as their international business expands, and are not reducing the amount of oil available to the United States and other consumers. On the other hand, CDB's loans are empowering anti-American regimes in Latin America and may increasingly provide Chinese companies with a competitive advantage over private sector firms that do not have access to financial support from state-owned banks.

CDB's lending supports some American interests in Central Asia

CDB's loan to Turkmenistan is aligned with some American interests in Central Asia. First, CDB's loan supports the US goal of bringing incremental energy supplies to the world market. The loan is earmarked for the development of the South Yolotan natural gas field, and some gas from this field will probably flow through the Central Asian Natural Gas Pipeline to China.

Second, CDB's loan—and the broader trend of Chinese economic expansion in Central Asia of which it is a part—advances the US goal of supporting the independence of Central Asian states by providing them with multiple energy export options. One of the most interesting developments in Central Asian geopolitics over the past decade has been China's economic expansion, notably in the energy sector, which has often come at Russia's expense. As Evan Feigenbaum has observed, Central Asia's principal strategic problem is geography.[284] Until China arrived in the region, Central Asian energy producers were highly dependent on Russian markets and export routes, which gave Moscow enormous economic and political influence over them. However, China has championed the construction of oil and natural gas pipelines from Central Asia to China, providing them with both non-Russian outlets for their oil and natural gas and greater autonomy from Moscow. The increasing competition between China and Russia for greater influence in Central Asia is arguably most acute in the case of Turkmenistan. The Central Asian Natural Gas Pipeline, which was financed in part by CDB, has broken Russia's near-monopsony on Turkmen natural gas exports and increased Ashgabat's bargaining power with Moscow.[285] As a

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[284] Evan A. Feigenbaum, "China's Big Play in Central Asia," January 5, 2010, http://blogs.cfr.org/asia/2010/01/05/chinas-big-play-in-central-asia/.

[285] "Russia: Losing Central Asia to China?" *Economist Intelligence Unit—Executive Briefing*, January 5, 2010; and Alexander Monro and Dana Denis Smith, "China taps into the heart of Turkmenistan's gas fields," *Financial Times*, December 17, 2009.

result, Turkmenistan will likely be able to leverage the project to extract a higher price from Gazprom for its natural gas exports to Russia.[286] China is likely to become a more important bargaining chip as the volumes of natural gas flowing to China increase; China may become Turkmenistan's largest buyer of natural gas as early as 2011.[287]

CDB's $4 billion loan to Turkmengaz is another manifestation of China's emergence as a counterweight to Russia in Central Asia.[288] Ashgabat turned to Beijing for financial assistance after an explosion on the pipeline that delivered the majority of Turkmenistan's natural gas exports to Russia in April 2009 during a protracted pricing dispute with Turkmengaz. Although Turkmen technicians were able to repair the pipeline within a few days, deliveries did not resume until more than eight months later.[289] Not only did the request for the loan indicate that Ashgabat viewed Beijing as an alternative economic partner to Moscow, but the loan itself is binding Turkmenistan more closely to China. Bilateral ties will undoubtedly become even tighter if CDB grants Ashgabat the second $4.1 billion loan Turkmen officials have requested for the development of the South Yolotan field.

CDB is concerned about good economic decision-making in recipient countries

China's emergence as a source of finance for developing countries has raised concerns in the United States and other

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[286] Julia Nanay, testimony before the U.S.-China Economic and Security Review Commission, hearing on "The Impact of China's Economic and Security Interests in Continental Asia on the United States," panel on "Continental Asia in China's Global Energy Strategy," May 20, 2009, http://www.uscc.gov/hearings/2009hearings/written_testimonies/09_05_20_wrts/09_05_20_nanay_statement.pdf.

[287] John Roberts, "Defining year for Caspian gas," *Platts Energy in East Europe*, January 15, 2010.

[288] For more on CDB's loan and Chinese influence in Central Asia, see Feigenbaum, "China's Big Play in Central Asia;" and "Riches in the Near Abroad," *The Economist*, January 28, 2010.

[289] Roberts, "Defining year for Caspian gas;" and Andrew Neff and Tom Grieder, "Chinese, Central Asian Leaders Celebrate Historic Launch of Gas Pipeline," *IHS Global Insight Daily Analysis*, December 14, 2009.

countries because the practices of Chinese lenders diverge from those of established multilateral donors, including the International Monetary Fund (IMF) and the World Bank, and members of the Organization for Economic Cooperation and Development (OECD).[290] Chinese banks generally have not emphasized combating corruption, fostering transparency or raising environmental and social standards to the extent that Western donors do. Moreover, many Chinese loans are tied to purchases from China or investment from Chinese firms, a practice that OECD member countries frown upon because it often prevents the recipient countries from receiving good value for money for goods and services.[291]

CDB's loans to Venezuela, however, indicate that the bank, like the established multilateral donors and OECD member countries, aims to promote good economic decision-making in borrowing countries. In May 2010, while the Chinese and Venezuelans were negotiating the terms of the $20.6 billion dual credit facility, a team of more than 30 Chinese consultants led by Liu Kegu, a former vice governor of and current advisor to CDB, and Zheng Xinli, a permanent vice chairman of the China Center for International Economic Exchanges, a think tank where Chen Yuan serves as an executive vice chairman, spent eighteen days in Venezuela.[292] The visit had two related

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290 For an overview of these concerns, see Deborah Brautigam, "China's African Aid: Transatlantic Challenges," German Marshall Fund of the United States, Washington, DC, 2008, http://209.200.80.89/doc/Brautigam0410aFINAL.pdf.

291 Organisation for Economic Co-operation and Development, "Untying Aid: The right to choose," http://www.oecd.org/document/50/0,3343,en_2649_33721_46345330_1_1_1_1,00.html.

292 Xu Yisheng 徐以升, Chen Xiaochen 陈晓晨 and Li Donchao 李东超, "走出去" 战略要放大 "委内瑞拉模式" ("The 'going out' strategy should enlarge the 'Venezuela model'"), 第一财经日报（*China Business News*), August 16, 2010, http://money.jrj.com.cn/2010/08/1601567950217.shtml; "郑新立：调控要以房价稳定为目标 避免大面积下降" ("Zheng Xinli: Regulations should aim at stabilizing housing prices and avoiding a large drop"), 凤凰网（*Phoenix Online*), July 20, 2010, http://finance.ifeng.com/news/special/CCIEE13/20100720/2426212.shtml; and Cheng Li, "China's New Think Tanks: Where Officials, Entrepreneurs and Scholars Interact," *China Leadership Monitor*, No. 29 (Summer 2009), p. 8, http://media.hoover.org/sites/default/files/documents/CLM29CL.pdf.

goals. First, the Chinese delegation, which included representatives from Chinese energy and mining companies, assessed Venezuela's ability to secure the proposed loans with natural resources.[293] Second, the Chinese drafted plans for Caracas to reform and grow its economy.[294] They provided roadmaps for Caracas to achieve price stability within three years and to improve the climate for foreign investment and economic development within six years. The Chinese also recommended that the Venezuelans focus on developing four pillar industries—agriculture, mining, real estate and consumer goods—into engines of economic growth. According to Zheng Xinli, "if Venezuela is able to execute this plan, within the next ten to twenty years, it will be no problem for Venezuela to maintain an 8 percent economic growth rate like China."[295] This goal, however, is likely to be very difficult for Venezuela to reach because of its low level of administrative competence.[296]

The Chinese efforts to help Venezuela reform and grow its economy indicates that as CDB and other Chinese banks continue to provide large loans to foreign countries, they will probably become more involved in trying to shape economic decision-making in borrowing countries to ensure repayment of their loans and to protect investments made by Chinese companies in conjunction with the loans. CDB, in particular, may continue to dispense advice to borrowing countries on how to achieve economic growth and stability because of its strong culture of managing risks and growing profits.

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[293] Xu, Chen and Li, "The 'going out' strategy."

[294] *Ibid*.; For a more colorful account of the advice provided by the Chinese, see Roger F. Noriega, "Chávez and China: Challenging U.S. Interests," *Latin American Outlook*, No. 3 (August 2010), pp. 3-4, http://www.aei.org/docLib/03-LAO-2010-g.pdf.

[295] Xu, Chen and Li, "The 'going out' strategy."

[296] I thank Kevin Casas-Zamora for this point. See also, Javier Corrales and Michael Penfold, *Dragon in the Tropics: Hugo Chávez and the Political Economy of Revolution in Venezuela* (Brookings Institution Press, 2011), chapter 3, especially pp. 59 and 69.

CDB's EBLs are not reducing the amount of oil available to other customers

CDB's EBLs are not removing oil from the world market and reducing the amount available to other consumers because the oil market is global. Although many media reports describe the deals as "locking up" oil for China, the supply contracts securing CDB's loans are not shrinking the pool of tradable oil because the oil market is global.[297] Any additional oil that China imports from Russia, Ecuador, Brazil or Venezuela as a result of these deals merely replaces oil that China would import from other countries.

Even the increase in PDVSA's oil deliveries to Chinaoil as part of CDB's latest "loans-for-oil" deal with Venezuela are unlikely to undermine the security of American oil supplies despite Chávez's goal of diversifying Venezuela's oil exports away from the United States, its largest customer, to other markets, notably China.[298] An extra 300,000 b/d of crude oil flowing to China means that China would have to purchase 300,000 b/d less on the world market, freeing up supply for the United States.[299] Although some industry analysts have noted that substitute oil supplies would be more costly if they came from producers further away from the United States than Venezuela, the United States has new sources of supply in the Western

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[297] See, for example, Ariana Eunjung Cha, "China Gains Key Assets in Spate of Purchases; Oil, Minerals Are Among Acquisitions Worldwide," *Washington Post*, March 17, 2009, http://www.washingtonpost.com/wp-dyn/content/article/2009/03/16/AR2009031603293.html; David Winning, Shai Oster and Alex Wilson, "China, Russia Strike $25 Billion Oil Pact; In Third Deal in a Week, Beijing Moves to Lock Up Natural Resources at Bargain Prices to Fuel Growth," *Wall Street Journal*, February 18, 2009; and Michael Lelyveld, "China Splurges on Foreign Oil," *Radio Free Asia*, March 9, 2009, http://www.rfa.org/english/energy_watch/china-oil-03092009143452.html.

[298] See, for example, Juan Forero, "Venezuela Cautions U.S. It May Curtail Oil Exports," *New York Times*, February 27, 2006, http://www.nytimes.com/2006/02/27/international/americas/27venez.html.

[299] Grant Laten, "Venezuelan Oil Embargo Wouldn't Impact American Energy Security, August 3, 2010, http://csis.org/blog/venezuelan-oil-embargo-wouldn%E2%80%99t-impact-american-energy-security.

hemisphere from Brazil and Canada, where production is projected to grow over the next 25 years.[300]

Moreover, it is unlikely that Venezuela will quickly export large volumes of crude to China at the expense of the United States because of refining and transportation issues. The United States, which has substantial capacity to refine heavy, sour Venezuelan crudes, is only a five-day tanker trip from Venezuela, whereas China, which currently does not have the refining capacity to process large volumes of Venezuelan oil, is a 30-day tanker trip.[301] Consequently, Chinaoil might opt to sell the oil the oil it receives from PDVSA to the United States. Indeed, China's NOCs have already established a trading presence in the Americas by buying refineries and storage facilities in the region.[302] A comparison of Venezuelan and Chinese oil trade data indicates that some of the oil PDVSA sells to Chinaoil to secure CDB's contributions to the China-Venezuela Joint Investment Fund may be sold locally. While PDVSA reports that it exported 275,000 b/d of petroleum products to China in 2009, Chinese customs data indicates that China only imported 85,000 b/d of petroleum products (all fuel oil) from Venezuela.[303]

CDB's loans are supporting anti-American regimes in Latin America

CDB's loans are bolstering the administrations of Hugo Chávez in Venezuela and Rafael Correa in Ecuador, two regimes unfriendly towards the United States. Empowering these governments is not CDB's objective. Nonetheless, CDB is supporting

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[300] International Energy Agency, *World Energy Outlook 2010*, p. 128.
[301] Forero, "Venezuela Cautions U.S."
[302] Lisa Viscidi, "Venezuelan Oil Production and Exports," presentation at the Center for International and Strategic Studies, Washington, DC, July 22, 2010, http://csis.org/files/attachments/100722_Venezuela_CSIS_energy_intl.pdf.
[303] PDVSA, *Informe de Gestión Annual 2009 (2009 Annual Management Report)*, p. 127, http://www.pdvsa.com/interface.sp/database/fichero/free/5889/1049.pdf; and "Oil Data: Tables of China December Oil Imports," *Dow Jones Energy Service*, January 21, 2010.

Chávez and Correa by serving as a "lender of last resort" to their governments, whose difficulties accessing international financial markets because of risk perception and hostility toward the IMF have left them with few, if any alternatives, to Chinese banks for external sources of capital. Both administrations are using money from CDB to address key political vulnerabilities that are negatively impacting their popularity.

CDB's largesse has made the bank one of Venezuela's lenders of last resort. Borrowing from the IMF, which is able to provide Caracas with the substantial amount of capital it needs to keep the economy afloat is politically infeasible for Chávez, in large part because the conditionalities imposed by the institution would likely cause his government to fall.[304] Regional multilateral institutions, such as the Inter-American Development Bank and the Andean Development Corporation, do not have the financial resources to provide Caracas with loans of the size CDB has offered.[305] As a result, Caracas has opted to raise funds by brokering oil and gold export-backed deals with foreign governmental institutions, of which the loans from CDB are the largest by far.[306]

The credit provided by CDB through its contributions to the JIF has helped cushion Venezuela's public finances, which have been decimated by gross economic mismanagement and the plunge in oil prices in the wake of the global financial crisis. President Hugo Chávez took advantage of the surge in world oil prices during most of the 2000s to engage in rampant public spending aimed at fostering a "socialist revolution" and keeping himself in power. The lower oil price environment in 2009 and 2010 threatened both of these objectives because oil provides more than half of government income. The decline

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[304] Telephone interview with an expert on the Venezuelan economy, May 14, 2010.

[305] Email from an expert on Venezuelan politics and economics, May 13, 2010.

[306] Steven Bodzin and Shigeru Sato, "Japan May End $1.5 Billion Venezuela Loan on Seizures (Updates)," *Bloomberg*, June 23, 2009, http://www.bloomberg.com/apps/news?pid=newsarchive&sid=aHfRkWQcvqeQ.

in windfall oil profits prompted Chávez to turn to CDB for additional financial assistance to combat Venezuela's mounting economic woes and shore up political support.

The $20.6 billion loan that CDB has extended to Caracas is helping to finance Chávez's bid to win a third consecutive six-year term as president in 2012. Chávez's popularity has declined amid a deep recession, steep inflation, water and electricity shortages, and rising crime. A survey conducted in the summer of 2010 by the Caracas-based polling firm Consultores 21 indicated that Chávez's popularity had dropped 12 percentage points over the past year and only 36 percent of Venezuelans approve of his performance.[307] Against this backdrop, Chávez suffered a blow in the legislative elections held on September 26, 2010. His party, the United Socialist Party of Venezuela (PSUV), lost the popular vote and only retained majority control because of gerrymandering.[308] These results suggest that Chávez may face more competition for the presidency in 2012.

Statements by Chávez and other government officials indicate that the new $20.6 billion line of credit from CDB will be used to tackle some of the economic problems that have hurt Chávez's popularity, notably the shortages of electricity and housing. First, $5.5 billion has been earmarked for the addition of at least 2,750 megawatts of capacity to the national power grid by the end of 2012.[309] This new spending in the electricity sector is part of Caracas' efforts to prevent the recurrence of the widespread blackouts that plagued Venezuela in late 2009 and early 2010 due to a severe drought, underinvestment,

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[307] Fabiola Sanchez, "Chávez popularity at 7-year low as campaigning starts for Venezuela vote, pollster says," *Associated Press*, August 25, 2010.

[308] Mery Mogollon and Chris Kraul, "Discretionary Powers for Chávez; The Venezuelan Congress allows him to govern by decree for the next eighteen months," *Los Angeles Times*, December 18, 2010, p. A4.

[309] Dan Molinski, "Venezuela to Spend Half of $20 Bln China Loan Within 3 Years," *Dow Jones News Service*, September 1, 2010.

rising demand and low tariffs.[310] Second, 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.[311] Indeed, one of the Chávez administration's vulnerabilities has been its failure to address the country's housing deficit. The country's housing shortage has increased every year since Chávez assumed office in 1999, and the Venezuelan Construction Chamber estimates at least 200,000 houses per year need to be built to begin to solve the problem.[312]

CDB's loan to the Ecuadorean government is part of broader trend of Chinese firms helping President Rafael Correa cope with fiscal hardships largely of his own making. First, in December 2008, Correa willingly defaulted on global bonds worth $3.2 billion, which has severely curtailed Ecuador's access to external financing.[313] Second, Correa's efforts to increase state control over the oil industry since he took office in 2007 have discouraged investment from foreign oil companies, which has contributed to a decline in Ecuador's oil output from a high of 545,000 b/d in 2006 to 495,000 b/d in 2009.[314]

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[310] For more information on Venezuela's electricity crisis and its negative impact on Chávez's popularity, see "Chávez declares 'electricity emergency' in Venezuela," *Reuters*, February 8, 2010; "Venezuela economy: Short on energy," *Economist Intelligence Unit*, November 19, 2009; and Benedict Mahler, "Chávez fails to deliver power to the people," *Financial Times*, October 31, 2009.

[311] Diego Moya Ocampos, "Venezuela to Build 25,000 Houses with Chinese Funds," *IHS Global Insight*, September 30, 2010; and Fabiola Sanchez, "Chávez's support eroding in slum strongholds as hard times return and an election looms," *Associated Press*, September 6, 2010.

[312] Ocampos, "Venezuela to Build 25,000 Houses;" and "The revolution checked; Venezuela's legislative election," *The Economist*, October 2, 2010.

[313] "Ecuador: Short of investment finance," *Business Latin America Select*, May 3, 2010; and Anthony Faiola, "Calling Foreign Debt 'Immoral': Leader Allows Ecuador to Default," *Washington Post*, December 13, 2008, http://www.washingtonpost.com/wp-dyn/content/article/2008/12/12/AR2008121204105.html.

[314] "Cash Crunch Forces Ecuador to Get Creative," *EI Finance*, February 17, 2009; and *BP Statistical Review of World Energy*, June 2010, p. 8.

The lower production volumes and the lower oil price environment have resulted in lower oil revenues, which historically have provided at least thirty percent of government income.[315] Together, the isolation from international capital markets and the decline in oil revenue have made it difficult for Correa to continue the robust social spending necessary to maintain his popularity. Indeed, Ecuador's Minister of Finance, Patricio Rivera put Ecuador's budget deficit at more than $4 billion when Ecuador signed the loan agreement with CDB.[316]

Over the past two years, Correa has repeatedly turned to China for funds to cover Ecuador's budget deficit and to finance badly needed infrastructure, including a hydroelectric plant needed to ease electric power shortages. Although Ecuador has pursued other non-traditional sources of financing, including Iran, Russia and Venezuela, none has delivered as much as China. In 2009, PetroChina provided PetroEcuador with $1 billion in exchange for crude oil deliveries of 96,000 b/d for two years. In 2010, China Eximbank agreed to lend Quito $1.68 billion for the construction of the Coca Codo Sinclair hydroelectric project and CDB extended a $1 billion line of credit to the Ministry of Finance.

Quito's acceptance of the terms imposed by PetroChina, China Eximbank and CDB, which many Ecuadoreans consider to be stringent, indicate that China may have become Ecuador's lender of last resort. For example, PetroChina took advantage of Quito's cash crunch to negotiate a 25-28 percent discount on the market price of oil over the duration of the contract, equivalent to a 7.25 percent interest rate on the loan.[317] Similarly, China Eximbank's loan has a higher interest rate (6.9 percent) and a shorter term (fifteen years, with a grace period of five and one half years) than those extended by multilateral

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[315] Fargo, "Ecuador: Turning to China."
[316] Jason Fargo, "New Chinese Loan Helps Beijing Extend Influence in Ecuador," *International Oil Daily*, September 2, 2010.
[317] Fargo, "Ecuador: Turning to China."

institutions.[318] The Ecuadorean government also suspended negotiations with CDB for several months in 2009 because of CDB's conditions, including the requirement that the funds be placed in a third party account before disbursement to Ecuador, probably to protect CDB's interest as a secured lender by limiting the exposure to Ecuadorean political risk.[319] Although Minister of Economic Policy Diego Borja declared that "Ecuador won't accept the impositions from China nor from the International Monetary Fund, nor from anyone," Quito did agree to terms that have proven controversial in Ecuador.[320] For example, CDB insisted, quite reasonably given the risks involved in lending to Quito, on binding third-party arbitration of any disputes in London, which some critics complain violates Ecuador's sovereignty.[321]

CDB's loans may give China's NOCs a competitive advantage over international oil companies.

The international expansion of China's NOCs has raised concerns that China's oil majors have important advantages over international oil companies (IOCs) in the global competition for exploration and production assets. Chief among these advantages is the provision of direct and indirect financial support by Chinese state-owned entities. The most high-profile example of direct financial support is the loan package CNOOC assembled to finance its $18.4 billion bid for Unocal in 2005. The fact that the terms of at least some of these loans were not available to any western publicly traded company prompted Peter Robertson, the vice-chairman of

[318] "Ecuador: China funds hydro expansion, but worries remain," *Business Latin America Select*, July 5, 2010.

[319] "Ecuador: Borja outlines economic policies, opinions and forecasts," translation of article from *El Comercio*, provided by Esmerk, September 2, 2009.

[320] Mercedes Alvaro, "Update: Ecuador: Talks With China on $1.0 Bln Loan Suspended," *Dow Jones News Service*, November 12, 2009.

[321] Redacción Negocios, "El Gobierno defiende cláusula de arbitraje de crédito con China" ("The government defends credit arbitration clause with China"), *El Comercio*, October 6, 2010, http://www4.elcomercio.com/Generales/Solo-Texto.aspx?gn3articleID=273332.

Chevron at the time, whose offer of $16.4 billion had already been accepted by Unocal at the time of CNOOC's bid, to cry foul: "We're not competing with this company; we're competing with the Chinese government—I think it's wrong."[322] The most high profile examples of indirect financial support are the multibillion dollar loans that the China Eximbank extended to the government of Angola in the mid-2000s, which helped Sinopec establish a presence in the Angolan upstream. It seems unlikely that Sonangol, the Angolan NOC, would have rejected the deal struck between Shell and India's Oil and Natural Gas Corporation Ltd. (ONGC) for the latter to purchase Shell's 50 percent stake in Block 18 (Greater Plutonio fields) and instead sell it to Sinopec, had China Eximbank not extended a $2 billion low-interest loan to Angola in 2004 to finance infrastructure projects involving Chinese companies.[323]

CDB's emergence as an increasingly central player in China's cross-border energy deals raises the question of whether its loans will give China's NOCs a leg up on the competition in the international upstream market. After all, CDB has a mandate to help Chinese firms expand abroad. Moreover, some NOCs, which control more than three quarters of the world's oil reserves, may prefer to negotiate with "China, Inc." instead of multiple international oil companies and banks. As José Sergei Gabrielli noted after Petrobras concluded its negotiations with CDB, "The US has a problem. There isn't someone in the US government that we can sit down with and have the

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[322] James Politi, "CNOOC funding for Unocal scrutinized," *Financial Times*, June 29, 2005.

[323] For discussions of the link between Chinese aid to Angola and Sinopec's acquisition of Shell's 50 percent stake in block 18, see Xu Fei 许飞 "石油搭桥，中国企业的安哥拉舞步" ("Building a bridge to oil, the Angolan dance of Chinese companies"), 南风窗 *(Nanfengchuang Magazine),* and No. 22 (2006); Margaret McQuaile, "Africa is staging ground for push by China, India to control more output," *Platts Oilgram News*, October 26, 2004. For more on China's financial relationship with Angola, see Indira Campos and Alex Vines, "Angola and China: A Pragmatic Partnership," Center for Strategic and International Studies, June 4, 2008, http://csis.org/files/media/csis/pubs/080306_angolachina.pdf, pp. 3-7.

kinds of discussions we're having with the Chinese."[324] Similarly, Richard Morningstar, the U.S. Special Envoy for Eurasian Energy, told the Senate Foreign Relations Committee that CDB's loan to Turkmengaz made it difficult for American companies to compete with China's NOCs in Turkmenistan: "It's easy for Turkmenistan to make a deal with China, when China comes in and says, 'hey, we're going to write a check for X amount of money, we're going to build a pipeline. That's not a hard deal to accept, and we (the United States) can't compete in that way."[325]

CDB's EBLs indicate that its efforts to leverage its financial assets to help China's NOCs secure exploration and production assets abroad have yielded mixed results. The bank's loan to Turkmenistan secured the biggest prize in terms of upstream assets—a role for CNPC in the development of the South Yolotan natural gas field. The biggest disappointment was probably the bank's deal with the Russian companies which did not include any upstream assets for China's NOCs despite the Chinese negotiators' request that access to the Russian upstream for China's NOCs be part of the deal.[326] The loan to Petrobras yielded a memorandum of understanding between Petrobras and Sinopec to look for opportunities to cooperate in exploration and production, but the two blocks Sinopec may acquire as a result are not located in the pre-salt deposits. CDB's loans undoubtedly increased the already considerable enthusiasm of Hugo Chávez for Chinese investment in the Venezuelan upstream. The fact that negotiations over the $20.6 billion dual loan facility coincided with negotiations between CNPC and PDVSA to finalize an agreement for the joint development of

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[324] John Lyons, "Brazil Turns to China to Help Finance Oil Projects," *Wall Street Journal*, May 18, 2009, p. A6.

[325] "China ups energy clout in Central Asia – US envoy," *Reuters*, July 17, 2009. http://in.reuters.com/article/2009/07/16/energy-usa-china-idINN1642081320090716.

[326] Wang Xiaoming 王晓明, "中俄新一轮谈判再启动 贷款换石油进入收官阶段" ("China and Russia Restart a New Round of Negotiations; the loans for oil talks enter the closing stage"), 21世纪经济导报 (*21st Century Business Herald*), November 25, 2008. http://www1.21cbh.com/HTML/2008-11-25/HTML_BWO2LR0ML0WD.html.

Junin-4 block in the Orinoco Belt indicates that there may be a link between the loans and the upstream investment.

The upstream asset associated with a loan from CDB most attractive to the IOCs is probably Turkmenistan's South Yolotan natural gas field, which ranks among the five largest in the world. CNPC did not directly compete against the IOCs for its role in the development of South Yolotan because the Turkmens did not hold an auction. However, the decision of Ashgabat to award a development phase to CNPC after CDB agreed to loan $4 billion to Turkmengaz is an example of how financial support from Chinese state-owned entities can give China's NOCs an advantage over the IOCs in the competition for exploration and production projects.

CDB's loans to energy companies and governments are worth watching because China's NOCs are likely to increasingly compete head-to-head with the IOCs for upstream assets. The struggle between CNOOC and Exxon Mobil in 2009 and 2010 to acquire the Ghanaian assets of Kosmos Energy, including a 23.49 percent stake in the Jubilee oil field, is a case in point. Neither company prevailed because Kosmos Energy ultimately decided not to sell.[327] CDB's extension of a $3 billion line of credit to the government of Ghana, however, was undoubtedly aimed in part at giving CNOOC a competitive advantage by winning the support of Accra.[328]

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[327] For more information on Exxon Mobil and CNOOC's interest in Kosmos Energy's stake, see "CNOOC, GNPC 'Bid' Raises Doubts," *International Oil Daily*, October 25, 2010; Tom Grieder and Marné Beukes, "CNOOC Reportedly Makes US$5-Bil. Bid with GNPC for Jubilee Stake," *IHS Global Insight Daily Analysis*, October 22, 2010; "The Politics of No," *All Africa*, September 8, 2010; and Jeffrey McCracken, Russell Gold and Will Connors, "CNOOC, Exxon Vying for Stake in Ghana Field," *Wall Street Journal*, October 13, 2009.

[328] For more information on CDB's loan to Accra, see "Statement by the Honourable Hanna S. Tetteh, Minister for Trade & Industry, on Behalf of Government at a Press Conference on the outcome of the Official Visit of President J.E.A. Mills to China," October 26, 2010, http://www.ghana.gov.gh/index.php?option=com_content&view=article&id=3720:statement-read-by-the-honourable-hanna-s-tetteh-minister-for-trade-a-industry-on-behalf-of-government-at-a-press-conference-on-the-outcome-of-the-official-visit-of-president-j-e-a-mills-to-china&catid=58:press-releases&Itemid=207.

Conclusion

CDB's EBLs highlight its emergence as an increasingly central actor in China's cross-border energy deals. Since the mid-2000s, the bank has sought to leverage its financial resources to secure the energy China needs to fuel its continued economic rise. The global financial crisis provided CDB with an opportunity to substantially expand its portfolio of cross-border energy deals. Not only had China's top leaders apparently decided that Chinese financial institutions should abandon investing in western financial institutions in favor of natural resources, but the crunch and the collapse in the price of oil left many oil and natural gas producers desperate for capital. Moreover, China emerged from the financial crisis relatively unscathed in comparison to the dominant outside powers in the two regions of the world that received EBLs from CDB—Russia in Central Asia and the United States in Latin America. A perception that China's relative strength vis-à-vis Russia and the United States may have emboldened CDB, China's NOCs, and the Chinese government to broker deals that will almost certainly enhance China's economic and political clout in countries where Russia and the United States have warily watched China's expansion and where Beijing has sought to reassure Moscow and Washington that its growing presence is not a threat to their interests.

The EBLs were the outcome of coordination between CDB, the NOCs and the Chinese government with CDB functioning as the main point of coordination. The bank's loans provided a link between the policy priorities of the State Council and the commercial activities of China's oil majors. Indeed, CDB itself embodies the intertwining of government and commercial objectives in its efforts to profitably support China's national interests.

One reason CDB was able to successfully and quickly coordinate the EBLs is because these transactions served the strategic priorities of each of the key participants. For CDB, the deals not only helped to fulfill its overlapping mandates to support the "going out" strategy and to ease China's energy bottlenecks but also furthered its interest in making money, growing its international business, and demonstrating its continued relevance as a policy bank. For the State Council, the loans aligned with its objectives of enhancing China's oil supply security and diversifying China's foreign exchange reserves. For the NOCs, CDB's lines of credit bolstered their efforts to build their international upstream portfolios. In short, the EBLs provided a vehicle for CDB, the NOCs and the State Council to jointly take advantage of the global financial crisis to pursue their respective interests.

The EBLs also demonstrate that well-coordinated cross-border deals, even ones that are considered "national projects" (*guojia xiangmu*), do not always originate from the top down. CDB's loan to Petrobras is a case in point. This transaction grew out of CDB's efforts to develop business opportunities in Brazil. Indeed, CDB's bureaucratic reorganization in the mid-2000s for international expansion facilitated CDB's rise as a driver of China's "going out" strategy. The fact that each of the bank's domestic branch offices are responsible for different parts of the world and that CDB has dispatched work teams to more than 140 countries indicates that at least some of the bank's overseas projects are driven from the bottom up.

CDB's emergence as a key financier of China's "going out" strategy makes it part of the proliferation of actors on the margins of the official Chinese foreign policy establishment that are influencing China's diplomacy.[328] Although CDB has a mission to bolster China's foreign policy, the growth in the bank's overseas lending indicates that CDB's cross-border deals may not only serve but also shape China's diplomacy. One foreign policy challenge that CDB's deals may create for Beijing is dealing with borrowers who default on their loans. For example, both the governments of Ecuador and Venezuela are very risky borrowers. Ecuador defaulted on foreign debt in 1999 and 2008, while Venezuela is considered by some analysts to be the most risky sovereign borrower in the world.[329] Although CDB hired top tier international law firms to structure the deals to provide additional assurances that their loans will be repaid, these assurances may not be enough.[330] If either Quito or Venezuela defaults, working out a resolution will ultimately become a political problem for Beijing.

In addition, the EBLs illustrate that cross-border deals influenced by the political priorities of the Chinese government impact American interests in a variety of ways. The positive and negative implications of CDB's loans to Brazil, Ecuador, Russia, Turkmenistan and Venezuela for the United States underscores the importance of recognizing that deals motivated in part by Beijing's foreign policy objectives are not categorically harmful—or helpful—to the United States. As CDB continues to build its international portfolio, it is likely to increase its global influence, and that of the Chinese government, especially in countries like Venezuela where CDB is the largest, or one of the largest, sources of external finance. Whether and to what extent CDB's and Beijing's use of this influence aligns with or runs counter to American interests is something Washington should track carefully.[331]

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[328] Linda Jakobson and Dean Knox, "New Foreign Policy Actors in China," Stockholm International Peace Research Institute Policy Paper No. 26 (September 2010), pp. 24-46. http://books.sipri.org/files/PP/SIPRIPP26.pdf.

[329] Anousha Sakoui, "Venezuela head debt default risk list," *Financial Times*, April 8, 2010; Faiola, "Calling Foreign Debt 'Immoral'" and Ana Maria Echeverria, "Ecuador defaults on debt as creditors demand payment," *Agence France Presse*, October 1, 1999.

[330] Clifford Chance advised China Development Bank on its loans to Rosneft, Transneft, Petrobras and Turkmenistan. White & Case advised China Development Bank on its two loans valued at $20.6 billion to Venezuela's Bank of Economic and Social Development.

[331] I thank Kevin Gallagher for this point.

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