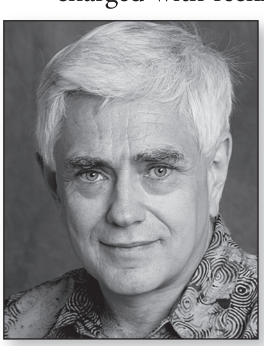
# Blank Checks for Unsustainable Development

*China will soon be by far the biggest international public financial player in poorer countries, dwarfing the largest development agencies such as the World Bank. Unfortunately, the economic giant is also exporting lowered environmental and human rights standards*

Bruce Rich

Last fall, both the president of the World Bank and the head of the European Investment Bank (the European Union's development finance agency) did something quite unprecedented in the history of their institutions. They undiplomatically and publicly lambasted a major world economic power, China, criticizing its banks for not adhering to environmental and social standards in massive lending to Sub-Saharan Africa and other developing regions. In one of recent history's greatest ironies, China's ruling communist politburo stands accused of no-holds-barred international finance capitalism, charged with reckless disregard of ethical concerns for the sake of profit and control of natural resources.



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Indeed, in a matter of just three or four years China has emerged as a financial giant on the international scene. In 2004, Chinese President Hu visited five Latin American countries and signed $100 billion worth of investment commitments in 10 days. Most of these loans and other investments are in oil and gas development, pipelines and other infrastructure, and mining in nations plagued by instability such as Bolivia, Ecuador, and Venezuela. Chinese investments in Sub-Saharan Africa have grown explosively, too, and China recently surpassed Britain to become Africa's third-biggest trading partner, behind the United States and France, and aims to increase annual trade with the continent to $100 billion in 2010.

The U.S. Export-Import Bank reported to Congress in 2006 that, by 2010, China's Export-Import Bank and Sinosure (the state overseas investment insurance agency) will be lending and guaranteeing more than $70 billion annually for large scale investments in developing countries and economies in transition. China will be by far the biggest international public financial player in developing countries, dwarfing the largest development agencies, such as the World Bank, with lending of $25 billion a year, and the largest competing export-import banks, those of the United States and Japan, which consistently lend between $12 and $18 billion annually.

Moreover, western donor countries and international financial institutions such as the World Bank allege that China's accelerated lending is occurring at the very moment when governments and development agencies have forgiven large amounts of developing country debt. China's aggressive promotion of loans threatens to undermine a decade of carefully negotiated debt relief. Experience shows there is an environmental consequence to unsustainable debt, since it increases pressures on economies heavily dependent on commodity exports to scale up production of oil, minerals, timber, or agricultural crops to earn revenue for burgeoning loan repayments.

China's precipitous financial rise is a huge opportunity and challenge for the rest of the world. More investment in poorer countries is certainly needed, especially in Sub-Saharan Africa. Chinese support for energy and water infrastructure and agriculture and its growing trade with Africa are already providing a boost to growth in the region. The revenue from its massive commodity investments, if well-managed, could be a critical source of finance for health, education, and other critical social investments. But the sad record of failure of western foreign assistance in Africa over the past four decades — over a half trillion dollars of aid with little lasting results — shows that without conditions to address governance and corruption, aid is wasted. Investments in oil and mining in Africa not only have left environmental ruin in their wake, they have spurred massive corruption and politically destabilized whole regions, sometimes even catalyzing civil wars. If Chinese financial institutions ignore the international standards of environmental and social good governance so painfully achieved over many years, they will lead a classic race to the bottom, undermining the policies of banks and institutions with stronger standards.

*Projects the multilateral development banks won't touch are being financed by Chinese banks.*

## The Emerging Common Environmental Framework

The World Bank began to improve its policies on environmental and social impacts to guide its investments in the 1980s. Other multilateral development banks, or MDBs, such as the Inter-American Development Bank ($7.1 billion in new lending in 2005) and the Asian Development Bank ($7.4 billion in 2005), adopted similar policies in the late 1980s through 1990s. These policies address critical development issues such as environmental assessment, conservation of critical habitats, rehabilitation of communities displaced by big infrastructure, and protection of indigenous peoples.

Research and advocacy of NGOs around the world played an important role in creating public awareness and political pressure that catalyzed the evolution of these policies. NGOs realized that "following the money" is a very effective, leveraged strategy for promoting greater attention to environmental and social concerns. In the late 1990s the World Bank extended its "environmental and social safeguard" policies to cover finance of private sector investment, conducted principally by a special affiliate, the International Finance Corporation. IFC's policy role since the late 1990s has become very influential, much greater than the simple volume of its lending ($6.7 billion in 2006), since it elaborated the first comprehensive international environmental and social lending guidelines for the private sector.

In the mid-1990s it became clear that projects the World Bank and other MDBs were refusing to finance because of major environmental and social risks were being boosted by the government-supported export credit agencies of industrialized nations. ECAs provide subsidized loans and loan guarantees to buyers, mainly in developing countries, with the goal of promoting the exports and investments of industrialized country corporations.

A growing international NGO campaign has emerged calling upon ECAs to adopt common environmental and social guidelines (see *eca-watch.org*). Former President Clinton raised the issue at several G8 economic summits in the late 1990s, leading in 2003 to an international agreement for environmental standards for ECAs in the countries of the Organization for Economic Cooperation and Development, a negotiating forum for the industrialized nations. The agreement, which is being revised and strengthened this year, uses World Bank/IFC environmental and social safeguards as benchmarks.

*China's financial rise is occuring outside the system of international environmental good practice.*

That same year, 10 of the world's biggest commercial banks, under growing public scrutiny for the environmental and social impacts of their lending practices, committed to the Equator Principles (see *equator-principles.com*), a voluntary set of environmental guidelines for financing large projects that also uses the World Bank/IFC's environmental and social safeguard policies as benchmarks. Now 46 of the largest banks on earth, accounting for more than 90 percent of global private-sector project finance, have commited to revised, even stronger Equator Principles.

China's financial rise is occurring outside this system of international environmental good practice for major project finance, undercutting more than two decades of progress in sustainable project financing. As we shall see from some recent examples, the stakes for the environment, and for the social stability of large parts of the world, are high, and getting riskier.

## Bearing Bushels of Money, With No Strings Attached

Sudan provides an illustrative case study. Beijing's investment in Sudan's oil production, of which over half is exported to China, has received wide international attention; the oil revenues have fueled a raging civil conflict in the southern oil-producing regions, with widely documented genocidal atrocities in Darfur. The Chinese have invested over $20 billion in Sudan in recent years — via development aid, export credits, and low-interest loans — in infrastructure, dams, power stations, and agriculture as well as oil production.

*Beijing's investment in Sudan's oil production, half exported to China, has spurred a raging civil conflict and genocide in Darfur.*

One of China's more prominent investments is the Merowe Dam on the Nile, in southern Sudan. The dam was constructed by a consortium of Chinese companies, with about $387 million in loans from the China Ex-Im bank. The $1.2-billion hydropower project will create a 200-kilometer-long reservoir, forcibly resettling some 50,000 poor farmers. The resettlement has been marked by increasingly violent protests, since the farmers are being displaced from fertile lands along the Nile to a virtual wasteland in the Nubian desert. In April 2006 Sudanese security forces shot three people to death and injured 47 others in a village protesting the project, and in August hundreds of desperate villagers literally fled for their lives, abandoning their communities as rising waters inundated their homes after Sudanese authorities closed the gates of the dam with no notice.

That same year, an independent review of the project by the Swiss Federal Institute of Aquatic Science and Technology identified flagrant violations of good practice in the dam's environmental assessment, which neglects to address critical issues of sedimentation of the dam reservoir, spread of waterborne diseases, collapse of fish spawning and fisheries in the Nile, as well as significant contributions to global warming through methane emissions associated with large amounts of decaying organic matter in the reservoir. Many of these problems could have been addressed by rigorous implementation of the policies of the Equator Principles or the the World Bank's safeguard guidelines, but an independent site visit in 2005 by British and American NGOs found that the project violated the bank's criteria for environmental assessment on 38 different counts, and on involuntary resettlement on 12 counts (SEE *irn.org/programs/merowe).*

As international concern over tropical deforestation has grown over the past decade and a half, NGOs, consumer movements, aid agencies, and governments have tried to promote a global framework for certifying trade in tropical timber. In many countries, increasing numbers of corporations, cities, provinces or states, and branches of national governments have committed to purchase only timber labeled as sustainably harvested by international certifying organizations such as the Forest Stewardship Council (SEE *fsc.org*). Over the same period China has become the world's largest timber importer, and the largest single importer from a growing number of poor nations, for example, Gabon (an estimated 46 percent of Gabon's timber exports) and Equatorial Guinea (60 percent). In Gabon an estimated 70 percent of the logs are being exported to China in violation of Gabonese law and the most rudimentary sustainability standards. In Equatorial Guinea the World Wildlife Fund estimates that 90 percent of the wood exports to Chinese trading partners are illegal. In southeastern Nigeria, NGOs have accused Chinese-owned pulp mills of dumping toxic effluents into the Cross River, poisoning local communities and destroying fisheries. In the early 2000s, China was the major importer of timber from Liberia. The revenues — accounting in 2001 for nearly 60 percent of the country's *total* export income — went directly to the country's murderous dictator, Charles Taylor, to fuel a devastating civil war, leaving a totally failed state and economy. Belatedly, only a 2003 UN Security Council embargo on Liberian timber halted this scandalous trade. China did support and fully comply with the embargo.

*As the world's largest timber importer, China's dealmaking is undermining standards in forestry.*

In Mozambique there is a similar pattern where Chinese investments in oil, large dams, and timber are characterized by negligence of environmental and social impacts, lack of transparency, and obliviousness to human rights. As with many risky investments in poor countries with poor governance, these issues are linked. Mozambiquen researchers Anabela Lemas and Daniel Ribeiro, associated with the Maputo-based NGO Justicia Ambiental (Environmental Justice; SEE *pambazuka.org/issue/282*), have documented how Chinese timber traders are colluding with corrupt local interests and officials to illegally pillage the country's forests: "Rather than combating illegal logging, China, through measures including the manipulation of forest regulations, false technical information and statistics, bribes, and indirect involvement in logging, is actually facilitating illegal logging and hindering sustainable development in the sector."

Justicia Ambiental and international NGOs are also concerned over China Ex-Im's 2006 public statement of intent to support the $2.3-billion Mphanda Nkuwa Dam on the Zambezi River. The structure will displace 1,400 poor farmers and undermine years of internationally financed restoration work in the Zambezi River Delta, which is an internationally protected wetland and wildlife refuge under the RAMSAR Convention. The dam is situated near an active seismic fault zone, where a 7.5-magnitude earthquake took place just last year. In contravention of international good practice and Mozambiquen law, the most basic information on the project has been withheld from the public and affected populations (SEE *irn.org/programs/mphanda)*.

In Latin America there is a similar pattern. Chinese oil companies are involved in large-scale joint investments for oil development and pipelines with the national oil companies of Bolivia, Brazil, Cuba, and Venuzuela and have bought substantial shares of major regional oil companies and pipelines in Ecuador and Peru.

In Ecuador, the Chinese financial and environmental footprint has gone from negligible to major in just three or four years. In 2006 Andes Petroleum (a consortium owned by the Chinese oil companies CNPC and Sinopec) purchased four major oil concessions and a 36-percent leading share in the environmentally controversial Heavy Crude Pipeline, which links new oil development in the Ecuadorian Amazon to the Pacific Coast for export. All four of the concessions are located in extremely sensitive, supposedly protected, environments. Two are located substantially within the renowned Yasuni National Park, one includes a section of the Cuyabeno Wildlife Reserve, currently a prime ecotourism destination, and one is located within core territory for uncontacted, highly vulnerable indigenous peoples, the Tagaeri-Taromenane.

Yasuni Park, which conserves nearly 1 million hectares of a large contiguous tract in the Amazonian rainforest, has been identified by scientists as one of the most biodiverse protected areas on earth; it is also a UNESCO Man and the Biosphere reserve. In 2006 Andes Petroleum conducted intensive seismic prospecting within Yasuni, and is preparing to drill two new exploratory wells within the park. Late last year, the Ecuadorian press reported on several occasions that Andes Petroleum was pressuring the Ecuadorian government to exclude an oil reserve, located within one of its four concessions, from a proposed protected "Intangible Zone" to be created by the state to protect the Tagaeri-Taromenane. In this case, these efforts were unsuccessful, and the Intangible Zone was signed into law in January.

## The Way Forward

Much of the concern over the environmental and social impacts of China's growing financial clout in the developing world is linked to the astounding rapidity of its rise. Criticisms by western development institutions, let alone banks and companies, ring at times hypocritical since their protests over China's unethical lending appear to be spurred as much by the prospect of losing business as by concern for the environment or human rights. According to the *London Times,* at the World Economic Forum in Davos, Switzerland, in January, the heads of over a dozen of the world's leading mining companies met for six hours to formulate a strategy to head off Chinese competition for mineral resources in Africa. One idea, characterized by the *Times* "as perhaps the most fanciful," was to appeal to the United Nations to promote an agreement among members that they would only enter into mining agreements with high environmental and worker safety standards, which, in response to international pressure, major western companies have adopted in recent years.

*Within China, the government is strengthening domestic environmental laws and broadening public involvement.*

Within China, the government is strengthening domestic environmental laws and broadening public involvement. The new environmental assessment law, which went into force in 2003, provides measures for sharing environmental impact information with the public, consultation, and serious consideration by authorities of public comments (SEE RELATED ARTICLE, PAGE 35). The next step is to build on this growing environmental awareness at home into the practices of China's banks and companies abroad.

Indeed, some 50 representatives of Chinese NGOs met in Beijing in November to examine together for the first time the impact of Chinese finance abroad, as well as impact of foreign financial institutions, public and private, within the country. Chinese groups said that international environmental standards such as the Equator Principles were relevant both outside China, with respect to the impact of Chinese financial institutions abroad, and inside China, since the World Bank and Asian Development Bank as well as private Equator Principle foreign banks are all financing projects within China and increasingly working together with domestic financial institutions.

*50 Chinese NGOs met to examine the impact of Chinese finance abroad and of foreign financial institutions domestically.*

The IFC is actively engaged in promoting the Equator Principles with Chinese banks. Leading Equator banks like Citigroup and HSBC have been conducting training sessions in the principles with their Chinese bank colleagues as well as with state institutions like China Ex-Im. The OECD has also been in touch with Chinese authorities concerning international standards and China Ex-Im, and representatives of China Ex-Im have participated for the first time as observers in meetings of the OECD Export Credit Group in discussions about common environmental standards. China Ex-Im has instituted environmental procedures, but they cannot be evaluated since the bank refuses to publicly disclose them, lagging behind the increased transparency provisions in China's domestic environmental assessment law.

Unfortunately, for now official policy remains adamant. During President Hu's trip to Africa in February — the third in three years — high-ranking foreign and commerce ministry officials reiterated that China's aid and loans will continue to come with no strings attached, and no "political" interference — code for ignoring even the most flagrant environmental, social, and human rights abuses

Beijing's insouciance may not be politically sustainable. Already there have been incidents of an anti-Chinese backlash in Africa, linked to the perceived environmental and social indifference of Chinese-backed enterprises. Last April, one of the growing guerilla movements in the pollution and conflict ravaged Niger Delta, the Movement for the Emancipation of the Niger Delta, launched a car bomb attack near a partly Chinese-owned oil refinery, declaring publicly, "We wish to warn the Chinese government and its oil companies to steer well clear of the Niger Delta. The Chinese government by investing in stolen crude places its citizens in the line of fire." A massive industrial accident at a Chinese copper mine in Zambia in 2005 resulted in the death of 46 workers, spurring violent protests against alleged safety negligence. The following year Zambia's presidential elections included a candidate, Michael Sata, who ran unsuccessfully on an anti-Chinese investment platform, gathering strong support among communities affected by the Chinese copper mine and other projects. And China's President Hu was obliged to cancel a visit to Zambia's copper belt in his recent Africa trip because of growing local resentment over China's alleged disregard for environmental and worker safety concerns.

*Hopefully, as financial institutions worldwide see their longterm interest in sustainability, China's will too.*

In the final analysis the framework of international environmental standards for public and private finance is gathering strength because financial institutions increasingly recognize it is in their long-term interest to anticipate and mitigate environmental and social impacts, which increasingly can translate into political and project risk. They also recognize it is in everyone's interest to establish a level, transparent financial playing field.

Over the past two decades global networks of NGOs uniting concerns of affected populations in developing countries with civil society groups and consumer movements in the rich nations played a critical role in convincing international lenders they could no longer ignore the environmental and social risks associated with their activities. China's growing movement of NGOs may appear relatively small and undeveloped in the face of the country's titanic internal environmental challenges, not to speak of being simply overwhelmed by the prospect of addressing global environmental issues posed by China's development finance. But recent history demonstrates that it would be a mistake to underestimate the capacity of Chinese society and its leadership to rapidly evolve and surprise the world. •