

Donors' contribution to China's development - strategies, policies and practises

Introduction

It is my honour and my pleasure to contribute to this event, which marks a further step towards deepening cooperation and mutual understanding between China and the OECD/DAC. China started receiving official development assistance (ODA) as part of its reform and open door policy. Contributions began in 1979 with the partnership between the World Food Programme (WFP) and the People's Republic of China, as a means of providing relief through food assistance, and the allocation by UNDP of 15 million US\$ (Cicete s.a.). This was the beginning of the now thirty-year history of development cooperation between foreign donors and China.

In my presentation, I will concentrate on four popular narratives on donors' contribution to China, narratives regarding development, growth, poverty reduction and development partnership which I offer here as starting points for the subsequent discussion. Before presenting and analyzing these four narratives from the perspective of development cooperation in China as a mutual learning process, let me first share with you some insights into the volume and distribution of foreign aid in China.

Volume and distribution of foreign aid in China

According to OECD statistics, the total sum of ODA net disbursements (grants plus loans minus loan repayments) to China during the period 1979-2007 was 48.92757 billion US\$. Out of this total sum of ODA disbursements, 20.46696 billion US\$ was in grant form and 28.46066 billion US\$ in (net) loans. (Please refer to slide 1 on *Official Development Assistance to China 1979-2007*) The first half of the 1990s saw a steady rise in ODA; during the second half of the 1990s ODA contributions to China fell and rose again during the first years of the 21st century.

The OECD/DAC statistics suggest a higher proportion of bilateral than multilateral ODA (please refer to slide 2 *ODA by bilateral and multilateral donors*), but one has to keep in mind that e.g. the considerable contribution of lending by the Asian Development Bank is regarded as Other Official Flows (OOF) and not as ODA, because ADB does provide non-concessional loans to China.

By far the largest bilateral donor to China has been Japan, and it was also one of the first bilateral donors to China. (Please refer to slide 3 *Bilateral government loans and grants to China*) With Japanese loans, China has been able to complete a large number of urgently needed national infrastructure projects (Lu 2000:55/56).

Other donors providing less than 2 per cent of lending were Australia, Sweden, Finland, Belgium, Denmark, Norway, Switzerland, Korea, Israel, Saudi Arabia, Russia, Poland and Luxembourg (NDRC 2009: 029-043).

If we look at the sectors (please refer to slide 4 *Sectoral distribution of loans and grants*) benefiting from foreign lending, we find that more than half of all bilateral and multilateral loans between 1979 and 2005 went into the transport and energy sector; indeed, for the ADB

and Japan, over two thirds of lending was directed into these sectors (NDRC 2009: 003,024,029).

Grant funding, which according to MOFCOM amounted to no more than 6.6 billion US\$ over the last thirty years, mainly went into the following sectors:

- Education 23%
- Environmental and Ecological Protection 22%
- Rural development and Poverty Alleviation 16%
- Health 14%
- Child Protection and Population Development 11%
- Public Policy and Institutional Reform 11%
- Others 3% (MOFCOM 2009:8)

During the reform period three main trends can be discerned in foreign aid to China:

1. Sector distribution: from “hardware” to “software”

Whereas at the beginning of China’s reform period, preferential loans dominated foreign aid and were used mainly in the fields of transport and communication, since the 1990s more investment has gone into environmental protection and other sectors that could be termed “soft” (NDRC 2009: 003). I will come back to this in a minute.

2. Forms of aid: Decrease in soft loans

Even if the OECD statistics suggest a decrease in loans, I would hesitate to formulate a general tendency such as “from loans to grants”, because one has to bear in mind that market-based loans from multilateral and bilateral development banks still play an important role in providing development assistance to China. But if these financial institutions are not providing preferential loans, why are Chinese clients still borrowing from them? The answer is that the “added value” to be gained by borrowing from foreign donors is seen as the knowledge transfer that comes along with these loans. This may help in the identification, formulation, and implementation of projects, improve the institutional capabilities of executing agencies or promote the transfer of technology.

3. Regional distribution: from east to west

With regard to ODA loans, it was not only China that considered the east coast to be the priority area; the donors (particularly Japan) also tended to choose such areas offering a favourable environment. With a growing gap in regional economic development, China started a development strategy of “opening up the west” (xibu da kaifa) at the end of the 1990s and encouraged the donor community to shift its focus to central and western China. (Lu 2000:55/56). In the period 2001-2005, more than 80% of foreign aid (including loans, grants and TA) was invested in central and western China (NDRC 2009:004; MOFCOM 2009:8).

Looking at all these trends, we can already see that the donors’ contribution fitted in well with the changing priorities of China’s own development agenda. This becomes even clearer when discussing the first popular narrative on foreign donors in China:

Development narrative

When China’s economic reform was initiated in 1979, its leader did not have a comprehensive blueprint for development. The intention was simply to adjust the economic structure and

improve the incentive mechanism (Lin et al 2003:308). The authorities realized that the best path to reform starts with pragmatism, with unleashing people's initiative and learning from experience (Wang 2005:58). The idea of gradualism as a distinct development strategy was yet to be born.

At the beginning of the reform policies, Deng Xiaoping argued that China's overall objective of becoming a wealthy nation should be achieved in three steps:

- As a first step, per capita GDP should reach a level of 500 US\$ during the 1980s. In this way, it should be ensured that the population had basic supplies of food and clothing .
- The objective of the second step was to double per capita GDP to 1,000 US\$ by the end of the 20th century. In this way, China should become a moderately well-off society .
- As the third step, per capita GDP should be quadrupled during the first thirty to fifty years of the 21st century to reach 4,000 US\$. By this time, a society with a middle-range development level should be reached (Deng 1994: 226).

In accordance with this three-step scheme of development, the reform process can be divided into three basic periods, namely the 1980s, the 1990s and the first decade of the 21st century. Donors contributed to each of these development periods in specific ways.

- The *first period* was a phase of **economic liberalization** (1980s) with the introduction of the Household Responsibility System in the countryside, price reforms and the rapid development of township and village enterprises. A lack of foreign exchange was constraining China's development. Foreign donors contributed mainly to the development of China's economic infrastructure by providing capital and modern technologies.
- The *second period* (1990s) was a phase of **economic growth** and the **externalization** of the costs (social and environmental) of this development. It benefited mainly urban areas and resulted in an increasing income gap. Continued investment of foreign aid in energy and infrastructure was accompanied by investment in environmental protection and social development, including poverty reduction.
- The *third period* (the first decade of the 21st century) was characterized by **continued economic growth** with an **emerging agenda of internalising** the social and environmental consequences of China's rapid process of economic growth. More foreign aid went into environmental protection, clean energy and renewable energies, resource conservation, health, culture and education, climate change, public goods and high-level policy consultancy.

Foreign donors thus contributed to China's development according to the specific needs of the different development periods. China is successful in using foreign aid, because it follows its own development agenda. Having said that, it must also be noted that foreign aid to China is not only shaped by cooperation and a rational division of labor, but also by competition and the profit motive. Mixed purposes of providing and receiving aid may increase the transaction costs both for China and for donors.

Growth narrative

As can be seen from the timely investment of foreign aid, donors contributed to China's economic growth and brought innovations to China's development and reform process. It is generally assumed that foreign aid promotes China's development by contributing to

economic growth. In addition, foreign aid to China is coupled with knowledge transfer, including environmental and social safeguards.

Obviously, investment in infrastructure was of special importance – for China’s own development strategy and for donor strategies. As regards multilateral donors, the World Bank and the ADB played a particularly important role here; of the bilateral donors, it was Japan that played the greatest role. But the process of economic growth in China turned out to be uneven, accompanied by self-made social and environmental problems. A wide consensus has been reached that growth has to be combined with sustainability strategies. This reflects a broader strategic shift in development thinking. To give but one example: multilateral and bilateral donors introduced modern project management methods to public investments to China. These include, for example, environmental and social assessments, including resettlement planning, gender analysis, minority and poverty assessments, other safeguard policies and participatory development approaches. Thus, in addition to contributing to economic growth, foreign aid to China is coupled with knowledge transfer, including environmental and social safeguards.

More recently, China has made wider use of this kind of modern project management, making development interventions more sustainable (WB 2007:3). Great attention is paid to making growth “green” and “pro-poor”, but few efforts are undertaken to reflect on the immediate impacts of development interventions on local populations, particularly with regard to minority nationalities and the poor. This brings me to the next narrative of China’s success in poverty reduction and the question of to what extent foreign aid has contributed to poverty reduction in China.

Poverty reduction narrative

Public opinion in donor countries is that foreign aid to China is no longer justified. With China’s high growth rates, tax-payers in these countries find it hard to understand why they should still finance poverty reduction efforts in China. This argument presupposes that foreign aid made a substantial financial contribution to poverty reduction in China in the past. It further implies that poverty alleviation is simply a financial problem. Neither assumption stands up. The main contribution donors have made to poverty reduction in China has not been a financial one, but rather the introduction of innovative methods such as comprehensive poverty reduction approaches, participatory poverty assessments, including gender and minority dimensions

In fact, the financial contribution foreign donors have made to poverty reduction in China has been quite modest. Between 1995 and 2000, they invested around 5.27 billion Yuan in poverty reduction, 60% of which came from the World Bank. (Wang Guoliang 2005: 247). By way of comparison, Chinese government investment during nearly the same period (1994-2000) amounted to 189.11 billion Yuan. So foreign aid investment in poverty reduction amounted to less than 3% of Chinese investment. The rationale for the exit of foreign donors from China – which has become popular during the last couple of years – can therefore hardly be sustained by the argument that China could now finance poverty reduction by itself; China always did. But it is not only the Chinese government that is paying for poverty reduction – if we look at the remittances sent back by rural migrants each year, we can see that these are around ten times higher than the entire annual ODA provided to China. In 2005, for example, rural migrants sent back 30 billion US\$ in remittances (Murphy 2006:5), whereas ODA to

China amounted to no more than 2 billion US\$ in 2005. China's birth planning policy and its potential impact on poverty reduction in China should also be taken into consideration.

That is not to say that the contribution made by foreign donors to poverty reduction has been ineffective or negligible. Rather, their main contribution has been not funding, but the introduction of innovative methods such as comprehensive poverty reduction approaches, participatory poverty assessments, the gender dimension in poverty reduction and poverty monitoring. Among bilateral donors, the UK development ministry DFID is a good example of how interventions can be focused on contributions that improve China's performance on achieving the MDGs. Poverty reduction in China has become a learning process for the international donor community, for Chinese academics and aid practitioners in various regions of China, and for other developing countries as well, indicating clearly the important role of rural development and migration in poverty reduction and also indicating that the transformation from poverty reduction measures to the establishment of a more comprehensive social security system is a crucial turning point in China's development.

Partnership narrative

The popular narrative that "development cooperation with China has changed from a traditional donor-recipient relationship to a relationship between equal partners" suggests that old partners are taking on new roles and that an unequal relationship is changing into an equal one. In fact, the picture has become more complex both on the donors' side and in China. Starting from the late 1990s, multilateral and bilateral donors have been joined by an increasing number of international NGOs working in China. Private giving is on the rise (including powerful private foundations), private corporations have begun to expand their funding in the name of corporate social responsibility (CSR), social entrepreneurs and NPOs are exploring new channels of aid giving, via internet platforms etc. On the Chinese side, we can observe a rapid process of pluralisation of society, with a growing variety of actors in the field of development cooperation, including not only strong central and local governments, but also a growing private sector, public-private partnerships and a developing – although limited – vibrant civil society. What has been termed a dynamic world of "many-to-many" (by Carol Lancaster 2007:225) can also be observed in the sphere of foreign aid in China.

What will be the impact of such a dynamic many-to-many architecture of foreign aid in China? It seems that a long period of foreign aid to China with concessional development finance from rich countries is now slowing down. Multilateral donors already stopped giving preferential loans to China several years ago and some bilateral donors have announced or launched exit strategies. But commercial loans and TA projects are on the rise. This indicates that there is still a need for development cooperation. In addition, China has walked out of its open door and strengthened its position as an international donor in various global regions including African countries. This is definitely not the end of the story, but it does mark a sea change. Development partnerships with Chinese institutions are not restricted to Chinese territory. Various forms of development partnerships with China are imaginable in the future. Obviously, the many decades of working together with multilateral and bilateral institutions in China has been a valuable mutual learning process not only for Chinese institutions, but also for multilateral and bilateral donors.

The more individuals and groups that are engaged in development cooperation, the more coordination, organisational and management challenges will emerge. Public aid agencies active in China will have to be more flexible and collaborative than in the past. In the future,

global problems are likely to intensify and there will be a greater demand for aid to address them (Lancaster 2007:223). From the example of climate change it can be seen how foreign aid in China is changing from a redistributive tool between rich and poor countries to a tool for joint efforts in dealing with global public goods. Here, the networks and webs of development partnerships that have emerged over time both in and with China can be seen as an advantage in addressing global challenges using aid resources in the future.

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