

The Paradox of the *Cuentos Chinos*:
The Future of Sino-Ecuadorian Relations

by

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Esto es para ustedes...

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CHAPTER I:

Introduction: The Dragon in Ecuador

Despite the 10,000 miles dividing the two port cities of Shanghai and Guayaquil, and the proximity of Ecuador to the US, future ties between China and Ecuador can no longer be considered a *cuento chino*. In Ecuadorian newspaper headlines or in casual street conversations the expression *cuentos chinos* means falsehood or a deception. The direct translation means “Chinese Stories” or “Chinese Tales,” though it has nothing to do with an actual Chinese legend or with China. The term is commonly used in a political context, especially when commenting on a political figure that has embellished the reality or pulled a political sham. In the context of this thesis, China as a *cuento chino* refers to the creation of a stereotype that views China as a distant foreign and sometimes dangerous force unlikely to play a significant or positive role in Ecuador’s development. The expression becomes doubly ironic when examined in light of the growing relations between Ecuador and China. As their relationship develops, China has the option of either fulfilling its stereotype by exploiting Ecuador through false promises, or in disproving the *cuento chino* by forging a strong relationship with Ecuador.

On January 2006, newspaper columnists and Latin American foreign affairs analyst, Andres Oppenheimer, published *Cuentos Chinos: El Engaño de Washington, la Mentira populista y la Esperanza de América Latina*.¹ In his book, Oppenheimer

¹ Translates to: Chinese Tales: Washington’s Trick, the Populist Lie, and the Hope for Latin America

provides an overview of Latin America's poor economic development and the lies and tricks that have been imposed by major powers against the region. Part of his study involves an overview on China's incredible growth and its growing interest in Latin America. Oppenheimer concludes that China has tricked Latin American nations to believe that it will invest heavily in the years to come. He also mentions that China may be irrelevant to the region because of distance, lack of cultural understanding and China's future lost of significance to the world economic order. However, if China manages to increase its presence it may hinder development and democracy in Latin America.

Sino-Ecuadorian ties go back to the 1970s, but Chinese immigrants have migrated to Ecuador since the 19th century. Today about 50,000 people of Chinese decent live in Ecuador.² During my visit to Ecuador in the summer 2008, I remember the surprising number of Chinese-owned businesses, and locals' fears or unsettle views of Chinese entering their local industries with better skills and cheaper goods. While the Chinese business scene is well established in the region, China as a potent economic partner is arriving today with interests that are mostly oil centered and may bring large investments and economic opposition to the Ecuadorian society. New large-scale infrastructural projects are being placed in the hands and finance of Chinese firms and banks. In the meantime, China is expanding into Ecuador's inland regions to find its oil needs.

To understand China's impact in Latin America, it might be useful to examine China's role in another part of the world, such as in certain, oil-rich, African countries.

² Ellis, 124

In Africa, China has pursued an experiment described by Deng Xiaoping as “crossing the river by feeling the stones,” where it has “move hundreds of millions of its people out of poverty by combining state intervention with economic incentives to attract private investment.”³ China has brought several positive and negative economic impacts to oil-rich nations like Angola, Africa. The sudden strong Sino-African ties allowed me consider the large possibility of Sino-Latin American engagement and question whether Oppenheimer’s conclusions about China in Latin America were a *cuento chino*. These doubts guided my initial questions of China’s role in Latin America, especially in oil rich nations seeking to diversify from the West. I realized that China’s impacts and presence in Africa is shaping new views of China in Latin America. This thesis, therefore, focuses on how this phenomenon can evolve in Ecuador, a smaller oil rich country, less heard of in American headlines, but silently moving towards stronger ties with China.

Ecuador is of strategic importance to the US because it is home to the only US airbase in South America, Manta; it is the smallest member of OPEC; it is the largest banana exporter in the world; and it has the largest economy outside the US using the dollar. Despite all these strengths, Ecuador’s history is marked by negative US involvement, political instability, and poor economic prosperity. Despite being its largest trading, financing and investing partner, Ecuador has developed a critical view of US interference in their country.

Factors in Ecuador are slowly and quietly shaping national affairs and foreign policy, especially with the rise of a leftist socialist leader. The 1999 elections incurred

³ Brautigam 2010

political instability and the collapse of four administrations (J. Muhaud, G. Noboa, L. Guitierrez and A. Palacio). In 2006, Ecuadorians elected Rafael Correa, the populist leftist economist, under his new political party, Alianza Pais. As of today Correa's presidency has amended Ecuador's politics, reforming the nation's relation to the outside world, and its control of the economy. Correa has worked to change Ecuador's integration with international markets, while supporting regional integration. The new Constitution of 2009 and social movements under "Revolucion Ciudadana" have led to changes in Ecuador's outward initiatives and goals. In response to negative experience with Western control of local industries, the current government is seeking to forge other nations to invest in their oil and infrastructure.

US-Ecuadorian ties will soon be challenged as Ecuador seeks engagement with other countries of the world, and as the US focuses in other regions of the world. In the meantime China's hunt for energy in Latin America is silently growing with Ecuador rising as the leading recipient of Chinese energy investment in Latin America in 2006 with "Chinese corporations now account[ing] for more than a quarter of all planned spending in the petroleum sector, including programmed spending by Ecuador's national oil company."⁴ China's interest in Ecuador makes sense given its strategic geographic location on the Pacific rim.⁵ For Ecuador, China's investments have come at a crucial time to deal with mounting debt problems.⁶

China's new foreign policy and Ecuador's new strong governance are often ignored and conceived as too unreal to go any further and happen, thus Sino-

⁴ Palacios 2008, 178 and Ellis, 126

⁵ Palacios 2008, 179

⁶ Wall Street Journal, "Petroecuador Signs Contract With Petrochina To Sell Crude," July 23, 2009. <http://online.wsj.com/article/BT-CO-20090723-723360.html> (accessed July 25, 2009).

Ecuadorian engagement is often considered a *cuento chino*. China's growing presence in oil rich nations like Ecuador brings to the central thesis question that seeks to view from different angles the *cuento chino* asking: how will China's role and FDI in Ecuador impact Ecuador's economic growth and economic well-being?

By looking into this recent engagement, addressing China's engagement in African oil rich nations like Angola, and creating scenarios for possible outcomes of the Sino-Ecuadorian relation. My thesis shows how Sino-Ecuadorian relations may evolve differently due uncertain outcomes of China's foreign policy and governance factors. The variety of future outcomes that may evolve mark the paradox of the *cuento chino*, as Sino Ecuadorian relations may fulfill the stereotype or bring positive changes to Ecuador.

Creating Futures for Ecuador: Methodology

To address the main question on how China's investments in Ecuador will affect its economy, I will consider the role of Ecuador's government and China's foreign policy practices in the region. I will also look at Angola's experience with China to determine different routes and courses of action China may take in Ecuador. After the outset of Sino-Angolan relations in the 1990s, Angola suffered great economic change, with an average GDP growth of more than 15 percent per year from 2004 to 2007.⁷ By looking at China's role in Angola in the first decade of the 21st century, this study demonstrates that China's role contribute much to this growth.

⁷ CIA, Angola, and Corkin 2009

However, economic growth did not mean improvements in the economic well-being for the people of Angola.⁸ While there are important differences, Angola is a worthwhile country for comparison because of similarities with Ecuador in such things as weak levels of governance, issues of financial debts, and significant reliance on oil. The Angola case study will help build scenarios to tell alternative stories of how the future of Ecuador's economy may unfold.

This study will use the scenario building method to organize information and create four different scenarios that show different paths for the Sino-Ecuadorian future relations. The main goal is to evaluate developmental impacts China may have in Ecuador. In each scenario, I will consider China's future outcomes on economic growth, inequality, and employment in Ecuador. Methods of comparative studies and scenario building help develop constructive ways to think about the future and tackle uncertainties, while testing existing ideas and arguments.

In examining China's potential impacts on Ecuador, this study engages literature and arguments related to FDI and economic development, the Oil Curse, the impact of governance and development, and the role of China in the developing World. The first literature review covers the impacts of FDI in developing countries. The main concern regarding this topic is whether FDI hinders or promotes inequality. Especially when evaluated as part of the oil sector of hosting nations. This literature proves that one way FDI can reduce inequality is by enabling positive spillover effects through the oil industry, leading to more jobs, better technology and skills.

⁸ Natanson 2009

The second literature review covers the economic implications of the Oil Curse theory, which states that countries endowed with natural resources may encounter the worst economic development. The Oil Curse is often blamed for leading to less liberalization, slow development and openness to private investment.⁹ The 1970s oil boom and the aftermath bust of the 1980s and 1990s, led Ecuador to suffer tremendous macroeconomic stability and the infamous *dutch disease*, undergoing a period of poor economic development and reliance on oil revenue. Graciela Chichilnisky, professor and Latin America economics analysts, has argued that “Exporting commodities is a bad foundation for development, and is an unsustainable policy ... There are two regions of the world that have failed to grow since World War II: Africa and Latin America - the two that have specialized in commodities. That is not a coincidence.”¹⁰ The Oil Curse theory is relevant to this study of the economic development of Ecuador and Angola, because both nations have suffered from the negative outcomes of relying in an outdated oil-based economic model.

The third literature review covers the topic of governance as an important determinant of economic development. Governance is usually evaluated in terms of: political stability, government effectiveness, rule of law, control of corruption, among others. This is particular to our study because Ecuador has one of the lowest level of governance in Latin America.¹¹ Government effectiveness in Ecuador changed from a rank of 35th percentile of countries in 1998 to a much lower 15th percentile rank in

⁹ Palacios 2002

¹⁰ Seligman 2006

¹¹ World Bank, “Ecuador Worldwide Governance Indicators, Comparison with Regional Average.”

2008, a period marked more by extreme political instability with eight presidents were elected to office.¹²

The last discussed literature assesses China's changing and expanding foreign policy in the developing oil rich world. China has set out an agenda of policy goals that promises to developing nations, mutual cooperation, development and "growth-growth" economic strategies. African nations have been one of the first to experience this policy and though it has brought some issues and questions regarding the contrast between what China says and does, overall, African nations have benefited from the new foreign policy.

These four themes directly apply to this study of Angola and Ecuador. It is important to Angola's and Ecuador's experiences with FDI, especially FDI in the oil industry, and how it has interacted to lead to further dependence on the oil industry. It is also important to assess how the Oil Curse has undermined progress, and how governance has enforced or fought against the Oil Curse. Finally, it is important to recognize how China can change or prolong its new foreign policy and interest in the developing world. Methods of scenario building and theoretical study will help better analyze different aspects of China and Ecuador's special relationship.

Forces at Play:

Many forces are at play in Ecuador's growing relations with China. Political and historical forces have shaped Ecuador's aspirations to forge relations with non-Western nations and concentrate on internal development. Although Ecuador is the

¹² World Bank, "Country Data Report for Ecuador, 1996-2008."

second largest exporter of oil products to the US from South America, exporting 44 percent of its goods to the US, Ecuador is seeking to diversify relations and move away from the West.¹³ Recently, it is working on building the largest refinery in the Pacific, enforcing regional ties and seeking to create on its coast a center for Asian commerce and importations to Latin America.¹⁴

The second force is Ecuador's reliance on oil and need of new non-Western partners. In 1987, John D. Martz wrote, "Ecuador [oil] output is marginal, and its petroleum policy does not significantly influence the industry internationally... Domestically, however, Ecuador is a country in which the petroleum industry enjoys hegemony over the economy, both in terms of national development and as a primary generator of revenue."¹⁵ Ecuador is continuing to expand this industry and forge relations with China based on petroleum exportation and exploration, such will determine to great extend Ecuador's economic decisions and future development.

Ecuador's reliance on oil and on foreign investors for development is significant when considering its own past negative experiences with oil and development, and at Angola's current situation. Though Angola has suffered great economic growth and has become China's biggest supplier of oil, most profits have ended in the hands of the wealthy and powerful classes.¹⁶ Angola's socio-economic conditions continue relatively the same, with the highest mortality rate, and about 41 percent of the population under poverty level and unemployed.¹⁷

¹³ EIA, "U.S. Imports by Country of Origin," and CIA, Ecuador

¹⁴ Reuters, "Ecuador seeks \$4 billion for New Oil Refinery," Feb 22, 2007.

<http://www.reuters.com/article/companyNewsAndPR/idUSN2244157820070222> (accessed July 2009)

¹⁵ Martz, 3

¹⁶ Natanson 2009

¹⁷ CIA, Angola

As I consider China in Angola and all the forces shaping China's foreign policy, this thesis questions concerns related to the unpredictable positive or negative impacts that can China bring to Ecuador. Many challenges and fear remain uncertain about Sino-Ecuadorian ties, especially when considering Ecuador's negative experience with the West in the past, which invested solely in primary good industries and contributed little to the growth, while enforcing their own practices. Will China be an ideal foreign partner for Ecuador? Or will it be worse than the West? The vision of Chinese bargains with Ecuador is a complicated *cuento chino* because it is unsure how it will play.

While it is easy to discard and believe that Sino-Ecuadorian ties will never occur, this thesis looks at areas of investments that have potential improving in the near future. This thesis also examines ways to evaluate the future interactions between China and Ecuador, as uncertain factors may play differently. One of the uncertainties regards Ecuador's level of governance. Though President Correa is expected to bring change and improve governance, governance conditions are unsure. The uncertainty also stands for China, and the role of its new foreign policy based on a path of development and progress. As the interplay of these two uncertainties may vary, my conclusion considers them and looks for different angles at how Sino-Ecuadorian ties may follow several paths of development.

Road Map:

The road map from the rest of this thesis goes follows: after this introduction and overview of the project, Chapter II will consider the theories in question. The theories or literature covered will provide relevant information and raise issues that will help guide the central questions of this study and generated scenarios. In order to build scenarios, this chapter concludes with a brief section and overview of the methods of inquiry: scenarios building and comparative case study.

Chapter III will provide background information on Angola's pre-China experience, and focus on China's recent entrance and role in Angola's oil industry. This case study chapter provides information on China's bargains and outcomes on Angola's economic development and well-being. It concludes that though Angola has suffered significant economic growth, it has not received the same well-being results.

Chapter IV will offer a historical overview of Ecuador's experience with the US and its current relation with China. This chapter focuses on factors such as the changing government and growing ties with China. It concludes on the variety of opportunities China is offering to Ecuador that may shape a new development model.

Chapter V will use all literature and background information to present a set of scenarios for Ecuador's near future as it strengthens ties with China. The scenarios evaluate possible patterns of development that Sino-Ecuadorian ties may suffer. All scenarios look at factors such as economic growth and economic well-being to provide a more holistic view of China's investments and impacts in Ecuador. The study concludes with conclusion and synthesis in Chapter VI.

CHAPTER II:

Theory and Context

Introduction: Theoretical relevance

The central question of this study is: How will China impact Ecuador's economy? China has emerged as an important exporter of capital to world markets.¹⁸ An issue that is central to this study is whether China's role in providing finance and aid to developing countries, such as Ecuador, will have impacts that are different from those we have seen in the past when Western industrialized countries played this role. This chapter considers literature and arguments about the role of FDI in development, the Oil Curse theory, governance and development, and China's foreign policy. These theoretical arguments help organize thinking of the past and present while helping to build scenarios of future expectations. The following section explores these important themes to Ecuador's growing economic ties with China, and the ways these ties may affect Ecuador's economy.

Theoretical arguments help examine the comparative case-study method and scenario method. These methods of inquiry explain why the study of Angola is helpful to the analysis, as well as conducive to making scenarios and determining conclusions of China's impact in Ecuador.

¹⁸ Lederman, Olarrega, and Perry 2009, 16

Argument I: of Foreign Economic Relations and Economic Development

Throughout the last oil boom period, 1973-1981, investments in Latin America represented about 70 percent of all FDI flows to the developing world.¹⁹ Though FDI has shifted more evenly across other regions of the world, it still plays an important role in the economic development of Latin America. China's recent surge of FDI in Latin America is a result of seeking for natural resources, like oil, and need to expand to new markets. Before the 21st century, China's outward flow of FDI to the world ranged below \$3 billion yearly.²⁰ However, by 2006, it reached \$15 billion, and by 2009, China's outbound of FDI totaled \$120 billion.²¹ China's new position as a major foreign investor questions the impact this presence may have in the economic development of oil-rich developing countries reliant on oil revenue. It is important to evaluate to what extent FDI promotes economic development as a factor of economic growth and economic well-being, by measuring indicators such as GDP growth, unemployment rates, and GINI levels. To consider outcomes, this section evaluates some important features of FDI and China's role in promoting or hindering development through investments in developing nations.

Literature and arguments

According to Susan MacMillan study of the consequences of FDI in developing host countries, it is important to evaluate FDI because it gives information regarding

¹⁹ Ocampo and Martin 2003, 78

²⁰ Ministry of Commerce and China Statistic Bureau, "Figure 1. China's Outward Foreign Direct Investment (1979-2006)." http://www.usc.cuhk.edu.hk/webmanager/wkfiles/6538_1_a1.gif (accessed Nov. 27, 2009).

²¹ Brown and Wood, 16

international trade patterns, it involves a degree of foreign control in host countries, and it marks patterns of development.²² FDI outcomes in economic development can be explained through three frameworks: the modernization, dependency and state-led.²³ The *modernization* framework uses neoclassical economic practices to create FDI effects that are beneficial for the host-country economy. The *dependency* state shows how advanced nations use their firms to exploit the resources of developing nations. In the *regulated* state, the state has dominance and autonomy over the ideological orientation of its population, enforcing development policies it sees fit. These approaches help ways China's FDI may evolve in Ecuador.

According to Hausmann and Fernander, the amount of FDI capital flows and state development paths depends largely in countries' "environment for investment and the functioning of markets."²⁴ This often refers to a free trade neoclassical economics environment. Countries like Venezuela and Ecuador currently refuse to create this kind of environment because of negative experience with US imposed neoclassical economic policies, known as the Washington Consensus.

When considering FDI direct outcomes in socio-economic issues, FDI analysts Gallagher and Chudnovsky argue that FDI reduces inequalities by expanding to other industries beyond natural resources through "the establishment of the dynamic investment-export nexus [that] led to steady diversification of production away from those activities requiring only natural resources and unskilled labour."²⁵ They conclude that FDI brings positive results when it creates technological and

²² McMillan 1999, 1

²³ McMillan 1999, 3-5

²⁴ Hausmann and Fernandez-Arias, 5

²⁵ Ocampo 2009, xix.

organizational spillovers that can lead to jobs in new industries. However, in countries like Ecuador and Angola, FDI has brought little incentive to expand to other areas because weak domestic conditions such as corruption, weak governance, and poor firm responsibility. Domestic conditions set the economic and political factors that draw in FDI as well as determine the development outcomes.²⁶

Though this study tries to look at China's FDI in Ecuador to present with development outcomes, it is challenging to determine development outcomes because "the search for a 'universal result' of FDI on the developing-country economy is simply misguided. FDI can dramatically different impacts—both positive and negative."²⁷ Human resources, financial systems, governance, and institutional constraints help us define to some extent the kind of positive or negative impacts.

Positive Outcomes of FDI

Positive outcomes of FDI promote economic development through deterring inequality and improving economic wellbeing. Some direct characteristics of these positive results include: establishment of new kinds of efficient activities, larger flows of capital, advances in research, increase in competition in individual sectors, lower input prices, and improvement in local firms' profitability.²⁸ FDI can increase exports and competitiveness of firms while generating technological and other spillovers.

Positive impacts generally brought by Chinese FDI arrive through investments in infrastructural projects. China has a record of directly investing in fast, high-quality

²⁶ McMillan 1999, 11

²⁷ Moran, Graham, and Blomstrom 2005, 375

²⁸ Moran, Graham, and Blomstrom 2005, 375

infrastructure projects. As Xiang Lanxin mentions, China is a key commercial player and potential source of much-needed infrastructure investment in the region.²⁹ This kind of FDI in infrastructure promotes better relations with the host country, and in the long-run benefit China's access to transportation and communication.

Some positive Chinese FDI outcomes include host-countries to shift loan demands from worldwide financial institutions like the IMF and World Bank, to Chinese low interest loans. In 2006 the government of Angola was no longer interested in borrowing from the IMF because it could borrow from China without having to comply with any provisions, while paying very low interest rates.

Investor countries bring their own skills, knowledge and capital to residing and work areas. These usually results in several spillovers for locals who can benefit directly from employment opportunities, better schools, and the arrival of health providers. In their transnational analysis of 69 countries, Borensztein, De Gregorio and Lee confirm that FDI can bring transfers of technology and innovations that contribute to economic growth. However, local factors can challenge outcomes since "FDI contributes to economic growth only when a sufficient absorptive capability of the advanced technologies is available in the host economy."³⁰

Negative Outcomes of FDI

Developing nations encounter negative FDI outcomes because of weak governance, bad control over home industries, and dependence on natural resources.

The absence of regulations that govern measures such as natural resource extraction

²⁹ Xiang Lanxin 2008, 55

³⁰E. Borensztein, J. De Gregorio, J-W. Lee 1998

and weak policy enforcement increase the probability of unsustainable FDI outcomes.³¹ Some traits of negative FDI practices include the inefficient use of local resources and subtraction of the local welfare of communities through over-exhaustion of natural resources, domination of goods and workers. These often result in less job opportunities, flight of capital, and few infrastructural investments.³²

Gallagher and Chudnovsky provide an overview of FDI negative outcomes:

In the absence of appropriate policies, it can also lock a nation into low-value-added assembly manufacturing, create “enclaves” where foreign firms operate on high productivity devoid of spillovers, and even crowd out domestic investment.³³

In a study of the role of FDI in developing countries, the Organization for Economic Co-operation and Development found that negative impacts are also found in environmental and health problems. Other negative outcomes led to the disruption of local cultures, increases commodity price, and population displacements.

Implications for Case-Study Nations

Differences in policies and economic factors result in different FDI benefits.³⁴ Preexisting institutions and conditions may set an unequal environment that is ignored, prolonged, or furthered by FDI. FDI in oil rich areas can lead to foreign ownership and extraction of oil that marks increasing inequality, as the rich minority becomes wealthier. The dependency development approach has often defined FDI in Latin America. Throughout the 20th century, the lack of favorable domestic

³¹ OECD 2002, 18

³² Moran, Graham, and Blomstron 2005, 376

³³ Ocampo 2009, xix

³⁴ Dirk Willem te Velde, 37

conditions, weak infrastructure and high bureaucracy, combined with Latin America's reliance on primary goods, allowed firms to act irresponsibly.³⁵ In response to past FDI negative outcomes, the new century has brought the rise of leftist charismatic leaders with reforms against foreign control. As a result, foreign firms are facing higher taxes and accountability. These changes are moving Latin America away from the dependency approach towards a more regulatory one that though necessary for the process of development, it creates less favorable FDI conditions. Latin American and African countries share similar experiences with FDI that has often led to more inequality and less development. The main concern is whether China's rising FDI in developing nations may be an opportunity or danger to oil-rich nations where it is investing.

Oil producing nations with high energy-related income dependence like Ecuador have the bargaining power to attract investors even though their foreign relations are considered unstable and their policies unfriendly to investors. For example, in order to regain control of the oil-industry, President Correa has been "passing previous legislation and moving away from previous contracts [with foreign firms]."³⁶ The foreign firms have accepted the changes and agreed to renegotiate contracts, as long as profit was made.

The connection between Chinese FDI, development, and inequality will be determined by the conditions set by Ecuador's governance and China's foreign policy practices. It is important to consider Ecuador's FDI environment, whether it has the necessary absorptive capacity among domestic firms and institutions, and whether it

³⁵ McMillan 1999, xi

³⁶ Stanley, 181

has made efforts to diversify. It is also necessary to evaluate how China can help Ecuador break away from the dependency framework.

No matter the attractive or unattractive measures established by the host country, the type of FDI a “country attracts is...its advantages [that] are shaped by the structural, geopolitical, and strategic characteristics of the country relative to those of its competitors.”³⁷ Other factors are behind China’s investments in Latin America, such as the Taiwan diplomacy issue and geopolitics.

Argument II: The Oil Curse

*Mineral-rich states tend to be poorer, more conflict-prone, more authoritarian, more unequal, and more corrupt and dysfunctional than their non-mineral peers.*³⁸

This quote is true for both Angola and Ecuador. During the 1970s oil boom, Angola suffered from a war financed by its oil revenue, while Ecuador suffered from high price of commodities and lack of investments in other industries. Oil rich nations own a commodity good that gives them access to capital, while perpetuating a dangerous economic model. The reasons behind this are explained by the Resource Curse theory, or Oil Curse, which states how countries with the most resources may perform the worst in development. A paradox of the Oil Curse is that though oil is valuable and capital intensive it requires little labor. A careful examination of the Oil Curse and its economic impacts is important to guide the evaluation of China’s investment in the oil sectors of Ecuador and Angola. This section addresses the

³⁷ Kumar 2002, 9

³⁸ Shaxson, 2

relationship between oil and economic development, to help evaluate its role in the economic progress of Angola and Ecuador.

Literature and Arguments

The 1990s brought the recognition of the Oil Curse theory when Jeffrey D. Sachs and Andrew M. Warner published “Natural Resource Abundance and Economic Growth.”³⁹ Their paper questioned why economic growth in economies with abundant natural resources tends to grow less rapidly than in economies where natural resources are more scarce. Their evaluations consider the effects of macroeconomic instability and *dutch disease* in the development of oil-rich nations.

Macroeconomic Instability

The Oil Curse theory states that dependence on oil revenues can lead to macroeconomic instability. Oil is a political commodity, dependent on the changing realities of supply and demand, affected by unpredictable price variations.⁴⁰ Price variations are vulnerable to drastic swings that make oil prices climb rapidly to unprecedented levels, such as those recorded in 2007 when the oil cost reached \$132.8 a barrel.⁴¹ Two big issues can result from this macroeconomic phenomenon.

The first issue is that price variations lead to uncertainty and instability in the use of revenue and decision-making. Oil prices dependence on market price flows, makes budgeting unpredictable, oil-back payments dangerous, and investment in

³⁹ Sachs and Warner 1997

⁴⁰ de Olivera Soares 2007, 31

⁴¹ Mongabay, “10-year commodity price chart for Crude oil”
http://www.mongabay.com/images/commodities/charts/crude_oil.html (accessed Dec. 16, 2009)

future projects financially insecure. High prices and demand for oil enables false overconfidence in using this form of revenue for future projects and policy reforms. Nations involved in the oil industries have difficulty responding to financial instability and making macroeconomic decisions. Overconfidence and decisions made on the premise of high oil prices may lead to more borrowing, concluding in a unsuitable debt burden when prices decline.⁴²

The second issue brought by Oil Curse related to macro instability is inflation, found when nations are “faced with money flows that far surpass their absorptive capacity, resulting in overheated economies and rampant inflation.”⁴³ Macroeconomic instability creates large-scale damages in the oil country’s economic development, raising the stakes for decisions dependent on this revenue, and leading to more mismanagement of revenue and issues of corruption.

Dutch Disease

Dutch disease refers to the lack of development in manufacturing and the increase in exploitation of natural resources because of bad administration and redistribution of funds within the state.⁴⁴ The term was coined after the economic disaster that hit the Netherlands in the 1960s, as gas discoveries led to the increase local goods prices, promoting cheaper importation and less domestic industrialization.

The *dutch disease* evaluates the negative effects brought by oil booms as they increase the entrance of cash flows leading to domestic price increases which make

⁴² Hodges 2004, 3

⁴³ Hodges 2004, 31

⁴⁴ Oppenheimer , 78

local goods more expensive than those able to be purchased abroad.⁴⁵ More imports paid by oil revenues led to lack of development in other industries, displacements of jobs, and income inequality.

Implications for Case-Study Nations

The “resource boom” is a dangerous phenomenon comprised of possible economic and political unstable outcomes. The Oil Curse theory is applicable to the countries in study because though nations like Angola may today be “...enjoying the biggest financial bonanza in history... past experience and early indications amid the current boom suggest that these resource-rich countries not only are not translating this into real human development, but are likely to see their populations actively impoverished.”⁴⁶ Angola and Ecuador have already experienced negative outcomes of the Oil Curse. As China plans to expand its investments in the oil industry, and as financial booms and bust bring price variations, these two nations need to carefully protect themselves from issues of macro instability and *dutch disease*. The Oil Curse theory provides different ways of observing how this event may take place if China invests irresponsibly. The Oil Curse theory recalls past experiences and considers the threats that countries like Ecuador and Angola are likely to face if they continue to rely on one commodity without diversifying or establishing better policies.

Historically, dependence on oil revenues in Latin America has proven to be a negative force, leading to less liberalization, less development, and less openness to

⁴⁵ Shaxson 2008,18

⁴⁶ Shaxson, 2

private investment.⁴⁷ The same principle applies to Africa, especially in Angola where oil development and exploration has led to a greater focus on an industry exposed to further unemployment, and inequality. In Angola, oil dependence is far more dangerous as it accounts for over 90 percent of the total revenue. In Ecuador, oil receipt in 2001 represented 48 percent of Ecuador's exported goods, and 34 percent of fiscal revenues.⁴⁸

Argument III: Governance and Development

The role of government is essential for development. As we look at the role of China and its impacts in Ecuador's development, it is crucial to understand the role the government plays in advancing or hindering progress. This issue is important when considering that Ecuador has one of the lowest levels of governance in Latin America.⁴⁹ There are many ways to define and evaluate governance, here we defined it as "the nature of rules that regulate the public realm— the space where state and economic and societal actors interact to make decisions."⁵⁰

Literature and Arguments

The World Bank mentions that governance can be defined as "the traditions and institutions by which authority in a country is exercised." To evaluate governance, the World Bank has constructed a series of indexes measuring the following qualities of

⁴⁷ Palacios 2002, 31

⁴⁸ Palacios 2002, 39

⁴⁹ World Bank, "Ecuador Worldwide Governance Indicators, Comparison with Regional Average."

⁵⁰ ODI 2006

governance: voice and accountability, political stability, government effectiveness, regulatory quality, rule of law, and control of corruption.

When talking about governance in the rest of the project, I will consider particularly issues related to political stability, government effectiveness, and rule of law. According to the World Bank, we can define my measurements of interests as follows: political stability and absence of violence evaluate the chances of a government getting overthrown by unconstitutional terms. Government effectiveness focuses on the direct impacts of governments in sponsoring public services, effective policy formulation and implementation. The rule of law measures the extent to which people support and abide by the rules of society. Lastly control of corruption measures the extent to which power is used for private gain.⁵¹

The World Bank provides important traits of good governance; however an issue that remains is evaluating governance as a contextual issue. “Particular conditions of each country provide both constraints and opportunities to improve governance,” these conditions help define different effective courses of actions that are not considered in the context of “good governance” but may be better effective for those countries.⁵² Issues of voice and accountability measure citizens’ participation in selecting governments and freedoms of speech and press. In Ecuador, recently this freedom has been challenged by President Correa, but one cannot take only this measure to define whether he heads under strong or weak governance.

In Ecuador democracy has not meant stability, and usually the most stable governments are those that have more authoritarian traits. The President of Ecuador,

⁵¹ Kaufmann, Kraay, and Mastruzzi 2009, 3

⁵² ODI 2006, 1

Rafael Correa, is often criticized for his hard-line decisions and actions to grant himself more power over the national affairs, but his presidency is comparatively. Better governance can be often associated with features such as “improved investment and growth rates...government effectiveness, an efficient bureaucracy.”⁵³ These features are important for our measurements of good governance and will help guide the scenario overview of distinguishing between strong or weak governance.

Implications to Case-Study Nations

Governance in Ecuador is a crucial changing variable that helps determine economic development and effectiveness. Ecuador has one of the lowest government effectiveness rates in the region.⁵⁴ In Chapter V, I will construct scenarios that measure different ways governance may evolve in the next decade in Ecuador. Ecuador’s governance can take two paths of either remaining at weak levels, or improving to strong governance levels. Strong versus weak governance will be measured in regards to government action to promote or hinder economic growth, unemployment and inequality. Weak governance can be described as a world where the government is incompetent to make the right decisions to hinder the progress of his country. It is a society marked by lack of accountability and transparency, and a poor rule of law. On the other hand, a strong administration exists in a society where an efficient bureaucracy is in place, government has wide support and accountability for actions and efficiency.

⁵³ ODI 2006, 1

⁵⁴ World Bank, “Country Data Report for ECUADOR, 1996-2008.”

Argument IV: China's Interest and Foreign Policy in Developing World

Forces driving China's interest in developing growth and new foreign policy are related to goals of gaining more influence in the global economy while safeguarding natural resources. China's FDI has recently focused on a "strategic pursuit of resources and attempts to ensure raw materials supplies for growing energy needs."⁵⁵ Today securing oil supplies has become a vital feature of China's national security.⁵⁶ The hunt to secure natural resources while seeking to diversify and compete with other nations has led to a new Chinese foreign policy to implement in developing nations with abundant resources.

Literature and Arguments

As the largest developing country in the world, China is committed to the path of peaceful development and the win-win strategy of opening-up. It is ready to carry out friendly cooperation with all countries on the basis of the Five Principles of Peaceful Coexistence and build a harmonious world of durable peace and common prosperity.⁵⁷

In his overview of China's new foreign policy, Thomas Cieslik states that China's main goal overseas is to foster a new harmonic world order.⁵⁸ The text above taken from "China's Policy Paper on Latin America and the Caribbean," enforces this new move of establishing better engagement and cooperation with developing regions of the world. The publication of such work goes hand in hand with China's foreign

⁵⁵ Alden, Large and Soares de Oliveira 2008, 7

⁵⁶ Ziegler, 183

⁵⁷ Xinguanet "Full text: China's Policy Paper on Latin America and the Caribbean.

⁵⁸ Cieslik 2010, 162

policy strategy, setting the stage to engage in more in-depth relations with developing regions that can assist China in meeting its economic goals.

China promises to advocate pragmatic friendship and to push for international cooperation and mutual respect. The Chinese foreign ministry spokesman Qin Gan has adopted the following foreign policy program:⁵⁹

- China will not seek hegemony. China is still a developing country.
- China will not play power politics nor interfere in other countries affairs.
- China believes that all countries should be treated equally.
- China cannot do to others what they do not wish others do to them.
- China advocates that all countries handle their relations on the basis of United Nations Charter and norms governing international relations.
- China respects the diversity, and advocates different cultures, and the ability to make exchanges, learn from others and complement others with their own strengths.

In accordance with this mission, Cieslik mentions that the role of Latin America in China's foreign policy is centered on Beijing's strategies to seek diversification of its economy and markets, find places for exports, and secure resources to reduce help China's raising."⁶⁰ To address this need China is enabling loose and friendly policies. In his analysis of China's foreign relations, Robert Sutter presents some of China's foreign policy strategies based on:⁶¹

- Growth in cooperation and partnership with all states around the world
- Enforcement of a good image of China to the world
- Willingness to not make complaints against the US hegemony in world politics as long as the US does not challenge core Chinese interests
- Diversification of manufacturing facilities and secure raw materials.

⁵⁹ Cieslik 2010, 165

⁶⁰ Cieslik 2010, 166

⁶¹ Sutter 2008, 81

While promoting a positive foreign policy agenda, China reaffirm that: it does not seek to implement ideologies, it does not intend to promote human rights, democracy or global capitalism, and it is not devoted to moral values.

China's interest in the developing world becomes evident when evaluating its new move to gain ground in the political and diplomatic fronts of regional organizations of nations of interest. In 2004, China gained observer status in several Latin American regional associations, including the Organization of American States (OAS), the UN Economic Commission for Latin America and the Caribbean (ECLAC), the Inter-American Development Bank (IADB), and the Latin American Parliament (Parlatino).⁶²

In 2004 Chinese president Hu Jintao set out three goals for Sino-Latin American relations. The goals call for strengthening strategic ties and mutual political trust, taking practical and creative steps to tap the potential for economic cooperation, and attaching greater importance to cultural exchanges to deepen mutual understanding.⁶³

To enforce goals and create a sense of understanding, Xiang Lanxin mentions that this nascent and unusual relationship between China and Latin America is built on three pillars: a common sense of colonial roots, similar economic challenges as developing nations, and complementary rather than competitive economics. Xiang Lanxin adds that "China...offer a unique opportunity for the region to experiment with a new model of international relations."⁶⁴

⁶² Jiang Shixue 2008, 35

⁶³ Jiang Shixue 2008, 38

⁶⁴ Xiang Lanxin 2008, 57

China is questioning the geopolitical dynamics of the Western hemisphere and offering a new development opportunity to Latin America. The prospects for partnership are many because “China and Latin America have been pursuing similar parallel paths of economic liberalization, and in the context of globalization, there is a clear opportunity for South-South Cooperation. Both... would benefit from working together toward regional peace and development in Asia and Latin America.”⁶⁵

China’s external diplomatic model is attractive to developing nations because of conditions that differ from the US model. As discussed by Tokatlian in his overview of the Latin American perspective of China, the Chinese model seductive because it is based on “multipolarism (as opposed to unipolarism), multilateralism (as opposed to unilateralism), noninterference (as opposed to interventionism), soft power (as opposed to hard power), pragmatism (as opposed to ideologization), collaboration (as opposed to domination), and persuasion (as opposed to coercion).”⁶⁶ While some believe that China plans to take on the traditional roles played by the West in trade and investment in Latin America, China asserts that is aware of the role of the US in Latin America and has no intention of challenging the US hegemony in the region.

China remains strongly committed to these foreign policy goals because they seem to be playing out well and securing energy markets. Keeping in mind that “Energy, and in particular oil, is too important to be left to the market forces alone,” China needs to create the best foreign policy approaches to secure this energy need.⁶⁷

⁶⁵ Jian Shixue 2008, 41

⁶⁶ Tokatlian, 64

⁶⁷ Ziegler , 180

Implications for Case-Study Nations

A critical implication to the cases-study nations is how can we distinguish between what China says and the way it acts in investing nations across the world. Will China behave in Latin America the same way it behaved in Africa or Southeast Asia? China may implement different foreign practices in different regions of the world, thus the ways these practices will be conducted are uncertain and critical to those nations China invests in. These questions and concerns are important to determine China's future outcomes in Ecuador. Part of the scenario-building process is looking at how China's foreign policy goals and practices are executed in Ecuador. The ways these foreign policy practices are executed is evaluated in terms of their altruistic or malevolent foreign policies.

Altruistic foreign policy practices support a positive view of China in the developing world. The term, Beijing Consensus, as coined by British economist Joshua Cooper Ramo, exalts China's offer of development to developing nations of the world.⁶⁸ China enforces an oil strategy for the 21st century, which calls for diversifying oil imports, cooperation on the development of oil in other countries, establishing a national oil reserve, and increasing efficiency in oil consumption."⁶⁹ China has the overall effect of shaping business opportunities, offering deals for infrastructure and shaping cooperative strategies, as well as providing these countries with more sources of finance.⁷⁰

⁶⁸ Ramo 2004, 3

⁶⁹ Ziegler 2007, 183

⁷⁰ Ziegler 2007, 197

Malevolent foreign policy practices can be described as those where China is a irresponsible investors who does not comply to promise foreign policy goals. It enforces the fact that China is after all the largest developing nation in the world with strength to fill a similar role that was once solely characterized by the West. This view enforces how China can promote a positive image of itself, but act in a way that may hinder the development of oil-rich nations. Other signs of China's weak foreign policy include the reinforcement and support of weak governments found in these nations, that can led to practices that increase inequality. This fear is enforced by the presence of a power and a model that promotes no accountability for its actions.

China's impacts and engagement in the developing world may differ across regions of the world, especially among nations with different preexisting structures and institutions. As "Chinese development assistance and FDI can provide the right conditions for Africa's 'take-off,'" it may have different outcomes in Latin America.⁷¹ China is special to Latin America because it is expected to be different from the imperialistic Western power. China is an emerging player now competing in the top ranks for natural resources, yet it still acts like a developing nation itself, acting in other countries as a development partner over a foreign imposed power. Despite Western arguments against Chinese methods of foreign policy, such as the lack of transparency and the breaking of environmental laws, developing nations in urgent need of Chinese investments, ignore these figures. Still, it is important to consider features behind its foreign policy. Though China promotes partnership, set by few

⁷¹ Alden 2007, 129

provisions without considering unsustainable practices, it is able to implement measures and practices that have short-term benefits.

Conclusion on Theoretical Arguments:

Different theoretical questions derive from this phenomenon that will help guide the central question of this study: what impacts will China's investments have in Ecuador's economy? This chapter has so far addressed different arguments that help to construct an overview of the case study nations, Angola and Ecuador, and later help prepare scenarios for evaluating the impacts of China's investment in the oil industry of Ecuador. Today, as Ecuador faces working under the control of new investor, with a new philosophy and history, we need to consider various arguments in order to construct educated models to represent potential scenarios in the future.

The arguments concerned with FDI and economic development will provide a framework to evaluate possible situations that impact the economic well-being of Ecuadorians. Oil Curse arguments provide information on possible impacts Ecuador may fall if it continues focusing its growth strategies in the oil industry. Arguments on governance are essential to understandings of the role in the state in advancing development. Finally, arguments about China's interest in the developing world provide information about China's foreign policy goals and possible impacts in investing nations.

Methods of inquiry:

The case-study comparative and scenario-building method will help oversee and define China's trajectory of investments. The case study method will look at Angola as a country from which to learn and derive questions and concerns to better guide the study. The comparative method seeks to understand to what extent Angola is worthwhile example for understanding China's economic impacts in Ecuador.

Case studies and Comparative method:

The purpose of the case-study method is to investigate a real-world phenomenon within its naturally occurring context to make educated predictions as to how that phenomenon will evolve elsewhere. Case studies help enable “how” and “why” questions, acting as sources of guidance and further understanding of the pending questions, especially of the specific research question, “how will China impact Ecuador's economy?”⁷²

The case study will ask the same question for the chosen case study country, Angola. The example of Angola can help provide alternative ways to understand China's role in Ecuador. In Africa, Angola has received the highest Chinese investments and experienced high economic growth. Though I do not expect the same to happen with Ecuador, Angola can provide ways of observing real life arguments and literature, while developing new questions to ask and consider in this study. Ultimately, the purpose of Angola to my study is to: demonstrate theories, present lines of convergence and differentiation, contribute with more causal forces, and help establish wildcards, or areas of uncertainty.

⁷² Kaarbo and Beasley 1999, 389

Through highlighting shared traits and trends between the two developing regions, and bringing up areas of differentiation, the Angola scenario will help shape new scenarios that will describe a range of potential impacts as well as help predict Ecuador's economic prospects.

Scenario-Building Method:

Scenarios are simply a range of predictions guided by educated judgments with reasonable chances of being right. Scenarios provide constructive ways to think of the future and to develop plot lines of different ways uncertainties may evolve. In order to build scenarios it is important to combine local knowledge, observe other examples, and have sensitivity to temporal considerations.⁷³

Several steps guide the scenario building process, and the first key step is determining the driving forces or independent variables, those causal forces that surround the event of focus. The driving forces help determine factors that are evident to remain the same or suffer little change throughout the time frame of the model. Predetermined elements are those factors that appear relatively certain, "they are the parameters that can safely be assumed for the scope and span of the scenario exercise."⁷⁴ They are slow changing phenomena or factors that are most likely to remain the same throughout the study time, like demographics and geography.

The driving forces and predetermine factors help determine the critical uncertainties, or those factors of influence that are highly uncertain and will be constructed in the model. The critical uncertainties set the stage for determining

⁷³ Bernstein et al. , 62

⁷⁴ Bernstein et al. . 55

unknown consequences of certain events, and set different scenario plot lines that tell a compelling story of how events may happen. Within each plot line a variety of indicators show how events are unfolding along a particular path of data. Two critical uncertainties have been defined for the rest of the study: level of governance and Chinese foreign policy practices.

Once constructed and analyzed, the implications of scenarios provide us with an area of decision-making in response to a newly constructed model of expectations. Although determining implications of scenarios is the last stage of the scenario process, happening before decision making or taking action, it is important to consider the presence of wildcards, or low probability events that may break the logic of the plot. Wildcards are those forces that may alter the whole scenario and require a new observation of the area of study, for example, the possibility of natural disasters. Taking this process as a whole, this study will use this methodology process to build different narratives of Sino-Ecuadorian relations in the years to come.

Conclusion

The goal of my study is to evaluate the kinds of changes that may be incurred by China's FDI and financial flows in Ecuador's economy. This chapter provides us with theoretical analysis and methods of inquiry required to assess this change. In addition to evaluating important theoretical arguments, this chapter also evaluates the importance of looking at case-studies nations like Angola. It also describes the

relevance of scenario building to this study, which provides a framework for assessing changing relations and economic impacts.

Overall, this chapter provides the general framework for the rest of the thesis. Angola's role in this project is to serve as a case study for comparative analysis, and to act as a guide to build scenarios and tell alternative stories of how the future might unfold in Ecuador's economy. Scenarios will compare the Angolan experience with China, focusing on causal linkages found in the comparative method to measure Ecuador's experience. As Chapter III and IV set the stage, Chapter V will explore "critical uncertainties", constructing scenarios that will examine if China will negatively or positively impact Ecuador's economy. Through evaluating a number of different figures, using different methods of analysis and guidance, this study seeks to build a logical framework for evaluating China's impacts in Ecuador.

The following chapter will provide an in-depth study of China's impact in Angola, evaluating background information and events in Angola before China's debut on the global scene and until the latest 21st century economic developments.

CHAPTER III:

China in Africa: Focus Angola

Introduction: Why Angola?

China's entrance into oil-rich nations in Africa is a result of its new role as the second largest importer of oil in the world.⁷⁵ This chapter explores the sudden arrival of financial flows to Angola from China. Though Angola's economic background, geography and political history differ from Ecuador's, Angola is a source of good comparison for Ecuador to study the course of Chinese investments and impacts in developing oil nations. Chinese investments in Angola's oil led to sudden economic growth outcomes, but small changes in the economic well-being of the Angolan people. The purpose of this chapter is to consider and establish those forces that allowed for Angola's sudden economic surge. This chapter seeks to evaluate the extent to which FDI in Angola led to socioeconomic improvements, especially to changes in inequality and unemployment.

Sino-African relations are strengthened by a common desire for mutual development, for expansion into new markets, and for sovereignty and international recognition. Chinese entrepreneurs have entered various countries in Africa and built in record time urgent infrastructure needs like roads, railways, hospitals and schools. Some have restored abandoned factories and offered local job opportunities. While

⁷⁵ Nation Mater, "Energy Statics, Oil Consumption." http://www.nationmaster.com/graph/ene_oil_con-energy-oil-consumption (accessed Dec. 17, 2009).

others have invested and constructed mega-power plants to bring energy to areas that previously lacked. China's impacts in African nations provide an insight into what China has to offer to the developing world.

China's presence and investments have been noticeable in oil-rich nations like Angola. In 2002, Angola had an urgent need of financial assistance to fund reconstruction efforts after the ethnic civil war. China rapidly offered financial resources with no provisions, in return for Angola's natural resources.⁷⁶ In a few years relations expanded considerably and China gained an influential role in external trade, FDI, and public works. Despite close to zero exports to China in 1991, by 2006, 35 percent of Angola's exported goods were off to China.⁷⁷ China's oil needs align with Angola's financial needs, leading to a partnership based on mutual interests.

Angola's oil production increased considerably. By 2008, Angola produced about 2.1 million barrels of oil daily, a considerable amount in comparison to the 84.4 million barrels of oil produced daily in the world.⁷⁸ Angola today is one of the fastest growing economies in the world, but opinions vary over China's impacts in Angola. The president of Angola and Chinese negotiators regard the relations as an example of "growth-growth" strategy and development miracle. However, the same thoughts are not shared by all the local people. These conditions are important to study because many of the financial bargains between Angola and China appear to be similar to those China is making in Ecuador.

⁷⁶ Ferreira 2008, 299

⁷⁷ Goldstein, Pinaud, and Reisen, 42

⁷⁸ EIA, "Angola Energy Profile."

Before turning to the findings, it is important to note the few statistical data regarding Angola's economy and economic well being before 1985. This chapter tries to address these areas despite limited information. The rest of the chapter is structure as follows: Section I explores Angola's civil war and how it shaped its political economic history. Section II provides an overview of China's diplomatic and economic ties with Angola. Section III provides an evaluation of China's impacts and outcomes in Angola today. The three sections will be followed by a conclusion.

Section I: Background

A violent and what seemed eternal, civil war marks Angola's recent history. Throughout the 20th century, Angola suffered from both imperialistic conflict and internal ethnic. The violent conflict started when nationalists first took up arms against Portuguese colonial rule in 1961. A couple of years of peace followed from 1974 to 1975, but independence in 1975 cause war to strike again. A civil war continued as different ethnic powers fought for control, while international forces supported different groups. After 26 years, the war concluded in 2002, leaving the country with a broken infrastructure and economy, over 1 million lost lives, and over 3 million displaced in the cities.⁷⁹

Many forces of conflict led to Angola's twenty-six years of instability and violence. First, Portuguese colonialism failed to prepare Angola for a stable transition to independence. Second, three rival nationalist ethnic-regional movements endorsed violence against each other: the Communist MPLA (Movimento Popular para a

⁷⁹ World Bank 2007, 13

Libertacao de Angola), the anti-Communist UNITA (Uniao Nacional para a Independencia Total de Angola), and the FLEC (Frente para a Libertacao do Enclave de Cabinda). Though power was granted to the MPLA after independence, UNITA maintained a guerrilla war in the south and forces continued to fight for power.⁸⁰

Third, geopolitics and foreign interests in Angola procured instability. Before independence, Angola had an agricultural economy and was the fourth largest exporter of coffee in the world.⁸¹ Though oil had been part of Angola's landscape since 1955, in 1973 oil surpassed coffee as the largest export, accounting for a major source of revenue for Angola. In response to the high oil demands, the government established Sonangol as Angola's national oil company in 1976 to manage the oil industry on behalf of the government.⁸² After independence in 2002, oil brought high GDP levels to Angola, but destroyed reliance on other industries, raised political stakes, and financed a civil war. The war years are associated with foreign nations' involvement and interest in Angola's oil. The purchase of Angola's oil by foreign forces brought capital that assisted opposing ethnic groups against each other.⁸³

In the 1970s, as Angola tried to define its identity as a newly independent state, world conflicts deterred economic and political progress. International forces prolong the Cold War struggle in Angola, dividing and supporting different ethnic groups in terms of their involvement in either communists or non-communists ideologies.

By the end of the war in 2002, Angola suffered from high income and social inequality, a huge debt and lack of infrastructure and transportation. The flight of the

⁸⁰ World Bank, 2007, 12

⁸¹ World Bank, 2007, 13

⁸² World Bank 2007, 39

⁸³ Sogge 2007, 1

Portuguese had furthered complicated the situation. Over 90 percent of the residing Portuguese population (300,000) left when the nation declared independence, leaving empty most administrative and skilled jobs, and leaving behind a country unprepared to rule itself.⁸⁴ Angola turned to the use of inefficient economic management and poor economic policies, which shifted industries and levels of production.

Throughout the civil war years, China's and Angola's relations centered on defense and security. China's main role was through the support of different strategic political groups in Angola. During the anti-colonial struggle Angola's ruling party, the Movimento Popular de Libertacao de Angola (MPLA) depended on Chinese political and military support; After independence, China frequently switched support and military aid between FNLA and UNITA.⁸⁵ China's presence created more tensions between the political groups in power.

China officially established diplomatic ties and recognized Angola's independence in 1983. In October 1988, the first free trade agreement, the China-Angola Joint Economic Trade Commission, was created but ties remained weak and stagnant for a long period. The commission did not gather until December 1999, and only met twice after that in May 2001 and February 2007.⁸⁶

With the end of the civil war in 2002, Sino-Angolan engagement rapidly shifted towards financial and economic cooperation. While Angola resorted to its oil reserves for revenue and investments, China suffered from huge industrial changes that brought a need for natural resources. Though oil once provided the means to finance

⁸⁴ World Bank, 2007, 1

⁸⁵ Campos and Vines 2007, 2

⁸⁶ Ferreira 2008, 297 and Campos and Vines 2009, 2

the war, now it could restore Angola's economy by attracting foreign investors to invest in its oil industry and infrastructure.

Section II: China Returns to Angola

Today Angola's civil war is over. Inflation is falling, the financial sector is cleaner, millions of people displaced by conflict have returned home, and the oil industry is generating torrents of cash—the budget nearly double between 2005 and 2006 alone, to \$23 billion of dollars, as oil companies ramped up production, as oil prices rose, and as billion of dollars of new oil-backed credits rolled in from China.⁸⁷

China's investments in Angola, reliance on oil-led development model and high oil prices helps explain these results. When Angola decided to look at oil as a means to deal with the post-civil war crisis, China rapidly invested in the vulnerable oil-based development model. Since 2002, Angola has continued to expand the oil industry, used oil money, taken out loans and relied on China's capital to fund postwar reconstruction projects. Now that oil prices are high, Angola has China's encouragement and support to continue down this oil-led economic model. This has directly resulted in the exploration and extraction of Angola's oil, with record high oil discoveries in a short time span.⁸⁸

Though Angola's history demonstrates a state of fragility, violence, poverty, corruption, inequality and undemocratic procedures, for the last decade China has expanded cooperation and agreements on financial and economic cooperation. It has strengthened ties and promoted a "growth-growth" developmental strategy. Underlying this relationship is Angola's accessible oil wealth and investment

⁸⁷ Shaxson 2008, 184

⁸⁸ Alden 2007, 93

opportunities in a range of sectors.⁸⁹ China's strong presence in Angola is a result of China's goal of diversifying manufacturing facilities and securing raw materials for its development and future.⁹⁰ In return, China's new foreign policy goals strengthen relations and provides with rapid no-strings-attached aid packages and fast pace infrastructural projects. China's effort to invest and enforce friendly bilateral relations with Angola has to a certain extent benefited both nations.⁹¹

Political and Diplomatic Relations

Sino-Angolan strong ties are a result of a "perfect marriage of convenience," where China has the financial resources, firms, skills and knowledge to access Angola's growth project. In return, Angola possesses abundant petroleum to feed China's enormous need for natural resources. The two nations have formed a mutual advantageous partnership with no political preconditions and a pragmatic.⁹²

After African leaders meet in Beijing to establish dialogue and pragmatic cooperation and form the China-African Cooperation Forum on October 2000, by 2002, China offered Angola new credit lines and show interest in areas for future investments. In March 2004, Manuel Vicente, the CEO of Angola's national oil company Sonangol, visited China to enable a joint venture between Sonangol and China's largest oil company, the China National Petroleum Corporation (CNPC). A few months later the Angolan foreign Minister visited Beijing, and in September

⁸⁹ Alden 2007, 67

⁹⁰ Sutter, 2008, 84

⁹¹ Campos and Vines 2007, 2

⁹² Ferreira 2008, 299

2004 Yang Zilin, the president of China's Exim Bank, discussed the application of the first Chinese credit funds.⁹³

Increasing number of visits and conversations led to further engagement and opportunities for expansion of credit lines that granted China exploration rights for blocks of oil resources.⁹⁴ Cooperation and political ties became characterized by officials' frequent bilateral visits and the expansion of financial ties and cooperation.

Financial and Economic Cooperation:

It is not clear the total amount of financing China has supplied to Angola up to today. Since the end of the war in 2002, the amount of loans received by China is somewhere between \$5 billion to \$8 billion, without considering 2009 developments.⁹⁵ In return for sources of finance, tens of thousands of Chinese arrived in Angola to work in different projects, especially on brick-building plants to road projects.⁹⁶ Sonangol has worked along with Sinopec on different oil extractions projects designed through special financial arrangements.

China initially entered Angola with investments in small projects related to the rehabilitation of infrastructure.⁹⁷ To manage public investment projects in agro-business, infrastructure, telecommunication, and address international investments, the Angolan government created the Angolan National Reconstruction Program or Gabinete de Reconstrucao Nacional (GRN). The GRN managed credit facility by

⁹³ Ferreira 2008, 297

⁹⁴ Sutter, 321

⁹⁵ China Economic Review, 2009

⁹⁶ Reuters, "Angola Close to Signing \$1 billion Chinese Loan," Feb. 5, 2009.
<http://uk.reuters.com/article/idUKL505263520090205> (accessed Dec. 6., 2009)

⁹⁷ Vivian Foster, et.al. 2009, 26

organizing the large inflows of money invested. The GRN was responsible for the kick start of infrastructural reconstruction projects.⁹⁸ Sino-Angolan financial relations took full strength in late 2003 when Angola's Ministry of Finance and China's Ministry of Trade agreed on economic and commercial cooperation. Ever since financial cooperation has been mandated by China's financial assistance to GRN, with China's Exim Bank providing loans for infrastructural projects.

The Export-Import Bank of China (Exim) is one of the world largest providers of credit and a significant source of credit to African countries.⁹⁹ Exim Bank credit loans are often associated with broader political aims. The first agreement that officially enabled Ex-Im Bank lines of credit in Angola took place on March 21, 2004 to fund the repair of damaged infrastructure from the civil war.¹⁰⁰ The Angolan government's willingness to open up the country to Chinese investments has meant the entrance of over \$5 billion of loans from China's Exim Bank since 2004. Loans have been targeted for the construction of oil refineries, a new international airport, diamond mining facilities, and expansion of the fisheries industry.¹⁰¹ Some of Sino-Angolan agreements are explained below and summarized in Table 1.

On March 21, 2004, Angola and China approved the first \$2 billion financial package for public investments projects related to energy, water, health, education, communication, and fisheries.¹⁰² The loan was divided into two phases of \$1 billion each, one granted in January 2005 and the other to be used after March 2006. In return, Angola supplied China with 10,000 barrels of Angolan crude per day. In May

⁹⁸ Campos and Vines 2007, 5

⁹⁹ Moss and Rose 2006

¹⁰⁰ Vivian Foster et. al. 2009, 26

¹⁰¹ Alden, 2007, 67

¹⁰² Ferreira 2008, 300

2007, China provided an extension of \$500 million to finance “complementary actions” of the first phase projects.¹⁰³ Much before this though, in June 2006, China announced the opening of a major line of credit of \$2 billion, along with a Memorandum of Understanding for future credit.¹⁰⁴ In September 2007, Angola’s finance minister, Jose Pedro de Morais, and Chinese Exim Bank President, Li Rougu, agreed on another oil-backed loan of \$2 billion to finance projects for health and education and construction of schools and hospitals.¹⁰⁵

In 2005, the China International Fund (CIF) extended a major line of financial assistance of \$2.9 billion for Angola’s postwar reconstruction effort. The China International Fund enforced the aims of South-South cooperation and succeeded in forging better relations and visions for future projects.¹⁰⁶ Another \$3 billion two-year loan was negotiated with provisions for building the oil refinery at Lobito.¹⁰⁷ By 2009, new talks insisted on China’s issuance of a \$1 billion loan to Angola to help develop the country’s agricultural sector.¹⁰⁸

Ever since, credit lines were opened, Sinopec Group acquired its first stake in Angola’s oil industry, acquiring 50 percent the operated by BP Block 18. To secure and explore further stakes on blocks, the Sonangol Sinopec International (SSI) was created as a joint venture between Sonangol and Sinopec.¹⁰⁹

¹⁰³ Campos and Vines 2007, 4

¹⁰⁴ Ferreira 2008, 301

¹⁰⁵ Campos and Vines 2007, 4

¹⁰⁶ The China International Fund Limited, <http://www.chinainternationalfund.com/> (accessed Dec. 10, 2009)

¹⁰⁷ Alden 2007, 68

¹⁰⁸ APF, “Angola Wins New Billion-Dollar Loan from China,” March 12, 2009.

<http://www.google.com/hostednews/afp/article/ALeqM5i0hpgnhmj3GYfBFS8IbzAJ1Wdf5w> (accessed Dec. 15, 2009).

¹⁰⁹ Ferreira 2008, 306

Table 1: Financial Relations between China and Angola:

Date	Amount	Purpose	Forms of Payment
March 2004	\$2 billion	For projects of energy, water, health, education, communication and public work	Loan: payable in over 12 years with three years of grace period. Agreement to supply with China with 10,000 barrels of Angolan crude per day
2005	\$2.9 billion	(CIF) for financial assistance for postwar reconstruction	Granted by the China International Fund
June 2006	\$2 billion	Telecommunications and fisheries sectors	Unclear
May 2007	\$500 million	To finance the continuation of the first project set in March 2004	Unclear
September 2007	\$2 billion	Finance 100 projects related to health and education	Oil-backed load, 15 years for repayment
March 2009	\$1 billion	Developing agricultural sector	Loan unclear



China's reliance on oil and Angola's urgent shift to focus on reconstruction and development has strengthened commercial relations. In 2006, Angola became China's leading supplier of oil, providing about 15 percent of all Chinese oil imports.¹¹⁰ In the year 2000, bilateral trade between Angola and China exceeded \$1.8 billion, and increased considerably to \$12 billion by 2006. By 2008, Angola was China's largest trading partner in Africa, with bilateral trade reaching \$25.3 billion.¹¹¹ China's dependence on Angola's oil peaked in 2008, but decreased slightly in 2009.

Imports from China to Angola have increased about 138 percent from 2005 to 2006, making China the second-largest supplier to Angola.¹¹² In 2008, Portugal

¹¹⁰ Ferreira 2008, 302

¹¹¹ China Daily, "Angola China's Largest African Trade Partner." January 19, 2009. http://www.chinadaily.com.cn/china/2009-01/19/content_7407941.htm (accessed Dec. 10, 2009).

¹¹² OECD 2009, 129

continued to be Angola's principal import sources, by receiving 19.4 percent of Angola's imports with China closely behind receiving 14.8 percent of imports.¹¹³ By 2008, China surpassed the US as the leading export destination of Angola's goods, with 34 percent of Angola's goods exported to China, while only 27 percent exported to the US.¹¹⁴ Despite growing Chinese influence, the US has maintained oil interest in the region, keeping economic relations through oil exportation and aid.

Angola Mode:

The intensity of oil-back payments set by China in Angola has led to the newly coined term "Angola mode." "Angola mode" or "resources for infrastructure," identifies those financial agreements where China is repaid for credit lines or loans through monthly oil payments.¹¹⁵ Though it carries the name of "Angola," the term identifies any form of relation China has with foreign countries that provide oil backed payments for Chinese finance. Though it is a beneficial tool for exchanging countries, there are unstable features. Under the "Angola mode:"

Funds are not directly lent to the recipient country; instead, the Chinese government will mandate a Chinese construction company (with credit from the China Exim Bank) to undertake the construction works, following the approval of the recipient country. Then, in exchange for the infrastructure provision, the borrowing government will give the right to mine natural resources to a Chinese company operating in the field of natural resources (mostly oil or minerals), through the acquisition of equity stakes in a national oil company or through acquiring licenses for production.¹¹⁶

The "Angola mode" is China's unique form of economic cooperation to gain

¹¹³ Alden 2008, 303

¹¹⁴ Alden 2008, 303

¹¹⁵ Vivian Foster et. al., 55

¹¹⁶ Reisen and Ndoye 2008, 36

security over oil resources. The China Ex-Im Bank uses this exchange method for negotiation with countries that cannot provide financial guarantees to back their loan commitments. One benefit is that it allows countries with abundant resources but limited credit worthiness to sell their natural resources in exchange for infrastructure projects. It also limits opportunities for corruption by the recipient country. Though it has become a beneficial form of exchange with nations lacking credit, it is difficult to evaluate the level of transparency and the financial terms of the “Angola Mode.” Because oil is a political good dependent on demand and price changes, it is hard to evaluate the price information and whether agreements under the “Angola Mode,” can be beneficial to oil-rich nations. Until recently, Angola’s oil exportation has benefited from the rise of oil prices and domestic oil production, but negotiation gains are threatened by price fluctuation.

Today oil accounts for about 95 percent of Angola’s exports.¹¹⁷ High dependence on oil production and exportation revenue has led to concerns regarding the enforcement of sustainable practices. Most of Angola’s oil future lies in deep offshore waters in mature fields that are set to decline unless new fields are found.¹¹⁸ The alienation and distance from the mainland has many consequences for how the industry evolves. The separation of the oil industry from the common people has fewer impacts in their daily lives and hides environmental concerns. Angola’s reliance on oil production has growth considerably from 172,000 bpd in 1974 to 2.015 million bpd in 2008.¹¹⁹ In 2007, Angola joined OPEC and in 2008 was

¹¹⁷ Campos and Vines 2007, 7

¹¹⁸ World Bank 2007, 40

¹¹⁹ CIA, Angola

required to cap the production to no more than 2 million bpd. The financial crisis forced Angola to comply when in January 2009 Angola had to cut production to 1.6 million bpd in response to plummeting oil prices.¹²⁰

Section III: China's Impacts

China's role and interest in oil has improved Angola's bargaining power, increase its strategic importance, speed up development through investments in infrastructure, endorsed health and education initiatives, and opened the door to new businesses and entrepreneurs. The arrival of Chinese business marks the growing Chinese demographics in the area and defines much of the local economic growth. However, Angola still suffers from corrupted and weak governance, with poor incentives for expanding local business opportunities.¹²¹

China's Foreign Policy in the Developing World

The implications of China's foreign policy determine the level of progress and impact in Angola's development. Despite China's positive foreign policy that ideally advocates "a pragmatic friendship among governments to push for international cooperation and mutual respect," many fears predominate about China. These fears question China's lack of ethical code, and the possibility of China turning into Africa's next colonial power in control of resources while and not stimulating local

¹²⁰ US Department of State, "Background Note: Angola"

¹²¹ World Bank 2007, xxxviii

African economies.¹²² In African countries these concerns are enforced by past negative experience with imperial powers who extracted resources. However, unlike the West, China has no legacy of imperialism in African nations.

China has kept strong to its foreign policy goals of promoting oil strategy initiatives, while sponsoring “growth-growth” development plans that have benefited economic growth. China has also benefited the social well-being of the Angola people by investing in schools, fixing roads, opening abandoned factories and bringing health specialists to help with local health problems.

China has helped to provide Angola with financial independence. China does not exert pressure nor expects standards of accountability, unlike the IMF. By the end of the civil war, the IMF wanted Angola to perform well in a staff-monitored program for three trimesters in order to be eligible for financial support.¹²³ China provided with rapid loans and deals with few provisions. China also responded to Angola’s interest in associating with a new non-Western nation.¹²⁴ As Angola seeks new foreign relations, “China brings a model of economic recovery...able to work without the involvement of foreign advisors, institutions or bilateral mentors.... looking back on half a century of failed Western-led efforts... the new model provided by Beijing is a refreshing alternative.”¹²⁵ Thanks to China’s offering and benefits, Angola has been able to cope with the devastating results of the civil war.

¹²² South Africa the Good News, “China in Africa: Is the continent being re-colonized?” (May 9, 2008) http://www.sagoodnews.co.za/newsletter_archive/china_in_africa_is_the_continent_being_re-colonised_.html (accessed Oct. 12, 2009)

¹²³ Campos and Vines 2007, 11

¹²⁴ Brautigam 2008, 68

¹²⁵ South Africa the Good News, “China in Africa: Is the continent being re-colonized?”

Angola's and China's interactions center on a sense of understanding and partnership. Though different in size and history, Angola and China face similar issues like high levels of poverty and an opaque political system and markets.¹²⁶ In addition to this sense of connection, China has also offered to set long-term ties, and enforce cooperation on mutual development through the South-South cooperation and the Forum on the China-Africa Cooperation (FOCAC).¹²⁷

It must remain clear that Sino-Angolan relations are pragmatic and strategic.¹²⁸ Though China's foreign policy promises "cooperation" and "partnership," nothing prevents Chinese oil companies from partnering with some of the region's most brutal regimes. China has not been motivated to show any interest in good governance, human rights issues, environmental issues, or transparency.¹²⁹ Therefore while China's foreign policy has succeeded in creating great economic growth and pushed for cooperation that is mutually beneficial, it has failed in other areas to implement necessary steps to help the Angolan people's suffering. Beneficial long-term impacts depend on the transfer of knowledge and investments and improvements of institutions, which are currently not growing entirely from this process.

Commercial lines can be bended as an over populated China needs to secure resources and jobs for its people. For example, for many of the infrastructural projects and oil jobs China has invested and designated, it has brought thousands of workers to do these jobs, closing the doors for new employment opportunities for local

¹²⁶ Alves 2008, 80

¹²⁷ Ministry of Foreign Affairs of the PRC, "Hu Jintao Holds Talks with Angolan President Jose Eduardo dos Santos," Dec. 18, 2008. <http://www.mfa.gov.cn/eng/wjb/zzjg/fzs/xwlb/t526951.htm> (Accessed Nov. 23, 2009)

¹²⁸ Campos and Vines 2007, 11

¹²⁹ De Olivera Soares 2008, 108

people.¹³⁰ Another issue pertains to the lack of investments in cultural and language understanding. Much of this has to do with Chinese workers seclusion as they live in specially-built compounds, separated from the locals, with linguistic and cultural barriers.¹³¹ Other negative areas of Chinese foreign policy are felt within China's centrality in establishing its own contract provisions, and Angola's inability to promote efficient projects by itself.¹³² Many projects have failed due to the opaqueness and bad management related to lack of centrality and communication with the Chinese.¹³³ Angola's lack of transparent democratic processes and China's rapid way of doing business are both problematic for Angola's progress.

It is important to evaluate these forces against the good and bad brought by the West in the past. My belief is that China is pushing for a strong foreign policy that benefits greatly Angola; however Angola's weak governance, a result of historical failures and Western involvement in the politics and economics, lags progress.

FDI and Economic Development

Since 2002, China FDI has played as special role in Angola's economic development, allowing for an era of sustained peace and exceptional economic growth. Within a few years Angola's GDP levels reached extensive growth rates of 20.6 percent in 2005, which lowered to 14.8 percent in 2008.¹³⁴ China understood that in order to help Angola rehabilitate its economy, it needed to exempt them from their

¹³⁰ Johnson 2010

¹³¹ Jiang Shixue 2008, 38 and BBC News "In pictures: China in Angola" http://news.bbc.co.uk/2/shared/spl/hi/picture_gallery/07/africa_china_in_angola/html/6.stm(March 18, 2010)

¹³² Campos and Vines 2007, 5

¹³³ Campos and Vines 2007, 6

¹³⁴ World Bank, "Angola: GDP Growth (annual %)"

own debts and enable a duty free relation system.¹³⁵ China's positive bargain offerings are obvious by looking at contracts, its low interests rates and long grace period for repayment. The Chinese also offer fast and cheap services of construction, incomparable to competitor prices. China's willingness to take risks in return for natural resources benefited Angola's economic growth, and fostered incentives for other nations to invest, while pushing Angola to open up to more FDI.¹³⁶ In return, Angola has granted access to construction and civil engineering contracts to Chinese state-owned companies.

Though outstanding GDP levels may say something about economic growth, the same assumption cannot be used to determine economic development. FDI reduces inequality when "FDI brings increased technological and organizational spillovers to developing countries."¹³⁷ Though China has brought industrial changes to the oil industry, much has remained within their areas, and though spillovers may have spread, the Angolan government has not taken advantage of them. Much has to do with Angola's extremely low levels of governance. Angola still maintains low rates in government effectiveness, rule of law, and high corruption.¹³⁸ For this reason, despite the immense increase in GDP, there has been little poverty reduction.¹³⁹

Issues of inequality and other economic well-being indicators against economic growth can be evaluated just by looking at Angola's Human Development Index.

Despite a high GDP per capital PPP of \$5,500, its Human Development Index

¹³⁵ China Daily "Angola China's largest African trade partner," January 19, 2009
http://www.chinadaily.com.cn/china/2009-01/19/content_7407941.htm (accessed Oct. 28, 2009)

¹³⁶ Campos and Vines 2007, 8

¹³⁷ Ocampo 2009, xix

¹³⁸ World Bank Governance Matter

¹³⁹ Campos and Vines 2007, 12

remained low at 0.56 (closer to 1 means better human development, closer to 0 weak human development).¹⁴⁰ Though Angola has one of the highest GDP's in the region, GDP changes has not led to improvements in human well-being. However, very little information is published on evaluating inequality, the only GINI level measured was in the year 2000, where Angola index was 59. The same goes for income disparities, in the year 2000, about 45 percent of the income was in the hands of the top 10 percent of the population. Inequality is markedly pronounced outside the capital, it takes a "visit a rural village or walk into one of Luanda's desperate shanty-towns, and you will see that the Angola oil-fired miracle is hollow."¹⁴¹

Other issues include Angola's bad management and issues of financial integration. It is estimated that from 1985 to 2004 the level of capital flight totaled 216 percent of the recorded GDP, making Angola one of the worst cases of African financing hemorrhage.¹⁴² Quantities of capital flight and uncollected tax revenues are not known with precision. Greater financial integration then does not improve long-term economic growth as much capital leaves Angola. While these rates may have considerably decreased in the last years, China's lack of concern for democracy and transparency worsens this issue.¹⁴³

Despite great process and successful FDI, development does not apply to all sectors of the economy. One can define Angola as combining two opposite approaches of FDI development: the modernization and the dependency state. The *modernization* state approach follows neoclassical economic practices that create

¹⁴⁰ Human Development Report 2009: Angola <http://hdr.undp.org/en/statistics/> (accessed Feb. 20, 2010)

¹⁴¹ Gaydamak 2008, 185

¹⁴² Sogge 2009, 8

¹⁴³ Campos and Vines 2007, 7

positive FDI, while this is true to some extent Angola still acts under the *dependency* approach where China acts as the “developed” nation that continues the oil industry underdeveloped model. With about 95 percent of its total revenue coming from the oil industry, Angola is failing to conduct long-term development changes, and China is hindering progress by investing solely in Angola’s oil. The Chinese companies are not necessarily bringing direct investments that maintain a system of dominance; however, they are investing in the oil industry, unreliable for long-term development.

There is no doubt that China has been an important investor and commercial partner, but long term-impacts need to be secured through improved management of revenues.¹⁴⁴ China has the resources, technology expertise and good and political will; Angola needs further assistance to eliminate barriers of other areas of development.

The Oil Curse:

Despite all fears, Angola needs to protect itself against its legacy of the Oil Curse. Dependence on oil puts nations in a state of vulnerability, where “oil acts like heroin: it feels good, but the final result is catastrophic.”¹⁴⁵ At many times it can cause problems of land ownership, corruption and lack of development in other sectors. Since 1973, oil has been an important source of revenue but often played a problematic role in Angola’s politics, economics and foreign relations.¹⁴⁶ Oil allowed the war to continue by feeding with capital opposing ethnic parties. Oil also allowed other nations to extract resources and gain capital, explaining the ludicrous capital

¹⁴⁴ Goldstein, Andrea, Nicholas Pinaud, and Helmut Reisen 2008, 49

¹⁴⁵ Sogge 2009, 10

¹⁴⁶ Hodges 2004, 6

flight rates found in this country. It also changed Angola from a functional dependent agrarian economy to that of a non agrarian economy with displaced populations in urban areas, and few opportunities for employment. Though some Angolans have tried to return to farming as the nation picks up itself from the ashes of war, the country buys most of its food from abroad.

China's FDI in the country has endorsed much economic improvement, but with few investments outside the petroleum sector. The problem with petroleum is that it absorbs over three-quarters of all national and international investments, but it only generates about one percent of all national employment.¹⁴⁷ The oil industry employs about 20,000 Angolans, one of seven hundred people. It also feeds the high salaries of corrupted officials who live a very wealthy life.

Another concern is the building of extreme confidence in the oil sector, leading the nation to rely too much on its exports. Today oil accounts for 95 percent of exports and 83 percent of government revenues.¹⁴⁸ This dependence on oil has led to question the possibility of *dutch disease*, when a commodity boom leads to temporary rise in prices and revenue that encourages borrowing and may leave the country with an unsuitable debt burden when prices decline.¹⁴⁹

Angola is at risk of many other challenges when dealing with China, a nation that is a swing producer, exporting when prices are high and stocking when prices are not at favorable rates. Angola is subjected to the volatility of prices when China's raw

¹⁴⁷ Sogge 2009, 6

¹⁴⁸ US Department of State: "Angola"

¹⁴⁹ Hodges 2004, 3

material demands may shift from extremely high levels to none.¹⁵⁰ A swing in prices of commodities along with China's and other countries interest in one commodity have forced Angola to rely primarily on one sole commodity. Lack of diversification will turn into an issue when Angola finds itself in a situation with low commodity prices and lack of resources. Lack of diversification is a problematic issue especially as Angola enters a serious downturn in oil production after reaching its peak in 2010. Angola needs to find other ways to sustain economic growth.¹⁵¹

Angola Today

Despite the oil boom contributions and shift to one of the world's fastest-growing economy, Angola still ranks in the bottom 10 percent of most socioeconomic indicators.¹⁵² A view of Angola today shows a nation under the irony of extreme economic growth and extreme poverty. The nation is plagued by high levels of inequality and an expensive cost of living. To some extent, economic development has meant thousands of poor becoming victims of being swept away from their shanty towns to replace their homes with marketplaces and shopping centers.

It is hard to understand how a country so rich in oil and diamonds and with such a fast-growing economy can still have people living in bad conditions. Benefits, fears and challenges brought by Chinese loans and investments in oil question to what extent has Angola's destiny been shifted, if at all.

¹⁵⁰ Goldstein, Andrea, Nicholas Pinaud, and Helmut Reisen. 2008, 38

¹⁵¹ Sogge 2009, 6

¹⁵² US Department of State: "Angola"

Angola today is one of the larger producers of oil in Africa, pouring billions into the government, and doubling the country's national budget from \$13 billion to \$25 billion.¹⁵³ Growth has allowed for huge declines in debt. New investments and assignments are being placed to find the larger deep-water reserves. Many goals have been set and accomplished, such as the ones set on doubling production from 1.4 to 2.8 million bpd, a reachable goal that was nearly accomplished in 2008.¹⁵⁴ Angola is important not only to Africa, but also to OPEC, standing today as the third largest producer in the group, after Saudi Arabia and Iran.

Unfortunately, jobs in oil production account for less than 1 percent of employment, and though the common people notice the country is changing, few have received any benefits. In an interview by a news agency, a civilian commented: "I can see the country is improving, but I still can't find a better job...I know there's a lot of money being made but if it does not go to poor people like me, then where does it go?"¹⁵⁵ Improvements in the economic wealth being of the society are few.

Incredible discoveries of 55 oil reserves in northern off shore of Angola in only 8 years (1996-2003), along with 8 discoveries of oil reserves in deep-water blocks have boosted false confidence of fertile oil reserves. However, production rates are expected to peak very soon, with production rates to hit 1.2 million bpd by 2020, and close to zero by 2030. If the nation continues at this rate not only will it be deprived soon from its number one source of income, but it may also resurge into war. One

¹⁵³ BBC News, "Angola: China's African foothold," (June 20, 2006) <http://news.bbc.co.uk/2/hi/africa/5080626.stm> (accessed Oct. 24, 2009)

¹⁵⁴ Mills 2008, 130

¹⁵⁵ AFP. "Angola, the Fastest Growing Economy in the World." (Sept. 03, 2008) <http://www.videocrux.com/video/6049/Angola-the-fastest-growing-economies-in-the-world> (accessed Oct. 22, 2009)

possible solution is the reactivation of agricultural activity. Angola is well endowed with untapped agricultural resources that are ready to be developed.¹⁵⁶

China has played an important role in Angola's development but it is hard to evaluate solely China's impact. Issues of transparency and Angola's own governmental incompetence prevent a clear evaluation of China's role, marking it harder to determine the whole picture and forces playing along to led to such tremendous growth.

Though Angola represents one of the fastest growing economies in the world, it will take more than commercial relations with China and dependence on oil to respond to 48 percent unemployment levels.¹⁵⁷ Chinese investments alone cannot restructure such a society facing the second-highest rate of infant mortality in the world, where third of the children under the age of 5 die.¹⁵⁸ Not all trust and hope can be in China's hands, Angola needs further assistance to improve.

Forces preventing Angola from advancing and taking advantage of its new economic growth is the predominance of corruption and inequality. Angola's lack of transparency regarding how the money is spent, and China's lack of interest in getting involved in any of these affairs, obscures a problem that can be solved with better governance. Angola has the ability to do better and improve its situation, but it has tended to ignore the importance of social improvement. Today Angola needs to take advantage of its economic growth to deal with issues such as income inequality and

¹⁵⁶ World Bank 2007, xxxvii

¹⁵⁷ World Bank, "Angola: GDP growth rate" (November 20, 2009)

¹⁵⁸ Natanson 2009

poverty. If not it will be threatened by the ethnic tensions left behind from the war which may further social instability and at any moment spur civil unrest once again.

Conclusion

In his 2008 visit to China, Angola's President dos Santos said, "The cooperation between the two countries is mutually beneficial...The Angolan people and government are grateful for China's support on Angola's defense against foreign aggression and efforts for national liberation and reconstruction work."¹⁵⁹ An evaluation of the role of China in Angola confirms dos Santos views. Chinese investments have extended to infrastructural development to other fields of science, technology and culture, as well as gain of importance in the world arena. In general, China's impacts have kept strong to its original foreign policy goals, where mutual development and partnership is important for development. However, complying with its foreign policy goals does not assure that all impacts are sustainable.

China's FDI has promoted a great level of economic development that is not long-term sustainable. It may conduce to great economic growth, but enforce dependence on a dangerous industry often marked by the Oil Curse. Nothing is preventing this from happening in developing countries with such a low governance rate. Thus FDI does not entirely sponsor real economic development and may conclude in the complete downfall of the oil industry.

Angola is different from Ecuador. Angola's history has been marked by political instability, economic backwardness, years of wars and lack of safety and

¹⁵⁹ Ministry of Foreign Affairs of the PRC, "Hu Jintao Holds Talks with Angolan President Jose Eduardo dos Santos" (December 18, 2008).

peace. Nevertheless, considering the discussed theories and methods of analysis, Angola is a model and guide to study China's role in oil rich developing nations. It is a prospect for comparative study and scenario building. Despite the differences, Angola and Ecuador have much in common in relation to economic experiences with Western powers, and in issues of oil production and development.

Overall, Chinese engagement in Africa can be summarized as a combination of domestic Chinese dynamics, desire to expand into new markets, and international political factors. These factors are the ones that will similarly be found in Chinese relations into Ecuador. Angola is for China a strategic pursuit of resources and attempts to ensure raw materials supplies for growing energy needs, but in return China has been a unique contributor of funds and financial resources. It is important then to remember that "China's lunge for resources, they remind us, is not directed solely at Africa but is taking place right across the globe."¹⁶⁰ As the US continues to paying attention to other parts of the world, China is driving its influence into countries US is ignoring, like Ecuador.

As we will see in the upcoming chapter there are many lines of comparison and contradiction that help evaluate China's impacts. Angola's situation and story provides guidance with which to evaluate whether China is a threat or ally in the development of Ecuador's economy.

¹⁶⁰ Snow 2008, xviii

Chapter IV:

China in Latin America: Ecuador

Introduction: Tracing the Past to the Present

How, why, when, did China get involve in Ecuador? What are details behind China's involvement in Ecuador? After investing in several African countries, China has begun to extend its influence to nations in Latin America. This is perfect timing for Sino-Latin American relations. As China begins to diversify its oil interests and find new strategic partners, many oil-rich Latin American nations are undergoing center-leftists reforms, working to further develop their economy and politics, and seeking to shift away from West ideological and political hegemony. To achieve these goals Ecuador is expanding collaboration with China. This chapter seeks to provide an overview of Ecuador's economic development to parse out possible answers to the "how, the why, and the when" of China's investments in Ecuador.

Though Latin America provides less than 7 percent of China's petroleum needs, there are numerous reasons for rapid engagement. The first reason is China's hunt for oil. The Latin American region is important to China because of its oil reserves, which are considered to be the second largest petroleum reserves in the world. The second reason speaks to Latin America's current political situation, both internally and externally. The rise of leftist governments is transforming foreign policy and terms of trade with new partners. In recent years, despite the region's geographical, historical, and commercial ties to the US, its most influential neighbor has paid little

attention to the area. President Bush and his administration treated Latin America as a region of low priority and President Obama has yet to visit a Latin America country beyond Mexico. The third reason is about Ecuador's strategic position in Latin America and the Pacific coast.

In Chapter III, we investigated how China's engagement through finance, trade and investment promoted a variety of outcomes in Angola's economic development and well-being. This chapter looks into Ecuador's economic growth from three different time periods: before the arrival of major Western FDI from 1911-1970, to a time of strong Western presence 1970-2001, and today. Background concepts covered in this chapter provide empirical and statistical data that is essential to the scenarios we will construct in the next chapter that consider how China's FDI may further impact Ecuador's economic development.

Section I: Ecuador and the initial stages of Western Investment 1911-1970

Unlike other Latin American nations, the development of Ecuador's agriculture sector, and other parts of the economy, had little influence from foreign capital until World War II.¹⁶¹ After the war, investments arrived through three different mechanisms: investment in the banana and fishing industries, loans by finance agencies such as the World Bank, and FDI in public utilities. However, before WWII,

¹⁶¹ Mosley 1991, 412

the West had already settled in the oil industry. The period 1911-1970 marked the oil extraction and exhaustion of the peninsula of Santa Elena by Western nations.¹⁶²

On March of 1920, Henri Wilhelm August Deterding, the so-called “Napoleon of Petroleum,” declared British influence over Ecuador’s resources by entering the peninsula of Santa Elena.¹⁶³ The original legal structure of the oil industry was set by the transnational British Petroleum Comp, la Anglo. Of the profits made, la Anglo solely granted the Ecuadorian state 1 percent of profits.¹⁶⁴ In the 1920s, the Standard Oil of New Jersey brought American influence into the new industry. The interactions between the Royal Dutch Shell and the Standard Oil of New Jersey, partnered with the Ecuadorian government to influence the politics of this period.

Politics and Economics

Multinational firms’ interests contributed to the booms and busts of major primary industries. In 1921, Ecuador granted the first 1.6 million hectares of the *Oriente* to the Standard Oil to explore the Amazon region.¹⁶⁵ At this time, Ecuador’s economy was faring well, with cacao production and a liberal government.¹⁶⁶ However, by the mid 1920s, the nation became more unstable due to decreasing value of cacao, and political wars of conservatives and liberals. In July 1925, the military overthrew the government, and from 1931-1948, nineteen men served as presidents.

¹⁶² Guerra 2003, 11

¹⁶³ Galarza Zavala, 1974

¹⁶⁴ Galarza Zavala, 87

¹⁶⁵ Martz, 46

¹⁶⁶ *Encyclopedia of Latin America: History and Culture 2n edition*, 44

In 1937, Dictator Federico Paez passed a national petroleum law that opened the *Oriente* to foreign interests. It granted a lease of 10 million hectares to Royal Dutch Shell for exploration, ousting Standard Oil from the region. The Royal Dutch Shell used their concessions to explore and establish Shell Mera, a small town in the Amazon basin that had small importance and was abandoned in 1947. Though Shell's exploration had little significance, ousting Standard Oil from the region did not. In response to the exclusion, Standard Oil, which had influence in the lands between the border of Peru and Ecuador, financed the Peruvian military and encouraged border belligerence. As a result, Ecuador lost tremendous land to Peru in 1941. This loss of territory pushed Ecuador to maintain territorial integrity, to take urgent action to develop that territory, and to sustain claims to national sovereignty of the land.

Fortunately, the banana boom in the 1950s brought economic and political stability.¹⁶⁷ After 1948, three governments completed their terms. In the time being, oil did not fare well, and foreign oil companies became frustrated over the lack of progress in their efforts to explore new oil-rich regions. President Galo Plaza Lasso declared that "the Oriente is a myth," and that it lacked natural resources.¹⁶⁸ In 1967, this myth was disproved when the Texaco Gulf consortium discovered vast amounts of crude in the *Oriente* Sucumbios. Texaco's discoveries arrived as Ecuador entered a period of political stability led by the rule of a military junta from 1963 to 1966.¹⁶⁹

The election of Jose Maria Velasco Ibarra restored democracy in 1968. Ibarra had already been president five times, and had been unpopular as the representative of

¹⁶⁷ *Encyclopedia of Latin America: History and Culture 2n edition*, 45

¹⁶⁸ *Encyclopedia of Latin America: History and Culture 2n edition*, 52

¹⁶⁹ *Encyclopedia of Latin America: History and Culture 2n edition*, 46

an administration that raised taxes, and closed universities of opposition. In 1970 matters got worst when Ibarra assumed dictatorial powers.¹⁷⁰ However the opposition gathered and in February 19, 1972, General Guillermo Rodriguez Lara headed an effective coup d'état, taking Ibarra out of power for the last time.¹⁷¹

Economic Growth and Well-being

Western presence in the oil industry led to one of the first Oil Curse outcomes, the depletion of the Santa Elena Peninsula. During this period of time, Ecuador expanded and relied heavily on primary commodities, mainly cacao and banana. These commodities in turn determine the extent of economic growth. High unemployment and political instability correlated with community bust periods. Thus Commodity exportation booms determined Ecuador's economic growth. Oil brought little impact into these two factors with limited production. However, the interplay of oil in sponsoring the Peru border war had many political and economic implications.

In the 1960s: "Ecuador's dominant classes were still unable to effectively compromise their divergent interests; the agro-exporting, industrial, and financial sectors could not form a monolithic bloc. A decline in coffee and cacao prices had set in, and living conditions worsened."¹⁷² The economy suffered from declines in commodity price, low per capita income, low wages, and high unemployment. In 1969, President Velasco Ibarra allocated new blocks for exploration and renegotiated the Texaco-Gulf contract to promote new terms that enforced social well-being

¹⁷⁰ Gerlach, 35

¹⁷¹ Gerlach, 26

¹⁷² Martz, 69

practices. The terms stated that Texaco-Gulf had to “return 930,000 hectares, increase of royalties to 11.5 percent and had to agree that 80 percent of administrative personnel and 95 percent of workers be Ecuadorian.”¹⁷³ It was not enforced.

Economic growth remained low, similar to other Latin American nations in 1960s.¹⁷⁴ GDP levels increased by 1.5 percent in 1961, and continued with low and steady growth rates throughout the rest of the decade. However, the sudden discoveries of Texaco in 1967 will determined a new period of great economic growth led by oil, a political good that became the main determinant of Ecuador’s growth, and it remains so, even today.

Section II: Western investment in Ecuador 1970-2001

Western engagements with Ecuador during this period strengthen the present economic development model based on primary good revenue dependence that shape Ecuador today. It brought along a period of great growth and expansion, but followed by Oil Curse outcomes and decades of instability, slow growth and pressing levels of inequality. Looking back at the start of this period, Western engagement in Ecuador was viewed positively.

The discovery of oil sites in 1967 offered Ecuador new opportunities for expansion and progress.¹⁷⁵ In the 1970s oil and major Western investments brought Ecuador great changes and development. The government income quadrupled and GNP increased from 2.2 billion in 1971, to 5.9 billion in 1977.¹⁷⁶ The interplay of

¹⁷³ Martz, 59

¹⁷⁴ World Indicators, World Bank

¹⁷⁵ Mosley 1991, 412-413

¹⁷⁶ Martz , 4

politics and changes in oil industry determined the sudden economic growth. Western engagement arrived to take over increasing opportunities in the oil industry. Rapid expansion to the oil rich Amazon allowed Ecuador to focus on oil exploration and benefit from the 1974 and 1979 oil price shocks. During 1970s and early 1980s, oil revenues surpassed the banana industry and represented about 70 percent of GDP.¹⁷⁷

Politics and Economics

The military ousting of President Velasco Ibarra in 1972 brought a new age of petroleum in Ecuador. By June 1972 Petroleum began flowing the 312-mile trans-Andean pipeline from the *Oriente* across 12,000-foot mountains to the Pacific.¹⁷⁸ General Rodriguez Lara coup arrived at a time when oil overnight provided with one-half of government revenue, but politically things remain the same, “The coup amounted to the replacement of an unpopular and ineffective civilian dictatorship with a somewhat unpopular and only partially ineffective military one.”¹⁷⁹

Oil production rose from 27 million barrels in 1973 to 73 million barrels in 1978. Exports rose from \$195 million in 1971 to \$1.4 billion in 1977.¹⁸⁰ In response to oil demand Rodriguez Lara began the *Corporacion Estatal Petrolera Ecuatoriana* (CEPE) to administer the exploration, commercialization and industrialization of petroleum. As a result of the growing oil demand and role in international business, Ecuador joined OPEC in 1973, the second smallest producer among the thirteen members, moving about 200,000 bpd.

¹⁷⁷ Martz, 3

¹⁷⁸ Gerlach, 33

¹⁷⁹ Pineo, 179

¹⁸⁰ Pineo, 179

The oil industry fed the military state with a large share of profits from oil exportations throughout 1972 to 1980. The regime allocated about 50 percent of its oil royalties to the military, an estimated \$250,000 daily, reaching 98 million yearly in 1976.¹⁸¹ The military had high expectations and goals of reforms for the common people under the program: “revolutionary nationalism.”¹⁸² Oil granted Quito with their own source of money for social reforms. Following 1972, the government accelerated public expenditures at an astonishing rate of 12 percent annually.¹⁸³ Many changes helped the poor, but many were short-lived.

The military government endorsed a period of spending, high reliance in oil, and development of the armed forces. Once Ecuador’s oil revenue and own capital proved insufficient to sustain modernization plans, the military regimes began to borrow from abroad and use oil reserves as loan guarantees. The foreign debt swelled during the 1970s, from \$209 million in 1970 to \$4,167 million in 1980.¹⁸⁴ Over confidence in oil incoming revenue led to ostentatious consumption, thus in order to benefit from the subsidized domestic fuels many imported cars they could not afford.

Everyone overestimated the success of the state, and after the Supreme Court council took power from 1976-1979, oil reliance led to economic collapse. Oil prices fell, and oil policy failed to restore economic growth by the start of the 1980s, creating “stagnation under the burdens of debt, inflation, and volatile oil prices.”¹⁸⁵ The IMF and other international loaners made it hard for Ecuador to prosper. IMF loans came with provisions that included unpopular restrictions in federal spending,

¹⁸¹ Martz , 4

¹⁸² Pineo, 179

¹⁸³ Gerlach, 35

¹⁸⁴ Gerlach, 39

¹⁸⁵ Gerlach, 43

and no aid in projects for the social well being. This led to lack of focus on education, health, and new advanced industries. The 1980s continued this sense of political instability, combined with extreme low incoming revenue. To regain momentum in the oil industry, in 1989, the government of Rodrigo Borja renamed CEPE to Petroecuador to run oil exploration, extraction, preparation and exportation.

Foreign Involvement:

As FDI concentrated in primary industries it enforced economic dependence on an industry with little long-term growth benefits. Before oil, Western companies invested heavily in the cacao and banana industries. The United Fruit Company, for example, remains infamous for its role as a mega multinational corporation under the internal politics of unstable “banana republics.” The company is accused of bribing government officials in exchange for preferential treatment, exploiting its workers, contributing little through taxes, and consolidating monopolies.

The 1970s to the early 2000s represent a time high US involvement in the region, endorsed by US influential role under Washington DC’s specific economic recommendations, recently coined the “Washington Consensus.” The consensus pushed Latin America countries to enforce: tax reform (to lower marginal rates and broaden the tax base), a competitive exchange rate, trade liberalization, liberalization of inflows of FDI, deregulation (to abolish barriers to entry and exit), and interest rate liberalization.¹⁸⁶ Policies went in accordance with IMF and World Bank strict conditions for lending. In need of money, Ecuador adopted these classical economic

¹⁸⁶Global Trade Negotiations Home Page, “Washingong Consensus,” Center for International Development Harvard University. <http://www.cid.harvard.edu/cidtrade/issues/washington.html>.

recommendations prepared in Washington DC by loan experts.¹⁸⁷ The consensus paved the way for US influence and access to commercial and industrial sectors in Ecuador, yet lacked the ideal policy initiatives to ensure progress. In response to the failures “the people of Latin America are...rising up against an empire build under an extreme form of capitalism known as the Washington Consensus. Whole countries have been privatized, put up to sell, their natural wealth sold to foreign company, all for peanuts.”¹⁸⁸

Despite the US role in enacting economic policies and enforcing liberal practices, Ecuador’s political instability led to little FDI action. Through the period covered, FDI represented from 0 to about 5 percent of the GDP. In 1970, FDI net inflows represented 0 percent of the GDP, reaching the highest rates in when it represented in 2001, 6 percent of the GDP.

These figures are changing, as Ecuador seeks new partners and enforces responsible FDI. In 2008, the FDI income of Ecuador increased from \$193 million in 2007 to \$974 million, a relative difference 404 percent.¹⁸⁹ Incoming net flows of FDI arrived in the natural resources: 270million, manufacturing: 170million, and service: 533 million.¹⁹⁰ At the moment this number is small when compared to 2001, when total net FDI inflow reached \$1329 million. As the West loses ground in countries like Ecuador, the Chinese eagerly find space for expansion and investment, future FDI may be likely represented by Chinese FDI. China’s numbers have increased

¹⁸⁷ Pineo, 191

¹⁸⁸ Pilger, John. “The War on Democracy.”

¹⁸⁹ ECLAC 2008, 67

¹⁹⁰ ECLAC 2008, 67

relatively from past years, reaching \$85 million in 2007, but decreasing to \$49 million in 2008.¹⁹¹

FDI in Oil

*Domestically...Ecuador is a country in which petroleum industry enjoys hegemony over the economy, both in terms of national development and as the primary generator of revenue.*¹⁹²

This fact is true for the 20th century and today, making Ecuador more exposed to FDI in an industry likely to lead to oil curses. In the 1980s, the goals of promoting national agricultural and industrial production through investment in economic and social infrastructure crashed with the fall of petroleum prices in the 1980s and high public debt.¹⁹³ Focused on the petroleum industry lead to weak management of other sectors, unused lands, high taxes, and *dutch disease*.¹⁹⁴ Advance industries of high technology and knowledge become less sponsored. In response to the deficit, Ecuador began to rely on foreign finance, which accumulated high levels of external debt.

Many areas suffered from FDI mismanagement in the oil sector. While in Angola most of the oil fields are located in offshore areas that marginalize the industry and gains from the mainland, in Ecuador oil directly affects the lives on those living in the Amazon. Acknowledgment of large reserves trapped under the Amazon jungle led to a sudden oil hunt in the highlands of Ecuador's forest. Companies' investments and oil explorations endanger the local communities and natural environment. Pipes used for petroleum waste become hazards for locals,

¹⁹¹ ECLAC 2008, 70

¹⁹² Martz 1987

¹⁹³ *Encyclopedia of Latin America: History and Culture 2n edition*, 46

¹⁹⁴ Mosley, 417

leading to the contamination of indigenous communities who now suffer from health problems related to toxic waste.

The \$27 billion Ecuadorian lawsuit against Chevron for contamination of the Amazon indigenous communities in the eastern part of the country, questioned companies role and best steps regarding oil exploration and extraction.¹⁹⁵ According to Pablo Fajardo, the lawyer leading the case since 1993, Ecuador suffered “for 18 years, from the time Texaco started full-scale production in Ecuador in 1972, the company unloaded drilling mud and wastewater into hundreds of unlined pits or directly into waterways. Texaco [chose] savings over safety.”¹⁹⁶ Chevron defends itself and blames PetroEcuador for the contamination after it preceded Chevron in 1990. Unfortunately, this case has not progressed significantly and unsustainable practices continue in the Amazon region.

Today Ecuador is the fifth largest producer of crude oil in South America. Oil production and exportation has been a central focus for economic development with production rate ranging between 335,000-510,000 bpd.¹⁹⁷ In 2005, the US accounted for 63 percent of Ecuador’s oil exports.¹⁹⁸ With low local oil consumption, Ecuador’s production is expected to expand and enter other parts of the world.

Economic Growth and Economic Well-Being

Changing levels of GDP are indicative of the long-run investments in the oil industry. Oil investments induced a sudden surge of GDP growth in the 1970s. By

¹⁹⁵ Forero 2009

¹⁹⁶ Forero 2009

¹⁹⁷ Reuters, “Oil-hungry China moves to strengthen Ecuador ties.” July 2009 <http://www.reuters.com/article/GCA-Oil/idUSTRE56C6FF20090713> (accessed July 26, 2009)

¹⁹⁸ Stanley, 180

1973, the economic output rose to 233 percent, and GDP levels reached an all-time high in 1973 at 16.2 percent growth.¹⁹⁹ On the other hand, inflation rates doubled to about 20 percent and many other impacts like currency devaluation that directly affect the population.²⁰⁰ In Ecuador's case, GDP changes created negative impacts. In addition to inflation and currency issues, these changes led overconfidence, and thus, overspending and a heavy reliance upon economic growth. GDP is unpredictable and can have far reaching impacts in the economic well-being. Beginning in the 1980s and through to 2000, GDP remained around the same, rates \$14 billion. Throughout the 2000s, GDP increased and reached \$52.6 billion by 2008.²⁰¹ However, GDP cannot directly define well being, especially with impacts that can hinder or promote inequality and unemployment. Figure #1 shows the trajectory of GDP percentage growth.

GDP can affect inequality and other measures of economic well-being, but this in turn depends on the strength of the government in power. FDI in the oil industry sponsored inequality through the investments in an area that brings direct wealth to the ones in power and few opportunities to the common people. FDI promotes industries that may hinder economic development and well-being. In the oil industry, FDI sponsors the oil curse when it is not well managed by the government in power. A combination of weak governments and weak practices in foreign policy can lead to negative impacts in the economic well-being.

¹⁹⁹ Gerlach, 36

²⁰⁰ Martz, 4

²⁰¹ World Bank, Gross Domestic Product

In his examination of oil and politics in Ecuador, Marz uses a study by the University of Guayaquil to conclude that the expansion of the oil industry directly affects inequality. In 1968, the poorest 20 percent of population earned 4 percent of national income, the richest 5 percent of population received 26 percent. Despite the economic change brought by oil exportation, by 1975, the poorest 20 percent of population earned 2.5 percent of national income, and the top 5 percent had risen to 33 percent.²⁰² Inequality worsened, though some money was invested for the public good, most remained with the elite in power and military. Despite an increase in incoming revenue and a sudden GDP jump in 1932, inequality became a core problem. In 1975, one-fourth of the population held nearly three-quarters of the wealth. Factors like this lead to greater susceptibility to infant mortality issues, a weak educational system, and illiteracy.²⁰³

Since the 1950s Latin America has remained the most unequal area in the world. GINI levels have changed, but mostly remained around the 50s in Ecuador throughout the last half of century.²⁰⁴ See Figure # 2, shows the constant high GINI levels, enforcing the problematic high sustain levels of inequality in Ecuador. The highest GINI recorded levels, most inequality, is recorded in 2003, a result of an unchanging weak governance combined with weak political instability. The graph below emphasizes that despite alleged improvements pushed by Western investments in the region and the Washington Consensus, the GINI has remained the same for most Ecuadorians.

²⁰² Martz, 4

²⁰³ Pineo, 173

²⁰⁴ World Institute for Development Economics Research, "Summary features of WIID2c" United Nations University http://www.wider.unu.edu/research/Database/en_GB/wiid/

In regards to unemployment, the country has suffered no significant change, except for extreme levels recorded from 1999 forward. Much has been a result of currency issues and lack of development of other industries for more employment opportunities and capital. The high demand for Ecuador's primary good industries, especially banana and oil, encourage the nation to continue working on these industries, instead of expanding to other areas. Political instability and financial crisis play an important role in the lack of employment expansion.

Figure #1: GDP Percentage Change

Source: World Bank Indicators

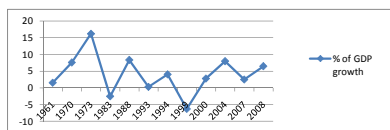


Figure # 2: GINI Coefficient

Source: World Bank Indicators

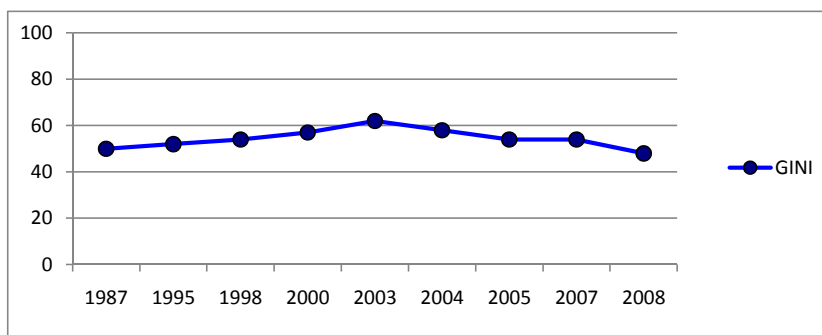
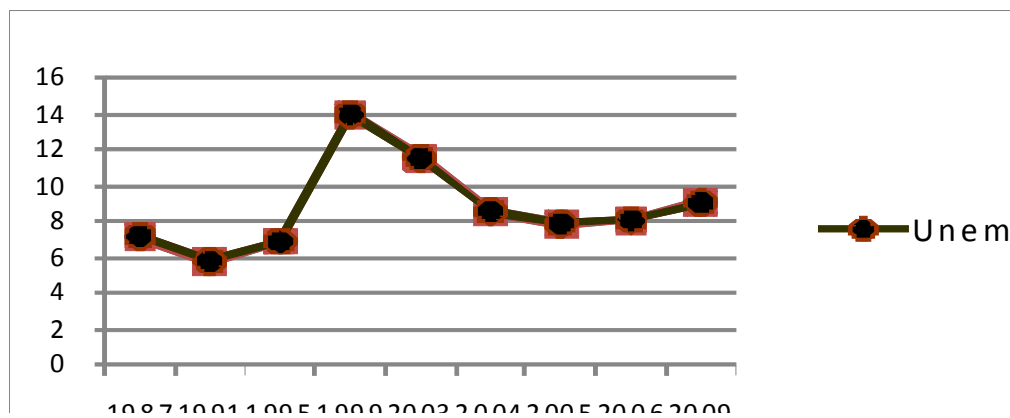


Figure #3: Unemployment

Source: World Bank Indicators



The Role of the West

Though the West is not solely responsible for the lack of development of Ecuador, it continues to play an important role in Ecuador's development. FDI brought changes that led to economic decisions that affected Ecuador's economy, helping to establish a flow of slow progress for the next two decades. The West did not provide any directly beneficial or long-lasting impact, a fact that is clear when evaluating Ecuador's socio-economic conditions and how they worsen after major West investments. The West provided Ecuadorians with advice that did not play out well in the region. It also failed to provide Ecuador with governmental support and the capabilities to address social well-being issues.

As Ecuador seeks to strengthen dialogue with other nations of the world one can conclude that there is something special about Western investments. The West represents the wealthiest and most imperialistic nations of the world, with influence spread wide across the globe. The bad record of the West in Latin America is enforced by its relation to cold war, imperialism and Washington consensus, and how

these enforced ideological, political and economic involvement. The West arrived to Ecuador not as a helping hand, but as a malevolent power to attend these needs.

Ecuador has had many negative experiences from relying on Western FDI. The rise of liberal-left governments in Ecuador requires more progressive methods and collaboration with more partners across the world, with oil serving as an object of national sovereignty and freedom.

Ecuador's new mission involves using oil as a tool to call upon new markets and shift away from business as usual. It involves taking a step against the enforced view that Ecuador is a nation of the deaf, mute, and blind. Deaf for those that govern, mute for the imperialists, and blind for those ignoring the injustices taking place.²⁰⁵ Shifting away from the old, Ecuador is seeking new partners and China represents new opportunity. It remains important to remember that the US is very important to Ecuador, as the nation's largest importer of Ecuador's oil. In 2005, US market accounted for 62.9 percent of Ecuador's total oil exports.²⁰⁶ But one cannot overlook what is currently taking place as Correa's administration works with China to strengthen relations on mutual need and "growth-growth."

Section III: Ecuador's Government in 21st Century

Socialist, Extremist, and Liberal, are some of the names for the current President of Ecuador, Rafael Correa, a leader revolutionizing Ecuadorian politics and economics. Correa is an economist that identifies himself as a liberal catholic, ready to mobilize Ecuadorians to fight corruption and create a stronger Ecuador. Rafael

²⁰⁵ Galarza Zavala, 17

²⁰⁶ Stanley, 180

Correa's politics take direct stands against forces that may hinder progress and has designed a new democratic constitution and promise to cut ties with the IMF and World Bank, restructure Ecuador's foreign debt, re-negotiate oil contracts, increase spending on social welfare, and end domestic weak governance by fighting corruption. The new government of Rafael Correa plays an important role in Ecuador's furthering of economic ties with China.

Despite criticism against his hard-line decisions and attitude towards the West and sovereignty, Correa is often as marked a new sign of hope and change for Ecuador. In Latin America liberal and leftist reforms are often supported because "the highest rates of private profits, growth rates, foreign exchange reserves and fiscal austerity have occurred under popularly elected center-left regimes, not the neoliberal rightist regimes of the 1990s."²⁰⁷ Center left regimes work well because of reliance on high-priced natural resources with parallel promotion reforms for the poor. Oil is an important feature of Ecuador's economy, with 45 percent of Ecuador's annual budget coming from oil revenues. President Correa is looking to further expand on this industry for rapid revenue to invest in social programs.

After taking office in 2007, by 2009 Correa had the Constituent Assembly rewrite the constitution. The new constitution, approved by a nation-wide referendum in September 2008, increased governmental control over monetary and oil policy, and reduced power of the legislative and judicial branches. It granted the state greater control of the economy, tripling of government spending, and strengthened the power

²⁰⁷ Petras and Veltmeyer, 13

of the president, to have more control of the state finances and credit and be able to dissolve Parliament if they interrupt Correa's plan of national development.²⁰⁸

Among many issues, the plan for national development concerns oil policy. Ecuador's petroleum policy suffers from monopoly issues, distortion in management of oil profits, high cost from low operational efficiency in the state enterprise and low quality products sent to market at a high cost and bad socio environmental record.²⁰⁹ According to President Correa the solution against this inefficiency lies changing those in control of the petroleum industry. With his growing influence, Correa plans the construction of the first efficient large scale refinery, the Refinery of the Pacific. The refinery will promote economic growth by allowing Ecuador to refine its own oil instead of paying another nation. The refinery will be the largest in the Americas, with the goal of attending local and Asian petroleum demands.²¹⁰

Correa has a large plate in front of him. In a television interview on July 23rd, 2010, President Rafael Correa said that Ecuador had liquidity problems due to its repurchase of 91 percent of its 2012 and 2030 global bonds, which retired the bonds for only 35 cents on the dollar, leaving Ecuador in possession of weak bonds and "fewer cash reserves and cut off from private overseas capital markets."²¹¹ A similar controversy took place under the April 2006 hydrocarbon law reform, which granted

²⁰⁸ Ferrand, "Ecuador's Correa until 2017?"

²⁰⁹ Mayorga, 115

²¹⁰ elDiario, "En Manabi estara la refinaria mas grande del Pacifico," August 10, 2010. <http://www.eldiario.com.ec/noticias-manabi-ecuador/48242-en-manabi-estara-la-refinaria-mas-grande-del-pacifico/> (accessed Nov. 21, 2010)

²¹¹ Wall Street Journal, "Petroecuador Signs Contract with PetroChina to Sell Crude," July 23, 2009. <http://online.wsj.com/article/BT-CO-20090723-723360.html>

the government with more shares of oil revenue, and control over the expropriation of Occidental fields, but weakened the country's investment outlook.²¹²

Slow economic change has resulted from restrictions imposed on imports. In February 2009, Correa imposed restrictions on imports, losing many investing partners. Import taxes led to a weaker commerce and reduction in importations. A total reduction of \$456 million in imports forced the administration to eliminate such measures and focuses on other alternative.²¹³ Despite economic uncertainties, Ecuador is determined to increase output in the following years to join the oil arena, and provide oil to other areas of the world.

According to Correa, Ecuador's oil production may increase to 180 million barrels in 2010, from an estimated 178 million barrels this year.²¹⁴ Many are skeptical that it can increase more because of old technology. Ecuador produced about 470,000bpd of oil in 2009, down from 503,000bpd in 2008.²¹⁵ To increase production, the state-run oil company PetroEcuador seeks to invest about \$2 billion in 2010 for studies and developments of the Oglan oil field in eastern Ecuador, a project it plans to work along with a unit of China Petroleum & Chemical Corp.²¹⁶

To attend its growing focus in oil exploration and exportation, Ecuador rejoined OPEC in 2007 after 15 years of absence. OPEC can help oversee just negotiations between Ecuador and its interest market, provide better information on steps taken by

²¹² Palacios 2008, 174

²¹³ elComercio, "El Petróleo Marca el Ritmo a la Economía," Julio 1, 2009. (accessed January 30, 2010)

²¹⁴ Bloomberg, "Correa Says Ecuador Oil Output to Rise in 2010," Nov. 30, 2009

<http://www.bloomberg.com/apps/news?pid=20601087&sid=abBQ6DMXtZKg&pos=7#> accessed Dec. 02, 09)

²¹⁵ Julio Gonzalez, undersecretary of hydrocarbons policy at the Ministry of Non-Renewable Natural Resources, said in an Oct. 27 interview.

²¹⁶ Bloomberg, "Correa Says Ecuador Oil Output to Rise in 2010, Ending Declines" Nov. 30, 2009

<http://www.bloomberg.com/apps/news?pid=20601087&sid=abBQ6DMXtZKg&pos=7#> (accessed Dec. 02, 09)

oil rich nations, and offer guidance to make better judgments and benefits from oil contracts. As a member, Ecuador agreed with OPEC on a three-year payment plan to clear its 5.7 million U.S. dollar debt.²¹⁷

Ecuador has sought to regain control of its oil and watch carefully other companies. A recent controversy with the French Oil exploration and production company, Parengo, ended with the removal of the company operations. From March to July 2009, Ecuador seized over \$2 million barrels from Parengo unpaid taxes. In a bid to collect more than \$350 million, Ecuador blames Parengo of “imperialistic” behavior and refusal to pay taxes.²¹⁸ In respond Parengo accused Ecuador’s government of violating the terms of contract, and suspended operations.²¹⁹ Ecuador lured China to consider the territory abandoned by Parengo. Controversy followed over whether China can take the place and offset the legacy of Western partners.

Another issue of controversy came over the Manta Air Base. In 1999, the Ecuadorian enacted a ten year contract with the USA over the Manta Air Base, granting the US the right to patrol the transport of narcotics in the region. When it came time to renovate the contract, Correa said that “Ecuador would extend the treaty only if the United States allows us to put a base in Miami.” Correa accused the US of paying little and increasing the regional drugs violence.²²⁰ Following Correa’s

²¹⁷ Xinhuanet, “OPEC Accepts Ecuador,” October 23, 2007.

http://news.xinhuanet.com/english/2007-10/24/content_6931568.htm (accessed Dec. 02, 2009)

²¹⁸ Reuters, “Ecuador Vows to Continue seizing Perenco’s Oil,” July 14, 2009.

<http://www.reuters.com/article/idUSN1429981120090714> (accessed July 30, 2009)

²¹⁹ Matthew Campbell and Amanda Jordan, “Parengo Ecuador Is in ‘Impossible Position,’ Regional Head Says,” July 15, 2009. http://www.bloomberg.com/apps/news?pid=20601086&sid=akGZzd2Wj_9c (accessed July 30, 2009)

²²⁰ Telesur, “Correa Entrevista,” Julio 27, 2009 <http://www.telesurtv.net/noticias/secciones/nota/54847-NN/correa-califico-como-arremetida-politica-acusaciones-que-pretenden-vincularlo-con-las-farc/>

statement, Manta has been designated to become a strategic airport for Sino-Ecuadorian relations, granting Chinese better access to the Latin American markets.

Lately controversy related to Western and Ecuadorian interests usually ends up benefiting the Chinese. A negative view towards the West's treatment of Latin America has in turn set a positive view of China. In his 1973 diplomatic analysis, *Relaciones con Pekin*, Manuel Rodríguez Sacoto states that Ecuador's progress relies on solidifying relations with China as it can strengthen economic and technical cooperation under mutual benefit and equality.²²¹ Those goals and expectations are driving the current diplomatic and economic relations between the two nations. Ecuadorians approve of China because of shared trajectories and experiences. Recent gatherings between local officials of both nations and the visit of president Correa to China in November 2007, have helped push forward goals of economic and trade cooperation with China in the fields of energy, technology, agriculture and infrastructure. Ecuador is ready to begin exploration of its oil fields through stronger cooperation with Chinese oil enterprises, hoping China will invest in the construction of roads, ports, airports and oil refineries.²²² The following section explores these efforts further.

Section IV: China and Ecuador: A Pragmatic Partnership

Under the new government administration goals have been set out to improve relations with other regions of the world, especially with Asian countries. Ever since the 1970s, analysts have highlighted the benefit of extending relations with China.

²²¹ Rodríguez Sacoto, 15

²²² Palacio 2008,174

They write that China can be a respectful and equal trading partner. Expectations building up since the 1970s will finally be put to the test going as China re-assures its interests in Ecuador and vice-versa.

The year 2007 marks the reinforcement of Sino-Ecuadorian relations. Past experiences, expectations for future investors, and new goals set under Correa's government pushed Ecuador to seek economic support and relations with nations outside the West arena. While the US consumes about 18 million barrels of oil per day, China follows as the second highest consumer of oil in the world, consuming about 11 million barrels of oil per day.

China has turned to Latin American oil-rich nations like Brazil, Columbia, Ecuador, and Venezuela to feed its oil imports, which represent about 50percent of the oil it consumes.²²³ Though Venezuela has sought to further strengthen its ties with China through increasing oil exportation, Ecuador has been the quietly growing partner of China in the region. Ecuador's location in the Pacific coast, and its relationship with Brazil, make the nation a significant point of access for Chinese products and investments.²²⁴ The following sections explore the growing Sino-Ecuador relations, emphasizing diplomatic and economic cooperation.

Political and Diplomatic Relations

January 2010 marked thirty years of Sino-Ecuador diplomatic relations, officially initiated on January 2, 1980.²²⁵ Engagement goes back to the late 1960s

²²³ elComercio, "China Pagara Crudo Con Descuento," Jul 29, 2009.

²²⁴ Ellis, 7

²²⁵ Xinhuanet, "30 years of sino-ecuadorian diplomatic ties marked in Beijing" December 31, 2009.

when Ecuador opposed UN blockage of China. As early as 1975 the two nations signed a trade agreement for exportation of bananas and fish to China. In the 1980s both embassies established their prospective embassies and Ecuadorian President Oswaldo Hustado Larea visited China on May 1984. Ten years later Ecuadorian President Sixto Duran Ballen visited China on March 18th, 1994 to enforce mutual protection of investments and petroleum cooperation. Future talks on foreign affair protection and cooperation were held on August 29 1999 when Ecuadorian President Jamil Mahuad Witt paid a visit to China, followed by President Gustavo Noboa Bejarano in March 19th 2002.²²⁶

After decades of small-scale engagement, Ecuador and China have begun conversations about strengthening diplomatic and political relations, financial and economic cooperation, as well as FDI in many areas. Pragmatic cooperation increased after President Correa's visit to Beijing on Nov. 21 2007, where Correa created incentives for China to trade and invest beyond oil. On July 8, 2009 both nations declared the need to boost military ties, and establish Ecuadorian trade offices in Shanghai and Guangzhou.²²⁷ In addition, Correa's revolutionary offer of the Manta air base to China in November 20, 2007 signaled the commitment in relations. The Manta airport base, for which the U.S. Air Force Southern Command's 10-year usage rights expired in July 2009, offers a geopolitical entry point for Beijing into South America.²²⁸

²²⁶ "China and Ecuador"

²²⁷ Xinhua, "China, Ecuador Military Ties," December 2, 2004.

http://english.peopledaily.com.cn/200412/02/eng20041202_165937.html

²²⁸ StratforGloInt, "China, Ecuador: Beijing's Latin American Opportunity," November 2007.

Ever since Correa's 2007 visit, back-to-back visits between both nations officials have followed. On February 13, 2009, the vice prime minister of China Hui Liangyu visited Ecuador to meet with vice President, Lenin Moreno. Liangyu considered Ecuador's and China's commercial and diplomatic relations to be excellent. According to Liangyu, "Our relations with Ecuador are highly satisfactory because we have no area of political conflict or conflict of interest... Despite distance, Ecuador and China always had a great friendship and cooperation."²²⁹

With the Manta case in hand, and coalition for future projects and growth in diplomatic ties, Correa has expressed Ecuador's need to have more Asian investments to help the country upgrade its infrastructure requirements and to expand its international trade. Asian countries like China can provide a mutual sense of understanding, as third world countries with common challenges.

Financial and Economic Cooperation:

Ecuador's fiscal problems have reaffirmed the need to strengthen relations with China. The counter effects of dollarization in 2000 began to impact their economy, and the world financial crisis has impacted oil prices. Liquidity problems arose after the repurchase 91 percent of Ecuador's foreign debt, the repurchase of the 2012 and 2030 bonds was surprising especially after Correa declared the debt to be "illegal" and "illegitimate."²³⁰ The repurchase cost Ecuador \$900 million.²³¹ Despite the financial crisis situation, trade deficit has improved. In 2007 Ecuador went into a

²²⁹ Xinhuanet, "Ecuador y China Fortalecen relaciones," Feb. 09

²³⁰ elUniverso, "China compra \$1.000 millones en crudo a Ecuador," Jul 2009

²³¹ "Ecuador Foreign Debt In November Down 19% To \$13.7B; 27% Of GDP" http://online.wsj.com/article/BT-CO-20100125-706515.html?mod=WSJ_World_MIDDLEHeadlinesAmericas (accessed Feb. 10, 2010)

state of panic when its trade deficit totaled \$500 million.²³² However after quick changes taken by Correa's administration, the trade has deficit decreased considerably. According to the Dow Jones, "Ecuador posted a trade deficit of \$8.4 million in December, compared with a deficit of \$555 million in the same month of 2008."²³³

Ecuador and China have settled several agreements for financing Ecuadorian infrastructure projects. An agreement of economic and technical cooperation granted Ecuador with 20 million yuan with no interest, and a line of credit of 200 million yuan.²³⁴ In February 2009, China and Ecuador signed four agreements of cooperation worth \$25 million as part of efforts to strengthen ties and trust. China also granted a credit line to Ecuador of 50 million yuan for trade in agricultural products and investments in the agricultural sector. Agreements between the Bank of Ecuador and China's Development Bank agreed to credit \$18 million for the Ground Terminal in Quitumbe.²³⁵

The \$1 billion oil deal formalized economic and commercial cooperation.²³⁶ In the summer of 2009, PetroEcuador and China agreed on an offer that granted Ecuador an immediate \$1 billion in exchange an export to China of 2.88 million barrels per month of crude oil for the next two years. The \$1 billion represents approximately 28

²³² Xinhuanet__Correa hopes to strengthen economic China Nov. 07__"President Correa hopes to strengthen economic coop with China"

²³³ Nasdaq, "Ecuador Dec Trade Deficit \$8.4 Million Vs \$555 Million Deficit On Year," Dow Jones Newswires. <http://www.nasdaq.com/asp/stock-market-news-story.aspx?storyid=201002081555dowjonesdjonline000281&title=ecuador-dec-trade-deficit-84-million-vs-555-million-deficit-on-year> (accessed Feb. 10, 2010).

²³⁴ Ecuador en ASEAN, "El Ecuador firma 14 convenios con la Republica Popular China" http://www.rafaelcorrea.com/la_noticia/1008/El%20Ecuador%20firma%2014%20convenios%20con%20la%20Rep%20C3%BAblica%20Popular%20China (accessed Nov. 22 09).

²³⁵ China Daily, "China signs cooperation agreements with Ecuador," February 14, 2009. http://www.chinadaily.com.cn/bizchina/2009-02/14/content_7477273.htm (accessed Feb. 10, 2010).

²³⁵ elComercio, "China Pagara Crudo Con Descuento," Jul 29, 2009.

²³⁶ elComercio, "China Pagara Crudo Con Descuento," Jul 29, 2009.

percent of the total value of the oil that Ecuador has agreed to export to China.²³⁷ The other 72 percent will be paid on the day of delivery and marked by the price set by West Texas Intermediate (WTI) on the particular month the oil is delivered.²³⁸ In total the deal puts about 69 million barrels of oil in the hands of PetroChina, or 35% of Ecuador's monthly production, which in May 2009 produced over 485,000 barrels of crude oil per day.²³⁹ Sponsored by Ecuador's Finance Minister, the deal seeks to provide funds for the state investment plan in infrastructural projects in which China is looked for investments and contributions. The crude oil is to be use for China's own consumption and not to be sold to other countries for profit. The \$1 billion dollar agreement is just the start of different numbers of finances that the Chinese are involved in to expand relations with Ecuador.

The most recent controversial Chinese finance project belongs to the construction of the largest hydroelectric plant: Coca Codo Sinclair, to be completed by 2015. The power plant will have the capacity to generate 1,500 MW of electricity, covering about 70 percent of domestic energy needs. The project (to cost about \$2 billion) was expected to receive \$1.7 billion in finance from the Export-Import Bank of China, 85 percent of the project's cost.²⁴⁰ However, on March 20, 2010 Correa broke ties with China over the project, accusing them of challenging Ecuador's

²³⁷ Eduardo Garcia, "Ecuador signs contract to export oil to China," *Reuters*, Jul 23, 2009.

<http://www.reuters.com/article/GCA-Oil/idUSTRE56N04820090724> (accessed July 25, 2009).

²³⁸ Wall Street Journal. "Petroecuador Signs Contract With Petrochina To Sell Crude." July 23, 2009. Wall Street Journal. <http://online.wsj.com/article/BT-CO-20090723-723360.html> (accessed July 25, 2009).

²³⁹ *elComercio*, "China Pagara Crudo Con Descuento," Jul 29, 2009

²⁴⁰ Wall Street Journal. "Petroecuador Signs Contract With Petrochina To Sell Crude." July 23, 2009. Wall Street Journal. <http://online.wsj.com/article/BT-CO-20090723-723360.html> (accessed July 25, 2009).

sovereignty through harsh demands that challenged its sovereignty.²⁴¹ Correa became angered over demands that had never been demanded in the entire history of the republic, after hope of creating a new form of partnership with China, Correa was disappointed by being considered by the Chinese as just another commercial partner. In response to the accusations, three days after Correa's statement, Beijing contacted Quito to reinstate dialogue and mend ties.²⁴²

Bilateral Trade:

The terms of bilateral trade between Ecuador and China are growing despite several ups and downs in Ecuador trade policy. Though China is one of the largest supplier and exporter of goods in the world, China buys more from Ecuador than what Ecuador imports. Efforts to expand Chinese interest in Ecuador's goods have been sponsored by CORPEI: *Corporación para la Promoción de Exportaciones*. CORPEI has worked along the Ministry of Foreign Affairs to promote exportation to China. Entrepreneurs and organizations tagged along to support trade ties. The Cámara de Comercio Ecuatoriano-China promotes ties between the two nations through delegation exchanges in the two countries, participation in business fairs, and promotion of presidential and high office visits between Ecuador and China.

Trade volume has increased rapidly. In 2002, bilateral trade volume reached \$208 million, of which \$194 million were Chinese exports and \$13.57 million

²⁴¹ Telesur, "Ecuador suspende negociaciones con China por hidroléctrica" March 20, 2010 <http://www.telesurtv.net/noticias/secciones/nota/68805-NN/ecuador-suspende-negociaciones-con-china-por-hidroelectrica/> (accessed March 20, 2010)

²⁴² Telesur, "China y Ecuador estrechan vínculos de cooperación práctica y fraternidad mutua." March 23, 2010 <http://www.telesurtv.net/noticias/secciones/nota/68970/china-y-ecuador-estrechan-vinculos-de-cooperacion-practica-y-fraternidad-mutua/> (accessed March 23, 2010)

Chinese imports.²⁴³ From January to September 2007, China-Ecuador trade volume totaled \$669 million dollars.²⁴⁴ In 2008, bilateral trade between Ecuador and China generated about \$2.4 billion in commercial trade, double of 2007.²⁴⁵ In 2008, trade represented 64 percent of Ecuador's GDP.

In comparison with Angola, Ecuador is far behind in reaching the commercial value of petroleum trade with China. In 2008, Ecuador's total import value to China totaled \$28,918 while for Angola it totaled \$1,217,866. In 2007, however, Ecuador's exports to China increased by 1,114 percent, while for Angola it increased 139 percent.²⁴⁶ It is too early to compare or measure Ecuador's capital trade levels with China, and there is much space for growth and expansion. While China imported 326,000 tons of crude oil from Ecuador in the first four months of 2009, the \$1 billion oil deal will change these numbers as China expects to receive about 3 million barrels of Ecuador's crude oil monthly starting August 2009.²⁴⁷

China's FDI

Along with increasing levels of finance and bilateral trade, China is investing in different industries in Ecuador. In addition to traditional investments in fishing industries, China has started to invest in the oil industry. On September 2005, China purchased for a total of \$1.42 billion the formerly own and largest Canadian

²⁴³ Ministry of Foreign Affairs of the PRC, "China and Ecuador," September 9, 2003
<http://www.fmprc.gov.cn/eng/wjw/zjzg/ldmzs/gjlb/3493/t17376.htm> (Nov. 26, 2003)

²⁴⁴ Xinhuanet, "President Correa hopes to strengthen economic coop with China" Nov. 2007

²⁴⁵ PRC Agreements with Ecuador 2009, 2010, PDF

²⁴⁶ Minister of Commerce of China, "Total Import and Export Value by Country (Region) 2008/01-06."
<http://english.mofcom.gov.cn/article/statistic/ie/200808/20080805719430.html> (accessed Feb. 3, 2010).

²⁴⁷ Reuters, "Ecuador seeks \$4 billion for New Oil Refinery." Feb 22, 2007.
<http://www.reuters.com/article/companyNewsAndPR/idUSN2244157820070222> (accessed July 2009).

independent oil explorer in Ecuador, EnCana Corp.²⁴⁸ The Chinese consortium, the Andes Petroleum Company, which includes China National Petroleum Corp (CNPC) and China Petrochemical Corp (Sinopec Corp), the parent companies of Hong Kong-listed PetroChina and Sinopec, gained the capacity to produce 450,000 barrels a day in Ecuador.²⁴⁹ It gained large scale production through the acquisition of “five blocks that are able to produce some 75,200 barrels per day and have proven reserves of 143 million barrels, as well as a 36 per cent stake in OCP Pipeline, which is able to pump 450,000 barrels of oil per day.”²⁵⁰

By 2007, Chinese investments had reached \$747 million. They are expected to increase after the visit of the chairman of political consultative conference of China, Jia Oinglin, who held talks in Ecuador about future projects, such as the Hydroelectric Coca Codo Sinclair and the hospital of Puyo. A project that would both benefit China and stand as a major work of Chinese interest and position in the region is the construction of the Corredor Manta-Manus Belen, an infrastructure project for Chinese to use and connect to Brazil through Ecuador. The project is expected to gain momentum soon, as players involved are ready to take action and benefit from the many opportunities of commerce, development and knowledge the project can bring.²⁵¹

In regards to the Manta air based, the “Hutchinson Port Holdings' (HPH), the port business of Hong-Kong based Hutchinson-Whampoa, originally set to invest

²⁴⁸China Daily, “China oil firm buys EnCana assets in Ecuador,” Reuters, September 15, 2005
http://www.chinadaily.com.cn/english/doc/2005-09/15/content_478015.htm (accessed Feb. 10, 2010).

²⁴⁹ Ellis, 18

²⁵⁰ Wang Ying, “Oil consortium buys EnCana Ecuador assets,” China Daily.
http://www.chinadaily.com.cn/english/doc/2005-09/16/content_478433.htm (accessed Feb. 10, 2010).

²⁵¹ Ellis 2009, 133

\$578 million over the course of 30 years to transform Manta into the largest port in the region and China's gateway to the Americas. Talks were hosted over establishing a direct flight between Quito and Beijing. However, negotiations hit a bump in January 2009 and Correa threatened to expel HPH if they did not fulfill their part of the agreement by investing the promised amount of money. With the global economic slowdown, China reconsidered their investments proposal, however in February 2009, negotiations were back up.²⁵²

Issues:

Issues pertaining to Chinese investments, demands and migration into Ecuador have raised tensions and backfiring progress. In order to protect the local industry against the increasing cheap Chinese business, in 2008 Ecuador imposed a high tax of textile and cloth coming from abroad. The tariff affected about 23 percent of Ecuador's imports, forcing importers of textile and cloth to pay an extra \$12 dollar per kilo. Of the 10,000 Chinese who run businesses in Ecuador, about 80 percent are looking to end their businesses. Profit lost has affected the Chinese and destroyed hundreds of local jobs.²⁵³ The flight of Chinese business inflicts an investment loss of \$20 million, hiding hardest businessmen who sell textiles and shoes.²⁵⁴

Another tax related dispute is over taxes in the oil industry. Unlike Angola which set a friendly export and FDI system, Ecuador is a relative unfriendly country

²⁵² Ferrand 2009

²⁵³ HoyComercioEcuador,"Los Chinos llevan sus comercios al Peru" April 2009. <http://www.hoy.com.ec/noticias-ecuador/los-chinos-llevan-sus-comercios-al-peru-344638.html>

²⁵⁴ HoyComercioEcuador,"Los Chinos llevan sus comercios al Peru" April 2009. <http://www.hoy.com.ec/noticias-ecuador/los-chinos-llevan-sus-comercios-al-peru-344638.html>

to invest in, a reality that has affected Chinese FDI. There has also been much disagreement between China's major state energy players (namely, China Petroleum and Chemical Corp., China National Petroleum Corp. and Sinochem International Oil Co.) and Quito over an unexpected October ramp-up of Ecuadorian oil taxes from 50 percent to 99 percent.²⁵⁵

Disagreements over contracts and China's set provisions over credit assistance have negatively ended great projects, such as the Coca Codo-Sinclair Hydroplant. Demands that sound similar to those imposed by the West have personally offended the president and the government, who had sought in China as a new reliable friend and partner. Correa's expectations and vision of China as a friend more than just a traditional commercial partner may hurt future agreements, especially as China's foreign policy promises friendship, but practices produce more domination than mutual cooperation and growth.

Chinese influence in Ecuador also has negative consequences. Human trafficking resulted from Ecuador's government removal of visa requirements. The government pushed for the new visa policy to engage more with Chinese and expand support through trade, tourism and the development and construction of a deep-water port in Manta.²⁵⁶ However, lax visa regulations placed by Ecuador's government in early 2008 have led a 500 percent increase in "Chinese tourism" from 2007 to 2008.²⁵⁷ In reality this Chinese tourism is the entrance of Chinese who want to make it across to the US. From January to June 2008, 2,875 Chinese entered the country.

²⁵⁵ StratforGloInt_China, Ecuador Nov. 07__ "China, Ecuador: Beijing's Latin American Opportunity"

²⁵⁶ Cieslik 2010, 174

²⁵⁷ <http://mexidata.info/id2146.html> (accessed Feb. 10, 2010)

Conclusion: China and Ecuador: A Perfect Marriage?

In the presentation of his book, *From Banana Republic, To No Republic*, Correa commented on many of the failures of past administrations and the role of oil in the politics and development of his country.²⁵⁸ The book highlights foreign affairs issues, negative experiences with multinationals, and a new vision for Ecuador economic development. Correa believes that lessons from the past have prepared today the Ecuadorian society to stand up against any foreign investor who may want to hinder Ecuador's progress and sovereignty.

Considering its past engagement with the US, Ecuador now turns to China for a new opportunity for development. Correa has put a lot of trust in China's hand, believing him to be the new figure for accomplishing Ecuador's new economic development goals. Ecuador seeks to no longer be recognized as the "backyard of the US," but as a stable independent nation important to world politics. China can assist Ecuador in this process through mutual exchange and growth.

The rise of a populist leftist presidency, along with weak relations with the US has set the stage for Sino-Ecuadorian engagement. China's entrance into Ecuador cannot be taken for granted, contemporary Sino-Latin American analysis often ignores the possible impacts China may have in Ecuador. Many believe that American influence is too large, while Chinese influence is too foreign and will have no direct impacts in Latin America. The truth is that as the US ignores the development and politics of its closes neighbor, China is gaining presence and building stronger ties with nations now developing an anti-America rhetoric.

²⁵⁸ Youtube, "Ecuador: de Banana Republic a la No República." <http://www.youtube.com/watch?v=uSGXGYIArAg> (accessed Feb. 1, 2010)

Angola and Ecuador have become gateway nations for Chinese investment in their respective regions. Though at different scales, Latin America and Africa underwent a number of injustices through Western colonialism and domination of home industries. The bad record of the West and the new Eastern opportunity have shape a similar trajectories in Angola and Ecuador. Today as both nations share a same vision of relying in oil for economic growth, they have sought to solidify their goals through joining OPEC in 2007 and having a voice in the oil sector.

Interestingly, several African and Latin American nations are sharing a new call for growth and separation from the West. Historically both regions have suffered from Western presence and been forced to adapt to the “good economic development models” of the so called Washington Consensus, or neoclassical economic principles. The reality is that these principles are not always the best for the progress of developing nations, who need at times protectionist policies and assistance in various areas to reach the developed state. In response to the Western failure to assure economic growth, and China’s new foreign policy that promises and practices direct investments and assistance for growth, is a new economic model that countries like Ecuador want for themselves.

As Beijing and Quito seek more of the other and continue increasing bilateral agreements, visits, interests and consideration, slowly but surely both nations will undergo different kinds of development. As China’s presence continues to grow in the Western periphery, the following chapter looks at different scenarios to determine ways in which China might affect Ecuador’s economic development.

Chapter V:

Relations with Peking: The Impacts

What will be China's impact in the economic growth of Ecuador and economic wellbeing of Ecuadorians? Will China's impact be better, worse or the same for Ecuador as that of the West?

This chapter seeks to construct different ways to observe how Ecuador's economic development may evolve as the nation develops future ties with China. This chapter analyzes alternative scenarios that differ in terms of the role of governance and strength of Chinese foreign policy practices. The analysis looks at assembled data on theories covered and observed in the last three chapters, Angola's relations with China, and Ecuador's past development.

Theoretical claims help access the logic behind China's impacts in Ecuador. The case study nation, Angola, provides us with guidance and tools to determine possible impacts China may have in Ecuador. Background on Ecuador's experience with the West helps us understand the reasoning behind Ecuador's move to strengthen ties with China. Drawing on insights of history, arguments, and current events, this chapter examines four scenarios considering different paths of Sino-Ecuadorian relations. The scenarios that follow look at the near future, measuring Ecuador's development in the next decade. Given the considerable uncertainty about possible changes in Ecuador's government and China's investments and interest in the region, this time period should be viewed as a variable.

Scenario Building Process for China in Ecuador

To build scenarios one must first identify the variables at play. In this study, the primary causal factors include Ecuador's economic bargains with China, terms of bilateral trade and China's FDI. The dependent variables, or future outcomes, are unknown and depend on how other variables evolve. This study is primarily concerned with Ecuador's economic growth and well-being as defined by GDP, income inequality (measured by the GINI coefficient) and unemployment.

Chapters II through IV helped us identify intervening variables. Some of these intervening variables have predetermined values and will remain the same throughout the various scenario plotlines. These variables are hard to alter, such as Ecuador's high corruption levels, and will remain the same in all scenario plotlines. Other predetermined variables include: the location of crude in places where exploration affects particular areas and communities; the limited amount of oil reserves, which limits the expansion of the oil industry; and China's interest and focus on oil.

Other intervening variables represent critical uncertainties, factors of high influence but high uncertainty regarding China's investments in Ecuador. Critical uncertainties set the stage for determining dependent variables through different scenario plotlines that tell a compelling story of how things may happen in the next decade. The first critical uncertainty for this study questions the role of Ecuador's governance in shaping the outcomes of China's investment. This uncertainty asks whether Ecuador's governance is strong or weak and how the degree of strength determines outcomes. The second uncertainty focuses on China's foreign policy goals and practices, and how these practices may determine paths for Ecuador's

development. This uncertainty questions whether China's foreign policy promotes weak or strong impacts in Ecuador's economic development. These uncertainties are elaborated on in the next two sections.

Critical Uncertainty #1: Ecuador's Level of Governance

As discussed in Chapter II, the level of governance is essential for determining development. This uncertainty evaluates how Ecuador's future may evolve if governance varies from strong levels to weak ones. This scenario looks at different ways in which President Correa's administration may govern Ecuador in the next decade, either enforcing new governance based on stability, effective rule of law and bureaucratic efficiency, or a governance challenged by historically weak levels of governance. I will use changes in economic growth, unemployment and inequality to measure the level of governance and its success.

A weak administration describes an environment of political instability, where those in power have no say or are indifferent to China's actions in Ecuador. Weak governance enforces an unstable government with unclear foreign policy goals and poor involvement in improving social conditions. Weak governance may result in the overthrow of the chief-of-state, something common in Ecuador's history. Weak governance refers to an unstable state led by leader suffering from political instability, corruption and poor rule of law. On the other hand, a strong administration results from the union of the President and the common people working for social reforms, better foreign relations, and growth of industries. Given strong governance we should

expect issues of inequality and unemployment to be addressed, and relations with China expanded, if China is trusted as a friendly partner.

Critical Uncertainty #2: Chinese Foreign Policy Goals and Practices

Chapter II provided an overview of China's foreign policy goals for developing nations. The actual implementation of these goals in Ecuador will be covered differently in each scenario, evaluating whether Chinese foreign policy remains consistent or breaks away from expressed foreign policy goals. Altruistic foreign policies will often result in positive outcomes in Ecuador's development by enforcing "growth-growth" strategies. Malevolent foreign policy practices are those that do not comply with the original foreign policy visions and have negative impacts in Ecuador's development. China decides which to enforce, as it takes into consideration its own goals and interest.

According to Cieslik, China's bargain in Latin America will be positive because they center on a new foreign policy commitment to the three Principles of Sun Yat-sen: sovereignty, emancipation and anti-hegemony.²⁵⁹ "China's Policy Paper on Latin America and the Caribbean," published November 2008, stresses this positive image by presenting China's commitment to cooperation in different areas. Not all literature promotes this image and instead focuses on the dangers China's policy can inflict in Latin America. Uncertain positive and negative visions of Chinese foreign policy and practices make this a critical concern for determining the dependent variables, or

²⁵⁹ Cieslik 2010, 161

impacts on growth and well-being. These two critical uncertainties present the main features around which the four scenarios are constructed.

Scenarios:

The intervening variable, predetermined factors and critical uncertainties identify a range of outcomes as a set of scenarios each with its own plot lines. This section presents scenarios of alternative economic development patterns. The scenarios evaluate different paths the critical uncertainties may take to determine different values of economic growth, inequality, and unemployment. Given the likelihood of Chinese investments in Ecuador the following scenarios explore alternative futures that differ in extent of the level of governance, and relative implementation of Chinese foreign practices.

The first scenario, *Business as Usual*, explores the cost of continuing low governance trends along with a malevolent Chinese foreign policy. The second scenario, *Not a Zero Sum Game*, evaluates similar paths of development as observed in Angola, where low governance and altruistic Chinese foreign policy enabled positive but limited impacts. This scenario explores how China may be an opportunity for development with strategies and practices that are not a zero sum game for Ecuador. The third scenario, *Better Solo*, discovers that malevolent Chinese foreign policy can push Ecuador to adapt development paths, if strong governance is present. This scenario concludes that it is better for Ecuador to follow its own strategies for growth, instead of relying on foreign investors. Finally, *No Chinese*

Tales, explores how the *cuentos chinos* are not true, and that Sino-Ecuadorian engagement will result in great economic and development outcomes for both Ecuador and China. It enforces that China is an opportunity and partner for development to an Ecuador under strong governance and altruistic Chinese foreign policy.

The scenarios names pertain to the impacts that result from the interaction effects of the two critical uncertainties. **Table #2** provides plot lines and scenarios.

Source: World Bank Indicators

Table 2: Scenarios

	Scenario 1	Scenario 2	Scenario 3	Scenario 4
Ecuador's Government	Weak	Weak	Strong	Strong
China's Foreign Policy	Weak	Strong	Weak	Strong
Scenario	<i>Business as Usual</i>	<i>Not a Zero Sum Game</i>	<i>Better Solo</i>	<i>No Chinese Tales</i>

Scenario 1: Business As Usual

Weak Governance + Malevolent Chinese Foreign Policy

Business As Usual reveals how Ecuador's economic progress may encounter no change if weak governance continues and if China reverses its original foreign policy goals. It is a low to no growth scenario where targets of economic development are not pursued. In this first scenario, we can expect that in the near future Ecuador's GDP will not change much, inequality will increase, and employment will also not change significantly.

The Significance of Weak Governance

The significance of having weak governance is high when considering that Ecuador has suffered from weak political institutions and recurring ousting of chief-of-states. In Ecuador, institutions of authority are often marked by a lack of efficiency, lack of participation or oppression against freedom of speech, high corruption, an unfair governmental process, and inequality in the law. This scenario explores the possibility of Correa's administration suffering from weak governance.

The likelihood of Correa's administration falling into weak governance is double sided. Correa's actions may either lead him to make no progress or become too powerful and be ousted from power. On one hand President Correa's hard-line decisions are moving towards actions against media that may threaten democracy, freedom of speech, and enforce an authoritarian power.²⁶⁰ Correa's new constitution theoretically gives him the chance to remain president until 2017, with increased powers against Congress. On the other hand, his administration may suffer from the rise of oppositional corrupted classes rallying the common people against Correa. Such an outcome can lead to another ousting, as in the summer of 2009, when President Zelaya of Honduras was removed despite widespread support from the common people.

Weak governance directly affects the economic growth by leading to poor decision making in the economic sector. One of the decisions commonly made is to continue reliance on oil without investing in other areas. Reliance on oil continues and may lead to several Oil Curse outcomes. Lack of advancements in new industries

²⁶⁰ Reuter, "Ecuador's Correa says to fight media corruption" May 23, 2009
<http://www.reuters.com/article/idUSTRE54M1L220090523>

eliminates possible job opportunities and enforces reliance on oil. Bureaucracy issues and lack of transparency in economic policy and accountability take over.

Administrative issues that Correa may face in the upcoming years may include the failure to put in place the promised civilian revolutions and equality because of high corruption levels. Correa's failure to implement his original socialist agenda may enforce inequality, and the poor might lose the voice they had been promised. Regulations and benefits are not equally spread across the population because corrupted classes manage to strengthen their power and shift policies in their favor, while enforcing unemployment. Lack of jobs and high levels of corruption will definitely increase inequality.

The Significance of a Malevolent Chinese Foreign Policy

China's foreign policy goals may change with time. The first decade of the 21st century marked China's economic rise and growth in its need for natural resources, Overflowed with revenue brought by the low currency rates and high demand of Chinese goods, China invested a great deal in different industries in Angola. However, with the start of a new decade, China's efforts and commitments to foreign policy are not assured. The outcomes of the financial crisis, of countries protecting their home industries against Chinese goods, and of a growing wealthier Chinese class will intervene in China's foreign policy vision.

Another issue is that China's foreign policy goals may mean one thing for one country but something else for another country. Malevolent Chinese foreign policy is for example enforced with China's lack of strong commitment to energy cooperation.

In “China’s Policy Paper on Latin America and the Caribbean,” thirty-four areas are covered on China’s cooperation with Latin America; however the “Resources and Energy Cooperation” is vague:

The Chinese side wishes to expand and deepen mutually beneficial cooperation with Latin American and Caribbean countries in resources and energy within bilateral cooperation frameworks.²⁶¹

It says nothing about how energy cooperation will be conducted. The lack of clear goals on energy cooperation makes it difficult to predict China’s future policies and goals. It may lead to different ways of defining energy cooperation, and may also lead to China strengthening its own energy policies under a weak governance society.

The way in which China’s foreign policy will be implemented is unclear, but it will surely affect economic growth in Ecuador through more expansion and participation in the oil industry. China’s urgent demand for oil may directly lead to higher GDP levels, as much capital enters the economy. A strategy that China is likely to use to secure oil is the “Angola Mode,” oil paid deals in exchange for rapid finance.²⁶² This move will lead to less focus in other industries and make Ecuador vulnerable to low market price flows and macro instability. This will result in less job opportunities and lack of investments in other areas. China may also weaken local industries by bring their cheap goods and creating competition for local producers.

The likelihood of China behaving in a malevolent way is supported by the fact that China itself is a developing country with a human development index lower than

²⁶¹ China Daily, “Full text: China's Policy Paper on Latin America and the Caribbean” Nov. 06, 2008.

²⁶² Eduardo Garcia, “Ecuador signs contract to export oil to China,” Reuters. Jul 23, 2009 <http://www.reuters.com/article/GCA-Oil/idUSTRE56N04820090724> (accessed July 25, 2009)

Ecuador's.²⁶³ China also suffers from high corruption, lack of respect for human rights, and lack of interest in promoting democracy.²⁶⁴

The Significance of the Combination of Weak Governance + Malevolent Chinese Foreign Policy

China's own weakness may directly take advantage of the weak situation of Ecuador's governance to practice a foreign policy different from the one promised. The interaction effects of these two weaknesses will significantly impact the oil industry. As Correa becomes busy dealing with administrative issues and lack of support, China will have the freedom to ignore internal Ecuadorian problems, focusing instead on taking advantage of the oil industry. China is a promising investor, that may be granted low prices, oil blocks and exploration rights to develop the oil industry.

Weak governance allows for large scale exploration and oil extraction without restrictions that will impact social-well being and the environment. China has already express interest in getting rights over the Yasuni ITT, one of the most biodiverse locations in the world, expected to hold over a billion barrels of oil.²⁶⁵ If granted, China may have no incentive to be a responsible investor and instead create long-term damage in the lives of the indigenous peoples and species.

Weak governance and Chinese ambition over the oil industry may lead to macroeconomic instability, *dutch disease*, and low levels of employment. Macro instability may results from the unpredictable oil booms and busts related to oil price

²⁶³ Human Development Reports 2009 <http://hdr.undp.org/en/statistics/>

²⁶⁴ Oppenheimer, 83

²⁶⁵ Ellis, 20

variations, leading to uncertainty in how the money should be invested and used, and at times if overuse may lead to borrowing and debt crisis. *Dutch disease* results when the influx of capital leads to an increase in the price of home products while lowering the price of imported goods. In this case it will allow the full entrance of cheap Chinese goods, which along with Chinese FDI in oil will negatively reinforce specialization in oil and deter development of other industries. Therefore, because of the lack of strong governance to do a better job at planning for the future, long-term development will suffer from reliance on oil that is not conducive to technological upgrading and diversification. Further bad governance and Chinese lack of concern may conclude in the complete extraction of oil, as happened in Santa Elena in the 1960s, and as it may happen in Angola, where the fact that oil is limited is ignored.

The Oil Curse will lead to negative impacts on inequality and unemployment. Issues may emerge as lax Ecuadorian visa policies permit the entrance of Chinese immigrants.²⁶⁶ This already happened in Angola, where thousands of Chinese workers were brought for infrastructural and oil jobs, closing job opportunities.²⁶⁷ Immigrants may also find gateways for business expansion for selling Chinese cheap goods, bringing to Ecuador's cities Chinese competition against local good and loss of product value. Like Angola, many Chinese workers may live in specially-built compounds, separated from the locals, with large language and culture barriers.²⁶⁸

²⁶⁶ Cieslik 2010, 174

²⁶⁷ Johnson 2010

²⁶⁸ Jiang Shixue, 38 and BBC News "In pictures: China in Angola"
http://news.bbc.co.uk/2/shared/spl/hi/picture_gallery/07/africa_china_in_angola/html/6.stm (March 18, 2010)

The goal of cultural exchanges to deepen mutual understanding may not be enforced in a country under a weak government and oil hungry Chinese policy.²⁶⁹

Despite higher levels of unemployment and inequality, GDP may increase because economic growth relies on economic output, not human conditions. China may untap Ecuador's oil industry and increase state output and revenue. This money however has the potential to feed corrupted officials, with the rest in the Chinese hands who use it to purchase more oil.

Key Lessons

This scenario shows how the administration may become more authoritarian or more unstable as opposing and corrupted forces in power make a stand. It also shows how weak governance may lead to poor decisions and allow the Chinese dominate the oil industry. These forces play along to enable negative impacts in the economic well-being by creating competition against local markets, reviving the oil curse, increasing inequality and unemployment, and promoting some economic growth that has no direct impact in the economic wealth being. The results of high volatile commodity prices, unskilled labor, and little labor in high-technology, enforce possibilities of going back to the old development model of the 19th century. As evidenced by the 19th century model, dependence on primary goods is dangerous for growth, democracy, and development.

Factors worked together to enhance the outcomes, but Ecuador's political instability may be the main driver in enforcing this business as usual scenario that

²⁶⁹ Jiang Shixue 2008. 38

returns to the old development model, with features that may be worse than past ones because of China's lack of interest in promoting democracy, human rights or social justice in general. China also has a bad record of conducting FDI abroad by "...asset stripping... poor at transparency, corporate governance, and observing environmental standards."²⁷⁰ For other scenarios China's role will matter as a force of development and underdevelopment, but it is important to consider the main role of the state in this feature. The following scenario will test this role of the state, as we look into an Ecuador with weak governance but beneficial Chinese foreign policy.

Scenario 2: Not a Zero Sum Game

Weak Governance + Altruistic Chinese Foreign Policy

Not a Zero Sum Game demonstrates how China's FDI can promote progress to some extent even if conditions in Ecuador are not supportive of FDI. In this second scenario, we can expect that in the next decade Ecuador's GDP will suffer some moderate increases, unemployment will decrease slightly, and inequality will remain the same. It is a low to moderate growth scenario where some targets of economic development are pursued but not taken full advantage of.

The Significance of Weak Governance

In the last scenario, *Business as Usual*, I showed how weak governance could lead to the removal of Correa's administration as challenges grew against him from corrupted groups, as well as from opposition and the failures of his socialist reforms.

²⁷⁰ Kerry Brown and Peter Wood, 16

This scenario seeks to describe an Ecuador suffering from similar drawbacks of governance instability. In order to imagine this weak governance state we can either look at Correa's administration as being deposed or as continuing in power but under a weak incompetent administration that is soon to be replaced by another incompetent leader that continues the cycle of bad governance. Both scenarios of weak governance are plausible, especially when considering past presidential experiences. In this scenario, the implications of weak governance are the same ones covered in the last scenario.

The Significance of Altruistic Chinese Foreign Policy

An altruistic Chinese foreign policy is significant to the economic growth of Ecuador. China has substantial financial resources, state-owned corporations and a need for natural resources that can be met by Ecuador.²⁷¹ China can bring economic growth through direct investments and involvement in the expansion of the oil industry. China also has many resources to provide financial cooperation for advancing other areas and infrastructural needs.

By staying true to its foreign policy goals of greater ties for creative community solutions, China may directly play a positive role in the economic well-being of Ecuadorians. The likelihood of this happening is foretold by China's practices in Angola. Though China's primary involvement in oil-rich developing nations is related to securing oil resources, in Angola, China has demonstrated its commitment to new altruistic foreign policy by investing outside the oil industry. Despite the weak

²⁷¹ Ferreira 2008, 299

domestic governance conditions that did not require it to invest in other areas, China took action to improve human conditions after the Angolan civil war by financing infrastructural projects, installing clinics with Chinese doctors, building schools, and encouraging entrepreneurs to invest, promote the business scene and open jobs.

China can offer employment opportunities by opening businesses that provide more incentive for other local businesses to expand, while increasing employment opportunities. Chinese cheap products can directly benefit those families that lack financial means. These areas of investments along with participation in the oil industry can sponsor great economic growth. These improvements directly increase local job opportunities. China can guarantee economic growth and employment opportunities when investing overseas; however it can generate little or no impact on inequality, which is dependent on local government policies and practices.

The Significance of the Combination of Weak Governance + Altruistic Chinese Foreign Policy

The Chinese motive to enforce the so called “pillar of harmony,” centered on the idea of complementary economies and common struggle, cannot be effectively implemented unless Ecuador has the necessary strong political institutions to retain and expand Chinese skills and positive impacts.²⁷² China in Angola enforced altruistic foreign policy actions, invested in various areas and promoted opportunities for growth; however its impact was limited by Angola’s weak domestic governance.

²⁷² Xiang Lanxin 2008, 45

Weak governance challenges or fails to take advantage of any benefit brought by altruistic Chinese foreign policy practices. The oil industry in Ecuador has potential for further expansion that can bring in rapid revenue. China's first move to invest in the oil industry will effectively lead to economic growth and some spillover effects like the arrival of knowledge and technical skills. Altruistic Chinese foreign policy practices can directly provide investment in areas that reduce unemployment in new areas of business and the oil industry. However, issues of corruption and bad bureaucracy will not allow the money to be invested in areas where it is needed most. Some employment opportunities are offered, but there is no incentive to expand to other industries by the government.

The main problem in this scenario is the lack of communication and understanding between Ecuador and China, thus the potential for success will be limited in many areas. For example when considering the construction of a new international airports, or a road connection Ecuador to Brazil, the project may be limited by issues related to lack of communication, especially over a lack of state presence and oversight in the projects. The lack of support and recognition of the national government is problematic. Impacts are limited to some areas and all money brought in by Chinese presence to the state does not get invested in areas that can benefit the population as a whole. The incompetence of the state becomes a great burden as China may lose motivation to stay strong to foreign goals and have too much freedom in the oil industry.

Key Lessons

Long-term impacts are the most important to consider in this scenario. In Angola, high corruption levels have interrupted Chinese progress, after extending about \$11 billion in loans to Angola, China is facing the challenges of investing in a country with high levels of violence and corruption which make Angola a “sobering, dangerous place” for Chinese businessmen and workers.²⁷³ As China enters one of the most corrupted and oil-dependent nations in Latin America, any progress brought by investments may be short-live and will have no direct impact in the country’s economic growth. The lack of strong governance to push for reforms, may led to further reliance in the oil sector. This scenario follows the dependency framework of FDI, where Ecuador continues relying on foreign involvement for expansion in the oil industry, its major source of revenue. The Oil Curse is a thread that can be manifested the same way it did in the first scenario, *Business as Usual*.

This scenario is a “zero-sum game” for Ecuador, because despite the wide number of issues the nation is facing under weak governance, China’s arrival might bring some overall benefits to the economic development. If the Chinese leave the country and stop investing, Ecuador may look the same or worst that it did before China’s arrival. This scenario confirms how the role of governance is essential for development. From this scenario we expect no long-term impacts because of a weak and unreliable state; however outcomes may change entirely if development is enforced by a strong government. The following scenario looks at development from the point of view of strong governance, but malevolent Chinese foreign policy

²⁷³ Johnson 2010

Scenario 3: *Better Solo*

Strong Governance + Malevolent Chinese Foreign Policy Practices

In this third scenario, we can expect that in the next decade, Ecuador's GDP will achieve moderate levels of growth, and inequality and unemployment will start to decline. This will result from the interplay of two factors, strong Ecuadorian governance and malevolent Chinese foreign policy. The *Better Solo* scenario explores how a strong Ecuadorian government responds to China's negative foreign policy practices by pushing for governmental unity while focusing on new development models that shift away from oil dependence and reliance on foreign nations. Thus, it explores the potential for Ecuador's development without reliance on foreign investors who in the past had to impose domination and dependence on primary industries that often backed development.

The Significance of a Malevolent Chinese Foreign Policy

Many of the traits of China's foreign policy follow those already mentioned in the first scenario, *Business as Usual*, where the lack of clarity in foreign practices and the challenges of investments in the oil-industry and a growing Chinese population in Ecuador may lead to stifled development. This scenario demonstrates how in the near future, China may become a burden on Ecuador's development by promoting an aggressive policy that goes against their original foreign policy goals. Such policies may include direct investments and domination over the oil industry without any efforts to invest elsewhere in the Ecuadorian economy. China has no interest or goal

of investing and promoting other areas outside the oil industry, enforcing practices of the oil-led development model.

China's rising investments in the oil industry can bring rapid economic growth, but can also enforce overconfidence in partnership. As the Chinese consortium, the Andes Petroleum Company is granted more territory by Ecuador, China's actions and demands in the oil industry may bring revenue but no local improvements, nor long-term development. China may expand on exploration sides without considering the population in the area, nor the environment.

The Significance of Strong Governance

China's malevolent foreign practices and irresponsible investments may motivate the current administration of president Correa to act fast and implement policies against foreign investors, while implementing his socialist agenda. Correa's re-election under the new Constitution in 2009 made him the first president to be re-elected in office in the last thirty years. Since the election Correa has carefully evaluated Ecuador's foreign policy.

After the negative experiences of the 1980s and 1990s, under the neoclassical principles of the Washington Consensus, Ecuador has learned lessons regarding the negative impacts of foreign nations managing its progress and affairs. In the 1970s Ecuador's relied on oil revenue to expand social spending, lower taxes, and subsidize petroleum. Relying in the oil industry concluded in instability with the oil price crash that led to loss of invested revenue, economic decline and high levels of debt. In response, the US promoted neoliberal policies in the 1980s that did not attend the

state and people needs and by the end of the century Ecuador faced high inflation, foreign debt, and a drop in oil prices. Recent economic mismanagement, the currency crisis, and political instability have impeded Ecuador's economic development.

Taking these lessons, Ecuador under President Correa will act rapidly to deal with inequality issues and unemployment. Correa has committed to a new agenda that pushes for more jobs, more investments in education, and a focus on domestic industrial growth. Based on his knowledge as an economist, Correa decides to deal with the issue of extreme reliance on oil by investing in education and research opportunities for surveying advance and high technology practices that can be well implemented in Ecuador. The arts and Ecuadorian culture have been sponsored in an attempt to increase feelings of national unity. This change in altitude and visions for the future will prepare better the Ecuadorian society and government to the challenges foreign investors may bring.

The Significance of the Combination of Strong Governance + Malevolent Chinese Foreign Policy

China is originally welcomed to Ecuador as a new equal partner that can assist in development goals of the new administration and provide mutually beneficial exchange. However, these visions are soon challenged as China begins to enact dangerous provisions and act in a way that affects the conditions of Ecuadorians and make damages to the local environment. The likelihood of China acting against its original foreign policies, the ones covered in Chapter II, are enforced by recent events. On March 2010, Sino-Ecuadorian relations suffered a rocky start when China made

dominating demands regarding the finance of the Coca Codo Sinclair. According to President Correa, China made demands detrimental to the sovereignty of Ecuador. In response Correa restated how Ecuador's sovereignty is first and that it is unacceptable for a foreign nation to make decisions for Ecuador. Ecuador's response displays the way in which Ecuador's governance is changing by getting ready for any challenge China may bring in the near future.

Therefore gathering lessons from past experiences Ecuador moves quickly to respond to and make reforms against dangers that may result from China's investments. Against the malevolent Chinese foreign policy Ecuador enforces measures against investors that require them to pay taxes and abide under set contracts. Economic growth is sponsored through China's limited participation in the oil industry, and Correa's own actions to expand home industries. To improve the oil industry and continue to make more gains, Ecuador will push to finish the construction of the refinery of the Pacific, in order to refine its own oil, while expanding technologically and increasing efficiency in oil transportation.

Correa's commitment to the socialist agenda will create positive impacts by promoting equality and dealing with unemployment. New jobs are created through large scale projects designed to advance industries. For example the hydro plant projected to will provide hundreds of jobs in low and advanced labor areas and millions in savings because of less energy spending. The Manta airport is another project with much potential, which can become the first step to better relations within Latin American nations, and countries in Asia. Exchange with other nations in Asia, like Indonesia and Vietnam, can provide lessons and knowledge for better economic

growth. These efforts will result in more focus on home industries, jobs, and future growth prospects, while diversifying partners.

Another issue Correa will respond to is the dependence on one country for finance. Instead of turning to only China for finance, it will also look at new partners. For future projects, such as the construction of the largest hydroelectric plant of the Pacific, Coca Codo-Sinclair, and the Manta airport, Ecuador may turn for revenue to the countries it already has strong ties through regional association or commercial ones like the OPEC.

For more than three decades Ecuador has fared poorly in terms of development when compared to other developing nations in Southeast Asia, because of slow productivity growth, the need to “squeeze more output from the same inputs.”²⁷⁴ An Ecuador with high productivity growth first needs to create incentives for firms to expand and operate efficiently in the economy. As President Correa mentioned in an interview,²⁷⁵ the problem with development policies are not the policies themselves but the players who implement them. The new administration may then work for business in innovation, micro-finance and investments in education and other knowledge based industries, while fighting corruption and bureaucracy. Public and tax policies need to be settled and enforced to give firms confidence and equal treatment across Ecuador. In order to achieve all these goals, Ecuador will need to improve the oil industry and expand relations with other trade partners, while pushing for social reforms that in the long-term benefit the whole society. Policies and

²⁷⁴ “Latin America’s Unproductive Economies,” *Economist*, 25 March 2010, online

²⁷⁵ Interview Rafael Correa, on his book, *Ecuador: de Banana Republic a la No República*
<http://www.youtube.com/watch?v=uSGXGYIArAg>

reforms that may quickly affect inequality and unemployment include investments in the poorest and rural communities, new areas for jobs, better education, and fight against corruption and distribution of wealth.

Key Lessons:

The “Better Solo” concludes that China may act like any other past foreign partner, playing no significant role in improving Ecuador’s economy. However, this scenario expects that Ecuador’s governance will improve in the coming years. Thanks to the stability and vision of the new Correa administration, Ecuador may start working on its own economic development patterns. For the last three decades Ecuador has suffered from weak governments, poor investments in infrastructure, lack of social spending, and low levels of FDI. In response to these failures the administration of Correa is taking action pushing for development policies and being watchful of investing nations. Learning from lessons of China in Angola, Ecuador can then prepare itself for the opportunity or challenge China may bring.

In this scenario, the strength of the government is the most important factor in determining Ecuador’s economic progress. It provides an overview of how China’s malevolent foreign policies allow Ecuador to wake up and enable a strong administration while realizing that development does not lie in the hands of foreign investors, but in the hands of the state, its people and home industries. China acts as an incentive for Ecuador to move away from the old development model.

Scenario 4: No Chinese Tales

Strong Governance + Altruistic Chinese Foreign Policy

No Chinese Tales scenario explores how great unexpected development can result from strong Sino-Ecuadorian relations. In this last scenario, we can expect that in the next decade Ecuador's GDP will increase considerably, that inequality will decline and employment will rise. In the near future, Chinese investments get across to impacting different sectors, working with an efficient Ecuadorian government to shape a new and progressive development agenda for Ecuador. The *No Chinese Tales* scenario draws on Ecuador's and China's need for mutual economic growth.

The Significance of Altruistic Chinese Foreign Policy

With an expected 5.5 percent increase in oil imports in 2010, China expands the rigorous agenda for securing natural resources, while enabling positive impacts in investing nations.²⁷⁶ Though criticized for dominating markets and development in African nations, China most likely will pursue positive foreign policy practices in Ecuador. This is true for many reasons: China wants to be on good terms because of its interest in Ecuador's unexploited natural resources. Additionally Ecuador's location on the Pacific coast acts as a gateway to future oil and political and economic influence in Latin American.

The Significance of Strong Governance

Correa's presidency brings new hope against historically high levels of political instability, government ineffectiveness, poor rule of law, and corruption. As presented

²⁷⁶ Xinhua, "China expects 5% growth of net oil import in 2010. March 22, 2010 (accessed March 22, 2010) http://www.chinadaily.com.cn/china/2010-03/22/content_9625216.htm

by his recent political reforms, Correa takes action against corrupted powers and changes legislature to strengthen his power against them.²⁷⁷ Correa's vision centers on enforcing the rule of law and running quality public services programs with credibility and commitment. New reforms arrive to improve governance, while China arrives as a commercial partner and source of investment.

The fight against corruption is felt across difference areas of power and media. For Correa the media is business that sells frequencies and uses political influence to get government concessions.²⁷⁸ Correa ignores criticism for his actions against mass media sources, and instead focuses on his socialist agenda to attend some of Ecuador's critical problems. Correa's recent decision to impose provisions on foreign companies and investors while enforcing payment of taxes and contributions will grant the state more revenues and strength for social expenditure.

The Significance of the Combination of Strong Governance + Altruistic Chinese Foreign Policy

This scenario highlights the probability of China enforcing altruistic foreign policy practices, supported by Correa's goals of aligning with Asian nations for development and diversification. This last scenario may unfold relations characterized by positive economic growth, improvements in economic well being through high rates of employment and decreasing inequality, respect for the environment, and enforcement of democratic transparent practices.

Correa's efforts to remove Western presence over certain areas such as the Manta airport and oil exploration sides has meant enforcing ties with China for future

²⁷⁷ World Bank. "Country Data Report for Ecuador, 1996-2008"

²⁷⁸ Reuter. "Ecuador's Correa says to fight media corruption," May 23, 2009.
<http://www.reuters.com/article/idUSTRE54M1L220090523>

projects finance and cooperation for mutual development. Ecuador will strengthen ties with China because of shared goals for development. Economically, China is a source of trade and investment opportunities, opening new markets and diversification of Ecuadorian trade, and “China does offer a unique opportunity for the region to experiment with a new model of international relations.”²⁷⁹

Ecuador support of Chinese foreign policy goals will most probably result in stronger ties in the years to come. China’s practices of “multipolarism” over “unipolarism,” and enforcement of pragmatism, collaboration, and persuasion over coercion will help promote areas for knowledge sharing and effective investment.²⁸⁰ In many ways China enforces the idea of comparative advantage, arriving with complementary over competitive economy that will depend on Ecuador’s oil but in return leave a number of positive spillovers.²⁸¹ For example stronger oil relations may lead to increases in exports, higher Chinese FDI in areas Ecuador needs it the most, such as infrastructure, education and higher technology. It also allows the entrance into China’s internal markets, integrating Ecuadorian firms into global production chains, expanding trade and diversification.

China’s entrance may be the ultimate force leading to an increase in Ecuador’s opportunities for jobs and economic growth. Ecuador has benefits such as closeness to important markets; abundant natural resources that if managed well can bring economic opportunities, a profitable tourism industry, a diaspora community that over

²⁷⁹ Xiang Lanxin 2008, 57

²⁸⁰ Tokatlia, 64

²⁸¹ Xiang Lanxin 2008, 45

can invest in the nation, and potential for greater regional integration benefits.²⁸²

China has much to benefit from these qualities, especially the chance to expand to Latin American markets, a chance to spread China's presence in the world. Therefore to leave a good impression without calling US attention, China enters Ecuador with goals and plans set under a new foreign policy of mutual growth.

China's investments in oil may rapidly conduce to increase economic gains in Ecuador. If Correa's government handles the incoming revenue well by investing quickly in social wellbeing projects, China's investments and commerce bestow initiatives for economic growth and employment. China's focus in the oil field areas, located in the poorest regions of Ecuador, may directly benefit local populations with new jobs and engagement with the new investors.²⁸³

Spillover effects of Chinese investments in the oil industry includes the arrival of Chinese business people and cheap Chinese products that can push for better efficiency of home producers, enable production networks, and provide technical and administrative skills.²⁸⁴ Competition will force home industries to adjust and invest in firm quality and scientific knowledge. It can also provide poor consumers with affordable Chinese products, reducing the cost of living for low income families.²⁸⁵

To enforce and establish long-lasting sustainable ties China and Ecuador need to create institutions for cultural, language exchange for understanding and working on new creative ideas for development.²⁸⁶ Hu Jintao's foreign policy goals of strengthening ties and enhancing mutual political trust through collaboration and

²⁸² Gaye 2008, 139

²⁸³ IDS, 8

²⁸⁴ Daniel Lederman, Marcelo Olarreaga, and Isidro Soloaga 2009, 117

²⁸⁵ IDS, 25

²⁸⁶ Jiang Shixue 2008, 38 and Ellis 2009, 135

communication are sponsored through these initiatives.²⁸⁷ Serving in regional organization such as the UN Economic Commission for Latin America and the Caribbean (ECLAC) and the Latin American Integration Association (ALADI) has granted China with more insight into the development goals of Ecuador.²⁸⁸

China's altruistic foreign policy affects economic growth, inequality, and unemployment. Employment opportunities are offered by Chinese investors and by government investments in new industries, along with educational ones in new industries. While learning and working in new areas, the poor and middleclass will have tools to fight the pressing inequality gap. Though corruption is expected to remain high in the near future, the government has the strength to start implanting policies against such. Good relations with China can help in this purpose. Other "growth-growth" efforts include expansion of schools and medical facilities, and development of the banking sector.

Key Lessons

Though China dominates in the Ecuadorian-Chinese relationship, Ecuadorian governance has an important role to play in its ability to affect the way in which Ecuador takes advantage of Chinese FDI." The government has the most weight in impacting economic well being by investing in new industries to assure employment, and fighting corruption to deal with inequality issues. The government has to find ways to protect against foreign investors domination and to enforce environmental standards for investing firms, eliminating health and environmental costs. In return

²⁸⁷ Jiang Shixue 2008, 38

²⁸⁸ Jiang Shixue 2008, 35

China's bargains and foreign policy goals arrived as an unexpected positive opportunity. China can be a good partner when its actions are correlated with commitment to foreign policy goals of mutual development and commitment. With a set of foreign policies goals of non interference and equality, China can enter Ecuador with a promise of respect for sovereignty, culture and mutual exchange for growth.²⁸⁹

Evaluation of Scenarios:

The preceding scenarios highlight some of the many ways Sino Ecuadorian relations may evolve to affect the future of Ecuador. The interplay of governance and foreign policy are just two of many critical uncertainties that can drive these scenarios down different paths. These uncertainties were chosen because they play an important role in the way relations are shaping today and in determining a variety of different outcomes that can actually take place as Ecuador undergoes changes in its level of governance and China changes its foreign policy practices across regions of the world and when it sees it most fit to do so.

In the first scenario, the weak level of Ecuadorian governance combined with the malevolent practices of Chinese foreign policy. This scenario portrayed one of the worst case scenarios for Ecuador's future that may happen if the nation does not prepare for oil hungry China focused on expanding its influence. The second scenario tries to change the course of action of Chinese foreign policy but faces constraints because of Ecuador's weak governance. In this scenario benefits are limited to Ecuador itself and China loses incentive to act responsibly. The last scenario

²⁸⁹ Cieslik, 165

therefore analyzes the full pursuit of strong governance and altruistic foreign policy creating an overoptimistic scenario of Sino Ecuadorian relations.

One can conclude then that in the face of Chinese constraints (on foreign aid, domestic resources, and the scope for productivity improvement), a preferred strategy may involve enforcing government policy. For two scenarios I limited the role of governance to conclude that the level of governance has the most important role in enforcing progress and either protecting or taking full advantage of the challenges and opportunities China has to offer. But a responsible strong level of government does not seek the most capital gaining practices, but the most beneficial to the sustainable development.

Assuming that the government cuts spending in the social well-being and in new projects, while taking in a lot of revenue, then the results indicate that sustainable progress is not made and that money is conserved in the corrupted powers, thus we have something like the second scenario and like the reality Angola faces today. Though Angola is China's largest supplier of oil most of the profit goes to the wealthy and powerful.²⁹⁰ Angola still has a high mortality rate, and about 41 percent of the population is under poverty and unemployed.²⁹¹ Though China can be said to have posed great positive economic growth and some local improvements in infrastructure, the entrance of Chinese unregulated investments have been damaging and ignore recommendations on transparency and accountability.²⁹²

²⁹⁰ Natanson, 2

²⁹¹ CIA, Angola

²⁹² BCC, "As Chinese Prime Minister Wen Jiabao visits Angola." 20 June 2006
<http://news.bbc.co.uk/2/hi/africa/5080626.stm> (accessed Oct. 10 2009)

An important argument that is supported by these scenarios, and shared by this thesis and the political writer, Nicolas Shaxson, is the argument that the main issue oil rich nations face is related to actions of governments, often led by corrupted players, and the question of how they divert their nations' endowments to their own personal benefit.²⁹³ Therefore even if the China acted under altruistic foreign policy goals, strong internal governmental efforts are required to maintain an acceptable and progressive level of economic development.

Before turning concluding it is important to consider some wildcards that though unlikely to happen in the near future, still have the potential to undermine the progress explicated in the scenarios outlined above. One wildcard can be the complete exhaustion of oil in Ecuador, eliminating the oil industry, thus ending the mains source of revenue. Though little is discussed regarding this issue, the fact is that oil is a non-renewable resource and that Ecuador's holdings are limited to some amount, mostly located in the most virgin areas of the Amazon rain forest. The location of crude brings me to another wildcard that may not be such a wildcard after all, and that is extreme environmental and health impacts in the indigenous communities close to areas of oil exploration. Not only is oil extraction dangerous to the people there, but the fact that the next new oil developments where China may be soon involve are located in the Ishpingo Tambococha Titupini (ITT) put in danger hundreds of endemic creatures and local indigenous life and cultures. Other wildcards include natural disasters such as hurricanes or tsunamis that might dampen China's interest in Ecuador and undermine progress.

²⁹³ Shaxson, 1127

In sum, the findings of this chapter suggest that Ecuador's government has the primary responsibility of adopting reforms that move the nation towards economic development, while taking advantage of the assistance and opportunity China's investments afford. Now that we have some scenarios that consider some of the outcomes Ecuador can expect when investing with China, it is time to complete the **Table# 3** presented in Chapter II. Though these scenarios were based on educated predictions taken from a compilation of data and research collected throughout this study, there are many other possible outcomes that may shape Ecuador's near future. Additional scenarios are discussed briefly to get a more insight in how a small change can completely change the story line.

Table 3: Case Study Design and Scenarios

Case study design: Economies of Angola and Ecuador Pre and Post China		
	Angola	Ecuador
Pre-China	Economy devastated by war	Economic debt and instability
Post-China	Incredible Economic Changes	<i>Scenarios:</i> <i>Business as Usual</i> <i>No Chinese Tales</i> <i>Better Solo</i>

Conclusion:

In an unpredictable world, scenarios provide “constructive ways to think about the future and parse out the uncertainties in an inherently unpredictable setting.”²⁹⁴ No matter how we construct and look at these scenarios, Ecuador is a nation that has faced little change in development, following a slow pace that will persists unless it

²⁹⁴ Bernstein et al., 62

commit to an effort of development and fight against corruption. China is this new and extreme thing, the question is how much advantage and opportunity will Ecuador take from it. We discussed four scenarios, some extremely positive, some negative, and others that bring little to know change. The studies of scenarios cannot stop there though; many other events can take place and change the way that those described in this chapter might evolve.

It is important to keep in mind unforeseeable information, such as the election and victory of a leader that goes along or completely against Correa's reforms (if any) such that everything constructed is soon broken apart. What if the US suddenly decides to involve itself in Ecuadorian affairs? What if the regional integration of Latin America strengthens and unites all nations under a common goal and practices? What if other areas of the world decide to play an influential role in Ecuador, like Iran or Southeast Asian nations? What if nothing changes? The importance of the scenario studies is to provide models based on well-research analysis from which much can be learned.

CHAPTER VI:

Conclusion: What May Lie Ahead

What impacts will China have in Ecuador's economy and economic well-being?

In the presiding chapters, I demonstrated how Sino-Ecuadorian engagement may cause no development to extensive positive outcomes on Ecuador's economy and economic well-being. As explored through the Angola case-study and defined in the scenarios for Ecuador, the interactions between governance and foreign policy practices will determine, to some extent, the future economic development outcomes. To reach any of these development outcomes, Ecuador and China need to recognize their needs and the prospect of a beneficial partnership. While China is motivated to diversify its oil partners and secure oil reserves across the world, Ecuador has many more reasons to engage with China and to disprove the *cuento chino*, the perceived falsehood of Sino-Ecuadorian ties.

Factors underlining potential Sino-Ecuadorian ties are Ecuador's call for diversification in foreign partners and China's offer of a new development path. The rise of President Correa triggers this move to engage with China. While the president has pushed for internal reforms and regional integration, he has also sought partnership for exports and investments in the oil industry with other nations. While Correa's actions have proven to be the anti-free market forces of the Western Hemisphere, especially after the failure of neo-classical policies under the Washington Consensus. In response to this shift in thought and foreign policy,

Ecuador has been more attracted to China's economic model, the Beijing Consensus.²⁹⁵ Attractive features of this model include the promise of economic cooperation without political interference, and insights on mutual development and "growth-growth" development strategies.

Beyond these factors Ecuador's abundant oil reserves is the major incentive for rapid engagement between these two countries. Oil expansion and investments are driving forces for the engagement of both China and Ecuador. China wants to gain presence in the oil fields of Ecuador to secure oil for its growth needs, while Ecuador wants China's presence, as opposed to a Western one, to advance the oil industry. This promising partnership also has a strategic location. In comparison to other Latin American markets with significant oil reserves, Ecuador's location in the Pacific gives it easier access to Asian markets. At the same time its proximity Brazil, provides an outlook for future markets opportunities for China in the region.

Due to the Oil Curse related fears, investments and expansion in the oil industry brings about many concerns that need to be further evaluated. This thesis pays great attention to the issue of development and the Oil Curse, because economic growth and economic-well being cannot be enforced without attending these issues that have plague Ecuador's progress. According to Nicholas Shaxon the Oil Curse is well established and found in nations where governments are the most corrupted and prone to instability and conflict. Shaxon suggest that the only way to eliminate the Oil Curse is by "distribut[ing] mineral revenues directly and equally to all of the

²⁹⁵ Sheng Ding, 119.

country's citizens directly," thus ending the corrupted control of revenue.²⁹⁶ The possibility of this model ever being implemented in Ecuador requires a greater level of strong governance that seems more like a *cuento chino* than a logical idea. President Correa's administration is challenging this pessimism as he works to enforce socialist reforms and more fair equal distribution policies that seek a world as that that Shaxson suggested. However, as shown by the scenarios, governance in Ecuador is most often negative than positive and would be put against the corrupted and powerful in control. Concerning Ecuador's development it is important to establish policy that can deal initially with the corruption situation.

Though it is important to look at the positive impacts of the expanding the oil industry, and deterring the Oil Curse, it is also significant to remember that the rising raw material demand from China can be far from a blessing for Latin America. When dealing with China it is important to distinguish its positive foreign policy from its practices. China can be a swing producer that exports when prices are high and stockpiles when they are not attractive. Such creates reliance in oil and vulnerability to price changes. Ecuador is a failed oil state because it continues to rely on the same oil model. The new President has brought new hope to change this through a "citizen revolution," and regional partnership.

Despite the positive overview of the new Presidency and their view of China's development option, other issues stand against this "perfect marriage." Ecuador suffers one of the highest levels of corruption and worst level of governance in the region. At the same time China has a legacy as a dangerous partner that seeks its own

²⁹⁶ Shaxson, 2

growth without observing their own foreign policy views. This project used the scenario methodology to deepen the understanding of different outcomes that may result from the Sino-Ecuadorian relationship.

China's growth is an important issue for the US and for Latin America and for most oil rich developing nations because: "What matters for Oil Producers ... is not where China is today but how it compares with its position in the world at the start of the 21st century and where it is going to be in 2030."²⁹⁷ With growing oil demands increasing about 55 percent from 2000-2006, China needs to make sure to match its oil needs and interest with broader foreign policy relations.

Considering these points and hopes of further work on this area in the near future, I conclude this study in a three part discussion that covers important lessons to take from this study. Section I covers the key findings of the Angolan and Ecuadorian experience with China. Section II discusses weaknesses of this study and areas of future work. Section III concludes with some last thoughts on this research project.

The Dragon in Angola and Ecuador: Key Findings and Lessons

One of the key findings of this project concerns the results of China's investments in the developing world. By looking at the economic impacts and indicators in Angola's case, China was shown to be potential force for economic change and development. Despite great distance and difference in culture, by the 21st century Angola had become China's largest supplier of natural resources, while

²⁹⁷ Palacios 2008, 170

achieving surprising economic growth. A synthesis of data collected in this study is shown below, summing up economic growth and well-being indicators for Angola and Ecuador. Considering these findings in Angola, can we expect similar changes for Ecuador?

Table # 4: Angola and Ecuador: Economic Indicators

Outcomes	Angola pre-China	Angola post-China	Ecuador pre-West	Ecuador pre-China (Today)	Ecuador Future with China
GDP	(2000): 9.13 billion	(2008): \$83.38 billion	(1967): 1.46 billion	(2008): \$52.6 billion	?
Economic Growth (GDP growth annual %)	(2000): 3%	(2007): 20%	(1967): 6.9%	(2008): 6.5%	?
Income Inequality (Income held by highest 10%)	(2000): 45%	No data	no data	(2007): 42%	?
GINI	(2000): 59	No data	no data	(2008): 53.6%	?
Unemployment	(2000): Extensive, half the population	(2008): 8%	no data	(2008): 7.6%	?
FDI Flows (net inflows % of GDP)	(2000): 10%	(2007): -2%	(1970): 0%	(2003): 5%	?

This thesis also defined and considered the critical uncertainties of Chinese foreign policy and Ecuador's level of governance. The four scenarios demonstrated the importance of governance and Chinese foreign policy in determining future outcomes. They explore how different outcomes can result from different interplay of these two forces. . These findings are important because they identify for policy makers and leaders those areas in need of reform and protection.

The interplay results of governance and foreign policy led to the recognition of the core factor in assessing change and development. By looking at the scenarios I

concluded that among the uncertain variables, governance had the most weight in determining development patterns. The strength or weakness of governance determines a great extent how China's foreign policy will play out.

Another finding of this study considers the issue of oil and development. Though often portrayed as a negative force that hinders development and democracy, oil does not have to be a curse. If well managed, the oil industry can lead to promote development and help with challenges of inequality and poverty, by providing the nation with revenue to invest in its most needed areas. Ecuador can learn from past lessons, how to deal more efficiently with its oil industry.

A final key finding covered in this section is the growing competition for oil resources and China's bargain in defeating other growing areas of the world by seeking a new foreign policy and strategies of non-intervention to secure its need. Though an obvious finding, this study reaffirms the existing literature that China's future exposition will affect the global economy. This study wants to mark the importance of studying Chinese interest in Latin America and the development paths that it may impose there. As China gains presence in the global economic order, developing oil rich nations need to prepare for the opportunity or challenge China may bring. This study does not argue for or against China, it sought instead to discuss how China's role may manifest in a nation with petroleum and one that is open to China's investments.

Limitations and Future Research

This study focuses on creating different scenarios that demonstrate numerous paths of development for Ecuador if it engages in economic relations with China in the near future. Some of the strengths of this project are the use of theoretical arguments and comparative studies to create educated scenarios of Sino-Ecuadorian relations. Statistics were compared across a variety of sites. That said this study has many limitations and could be improved in many ways.

The first limitation pertains to the lack of time and space for a more inclusive country analysis. While the Angola case proved helpful, there are many cases that could have strengthened the argument and been better case-study models. It would have been more helpful and applicable to study China in another Latin American country and compare those outcomes as well. Also this study has been conducted while the events are unfolding; thus, some data and information regarding current agreements and success are not considered.

A weakness of this study is constraining Ecuador's development to four models that fail to cover all areas of concern and all forces at play in Sino-Ecuadorian relations. Each model needed a more holistic assessment of concepts that have affected Ecuador's development and more literature regarding opposing views of China's interest in the developing world.

Concluding Thoughts

My study sought to state the importance of using scenarios as a means for creating futures or economic modeling for policy makers. Also of using scenarios for the assessment of current world affairs and their affect on the development of nations. Using these methods my thesis sought to prove that it is wrong to say that Sino-Ecuadorian relations are a *cuento chino*, or a deceit that will never take place or bring any development in the near future. As observed throughout this study, there are several ways to examine how these relations may emerge and many results maybe unexpected.

On March 18, 2010, President Correa announced that he had suspended negotiations with China over financing the hydroelectric plant because of unexpected conditions and “mistreatment” that put in danger Ecuador’s sovereignty. A few days later Correa asked Taiwan for finance, which it refused to give. However, in less than a week China agreed to change the imposed provisions and initiate conversations for new hydroelectric proposal. The back to back track of complaints and issues regarding finance brings into context the relevance of these relations and the paradox of evaluating the *cuento chino*. One day President Correa says that the Chinese are lying and treating Ecuador as an insignificant commercial player, the next day Ecuador goes to Taiwan for finance, and on the third day, China confirms the strength of Sino-Ecuadorian ties. The unexpected ways these relations are evolving support the need to create multiple scenarios and evaluate how issues of governance and

Chinese foreign policy may be playing along to determining diverse economic development patterns for Ecuador.

My study supports and illustrates the many ways Sino-Ecuadorian relations may be constructed to determine a different future for Ecuador. Though the future is unsure, we can assess that China and Ecuador have a special relationship that will be shaped by different issues of internal governance and the external policies and practices of a growing China with energy demands. Both countries should use their past experience to better shape their partnership today and to determine progress in the future.

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