U.S. Foreign Policy in Latin America Leaves an Open Door for China

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In the last week or so much of the international business press has been focused on the problems of financial stability in developing countries, some of whom have recently become more vulnerable to capital outflows. The main cause is that investors are trying to get the jump on possible moves by the US Federal Reserve to allow interest rates to rise, which will draw capital from developing countries and cause their borrowing costs to rise.

Argentina has gotten some of this attention, as it allowed the peso to fall by 15% in one day and increased some access for Argentines to dollars on the official market. Venezuela is not as affected by these market developments, but is always negatively portrayed in the international media, and more so since its exchange rate system problems have caused its inflation to rise to an annual rate of 56% over the past year.

The two countries face different sets of problems, but both likely have to stabilize their exchange rates to resolve them. This is where international help can make a big difference, and there is one country that has both the ability and interest in doing so: China.

China has already helped Venezuela with tens of billions of dollars of loans – much of which has already been repaid – as well as investment. It has also provided significant lending and investment in Ecuador, Cuba, Brazil and other countries. But there is more that they could do at this moment.

Much of Argentina and Venezuela's problems stem from some residents believing, with strong encouragement from the media, that their domestic currency is not safe to hold. While it is true that both countries have high inflation and their currencies have depreciated on their respective black markets, it is not clear how much of this is due to fundamental causes and how much is driven by a bubble in the black market price of their currencies. (Certainly in Venezuela, the black market dollar rate is a bubble caused by buyers betting that local currency will fall).

In any case, both governments could stabilize their currencies, and would get a big head start on bringing down inflation, if they were to have a large enough supply of dollar reserves. And they would not necessarily have to *use* these reserves: Bolivia, for example, has had a very stable exchange rate throughout the seven years of Evo Morales' presidency – despite serious political turmoil (including a violent secessionist movement), bursts of inflation, and considerable nationalizations and other government policy changes (eg withdrawing from a World Bank (ICSID) seen as terribly "business unfriendly" by international corporations. But Bolivia piled up more reserves than even China (relative to its GDP), and nobody doubts the government's ability to maintain the domestic currency at or near its current exchange rate.

The IMF has provided a "Flexible Credit Line" of reserves that is not borrowed, but is available, to approved countries. Because the United States controls IMF policy in developing countries, the only three countries approved for the FCL have been Mexico, Colombia and Poland – three countries with right-wing governments (Álvaro Uribe was president in Colombia at the time) that Washington considers strategic allies. Mexico has access to a hefty $47.3bn that it has not needed to tap.

China has $3.8tn in reserves and would barely notice the money that would be necessary to finance a similar credit line for Argentina and Venezuela. In fact, China would most likely be better off even if the money were borrowed. Argentina's dollar-denominated foreign public debt is only about 8% of GDP; this means that it would never make sense to default on such a small debt. Venezuela is also at low risk for sovereign default, with $90bn in annual oil revenue and some of the world's largest oil reserves. Currently, China has the bulk of its reserves in American treasury securities, which are virtually certain to lose value in the near future as long-term interest rates rise in the US.

China has a big foreign policy interest in stabilizing Latin America. Unlike the US, which is a global hegemon with hundreds of military bases around the world, China has no foreign military bases and no empire. With the US "pivoting" toward Asia, supporting militarism in Japan, and seeking to maintain military dominance in east Asia, China's main interest is in the further development of a multi-polar world and a greater role for the United Nations, developing countries and international law and diplomacy. Latin America, and especially South America, has become independent of Washington in the past 15 years and has a strong political interest in these same issues, with deep historical roots.

By the best measures of China's GDP (i.e. purchasing power parity), the Chinese economy is already bigger than that of the US; and even at its current, slower rate of growth it will more than double over the next decade. As Yan Xuetong has argued, China is beginning a new foreign policy path in which it will form alliances as it did not do in the past.

Although these alliances will primarily be closer to home, most of Latin America is a naturally ally not only because of its increasing trade and commercial relations with China, but because of its common interest in an international political order that favors respect for national sovereignty and independence over unilateral intervention and military force. On the other side, Washington would like to get rid of all of the left governments in the region and return to a world of "limited sovereignty" there that it maintained 20 years ago. It is well worth China's efforts, which could be made at little or no cost, to help maintain stability in the region.