



# PUBLIC INFRASTRUCTURE AND THE CHALLENGES OF GLOBALIZATION

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# THE LIBERAL INTERNATIONAL ORDER

- Liberal international order since 1950s
  - Economic: GATT, WTO, EU, NAFTA
  - Political: NATO, US-Japan, US-ROK security pacts
- Economic consequences
  - Quadrupling of global GDP 1970-2008
  - Exit of hundreds of millions from poverty in developing world
- Political consequences
  - The “Third Wave” of democratization 1974-2010

# THE EMERGENCE OF POPULIST NATIONALISM

- The “democratic recession”
- Emergence of “illiberal democracy”
  - Democratic but not necessarily liberal
  - Rise of outsider anti-elitist candidates
- Examples
  - Hungary, Poland, Turkey
  - Anti-immigrant/EU parties in Europe
    - Front National, AfD, UKIP, Danish People’s Party, Swiss People’s Party
  - **The United States**



# WHY POPULIST NATIONALISM NOW?

- Three drivers
  - Economic
    - Disparate impacts of globalization and technological change
  - Political
    - Perceived weakness of liberal democracies in the face of economic and security threats
  - Cultural
    - Immigration and globalization as threats to traditional national identities
- Immigration as common denominator of populist parties

# Democracy in Latin America

## Definition of liberal democracy

Modern state, rule of law, democratic accountability

## Strengths:

Latin America most democratic region of the world

## Weaknesses:

Failure to create modern states

Persistence of corruption across region

Poor application of law

## Populisms of Left and Right

# What about the End of History?

History = modernization, development

End = goal, objective

**Karl Marx:**

End of history is communism

**Georg F. W. Hegel:**

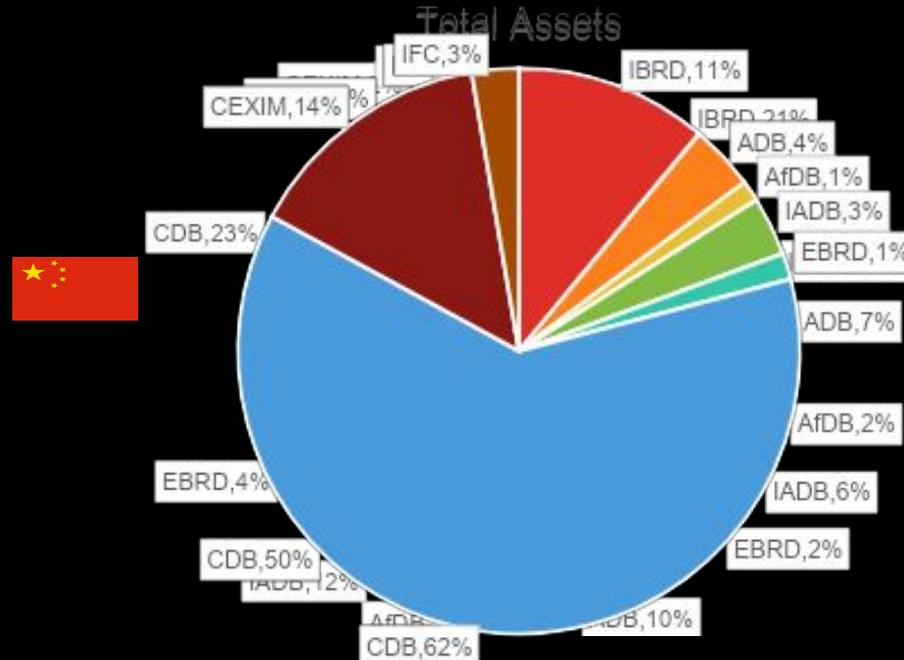
End of history is a liberal state

**Today's question:**

is there a higher form of social organization?

Challenge of the China model

# Trending West to East in Developing Economy Infrastructure Project Finance



2000

## Development Strategies: China v. US

- China's domestic development has been fueled by high levels of infrastructure investment
  - Up to 50 percent of GDP recycled into investment since 2008
  - Similarities to other East Asia fast developers
  - Large fiscal surpluses available for investment
- United States has turned away from infrastructure domestically
  - Lack of resources
  - Political gridlock
  - High cost of compliance with safeguards

# Drivers of Chinese Policy

Authoritarian  
Advantage

Strategic  
International  
Competition

Domestic  
Industrial  
Policy

# Drivers of the Trend



## Authoritarian Advantage

- Speed of development increases with state-centralized control of infrastructure projects
- Eminent domain, environmental concerns, community consultation less problematic
  
- Better explanation of domestic infrastructure growth
- International investments in both liberal democracies and other regimes

# Drivers of the Trend

*The Atlantic*

## China Is Quietly Reshaping the World

The staggering scope of the country's infrastructure initiative—and what it means for the international order

*At the sharp end*

How China's "sharp power" is muting criticism abroad

*And stealthily trying to shape public opinion in its favour*

Strategic  
International  
Competition

- General, high-level incentive to use infrastructure as source of influence
- Some evidence of correlation between infrastructure investment and geopolitical motives
- Limited effectiveness of infrastructure as geopolitical leverage

## Drivers of the Trend



Domestic  
Industrial  
Policy

- Massive excess internal capacity
- Longstanding “going out” policy as general guidance to invest abroad
- Policy banks are not designed as loss leading institutions

# Key Difference: Estimation of External Rates of Return

- ❑ Western approach to infrastructure investment
  - Initial focus on internal rates of return
  - Often topped off by public authorities
    - Role of the IFC and USAID/ExIm Bank
- ❑ Chinese approach
  - Internal rates of return are part of the calculation on a company level
  - Chinese authorities have different valuations of external rates of return than Western counterparts
    - Negative externalities are undervalued, positive ones overvalued
- ❑ Consequences
  - Chinese approach works much less well outside of China
    - China cannot capture externalities
    - Benefits come in terms of good will, strategic advantage, domestic employment

# Case of China's High-Speed Rail Network

- ❑ Between 2003 and 2016, China has created a HSR network totaling 22,000km
  - Compare to 2,647 in France, 3,164 in Japan, 0 in the US
  - Total investment now 5.4 trillion rmb (\$851 billion)
  - Total liabilities now 4,773 billion rmb (\$746 billion)
    - Debt ratio 65%
- ❑ Investment can be justified only in terms of long-term ERRs
  - MoR one of the last bastions of central planning
  - Initially seen as a pure public good
  - Inability to raise ticket prices
- ❑ Consequently, system loses huge amounts of money

# Rapid Infrastructure Buildout – Domestic v. International

- China's domestic infrastructure buildout coincided with the accumulation of bad debt at local government level
- Necessitated considerable local debt restructuring by national government
- Repeat of similar symptoms, but with sovereign counterparties

Policy banks get \$90b cash infusion

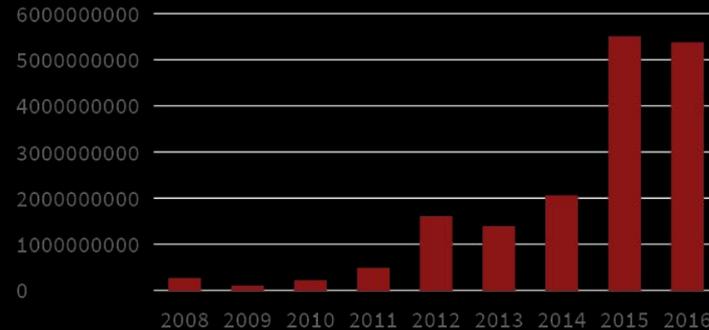
Chen Jia  
Updated: Aug 19, 2015 6:52 AM China Daily

## 2015 Cash Infusion

CDB CAR: 8.78% 11 → 1%

CEXIM CAR: 2.26% 12 → 7%

CEXIM – Loan Impairments (\$bn)



Source: Annual Reports

## Conclusions: China

- ❑ Chinese advantages
  - More centralized internal organization
  - Central govt willing to massively subsidize lenders
  - Lower costs, higher speed due to relaxed attitude towards safeguards and risk
- ❑ Chinese disadvantages
  - Overestimation of ERRs
  - Limited awareness of political risk
  - Speed and initial low cost harm long-term sustainability of projects
  - Despite centralization, internal institutional conflicts
  - Officials face conflicting incentives

## Conclusions: West

- ❑ World Bank
  - Safeguards regime designed for rich countries
    - And even there, not clear that it is appropriate
  - Procedurally slow
  - Limited resources
- ❑ United States
  - Resources limited by political polarization
  - No centralized decision-maker
    - Even with Presidential support
    - Too many agencies, too little coordination