INTERNATIONAL: Latin America wary of China dependence

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Abstract

The outlook for economic relations between Asia and Latin America.

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Full text

SUBJECT:The outlook for economic relations between Asia and Latin America.

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ANALYSIS: Impacts.

Economic relations between China and Brazil will become increasingly tense.

A sustained Asian, especially Chinese, slowdown would affect South America terms of trade.

In that scenario, prices for minerals will be more affected than those for food.

According to ESCAP's new report, Economic and Social Survey of Asia and the Pacific 2012, growth in the Asia-Pacific region (excluding Australia and New Zealand) will slip to 6.5% this year, down from 7.0% in 2011 (and 8.9% in 2010). However, Asia-Pacific would remain the world's fastest-growing region and its projected growth compares favourably with the 3.7% expansion for LAC forecast by the UN Economic Commission for Latin America and the Caribbean (ECLAC).

Downside risks.

There are two main downside risks for the and LAC Asia-Pacific (AP) regions:

Disorderly sovereign debt default in Europe.

According to ESCAP, this could reduce exports of goods from AP emerging economies by 3.0 and 6.3 percentage points in 2012 and 2013, respectively, compared to its baseline scenario, reducing the region's growth by up to 1.3 percentage points this year and 1.6 percentage points next year.

Higher oil prices.

The report estimates that a 25-dollar increase in international oil prices over an extended period would reduce growth in AP by at least 0.8 percentage points in 2012 and increase annual inflation by at least 1.3 percentage points (compared to its baseline projection of 4.8% inflation this year, down from 6.1% in 2011) (see INTERNATIONAL: Oil prices face medium-term decline - May 15, 2012).

	GDP Growth		Inflation	
	2011	2012	2011	2012
China	9.2	8.6	5.4	4.0
Japan	-0.7	2.1	-0.3	0.5
South Korea	3.6	3.5	4.0	3.3
India	6.9	7.5	8.4	6.5
Developing Asia-Pacific	7.0	6.5	6.1	4.8

GDP Growth and Inflation
Selected Asia-Pacific economies, %
Source: UN ESCAP

AP-LAC trade.

The increase in south-south trade, ahead of the overall growth of international trade, is particularly evident in trade flows between AP and LAC.

LAC exports to Asia-Pacific.

ECLAC estimates that LAC exports to AP climbed from 65.4 billion dollars in 2006 to 144.1 billion dollars in 2010, when they accounted for 16.7% of the region's total exports:

For Chile, the figure reached 49.7%, driven by sales of copper, its main export, to China (see INTERNATIONAL: Copper market set to face surplus - April 24, 2012).

In the case of Brazil, one of China's main sources of iron, growth reached 28.2% (see INTERNATIONAL: Chinese credit affects iron ore market - September 30, 2011).

It was 26.5% for Peru.

ESCAP suggests that, in the coming years, the annual increase in LAC exports to AP could reach over 25 billion dollars.

Asia-Pacific exports to LAC.

According to ESCAP, AP exports to LAC reached 194 billion dollars in 2010, up from just 4 billion dollars in 1990. The agency anticipates a continuation of this trend as AP economies increasingly look to markets in LAC (as well as Africa) in the face of weaker sales to industrialised countries:

By 2010, AP accounted for 27.2% of LAC imports, up from 10.6% in 2000, and in Chile, Peru, Mexico and Brazil it reached around 32%.

However, for AP, LAC remains a small market, with ECLAC estimating that it accounted for an average 3.7% of exports from developing Asia in 2008-2010.

Bi-regional FDI.

		Destination					
		Africa	Dev. Asia	LAC	Middle East	CIS	All dev.
Origin	Africa	12.2	18.4	4.0	3.9	0.5	39.0
	Developing Asia	2.8	47.6	3.7	3.8	1.7	59.6
	Latin America/Carib.	2.1	13.2	20.3	1.6	1.1	38.3
	Middle East	4.6	51.5	1.1	10.8	0.8	68.8
	CIS	2.1	13.3	1.2	2.7	18.1	37.4
	All dev. countries	3.3	39.0	5.6	3.9	2.8	54.1

South-South trade, 2008–10
% of total exports
Source: ECLAC

Asian investment in LAC was virtually non-existent until the mid-2000s, but has since increased sharply, led initially by Japan and South Korea and, more recently, China. ECLAC estimates that, in 2011, Asian companies accounted for some 9% of foreign direct investment (FDI) in LAC of 153.4 billion dollars (see LATIN AMERICA: Strong FDI growth will slow this year - May 10, 2012). Out of the ten largest mergers and acquisitions by overseas investors in LAC in 2011, three corresponded to Chinese companies (in the oil and gas sectors of Brazil and Argentina and in mining in Brazil) and two to Japanese companies (in mining in Chile and beverages in Brazil).

Initially, Asian FDI in LAC sought to ensure supply of raw materials and guard against fluctuations in their prices. Nonetheless, it has since diversified into infrastructure (where it is partly related to access to raw materials but also to the investors' competitive advantages in this field) and, as labour costs in Asia have risen, into sectors such as car making, electronics and textiles -- principally in Mexico and Brazil as a platform from which to target US and other Latin American markets (see INTERNATIONAL: China's wage-related advantage declines - March 28, 2011).

Latin American companies investing abroad -- the so-called 'trans-Latins' or 'multilatinas' -- are still few in number and have so far focused on other Latin American countries. As a result, LAC investment in Asia remains incipient, albeit growing, driven by Brazilian, Argentine and Mexican companies.

Challenges.

Although bilateral relations are crucial for the growth of both Asia and LAC, they also pose a number of challenges:

Commodity-producer trap.

Asian, and particularly Chinese, demand for raw materials has been a key factor in South America's recent growth but also has been to the detriment of the export diversification the sub-region had previously achieved. In a challenge shared by AP commodity exporters, this negatively affects job creation and quality, with an adverse impact on income distribution (see INTERNATIONAL: 'China effect' on EMs is multifaceted - September 21, 2010).

Consumer-product rivalry.

Although Chinese imports of products such as clothing, footwear and electronics have much reduced the price of these products in LAC, significantly increasing the purchasing power of lower-income segments of the population, they have also triggered resentment, particularly in Mexico and Brazil, by competing in both domestic and third-country markets and have fuelled pressure for protectionist measures (see CHINA/EU: Bilateral relations leave euro crisis behind - May 2, 2012).

Partly as a result of the differing interests of LAC countries in their relations with Asia, trade liberalisation between the two regions has taken the form mainly of bilateral free trade agreements, led by Chile and Peru, while progress on multilateral initiatives such as the so-called Pacific Arc, an alliance of Pacific Coast LAC countries designed to strengthen their relations with the Asia-Pacific region, has been slow and there are important doubts as to the prospects for the proposed Trans-Pacific Partnership (TPP) trade agreement (see

US/JAPAN: Trade talks will hinge on Japan's farmers - November 3, 2011).

CONCLUSION: Economic relations with Asia differ significantly across the Latin America region. However, without an acceleration of the incipient diversification of trade and investment flows, these relations will strengthen the widespread perception in LAC that, rather than a win-win situation, they represent a new centre-periphery relationship, with China as the centre and LAC as a periphery increasingly focusing on exports of primary products.

Details

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