Latin American Iron and Steel Congress

WORLD ECONOMIC SITUATION AND CHINA’S IMPACT ON LATIN AMERICA AND THE CARIBBEAN

• José Luis Machinea
  • Executive Secretary
  • Caracas, 31 October 2005
Summary

- World economy and trade 2004-2006
- China and Latin America: trade trends
- China and Latin America and the Caribbean: strategic relations and prospects
The economy in 2004-2005

- In 2004, GDP and world trade grew at the highest rates in 30 and 25 years, respectively.
- International trade and financial flows have shifted owing to the strong influence exerted by China and other Asian economies.
- The global business cycle is increasingly shaped by the link between the United States and China.
- The situation is unstable due to significant macroeconomic imbalances, and inflation is starting to trend upward (demand and oil).
- Current cycle effects are more beneficial for South America (and, to a lesser extent, Mexico) than for Central America.
In 2004, world exports again exceeded their historic average, growing by 10% (at constant prices)

Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of official figures from the World Trade Organization (WTO).
China is rapidly becoming increasingly important in the world economy

CHINA: PARTICIPATION IN WORLD ECONOMY
(Percentage of total)

- GDP (purchasing power parity in dollars)
- GDP (in current dollars)
- World trade (exports)
- Foreign direct investment received

Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of figures from the International Monetary Fund (IMF), the United Nations Conference on Trade and Development (UNCTAD) and the World Trade Organization (WTO).
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(Percentage of total)

Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of figures from the International Monetary Fund (IMF), the United Nations Conference on Trade and Development (UNCTAD) and the World Trade Organization (WTO).
The current cycle is favourable, but is based on unsustainable imbalances

Globally, growth is strong, inflation is low but rising, and interest rates are low

China has a positive influence, as it supplies inexpensive goods that sustain domestic demand in the United States and finances the deficit at low interest rates and (up until a few months ago) low inflation

Certain imbalances and threats remain: a hefty current account deficit in the United States and the associated forms of adjustment; revaluation of the yuan and worldwide exchange-rate adjustments; higher oil prices and interest rates
Current account imbalances (1997-2004)
(Billions of dollars)

Source: IMF, World Economic Outlook, September 2005.
The United States trade deficit with China, Japan and developing Asian economies is reflected in increased purchases of United States treasury bonds.

Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of figures from the United States Department of the Treasury and Department of Commerce.
How should the United States’ current account deficit be tackled?

The United States’ current account deficit is offset by a surplus (excess saving) in Asia (Japan, China, India, etc.), oil-producing countries and Germany.

The general consensus is that the United States’ current account deficit poses a threat to the world economy. A smooth and gradual solution to the problem will require policies aimed at absorption and relative price adjustments, both in deficit and in surplus countries.

Oil-producing countries, China and Asia in general also need to:

- Save less and spend more on productive investment (infrastructure improvements), social security, pensions, health and social spending in general (hospitals, schools, etc.)
- Undertake financial reforms aimed at: (a) encouraging companies to pay dividends; and (b) increasing access to credit for low-income groups
Developed countries’ real effective exchange rates
(Index: base year 2000 = 100)

Traditionally, rising oil prices tend to drive up interest rates. This has not happened in the last four years, but...

Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of official figures compiled by the United States.
The United States consumer price index has begun to climb in recent months, which could prompt the Federal Reserve to raise interbank interest rates.

In the United States, the monthly inflation rate for September 2005 (1.2%) was the highest in 25 years, while annual inflation to September (4.7%) was the highest in 14 years.

In the Euro Zone, the year-on-year rate for September 2005 (2.6%) was one of the highest in 4 years.

Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of official figures.
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In 1990, China’s share of world consumption of selected products was less than 5%.

Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of figures from the World Bureau of Metal Statistics (WBMS), the Economist Intelligence Unit and the United Nations Conference on Trade and Development (UNCTAD).
In 2004, China’s share of world consumption of tin, zinc, soya and aluminium was over 20%, and consumption of other products had also increased considerably.

![Percentage of world consumption, by product](chart)

Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of figures from the World Bureau of Metal Statistics (WBMS), the Economist Intelligence Unit and the United Nations Conference on Trade and Development (UNCTAD).
In 2004, 4% of exports from Latin America and the Caribbean went to China, which is now one of the main trading partners of several countries in the region.

In the first half of 2005: Chile (12% of exports), Peru (10%), Argentina (8%) and Brazil (8%).

Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of official figures.
South America: structure of exports to China and the world, by technological intensity, 2003

Source: Economic Commission for Latin America and the Caribbean (ECLAC), on the basis of official figures.
China and Latin America: features of trade (A)

Latin America is still a relatively small market for China, accounting for 3% of China’s exports and 4% of its imports.

Yet the market is buoyant: between 2000 and 2004, Chinese exports to Latin America jumped by an annual rate of 42% to US$ 21.668 billion, which was higher than the growth rates for exports to the rest of the world.

China accounts for only 4% of Latin America’s exports and 5% of its imports.

China has replaced Japan as the region’s main trading partner.

South America benefits from increased Chinese demand for commodities and lower prices for manufactures it purchases from China.

Central America is facing fiercer competition in textiles and maquila products in the United States market, which affects its sources of growth and generates unfavourable terms of trade (oil).

Mexico faces a similar situation but has more means of defending itself, such as NAFTA and oil.
The terms of trade have improved as a result of growing Asian participation in trade.

Terms of trade may remain high in the medium term.
China and Latin America: features of trade (B)

Trade flows are beginning to diversify, although inter-industry trade continues to predominate. Latin America exports primary products, while China mainly exports manufactures at varying levels of technology (low, intermediate and high).

Latin America is China’s main supplier of soya, copper, iron ore, nickel, fishmeal, hides, sugar, zinc, tin, grapes, etc.
Selected products for which the region supplies over 20% of China’s imports

% of China in world imports

- Nickel
- Soya
- Iron ore
- Copper
- Wood pulp
- Sugar

% of Chinese imports from Latin America and the Caribbean

- Cuba
- Argentina and Brazil
- Brazil and Peru
- Chile and Peru
- Chile, Argentina and Brazil

Source: Economic Commission for Latin American and the Caribbean (ECLAC), on the basis of official figures.
For Mexico and Central America, China is a competitor in the United States market  
(Textiles and clothing)

China and some Latin American and Caribbean countries: Share of United States imports (percentages)

Source: Economic Commission for Latin American and the Caribbean (ECLAC), on the basis of official figures.
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China’s interest in Latin America

- Because of its rapid growth, China needs a sure supply of raw materials and food (energy, minerals, metals, wood, soya)
- China seeks a market for its exports with a minimum of what it considers unreasonable anti-dumping accusations (market economy status)
- China wants to ensure that bilateral or regional trade agreements between Latin America and third parties do not harm its exports
- China wishes to strengthen relations with Latin America and the Caribbean in the same way that the United States and European Union are strengthening theirs with Asia or Latin America and the Caribbean
- For political and trade-related reasons, China is focusing on South America
- Hence, the key to these new bi-continental relations lies in the China-Brazil link and in how MERCOSUR approaches the issue
New stage in relations between China and Latin America and the Caribbean

- Intense exchange of high-level visits (more so than with the United States or the European Union)
- Broad network of investment and export agreements in:
  - Mining, agriculture, infrastructure
- Challenges for the region:
  - Identify and take advantage of complementarities
  - Foster business and technological partnerships
  - Encourage intersectoral trade
  - Join in the productive integration process focusing on China that is under way in Asia
  - Stimulate investment flows in this direction
China and Latin America: trade opportunities

- China offers large markets for Latin American exports
- Latin American and Caribbean countries are major exporters of energy, minerals, raw materials and agricultural products
- Chile and China have a special relationship: first free trade agreement (FTA) in the region, bridge between southern Latin America and the Asia-Pacific region

Network of negotiations
- Chile-Republic of Korea: first trans-Pacific FTA
- Chile-China
- Pacific Four (P-4): Chile-New Zealand, Singapore and Brunei
- Peru-Thailand (5th round)
- Peru-Singapore (negotiations soon to begin)
- Peru and Thailand may be invited to join P-4
- Peru actively seeking FTA with China and India
- FTAs in force: Thailand and New Zealand, Japan-Singapore
- Thailand proposing FTAs with Chile and with MERCOSUR
- Republic of Korea proposing FTA with MERCOSUR
- Republic of Korea is a full member of IDB and China is applying for membership
China and Latin America: building the future

- Considering China a strategic partner
  - Steady high demand for natural resources
  - Good outlook for terms of trade
  - Capitalize on these trends in terms of innovation and productivity

- Linking trade and investment
  - Take advantage of the boom in natural resources to strengthen technological and production linkages
  - Attract Chinese investment and venture to invest in China

- Participating in regional value chains structured around China
  - ASEAN is a considerable threat in terms of competition
  - The region should enter production and business networks in Asia that revolve around China

- Linking this strategic partnership with the new spirit of integration
  - Legal certainty
  - Macroeconomic stability
  - Unified markets (disputes, sanitary and phytosanitary measures, technical standards and rules of origin)
  - Energy and infrastructure
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