



The New Axis of Trade

A brief assessment of Sino-Brazilian economic relations since 2000

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Abstract

Although frequently described as complementary economies, Brazil and China increasingly compete on a number of industrial sectors. China is affecting labor-intensive industries in Brazil and is rapidly gaining market share in more technologically advanced segments. A popular view, much debated in 2005, is of a Chinese commercial invasion; this is not the case, however. The real immediate threat to Brazilian industries, particularly those engaged in exporting activities, lies beyond the national borders, as they increasingly face stiff competition from similar Chinese products in third markets.

Widely announced Chinese investments in the region are still to be implemented. After South American presidents queued to visit Beijing and later hosted Chinese president Hu Jintao in 2004, Chinese interest seems to have steadily diminished in sectors such as infrastructure. While some projects are advancing, circumstances in the host countries or in specific industries have led several others to be suspended.

Public perception about bilateral economic relations has swung widely in Brazil, from widespread awe in 2004 to widely held anti-China positions in 2005. In the beginning of 2006, those extreme views seem to be giving way to more serene positions. Especially in Brazil, it seems to be getting increasingly clear China carries a complex combination of opportunities and challenges, and the country could largely benefit from China's economic growth—and compete in third markets—should it implement the right policies to boost competitiveness and trade.



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Introduction

A new axis: Brazil and China will redefine the geography of trade. China bans Brazilian soybeans. Lula takes 500 businesspeople to China. Safeguards are necessary to protect our industries against China's unfair trade practices.

The paragraph above may seem confusing; one could hardly find four more irreconcilable phrases. And yet they are all headlines belonging to the same context—the rapidly evolving economic relations between Brazil and China—marked by strong polarization in public opinion about the economic relationship with China.

The fascination that prevailed in the Brazilian media in the first months of 2004, prior to a state visit to China that took a monumental business delegation to Beijing and Shanghai, gave place half a year later to strong public skepticism about bilateral relations. From economic panacea and strategic partner, China was quickly downgraded to a vile competitor destroying jobs in Brazil, with headlines commonly pointing to the industrial damage caused by Chinese imports and demanding the application of safeguards.

The origins of such extreme views can be traced back to recent developments in bilateral trade. The value of Brazilian exports to China grew an explosive 900% since 1999. It was commonly taken for granted that China's seemingly insatiable appetite, not only for soybeans and iron ore but also for auto parts, chemicals and other industrial inputs, was to propel Brazilian exports for many years ahead. On the other hand, starting in 2005, some industrial sectors—especially apparel, footwear and toys—began to present very vocal complaints about an alleged invasion of Chinese competitors. Others were soon to follow, equally concerned about the rapid penetration of Chinese electronics, machinery and industrial components in the Brazilian market.

Over the same period, the massive Chinese investments in infrastructure and natural resource industries that had been announced in the 2004 presidential visits failed to materialize. President Lula was the first Brazilian head of

state to visit China in a decade, and the enthusiasm for all things Chinese could be measured by the nearly 500 business representatives who accompanied him. President Hu Jintao reciprocated six months later, also leading a large business delegation. On both occasions, major projects were presented as material evidence of a new era in Sino-Brazilian relations. In the short term, an amount between US\$ 6 billion and US\$ 10 billion would be invested in Brazil, helping to soften significant bottlenecks that compromise export growth and industrial competitiveness.

Although they cannot be singled out as the most important factor leading to this outcome, the investment announcements made it easier for Brazil to grant China its much-demanded market economy status. In spite of strong opposition from some industrial sectors, the Brazilian government made this bold political gesture as a concrete mark of the "strategic partnership" with China, a term coined in 1998 by President Fernando Henrique Cardoso and Prime Minister Zhu Rongji. Two years after Lula's visit to China, however, only one of those large projects is still advancing (ABC, an alumina plant jointly developed by CVRD and Chalco). The others were halted or postponed due to causes varying from changes in the specific industries to tax-related issues.

The event that triggered increasingly negative views against China was the ban imposed on Brazilian soybean imports, allegedly because of fungicide contamination, when President Lula was landing in Beijing. Timing could not be worse for a relationship that would steadily deteriorate over the next year. Soybean prices were at a historical record when the president went to China. In the ensuing weeks, the Chinese intervention made them plunge, leading to significant losses among Brazilian producers and exporters and also affecting oilseed crushers in China (refer to box entitled "Beans of Wrath").

In the final months of 2005, the strong polarization about relations with China seemed to be converging to a more balanced perception. Currently, the press, government officials and business representatives increasingly assess the bilateral relationship in terms of the

enormous opportunities and challenges it entails. It is becoming more widely accepted that Brazil has benefited significantly from China's huge appetite for commodities, that it is inevitable that some sectors will be strongly and negatively affected by Chinese competition, and that only a strategic, long-term view, with public and industrial policies designed accordingly, can provide the much-needed boost in competitiveness that the Brazilian economy requires in order to face the rapidly mounting challenges coming from China, India, and several other emerging Asian nations.

SECTION ONE – TRADE

Is an invasion taking place?

In the first two decades of China's economic opening, trade with Brazil performed below its potential, with relatively few firms engaged in bilateral exchanges. A tectonic shift began to take place in 1999, caused by China's strong demand for raw materials, especially soybeans and iron ore. In the following six years, Brazilian exports grew exponentially, and China assumed an increasingly important role as supplier of industrial parts to Brazil. In the 1990s, China did not rank significantly among Brazil's trade partners; in 2003, however, it became the third largest destination of Brazilian exports (Table 1).

Steep increases in trade produced an asymmetrical relationship. Brazilian exports to China are heavily concentrated in a few sectors, notably mineral ores and soybeans, whereas Chinese exports are highly diversified, with a strong participation of electronic parts, machinery and telecommunications equipment. In 2005, iron ore, soybeans and their sub-products accounted for nearly 60% of all exports to China, whereas no single Chinese product accounted for more than 5% of the total value exported to Brazil.

At the same time, during the first half of this decade, Brazil experienced significant difficulties in agricultural trade - the sector in which the implementation of WTO commitments has been least effective in China. Few countries are better suited than Brazil to provide China with the

agricultural products that it will increasingly need to import as its average income raises; this is especially true for land-intensive crops, meat, fruit juice and, eventually, ethanol. However, market access has been hampered by the opacity of Chinese regulations, technical barriers raised by the Chinese bureaucracy, and slow market-access negotiations (see box about soybean trade below).

Compared to the average patterns of Brazilian foreign trade—with exports of manufactured goods and industrial parts accounting for the majority of the traded value—exports to China are atypical, highly concentrated in natural resources. This is a result, on the one hand, of the swift responses the mineral and oilseed industries were able to give to changes in Chinese demand in the last ten years. On the other hand, although a growing number of Brazilian manufacturers insert their products competitively in China, Brazilian and Chinese industries are widely overlapping, which translates into a more competitive, rather than complimentary, nature between them (Table 2).

China is rapidly gaining market share in nearly all industrial goods it exports to Brazil, in detriment of Brazilian and, especially, foreign competitors. Several Brazilian industries point out that a menacing Chinese invasion is taking place, and this is frequently stressed with statistics signalling shifts in market share and import growth, as well as job losses in labor-intensive industries such as apparel and footwear. Double or triple-digit import growth of certain products reinforces this interpretation.

Tempting as it may seem, the commercial-invasion thesis is not broadly supported by trade statistics. Growth in exports to Brazil over the last years is consistent with the expansion of China's industrial competitiveness and global reach. It is also consistent with foreign investment in increasingly sophisticated industries in China. Analyzed comparatively, trade data show China quickly replacing more traditional suppliers of the Brazilian industry, a trend clearly identifiable in the cases of American, European and Japanese players, especially in Brazilian industries that have historically depended on foreign inputs, such as

electronics, appliances, telecommunications equipment and machinery.

Critics also point out that granting China market economy status in November 2004 opened the floodgates to imports of cheap products. This argument has been explored as a major strategic mistake made by the Brazilian government, thus weakening the national protection mechanisms against unfair Chinese trade or industrial practices. The two governments signed a memorandum of understanding in November 2004, through which China was recognized as a market economy and a compromise was sought out to solve some trade and investment-related issues.

There is no correlation between the strong import growth registered in the first half of 2005 and that governmental decision. Granting China market economy status was a bold move by the Brazilian government, albeit one without sizeable commercial gains. The only significant effect of the memorandum then signed, in conformity to World Trade Organization rules, is a change in antidumping investigation procedures. Brazil thus agreed to cease using third-country normal prices as bases for comparisons in antidumping investigations.

The rationale behind the concession was that market status was an inevitable outcome of China's accession to the WTO, so that Brazil could draw economic and political benefits from its early support to China's demand. Since becoming a WTO member in December 2001 and thus accepting to be treated as a non-market economy for the following 15 years, China had been demanding to several countries bilateral recognition as a market economy. President Hu Jintao visited Brazil in November 2004. Since the beginning of that year, all official delegations and even missions of state-owned enterprises presented the market-status requirement as the country's most pressing need regarding its economic and political relations with Brazil.

It was also expected by the Brazilian government that, after being granted the desired status, China would come to support Brazil's bid to occupy a permanent seat at the United Nations Security Council should it be reformed.

This expectation was plagued, however, by China's seemingly opposition to UNSC reform—any of which is to include its historical rival Japan—and the lack of concrete clauses in the memorandum through which China obtained its recognition as a market economy.

Bilateral trade performance: 2000-2004¹

This section does not aim to offer an exhaustive analysis of the recent evolution of Sino-Brazilian trade nor does it advance policy proposals to increase or diversify trade with China or third countries; rather, it is limited to an overview of trade data in a few industries. Trade with China is compared to exchanges with Brazil's major partners: the United States, the European Union and Argentina, as well as with the total amounts imported by the country.

All data analyzed are provided by the Brazilian Foreign Trade Office (SECEX). It is important to stress that there are significant discrepancies between Brazilian and Chinese trade data. Some of them can be attributed to different methodologies used by the national statistical services. A large part of the differences, however, seems to be due to illicit trade practices (a large amount of Chinese imports circumvent Brazilian customs under several creative arrangements), which have a sizeable, negative impact on a growing number of Brazilian industries.

Table 1: Sino-Brazilian trade
US\$ millions

Year	Exports	Var %	Imports	Var %
1999	676	-25,3	865	-16,3
2000	1.085	60,5	1.222	41,3
2001	1.902	75,3	1.328	8,7
2002	2.520	32,5	1.554	17,0
2003	4.533	79,8	2.148	38,2
2004	5.439	20,0	3.710	72,7
2005	6.834	25,6	5.353	44,3

Source: SECEX

¹ Trade data covering the fiscal year of 2005 were not yet fully available when this article was written. Unless otherwise indicated, data and graphics shown are limited to the 2000-2004 period.

1. Exports

Sino-Brazilian trade experienced an enormous leap in the first half of this decade. Propelled by China's intense demand for natural resources, Brazilian exports grew by 900% since 1999. Imports from China grew an also impressive 600% in the last five years, and have been gathering momentum since 2003.

Compared to other countries that have been heavily investing in their relationship with China and developing the institutional framework to deal with this likely next economic superpower, Brazil is a sort of latecomer. Apart from a few exceptions, Brazilian companies lagged significantly in developing strategies for the Chinese market, for competition against Chinese similar products or for investing in China as a competitive export platform or a strategic access to China's potentially huge market.

Table 2: Composition of Brazilian exports in 2004 (%)

Products	World	Argentina	US	EU	China
Basic, raw materials	33,4	4,6	8,4	47,4	59,6
Semi-manufactures	50,0	3,7	18,2	11,4	22,7
Manufactures	16,6	91,3	73,4	41,2	17,7

Source: SECEX

Nevertheless, trade expansion and bilateral investment in the last few years suggest a new, if still incipient, degree of maturity vis-à-vis the Chinese economy. The government also took note, albeit belatedly, of China's crucial role in world affairs—over the last two years, governmental institutions have been gearing up to deal with China. While it has been making progress, Brazil still has a long way to go if it is to explore its full potential in the Chinese market and implement public policies to boost the competitiveness of its products both internally and in foreign markets where it increasingly competes with China.

Starting in 2001-2002, strong growth in commodity exports to China resulted in equally perceptible interest in China arising from other businesses, especially manufacturers. In April 2002, the first significant business mission to China in nearly a decade took place, led by the Ministry of Foreign Trade. From that point on, a

steady flow of Brazilian executives could be seen roaming through Chinese cities, searching business opportunities and presenting their products.

In spite of the high concentration and impressive values traded in mineral ores and soybeans, Brazilian exports to China have shown greater dynamism in products with intermediary technological levels, such as processed leather or paper and pulp, and in more sophisticated industrial products, such as auto parts, chemicals, machinery and electronic components. As the technological contents rise, the lists of traded products between Brazil and China get increasingly similar.

Compared to the previous five years, trade performance in 2005 was abnormal. Imports from China grew at a very high pace—close to 70% compared to the same months in 2004—

however, most strikingly, exports to China fell or did not grow at all. Much of this performance was tied to a loss of production due to a large drought and lower prices of soybeans, as well as to very high Brazilian demand for electronic components (for instance,

Brazil became a significant exporter or mobile telephones in 2005, with components imported mainly from China) tied to an appreciated currency.

Although the overall results in the end of the year were quite similar to the patterns observed since 1999, with exports accelerating after August and imports losing momentum in the last months, the surprising results in the first half of 2005 fuelled a strident anti-China campaign amongst several industries and in the press. It was feared, among other factors, that:

1. the positive trade balance consistently accumulated with China since 2000 would descend into a structural deficit;
2. exports of commodities to China had reached a saturation level;
3. cheap Chinese products would knock down production throughout Brazil;

4. increasingly, without protective measures, several industries in Brazil would not be able to compete against allegedly unfair Chinese competition.

The first three points mentioned above were widely used by representatives of some industries to call for government protection, demanding application of the special safeguards stipulated by China's WTO accession terms. The bilateral agenda in 2005 was thus heavily concentrated in trade negotiations similar to the trade restriction exercises also undertaken by the United States and the European Union regarding textiles (Sino-Brazilian negotiations on trade restrictions were concluded in February 2006, imposing limitations on the exports of 8 apparel articles to Brazil).

The debate about the effects of China's emergence on the Brazilian economy had the merit of increasing public awareness about China. Unfortunately, it was heavily concentrated on the impact in sectors such as textiles and apparel (even if Brazil did not apply

trade quotas under the WTO textile and apparel agreement that expired in December 2004), footwear and toys, and missed out on more strategic issues, such as competition against Chinese manufactures in Brazil's traditional export markets in developed countries.

This new, strategic twist in the perception of China's impact is beginning to take place, even if belatedly. A number of institutions, such as the Institute of Applied Economic Research (IPEA, a government-sponsored think tank), the Inter-American Development Bank (IADB), the United Nations Economic Commission for Latin America and the Caribbean (ECLAC), and a few Brazilian scholars and trade associations, are making significant efforts to understand China's impact on Brazilian industries and advance proposals to boost national competitiveness. Although all have contributed significantly, two should be mentioned here (a larger list is presented in the bibliography).

Table 3: Brazilian trade with China – selected sectors
US\$ millions

Product families	Imports			Exports		
	2000	2004	%	2000	2004	%
Agribusiness, vegetable extraction						
Meat and dairy	5,4	2,3	-57,4	14,7	43,5	195,9
Leather and skins	18,1	39,8	119,9	23,9	195,9	719,7
Vegetable-origin products	13,5	21,1	56,3	338,7	1626,9	380,3
Processed foods	2,0	8,9	345,0	66,0	139,3	111,1
Soy oil	0,0	0,0	0,0	21,2	493,3	2226,9
Timber	1,1	2,7	145,5	33,7	137,0	306,5
Steel, mining, chemicals and petrochemicals						
Petroleum	74,7	365,3	389,0	36,1	219,4	507,8
Mineral ores	4,0	5,4	35,0	273,7	1168,9	327,1
Cast iron, steel, other metals	59,6	142,4	138,9	41,3	451,1	992,3
Plastics and rubber	25,3	65,9	160,5	30,9	42,9	38,8
Chemicals	197,1	460,1	133,4	24,3	108,2	345,3
Paper and pulp	2,6	4,4	69,2	61,3	289,0	371,5
Manufactures						
Textiles and apparel	60,8	251,1	313,0	0,8	31,9	3887,5
Footwear	19,9	47,8	140,2	0,3	1,5	400,0
Mechanical machinery and parts	170,5	410,3	140,6	31,1	192,2	518,0
Electrical machinery and parts	360,3	1387,4	285,1	12,5	58,9	371,2

Source: SECEX

The beans of wrath

Soybeans have been Brazil's major export to China since the end of the 1990s. China cannot cope with its needs of animal feed as its burgeoning middle class increases its animal protein intake, due to either the high growth rates of meat consumption or the natural limits to increasing production and productivity of soybeans.

China accounts for nearly 35% of all soybeans Brazil exports. Its large demand has translated in significant gains for Brazilian producers. But the Chinese have proved to be especially tough players, with opaque sanitary practices frequently disrupting an otherwise highly lucrative market.

In August 2001, the Chinese press started reporting concerns, as opposed to other crops in which China is nearly self-sufficient, about "growing dependence of external soybeans sources", particularly because in that year, for the first time, the amount imported was larger than the national production. Shortly thereafter, sanitary authorities began reporting larger- than-acceptable amounts of solid contaminants (earth, pebbles, weeds and seeds) or mold in cargoes originating in Brazil and Argentina. Such complaints were unheard of in more traditional—and equally strict in sanitary terms—markets for South American soybeans. There were then only warnings about lack of quality compliance.

In March 2002, China introduced legislation requiring all imported genetically modified (GM) agricultural products to be declared as such and labeled. Conventional products were not required to present certification or labeling. Contrary to international sanitary standards, a "zero-tolerance principle" would be applied in all controls. Good for Brazil, which only produced soybeans of the conventional sort. Or did it?

In spite of a national ban on GM production, southern producers smuggled GM seeds from Argentina, thus contaminating the exported shipments and leading to great difficulties with Chinese authorities—the "zero-tolerance" principle meant that a few GM beans could lead a whole cargo to be classified as incompliant with the new rules. A political solution was worked out, requiring the Brazilian agriculture minister to sign a declaration that, in spite of likely GM contamination, soybeans exported by Brazil posed no threat to human or animal consumption. An apparently innocuous phrase, but it required a complicated legal and political engineering in order to enable the minister to sign a document that would make him endorse something irregular under the prevailing legal framework.

Then came the *Phytophthora*. In August 2003, Chinese authorities found traces of this bacterium in Brazilian and Argentine soybeans. According to Brazilian and American agricultural technicians consulted at the height of this new crisis, the bacteria posed no harm to crops. Nevertheless, the Chinese invoked the contamination problems detected in 2001 in order to make the point that sanitary controls applied by exporters (Brazil, Argentina and the United States) were not reliable. Companies had to pay huge demurrage costs and face severe losses (some vessels spent weeks outside Chinese ports) as they awaited a solution from sanitary authorities, which eventually came out as a result from political consultations.

The worst blow came in April-May 2004. Soybean prices, due to strong Chinese demand, were at their historical record. As President Lula was arriving in Beijing with a huge business delegation, the Chinese announced their ban on Brazilian beans. Allegedly, large amounts of fungicide were found in vessels originating in Brazilian ports. According to traders, there was, indeed, at least one vessel with abnormal concentrations of fungicide-treated seeds mixed to regular beans. Instead of punishing the responsible actors, however, the Chinese government blocked 23 soybean-exporter companies from access to Chinese ports, which amounted to nearly all exporters then trading with China.

The political imbroglio resulting thereafter tarnished the presidential visit. Companies—both Brazilian and foreign, as well as Chinese soybean crushers dependent on imports—mounted an international campaign against the Chinese treatment. After prices plummeted and exporters lost hundreds of millions of dollars, imports of Brazilian beans resumed.

There was no crisis in 2005—prices were not abnormally high, no contaminants were found, and Brazil can now certify and label GM crops. The scenario for 2006 also seems tranquil. But the incidents since 2001 should be seen as a cautionary tale, a reminder that China tends not to hesitate to use its weight to in commodity markets when it feels it is necessary.

The IADB has strongly focused on the competitive impact. It reminds us that, even if China's labor-intensive products have ravaged a few Latin American economies—especially in Central America and the Caribbean - Brazil still has time to adapt and apply policies accordingly. The bank compares China to a large alarm ringing, urging Brazil either to change or to risk increasing irrelevance in the world economy.

The second institution to be mentioned in contributing significantly to these issues is ECLAC. The ECLAC has published a thorough analysis of the Chinese impact on Brazilian trade competitiveness. One of its original contributions is an attempt to measure losses of competitiveness, estimating the value that could have been potentially exported to developed economies and other traditional trade partners were it not for increasing competition with China. The methodology has its shortcomings, especially if one of the assumptions is “what if there were no China”, but pointedly shows that losses attributed to such competition can already be counted as hundreds of millions of US dollars annually - and it is growing.

2. Imports

The most striking difference between Brazilian exports to China and imports from China is the large diversity of the latter. The five products with largest participation in the list of exports to China in 2004 contributed with almost 63% of the exported value. From China, the same index is only 22%. Besides the lack of concentration in a few products, the Chinese list of exports to Brazil is widely dispersed over an enormous amount of manufactures, especially electrical, electronic and mechanical components, chemicals and machinery.

Although Brazil has experienced a series of very positive results in its trade balance with China, imports from China have accelerated after 2003 (Table 1). Despite some analysis to the contrary, it is too early to point to a trend of structural, persistent trade deficits with China. However, the trade balance does seem to have embarked on a trajectory of diminishing results.

Recent criticisms about an “invasion” of Chinese products do not stand to scrutiny. Imports from China have indeed grown in value, volume and market share. In sectors such as machinery, capital goods and electronic components, however, Brazil has not registered significant growth in its overall imports - that is, total imports of these products from all of Brazil's trade partners have increased (or decreased in some segments)—with lower rates than the country's total import performance. Viewed in this context of low total import growth, China has displaced more traditional suppliers in several industries, especially the US and the EU.

The substitution of external suppliers of industrial inputs and consumer goods is compatible with the strong growth of China's industrial competitiveness. In textiles and apparel, footwear and machinery (Table 4), China is clearly gaining market share to the detriment of other foreign players, but not necessarily to Brazilian competitors. The roots of this phenomenon are well known to observers of the Chinese economy:

- a) incentives to rapid industrialization in China, with growing emphasis in more technologically-advanced industries;
- b) low production costs and immense economies of scale;
- c) a growing trend of developed-country industries to either outsource parts of their production to China or use it as an advantageous export platform.

To the factors above should be added the different exchange rate policies. Whilst China has historically, particularly after 1994, kept export-friendly rates, Brazil's floating *real* has appreciated significantly over the last two years, undermining the competitiveness of national industries before the rise of their Chinese equivalents in international markets.

The risks of China's competitiveness growth are not different from those faced by other industrialized nations. As a matter of fact, in the Latin American context—as pointed by an Inter-American Development Bank study (see bibliography)—Brazil is uniquely well positioned to withstand Chinese competition. It has a large, diversified industrial base, “only” requiring

regulatory adjustments, investments in infrastructure and more investment-friendly macroeconomic policies in order to boost its competitiveness.

Trade performance as that observed in electrical and mechanical machinery exports to China (Table 4) suggests two important phenomena and lends itself to optimistic prospects. On the one hand, despite being latecomers to China, Brazilian industries are beginning to successfully conquer significant niches in the Chinese market. High export growth rates displayed in technology and capital-intensive industries are a result, among other relevant factors, of growing exposure to the Chinese market and steady improvements in the information available in

Brazil about China, thus bridging the knowledge gap that hampered much potential trade until the end of the 1990s.

On the other hand, some caution is required about the reasoning above. Due to the precise fact that Brazil is a latecomer to China, industrial exports to China—as in the above-mentioned sectors—still are incipient. It is too early to conclude anything about the paths these industries are likely to follow in their relationship with China. However, exports of industrial parts and machinery seem to have taken off since 2002, a point that deserves further study in order to eventually apply its lessons learned to other industries in Brazil.

Table 5: Chinese invasion? Substitution of traditional suppliers in chosen sectors
(US\$ millions)

Product families	Imports			Exports		
	2000	2004	%	2000	2004	%
Textiles and apparel						
World	1606,5	1422,9	-11,4	1222,0	2079,4	70,2
US	254,3	220,6	-13,3	267,9	504,7	88,4
EU 15	246,3	209,2	-15,1	167,1	326,6	95,5
Argentina	217,9	126,5	-41,9	342,8	375,6	9,6
China	60,8	251,1	313,0	0,8	31,9	3887,5
Footwear						
World	48,5	72,1	48,7	1617,1	1898,8	17,4
US	0,9	2,4	166,7	1080,7	1026,2	-5,0
EU 15	5,5	4,6	-16,4	192,4	339,0	76,2
Argentina	0,7	0,4	-42,9	129,2	107,1	-17,1
China	19,9	47,8	140,2	0,3	1,5	400,0
Mechanical machinery and parts						
World	9023,1	9323,0	3,3	4282,8	7767,7	81,4
US	3139,4	2722,3	-13,3	1262,2	2121,9	68,1
EU 15	3478,3	3588,2	3,2	818,5	1749,4	113,7
Argentina	365,0	284,1	-22,2	788,0	983,2	24,8
China	170,5	410,3	140,6	31,1	192,2	518,0
Electrical machinery and parts						
World	9130,5	8704,4	-4,7	2961,4	3322,3	12,2
US	3183,2	1404,6	-55,9	1037,8	969,0	-6,6
EU 15	1962,9	1920,3	-2,2	242,6	574,0	136,6
Argentina	130,6	100,0	-23,4	783,8	641,1	-18,2
China	360,3	1387,4	285,1	12,5	58,9	371,2

Source: SECEX

SECTION TWO – INVESTMENTS

Not much to account for yet

As opposed to the long introduction to trade relations above, there is relatively little to say about Chinese investments in Brazil or in the rest of South America. Much was announced in 2004, huge expectations arose, but the implementation of the bold plans presented two years ago still remains to be seen.

Large investment announcements lent an aura of political accomplishment to the presidential visits in 2004. China seemed set to replicate its investment strategies deployed in Africa since the mid-1990s, when it started scrambling the continent for raw materials. China staged its first steps in the internationalization of state-owned enterprises (SOE) in the oil sector, tapping resources in extremely unstable countries such as civil war-ridden Sudan and Angola.

As the presidential visits of 2004 closed in, a number of factors and policies were in place to support larger internationalization moves:

- a) China already had a few large companies eager to invest abroad;
- b) China had created the State-owned Assets Supervision and Administration Commission (SASAC) to coordinate the SOE restructuring process and expansions abroad;
- c) financial mechanisms to support internationalization were under discussion.

China, a major importer of raw materials, looked to Latin America, Central Asia and Africa searching for safer access to natural resources it severely lacked in its growth process. And, as such, investment intentions in Brazil and other Latin American countries bent heavily over the need to tap the region's rich mineral and agricultural resources. Both direct production and investments in transportation and energy infrastructure were considered.

Projects announced as President Lula was heading to China included railroads (CITIC), a large steel mill (Baosteel-CVRD), an alumina plant (Chalco-CVRD), and a gas pipeline

(Sinopec-Petrobras). There were also many rumors, but no official declaration in this direction, of investment in ports, electricity generation, soybean and meat farming, and meat processing units.

With the exception of the alumina joint venture by Chalco and CVRD, all were suspended or abandoned. The reasons for this are to be found on both sides: lack of regulatory approval, inadequacy of regulatory frameworks, shifts in the prices of inputs, and delays in delivering political decisions. Some projects may also have been hastily presented in order to contribute to the environment surrounding the presidential visits of 2004.

Although it may seem that Sino-Brazilian investments have come to a dead end, two factors must be taken into account. First, Chinese companies and government institutions keep roaming Brazil discussing investment opportunities. There are no comprehensive surveys of these trends, but our experience shows that Chinese investors, especially SOEs, are consistently searching possibilities in mining, energy production, transportation, construction and farming, albeit in more modest perspectives than the bold plans announced in 2004.

Chinese investment has also taken form in not-so-grand sectors. Operating units are already producing in the fields of telecommunication equipments (Huawei and ZTE), air conditioning (Gree), timber production and processing (several players in the Amazon), and computers (Lenovo). Major SOEs have offices in Sao Paulo or Rio de Janeiro, and government-supported entities are also setting up operations or representations in Brazil.

Secondly, Brazilian investment is increasingly taking place in China. In spite of being a latecomer, Brazil seems to be willing to catch up with lost time. Besides pioneering compressor producer Embraco, which set up a plant in Beijing in 1995, large companies such as Embraer and CVRD have operations in China. Motor producer Weg set up the first wholly Brazilian-owned factory in 2005. Steel producer Gerdau has recently announced the acquisition of a Chinese mill. Belgo-Brazilian InBev acquired Fujian Sedrin Brewery.

Offices of Brazilian firms, a rare sight a few years ago, now abound. Investments in the pipeline, still to be officially confirmed, include projects in textiles and apparel, chemicals, steel, metallurgy, software, footwear, auto parts, tools and cutlery.

A likely scenario for the near future is more maturity in bilateral relations. China stands to become a significant platform for the global expansion of some Brazilian brands. This process is far from an economy-wide phenomenon; however, it is very significant that it is taking place. After all, there may not be a new trade axis to explore—others have already done it—but the prospects may be bright enough for Brazilian industries that adopt the right strategies and investment policies to the rapidly growing impact of China's emergence in the global economy.

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