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**China's Evolving Role
in Latin America**

**Can It Be
a Win-Win?**



By Enrique Dussel Peters



Atlantic Council

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China's Evolving Role in Latin America

Can It Be a Win-Win?

By Enrique Dussel Peters

Foreword

Chinese President Xi Jinping travels to Washington in September for his first state visit to the United States. Major bilateral and global issues like climate change, monetary policy, and the nuclear agreement with Iran are likely to top the agenda. But, an area of significance for both countries may not receive as much attention as it deserves: China's increasingly close political and economic relationship with Latin America and the Caribbean.

The growth in China's economic engagement with the region in the past decade and a half is staggering. Trade has increased by nearly 2,000 percent since 2000, spurred in large part by bilateral free trade agreements with countries such as Peru and Chile. China has also made billions of dollars in loan commitments across the region. And while the decline of the commodities boom has weakened a central pillar of the relationship, the Chinese government and private sector are not packing their bags anytime soon.

Much has been written about Latin America's relationship with China, but what is missing is a snapshot in time—a scorecard of sorts—to serve as a primer for understanding the complexities of the relationship both now and in the future.

As renowned Sino-Latin American expert and Atlantic Council author Enrique Dussel Peters explores in this report, trade is only one element in Latin America's broader engagement with China.

The next wave of Chinese interest in the region will show the tide increasingly turning from commerce to investment. Is the region ready? Can countries benefit from Chinese investment while avoiding the trap of murky deals that seek to ignore years of improvements in the region's rule of law? Investment diversification is good but only when it lifts the overall socioeconomic boats of the people

and facilitates industrial development, not when it spurs backsliding. The jury is still out on whether China is the right long-term partner.

The vigor and dynamism of Chinese engagement means that, given proper strategic planning, there are many possibilities for advancing the relationship so it is a win all around, including for the United States. The five case studies included here illustrate the spectrum of historical ties with China. From those with long and complex historical relationships, like Cuba, to those whose relationships are almost entirely structured around recent opportunities for economic cooperation, like Mexico.

This paper launches the Adrienne Arsht Latin America Center's initiative on China and Latin America, an effort that aims to inform public and private sector leaders in Latin America, the United States, and Europe about the complexities of China's growing interest in Latin America and how this growing relationship could evolve so it propels Latin America's further socioeconomic ascendance.

Many English-language reports on Sino-Latin American relations tend to focus on the US-oriented security implications of China's economic advances in the Americas. We agree with the majority of Latin Americans' view that a stronger China relationship does not have to preclude the United States from advancing its own relations. Rather, Chinese involvement can provide an avenue for all parties to collaborate in the shared goals of economic growth and social progress in the hemisphere. But only when China plays by the same rules as other trade and investment partners. As President Obama and President Xi meet, we hope that they will take advantage of this important moment in US-China relations to set the stage for a new period of cooperation in Latin America and the Caribbean.

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Executive Summary

China's increasing international reach is reshaping the global order with a burst of activity from Africa to Latin America. What is the extent of its new relations in Latin America and the Caribbean?¹ Is it a win-win, or must Latin American countries make adjustments now to ensure that China does not erode the region's political, economic, and social transformations over the last decade?

Today, China is a global economic giant. Since 2014, it took the reins as the second largest source of overseas foreign direct investment (FDI). The country is also the world's largest exporter, and, in the last decade, the most dynamic importer. Its currency, the renminbi (RMB), trades in the world's financial centers and exchanges in bilateral trade between a number of countries.

China is also leaving a cultural footprint. Confucius Institutes operate across the world to teach Mandarin as well as to educate locals on China's cultural activities. This increasingly aggressive global



Chinese Premier Li Keqiang prepares to depart Peru while on a four-country tour of Latin America in May 2015. His visit was one of many recent high-level trips by Chinese officials to the region.

strategy seeks to assert presence in countries critical to China's long-term strategic interests.

Latin America and the Caribbean is increasingly a focus of China's engagement. Even after several centuries of connection in immigration and trade, a substantively new, and deeper, relationship has emerged since 2000. Expectations are that this new relationship will continue to intensify in the short to medium term. This report shows why this is likely.

Is it a win-win, or must Latin American countries make adjustments now to ensure that China does not erode the region's positive transformations?



A new tunnel is inaugurated in February 2015 as part of the Coca Codo Sinclair hydroelectric project. Financed largely through a loan from the Export-Import Bank of China, it is the largest energy development in Ecuador's history.

China's reforms in the 1980s and rapid integration to the world market since then—culminating with its admission to the World Trade Organization (WTO) in 2001—precede this new Sino-Latin relationship. The dynamic goes far beyond economic interactions, with ties—for better or worse—permeating across sectors. In some countries, the broader relationship has already fundamentally recast the way both the public and private sectors operate.

Much attention focuses on how the China-Latin America relationship is changing the game for the United States with significant emphasis on the consequences for US national security. These issues are important but are comprehensively addressed elsewhere and are outside the scope of this report.²

Instead, this publication analyzes major recent regional trends related to China and the bilateral

relationship with five countries: Argentina, Brazil, Cuba, Mexico, and Venezuela. Each country analysis addresses the most relevant elements of the bilateral relationship to provide a framework for dealing with the opportunities and challenges ahead.

China is poised to grow its presence and linkages with Latin America. That means countries must take measures now to ensure that the result is long-term benefits that help to further drive socioeconomic development. The final section recommends a series of proposals on how national governments and regional institutions can better respond to and invest in the relationship, so that both China and Latin America can benefit from the evolving relationship. Among the top priorities should be constructing a long overdue development agenda between Latin America and China.

Four Factors That Define the China-Latin America Relationship

Understanding the institutional framework of China's public sector is critical to comprehending its relationship with Latin America. Under the leadership of the Chinese Communist Party, the relationship between the central government, provinces, cities, municipalities, and counties is dominated by consolidated institutional interactions.³ This political setting, which includes competition among public sector actors, differentiates modern China from other major economies.

According to some estimates, China's public sector controls and owns approximately 50 percent of total gross domestic product (GDP).⁴ Cities such as Beijing and Shanghai owned more than 34,000 and 16,500 firms, respectively, in 2012, including multinational corporations such as the motor companies BAIC Group (based in Beijing) and SAIC Group (based in Shanghai).⁵

The "omnipresence" of China's public sector allows for short, medium, and long-term development strategies, and for policies to address specific issues such as GDP growth, science and technology, urbanization, agriculture, environmental issues, the exchange rate, and the banking and financial sectors.⁶ This is one of the reasons why China can offer turnkey development packages in manufacturing, services, labor, and financial support in its

activities abroad. The result: discussions in some cases of unfair trade, subsidies, and an overall assessment that China improperly supports its own firms.

Much of China's relationship with Latin America is a product of domestic developments within China since reforms began in the late 1970s. China's domestic reforms have yielded impressive depth and dynamism. The last decade has seen an attempted shift toward the domestic market and

higher-level technological goods and processes along with an interest in financing global infrastructure projects.

Domestic reforms and transitions have rapidly expanded China's economic presence while fundamentally altering its global commercial dynamics. China has increased its share of

global GDP from less than 2 percent in the early 1980s to more than 12 percent since 2013, surpassing the US economy as the world's economic powerhouse based on purchasing power parity.⁷ With that, China is shifting from being a global factory built on cheap labor to becoming a major player in increasingly sophisticated commodity chains.

The consequences have reverberated among China's closest neighbors and throughout Latin America. Unlike the 1990s, most of the region is no longer significantly competing with China on

The omnipresence of China's public sector allows for short, medium, and long-term development strategies, and is one of the reasons why China can offer turnkey projects.

wages, although rising labor costs in China compared to Latin America have become an important factor in particular labor-intensive segments of value-added chains.⁸ Cheap labor production has increasingly been transferred from the main cities to other parts of China and/or from China to countries in Asia such as Bangladesh and Vietnam.

Four specific issue areas define the broader relationship: political relations; trade, investment and financing; energy and infrastructure; and education and cultural exchanges.

Political and Regional Relations

China's 2008 White Paper toward Latin America establishes long-term goals based on the existence of "abundant raw materials," growing economic linkages, and the Five Principles of Peaceful Coexistence.⁹ The strategy highlights fourteen areas of cooperation including trade, investment, infrastructure, energy and tourism as well as security, cultural and social issues. Since the paper's release, China has focused on deepening South-South relationships, regional infrastructure needs, and cooperation in economic and trade issues.¹⁰

One infrastructure project that is causing concern is the potential construction of a new canal in Nicaragua. If completed, with a 2020 deadline, the estimated \$50 billion project led by the Hong Kong Nicaragua Canal Development Investment Company headed by billionaire Wang Jing would have profound repercussions in the region and on the US-China relationship. Massive financing is still needed. If funds come from China's public banks, this would create a China-backed canal near the US-dominated Panama Canal.¹¹

Latin America's larger economic importance also permeates political discussions. The region is an important supplier of raw materials (particularly minerals, copper, and soybeans). Collectively, it is China's fourth most important trading partner. Economic relevance has resulted in a steady stream of public and private sector delegations and other high-level visits from China. Since 2000, Chinese president and premiers have regularly visited Latin America, with thirty-one total trips [see figure 1, p. 7]. Top destinations include Brazil (six visits), followed by Argentina, Chile, and Cuba (four each).

Bilateral visits beget increased engagement with the region's multilateral institutions. China became a permanent observer in the Organization of American States (OAS) in 2004 and a member of the Inter-American Development Bank (IDB) in 2009. It has participated actively in the Economic Commission for Latin America and the Caribbean (ECLAC) over the last decade.

After almost a decade of prodding, the First Ministerial meeting of the Forum of China and the Community of Latin American and Caribbean States (CELAC) took place in January 2015 in Beijing. The resulting Cooperation



Growing trade relations are also boosting diplomatic ties with China. President Xi Jinping, pictured here in Venezuela, made a four-country trip to the region in July 2014.

MICHEL TEMER/FLICKR

FIGURE 1. Visits of China's Premier and President to Latin America and the Caribbean, 2001-15

YEAR	PREMIER	PRESIDENT	Argentina	Brazil	Chile	Costa Rica	Colombia	Cuba	Ecuador	Mexico	Peru	Trinidad and Tobago	Uruguay	Venezuela	TOTAL	
2001	Zhu Rongji	Jiang Zemin	Apr 8	Apr 11	Apr 4			Apr 13					Apr 10	Apr 19	6	
2002																0
2003	Wen Jiabao	Hu Jintao								Dec 12					1	
2004			Nov 16	Nov 11	Nov 18			Nov 22								4
2005																0
2006																0
2007																0
2008								Nov 17		Nov 18			Nov 20			3
2009																0
2010						Apr 15										1
2011																0
2012					Jun 23	Jun 20	Jun 25					Jun 16			Jun 22	5
2013	Li Keqiang	Xi Jinping				Jun 2				Jun 4		Jun 1		3		
2014			Jul 18	Jul 14				Jul 21					Jul 20	4		
2015				May 18	May 24		May 21				May 22			4		
PREMIER TOTAL			1	2	2	0	1	0	0	1	1	0	1	0	9	
PRESIDENT TOTAL			3	4	2	2	0	4	0	2	1	1	1	2	22	
COMBINED TOTAL			4	6	4	2	1	4	0	3	2	1	2	2	31	

Source: Author compilation based on media reports.

Plan CELAC-China (2015-19) focuses on growing annual trade to over \$500 billion and increasing China's FDI stock to \$250 billion over the next decade. It also announced six thousand government scholarships, six thousand trainee positions and four hundred masters' level scholarships for Latin Americans to study and train in China.¹²

Trade, Investment, and Financing

China, like no other country in the world, is able to offer turnkey projects (or, a group of products in one package) as a result of the public sector's presence in its economy. These projects involve trade, financing, investments, and supporting services, all Chinese and, in most of the cases, in the public sector's control. The ability to offer such development

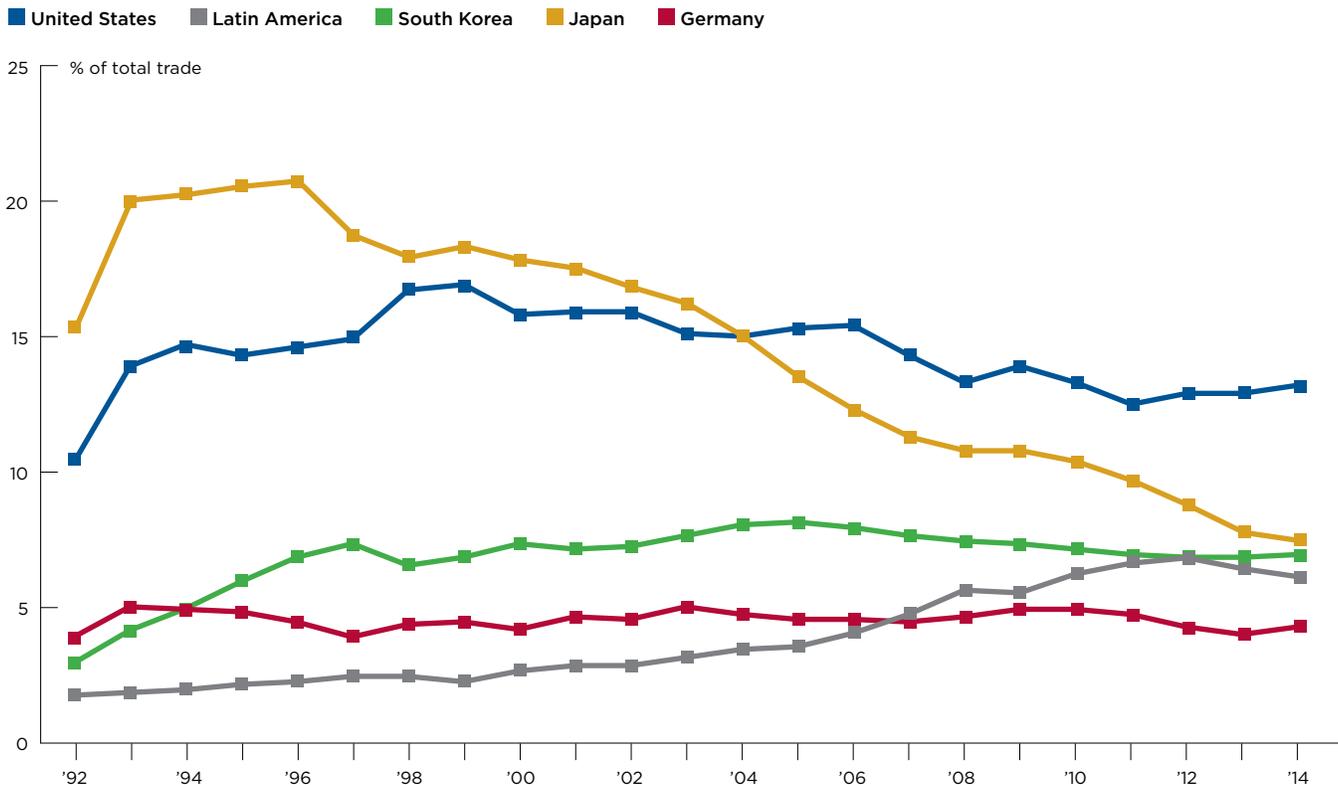
packages in Latin America contrasts with the practices of most industrialized countries, where projects originate in the private sector. The role of China's public sector sparks debate around the degree to which it gives Chinese interests an advantage in trade, investment, and financing activities in Latin America.

The region's trade relationship with China has changed dramatically over the last decade and continues to quickly evolve. China now has free trade agreements in effect with Chile (2006), Costa Rica (2011), and Peru (2011) in addition to the many institutional arrangements it has with other countries.¹³

Four issues dominate the broader commercial relationship.

First, beginning in the 1990s, trade and Chinese exports became the most dynamic part of the

FIGURE 2. China's Top 5 Trading Partners, 1992–2014 (Percent of total trade)



Source: Author compilation based on UN COMTRADE Database, 2015.

first stage of the new engagement. By 2014, China accounted for 12 percent of Latin America and the Caribbean’s global trade.¹⁴ Between 2000 and 2014 exports to China increased from 2 percent to 9 percent of the region’s global total. Imports from China grew from 2 percent to 16 percent. Based on Chinese statistics—and not including Hong Kong—Latin America is China’s fourth largest trading partner, coming only after the United States, Japan, and South Korea [see figure 2]. But statistics vary widely depending on their source. Based on Chinese data, Latin America has a trade surplus with China; the opposite is true if looking at numbers coming from the region. In Mexico-China trade, for example, Chinese exports versus Mexican imports differ by more than 250 percent.¹⁵

Second, regional statistics show that Latin America’s trade deficit with China has jumped from below \$20 billion until the mid-2000s to over \$75 billion since 2012.¹⁶ The Caribbean, Central America,

and particularly Mexico largely account for this deficit. Trade with South America is relatively in equilibrium. In 2014, the value of trade fell for the first time since 2009, mainly due to the drop in raw material prices.¹⁷

Third, low-value added and low-technology goods dominate exports to China as the level of Latin America-bound exports has increased [see figure 3, p. 9]. Medium- and high-technology exports to China barely account for 5 percent of total trade flows in the last decade (versus 30 percent to 40 percent of total Latin American exports over the last two decades). Chinese medium- and high-technology exports—all manufactured goods—accounted for over 60 percent of total Chinese exports to Latin America in the last decade.

This gap has created a strong social and political backlash in some countries against China. In Argentina, Brazil, Peru, and Mexico, for example, domestic-oriented business organizations and

unions have demonstrated and publicly criticized what is seen as unfair competition in domestic and global markets.

Fourth, Latin American exports to China are more concentrated than with any other trading partner. The top-three export categories to China—ores, oil seed, and copper (followed by oil and pulp of wood)—increased from 50 percent to 72 percent of total exports from 2000 to 2014. Over the same period, Latin America's exports to the world in these three categories fell from 42 percent to 32 percent.¹⁸

Beyond trade, investments and financing are guiding factors of the second stage of China's new regional engagement. Since 2014, China has become the second global source of FDI, after only the United States.

China has invested on average almost \$10.7 billion annually in the last five years. FDI flows, which vary widely across the region [see figure 4, p. 10], are expected to increase substantially due to China's CELAC commitments.¹⁹ But this FDI is quite different from that of other countries. From 2000 to

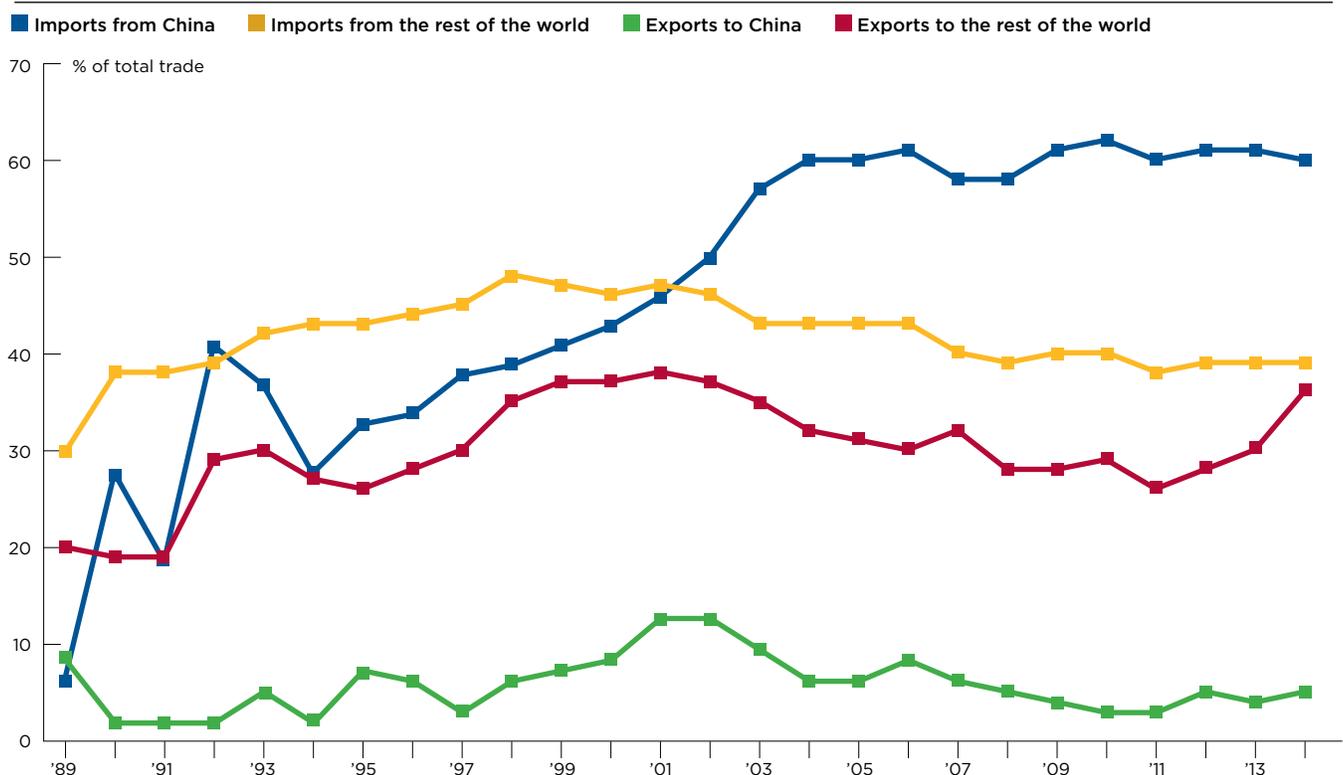
2012, 87 percent of China's Latin American-bound FDI came from public-owned firms. This FDI is also highly concentrated, with 57 percent focused on the acquisition of raw materials.²⁰

This is problematic for a number of reasons, particularly the increased dependency it creates on primary products. In no other top-FDI source country do public sources account for more than 3 percent of total flows.

Latin American investments in China, while dynamic in recent years, are much less substantial. Firms from Brazil and Mexico such as Embraer, Marcopolo, Grupo Bimbo, and Gruma are seeking new ways to invest in China—both through on-the-ground plants and by developing new relationships with Chinese suppliers and clients.²¹

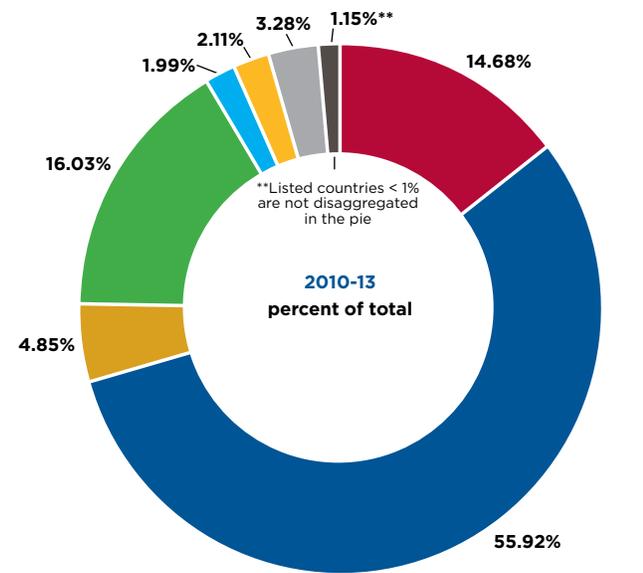
China is also increasing its financing presence. From 2005 to 2014, loan commitments totaled more than \$118 billion. Venezuela alone accounted for more than 50 percent of total loans and 42 percent of infrastructure projects in the region.²² This rather new Chinese economic activity will likely

FIGURE 3. Latin America's Medium- and High-Technology Goods Trade with China, 1989–2014 (Percent of total trade)



Source: Author compilation based on UN COMTRADE Database, 2015.

FIGURE 4. FDI Inflows from China to Latin America, 1990–2013 (Millions of US Dollars)



COUNTRY	1990–2009 (Millions of US Dollars)	2010–13 (Millions of US Dollars)
Argentina	\$143	\$6,270
Brazil	\$255	\$23,886
Chile*	-	\$100
Colombia	\$1,677	\$2,071
Ecuador*	\$1,619	\$278
Guyana*	\$1,000	\$15
Mexico*	\$146	\$100
Peru	\$2,262	\$6,846
Trinidad and Tobago	-	\$850
Venezuela	\$240	\$900
Other	-	\$1,400
Total	\$7,342	\$42,716

* Less than one percent Source: Author compilation based on 2015 ECLAC data.

grow substantially, given the expected increase in Chinese infrastructure projects.

The increasing internationalization of the renminbi is notably affecting trade and financial relationships. The Chinese currency has amassed a growing regional importance since the 2008 global economic crisis. Argentina, Brazil, and Chile

already have bilateral swap arrangements totaling more than 280 billion RMB. Other countries may secure such arrangements in the future. As discussions continue for accepting the RMB as one of the currencies for the International Monetary Fund’s Special Drawing Rights (SDR), these arrangements point to the potential for economic exchanges directly in RMB, and thus substituting RMB for other existing currencies in international exchange.²³

Energy and Infrastructure

As part of its turnkey projects, China has increasingly offered loans for specific energy and infrastructure projects. This practice is an extension of China’s own development experience since the 1960s: over half of all bilateral and multilateral loans between 1979 and 2005 went into transportation and energy sectors, while over two-thirds of lending came from the Asian Development Bank (ADB) and Japan.²⁴

From 2005 to 2014, 70 percent of China’s Latin America loans went to infrastructure and energy projects and 25 percent to mining.²⁵ Many infrastructure projects have generated controversy (see country case studies); others have failed. Social and political instability, environmental disputes, labor controversies, and disputes with local communities are among the key reasons.²⁶

Still, more infrastructure projects are likely on the way, especially considering China’s geopolitical strategy to internationalize its innovations in infrastructure construction and financing. Since the 2013 launch of the new Silk Road and the “one road-one belt” strategies, the Chinese government has committed hundreds of billions of dollars in different funds and regional and bilateral agreements to improve and enhance infrastructure beyond its borders—all part of a long-term plan that carries over to Latin America. These investments stem from capitalization of the China Development Bank (CDB), China’s Export-Import Bank, and the Asian Infrastructure Investment Bank (AIIB), of which Brazil is a founding member.²⁷ The CELAC-China Forum announced a China-LAC Special Loan for Infrastructure in its Cooperation Plan for 2015 to 2019.

These recent strategies will require careful

evaluation. There is no doubt that developing countries, including those in Latin America, need foreign investment to improve and develop infrastructure. The question is whether the investments will facilitate inclusive socioeconomic growth and development, beyond serving as conduits for commodity flows.

A lingering question is also whether transfers of power in multiparty democracies will affect investment strategies. Infrastructure projects in Sri Lanka have raised significant concern following a newly elected government's opposition to elements of previously inked Chinese projects.²⁸ China's strategy may find similar domestic hurdles in Latin America, particularly with projects that have weak a political, economic, financial, and/or environmental grounding and where local communities have divergent interests.

Culture and Education

Latin America and China share a deepening cultural relationship as well. One of the main and clearest signals of its recent boom is the increasing activity of Confucius Institutes in the region. A part of China's Ministry of Education, Confucius Institutes aim to promote Mandarin Chinese language and culture around the world. Today, China has more than three hundred such institutes in more than ninety-three countries, with the goal of expanding to one thousand centers by 2020. Twenty-five operate in nine Latin America countries, including Brazil (8), Mexico (5), Peru (4), and Chile (2).²⁹

Stronger cultural and educational ties are seen at all levels—counties, municipalities, cities, and countries—and across the public, private, and academic sectors. Public and private schools are increasingly teaching Mandarin Chinese. Student exchanges between universities are growing, and new cooperation agreements are seeking to promote common

research agendas and establish binational projects. Several business organizations and universities have established joint centers in China to promote their common interests, improve institutional relations, and support Spanish-language instruction in Chinese institutions.

Educational exchanges are also on the rise. In Guatemala, which does not have diplomatic ties with China and maintains its relationship with Taiwan, Asociación de Amistad del Pueblo China-Guatemala (ASACHIGUA) signed agreements in 2013 to promote cultural cooperation and teaching Chinese in schools, universities, and in other spaces. Other universities such as the National Autonomous University of Mexico (UNAM), for example, have signed more than a dozen cooperation agreements for jointly organized academic activities through exchange students and researchers. Business organizations such as Conselho Empresarial Brasil-China, Cámara Argentino-China, and Consejo Empresarial Mexicano de Comercio Exterior, Inversión y Tecnología, among others, have increasingly specialized in how to deepen Chinese trade and investment ties.



Latin American educational institutions such as the National Autonomous University of Mexico (pictured) are pursuing joint academic and research opportunities with their Chinese counterparts.

Countries in Focus

China is ratcheting up its relations with a number of countries across Latin America. But five countries stand out for how individually and collectively they represent the diversity of Chinese interests and how the relationship is likely to evolve in the coming years. These countries give an overall picture of when this growing relationship works—and when it backfires. In each case, China has learned from its successes and failures. Have Latin American countries done the same?

The country analyses that follow highlight select aspects of the bilateral dynamic both at present and in the future. The mix of countries

reflects a diversity of strong historical (Cuba), political (Venezuela), strategic (Brazil), and trade (Argentina and Mexico) ties with China. The results are often unexpected, with the impact permeating throughout the economy and society. Although most of the ties and Chinese projects are too new to be evaluated definitively, key themes emerge that will shape the future relationships.

Argentina

Since the establishment of bilateral diplomatic relations in 1972, Argentina, like most of Latin America, has substantially increased trade with China. Exports are mostly primary goods, largely without diversification and with low value-added and technology levels. One of the critical questions in the Argentina-China relationship is whether Argentina will be able to upgrade its value-added exports to China, particularly in the case of soybeans.³⁰

Since 2014, China is Argentina's second largest trading partner, trailing only the United States (if excluding the European Union as a group), with 7 percent of Argentina's exports and nearly 17 percent of its imports coming from China. Soybean exports account for over 64 percent of total exports to China. Combined with all oil seeds and animal and vegetable fats and oil, this grouping represents 80 percent of Argentina's exports to China in 2014.

Indeed, the soy oil case is worth exploring as an example of the erosion of Argentina's contribution to the soy value chain. Argentina is a top world producer of oil from soy and sold much of it to China. But, a few years ago, China slowed the purchase of Argentina soy oil, substituting the supply with their own capacity. Argentina exports to China are now



Soybean exports—including those from Argentina (pictured)—are a large component of the region's commodity-based trade with China.

JAVIER/FLICKR

only limited to soybeans.

Chinese FDI in Argentina increased in 2010-11, but has fallen substantially since. In 2013, it accounted for less than 1 percent of total FDI in Argentina. Even with the \$5.5 billion in investments from state-owned Sinopec and CNOOC in 2010 and 2011, total FDI continues to lag, particularly when compared to bilateral trade.³¹ Cultural differences are a major obstacle both at the firm-level and beyond between both countries.³²

Trade between China and Argentina will continue growing, although there are no signs that China's FDI will exceed the 2010-11 levels. Yet structural problems in the bilateral trade relationship remain, as technology inputs flows almost exclusively from China to Argentina. Buenos Aires must find a way to upgrade the value added component of its exports to China.

In July 2014, Argentina and China signed a bilateral agreement for a three-year swap operation of Argentina's debt, totaling \$11 billion. China's support was critical to Argentina's macroeconomic stability, helping Argentina

to avoid default on its foreign debt obligations. As part of the agreement, Argentina received \$7.5 billion in loans from the China Development Bank to construct two hydroelectric dams and a railway project. But this came with strings attached. Argentina granted Chinese investors preferential access to build the projects. Clauses guarantee preferences to Chinese suppliers and labor.

The agreement continues to generate controversy especially heading into the first round of presidential elections in October.³³ Beyond the growing public debate, a group of business organizations and companies started to draw more attention to the framework agreement's specific terms objecting to a deal that mandates the import of products and processes from China.

The agreement's fate is uncertain. Some opposition leaders have declared that they will not respect the signed agreement if elected, which would generate tensions that China has yet to experience as a creditor.

But the China debate in Argentina goes far beyond a swap agreement. A growing chorus of influential voices question the tangible benefits of growing Chinese influence for Argentine firms. They also point out that the very limited positive effects of bilateral trade; in some cases, such as the soy value chain, the result is a downgrading in the type of Argentine exports.³⁴

So far, China has been important for the macroeconomic stability of Cristina Fernández de Kirchner's administration, and the recent bilateral

agreement highlights that both governments expect to deepen this integration. But this may be less likely if Daniel Scioli, the government-supported candidate, does not win the fall election. Two issues, however, point to tensions in this new and dynamic relationship.

First, if an opposition candidate wins the election, he may reject the preferential access

component, and even the overall bilateral agreement, which would seriously affect the relationship. Second, and given the importance of soybean exports to China, the soy value-added chain is a critical example—for Argentina and the rest of Latin America—of an effective downgrading process in the last years. Argentina previously processed soybean and thus added value before export, but it cancelled these processes in light of China's expanding capacity to do the same but at lower prices. This could have profound implications in the development agenda in Argentina and the rest of Latin America. It represents a concrete example of China's effect on the region's short, medium and long-term growth agenda.

A recent bilateral agreement with China continues to generate controversy in Argentina, especially heading into the first round of presidential elections in October.



The largest recipient of Chinese FDI in Latin America, Brazil is pursuing investments in infrastructure and energy.

Brazil

Brazil-China diplomatic relations date back to August 1974. But the new relationship took off during the terms of President Luiz Inácio Lula da Silva (2003-11), consolidating one of the region's widest and deepest links with China. High-level bilateral meetings during that time focused on the geostrategic implications of renewed partnership. As emerging BRICS members, both countries' reached new prominence in South-South cooperation and the G20, contributing to cooperation on issues such as reform of the United Nations system.³⁵

The result: a wide range of agreements, from trade and investment to science and technology, industrial cooperation, education, and climate change. Continued progress in bilateral relations rests on each country's priority to expand its regional and global influence as an independent emerging market.³⁶

Cooperation has brought results. China is Brazil's largest trading partner since 2009 and Brazil is the region's top recipient of Chinese FDI.

Despite opposition from the United States, Brazil is a founding member of the China-backed Asian Infrastructure Investment Bank (AIIB), reflecting the increasing depth of the Brazil-China relationship.

But Brazil remains one of the most extreme examples of a Sino-Latin trade relationship dominated by a high concentration of low value-added, low-technology exports to China. The prices of Brazilian commodity exports are rather volatile, and highly concentrated in what is sent to China.

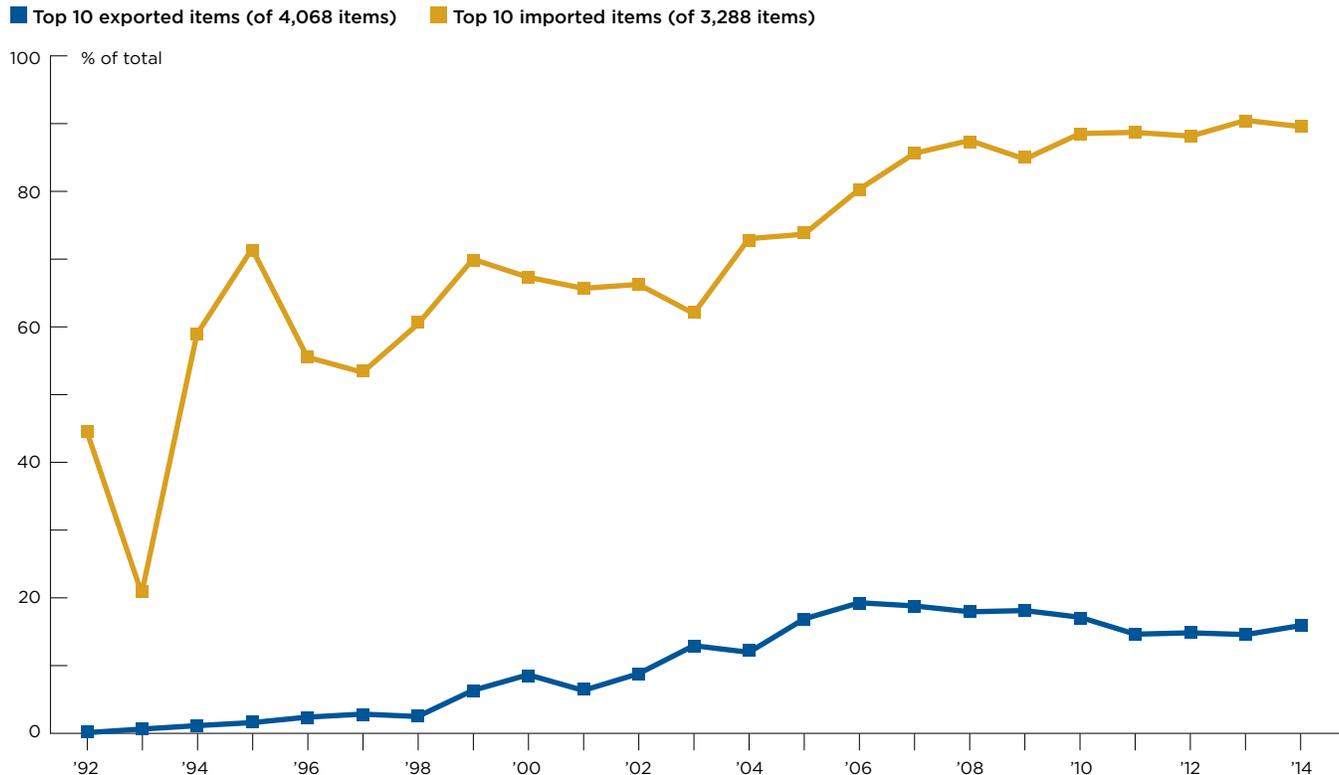
The top ten export products from Brazil to China increased from 67 percent to 90 percent of total exports from 2000 to 2014 [see figure 5, p. 15]. In 2014, of 3,288 items, soybeans and iron accounted for over two-thirds of total imports from Brazil. But the burst of the commodity bubble is taking its toll. Exports to China fell by nearly 5 percent in 2014 and by 18 percent as of May 2015.³⁷ It is not clear how Brazil will overcome this growing disparity.

In investment, Brazil is by far the most significant regional recipient of China's FDI, although far below initial expectations. Firm-level studies of China's FDI in Brazil show slow learning processes in both countries.³⁸ It will take years before Chinese FDI effectively achieves results that empowers further large-scale investment. The regulatory framework can also be uncertain for Chinese firms. For the electronics company Lenovo, for example, domestic market demand has changed drastically. Additionally, development in technology and backward and forward linkages have yielded questionable results.³⁹

The May 2015 visit of Chinese Premier Li Keqiang to Brazil reflects the recent and rapidly deepening ties. The two leaders signed thirty-five signed agreements worth up to \$50 billion in potential new Chinese FDI in areas such as agriculture, aeronautics, automobiles, infrastructure, energy, and mining. An additional thirty investment deals were also proposed.⁴⁰ In each of these cases Brazil will have to push for domestic backward and forward linkages. Otherwise, the deals will compound pre-existing trade structures with other countries and China (i.e., little value-added and little medium- and high-level technology exports).

Yet the ambitious proposal to create an

FIGURE 5. Concentration of Top 10 Items Brazil Exports to Versus Imports from China, 1992–2014 (Percent of total)



Source: Author compilation based on UN COMTRADE Database, 2015.

interoceanic railroad from Brazil to Peru is most significant for the future of China's role in Brazil and across South America. Plans for trans-Amazonian highways and projects have been developed since the 1970s with little success. The newly proposed railway would extend from Brazil's Port of Santos on the Atlantic Ocean to Peru's Port of Ilo on the Pacific Ocean, totaling around 3,500 kilometers.

The project is strategically important for global commerce. For China, the railway could be a key demonstration of its prowess in infrastructure, technology, and financing. For Brazil, it would be an important new channel for exports to Asia and China. The project's concept, however, is not new and has failed to materialize in the past due to environmental and local community concerns. It still lacks a concrete project proposal as well as trilateral agreements between Brazil, Peru, and China.⁴¹

Institutions such as the Industrial and Commercial Bank of China (ICBC) have pledged financing in Brazil, together with Caixa Econômica,

for a total of \$50 billion during 2015–21.⁴² There are also plans for a Bilateral Production Cooperation Fund accounting for \$20 billion from China in sectors such as iron and steel, cement, glass and construction material, and equipment and manufacturing.⁴³ Three Chinese banks also have committed loans of up to \$10 billion for Petrobras.⁴⁴ Brazil expects to deliver twenty-two jets from Embraer to Hainan Airlines, as part of a larger order of sixty airplanes.⁴⁵

Brazil-China relations are likely to deepen given the solid bilateral and long-term political understanding. This strategic political partnership and the effective trade and investment exchange is unique in the region. China is Brazil's main trading partner and Brazil the most important trading partner for China in Latin America.

But potential roadblocks lie ahead. Both governments will have to ensure that existing Chinese investments improve and upgrade Brazil's trade dynamic beyond the export of low value-added and low-technology goods. The proposed

trans-Amazonian railway could represent profound progress for the bilateral relationship and the region at large—or it could be a hallmark of unfulfilled promises. Brazilian political developments will also shape the relationship. The increasing domestic discontent toward President Dilma Rousseff will demonstrate how China understands and effectively adapts to the complexities of Brazil's political system.

Cuba

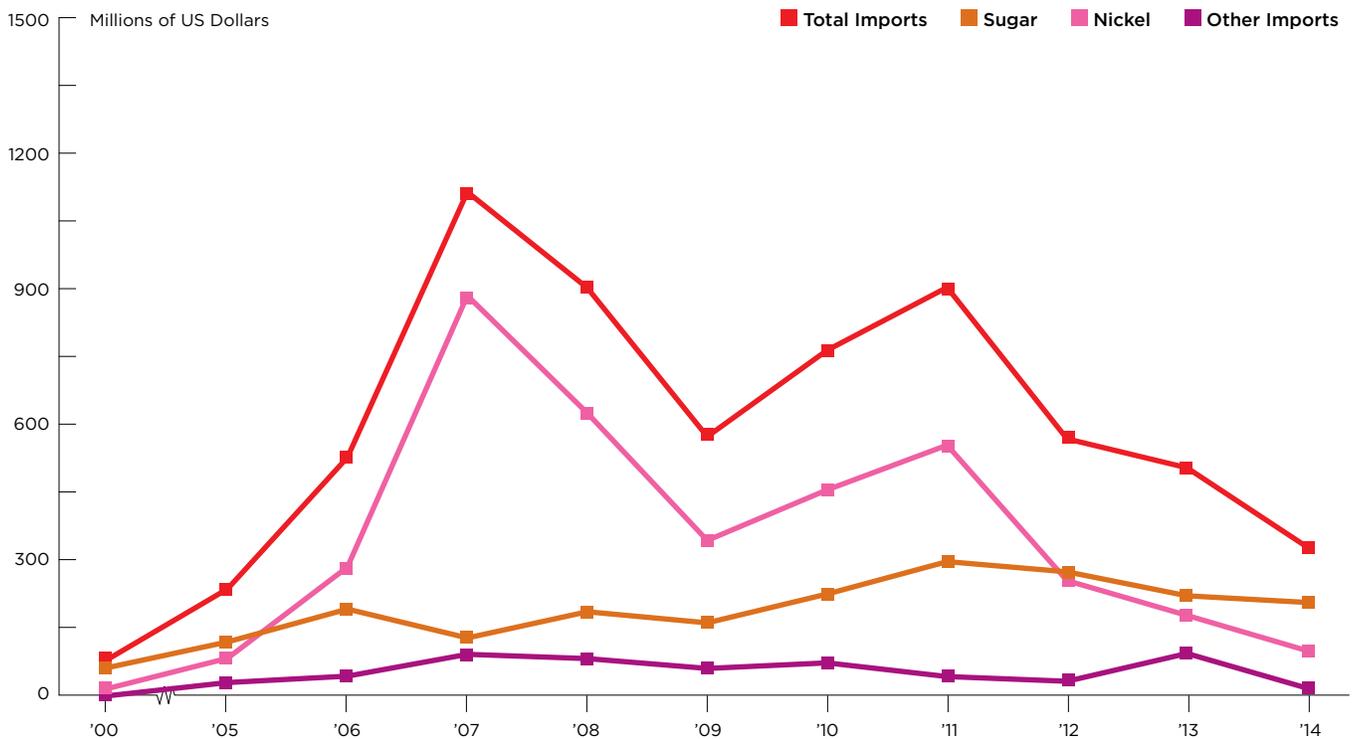
China's diplomatic relationship with Cuba is not only the oldest—established in 1960—but also the most complex in the region. It is often the most difficult to detail given the limited access to information in both countries. Despite decades of Cuban Communist Party political alignment with the Soviet Union (and against China in several cases), the fall of the Soviet Union in the 1990s created a new opening with China.

Since then, Cuba and China expanded collaboration on a level without parallel in the region. China fully understands the strategic and political



Modernization of the port of Santiago de Cuba has attracted Chinese investor interest. This could have implications on US-Cuba trade as relations move forward.

FIGURE 6. China's Imports from Cuba, 1992–2014 (Millions of US Dollars)



Source: Author compilation based on UN COMTRADE Database, 2015.

JOHN GAUTHIER/FLICKR

relevance of the bilateral relationship—in spite of the relatively small size of Cuba's economy and population.⁴⁶ Cuba's profound transformations in the last year have further raised the stakes for China, particularly Cuba's improvements to labor productivity and economic efficiency as well as its diplomatic re-opening with the United States.⁴⁷

Hundreds of bilateral agreements have been formally signed since the beginning of the 1960s. In 1988, the Intergovernmental Mixed Commission for Economic and Trade Relations (CMIREC) was established. Since then, the China-Cuba meeting has become the region's highest-level annual bilateral meeting. These meetings have led to unprecedented political and economic agreements in trade, investment and financing, infrastructure development, and cultural and educational ties.

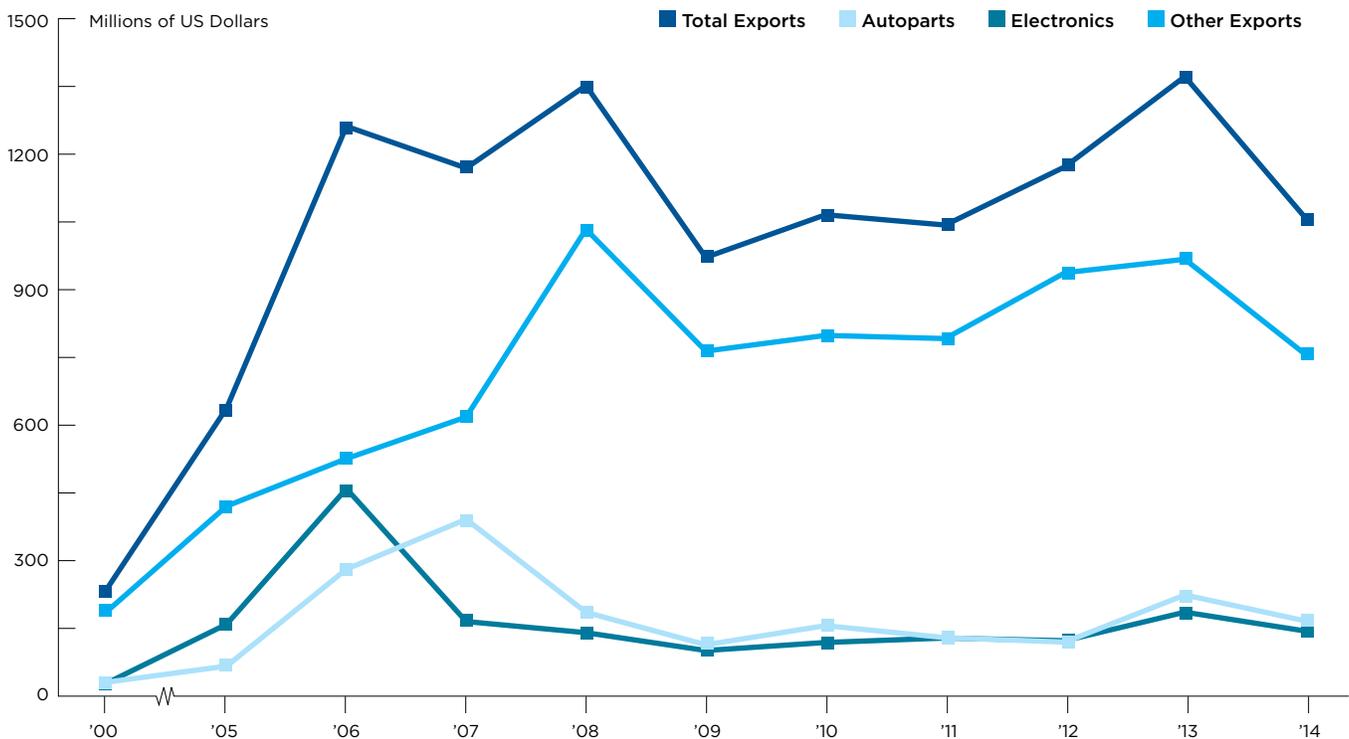
The reestablishment of diplomatic ties between the United States and Cuba in July 2015 could give Cuba renewed relevance in China's foreign policy. US-China competition as economic superpowers, the geographic proximity between the United States, and the island's cultural ties to the United States are other factors that could increase Chinese

interest in maintaining strong ties with Cuba. It has already shown interest in participating in the new special economic zone at Mariel and is modernizing the port in Santiago de Cuba.⁴⁸ The construction of ten new 45,000-ton ships, and a \$120 million loan to improve the port in Santiago de Cuba could play an important role in the short term as US investors approach new activity in Cuba. Yutong, Huawei, Haier, several oil companies, Geely, and other Chinese companies are expecting to invest in a group of projects related to the zone.

Additionally, China has played a fundamental macroeconomic role in terms of loans and financing since the fall of the Soviet Union in 1991. Although trade and services have been paid directly in convertible foreign exchange since 1995, China has periodically increased loans to Cuba with very favorable terms, often without any interest rate at all, but leading to an effective reduction of Cuban debt by approximately \$6 billion.⁴⁹

China also has become Cuba's second largest trading partner; Venezuela remains number one. Cuba's exports to China have not changed since 2000 [see figure 6, p. 16]. Trade consists mostly of

FIGURE 7. China's Exports to Cuba, 1992–2014 (Millions of US Dollars)



Source: Author compilation based on UN COMTRADE Database, 2015.

two items: sugar and nickel, accounting for more than 90 percent of all trade throughout 2000-14 and amounting to close to 95 percent of total trade thus far in 2015. This trend is worrisome given the drastic price declines of both sugar and nickel.

Cuban exports to China fell from \$1.1 billion in 2007 to \$330 million in 2014, creating a significant trade deficit. Similar to other countries, the proportion of value added and technology added exports is highly skewed toward China [see figure 7, p. 17]. Indeed, China continues to ramp up its exports of high-value-added materials such as buses to modernize Cuba's transportation system as well as electricity distribution equipment.

Both governments have promoted China's FDI in Cuba. Joint ventures, although extremely limited so far, are a result of hundreds of bilateral agreements including the recently reformed Foreign Investment Law, double taxation agreements and reciprocal protection for investments.⁵⁰ While FDI in Cuba is limited, expectations are that it will ramp up in the years ahead. A group of Chinese investments are expected to be worth over \$460 million, including the luxury housing project near Marina Hemingway.⁵¹

A small group of Cuban firms have invested in China, particularly in the tourism and gastronomy sectors and in the biotechnology field. A proposed commercial air route between China and Cuba—the first in the Caribbean—may become an important basis for deepening exchanges and increasing Chinese tourism to Cuba.

Based on common political agreements and the rapid negotiations between Cuba and the United States, Cuba could become a strategic host for Chinese trade and investment. Recent investments across multiple sectors in Cuba, and the interest of Chinese firms in the port of Santiago and the special economic zone of Mariel reflect this strategic relationship. From a Cuban perspective, China could become an important counterbalance in Cuba-US

negotiations and the resulting new openness. The pending fulfillment of Chinese FDI in Cuba in the short term will be critical for the medium-term relationship and China's evolving role in Cuba.

Mexico

The Mexico-China relationship began its most recent stage five years ago amid high tension. Between 2013 and 2014, political cooperation improved at the start of Presidents Xi and Peña Nieto's terms but has been on the rocks since November 2014.

Mexico is only recently beginning to discuss an explicit strategy toward Asia in spite of the increasing economic ties. This partly comes from the Mexican government's priority of "diversification of its economic ties,"⁵² which has prompted it to look beyond the North American Free Trade

Agreement (NAFTA) and toward Asia and China.⁵³ Yet a series of challenges have emerged that complicate the way forward.

The bilateral trade relationship is economically and politically unsustainable and has generated significant social and local fallout in a variety of Mexican

Political cooperation improved at the start of Presidents Xi and Peña Nieto's terms but has been on the rocks since November 2014.

states in the last decade.

While China has been the second largest source of Mexico's imports since 2003, the import/export relationship held an 11:1 ratio in 2014. China accounts for 16.6 percent of Mexico's imports and only 1.5 percent of its exports, leading to a \$60.3 billion trade deficit in 2014. While it is true that more than 91 percent of Chinese imports are intermediate and capital goods, Mexico has not been able to overcome this massive structural deficit.⁵⁴

China's FDI in Mexico accounts for less than 0.1 percent of its total FDI, and expectations are that this figure will not rise in the short to medium term.⁵⁵ Several failures in recent projects, such as Dragon Mart, Golden Dragon, and the China-Railway Construction Corporation's (CRCC) fast-speed train, reflect an increasing difficulty for and even a

hostility towards Chinese FDI.⁵⁶ As a result, the lack of Chinese firms' understanding of Mexico's socio-economic, political and legal framework—combined with accusations of corruption in the Mexican government—has resulted in an overall impasse in the China-Mexico relationship and a corresponding lack of confidence in Mexico's public sector.

The experience of these Chinese firms also reflects the unpreparedness of Chinese companies to execute potential FDI and work with local stakeholders—both from a financial and technical as well as from a political, social, and environmental perspective. Projects of this caliber, particularly in infrastructure, need more than just negotiation with government. Chinese firms will have to improve their preparation to invest in Mexico—and other countries in Latin America—including better knowledge of local and national stakeholders, the legal framework, and political and social conditions to effectively implement projects.

China will likely strengthen its trade position in Mexico in the short and medium term; there are however no expectations that in the near future Chinese investments will grow substantially. Recent reforms in Mexico, particularly in the energy and banking sector, however, could allow for new Chinese investments.

But a deeper relationship will come with some trepidation. An increasing gap exists between the booming trade and the institutional response across the public and private sectors. Chinese firms have limited knowledge of Mexico's political, social, and legal culture. In many cases, Chinese firms expect Mexico's public sector to support their activities just as the public sector would in China. For more than eighteen months China Railway Construction Corporation cooperated with the highest levels of the Mexican Executive, particularly with Secretaría de Hacienda y Crédito Público (SHCP). But the suggested construction firms became embroiled in corruption scandals, preventing, so far, implementation of the project. A better understanding of Mexico's political and legal system would have been important for CRCC.

Few institutions can support the specific demands of the new Chinese firms established in Mexico. At the same time, Mexico's public sector



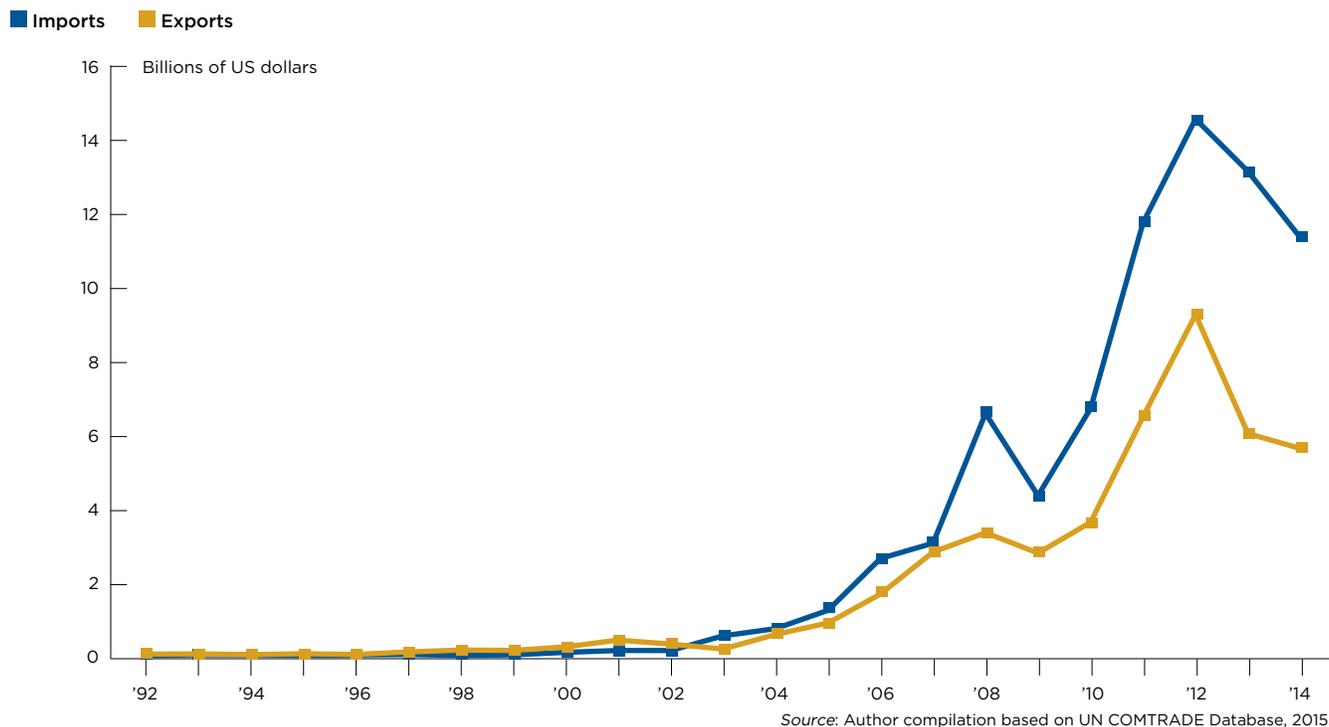
An uncertain future. Many Mexican textile workers worry that more trade with China could cost them their jobs.

has failed to outline a short-, medium-, or long-run strategy toward China. This differs from two of Mexico's major trading partners—the United States and the European Union—which have a more deliberate trade and investment strategy toward China.

Businesses and academic leaders, have developed a framework with one hundred specific suggestions, called *Agendasia 2012*, but the public sector has not adopted and implemented it. This institutional setting does not reflect the integral strategic relationship that both nations purported following bilateral meetings in 2013, and it magnifies the frictions stemming from a lack of a long-term Mexican strategy. In the trade and investment framework, for example, Mexican business organizations ask for reciprocity, meaning the door should be opened for China to invest in Mexico (such as in the oil industry) only if China also allows for the same opportunities in the same or similar sectors.

Additionally, China currently poses a massive challenge to Mexico's export-oriented industrialization and its long-term strategy within NAFTA.

FIGURE 8. China's Imports from and Exports to Venezuela, 1992-2014 (Billions of US Dollars)



Chinese exports to the United States, with the important exception of the automobile supply chain, have undermined Mexico's export-oriented production, particularly in electronics and yarn-textile-garments.⁵⁷ The dynamic calls into question whether Mexico can continue to specialize in cheap labor and cheap energy relative to its North American partners. This challenge is particularly pertinent for the NAFTA-region's specific value-added chains such as telecommunications, electronics, auto parts, automobiles, and textiles, among others.⁵⁸

In addition to the challenges that NAFTA poses to China, other regional trade agreements, while beneficial to Mexico in the long term, may disrupt its economic and political relations with China. For instance, the Trans-Pacific Partnership (TPP) is expected to impact trade balances in the Asia-Pacific and Latin American regions. China at one time openly criticized the TPP and has shown no visible intention of joining in the near future. Mexico already has bilateral free trade agreements with many of the twelve TPP countries, including the United States, Canada, and Japan. The rest of the TPP members are not significant in terms of

trade and investment from a Mexican perspective. Neither TPP nor the Pacific Alliance will improve Mexico's relationship with China, but both could establish new rules concerning issues such as intellectual property that could affect the growing bilateral trade ties.

China's relationship with Mexico lacks an explicit strategy to shape forward progress. While China has made efforts to increase investments in Mexico, the Mexican government should focus on coordinating specific items for a long-term agenda with China. Expectations in both China and Mexico are very high in terms of cultural, educational, and economic exchange in the short term. Both governments, however, should work on detailed and project-level support and evaluations to minimize recent failures and any effects on existing and future projects.⁵⁹

Venezuela

The Sino-Venezuela relationship is one of the few in the region that has gone far beyond trade since its beginning. The causes lie in the increasing tensions between the late Hugo Chávez government—since 1999 and particularly in the mid-2000s—and the US government. Still, it

is not clear if ideology and political dynamics are relevant for understanding the depth of the China-Venezuela relationship.

One of the most complex and strategic for both countries, the Sino-Venezuela relationship, has a depth that nearly matches its notoriety. Among other things, Venezuela has one of largest oil reserves in the world, and thus important to energy-hungry China.

Since 2008, Venezuela and China have created more than ten different funds for a total of \$37 billion. One of the first, the Fondo Conjunto Chino-Venezolano, has been capitalized several times since then for around \$27 billion.⁶⁰ China Development Bank (CDB) has become the main Chinese creditor, which requires Petr leos de Venezuela S.A. (PDVSA) to sell China oil in repayment for loans.⁶¹ According to some sources, Venezuela sends daily approximately 640,000 barrels; 42 percent of these exports are to service its debt.⁶² With more than 450 agreements since 1999, Venezuela and China have an extensive history, but their collective future may be uncertain.

For one, it is not clear—as most of the loan contracts are not public—if Venezuela will be able to pay its Chinese loans, particularly given the most recent fall in oil prices. As a result of the low price cycle, CDB softened loan maturities and repayment terms for 2014-15. President Nicol s Maduro's visit to China—parallel to the CELAC-China Forum in 2015—apparently prompted \$20 billion in additional investment and financing.

Yet there is increasing risk-aversion in certain investor circles in China toward unstable petro-regimes.⁶³ Although a drastically different situation, Libya's civil war in 2011, endangered more than \$10 billion in investments and forced the evacuation of around 36,000 Chinese citizens, which has caused Chinese investors to view Venezuela, although a completely different context, with increasing wariness.

Energy collaboration was one of the main goals of the Ch vez government in its commitments with China, but it dominates the relationship in a harmful way. Venezuela's exports depend almost exclusively on oil, totaling 99 percent of total China exports in 2014 [see figure 8, p. 20]. This high reliance on oil prices worries creditors, including China.

Despite many announcements of Chinese

investments, its firms have, in general, preferred to continue importing products instead of effectively fulfilling investment commitments. China National Petroleum Corporation (CNPC) announced \$28 billion for an oil project at Orinoco in 2013, and China Petroleum & Chemical Corporation (Sinopec) planned a \$14 billion investment in 2013.⁶⁴ Neither has been developed. Even older investments, such as CNPC and PDVSA's commitment to produce a specialized drill for the oil industry in 2008 and Chinalco's proposed \$403 million investment in 2011 have failed to come to fruition.

The future of the Venezuela-China relationship will be dictated by domestic decision-making in China. China is consuming and importing increasing amounts of energy and oil. But China is diversifying its sources, including Russia, Iran, Iraq, and other countries. So far, however, China's central government has fully supported Venezuela's government with loans and imports. Still, it is not very likely that effective large investments will take place in the near future. Further political complications in Venezuela are also generating an increasing awareness and risk-aversion in China.



An oil tanker crossing Lake Maracaibo is a reminder of the fledgling state of Venezuela's oil industry. Still, in September 2015, President Nicol s Maduro announced a new \$5 billion Chinese loan to boost oil output.

Conclusions and Policy Recommendations

The Latin America-China relationship is rapidly and dynamically evolving in terms of trade and, more recently, in Chinese FDI and loans. The institutional capability of both sides, including the Chinese, to deepen and improve knowledge of their counterpart is extremely weak: institutions are in general far behind the recent economic dynamism.

This is a severe impediment to furthering the relationship since neither China nor any Latin American country has extensively evaluated the relationship. Similar to other regions' experiences,

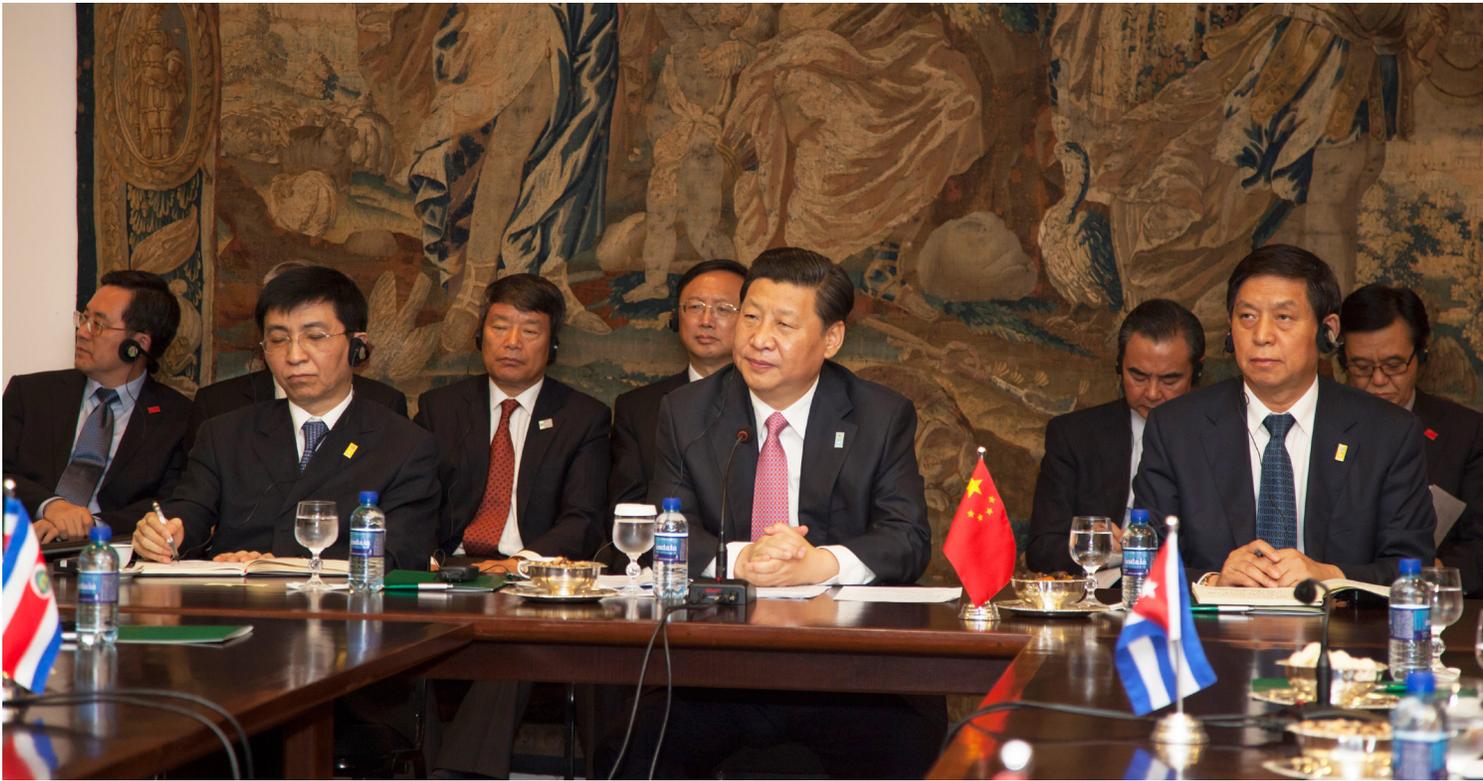
Latin America has so far been unable to understand and systematically respond to the implications of China's active public sector abroad and its ability to propose packages—including turnkey projects and a mix of services—like no other country in the world. Whether or not the public versus private ownership of Chinese firms plays a critical role in the success of the investments, recipient countries have to develop strategies to address the potential implications of public ownership.

Latin American countries have largely yet to develop a detailed short-, medium- or long-term



Open for business. Chilean President Michelle Bachelet inaugurates the Chile-China Business Forum in May 2015.

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What's next? President Xi Jinping at the inaugural CELAC-China Forum held in Brazil in July 2014.

cooperation agenda vis-à-vis China. Without such a plan, it will be a challenge to develop a model for Sino-Latin relations at the regional level. The nascent attempts of CELAC are underwhelming partly due to the lack of any detailed and in-depth analysis and respective proposals—a result of a pro-tempore Presidency that prevents institutional strengthening. China—based on its increasing importance in Latin America—deserves much more attention in policy instruments at all levels.

China's increasing regional influence is creating important new areas of engagement in energy, trade, investments, and, particularly, in infrastructure. Recently announced projects could change the economic landscape, such as the Nicaragua Canal and the Brazil-Peru interoceanic railway. Expectations are extremely high, despite a lack of precedents either in China or in Latin America for these kind of projects.

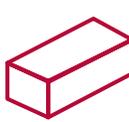
Yet while China is systematically and clearly illustrating its strategy toward Latin America, the region lacks the investment and commitment to

develop its own understanding of China's political system, trade, investment, and education initiatives. This makes bilateral understanding difficult. As a result, the errors of Chinese investments, the performance of terms of trade, and other elements of the relationship, often accumulate, with little deliberative response. This needs to change.

Chinese officials also rely significantly on their political counterparts and do not fully understand or are ill-equipped to deal with the transfer and diffusion of power in Latin America. Many of these countries have an independent press, consolidated academia, prominent labor unions, and environmental activists, but Chinese officials have yet to learn methods to address popular concern with rising Chinese influence. In several of the countries in focus—Argentina, Brazil, and Venezuela—new governments would prompt deep Chinese concern that previously negotiated agreements might be voided or ignored. These inconsistencies and setbacks risk erosion to the present regional relationship with China and will endanger future ties if not addressed.

Recommendations

The China-Latin America relationship would be more of a net win-win if measures such as the following are put in place:

 **1** In regional negotiations with China (such as CELAC) growing trade, investment, and financing ties need a long-term development agenda that pivots away from Latin America's export of raw materials. As recent CELAC meetings suggest, the region needs a post-commodity boom strategy toward China. The current trade relationship is not advancing regional economic development. The flow of extractive products such as copper, soybeans, meat, minerals, and other exports has limited the development of high value-added exports. Regional institutions such as CELAC should also make an effort to strengthen the capacity to monitor and evaluate bilateral agreements with China.

 **2** Regional institutions such as the IDB and ECLAC should highlight the benefits and costs of these bilateral agreements; specific clauses and conditionalities must be made transparent and clear. Too little understanding exists of the detailed loan agreements that China offers in Latin America and the Caribbean as well as the effects of new Chinese investments.

 **3** National governments should invest in creating or supporting institutions in the public, private and academic sectors that can help unify individual interests to define common strategies toward China. Both China's and Latin America's governments, private sectors, and civil societies must discuss and find

concrete solutions that address specific problems in trade, the enhancement of China's FDI, infrastructure projects, education, and exchange and cultural experiences.

 **4** Latin American countries should establish specific bilateral and multilateral working groups with China to promote transparent Chinese FDI for socio-economic development in necessary sectors and regions. Chinese investments are different from those of other countries⁶⁵ and require detailed policy mechanisms for promotion, evaluation, and proliferation. Chinese, Latin American, and regional institutions should focus on these issues in detail.

 **5** Trade and FDI agreements with China should be based on a common understanding and on reciprocity as a foundation for negotiations.⁶⁶ If Chinese companies wish to invest in Latin America in the oil and gas sectors, for example, they should guarantee that Latin American companies can also invest in sectors of interest in China. Reciprocity is critical to address the aggressive or defensive outlooks vis-à-vis China's influence, and instead facilitate a sector-by-sector negotiation for benefits across the board.

Growing trade, investment, and financing ties need a long-term development agenda that pivots away from Latin America's export of raw materials. The current trade relationship is not advancing regional economic development.

As the five country analyses demonstrate, the list of concrete items with China—bilaterally and regionally—is large and detailed, but each country has the responsibility to develop and clarify the ramifications for their economies and societies. Otherwise, social and political pressure against the rising influence of China may begin to erode several decades of promising evolution in the relationship.

Endnotes

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