SPECIAL REPORT

China's contribution to the renewal of the Latin American economic model

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developing ideas
LLORENTE & CUENCA

1. INTRODUCTION

This report aims at describing the aspects characterizing the relationship between China and Latin America. Foremost among these is the importance and degree of development that this relationship has achieved in just 15 years. Another prominent feature is its long-term nature and the fact that none of the actors seem to be willing to give up on the aforementioned relation, even at the most demanding times, such as the current scenario.

Both aspects are in turn related to the "shift in global economic power" towards emerging economies, a phenomenon led by China. Certain experts think that the Asian giant will not be the only global power in the future. Others still doubt the Chinese power and believe it is a mere flash in the pan. The Latin American region, however, seems to be clear in its own mind, at least, as regards the significant benefits generated by the partnership with China, thanks to its immense market and demand, as well as the opportunities for investment that this relation offers. In addition, the Latin American region does not consider this relation to be a temporary alliance, quite on the contrary, China is seen as a potential long-term partner. This is shown by the fact that the growth recorded in recent years is largely thanks to the trade relations that the region has established with China, since it considers that cooperating and promoting business and financial relations with China will be instrumental in order to overcome the current context.

Despite being rather recent, the relationship with China has been quite intense. From 2003 until now there has been a period of great business growth and expansion, which has resulted in an outstanding income for the Latin American region. This was followed by a scenario marked by the financial crisis, largely due to the decline the aforementioned trade exchange, which in turn translated into a significant slowdown in Latin American growth.

The analysis of these relations identifies the main shortcomings of the economic development model that has prevailed in the region since the 19th century: an approach based on exports of raw materials. Although the latter managed to provide a significant income at different points in history, it is greatly limited. The relations with China were also based on the aforementioned model.

"China is the only global power that can and is willing to face this challenge"

The structural weaknesses of undiversified economies whose exports lack any added value and which have an almost non-existent local industry output became evident when the prices of raw materials dropped due to the international situation and –more recently– because of the Chinese economic context.

At this point, all these problems are more evident than ever and the main proposals to overcome this economic model are based on economic diversification, through investment in technology and knowledge, infrastructure, logistics and value-added services, resulting in a circular economy and not a merely-extractive one.

For this new stage –which calls for necessary structural reforms in order to establish a more competitive model– the region counts on Chinese cooperation, which in turn has expressed its commitment to contribute to the renewal of the economic model. Beyond fine rhetoric, it remains to be seen whether the signed cooperation projects between China and the Latin American countries and the CELAC will ultimately be implemented in the region. Many expectations have been placed on China, as it is the only global power that can and is willing to face this challenge, but the main responsibility to successfully tackle this task lies with Latin America.

"The increasing economic importance of the Rising South does not seem to end soon or be reversible"

2. CHINA AND ITS POWER IN THE CURRENT INTERNATIONAL ARENA

Anything only remotely related to China has extraordinary dimensions. But if take a closer look at its economic data in relation to the rest of the world we may be able to grasp the importance of Chinese economy in today's world on its own and for the rest of the global economy.

The global importance of the Asian giant illustrates the new global order in which the "rise of the South" has become a critical element[1]. In recent years, significant changes have modified the global economic landscape, completely altering the traditional global order, to such an extent that in this new environment the growth rates of South countries are much higher than those of their northern counterparts (hitherto known as developed countries). However, changes are not merely quantitative; structural modifications have also been implemented. Hence, it seems as if the presence of South or emerging countries will be merely circumstantial. At this point, it seems unlikely that there will be a return to the past, even if much changed. This being said, the global economic trends have been recently set by the emerging economies and, leading all this processes, we find China.

The importance of this new international economic context and its continuity should be stressed, since this process is critical to understand the relevance of China and the interest of Latin America to keep the former as partner not only in the short, but also in the medium to long term.

Figures are really overwhelming. The increasing economic importance of the Rising South economies is here to stay: it does not seem likely for it to end soon or be reversible. Although the long-term economic outlook is highly uncertain, current prospects show that the South will continue increasing its importance in the global economic arena. According to the "Global Development Horizons 2013" carried out by the World Bank, the South's share in global GDP will reach 55% by 2025. A report drafted by the U.S. National Intelligence Council in 2012 expected this figure to rise to 70% by 2030. According to the Asian Development Bank estimates, South exports will account for 64% of the global exports by 2030[2].

[1] Apart from China, the major southern economic actors would be Brazil, Russia, India and South Africa.

[2] *Latin America and the Rising South. Changing World, Changing Priorities, The World Bank*, 2015, https://openknowledge.worldbank.org/handle/10986/21869, p. 3.

"Many experts fear that a potential Chinese crisis will push the remaining economies into a financial crisis"

China –leader of the emerging economies– is a clear example of the development experienced by these countries. Since 1978, when the Asian Giant first launched its economic liberalization reforms, its economy has been growing steadily at an average of 1%. According to the International Monetary Fund (IMF), the Chinese economy led the global ranking in purchasing power parity in 2015. On its own, it is greater than the economies of Germany, France and Italy combined.

Trade volume data also give us an idea of the size of its economy, which has already achieved impressive figures, based on the export of low-cost manufacturing and import of all types of energy, mining and equipment products that the country needs for its industrial development as well as food and consumer goods to meet the increasing domestic demand.

Based on this trade model, China became the leading country in trade of goods in 2013. This was achieved in record time, as the country increased its share in world exports from 3.6% in 2000, up to 12.4% in 2014. Moreover, foreign sales increased by 9.4 times over the same period. On the other hand, imports increased from 3.3% in 2000 to 10.3% in 2014, growing by 8.7 times.

However, despite these years of spectacular growth, since 2012 growth figures have gone down and this concerns many countries all around the world. These concerns have become so serious that many experts fear that a potential Chinese crisis will push the remaining economies into a financial crisis. Nevertheless, the current growth figures should not be belittled, even if China is experiencing an economic slowdown. From the sustained average annual growth of 10.5% achieved between 2001 and 2010, the Chinese growth figures dropped to 7.4% in 2014. This figure is expected to drop to 7% for the current year and to 6-7% for the remainder of the decade.

There is certainly a significant change in the growth rate, but they are still impressive rates if we compare them to those of developed countries since 2011 –almost non-existent growth–. The country that has recently shown greater dynamism and surpassed other developed countries has been the United States. However, its average growth in 2014 was close to 2.4%, well below the Chinese figures.

According to these data, it seems that the debate about whether China will become the great global power that ultimately replaces the United States seems pointless. This eternal issue –addressed for far too long– will not be solved now. Certainly, it

"China has clearly become the preferred partner"

seems as if international power will not be exclusively concentrated in a single point. For some years, we have been living in a certainly imperfect, multipolar world, but the future will belong to more than a single actor. Various powers will establish the economic, political and military rules over the next years. Meanwhile, it seems clear that no country should ignore China and in that respect Latin America has wisely decided to continue developing its relations with the Asian country. The Chinese power and the compatibility between both regions enhance their mutual interest. Moreover, if we consider the economic situation of the countries in the north and the void left by the latter in Latin America[3], China has clearly become the preferred partner.

3. WHAT IS GOING ON WITH CHINA?

If Latin American economies have benefited from a decade of unprecedented growth it has been largely due to the demand for raw materials of the Chinese market. Its insatiable demand for these products was result of the industrial development model of the Asian country until 2012, when it made certain changes to the model as it was seen an unsustainable option.

The restructuring of the Chinese economic model has translated into a new development model, previously based on an intensive, manufacturing approach with products with low added value and state investment, which turned the country into a major consumer of commodities such as oil, copper or iron. Now Beijing wants its economy to grow more sustainably, prioritizing the service sector and citizen consumption. This has logically entailed a decline in the demand for raw materials and their prices.

The situation triggered by the changes made to the economic model has been described in many different ways. Many experts have referred to it as a crisis ("slowdown", "stumble"), others as a socio-economic transformation and Chinese authorities have defined it as the "new normal". These varied reactions are, not coincidentally, directly linked to the moment in which these changes take place.

Those who believe it to be a crisis are sometimes even terrified, as they assume that the impact of the Chinese economy on the global domain would leave the latter in shambles. The raised concerns were so serious that Paul Krugman himself wanted to send a reassuring message. The Nobel prize winner believes

[3] "El futuro de América Latina... ¿apunta al Pacífico?: la historia de cómo China ocupó un espacio dejado al descuido", ARI, 58/2015

"There is no alternative plan if the Chinese economy impacts on the global economy"

that, despite accounting for a quarter of the world's manufacturing and the fact that what happens there has implications for the rest of the world, a drastic fall in Chinese imports would not severely disturb the international market and, as regards financial linkages, China has capital controls. Thus, in the face of plunging stocks or even domestic debt defaults, this would have a minimal impact on the international economy.

However, his concluding comment is more worrying, since Krugman admits that this is nothing but his analysis and considers that there is no alternative plan if the Chinese economy severely impacts on the global economy[4]. Nevertheless, beyond the existence of potential solutions, it does not seem positive for the whole world to depend on the average Chinese growth. Not only for Latin America, but for the whole world. In other words, if some experts have legitimate fears it is because there are doubts about the capacity of the Chinese economy to continue progressing in a rather stalled economic context, after doing it for years.

Analyzing these changes through growth rates is not enough, since they are not merely circumstantial, but of structural nature. The Chinese objective is to set up a development model and, in this sense, Maurice Obstfeld –IMF economist– believes that "its economy is slowing as it transitions from investment and manufacturing to consumption and services", and the immediate consequences of this change on the global economy is the reason behind the aforementioned concerns. However, in order to understand the complexity of this process and the consequences it may have in the medium and long term for the rest of the world, an analytical and reflexive approach is needed –and not fears–.

It is important to closely monitor the process and see it as a window of opportunity, even if this implies that the parties who are still interested in maintaining relations with China need to make major adjustments. The change in the development model does not close the Chinese market, but modifies the trade contents and products. To this end, there will be new opportunities to conduct business, attract investment or establish cooperation mechanisms with China, although the aforementioned economies will inevitably need to be adapted to this new scenario. There is no alternative way, since the "new normal" has already started.

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[4] Paul Krugman, "When China Stumbles", http://economia.elpais.com/economia/2016/01/08/actualidad/1452269322_879119.html, 9/01/16.

4. FROM THE SHIFT OF GLOBAL WEALTH TO THE SHIFT OF THE GLOBAL ECONOMY II:

"NEW NORMAL" AND ITS IMPLICATIONS FOR EXPORTERS OF RAW MATERIALS

The transition from one stage to the next one is what is entailing a change that seeks to become the new normal: "changing the growth model, changing the concept of development, the way in which we grow and implementing a more quality-oriented growth", as stressed by Li Yuanchao, Vice-President, in his speech at the World Economic Forum in Davos (Switzerland) in January. Mr. Li also added that a new era was beginning in which China would achieve "to grow more steadily and have more diversified driving forces".

The consequences of this new phase came to be felt in 2012, when the fall in the prices of commodities began and consequently an almost immediate sharp decline in the impressive growth rates registered among the countries which mainly focused on the exportation of the aforementioned products, i.e., Latin American countries. This impacted on the nations which, thanks to the Chinese demand, have experienced a decade of unprecedented growth.

The reason for this change is based on the features of the new economic model, as it necessarily changes the priorities of the Chinese market. First, it significantly affects the exports of raw materials. The traditional secondary sector will remain important, but it will not be the Chinese economic cornerstone anymore. Growth will be less dynamic and the economy will have a greater reliance on domestic consumption. To this end, it is necessary to implement a structural change based on the development of knowledge-intensive industries and technology. This economic change shall be accompanied by social transformations which in turn will translate into processes of social ageing, urbanization and a steady increase of middle-income households.

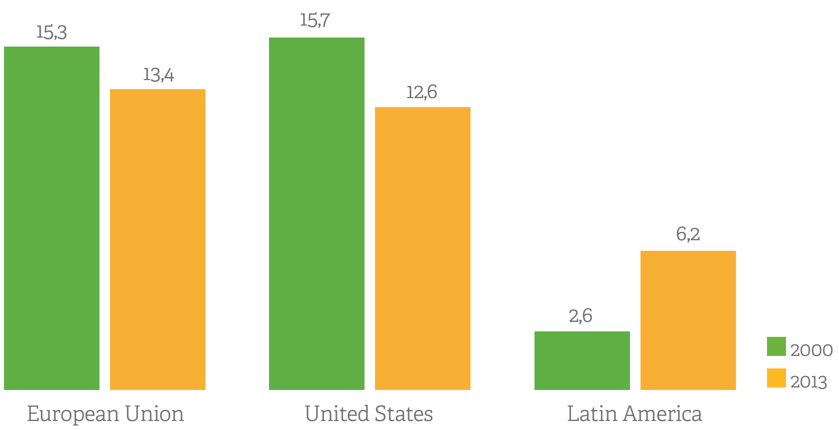
Secretary-General Xi Jinping illustrated this decision to transform, the features of the process and its reasons when he said that "...we must realize that our economy, despite being very large in size, is not strong and its growth, though fast, is not of high quality. The extensive development resulting from economic growth mainly based on factors such as natural resources and growth in size is not a sustainable model... It is a dead end".

"We need to implement an innovation chain to enhance the industrial chain"

"Where should we go from here? Towards scientific and technological innovation, moving forward from a model driven by factors and size of investment towards growth based on innovation." "We need to implement an innovation chain to enhance the industrial chain and the funding chain (financing)... we must promote innovation in relation to the product, the brand, the industrial organization and the trading platform"[5].

This structural transformation forces Latin America not only to face short and medium-term challenges as a result of the contraction in demand for commodities, but also to modify its own economic model. A challenge that should be seen as an opportunity.

Figure 1. Development of the Chinese share trade in the EU, U.S. and Latin America, 2000-2013



Source: UN comtrade

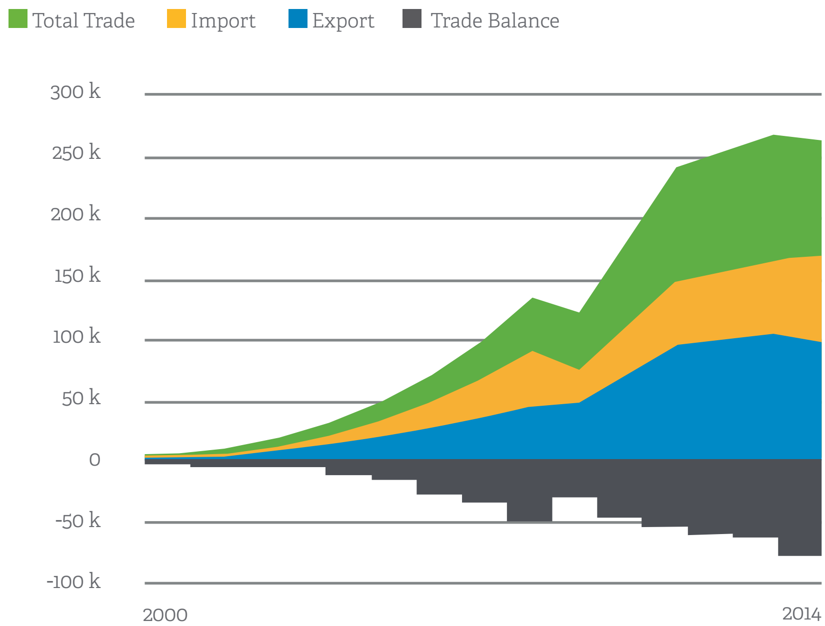
FROM THE GOLDEN AGE OF THE DEMAND FOR RAW MATERIALS TO THE STRUCTURAL CRISIS

Although the relations between China and Latin America had been established long ago, there was no history of relations between both actors. However, it should be noted that it was not until this moment when both players began seeing each other as strategic partners for their economic and social development.

The process of Chinese growth and development is the reason for this relation, the insatiable need for raw materials required by the growth of the Asian country made the latter focus its attention on the American region, as it was considered as reservoir of natural resources and minerals. In addition, the region was a suitable market to place their low-cost goods, since the region lacks –in general– a significant industrial fabric. Thus, Latin America was seen as fertile ground for business relations to flourish and they grew at an impressive pace. This can be seen if we compare the data on the share of Chinese trade in the EU, U.S. and Latin America between 2000 and 2013 (Figure 1).

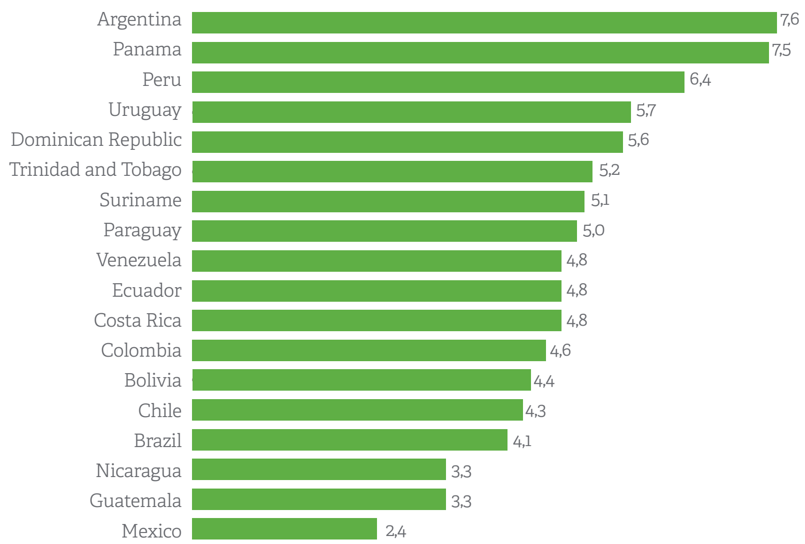
[5] "Transición al desarrollo impulsado por la innovación" ("Transition towards innovation-driven development"), excerpts from the speech made by Xi Jinping at the XVII Assembly of the Members of the Chinese Academy of Sciences and the Assembly of Members of the Chinese Academy of Engineering, La gobernación y la administración de China ("Chinese Governance and Administration"), Ediciones en lenguas Extranjeras Cía. Ltda., Beijing, China, 2014.

Figure 2. Latin America and the Caribbean: Trade in goods with China, 2000-2014 (Dollars in Millions)



Source: CEPAL

Figure 3. Average Growth Rate between 2003 and 2011 in several Latin American and Caribbean Countries



Source: FMI

Trade between both economies grew by a rate of over 150% a year and increased by 21 times between 2000 and 2013, amounting to USD 275 billion annually. The share of China in the exports from the region increased from 1% to 10% and imports rose from 2% to 16% over the aforementioned period. Although the trade relations between China and the rest of the world were also growing at a rapid pace, the relations with Latin America were particularly impressive: the latter increased its trade share in China from 2.6% to 6.2%, while the EU dropped from 15.3% to 13.4% and the U.S. fell from 15.7% to 12, 6%[6] (Figure 2).

This trade relationship had an immediate impact on the economic growth of Latin America countries. The demand for raw materials pushed up prices and, consequently, generated income for the region. This sustained boom was directly reflected in the growth rates of Latin American countries. In this sense, while the regional growth rate is impressive by itself –5.4%– it is even more striking when compared with the OECD average, close to 2,3% (Figure 3).

[6] UN Comtrade.

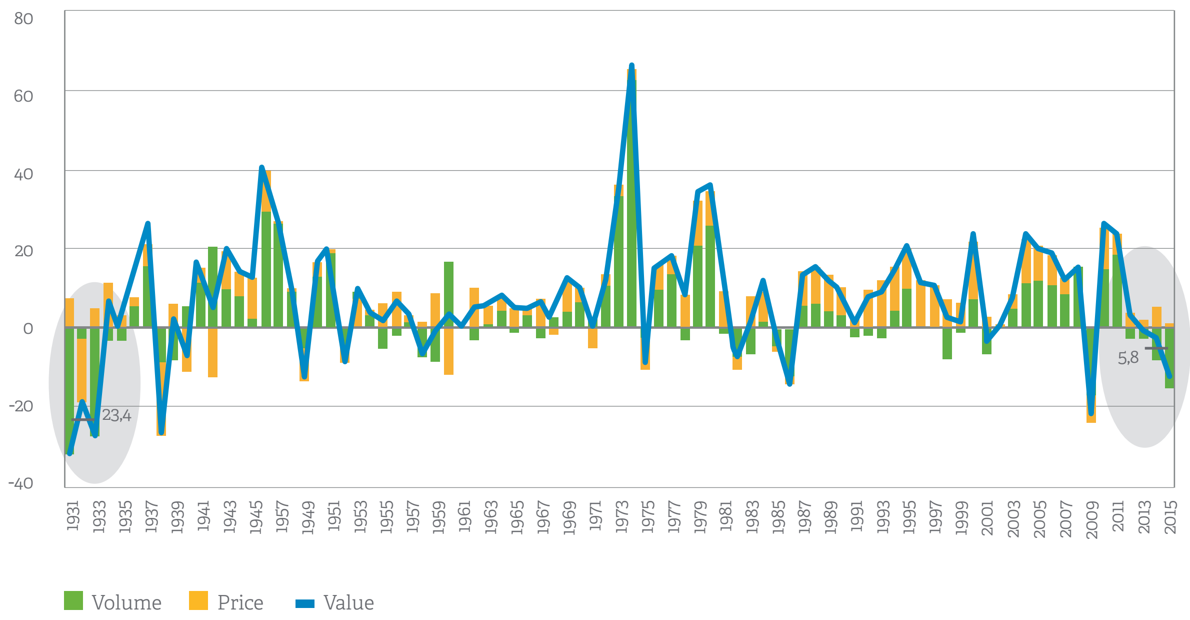
The international financial crisis in 2008 had an important impact on Latin America, as can be seen in the previous figures. However, the sustained Chinese demand did not only alleviate the consequences, but also enabled an early recovery. While the recession in the OECD region amounted to 3.4%, Latin American production only fell by 1,9 %.

THE CRISIS ENTAILED BY THE "NEW NORMAL": THE FALL IN PRICES OF RAW MATERIALS

Although the region was able to withstand the global crisis thanks to the stable Chinese demand, it has not been able to endure the change of the demand in question. A change that is directly related to a new production model, developed in accordance to the budget with which the new normal has been established.

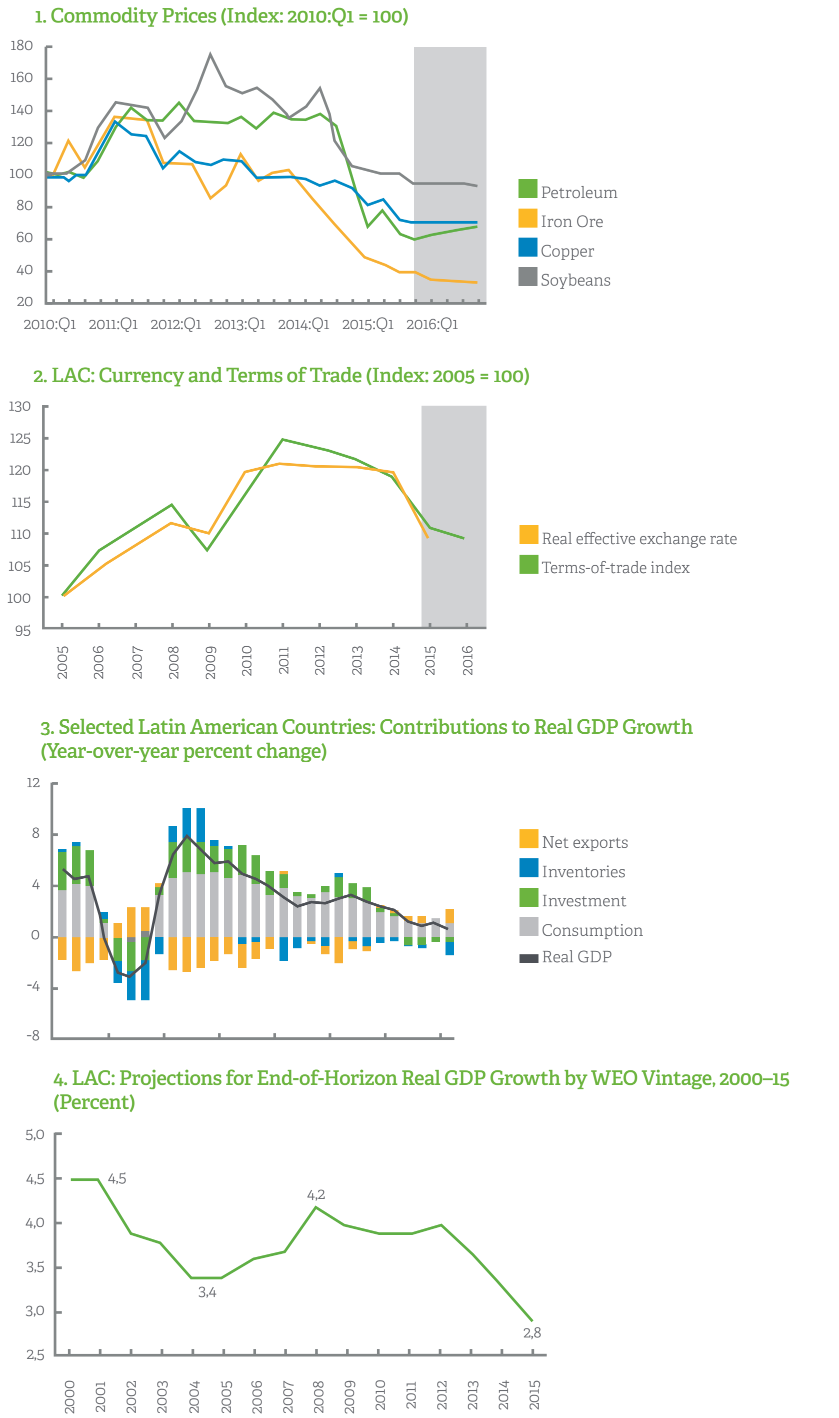
The direct consequence has been a sudden decline in the demand for raw materials and the subsequent drop in prices. A factor that has directly affected the continued decline in exports in the region since 2012. As noted by the ECLAC, "between 2012 and 2015, Latin America has registered its worst export performance in eight decades".

Figure 4. Latin America and the Caribbean: variations in exports by value, price and volume, 1931-2015 (Percentages)



Source: ECLAC, on the basis of ECLAC, "América Latina: relación de precios de intercambio" (Latin America: Trade prices comparison", Cuadernos Estadísticos de la CEPAL, Nº1, Santiago, 1976 and data collected from regional indices.

Figure 5. Economic Activity in Latin America and the Caribbean



Source: "Regional Economic Outlook: Western Hemisphere, Adjusting Under Pressure", October, 2015, https://www.imf.org/external/spanish/pubs/ft/reo/2015/whd/pdf/wreo1015s.pdf

Logically, the degree of dependence on the Chinese economy and its needs and the inability to find a power to replace the Asian giant are the reasons behind the impact that the new Chinese growth model may have on Latin American economies. The rest of the world has recorded rather modest growth rates and by no means comparable to those of China. It should be noted that currently the most dynamic economy is that of the United States, expected to grow by 2.6% in 2016. As regards the Euro Zone, the recovery is still shaky and the region is expected to grow by 1.7% over the year.

2015 was the fifth year running of decline. In recent years, regional economies recorded relatively low rates of growth –between 2% and 2.5% GDP–. All international organizations agree that the dwindling growth in the region is "quite concerning", as pointed out by the UNO. According to its estimations, GDP will grow by only 0.7% or even less and insists that the main reason behind it is the fall in the prices of raw materials and the weak trade growth. It should be noted that there is a risk of a chain effect, since the decline in Chinese demand directly affects Latin America products, but also indirectly, since the contraction of trade, enhanced by the Chinese situation, also affects

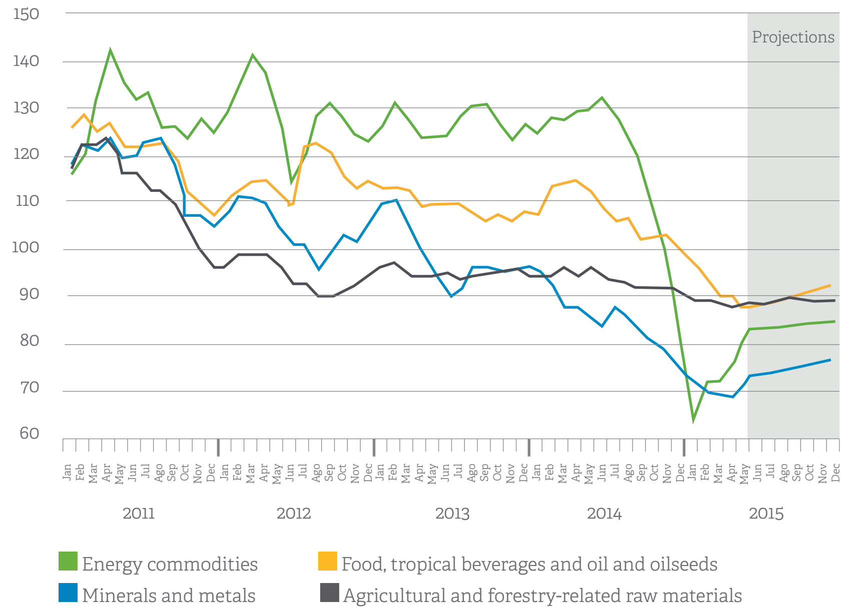
Europe and, consequently, the European demand for Latin American products[7].

The IMF projections were published in October 2015 and further corrections had to be made to write them down for 2016. Thus, the IMF expected the region to continue contracting with a fall of 0.3%, reducing by 1.1% its previous projection. The current forecast amounts to 3.4% for 2016 and 2.9% for 2017.

This correction is mainly due to the Brazilian situation, whose recession is proving more complicated and intensive than initially thought; political factors and the uncertainty generated by the cases of corruption are also exacerbating this problem.

[7] UNO, "World Economic Situation and Prospects, 2016".

Figura 6. Latin America: export commodity prices, January 2011-May 2015 (Index: 2010=100)



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

THE HETEROGENEITY OF THE REGION IS ALSO REFLECTED IN THE CURRENT CRISIS

The region, as a whole, is facing the crisis of raw materials, since this is the prevailing economic model in Latin America. However, the truth is that within this pattern we can find economies with varying levels of diversification. A factor that certainly helps in order to tackle the aforementioned crisis. Another important element which determines how deeply this crisis will affect each country is the type of exported commodities. In line with China's new economic model, the decline in demand is worse for economies that depend on the export of minerals or fossil fuels than those who mainly export food. This can be seen in the figure below: the decline in prices is sharper in the mining and fuels sectors than in the food category.

This explains the complex situation for fossil fuels-exporting countries such as Venezuela, Ecuador, Colombia and Bolivia, since fuel prices are reaching record lows. Mining countries like Peru and Chile will inevitably suffer as a result of this new situation.

Similarly, countries with greater economic diversification, such as Brazil, will be in a better position to face this challenge than the countries which practically have a single export product and lack any further exporting goods or industrial fabric, for example, Venezuela.

Figure 7. Latest IMF Projections (Real GDP growth, annual average percentage)

	2013	2014	2015	2016
	EST.		PROJECTIONS	
SOUTH AMERICA				
ARGENTINA	2 9	0.5	-0.3	0.1
BOLIVIA	6.8	5.4	4.3	4.3
BRAZIL	2.7	0.1	-1.0	1.0
CHILE	4.3	1.8	2.7	3.3
COLOMBIA	4.9	4.6	3.4	0.1
ECUADOR	4.6	3.6	1.9	3.6
GUYANA	5.2	3.8	3.8	4.4
PARAGUAY	14.2	4.4	4.0	4.0
PERU	5.8	2.4	3.8	5.0
SURINAME	4.1	2.9	2.7	3.8
URUGUAY	4.4	3.3	2.8	2.9
VENEZUELA	1.3	-4.0	-7.0	-4.0
CENTRAL AMERICA				
BELIZE	1.5	3.4	2.0	3.0
COSTA RICA	3.4	3.5	3.8	4.4
EL SALVADOR	1.7	2.0	2.5	2.6
GUATEMALA	3.7	4.0	4.0	3.9
HONDURAS	2.8	3.1	3.3	3.4
NICARAGUA	4.4	4.5	4.6	4.3
PANAMA	8.4	6.2	6.1	6.4
LATIN AMERICA AND THE CARIBBEAN	2.9	1.3	0.9	2.0

Source: IMF, World Economic Outlook; and IMF staff calculations and projections.
Regional aggregates are purchasing-power-parity GDP-weighted averages unless otherwise noted.

The level of dependence on the Chinese economy is also a reason for which certain countries have been more affected than others. In this sense, South America relies more on this market and, therefore, its economic indicators are worse than those of Central American countries and Mexico, whose economies are significantly affected by the U.S., which at this time is experiencing a slight economic recovery. Although the region as a whole is facing a crisis, the aforementioned reasons explain why not all Latin American actors have been affected in the same way. This aspect can be seen by the data on GDP growth, which underlines the heterogeneity that characterizes the region.

THE RE-PRIMARIZATION OF AN ECONOMY BASED ON THE PRODUCTION OF RAW MATERIALS

This is not the first time that Latin America faces a crisis like the current one. Actually, these crises are cyclical and the region has been facing them since the second half of the nineteenth century, when its production model was established. Aware of the limitations of this model, the region has also sought to modify it. The most important attempt took place after WWII, when the region tried to promote an import-substitution industrialization process. This model had little success and resulted in a highly uncompetitive industry funded by the State.

"The challenge is transforming the economic model of the 19th century to face a crisis of the 21st century"

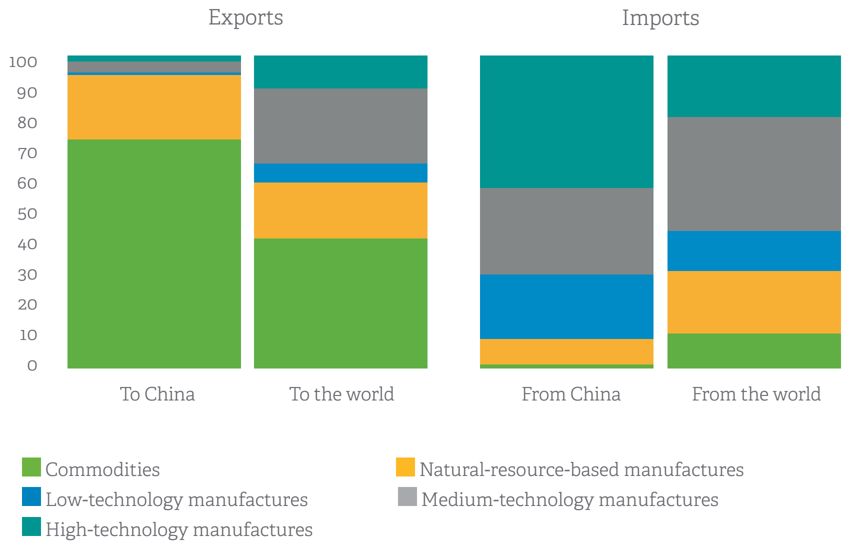
At this time, the challenge is critical as it implies transforming the same economic model of the 19th century to face a crisis of the 21st century. This means that the region needs to invest in knowledge and new technologies to ensure the diversification of the economy, among other things.

Trading with China entails so many advantages that no Latin America country, regardless of their political ideology, has been reluctant to conduct business with the Asian nation. Latin American countries have tried to make political capital out of this relationship, since all governments without exception have benefited from it. The governments who advocate for a free market signed FTAs and have openly established a relationship based on free trade, while ALBA governments defend this relationship as a departure from the traditional hegemonies.

But beyond political messages, for many experts such as Margaret Myers –Director of the China-Latin America program of the Inter-American Dialogue think tank– the relation with China entails "greater advantages than disadvantages for the development of Latin America" in areas such as infrastructure and technology, among others.

However, in addition to the current and the potential advantages, there have also been negative consequences such as the re-primarization of the economic model. Thus, this approach provided significant benefits in the short term, but was a real step backwards in the medium and long term, as it was based on a development model that certain experts have defined as "neo-extractive". In this context, the economic activity did not only focus on the production of commodities, but only included a very low number of products. This has favored the strengthening of the business relationship with China, a rather skewed one, greater than the relations that the Latin American region had established with other trading partners.

Figure 8. Latin American and Caribbean Trade with the world and China by technological intensity, 2013 (percentages)



Source: Economic Commission for Latin America and the Caribbean (ECLAC)

By 2012, commodities accounted for 69% of the total exports from Latin America and the Caribbean to China and natural-resource-based manufactures accounted for 24% of the total exports. Low-, medium- and high-technology manufactures accounted for only 2%, 3% and 2% respectively. With the exception of Costa Rica (whose main exports to China are electronic circuits) for Argentina, Brazil, Bolivia, Chile, Colombia, Ecuador, Peru and Paraguay these exports focused on soybeans, minerals and crude oil depending on the available basic product that each country exported. In 2012, Chinese exports to Latin America and the Caribbean focused on high-technology manufactures (41%), while medium-technology manufactures amounted to 27 %[8].

5. DIVERSIFICATION, KNOWLEDGE AND INTEGRATION: KEY FACTORS FOR THE LATIN AMERICA-CHINA RELATIONSHIP

The fact that China is the cause behind all Latin American ills does not mean that the region needs to give up on its relationship with the Asian power. Even if the region were willing to terminate this relationship, it is something that it simply cannot afford to do. It would be neither the most realistic option nor the best. First, because it is not possible to picture a similar power –in the short term– with such a high demand for raw materials. Second, because this economic model is not sustainable and, therefore, even if a similar new power were to replace China, sooner or later Latin

[8] A survey carried out by Mexican newspaper El Financiero, provided worrying examples of the degree of Latin American dependence on raw materials. According to the newspaper, the following data were collected in December 2014:

- Venezuela has an almost absolute raw materials dependence, since commodities account for 98% of its total exports. The country hardly produces anything besides oil, iron and aluminum.
- Ecuador depends on raw materials for 86% of its total exports, most of them being oil, coal, coffee, gold and flowers.
- Bolivia mainly depends on oil and silver and commodities account for 72% of its total exports.
- Argentina and Peru have agricultural manufacture and raw materials dependence for 70% of their total exports.
- Chile depends on raw materials, mainly copper, for 63% of its export income.
- Brazil depends on commodities for 52% of its exports.

http://www.elnuevoherald.com/opinion-es/opin-col-blogs/andres-oppenheimer-es/article32743806.html#storylink=cpy

"The change in the Chinese demand should be seen as an opportunity to progress and generate further added value"

America would have to face a crisis like the one taking place at the moment. However, the context would be even grimmer, since the rest of the world would have moved on and Latin America would be trailing behind due to the shortcomings of the economic model in question. In short, it should be stressed that the relationship with China is not only an opportunity but a critical element that Latin America has to take advantage of.

To overcome this hurdle, continue growing and enhancing the economic development of the region, the region needs to meet a sine qua non condition: the export system of commodities without any added value cannot continue existing in today's economy. Latin America needs a sustainable economic system and it must face structural changes.

As pointed out by Jorge Cachinero, "the change in the Chinese demand should be seen by Latin American countries as an opportunity to progress and generate further added value in their exports. This could be achieved through structural reforms in order to enhance productivity and competitiveness. In this way, the region would be able to overcome its current dependence on raw materials"[8].

This challenge will certainly be no easy task. The very nature of the changes makes it significantly complex and the process will also require large investments. However, as it is typical in these cases "now there are no public funds to finance this process"[9]. Therefore, Latin America cannot ignore the Chinese market and its investors, as it needs them in order to finance the future reforms.

As regards the aforementioned amendments, both international organizations and experts agree on the need to ultimately abandon the exclusively extraction-based economy and the elements that are needed to achieve a competitive and sustainable development. Investment in knowledge, infrastructure, technology, environmental safety and energy efficiency are instrumental areas to modify the economic model. However, the productive field in which these elements should be implemented is not as clear.

Perhaps the key lies in the concept of circular economy, rather than the productive sector in which investments should be made. The concept of circular economy needs to be implemented in order to ensure a better use of natural

[9] J. Cachinero, op. quote

[10] Federico Steinberg, "Lo que nos deja el ciclo de las commodities en América Latina", ("The legacy of the commodities era in Latin America"), February 8, 2016, http://www.infolatam.com/2016/02/08/lo-que-nos-deja-el-ciclo-de-las-commodities-en-america-latina/.

"Latin America can be competitive and develop a sustainable economy"

resources across the region, investing in all relevant areas to prevent all these resources –gold, copper, silver...– from leaving the region. The objective is not only to ensure that these resources are not depleted, but to also use them in other sectors to ensure the creation of the aforementioned circular economy, since everything is exported as it is extracted. Under this economic concept a rather fruitless debate could be solved. In this sense, the challenge is not whether all efforts should be made to establish an industrial fabric and carry out a systematic process of industrialization, as has been pointed out in many occasions. The key is not whether the economic activity should focus on agriculture, industry or the service sector. The key is to apply a criteria of circular economy based on knowledge, technology, infrastructure... which make any economic activity sustainable.

In accordance to this approach, the changes that need to be made do not necessarily mean that the production model needs to be thoroughly transformed, but merely reformed. This means that Latin America can be competitive and develop a sustainable economy even if it maintains its mainly agricultural and mining-based economies. But regardless of the economic activity each country focuses on, it is essential to generate added value and ensure economic diversification. To this end, knowledge, technology and a skilled labor force are critical.

Diversifying export markets and products and giving further added value in foreign sales is a fundamental task. Under these criteria it is necessary to analyze the international market and develop the productive activity that the market demands. As regards China, agricultural production –under the aforementioned conditions– may be a great option.

It should be noted that China has only 7% of arable land and 6% of the world's water resources but needs to feed 22% of the world population. Consequently, agriculture and agribusiness are a great market for the Latin American region, even more if we take into account the transformation –both social and economic– that is currently taking place in China. The development of the country is making the urban population and middle-class grow at a fast pace. This social process entails changes in dietary habits. As has already been shown, the demands of the new consumers have changed, since they now seek a higher quality and a wider variety. Therefore, there has been a greater demand for protein food, processed food, higher quality requirements and food with specific properties.

"It is a matter of implement a new production model in Latin America"

Service and tourism offer great opportunities that the region should not ignore, since millions of Chinese citizens have also changed their recreational activities thanks to their newly acquired middle-class status.

If we take into account this new market and all the opportunities it will offer it can be seen why the economic transformation does not necessarily require a change in the production model, although diversification needs to be promoted, as well as the generation of added value and the processing of agricultural products. This will require knowledge, technology, production infrastructure, transport and logistics.

In this sense, another key aspect –as mentioned by the Executive Secretary of ECLAC, Alicia Barcena– will be regional integration. This integration shall increase the changes of accessing further markets and enhances the negotiation power of the region, in this case, vis-à-vis China.

6. WHAT ROLE DOES CHINA PLAY IN THE TRANSFORMATION OF THE PRODUCTION MODEL?

Latin America has already stated that it will not be able to move forward without China, neither now nor in the future. China, for its part, has shown no intention of abandoning the relations with the American region.

However, one of the question to be resolved is the degree of complementarity they will achieve. Despite being quite high until recently, considering the changes in the Chines demand it should be wondered whether the latter remains the best trade partner for Latin America. The truth is that Latin America currently needs China mainly to promote the aforementioned reforms in its production model but, so far, Chinese interests have not greatly fostered said reforms. The asymmetry in trade and the concentration of Chinese investment in mining opportunities or infrastructures which further enhance the Chinese business have not promoted the necessary changes.

It is thus a matter of modifying the terms governing the trade and investing relationship with China in order to implement a new production model in Latin America. The experience acquired during the economic boom should not be wasted: "What we have learned so far is that global trade or receiving FDI is not enough. We need to make further efforts to fully seize this trade and investments"[10].

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[11] Statements by Augusto de la Torre, Chief Economist of the World Bank for Latin America.

Taking advantage of this opportunities necessarily involves establishing a "more symmetrical" relationship between Latin America and China. This new relationship would promote a "more competitive model with global supply chains with more added value, technology, innovation and the creation of better employment", said Enrique Garcia, President of the Development Bank of Latin America (CAF)[11].

So far, the interest of China in the region has been clearly shown and it does not seem a passing fad. For the ECLAC there are five milestones that have strengthened the links between both regions and which demonstrate the interest of China in Latin America. The first was the White Paper on the relations with the region, published in November 2008. The second was the proposal to strengthen the political, economic and cooperative relations made by the former Prime Minister Wen Jiabao in June 2012. The third milestone was the proposal of an ambitious framework for cooperation for the 2015-2019 period, known as "1+3+6" announced in July 2014 by President Xi Jinping at the first Summit between Latin America and the Caribbean and China held in Brasilia. The fourth was the approval of the aforementioned Cooperation Plan 2015-2019 between the Member States of the CELAC and China. The fifth was the visit of Prime Minister Li Keqiang to Brazil, Chile, Colombia and Peru in 2015.

In addition to the interest shown by China through the aforementioned milestones, if we take a closer look at its statements and the documents it has drafted so far we can see its explicit willingness to help the Latin American economic model change towards the new approach that the region seeks to implement through the aforementioned cooperation plans. This is critical in order to successfully meet this challenge. In this sense, there was a declared and constant intention of contributing to revert the concerning export re-primarization of the region through further support in order to enhance productivity, innovation, infrastructure, logistics and education and training of human resources.

It should be noted that this is a double historic opportunity for Latin America, if it is finally implemented, since Chinese authorities

[12] President of the Development Bank of Latin America (CAF): Latin America and China should seek a more symmetrical relationship, May 5, 2014, http://www.7dias.com.do/economia/2015/05/14/i188441_presidente-caf-america-latina-china-deben-buscar-relacion-mas-simetrica.html#.Vrs4WVjhDIU

have promised to increase and diversify investment flows. Such investment should be directed towards infrastructure, logistics and connectivity. This would not only enable the redefinition of the trade relations with China, but would also foster intra-regional trade and the creation of regional value chains.

However, this possibility does not merely depend on China. Actually, the main responsibility lies with Latin America. It is essential for the region to launch initiatives and proposals to direct these investments in order to ensure that they remain attractive for China but also help promote Latin American development. It is not an easy task.

Now is the time to think which steps should be made, how these proposals should be drafted and in which way should they be implemented. This requires clear objectives in relation to the development model, multilateral coordination between Latin American countries and previous agreements between the governments of the aforementioned nations.

There are no guarantees in these issues, as nothing seems clear. The heterogeneity of criteria and nationalist budgets have wasted many opportunities for the region to promote a greater development. If this became the reason to waste another Chinese opportunity, only Latin America would be to blame.

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