

China and Latin America: Experience, lessons and challenges

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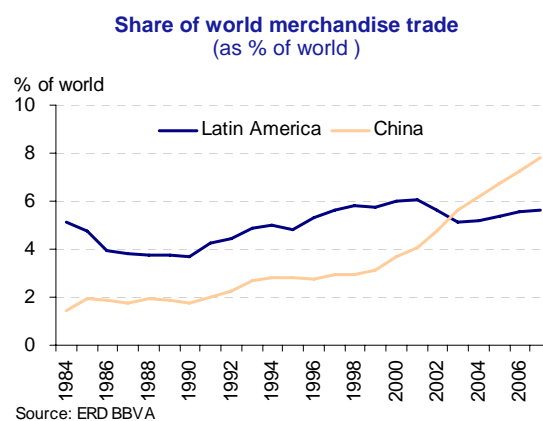
- Experiences from China

- 1. How to become an export powerhouse?*
- 2. How to create a strong domestic market?*
- 3. How to move up the ladder in terms of economic structure?*
- 4. How to sustain growth in the long-term?*

1. How to become an export powerhouse?

- Latin America has had a good export performance in the last few years ...
- ...but mainly due to a positive terms of trade shock: very high commodity prices
- China has performed much better

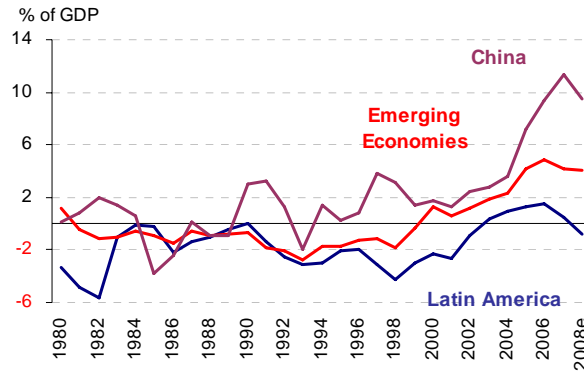
China has clearly surpassed Latin America as exporting block



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It has also managed to keep imports have remained under control

Current account balance China, Latin America and Emerging Economies
(as % of GDP)

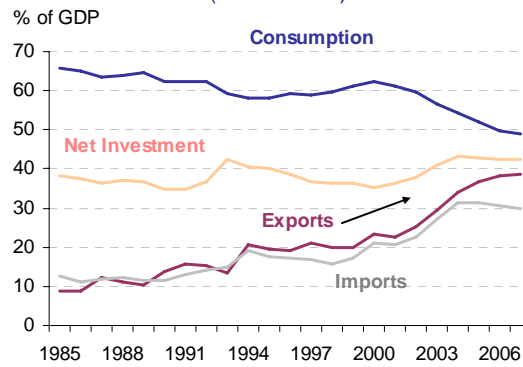


Source: ERD BBVA, IMF (Oct.2008)

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Exports are increasingly the driver of China's economy

China's economic structure by expenditure
(as % of GDP)

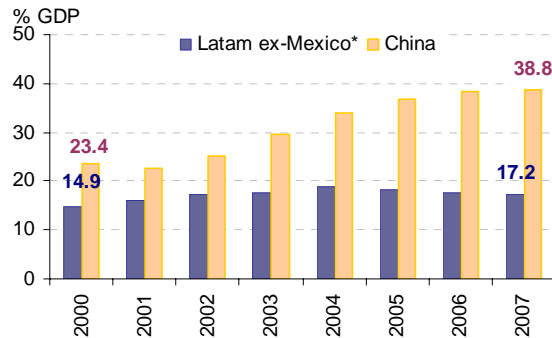


Source: ERD BBVA

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but much less so in South America. More the case of Mexico

Exports/GDP Latin America vs China
(as % of GDP)



*Argentina, Brazil, Chile, Colombia, Peru, Uruguay and Venezuela.

Source: ERD BBVA

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1. How to become an export powerhouse?

How did China manage?

- Promoting FDI for export purposes
 - Through tax incentives for FDI and derogation of VAT on exports
 - Friendly business environment
 - Flexible labor regulation
- Once JVs and foreign companies managed, promote same pattern for Chinese companies

1. How to become an export powerhouse?

Why not Latin America?

- FDI focused on non tradable sector
 - Except in Mexico
- And probably not because of distance (as China demonstrate) but
 - Not good enough business environment although clearly improving
 - Labor also more expensive but not too expensive

Clear opportunities!

2. How to develop a domestic market?

Easy for China given its size

- But still merit in terms of industrial policy
 - Importance of creating winners in different sectors
- Also the case of the largest countries in Latin America
 - Mexico and Brazil, although to a lesser extent

3. *How to move up the ladder?*

- China confirms that the usual suspects of common theories of economic growth are key
 - Physical and human capital
- Both lagging behind in Latin America
 - But moving fast in the right direction

Opportunities for investment in infrastructure in Latin America should pay out given the needs

3. *How to sustain growth in the medium term?*

China's model: saving in good days for rainy ones

- Importance of reining in fiscal accounts in good times
- Accumulating international reserves as a precautionary device
- Some countries in Latin America quite similar to China's policies...
- even if more difficult given the increased procyclicality attached to exporting commodities
 - Chile's copper stabilization fund
 - Brazil's fiscal responsibility law
- Even more important: have a clear development model
 - export-led in China; for Latin America?

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- **Experiences from Latin America**

- 1. How to reform the banking system?*
- 2. Granting financing access to SMEs*
- 3. How to move from fixed to floating rates?*
- 4. How to live with full convertibility of capital account?*

1. How to reform the banking system?

- After recurrent crises, Latin America has undergone a major reform of the financial system through:
 - Opening up to foreign competition
 - Introduction of international standards in accounting and regulation
 - Improving supervision (independence of supervisors)

2. Granting financing access to SMEs?

- Although the size of the financial system is smaller in Latin America than in China, **access to financing by SMEs is easier**
 - Chinese SMEs are still too dependent on retained profits to grow
 - This is easy in good times but it may be a big problem in bad times
 - In addition, without borrowing SMEs will find it much harder to move up the scale and become bigger companies
- The role of the **banking system** has been key in Latin America to give access to SMEs
 - Foreign banks have been instrumental by introducing credit scoring systems
- Also microfinance in the case of micro-entrepreneurs
 - See paper by GAO Jing (CASS) presented at BBVA- HKU conference

3. How to move from fixed to floating ex rates?

- Most Latin American countries have made such move
 - The most successful cases have been those which have
 - Switched in good times and not in crisis ones
 - Have introduced a clear inflation targeting scheme at the same time
- Having an anchor is absolutely key**
- Having a flexible exchange rate has given Latin American countries a lot of flexibility during the current turbulences
 - Large depreciations without major problems

4. *How to live from full capital account convertibility?*

- Most Latin American countries have a fully liberalized capital account
- But have not suffered so much from capital outflows as many Asian countries during the current crisis
- **Why?**
 - Importance of developing a domestic market for the government /private sector to finance itself: development of domestic bond market (in domestic currency)
 - Active use of regulatory tools such as limit on forex exposure by banks, etc

In sum

- **China offers important experiences for Latin America on the real sector**
 - *Specially how to export and how to move up the ladder in terms of economic structure*
- **Latin America offers more experiences on the finance side**
 - *Faster opening up of banking sector*
 - *Also a different model in terms of exchange rate and capital account management*

In sum

- Both regions are not only complementary in economic terms...
- But also in terms of experiences!



Thank you!

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