Foreign Trade

World of opportunities



Solange Monteiro, *Rio de Janeiro*

THE BRIGHT SPOT in the economies of Brazil and China in recent years has been trade. The two countries recorded healthy export growth—in the case of Brazil, thanks mainly to Chinese demand—and are among the top recipients globally of foreign direct investment (FDI). The challenges for trade as a driver of economic expansion in the future, however, are different for each country: while Brazil needs to increase the share of exports in the economy, diversifying export goods and markets, China needs to reduce the share of exports in its economy, focusing more on improving the quality of FDI and innovation.

In China, the remarkable expansion of trade and FDI is the result of reforms that in recent decades have promoted economic liberalization, changing the reality of a country that until the early 1970s was a closed economy with trade in goods limited by the centrally planned economy. Among the elements that were part of the change was the establishment of four special economic zones in 1980, investment in infrastructure, and devaluation of the Chinese currency, the renminbi, since 1994.

The changes accelerated after China's entry into the World Trade Organization (WTO) in 2001. From 2002 to 2010, China's exports rose an average of 22% a year, and imports by 20%. Hu Zhaoxia, professor, the Faculty of Economics and International Trade of Xiamen University, has pointed out that after China's entry into the WTO, the average tariff on imports fell to 15% in 2001, about half the 1982 level, and was reduced further to 10% in 2005. "The volume of goods that needed import licenses fell from 46% of total imports in the early 1980s to less than 4% by the time China joined the WTO," she said.

Another important feature was the diversification of exports from agricultural products and crude oil in 1980 to labor-intensive manufactures, and gradual improvement of those products. "Currently, we see that China is becoming less competitive in producing goods that have a lower aggregation of technological factors and is making efforts to increase the competitiveness of its higher-value-added goods," noted Roberto Milani, director of the Brazil-China Business Council.

Boosted by strong Chinese demand for agricultural commodities and iron ore, Brazil also recorded significant growth in its exports in the last decade. It has become China's ninth largest trading partner, surpassing the United States in 2009. The value of trade between Brazil and

China has grown almost 25 times in a decade; in that time the Chinese trade deficit with Brazil increased nearly 20 times, to about US$20 billion.

However, behind these glowing results Brazil's trade has a darker side: problems of the competitiveness of domestic industry led to a steep decline in the share of manufactures in total exports, from 60% in 2000 to just 13% in 2012. This is partly explained by the persistent protectionist bias of Brazilian trade policy, making the country one of the least open of the BRICs—Brazil's total trade-to-GDP ratio is 23%, compared to 53% for China—and limiting its share in total world exports to 1.3%, higher only than that of South Africa (0.6%). Lia Valls, IBRE researcher, has identified a major issue: "Brazil has often used higher tariffs on imports as an instrument of industrial policy. Today's situation calls for a tariff policy that allows cheaper imports of capital goods to improve the economy's competitiveness . . . . We should not protect whole chains of production; instead we should encourage production chains that have a comparative advantage in being integrated with other regional or global chains."

Valls noted, however, that in Brazil the protectionist bias does not apply to attracting foreign investment, explaining, "Brazil has always lived with an external current account deficit and has needed to attract foreign investment to finance it. Today, the big challenge for Brazil is to improve competitiveness. Trade will always be important. Brazil will never have to depend on exports because of the size of its domestic market, but we are not immune to external crises, and assuring diversified and high-quality exports is necessary to reduce external vulnerability."

"Brazil has often used higher tariffs on imports as an instrument of industrial policy. Today's situation calls for a tariff policy that allows cheaper imports of capital goods to improve the economy's competitiveness."

Lia Valls

In contrast, the main challenge for China is to reduce its dependence on export-led growth, especially when, as now, international demand is low. Hu emphasizes that "while trade liberalization has contributed to raising China's GDP, it is not a sufficient condition for ensuring sustained long-term growth."

To avoid the risks of over-dependence on export-led growth, Hu emphasizes the importance of the current government's strategy of boosting the domestic market. She believes that in China the beneficial effects of bringing in foreign capital to promote technology transfer and productivity are not yet clear. There is a need to focus more on the quality of foreign capital. In addition, Hu advocates replacing the current policy of granting foreign capital access to the domestic market in exchange for technology transfer with a policy of incentives to scientific and technological development with an emphasis on innovation.