China's Investment in Latin America:
Themes, Challenges and Future Trends

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INTRODUCTION

Economic growth in China over the last decade has been remarkable. During the same period, economic growth in a number of Latin America's maturing economies (most notably Brazil, but others as well) has also caught the world's attention.

Both China and Latin America showed resilience during the world financial crisis, during which Chinese demand for raw materials from Latin America provided a helpful stimulus to the region. Today, both are sought-after regions for investment. Buoyed by confidence from their economic successes, China and Brazil are playing greater roles on the world stage; by the accounts of most experts, both are on the short list of those countries most likely to shape the 21st century.

Chinese-Latin American trade has recently reached historic highs, to the mutual benefit of China and its Latin American trading partners. Chinese foreign direct investment in the Latin American region has also skyrocketed, and it seems each week a new blockbuster investment deal is announced. Latin America has generally welcomed this investment, though it has also presented some challenges. On another level, the increasingly important role China is playing has concerned some U.S. policymakers, who view China as challenging the historical U.S. hegemony in the region.

This article outlines the nature of China's foreign direct investment in the region to date and what is driving these investments from both the Chinese and Latin American perspective. The article then explores challenges the investment relationship faces and concludes with some predictions for future trends.

RECENT TRADE AND INVESTMENT TRENDS

1. The Explosion of Chinese-Latin American Trade. China's recent investments in Latin America have been preceded by a vibrant and expanding trade relationship with many Latin American countries over the past decade. Understanding the Chinese trading relationship with Latin America provides helpful context for the investment relationship.

The change in the trade relationship has been staggering. Trade between Latin America and China in 1999 totaled approximately $8 billion; by 2010, it had grown 22 times to approximately $180 billion. By comparison, trade between Latin America and the United States grew by approximately 0.5 times[2] over the same period.[3] This statistic is often cited to support the perception of the ascendancy of Chinese commercial influence in Latin America. The inability of the United States to implement a free trade agreement with Colombia[4] (with critics citing the divisive American political environment as the cause) has further undermined the U.S. trading relationship with Latin America vis-à-vis China. During the same period, China signed a number of free trade agreements with countries in the region, including Chile, Peru and, most recently, Costa Rica.

The trading relationship between China and economies in Latin America has three principal facets: it is at the same time a buyer, seller and competitor. First, China is a huge buyer of raw materials from resource-rich countries such as Brazil, Chile, Argentina, Ecuador and Venezuela. Second, China exports manufactured goods to almost every country in the region. Third, China competes in the region's export markets for manufactured goods (particularly Mexico and Central America). Thus, China's trade relationship with resource-rich countries in Latin America differs considerably from its relationship with those countries that depend primarily on the export of manufactured goods.

2. The Chinese Investment Boom Follows Trade Expansion. The Chinese government has encouraged investment in Latin America as a way to strengthen trade ties.[5] Sources vary on the amount of Chinese foreign direct investment in Latin America, though by almost all accounts 2010 was a watershed year. The following provides data on Chinese direct investment in certain economies of Latin America and the Caribbean. (Other figures for Chinese direct investment in Brazil alone put the number for 2010 in the $12 billion to $20 billion range.)[6]

a. The Investment Recipients. The vast majority of direct investment from China, over 90%, has gone to natural resource enterprises, including hydrocarbons, copper and iron ore, and agriculture. Not surprisingly, the primary recipients of this investment have been those economies where natural resources are abundant, namely Brazil, Argentina and Peru. While China has been an important

China: Foreign Direct Investment in Selected Economies of Latin America and the Caribbean[7] (Millions of dollars)

Country	Confirmed Investments		Investments Announced
	1990 to 2009	2010	2011 Onwards
Argentina	143	5,550	3,530
Brazil	255	9,563	9,870
Colombia	1,677	3	—
Costa Rica	13	5	700
Ecuador	1,619	41	—
Guyana	1,000	—	—
Mexico	127	5	—
Peru	2,262	84	8,640
Venezuela	240	—	—

source of investment for certain smaller economies, such as Ecuador and Guyana, Chinese investment has had very little relevance in Mexico and most of Central America.[8]

One feature of Chinese investments is the willingness of the Chinese government to make significant investments in a number of economies that have been otherwise shunned by Western investors. For instance, Ecuador has been shut out of global markets since it defaulted on its bonds in 2006, and Venezuela similarly has had a difficult time attracting foreign investors given the nationalization program instituted under the Chavez regime. Both countries have been significant recipients of Chinese investment, as has Cuba.

b. Types of Investments. The form of these investments varies widely. They range from greenfield projects (such as the purchase of exploration and production concessions — namely in the hydrocarbons sector) to taking minority or control equity positions. In addition to these equity investments, Chinese banks have proven to be an important source of debt financing, both in assisting Chinese companies seeking to finance their overseas investments and, in some cases, lending directly to companies and sovereigns in the region.

c. The Investors. Nearly all of the Chinese investors making the headline-grabbing deals are large state-controlled companies in the natural resources area.[9] As state-controlled companies, these companies are obviously useful instruments for the Chinese government to implement state policy. In addition, the debt financing mentioned previously offered to Chinese investors by Chinese state-owned banks for overseas expansion projects has been an important tool to promote expansion abroad.

While large state-owned companies have been associated with many of the largest investments in Latin America, Chinese private investors, the source of most of the growth in jobs and wealth in the Chinese economy, are not far behind.[10] The Chinese government recently indicated that it would more aggressively promote these private investors, who have argued that the government had previously focused too heavily on providing overseas expansion opportunities to state-owned companies, to the detriment of Chinese private companies.[11]

WHAT IS DRIVING CHINESE INVESTMENT IN LATIN AMERICA?

The Chinese government has been vocal in its support of investment in Latin America,[12] but what is the underlying rationale? Some considerations are obvious and others less so. While motivations will vary depending on the particular investment, some consistent themes are listed herein.

1. Resource Security: Feeding the Dragon. The primary motivation associated with Chinese investment is the need to secure a stable supply of raw materials necessary for China's economic growth. As mentioned earlier, state-owned corporations and financing provided by state-owned banks are incredibly useful instruments to effect these goals of resource security. Chinese investment has not only supported the companies that supply these natural resources, but also the infrastructure that allows for more efficient transportation of these goods to China. For instance, the Chinese and Colombian governments have been in discussion regarding the construction of an alternative to the Panama Canal, a rail route that would link the Pacific and Atlantic coasts of Colombia. This would provide for more efficient transportation of goods to and from the Atlantic coasts of Latin America to Asia.

2. It's Good Business. Somewhat less considered than resource security is that even while the Chinese government is promoting expansion abroad, such expansion is simply good business for many Chinese companies. As natural resource companies in China have grown to feed their economy's demand, investing abroad often makes sense for a company's own growth and diversification strategies.

Infrastructure construction in China is another excellent example. Over the last two decades, China has gone through a "golden age"[13] of infrastructure development, building up its transportation, telecommunications and energy infrastructure. A common estimate puts recent Chinese construction projects undertaken in a single year as being equal in scope to all infrastructure currently existing in Great Britain. In some sectors, such as railways and telecoms, Chinese companies have demonstrated exceptional technological progress over the last few years. Chinese companies are known for their low-cost operations and their ability to offer financing to their customers from state-owned banks. Infrastructure construction is one area in which China has a significant competitive advantage, one that will help it considerably in international markets.[14]

3. Side-Stepping Trade Barriers. While the largest investments made by China have been primarily in the natural resources area, Chinese manufacturing companies are also increasingly investing in Latin America. Although the size of these investments is generally smaller, their number will likely increase in light of Chinese capabilities in this sector. By investing in export markets, Chinese companies are often able to get around trade restrictions to which they might otherwise be subject if exporting goods directly from China. Also, selling locally produced manufactured goods may help reduce trade deficits in those markets where trade imbalances have been identified as problematic (as further described hereafter).

4. Diversification and Portfolio Investment. China needs sound investments for cash generated by its huge trade surplus and high savings levels. For a number of political and economic reasons, U.S. treasuries, historically the home for surplus Chinese cash,[15] look less attractive than they once did.

5. Diplomacy. A common perception, promoted by the Chinese government, is that China has a policy of making investment decisions without regard to a host country's domestic affairs, and this policy has given China an advantage over U.S. and European companies, especially when doing business with more "controversial" regimes around the globe (this is sometimes referred to as China's "no strings attached" policy). The accuracy of this perception is certainly open to debate,[16] though what seems certain is that stronger commercial ties result in stronger diplomatic relations. Over the past decade, China has succeeded in building on its commercial ties and expanding and strengthening diplomatic relationships throughout

Latin America, from the largest to the smallest economies, with both strong U.S. allies in the region (such as Chile and Colombia) and those countries with more antagonistic views of Washington (such as Venezuela, Ecuador, Nicaragua and Cuba). This comes during a time that critics have argued the U.S. government did not "prioritize" its relationship with Latin America, given its preoccupation with the War on Terror.

WHAT'S IN IT FOR LATIN AMERICA?

The benefits of Chinese investment for Latin American economies are multifaceted, and vary from country to country and investment to investment. Four of the most often-cited benefits include the following:

1. The Need for Financial Capital in Latin America, Especially for Infrastructure Investment. Latin America has an incredible list of infrastructure needs. While Brazil's preparations for the upcoming World Cup and Olympic games and pre-salt oil exploration grab headlines, throughout Latin America inadequate roads, ports, airports and energy grids are in serious need of upgrading. Without this upgrading, many Latin American economies will not be able to fulfill their economic potential. In the period from 2011 to 2014, Brazil alone anticipates spending $750 billion[17] on various infrastructure projects. The infrastructure needs are greater than the money available from traditional sources. Historically, financing has come from a mixture of international banks, local banks and international development banks, as well as local development banks such as Brazil's Banco Nacional de Desenvolvimento Economico e Social (BNDES).

With the debt crisis in Europe unresolved, the United States teetering on the brink of another recession and the possibility of banking regulations forcing a shift to more conservative lending practices, many international banks will be less able to play the prominent lending role they once did. While BNDES and other development banks have financed a significant portion of infrastructure needs, it is clear they will not be able to fund the existing shortfalls. The local banking sector in Latin America has strengthened and deepened over the last decade, providing an important source of financing for local companies during the growth phase. Nonetheless, the scale of infrastructure needs dwarfs what the local banks would be able to provide. Chinese financing sources can help fill this gap.

2. A Political and Economic Alternative to the United States and Europe. The recent financial crisis provides an excellent argument for diversifying financing sources — i.e., embracing sources other than Western ones — for Latin American users of financial capital. On a political and philosophical level, many in Latin America are paying closer attention to the Chinese economic model given that China has been less affected by the global economic slowdown than the United States and other leading capitalist countries. With increasingly robust democracies and economic gains, many Latin American countries have become more self-confident with a view toward asserting their own diplomatic independence. In other cases, countries have elected left-wing governments that are seeking a different status quo for ideological reasons, such as building "south-south" alliances.

3. "No Strings Attached" Policy. The "no strings attached" investment policy of the Chinese government cited previously certainly has appeal to a number of Latin America's countries today, including those economies that do not have access to traditional Western market sources of financial capital.

4. China's Long-Term View. Given the Chinese government's involvement in many of its country's foreign investment decisions, there is a sense that Chinese investments are motivated by stability over the long term (especially as related to energy and food security) and not subject to the same pressures as investments from publicly traded companies in the United States and Europe, whose shareholders typically demand immediate returns. While there may be some merit to this notion, whether the Chinese government will in fact be a patient investor has not been tested by time. Also, it seems that the next wave of investors in Latin America — the Chinese private investors — may face the same market demands as their Western counterparts.

WHAT ARE THE CHALLENGES?

The increasing commercial relationship between China and Latin America is not without its challenges.

1. The "De-Industrialization" Concern. Given the huge outflow of raw materials from Latin America and the large inflow of manufactured goods from China that compete against products manufactured domestically, there is an increasing concern among policymakers in Latin America that the commercial relationship with China will not lead to the long-term diversification of Latin American economies. For instance, in 2002 approximately 29% of Brazil's exports were raw materials, though by 2009 that figure had grown to 41%. The Brazilian trade deficit with China in manufactured goods has grown from several hundred million dollars a year to $23.5 billion in 2010. Policymakers are concerned this imbalance will hinder growth and lead to "de-industrialization."

2. The "Foreign Government Control" Concern. This concern manifests itself in several different ways. First, given that the Chinese companies closing blockbuster deals in the region are state-owned, there is an increasing concern that large and valuable segments of Latin American economies are coming under the control of a foreign government. On another level, many in Latin America are concerned with the concept of foreign ownership of land and mineral rights. A Brazilian court recently took a reportedly "novel" approach to interpreting an old law in order to prevent a transaction in the agricultural sector in which huge tracts of agricultural land would be turned over to a Chinese concern. New regulatory frameworks are contemplated in Brazil that will restrict foreign ownership of "strategic" areas and minerals. In other examples, critics worry that entire economies are becoming overly dependent on China (e.g., Ecuador and Venezuela, which have much smaller economies than Brazil, but which have recently announced large investment deals with Chinese companies).

3. China as Latin America's Competitor. Competition from manufactured Chinese imports is harming the manufacturing sectors of many Latin American economies, and this image of China in Latin America is one that China must take care to manage. Mexico and certain Central American economies have been the hardest hit, especially for competition in the U.S. market, where Mexico has seen its share of the textile market lose considerable ground to the Chinese. In Brazil, certain manufacturing sectors have been very adversely affected (the toy and shoe sectors are often cited). A primary cause suggested for this imbalance is that average wages in China are one-fifth to two-fifths of those in Latin America, thus allowing substantially cheaper production and sale of Chinese goods.[18] As a result of these concerns, Latin American countries have filed more than twice as many anti-dumping actions at the World Trade Organization than the United States. Similarly, Brazil has increasingly sided with the United States over China's monetary policy, which keeps the yuan at artificially low levels and greatly assists China in export markets.

4. Cultural and Political Challenges. Some suggest that growing commercial ties with a non-democratic country like China undermine Latin America's own hard-won commitment to democracy. At least for those economies in Latin America that are strong democracies, this fundamental difference in political and, in some sense, cultural systems would seemingly put a cap on how deep the Chinese relationship with some countries can naturally progress (consider the U.S. relationship with Saudi Arabia). While there is no way to quantify this issue, this aspect of the relationship seems impossible to ignore.

WHAT'S NEXT?

What does the future hold for Chinese-Latin American trade and investment?

1. Material Chinese Investment in the Region Will Continue. While the interests of Chinese and Latin economies are not perfectly aligned, significant Chinese investment in Latin America will likely continue because the mutual benefits outweigh the challenges by a significant margin. The Chinese demand for raw materials has been lucrative for many Latin countries. Financial capital in Latin America, particularly in the case of infrastructure investment, is sorely needed. The heavy involvement of Chinese state-owned enterprises, the significant investment already made and the material efforts of the Chinese government to expand commercial and diplomatic relationships in Latin America suggest that Chinese interest in the region will continue for some time. The first wave of Chinese investment in Latin America, characterized by large blockbuster deals by Chinese state-owned enterprises, has paved the way for the second wave, which will likely include more activity by private Chinese companies. While transactions by private Chinese companies may be smaller in size, these companies will be able to move more nimbly and increase the number of transactions, suggesting that the second wave will have as great an impact as the first.

2. Chinese Infrastructure and Manufacturing Investment Will Increase. While natural resource transactions will continue to be a staple of future Chinese-Latin American trade and investment, it seems likely that the second wave of Chinese investment will be characterized by the increasing role of Chinese companies involved in infrastructure, manufacturing and other sectors in which the Chinese have significant competitive advantages. Infrastructure investment in particular would seem to be neatly aligned with the needs of many Latin economies, and it would seem to serve the Chinese image in Latin America well to be part of the story of Latin America's development.

Given the increasingly important role Chinese companies play in infrastructure development in Latin America, Chinese banks will follow, offering financing for projects. Less certain is whether Chinese banks will leverage this activity to provide capital for Latin American corporate borrowers (much the way many Japanese banks became active in Latin America). This seems less certain, though it will be interesting to see how the role of Chinese banks develops. So far, apart from investments in international banks doing business in Latin America and a few large transactions, Chinese banks have been fairly quiet in the region.

3. The United States Will Continue to Play a Leading Role in Latin America. Alarmist concerns in some U.S. policy circles of the deepening Chinese involvement in Latin America seem misplaced. While Chinese trade and investment has reached historic highs in recent years, the Chinese numbers are still a fraction of the U.S. figures, and it seems likely that the United States will continue to lead in these areas for the foreseeable future, especially in Mexico. Notwithstanding China's recent diplomatic successes, significant challenges to the China-Latin America economic relationship remain. Also, business, governmental and cultural ties between the United States (and its significant Latin populations) and Latin America are very deep. As a leading think tank recently reported (in this instance, on U.S.-Brazil relations), "[T]he two countries are remarkably similar: both are multi-ethnic young democracies that uphold common values with respect to free markets, rule of law, individual rights, religious freedom, and diversity and equality..."[19]

Chinese diplomacy in Latin America has so far been a natural outgrowth of its trade and investment ties. These ties have on balance contributed to economic growth and development in Latin America and are part of the collective story of Latin America's successes over the last decade, a story that includes tens of millions of Latin Americans crossing the threshold to the middle classes. This prosperity results in additional markets for U.S. goods and services. As long as Chinese economic and diplomatic ties contribute to this virtuous cycle of prosperity and stability, U.S. policymakers should not be alarmed. This is not to suggest the United States should "stand down" in Latin America—to the contrary, the United States should monitor Chinese ties and aggressively work with Latin American governments on a number of areas of common interest (including on issues of trade and monetary policy vis-à-vis China). The United States must also work to undo the perception that it has neglected its Latin American neighbors.

In short, the challenge to Latin America will be one of sustainable development—of balancing its lucrative trade in raw materials while protecting its local manufacturing sector and developing its infrastructure. China's challenge will be to secure its raw material sources while maintaining a positive image in the region. To do so, China will need to carefully consider its export policies, especially in the manufacturing sector. Finally, the challenge to the United States will be to not overreact to deepening Chinese ties in the region, while at the same time re-engaging with Latin America in a manner that underscores the importance of its relationships there.

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1 *The authors would like to thank Bingham summer associate candidate Annie Selden for the research she contributed to this article.*

2 *This figure represents approximately $636 billion of U.S.-Latin American trade in 2010. Doreen Hemlock,* United States Trade With Latin America Reaches $636.2B in 2010, *LATIN BUSINESS CHRONICLE, Feb. 22, 2011,* available at *http://www.latinbusinesschronicle.com/app/article.aspx?id=4785.*

3 *John Paul Rathbone,* China Is Now Region's Biggest Trading Partner, *FT.com, Apr. 26, 2011.* available at *http://www.ft.com/cms/s/0/cce437bc-6ef5-11e0-a13b-00144feabdc0.html#axzz1Zpx2nJec;* see also Latin America: Relying on China, *THE ECONOMIST: ECONOMIST INTELLIGENCE UNIT, Aug. 22, 2011 [hereinafter* Relying on China*]; Hemlock,* supra *note 1.*

4 *This free trade agreement was finally passed by the U.S. Congress on Oct. 12, 2011.*

5 *At the 2004 Asia-Pacific Economic Cooperation Summit in Chile, media outlets widely reported that the Chinese Premier Hu Jintao promised that the Chinese government would invest $100 billion in Latin America over the next decade.* See, e.g., *Michael Diaz, Jr. & Robert Q. Lee,* China's Rising Interest in Latin America, *THE CHINA BUSINESS REVIEW, September/October 2009,* available at *http://www.diazreus.com/assets/attachments/261.pdf. Other sources indicate the Premier was misquoted, and that Mr. Jintao actually indicated that he hoped two-way trade would reach that figure by 2010, and that foreign investment would double.* See Relying on China, supra *note 2.*

6 *COUNCIL ON FOREIGN RELATIONS, INDEPENDENT TASK FORCE REPORT NO. 66: GLOBAL BRAZIL AND U.S.-BRAZIL RELATIONS (2011) [hereinafter TASK FORCE REPORT]. U.S. direct investment in the region was estimated to be approximately double that of China.* See *UNITED NATIONS ECON. COMM'N FOR LATIN AM. & THE CARIBBEAN (ECLAC): FOREIGN DIRECT INVESTMENT IN LATIN AMERICA AND THE CARIBBEAN (2010) [hereinafter FOREIGN DEBT INVESTMENT].*

7 Id.

8 *Costa Rica is one exception. Since Costa Rica switched political recognition from Taipei to Beijing, the Chinese government built a new $100 million soccer stadium as a "gift" for the people of Costa Rica, and the two nations have entered into a joint venture investment in the petroleum sector worth approximately $1.2 billion in direct investment.* See *Adam Williams,* Costa Rica's 35,000-Seat National Stadium Opens, *TICOTIMES.NET, March 25, 2011,* available at *http://www.ticotimes.net/Current-Edition/Top-Story/News/Costa-Rica-s-35-000-seat-National-Stadium-opens_Friday-March-25-2011; Diaz & Lee,* supra *note 4 at 3.*

9 *These include names like Sinopec (China Petroleum and Chemical Corporation Limited), CNOOC (China National Offshore Oil Corporation), CNPC (China National Petroleum Company), Sinochem (China's largest trading company that deals primarily in petrochemicals distribution, but also in rubber, plastics and agrochemicals), Minmetals (a Chinese metals and mineral trading company) and Chinalco (the Aluminum Corporation of China Limited), to name a few.*

CONTINUED

10 *Joe McDonald,* China Promises Bigger Role for Private Investment*, USA TODAY, July 26, 2010, http://www.usatoday.com/money/world/2010-07-26-china-private-industry_N.htm.*

11 Id.

12 *China's 11th Five-Year Plan (2006 – 2011) provides some guidance to helping to understand the country's official overseas investment strategy: The plan indicates primary objectives of continued economic expansion balanced by energy conservation and protection of natural resources.*

13 *Satoru Murase,* Focus Report: Asia*, GLOBAL INFRASTRUCTURE, Spring 2011.*

14 *In fact, the U.S. subsidiary of a Chinese state-owned construction company recently won significant contracts to refurbish the Tappan Zee bridge as well as construct part of the 7 subway line in New York. Kirk Semple,* As Investors, Chinese Turn to New York*, The New York Times, Aug. 10, 2011,* available at *http://www.nytimes.com/2011/08/11/nyregion/chinese-investment-grows-in-new-york-city.html.*

15 *As of June, according to the Treasury Department's latest data, China held a total of $1.1656 trillion in U.S. debt (or 29.5% of the $4.4992 trillion in U.S. debt held by foreign interests).* See *Fred Lucas,* Biden to Chinese Premier: 'We Appreciate Your Investment in U.S. Treasuries,' *CNSNEWS.COM, Aug. 19, 2011,* available at *http://www.cnsnews.com/news/article/biden-chinese-premier-we-appreciate-your-investment-us-treasuries.*

16 *For example, China's recent "gift" of a $100 million soccer stadium to Costa Rica and entering into free trade agreements with Costa Rica came after Costa Rica severed ties with Taiwan.* See *Williams,* supra *note 7.*

17 *Ben Miller,* Infrastructure Investment: The Big Shortfall*, LATINFINANCE, Nov. 1, 2010, at 26. Brazil's second Growth Acceleration Program (PAC 2) calls for R$ 955 billion to be spent during 2011 to 2014.* Id.

18 The Dragon in the Backyard: Latin America is Tilting Towards China, Iran and the Global "South" and Away From the United States*, THE ECONOMIST, Aug. 13, 2009,* available at *http://www.economist.com/node/14209932.*

19 See *TASK FORCE REPORT,* supra *note 5.*