

Shifting wealth, China and Latin America: Current and Future Challenges

Rolando Avendano

OECD Development Centre

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China and Latin America: Current and future challenges

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Shifting Wealth: A growing process

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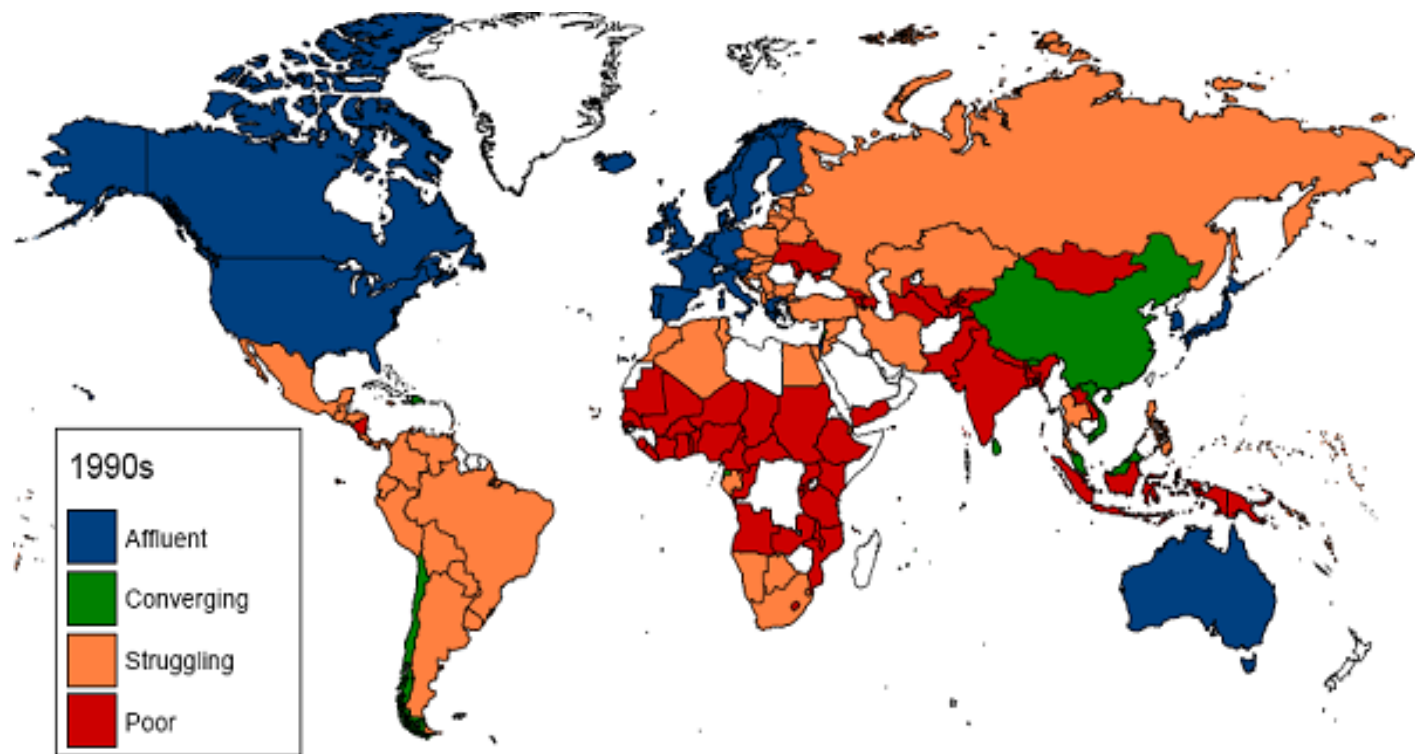
The Skills effect: a growing concern for Latin America

3

China and Central America: growing ties

New Geography of Growth: The Four-speed World in the 1990s

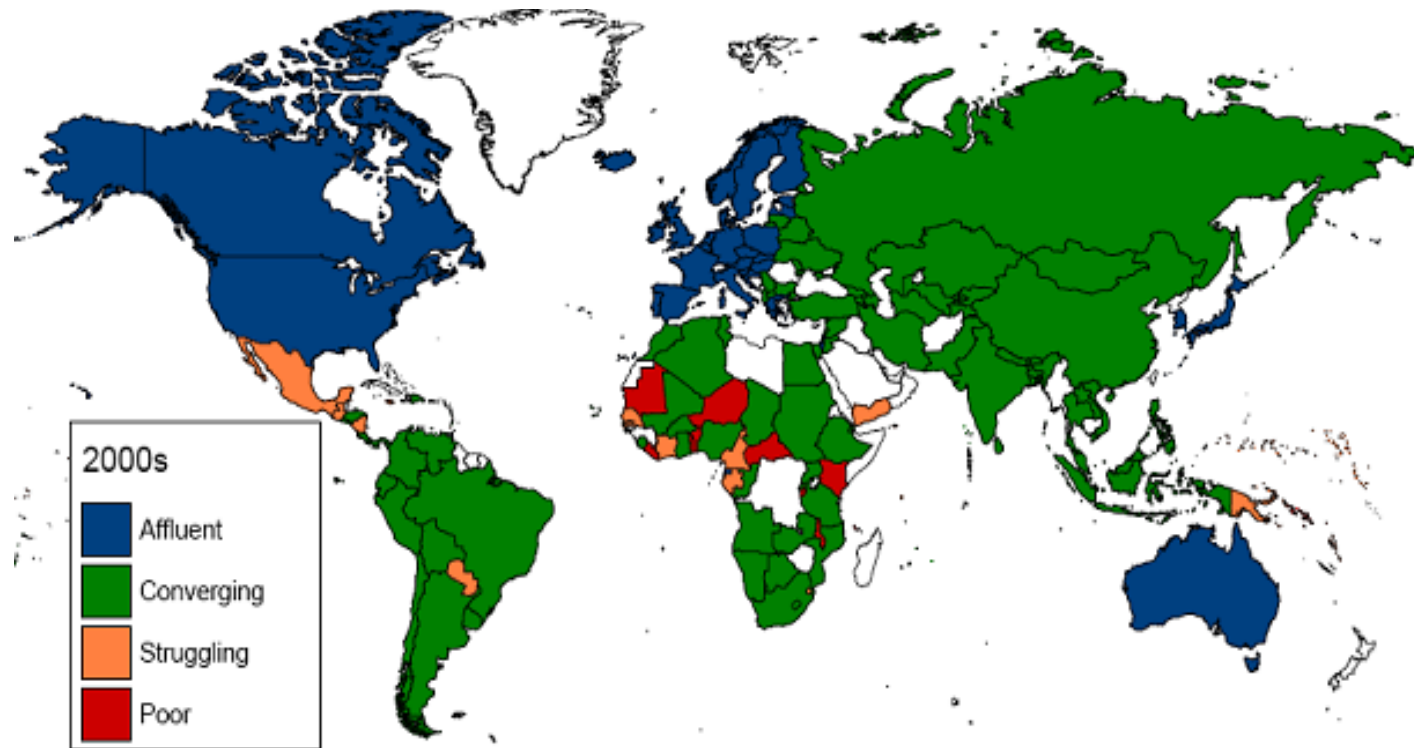
The disappointing reality



Source: OECD Development Centre, *Perspectives on Global Development 2012*

A New Geography of Growth: The Four-speed World in the 2000s

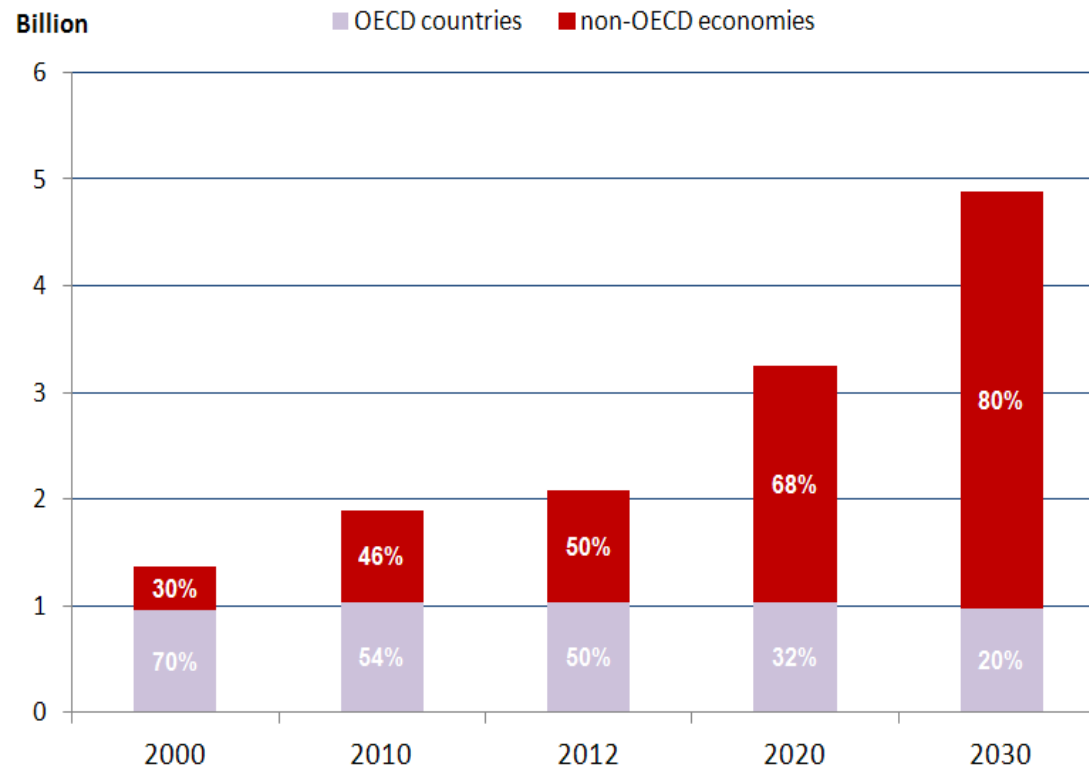
Goodbye divergence, hello convergence?



Source: OECD Development Centre, *Perspectives on Global Development 2012*

The impacts of Shifting Wealth (1): The rise of new “middle classes” and focus on domestic sources of growth

- **By 2030, 80% of the world’s middle classes will be living in developing economies**

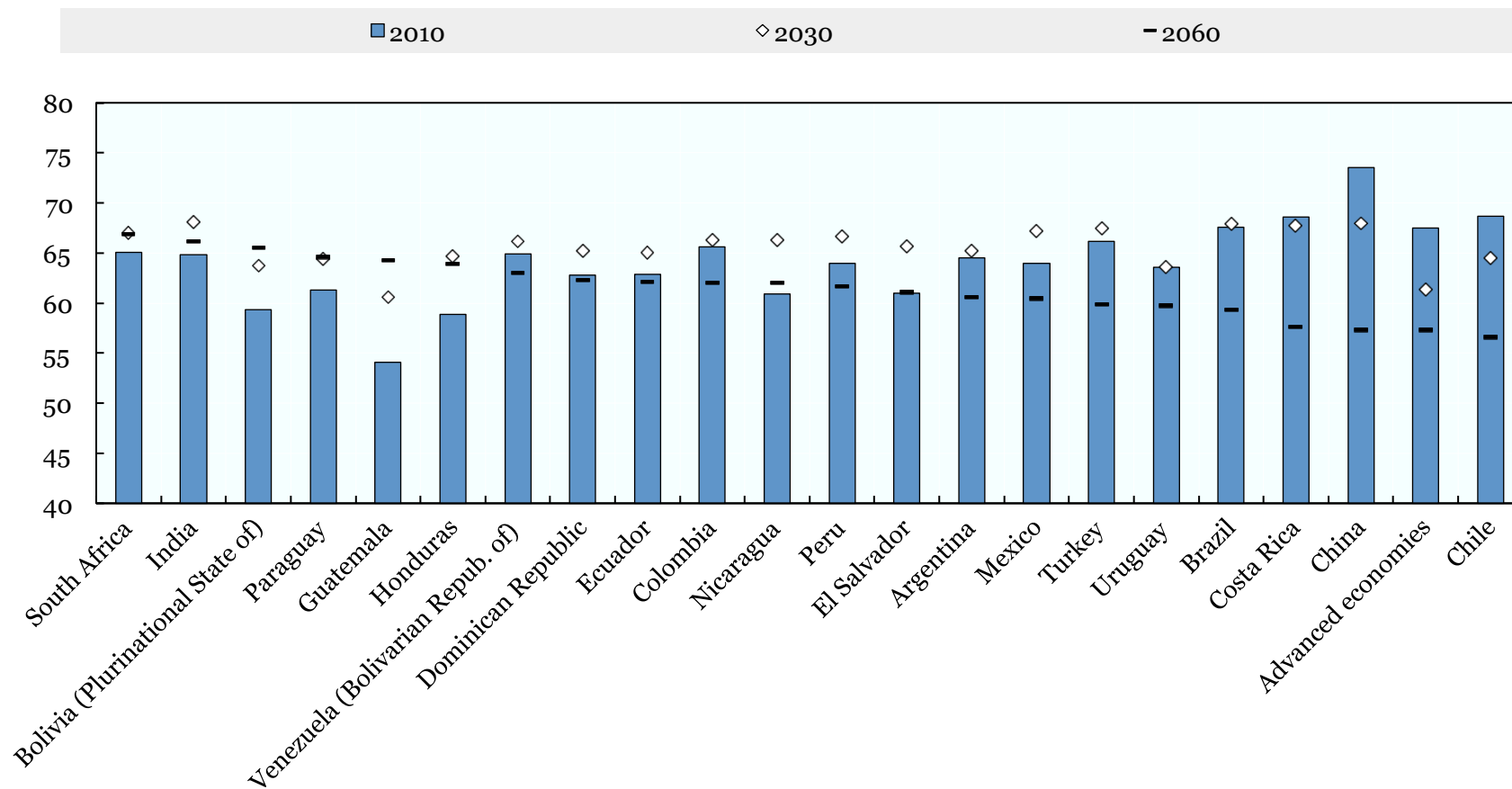


Note: « Middle classes »: People living between 10 and 100 USD PPP a day.

Source: OECD Development Centre based on Kharas (2010).

Demographic trends underpin the continuation of shifting wealth

Active population (percentage of the population of 15- to 64-year olds)



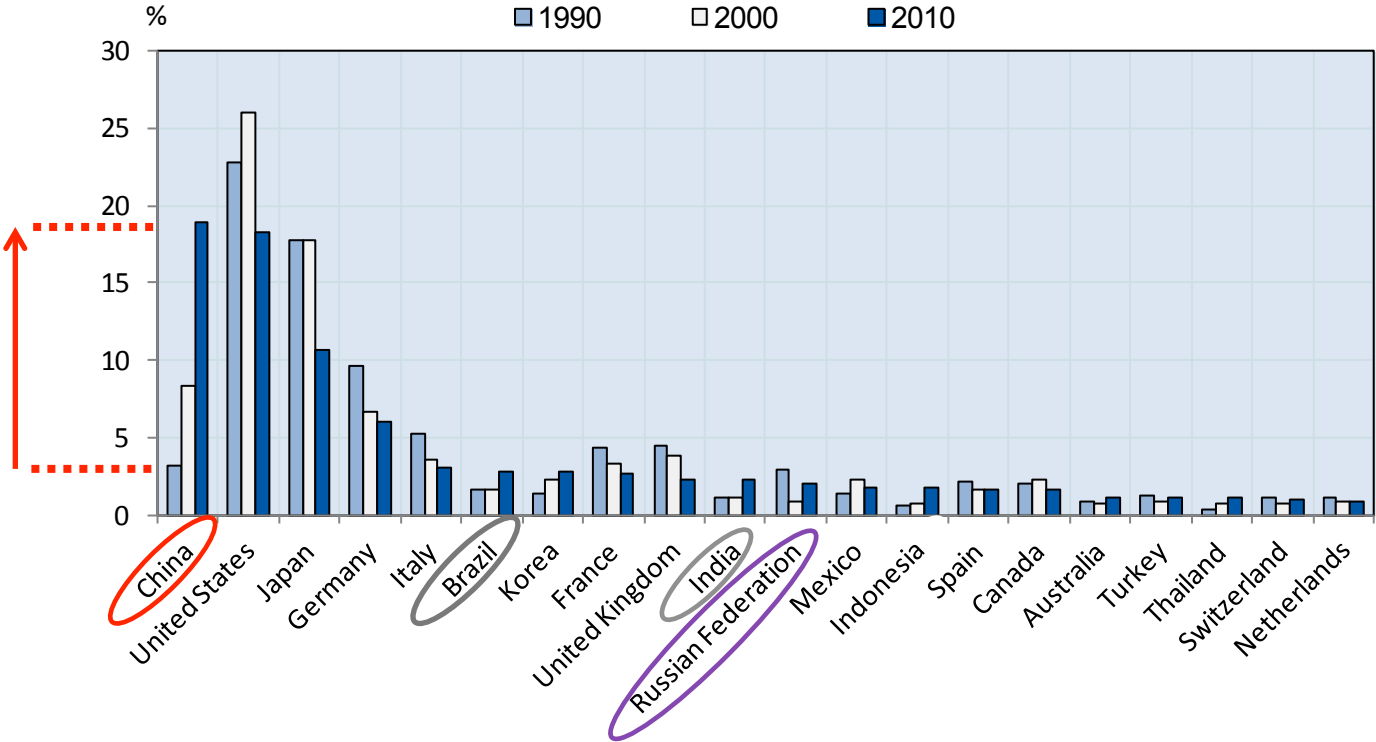
Source: Based on United Nations (World Population Prospects 2012).

The impacts of Shifting Wealth (2): Changing the global geography of production

China is the main driver, but other countries are also contributing

World top 20 manufacturers, 2010

Country share in total world manufacturing value added



Source: OECD (2013), *Perspectives on Global Development 2013 - Shifting up a Gear: Industrial Policies in a Changing World*, OECD, Paris.

Chinas leadership in the different stages of Shifting Wealth

China's development helps to define two phases in the Shifting Wealth process:

1. Shifting Wealth I :China's integration to the global economy → reduction in the world land/labour ratio.

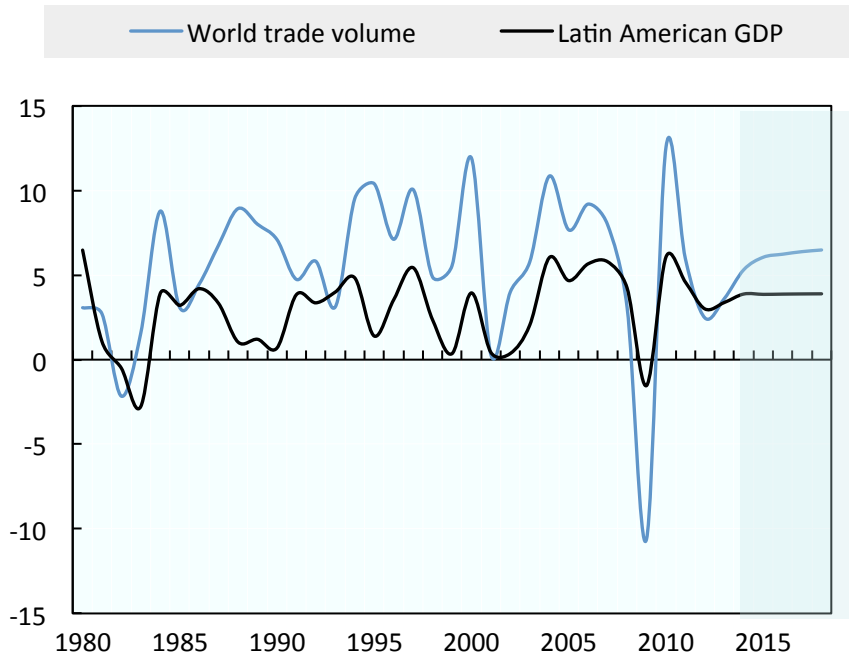
2. Shifting Wealth II

- a. Towards a growth model based on consumption
- b. China's structural transformation

→ Changes in demand patterns, opportunities in commercial specialization

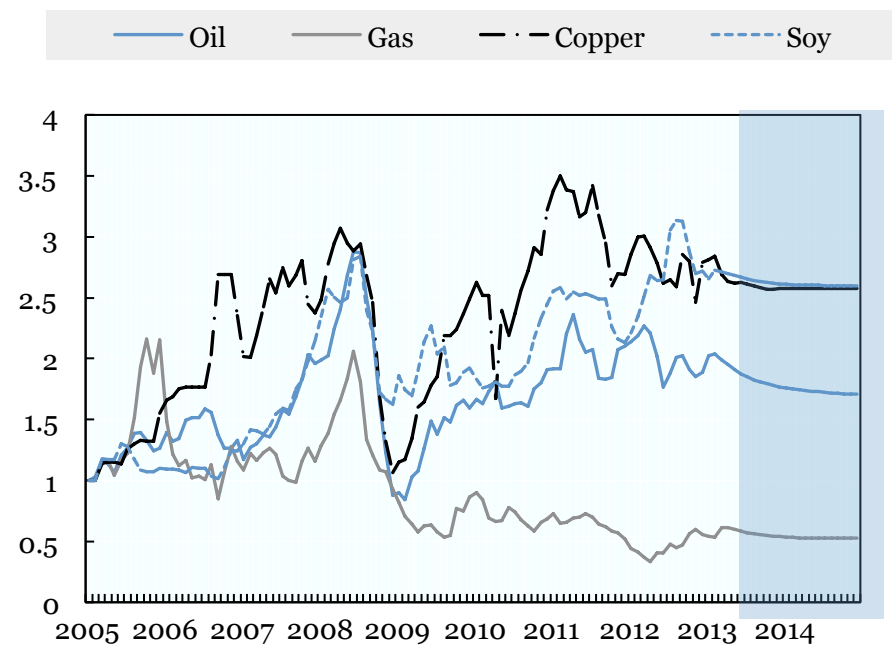
Low global demand impacts Latin America via two ways: the volume of international trade and the price of commodities

Global trade and LAC GDP growth



Source: Based on IMF(2013), World Economic Outlook.

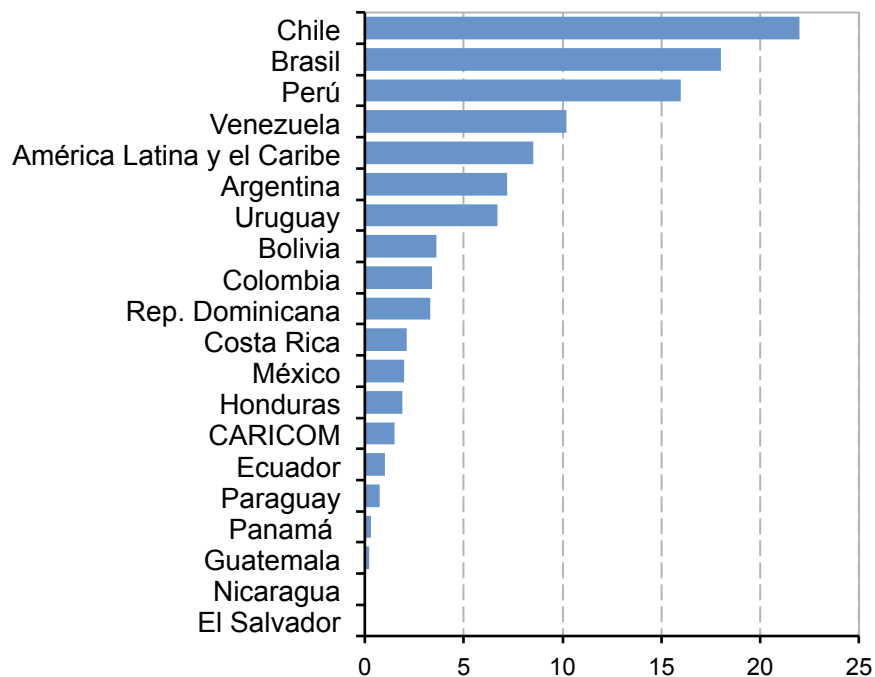
International commodity prices



Source: Authors' calculations based on Datastream and Bloomberg data.

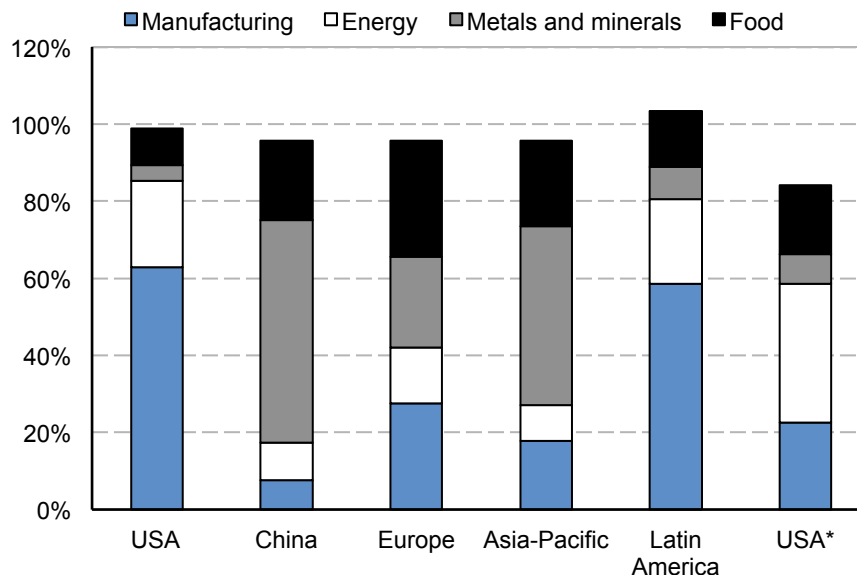
The concentration by product and market are two vulnerabilities that raise concern

Exports of Latin American countries to China (% of total exports)



Source: Based on ECLAC data.

Latin American exports by type and destination



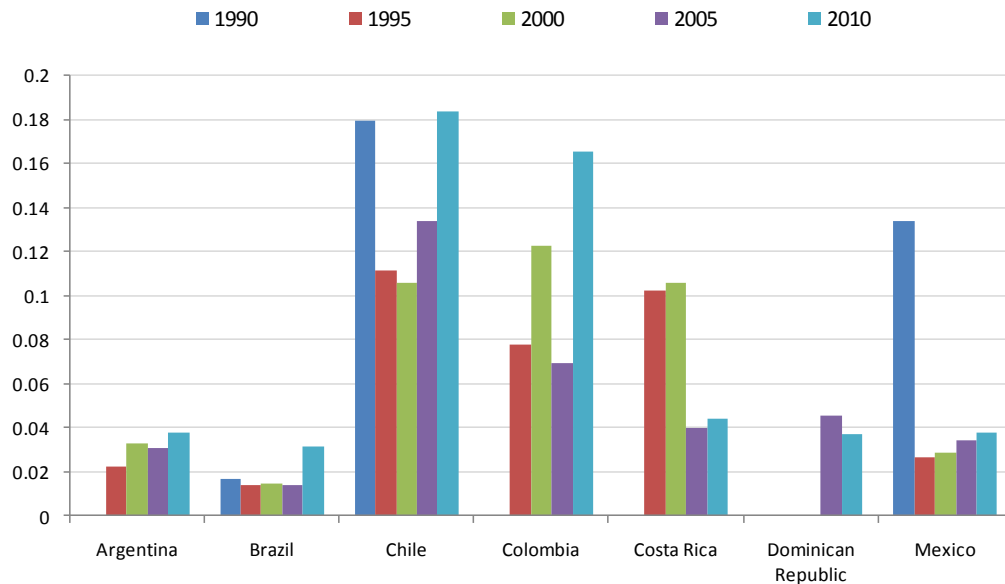
Source: Based on COMTRADE.

* Latin American exports without Mexico

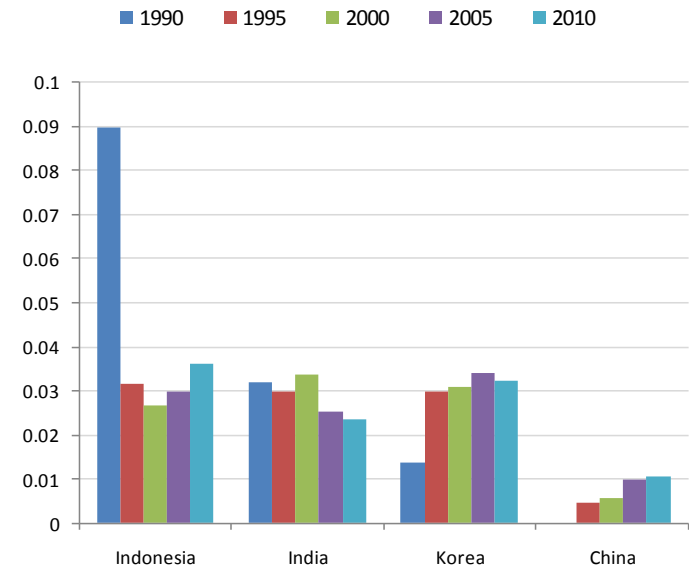
The rise of China still poses the risk of overspecialisation for the region

Herfindahl-Hirschman Index of concentration by Product

Latin America and Caribbean



East Asia

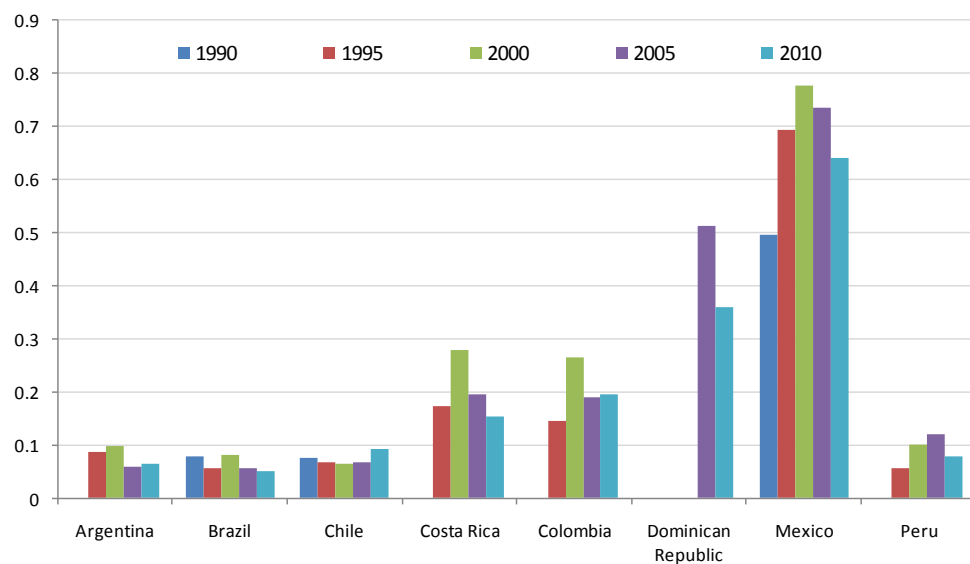


- Note: Herfindahl-Hirschman index estimated as the squared sum of market shares of exports of country i to country j on all 4-digit levels of goods, corrected by the number of exported goods. Nomenclature SITC Revision 3, 2012.

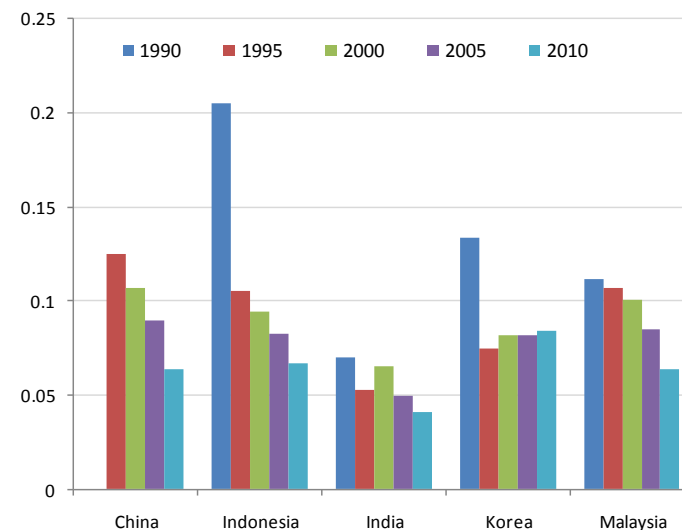
Latam more resilient by diversifying its export destinations

Herfindahl-Hirschman Index of concentration by destination

Latin America and Caribbean



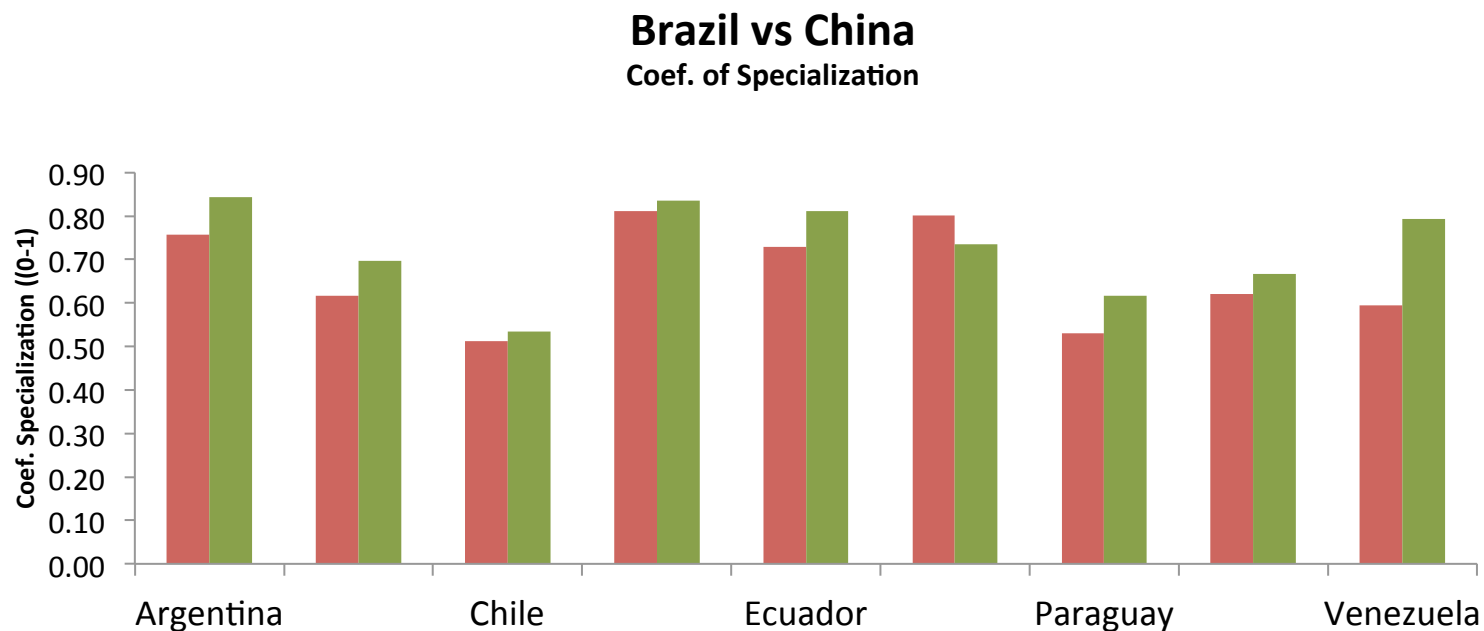
East Asia



- Note: Herfindahl-Hirschman index estimated as the squared sum of market shares of exports of country i to country j on all destinations, corrected by the number of country partners. Nomenclature SITC Revision 3, 2012.

Competition in regional markets has increased

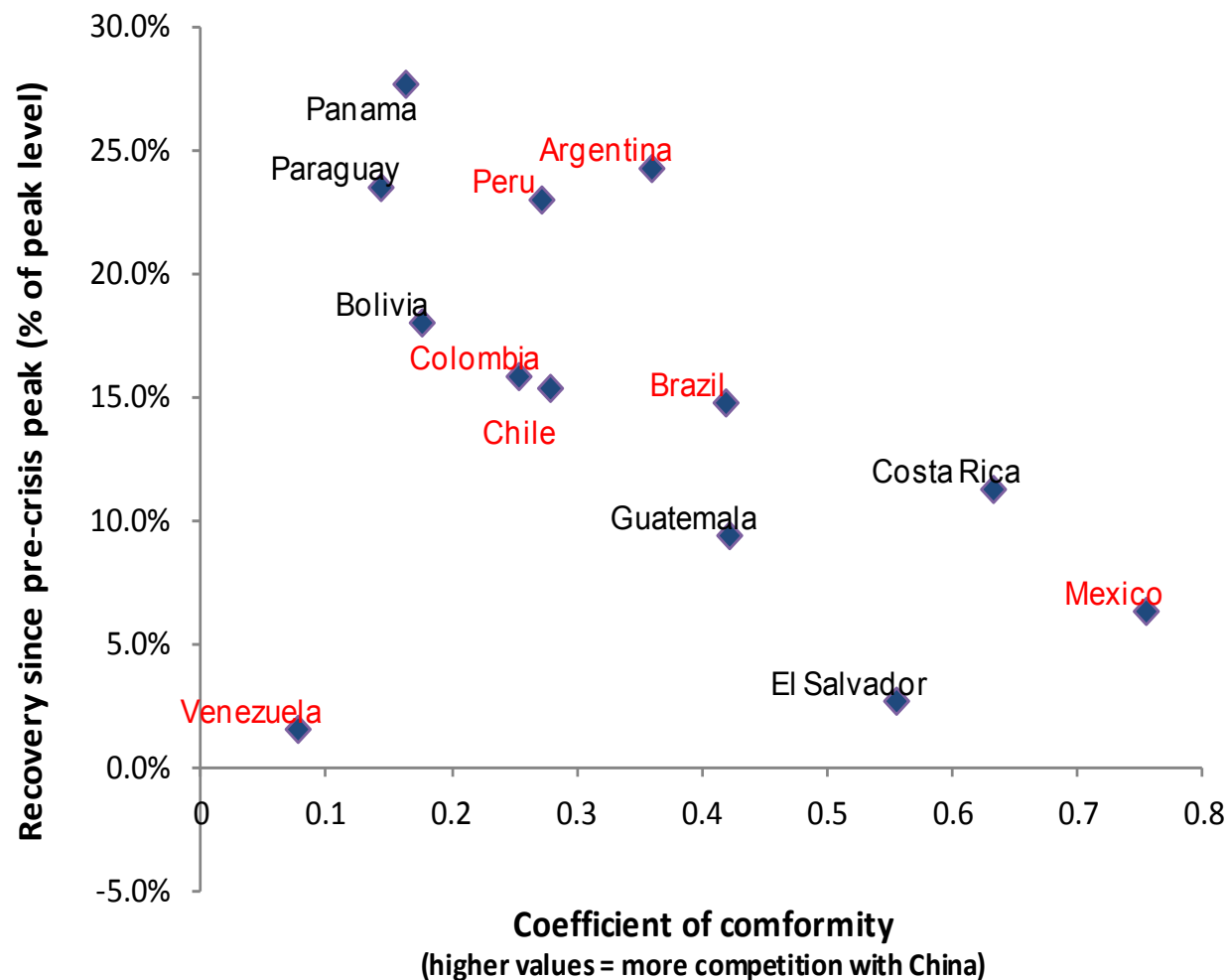
Trade Competition in South America (2000-10)



Note: CS and CC coefficients calculated with exports of country *i* and exports of country *j* to a specific region (in this case Latin America).

Source: OECD Development Centre, based on WITS Database, 2012.

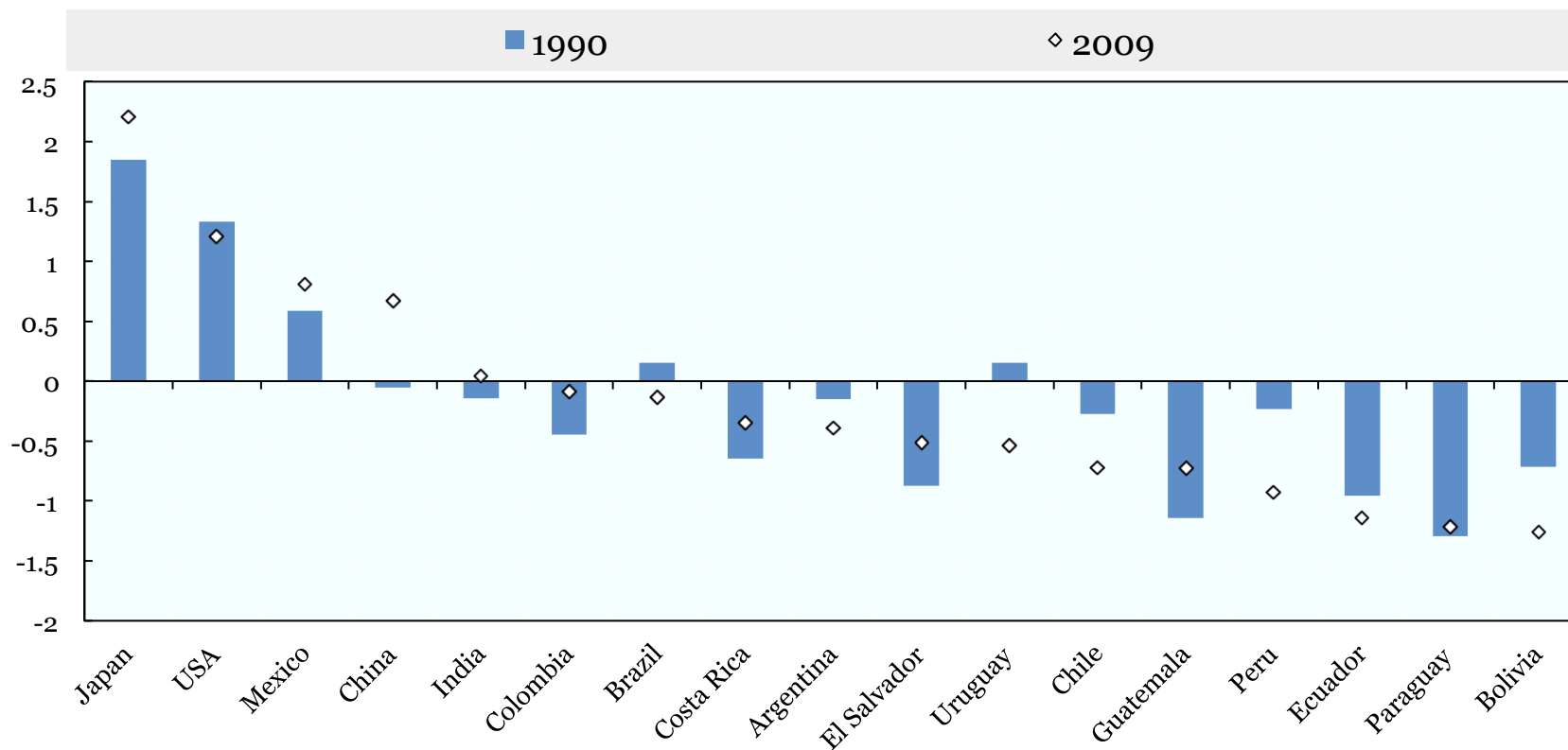
Recovery after 2008 crisis: A strong link between speed of recovery and links to China



Source: OECD development Centre, 2012.

The region has advanced little in structural change and capabilities

Productive capabilities indicator (1990 vs 2009)



Note: Productive capabilities index (Appendix 2.A2). Higher values in the variable let a country produce a more sophisticated range of goods. At any given moment, the capacity variable depends on the level of connectivity of the network of products, which is why it is normalised. Thus a value equal to the worldwide average. A value of 1 (-1) indicates capabilities one standard deviation above (below) that average.

Source: Authors' calculations based on data from COMTRADE and Feenstra, R. C., R. E. Lipsey, H. Deng, A. C. Ma y H. Mo (2005), "World Trade 1962-2000", NBER Working Paper N° 11040.

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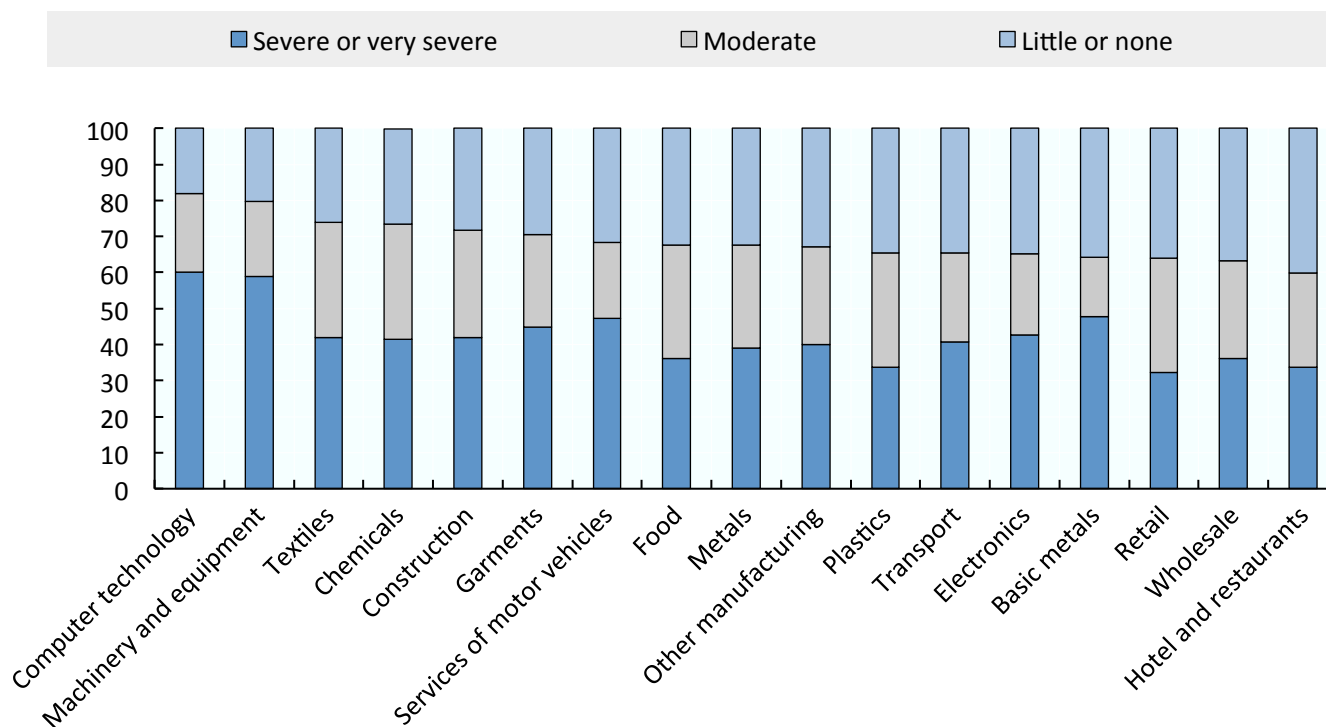
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Human capital: connecting the production sector with the educational system

Difficulty encountered by Latin American SMEs in finding skilled labour, by sector and level of difficulty, 2010
(as percentages)



Source: Based on data from the World Bank Enterprise Surveys.

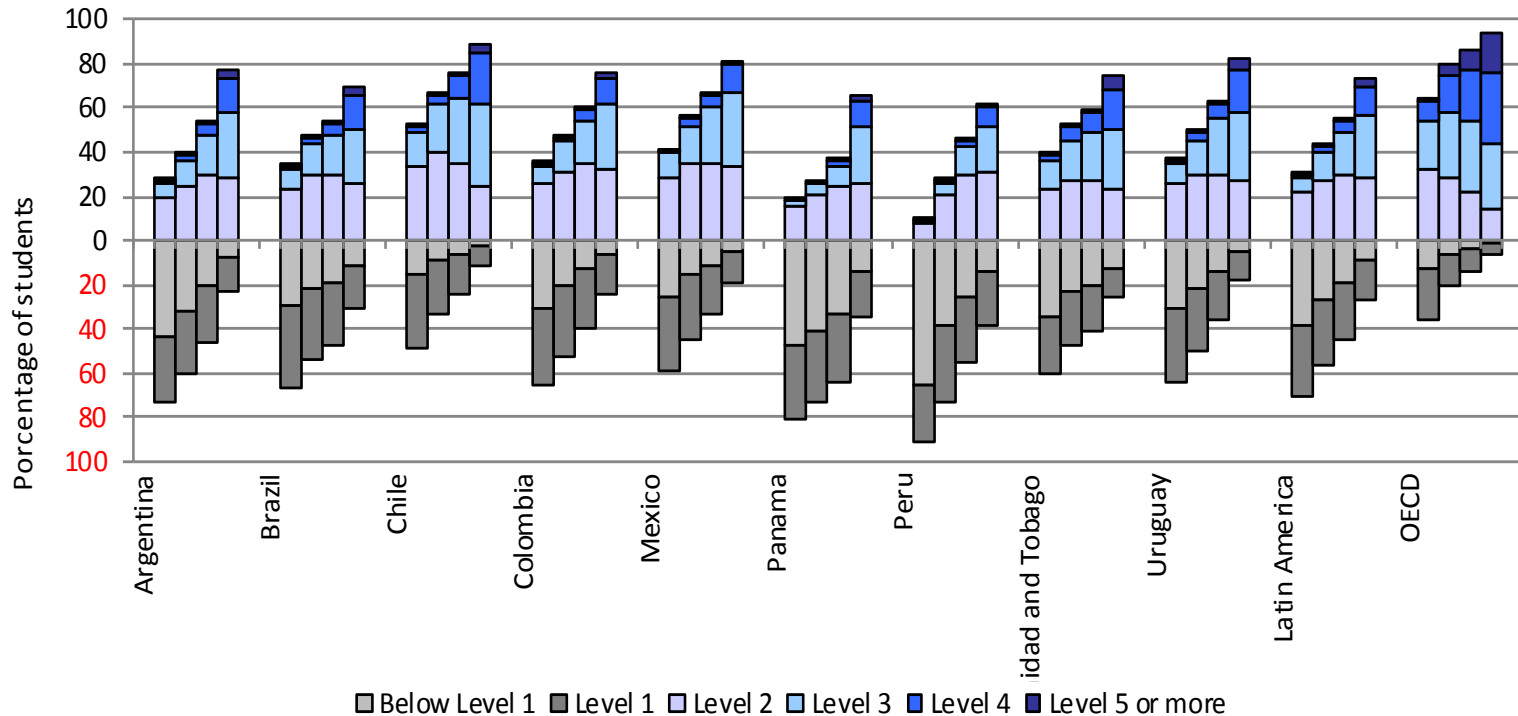
PISA: LAC performs consistently below average in all measures

- For all three areas, Latin American countries are in the lower third of the ranking, which includes a total of 65 countries.
- Within the region, Chile is the best positioned and Peru is the worst.
- **Position of Latin American countries in PISA tests rankings (out of 65 countries)**

Country	Math	Reading	Science
Argentina	59	61	58
Brasil	58	55	59
Chile	51	47	46
Colombia	62	57	60
Costa Rica	56	49	51
México	53	52	55
Perú	65	65	65
Uruguay	55	54	54

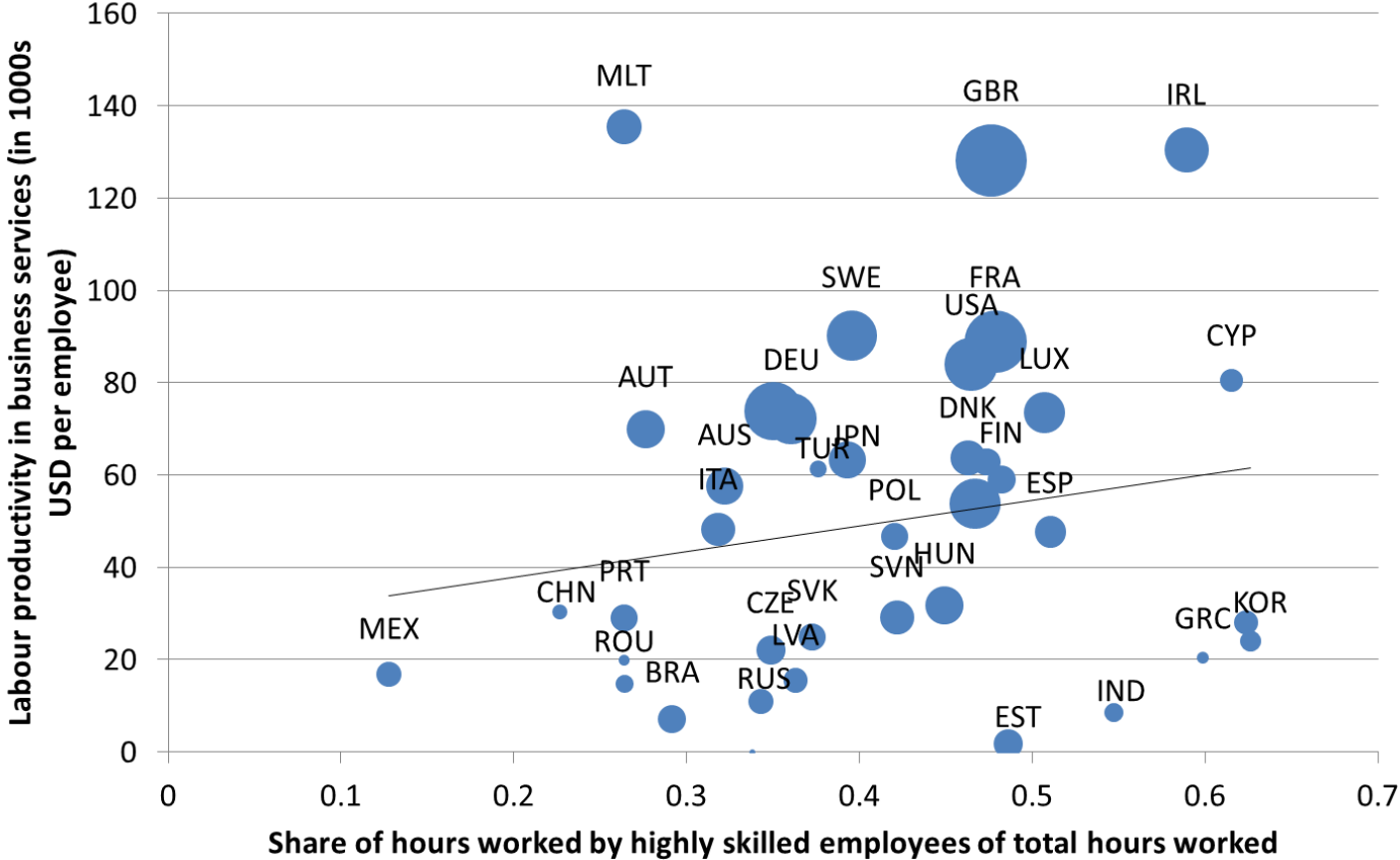
PISA: Income inequality influences school performance

- Latin America and the Caribbean (9 countries) and OECD average: distribution of test score in PISA reading tests, by socioeconomic and cultural household background quartiles



- PISA test results of secondary students distributed by income quartiles show that most students in the first and second quartiles (that is, from the poorest households) perform below level 2.
- This confirms the importance of the socio-economic status in generating differences in education outcomes.

An example: Skills matter for productivity in business services

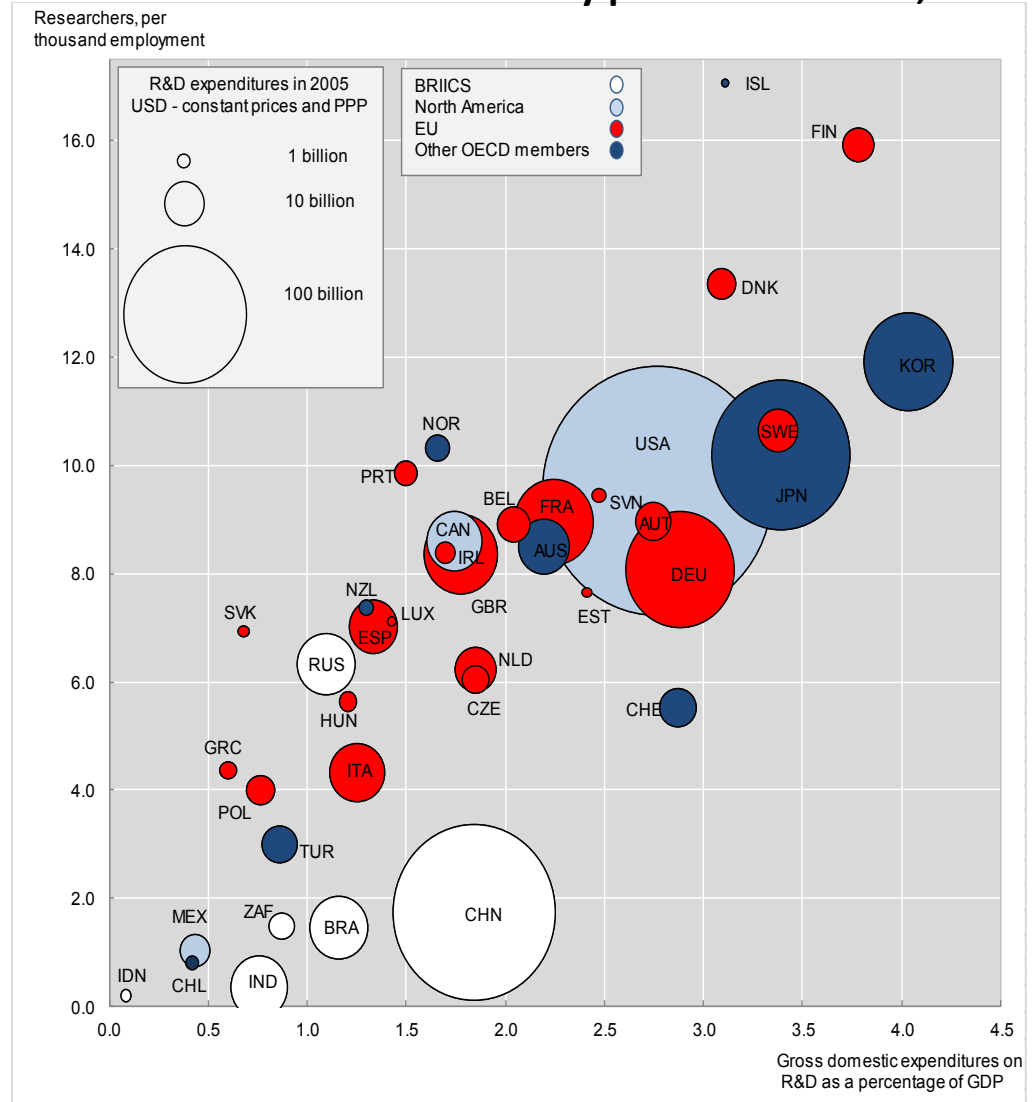


Reference year: 2007

OECD STI Scoreboard 2013: large gap of LAC against OECD and China

- Latin America maintains a marginal position in the R&D landscape
- China has made a remarkable progress on the three indicators (R&D expenditures, both in constant USD and as a share of GDP, and in the number of researchers in employment), surpassing Latin American countries in a relatively short period of time.

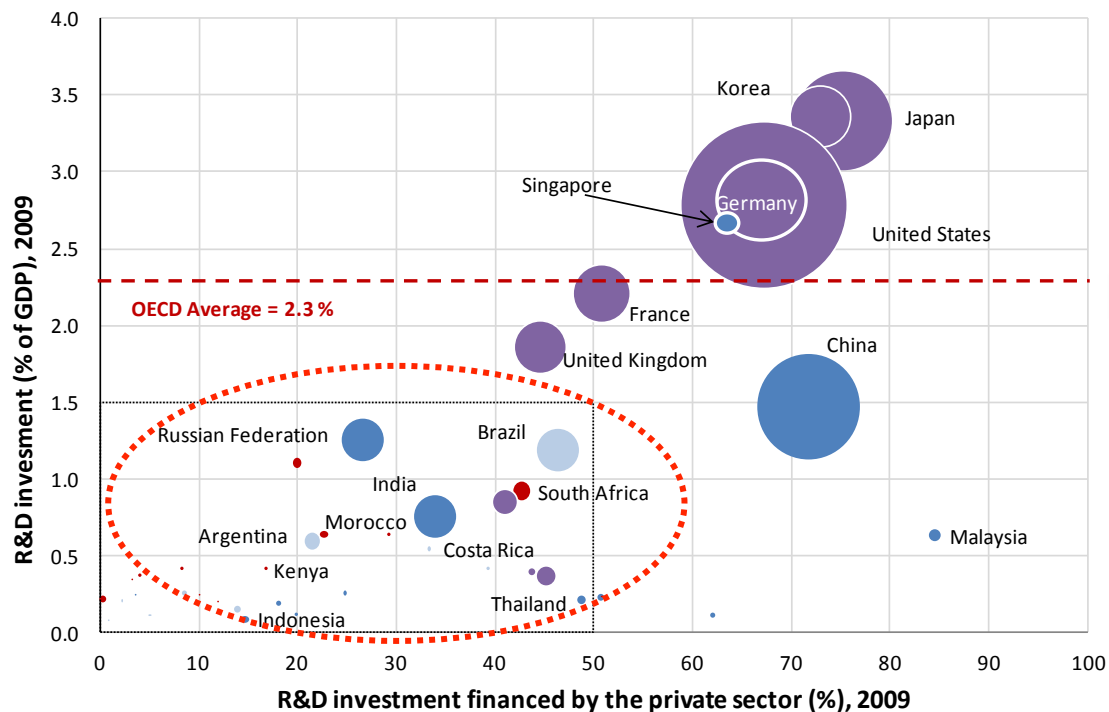
R&D in OECD and key partner countries, 2011



Latin America still faces big challenges. However, some are implementing targeted policies to address them.

- Although developing countries are increasing their production and innovation capabilities, they are still far from the OECD average

Intensity in R&D investment and private sector contribution, 2009

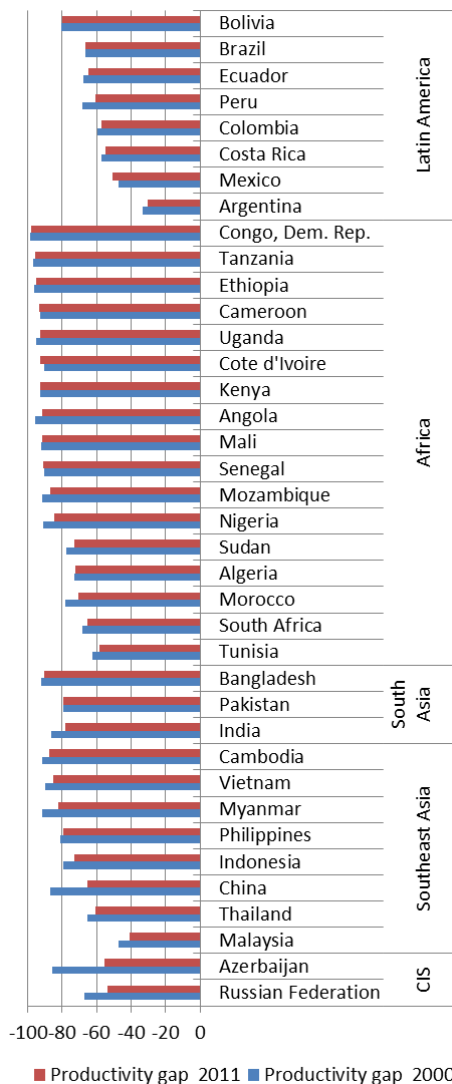


- Targeting resources to specific scientific and technological areas (new materials, biotechnology and clean energy vehicles; healthcare, etc.).
- Public procurement for innovation (e.g. Brazil, China, India and South Africa)
- Attracting more knowledge-intensive FDI (e.g. Brazil, Costa Rica, Malaysia, Morocco)
- Promoting start-ups (Brazil, Colombia, Peru)
- Promoting cluster development (e.g. Brazil, Chile, India)

Boosting productivity to avoid the middle-income trap

- The middle-income trap is characterised by a slowdown in growth due to difficulties of moving from a factor accumulation-based to an innovation-based growth path, which in turn is related to low productivity levels and insufficient productivity growth.
- >> Productivity and efficiency are compared across middle-income countries and benchmarked against more advanced countries.
- >> Different factors determining productivity and efficiency (including skills availability and intensity) are studied to identify key development challenges in middle-income countries.
- >> In depth analysis at the firm-level is done for the BRIICS and other emerging economies, including Colombia

Gap relative to OECD in GDP per person employed



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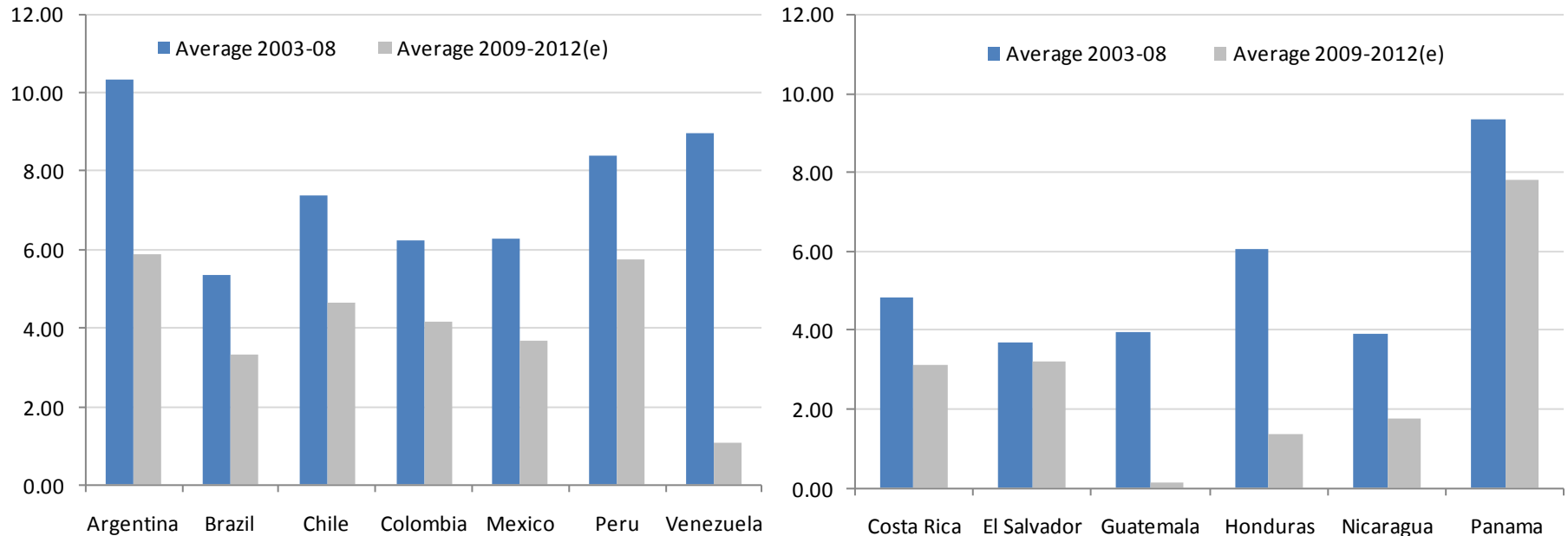
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Central America's growth: lower than LAC-7 but sustained, despite the crisis

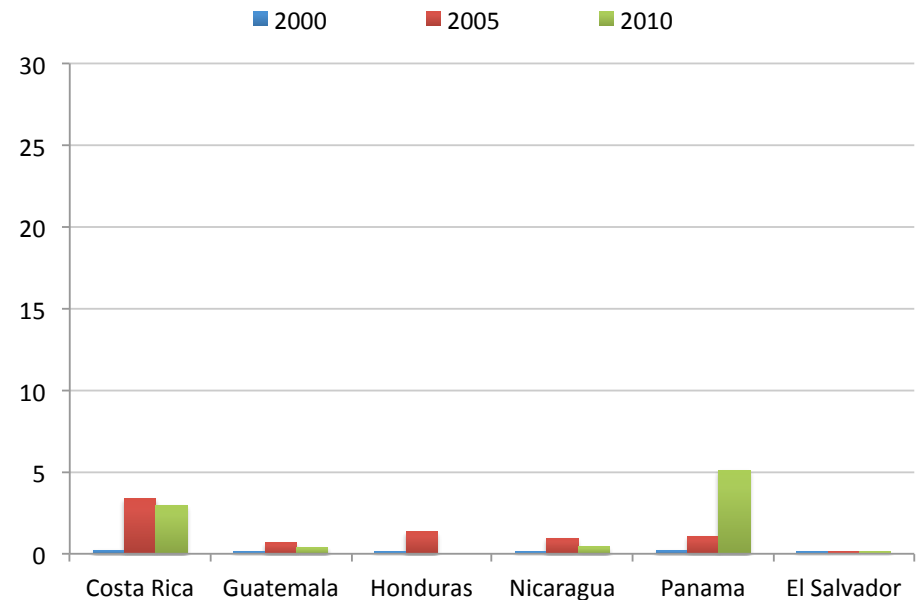
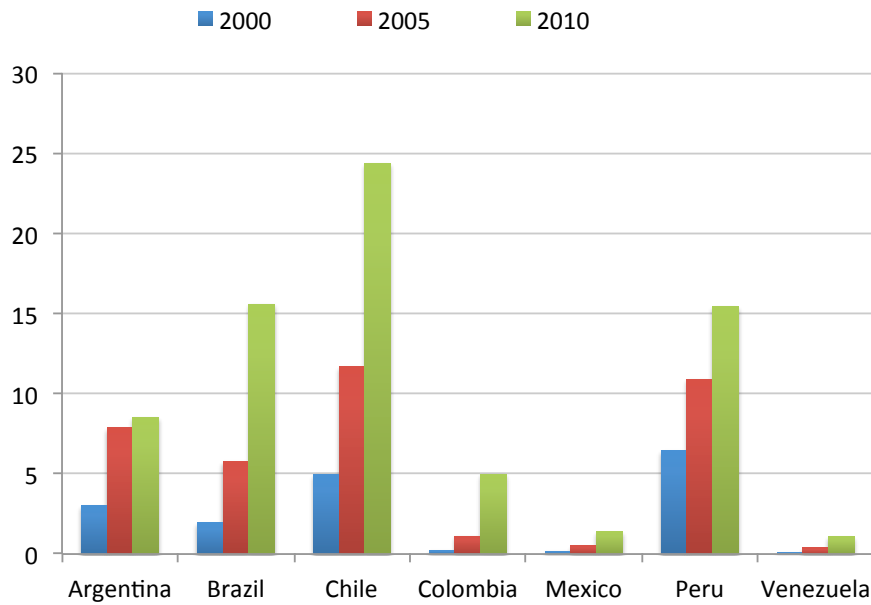
Average Rate of per Capita GDP growth 2003-2008 and 2009-2012 (e)



Source: Based on National accounts, 2012.

Central America's link with China: it has increased, but extremely low compared to other LAC countries

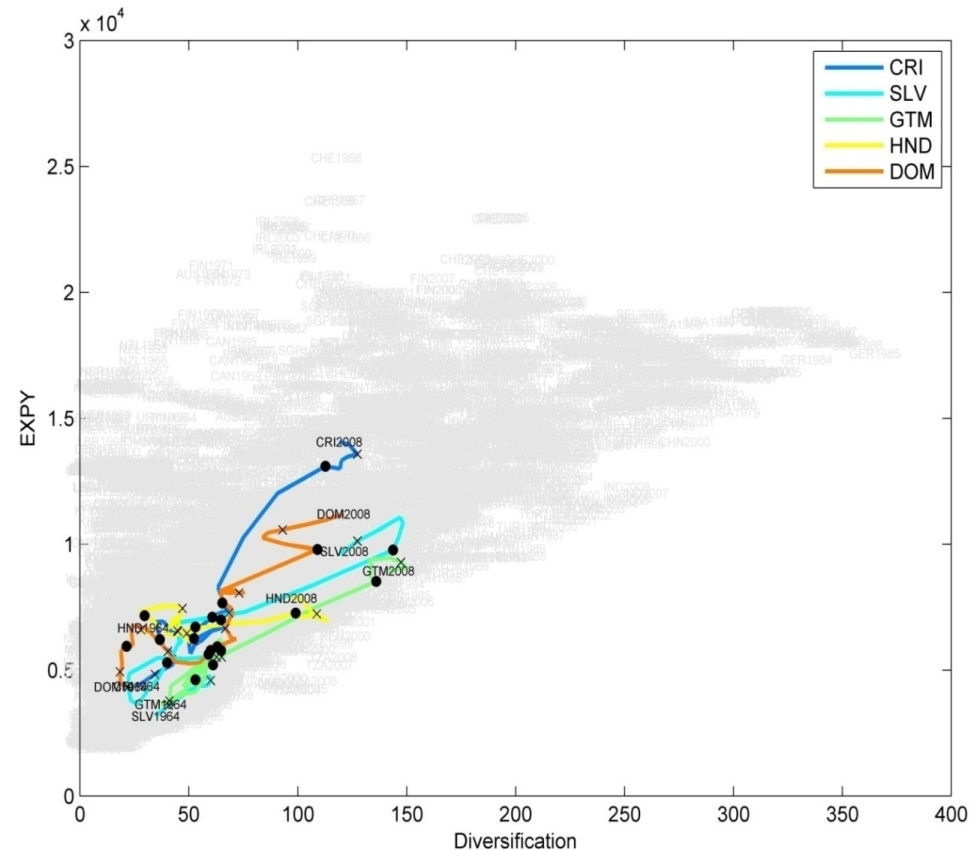
Share of Exports to China as % of total exports 2000-2010



Source: UN Comtrade, 2012.

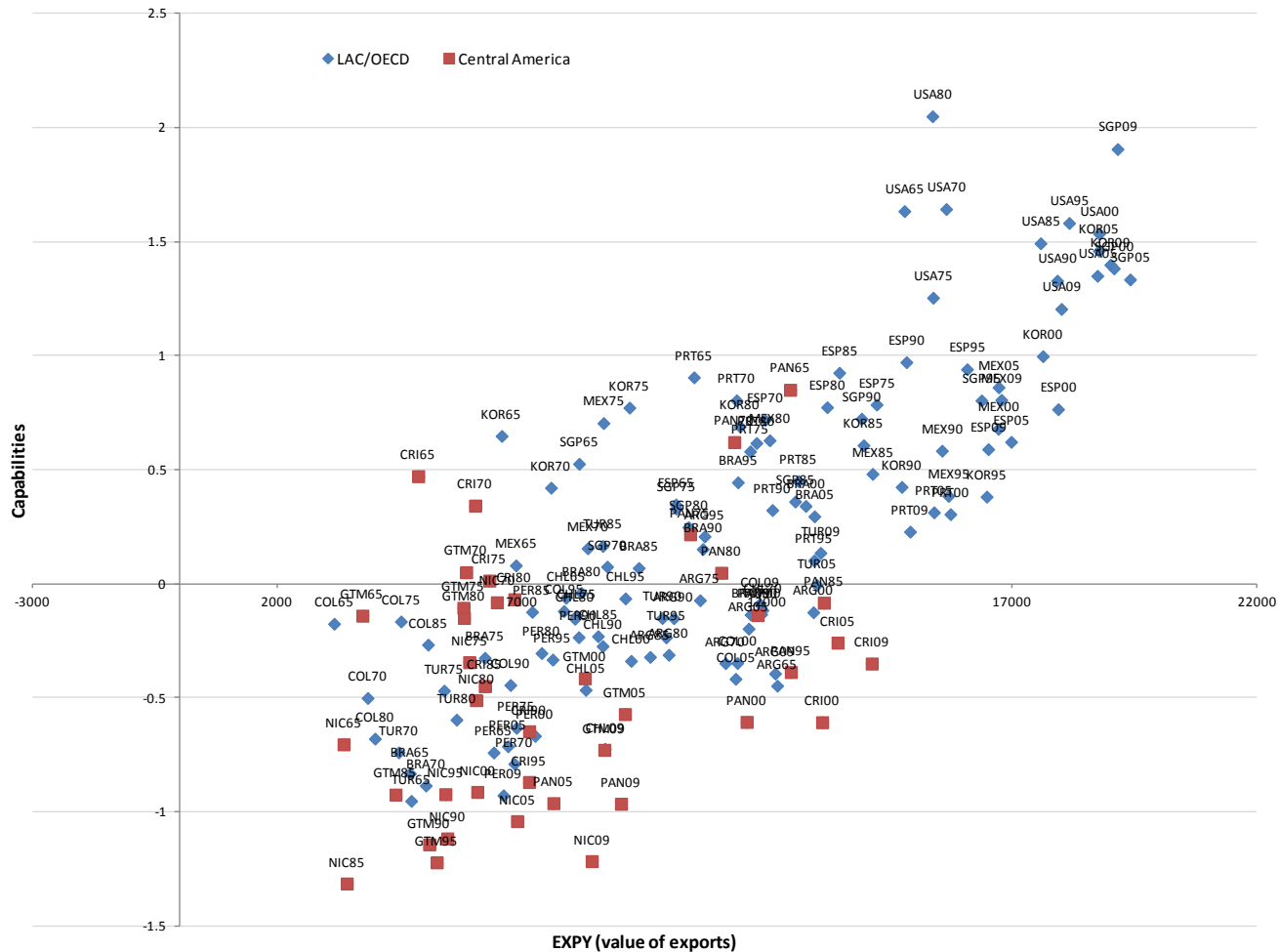
Diversification vs Upgrading: Latin America

➤ Central America follows a roughly similar pattern, with CRI reaching a higher stage in product sophistication.



Source: Jankowska, A. Nagengast, A., Perea, J.R. "The Product Space and the Middle Income trap: Comparing Asia and Latin American Experiences. OECD Development Centre Working Paper No. 311.

Export sophistication and capabilities, various countries, 1965-2009



Source: Jankowska et al. 2012.

China in Central America: growing links

China's engagement in Costa Rica:

- China and Taiwan have historically competed for allies in Central America.
- Costa Rica. Less obvious agreement. Modest economic ties with China
- June 2007. Announcement of agreement with China

China and Strategic Sectors in Central America

- Entrance of China in Telecommunication markets (Huawei, ZTE) in Costa Rica, Panama (even if doesn't recognize PRC), Honduras (through Hondutel) and Guatemala (ZTE)
- Competition of China in Central American markets?

China's influence and infrastructure "hubs"

- Other possible areas of influence: Honduras inter-oceanic canal, Nicaragua. A competition among Central American to become "hubs"

A Glance at China-Latin America

- Central America's growth has been steady, even after the crisis
- A high dependence on exports, compared to other LAC countries
- Exports to China have marginally increased, but remain very low. High dependence on U.S. demand
- The middle income trap in Latin America: not really for Central American countries (all lower-income except for Costa Rica)
- Product specialisation due to China's demand is less pronounced than LAC-7. A strength?
- What options for Central America?

Concluding Remarks

Shifting Wealth is an established phenomenon with sustained effects, and Latin America needs to position in it.

LATAM resilience: countries have built more buffers. Financial and trade openness have increased exposure to external shocks.

Adaption strategies to Chinese competition are heterogeneous, depending on the sector and firms and country capabilities.

Overcoming the “middle income trap” that Latin America is facing requires active public policies in education and skills.

Breaking away from the middle income trap has, almost always, encompassed an upgrading of the export base towards manufacturing.

China and Central America. Too little, too late?

Thank you!
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Structural challenges and production transformation strategies: commonalities and differences

Key features of industrial policies			
GOVERNANCE	<p>TOP-DOWN (Low margin of maneuver of regional/local governments); ex. Chile.</p>		
	<p>MIXED (Coexistence of national and regional/local initiatives); ex. China, Brazil.</p>		
	<p>BOTTOM-UP (High margin of maneuver and responsibilities of regional/local governments); ex. India.</p>		
PRIORITIES	<p>TRADITIONAL</p>		
	<p>EMERGING</p>		
	<p>Growth Job creation International competitiveness</p> <hr/> <p>Territorial inclusion and competitiveness Social cohesion Sustainable development</p>		
OBJECTIVES	<p>Diversification (<i>i.e.</i> entry in new sectors/types of activities)</p> <p>Specialisation and upgrading (<i>i.e.</i> scaling up in local and/or global value chains)</p> <p>Increasing the density of the production system (<i>i.e.</i> entrepreneurship, linkages, networks)</p>		
POLICY MIX	<table border="0"> <tr> <td> <p>Industrial policy tools (<i>i.e.</i> direct and indirect incentives to firms)</p> <p>Trade policy and FDI</p> <p>Support to science and technology</p> <p>Skills development</p> </td> <td> <p>Infrastructure building and upgrading</p> <p>Financing (<i>i.e.</i> development banks)</p> <p>Macroeconomic policy (<i>i.e.</i> exchange and interest rate management)</p> <p>Competition policy</p> </td> </tr> </table>	<p>Industrial policy tools (<i>i.e.</i> direct and indirect incentives to firms)</p> <p>Trade policy and FDI</p> <p>Support to science and technology</p> <p>Skills development</p>	<p>Infrastructure building and upgrading</p> <p>Financing (<i>i.e.</i> development banks)</p> <p>Macroeconomic policy (<i>i.e.</i> exchange and interest rate management)</p> <p>Competition policy</p>
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Service development (often related to manufacturing) might be a way to achieve more product sophistication and increase value added retention

Latin America: Value added of service activities, 2009 (as a percentage of total export value)

