REGIONAL ADVANTAGE

IT'S ALL ABOUT INTEGRATION

Interview with Rolando Avendaño, OECD specialist for China and Latin America relations.

By Ellen Thalman / Photography by Kai Jünemann

Does every industry have its China – in other words does every industry have an emerging-market country that you could identify as a boom country?
Many of the big emerging-markets companies are in commodities, that is, raw materials, which is an important difference to China, where manufacturing is at the core of growth. In Latin America and Africa, the countries with the highest growth rates are commodity exporters. So we are in a very specific context where high commodity prices are bolstering growth of these countries. There has been a lot of discussion about which will be the next countries after China and India. If you look at what the literature says today – Bangladesh, Egypt, Mexico, Iraq, etc. – these countries don't have the same size effect of China and India in terms of demand and production. But they are improving their integration in world markets.

Is the pace of regional integration accelerating in other parts of the world besides Asia?
Regional integration has increased not only in Asia, but also in Latin America. Also, some investment is going from south to north. For example, companies like CEMEX from Mexico, VALE (previously known as CVRD) from Brazil and Tata from India are investing in industrialized countries to increase their market share. While these industries are very closely related to commodities, there are some other cases, like Embraer in Brazil. They are gaining a lot of market share in the small-plane sector, which is an added-value sector that requires a lot of investment in research and development.

What is the impact of this regional integration and south-north investment?
China's investment in Latin America has increased dramatically, mainly to gain easier access to raw materials. In Africa they are investing in infrastructure. But partnerships are also developing. In Latin America there are a number of joint ventures. For instance, Bematech, which is an IT hardware and software company in Brazil, and Nemak, which is a Mexican automotive parts company, have started to work more closely with China. Instead of competing in their own sectors, they have started to work together. Corona, a Colombian company, is integrating Chinese home-building-product makers into their production chain. Still, this is not a typical case given that China is a big importer of commodities, and one of the dangers that emerging countries are having now is that they over-specialize in raw commodities production, which could be dangerous in future.

What are some of the pitfalls high-growth countries are facing?
There is an increasing specialization phenomenon. Commodity exporters tend to overlook the development of other sectors, and there is a negative effect for the economy. The OECD Development Centre calculates a concentration index, the Herfindahl-Hirschman, for emerging regions – Africa and Latin America – and what we observe is an increasing specialization by product in these regions. This means that they depend more and more on very few sectors. This is much more dramatic in Africa, particularly in hard-commodity exporters – oil, gas, copper. In this sense, economic growth should be combined with diversification policies.

How can governments engage on the policy side to help to manage a boom?
The big commodity boom we are seeing right now is produced by demand from Asian countries. However, government policies can influence booms. One of the channels is regulation – not necessarily more, but better regulation in some sectors. A good example is in Latin America, where countries have modernized their telecommunications infrastructure. Public efforts to ensure contestable markets and competition in this sector have been crucial. Governments can also help capital formation. In China, the government plays a big role in increasing financial deepening and access to capital for small and medium-sized companies. That could be very important for Latin America, where 80 percent of companies are in this category. The third channel is innovation and R&D, which is at the core of the growth process.

What are some examples of countries that are getting it right? What are these governments doing that makes them exemplary?
Getting it right can mean many things. For example, Angola has an amazing growth rate of around 20 percent, but they have this diversification problem. Those that are doing it right have stable macroeconomic policies and want economic diversification. For example, Brazil passed from a very chaotic decade of macroeconomic mismanagement to one of inflation targeting and stable monetary policy. It is also a very diversified economy, even though Brazil is one of the biggest producers of sugar cane, which is used for biofuels and has gained public attention these days. Also, there has always been the question of whether growth means sacrificing the redistribution of wealth. There is a famous World Bank study showing that growth doesn't necessarily mean more inequality. Some east Asian economies show this trend, where they have high growth and improved wealth distribution. In some places in Latin America, this seems to be the opposite case, where you not only have lower growth, but really high inequalities. Traditionally, fiscal policy should play this redistributive role, through effective and quality spending on public goods. This has not been the case, unfortunately, for many emerging economies.

Looking into your crystal ball, where do you see growing markets picking up the pace and becoming new boom regions?
The high soft- and hard-commodity prices are not going down soon. Many countries will consolidate their positions in the next few years; for example, Chile, which is one of the biggest copper providers for China, and Mexico, which has recently been exporting oil, and also African countries like Nigeria, Algeria, Zambia, which are big commodity producers. Maybe they can play a role in the next few years, but that doesn't mean they will establish a consolidated economy. Much depends on what they do with the revenues. Many of these countries have established so-called sovereign wealth funds. These funds are increasingly important in the emerging regions, and people are curious to see what will happen with all the money countries are amassing. The next step will be how to consolidate and how to diversify the economy and what strategies they use.

What role can foreign direct investment (FDI) play in helping emerging economies establish the kind of balance you say is needed to create a stable economy?
It has to be a very productive investment. There should be a transfer of technology, or know-how, and these kinds of spillover effects for the recipient. FDI has been regarded many times in different ways. Thirty years ago it was considered a threat for countries, which felt wealth was leaving their country. But today it is synonymous with financial and trade integration. The quality of FDI is very important. It's not only a matter of attracting all the FDI in the world, but also attracting the right kind of FDI for the sectors they want to develop long-term. Countries should target underdeveloped sectors. This is the case in Chile where they developed their fishing and wine industries, instead of only the copper sector. Chile's economy is now less dependent on copper. The government has to be more strategic in targeting foreign investors. ■

Rolando Avendaño is chief researcher at the OECD Development Centre, Paris, working on issues of development finance and Asia's impact on emerging economies. He is a specialist on China and Latin America. He holds a master's in international economics and economic policy analysis from the Paris School of Economics, and is Ph.D. candidate from the same institution. He has previously worked for the OECD Economics Department, and the Institute of Latin American Studies, University College London.