Brazil, China deals challenge US position in Latin America

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6 June 2009

Brazilian President Luiz Inácio Lula da Silva's high-profile visit to Beijing last month deserves close examination for the light it sheds on the geo-strategic shifts taking place in the shadow of the deepening capitalist crisis. The defiant tone of the speeches, the ambitious agenda for long-term collaboration and the breadth and scope of the 13 bilateral agreements signed say a good deal about the enormous vacuum in world affairs left by a weakened United States tied down in two wars and desperately struggling to resolve its own colossal financial and industrial catastrophe.

As the present crisis has unfolded it has become apparent that Washington has simply run out of resources to maintain the tight control it once exercised over Latin America.

The economic agreements signed between China and Brazil and the joint pledge for long-term bilateral collaboration have global significance.

The fastest growing economy in the world, China ranks third in terms of GDP with $4.4 trillion, according to the IMF. China's growth is on course to overcome Japan's (second largest GDP in the world with $4.9 trillion) within the next two to three years. Furthermore, economists estimate that given China's growth, it can catch up to the US in the next quarter of a century (US statistics: $14.3 trillion GDP or 25 percent of world GDP, down from nearly 50 percent in the 1950s).

Brazil's $1.6 trillion GDP makes it the world's 10th most powerful economy and by far the largest in Latin America. It is followed by Mexico, with $1.1 trillion in GDP, and more distantly by Argentina, with $326 billion.

While Brazil was an importer of oil a few decades ago, today foreign capital anxiously competes for a piece of the $174 billion investment required to exploit the newly discovered offshore oil fields in the Santos basin off the Brazilian coast—the largest field discovered in the Americas since Mexico's Cantarell in 1976. So powerful has Brazil's presence in the energy sector become that its state-owned oil company, Petrobras, aspires to become one of the five largest integrated energy companies in the world.

Brazil is a major exporter of manufactured goods, engineering and technology to Latin America and Africa. Through Mercosur (a free-trade agreement between four neighboring countries in Latin America's Southern Cone) Brazil dominates trade with Argentina, Uruguay and Paraguay. Furthermore, Brazil has strong economic ties with the nationalist regimes of Venezuela and Bolivia, though Lula maintains his distance from the left-nationalist rhetoric employed by presidents Hugo Chávez and Evo Morales.

Economic giants in their own right, China and Brazil now turn to each other to protect their future from the impact of the US recession, as their economies have been largely dependent on exports to America. In October 2007 China ranked as its second-largest trading partner with $318 billion year-to-year two-way trade with the US, and Brazil ranked 11th with $41.5 billion.

China replaces US as Brazil's largest trade partner

In February 2009 China became the second largest trading partner with Latin America. But the announcement that in April China displaced the US as Brazil's top trading partner is an indication of how quickly its influence in the region is growing at the expense of its American rival. The value of Brazil's two-way trade with China reached $3.2 billion in April, surpassing the $2.8 billion in trade between Brazil and the US.

A further indication of China's relevance to Brazil's economic future is indicated by its export figures: exports to the Asian country grew 65 percent from January to April compared with the same period a year ago, according to government officials. These statistics are an unmistakable indication of the weakening of US political and economic influence in Latin America.

In his visit to China from May 18 to May 20, Lula was accompanied by 240 Brazilian businessmen as well as top government officials, who, according to the *People's Daily* web site, were "welcomed by Chinese President Hu Jintao with a 21-gun military salute at Tiananmen Square, festooned with the national flags of China and Brazil."

At the Great Hall of the People, "Hu and Lula witnessed the signing of 13 bilateral agreements covering oil, equipment, financing, science, space, justice, ports and agricultural products, among others," according to the *People's Daily*.

Brazil is trying to increase its exports of high-value manufactured products because it doesn't want to remain merely an exporter of raw materials to China. "Some 70 percent of Brazilian exports to China are primary goods such as soy and iron ore, while 60 percent of Brazilian exports to the United States are manufactured products," *Reuters* reported May 15.

On the other hand, China is compelled to buy manufactured goods if it wants to continue outpacing the US as Brazil's top trading partner. On his return to Brazil, President Lula announced that it was only a matter of time before China purchased up to 45 airplanes made by Embraer, a Brazilian company that has a factory in China, reported the Brazilian daily *O Globo* on May 25.

The sale of airplanes, cooperation on bio-fuel engines and sea drilling, and a communiqué on a Chinese-Brazilian satellite joint venture, released during Lula's visit to the Chinese Aerospace Technology Agency, underscore the high-tech nature of the relationship between the two countries. In the not so distant past, these technologies were the exclusive preserve of US capitalism.

To cement their further collaboration, "the Chinese Development Bank and the Brazilian Development Bank agreed on a framework deal for an $800 million credit extension loan. The Chinese president also proposed closer cultural and people-to-people exchanges," the *People's Daily* said. Lula reciprocated by opening a Brazilian studies center at the Chinese Academy of Social Sciences, considered the country's top research body.

At the Chinese Academy, Lula told an audience of around 200 officials and scholars, "In 2009, China became Brazil's first trading partner. Now we still face the challenge of exploring the full potential of investments that our economies can offer to each other."

Lula also addressed more than 200 Brazilian and Chinese entrepreneurs who attended a business forum on how to explore new opportunities for both countries, the *People's Daily* reported. Of special interest to Brazil is attracting foreign direct investments from cash-rich China. The Asian giant has nearly $2 trillion in reserves and owns $ $768 billion in US Treasuries.

With regards to energy, China Petroleum and Chemical Corporation (Sinopec) and Brazilian oil corporation, Petrobras, signed agreements that include a $10 billion loan for oil exploration, as well as a commitment to ship 100,000 barrels of Brazilian oil per day to China.

The *Oil & Gas Financial Journal* reported May 5 from Rio de Janeiro that days before his visit to China, on the occasion of inaugurating production of the newly discovered offshore oil fields in the Santos basin, a defiant Lula, speaking to an audience of two thousand, including artists, athletes, oil workers, businessmen, politicians and union leaders, took a swipe at Washington. "The great economic lesson of the 21st Century did not come from the failure of some emerging country," he said, "but from the post-graduates of world economy who know everything when a crisis hits Bolivia, Brazil and Russia, but know nothing when the crisis is in their own backyard."

These words found an echo in Lula's visit to China, where the Brazilian president indicated his interest in promoting the Chinese currency, the yuan, as an alternative to the US dollar as well as willingness to work together with Beijing in seeking to increase Chinese-Brazilian influence on multilateral institutions such as the G20 and the World Trade Organization (WTO), which remain under the control of the US and Western Europe.

On May 21, *Bloomberg News* reported that Lula and Hu "discussed the plan to settle trade in local currency during Lula's three-day state visit to China this week." China is clearly concerned about potentially huge losses on its $2 trillion in reserves in the event of a massive devaluation of the US dollar. In response to this possibility, over the past six months or so, China has taken several steps to move away from the US dollar and promote its own currency, the yuan, as a possible candidate for world reserve currency.

Jim O'Neill, head of global economic research at Goldman Sachs noted, "Chinese policy-makers are getting more confident and are thinking about life without the need for the dollar." Earlier this year, China suggested reviving the SDR (Special Drawing Rights) as an alternative world reserve currency.

O'Neil explains, "Every five years the SDR is 'updated'—its weights are changed to reflect economic reality. Currently the SDR consists of the dollar, yen, pound and euro. The next five-year re-weighting is due next year. It is probably a bit soon to include the yuan, but in another five years it is very likely."

China has already received support from Russia's Vladimir Putin, who has called "for a greater use of the yuan." In the light of these developments, China is actively seeking Lula's endorsement. China is aware that in order to gain credibility for its currency, it must first allow greater use of the yuan. To this end, it has already signed $95 billion in currency swap agreements with Argentina, Indonesia, South Korea, Hong Kong, Malaysia and Belarus to facilitate trade independent of the US dollar.

"It's absurd if two important trading nations such as ours continue to carry out our commerce in the currency of a third nation," Lula said in an interview published in the most recent issue of China's *Caijing* magazine.

Lula's support for the yuan has sparked a controversy in Brazilian financial circles. At the heart of this controversy are opposing tendencies within the ruling elite; one representing those who believe Brazil should side with China—and presumably the BRIC (which stands for Brazil-Russia-India-China) and other emerging countries—and break-away from the US dollar, and those whose consider that close ties to the US finance capital remain the best option for Brazil.

"The US has a problem," Sergio Gabrielli, Petrobras' CEO, said recently when asked about the loan talks. "There isn't someone in the US government that we can sit down with and have the kinds of discussions we're having with the Chinese."

"Gabrielli," *Oil & Gas* reported, "was referring to the fact that Chinese government banks are willing to extend huge foreign loans to further China's long-term energy-security goals: ensuring diverse global supplies and winning entree into competitive regions for its oil companies. A string of recent oil loans to Russia, Kazakhstan and others has pushed China's total commitments to more than $45 billion."

Opposing Lula and the Petrobras CEO is Gustavo Franco, former Brazilian central bank president from 1997 to 1999. Franco, whose past credentials include having engineered the Real Plan in 1994 (instrumental in bringing hyperinflation under control to guarantee Brazil's participation in the post-USSR world free market), called China and Brazil's proposal to abandon the US dollar for bilateral trade "pure idle talk," according to *Bloomberg News* (May 21). Franco speaks today as chief economist at Sao Paulo-based Rio Bravo Investimentos, a firm that enjoys close ties with Wall Street financial circles.

"It is not going to succeed," Guilherme da Nobrega, chief economist at Itau Securities, the Sao Paulo-based brokerage arm of Latin America's largest bank, said in an interview in New York, according to *Bloomberg News.* "If you let people choose in which currency they want to trade, they want to trade in dollars."

"I am skeptical," said Ilan Goldfajn, a former Brazilian central bank director, in an interview in New York.

To explain the difficulties involved, *Bloomberg News* cited a recent similar attempt by Brazil and Argentina:

"The two biggest South American economies, agreed in September to trade in local currencies, dropping the dollar. The move was an attempt to reduce transaction costs by eliminating fees on currency exchange and 'until now it hasn't worked,' Goldfajn said. Last month, the two South American nations traded $22.6 million in local currency of the more than $1.6 billion trade flow, according to figures by the Brazilian central bank and trade ministry."

The relationship developing between Brazil and China is by no means purely harmonious. There is no doubt that Lula was performing another errand for the Brazilian bourgeoisie in his visit to Beijing: that of protecting Brazil's trade with and capital investment in its neighboring countries in the face of China's aggressive plan to expand its influence in the region.

Meanwhile, Washington, despite its close and complex economic relations with China, can only see the deals struck between Lula and Hu as a further threat to its own weakening position throughout Latin America. It is inconceivable that it will accept without a struggle being displaced as the hegemonic power in a region it long regarded as its own "backyard."

Lula: using the dollar is "absurd"

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