Yuan Diplomacy: China, Taiwan Vie in Latin American Trade Arena

In recent years, much of the talk in Central America's business communities has revolved around competition with China in the garment trade. In the early 1990s, Chinese apparel exports to the United States were more than twice those of the countries that would become part of the Central American Free Trade Agreement (DR-CAFTA)—Costa Rica, the Dominican Republic, Guatemala, Honduras, Nicaragua and El Salvador. By 1994, these countries had begun to capture U.S. apparel market share from China and, by 1998, had overtaken China.

The DR-CAFTA countries' competitive advantages included trade openings with the U.S. that China did not share. The U.S. has encouraged the apparel industry in Central America and the Caribbean islands through trade arrangements in the Caribbean Basin Initiative (1985) and related acts and agreements in 2000 and 2002. However, China's 2001 entry into the World Trade Organization increased its competitive opportunities in textiles and apparel. The following year, China's U.S. apparel sales pushed past DR-CAFTA's.

The competition remains intense. China's apparel production costs are only 75 percent of Nicaragua's and 62 percent of Guatemala's. But the average time required for transporting textiles and apparel to the U.S. from DR-CAFTA countries is less than one-third China's. Overall, the average turnaround between receipt of an order and delivery to the U.S. is about four weeks for DR-CAFTA nations and 10 weeks for China.[1]

Although the DR-CAFTA countries are going head to head with China in economic competition, there is reason to think that China may seek ways to buy their diplomatic cooperation. China has been devoting considerable effort to economic diplomacy in Latin America. In 2004, President Hu Jintao visited Argentina, Brazil, Chile and Cuba. China's vice president, Zeng Qinghong, visited Mexico, Venezuela and Peru. Chinese investment projects in those countries were announced in conjunction with the visits. These investments seem designed largely to create stable supply sources to China and to allow Chinese firms to profit on the supply end. Many of the announced investment plans involve raw materials production, metal smelting and transportation infrastructure. Another Chinese initiative appears to be textile investments in Mexico—another significant, though waning, apparel exporter to the U.S.

China's investments in Latin America have been small by U.S. standards. But in Brazil alone, some 50 Chinese firms have already directly invested. In 2004, 46 percent of total Chinese foreign direct investment went to Latin American and Caribbean countries. The new projects are said to be dominated by the Chinese equivalents of Japanese *keiretsu*—large business conglomerates with strong government ties.

China's Latin American diplomatic forays and investments may well have political implications for its future involvement in Central America. It is no secret that China wants Latin American nations to break their diplomatic ties with Taiwan. Twelve of the 25 nations that still recognize Taiwan are in Latin America and the Caribbean. Six of the 12 are in DR-CAFTA.

In some countries, China has already announced investment and aid plans substantially larger than Taiwan's. Last year, Taiwanese newspapers complained that the new prime minister of the Caribbean island country of Dominica asked Taiwan for $58 million in aid and then accepted a package from China for double that amount. In response, Dominica dropped its diplomatic recognition of Taiwan. The Taiwanese argue that China's financial program for Dominica is part of an ongoing attempt to discredit Taiwan's unusually independence-focused president, Chen Shui-bian. Since Chen took office in 2000, not only Dominica but also Macedonia, Nauru, Liberia and Grenada have all dropped diplomatic recognition of Taiwan.

Taiwan's ties to the DR-CAFTA countries include announcements of investment plans in Guatemala and other DR-CAFTA countries. Not to be outdone by Chinese diplomacy, Taiwan's Chen made a 12-day tour of Central American and Caribbean countries in September. Taiwanese Vice President Annette Lu also made a diplomatic tour of Central America.

But President Chen's term of office ends in 2008, leaving plenty of time for more Chinese diplomatic efforts at reducing world support for Taiwan during his administration. It would not be surprising to see China attempt to make the DR-CAFTA countries adopt its political perspective. There are already reports that China plans textile investments in Central America.

The DR-CAFTA accord includes duty-free benefits on fibers, fabrics, yarns and apparel made in member countries, giving DR-CAFTA countries an advantage over China in selling to the U.S. The tariff savings might offset some of China's lower production costs. Coupled with these factors, political incentives might be more reason for Chinese textile operations in Central America.

It is conceivable that the Chinese might realize a price advantage from the region's "spaghetti bowl" of free trade agreements, perhaps by producing textiles in Mexico for manufacture into apparel in Central America. This, however, ignores the Taiwan issue. Investments, whether in textiles or other industries, could turn up as carrots for DR-CAFTA countries that consider playing the mainland China side of the street.

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Note

[1] *The Emergence of China: Opportunities and Challenges for Latin America and the Caribbean,* edited by Robert Devlin, Antoni Estevadeordal and Andres Rodriguez, Inter-American Development Bank, 2005.