Macro Vision

August 15, 2024

Imports from China on the rise: relevant aspects for the Brazilian economy

- Rising imports of Chinese products into Brazil have garnered increased attention recently. This study examines what is behind the increase in terms of volume and prices, as well as impacts across sectors.
- The increase has been driven by higher volumes (quantum), despite a simultaneous decline in prices in many cases. Products from the following sectors more often experienced higher imported volumes and/or lower prices: chemicals, semi-finished metals, plastics, rubbers, textiles and automotive.
- In the domestic industry, sectors facing rising Chinese imports are showing signs of falling input prices and disinflation in industrial goods prices, in addition to reduced capacity utilization.
- Growing Chinese exports have prompted reactions from several countries, such as higher tariffs and non-customs barriers. In Brazil, similar measures are likely to be even more costly than in other regions due to China's significant role in Brazilian exports.
- In our view, the situation caused by the recent increase in Chinese imports reinforces the need to advance with agendas aimed at improving the domestic business environment through structuring reforms, such as tax simplification (the recent tax reform was an important step), reduced bureaucracy, bolstered infrastructure, in addition to ensuring lasting macroeconomic stability.

1. Context: China as a two-speed economy

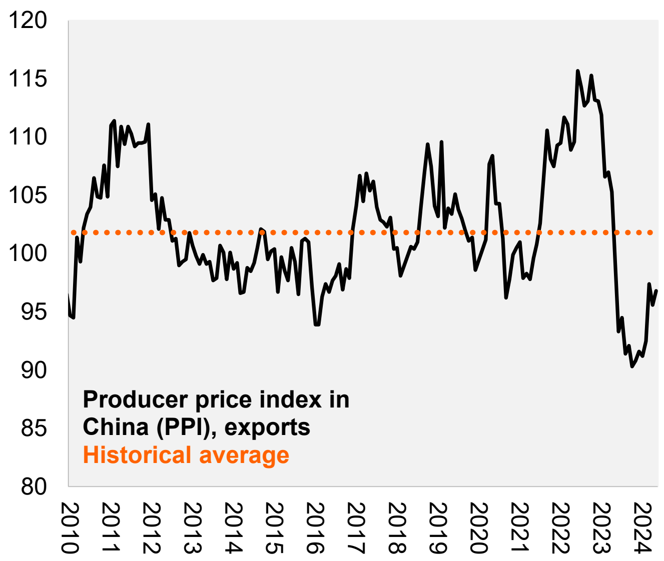
China's economic dynamics have shifted significantly from the previous decade. The structural crisis in the real estate sector, unfavorable demographics and tumultuous geopolitical scenario are impacting China's growth outlook, as well as its composition. Hence, the once common double-digit growth rates are no longer anticipated for the future. According to our forecasts, the Chinese economy will grow 4.8% this year and 4.5% next year.

In response to this slowdown, recent economic policies have been directed toward stimulating the manufacturing industry (among other sectors), particularly exports. In a recent study published here, we show that the Chinese economy has been moving at two different paces since 2021, with weakness in the real estate sector and moderate consumer spending, but a better performance in the infrastructure sector and excess capacity in manufacturing. This last aspect has led to lower export prices, as shown by China's Producer Price Index - Exports (PPI Expo).

During the Third Plenum of the Central Committee of the Communist Party on July 15-18, authorities reaffirmed their support to "supply chains" and technological innovations. During this plenary, which takes place once every five years, approximately 300 measures were announced, focusing on "high-quality development" and "new productive forces". This indicates a continuing reliance on a growth model led by manufacturing – where excess production is exported.

In this paper, we analyze various aspects of the increase in Chinese imports to Brazil. While Brazilian exports to China are also a relevant subject, especially amid significant geopolitical shifts, this is not the object of this work, which focuses on imports from China.

Producer Price Index in China – Exports (China PPI Expo)



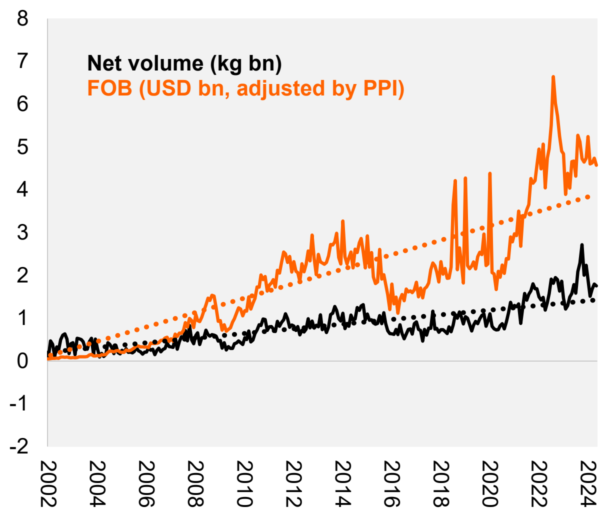
Source: BBG, Itaú

2. Rundown of imports from China: how did the increase happen (and in which sectors)?

Imports from China into Brazil increased as a consequence of higher volumes (quantum), despite concurrent price declines in many sectors. Foreign trade data (Comex) show that imported values are above the historical trend, boosted by rising imported volumes, given that average prices (adjusted by the PPI US in the same period) have been below-trend recently.

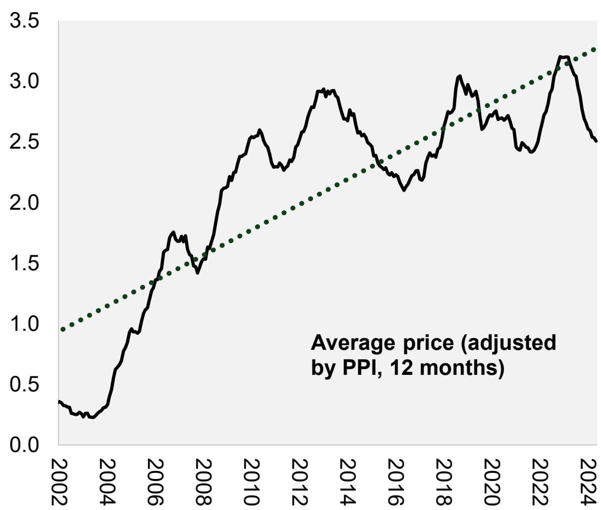
Brazilian imports of Chinese products

Volume and total (FOB)



Source: MDIC, Itaú

Average price

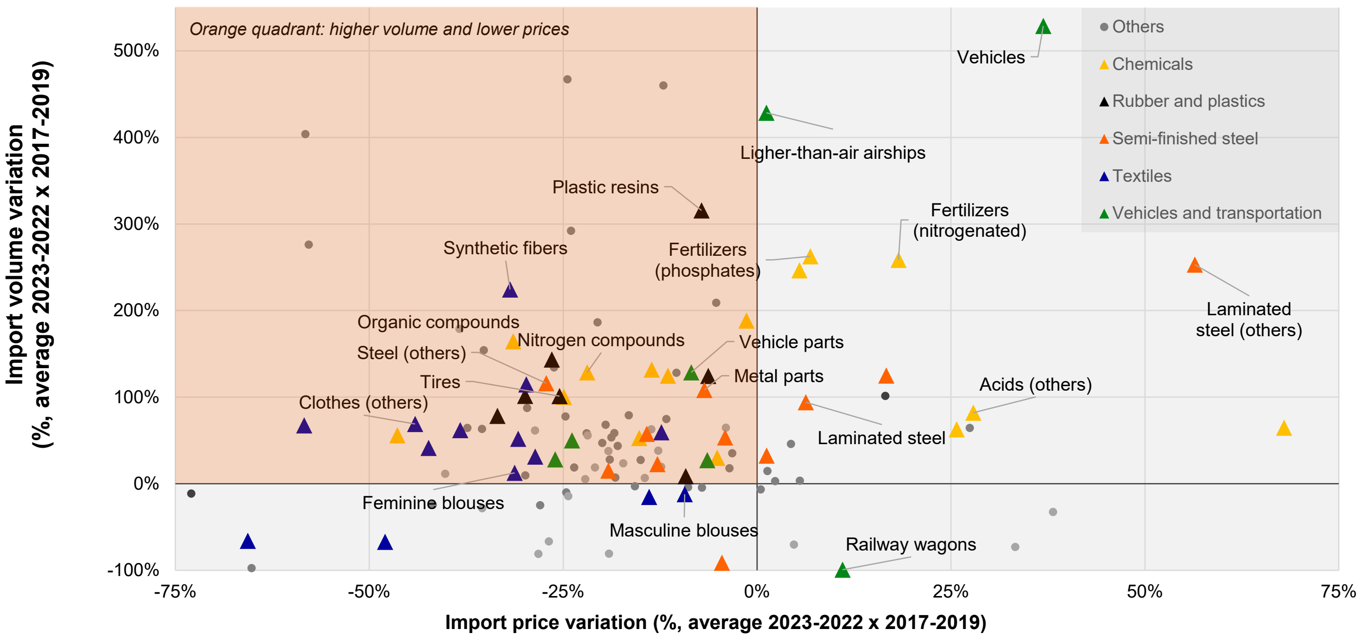


Source: MDIC, Itaú

Most items showed increased volumes and lower prices. The scatter chart below shows the variation in prices and import volumes between the pre- and post-pandemic periods (average 2023-2022 vs. average 2017-2019, adjusted by the US PPI) for several relevant items on Brazil's imports list[1] (around 230 selected items, representing 75% of Chinese imports).

Products from the following sectors experienced higher imported volumes and/or falling prices more often: chemicals, semi-finished metals (such as long and flat steel and their byproducts), plastics, rubbers, textiles and automotive.

A substantial share of items purchased from China experienced greater volumes and lower prices
Change in quantity vs. prices of Chinese imports into Brazil, main items (230 products, 75% of total imports) adjusted by PPI US



Source: MDIC, Itaú

3. Is there impact to industrial goods prices in Brazil?

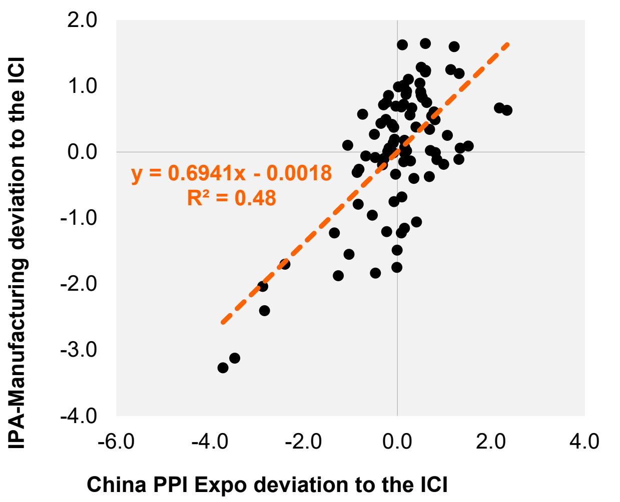
Cheaper Chinese manufactured goods coming into Brazil may contribute to lower industrial goods prices because many of these are intermediate goods. However, this is not a direct relationship, as it depends on the evolution of commodity prices and the exchange rate.

Largely, disinflation in industrial goods in Brazil – for producers as well as consumers – was primarily driven by recent declines in commodity prices and lower import prices from China. We built historical series of industrial goods prices in Brazil (Wholesale Price Index-Manufacturing – IPA) and export prices to producers in China (PPI Expo) adjusted for commodity prices in BRL. This adjustment is carried out by subtracting the change in commodity prices in BRL (measured by Itaú's ICI indicator) from the original series.

The scatter plot on the left indicates a positive correlation between deviations of PPI Expo and IPA-Manufacturing in relation to commodity prices. Furthermore, the change in the IPA-Manufacturing can also be seen as a driver of consumer goods prices (IPCA-Industrials), although with an average lag of 8 months.

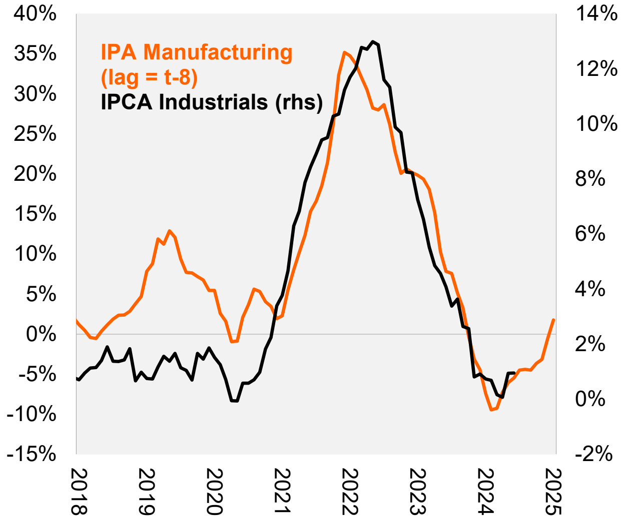
[1] We use the Mercosur Common Nomenclature (NCM) for each item, up to 4 digits (SH4).

Producer price index in China (exports) and IPA-Manufacturing, deviation to the ICI (commodities), 2016-2024



Source: FGV, MDIC, Itaú

IPA-Manufacturing vs IPCA-Industrials

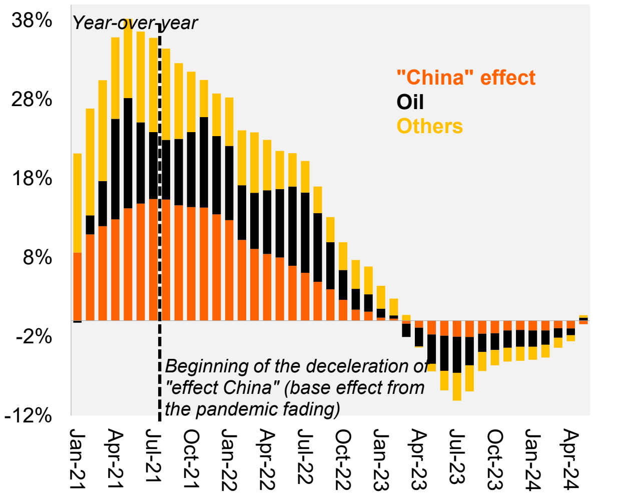


Source: FGV, IBGE, Itaú

The recent slowdown in the IPA-Manufacturing was particularly influenced by sectors that experienced higher volumes of Chinese imports at lower prices. We considered three groups: (1) “China effect” group – sectors listed above after experiencing lower prices and higher imported volumes: textiles, chemicals, plastics and rubber, metallurgy and automotive; (2) “crude oil” – given that this commodity and its byproducts have significant weight in the composition of industrial prices; and (3) others – remaining sectors. The deceleration is observed from 2021 onwards, after the beginning of the post-pandemic normalization and dissipation of the base effect of that period, reaching negative territory in early 2023 (graph on the left).

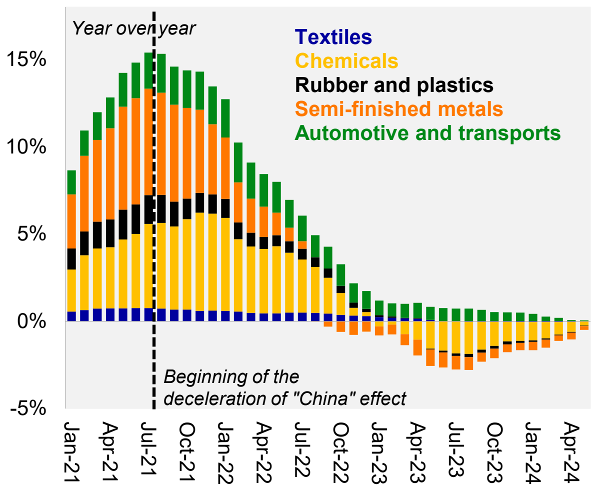
The recent slowdown in industrial prices is more evident in the chemical and metallurgy industries.

Contribution to the IPA-Manufacturing, by factor



Source: FGV, Itaú

Contribution to the “China effect”, by sector

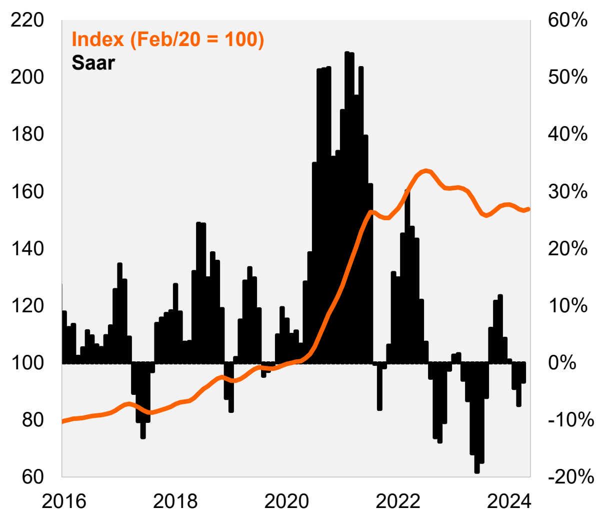


Source: FGV, Itaú

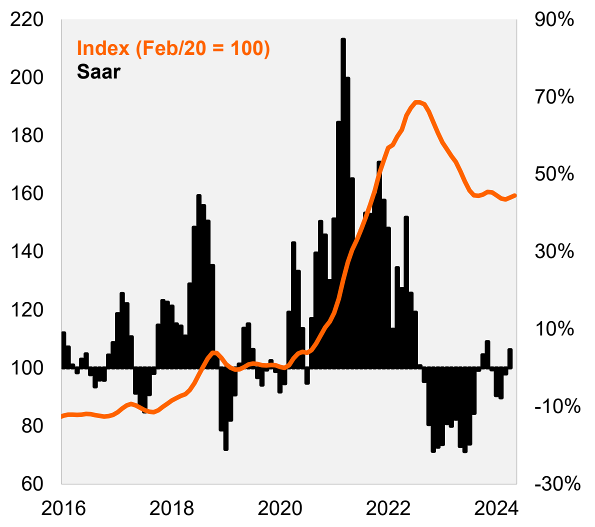
Monthly declines in most industrial goods prices became steeper from 2022-2023 onwards. In terms of price level (index), although no sector has fully reversed the increase seen during the pandemic, some saw relevant drops from their recent peaks.

Monthly change and IPA-Manufacturing indexes, by sector
3-month moving average

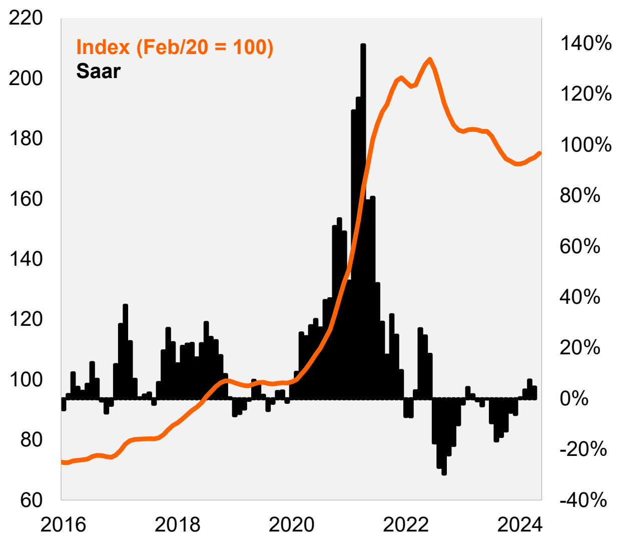
IPA - Manufacturing



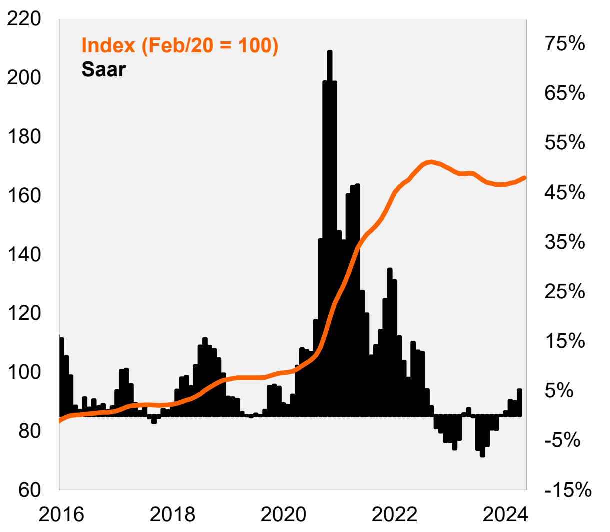
Chemicals



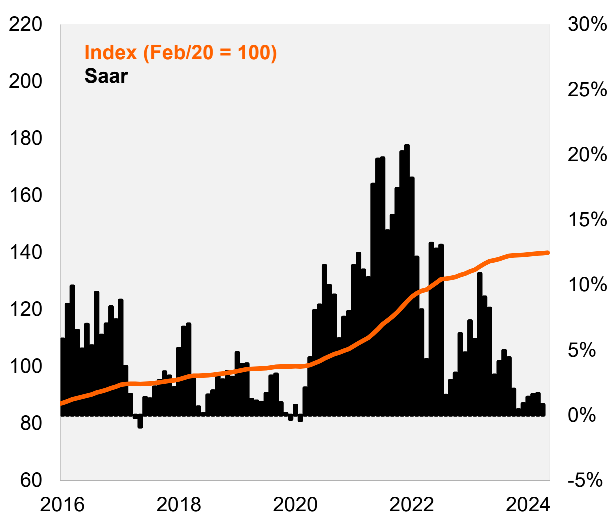
Basic metallurgy



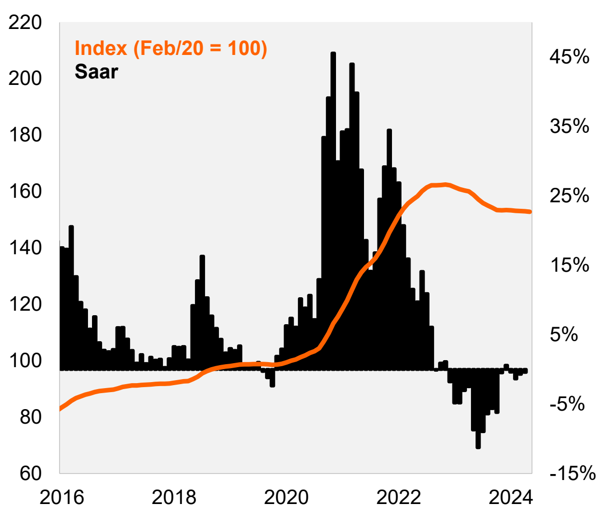
Rubber and plastics



Automotive



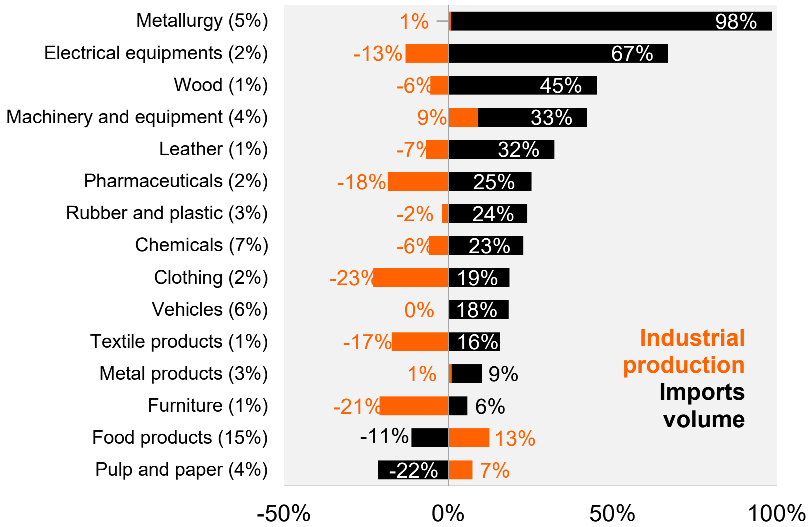
Textiles



4. Effects on Brazilian industrial production

Analyzing the recent dynamics of Brazilian industrial sectors, we found no clear relationship between the magnitude of the increase in Chinese imports and domestic production. For most sectors experiencing rising imported volumes, industrial production receded between 2019 and 2023. However, the elasticities vary greatly between sectors, as shown by the graph below comparing industrial production and imported volumes based on a reconciling of sector bases used by Comex (trade balance) and IBGE (monthly industrial production survey, PIM-BR).

Industrial production vs imports volume, 2023 x 2019 change, by sector



Weight in the total index in parenthesis

Source: MDIC, IBGE, Itaú

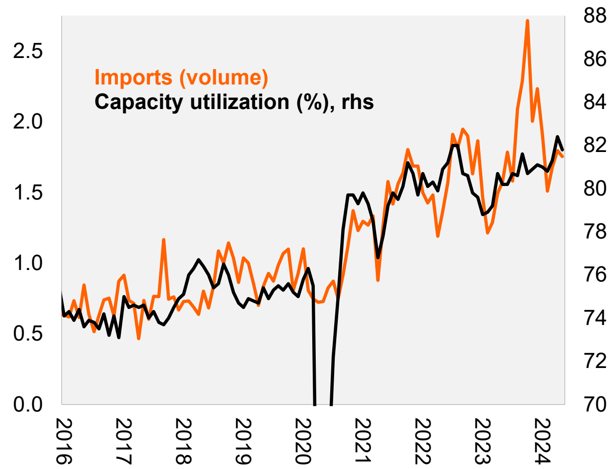
As discussed in the previous section, falling imported prices tend to reduce production costs and make items that are not manufactured domestically more accessible. However, identifying which imported products are not produced domestically is not a trivial task, given the capillarity of industrial products in Brazil.[2]

The complementary role of Chinese imports can be traced from the correlation between imported volumes and capacity utilization (NUCI) across sectors. According to the graphs and table below, imported volumes and capacity utilization across sectors usually have a positive correlation, demonstrating the complementary role of Chinese inputs for domestic production. But a few sectors – again, metallurgy, textiles, as well as capital goods – have visibly lost this historical relationship and experienced greater slack during the period of rising imports, in a sign of the low competitiveness of domestic products vs. imports.

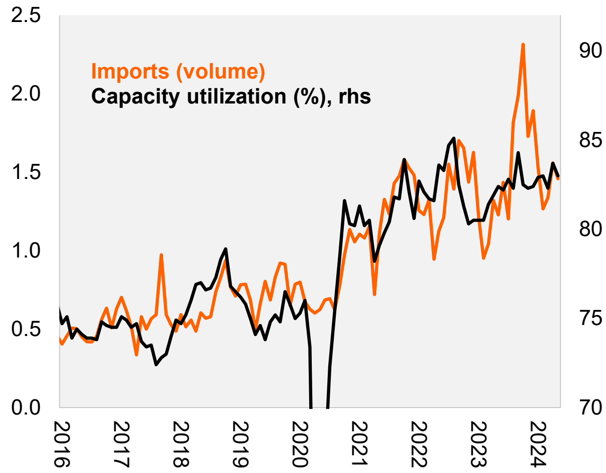
[2] Granularity also impacts the reconciliation of databases. In Brazil, industrial production bases by product, derived from the Annual Industrial Survey – Products (PIA-Products) rely on PRODLISTS, while the foreign trade databases use different nomenclatures, such as the Mercosur Common Nomenclature (NCM SH2-SH6). The more granular the analysis, the higher the operational cost of reconciling them. As this paper focuses on the macroeconomic impact, our efforts were limited to analyzing large sectors.

Imported volume (million tons) vs. capacity utilization (%), by sector
Source: FGV, MDIC, Itaú

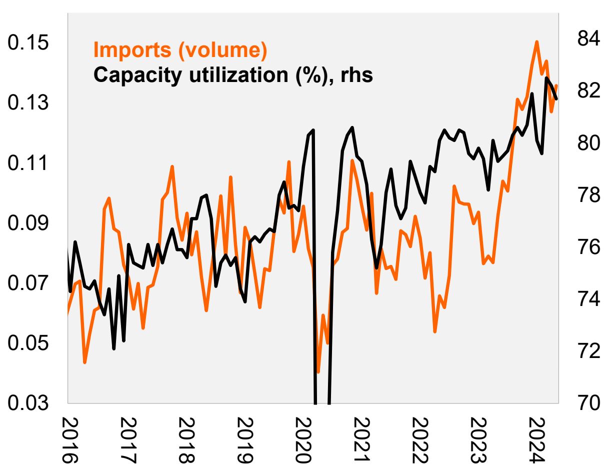
Manufacturing



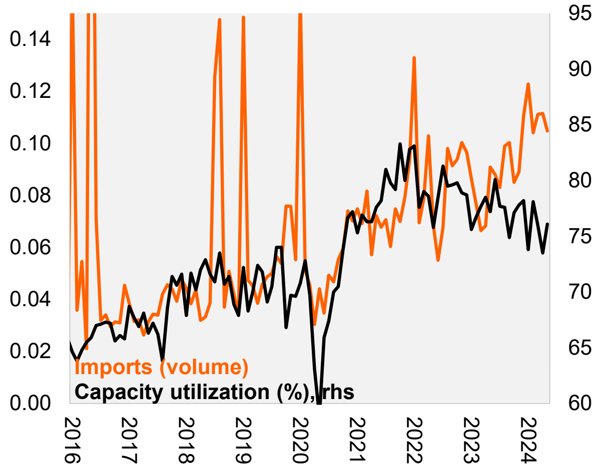
Intermediate goods



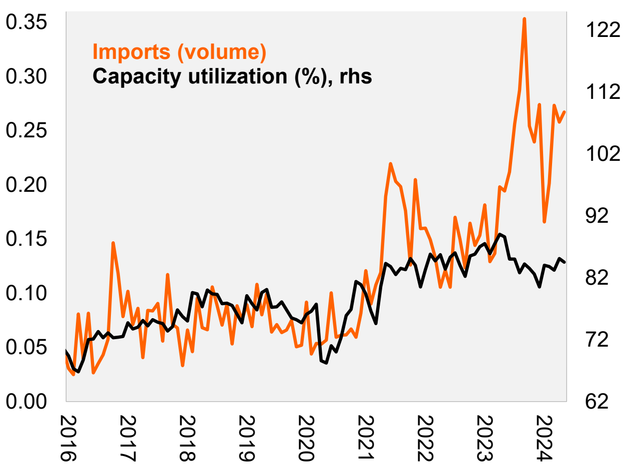
Consumption goods



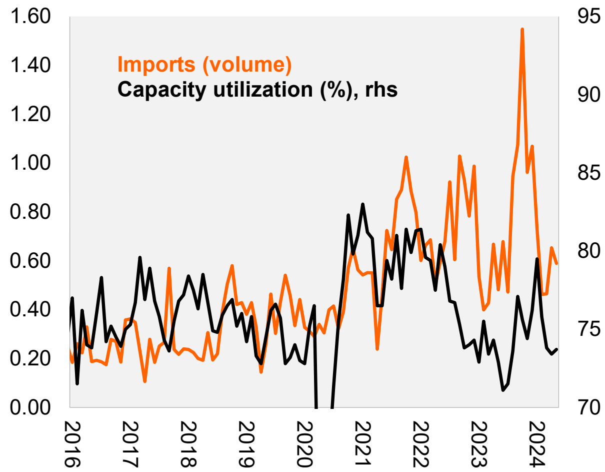
Capital goods



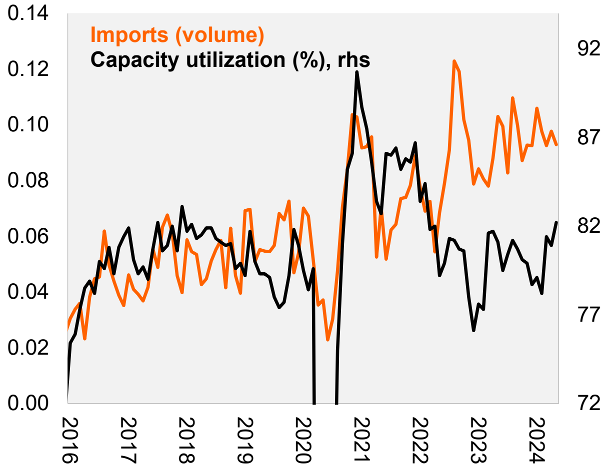
Metallurgy



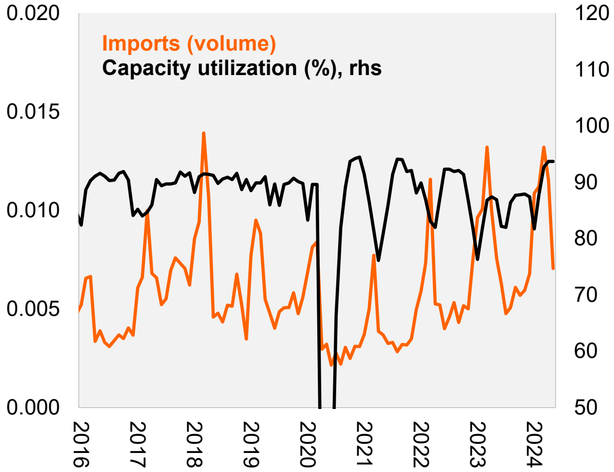
Chemicals



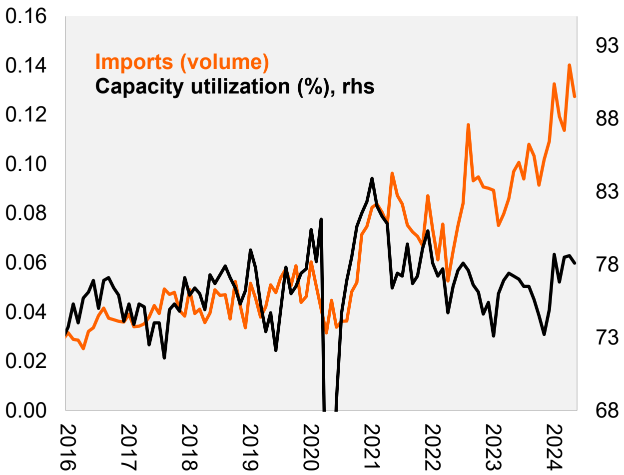
Textiles



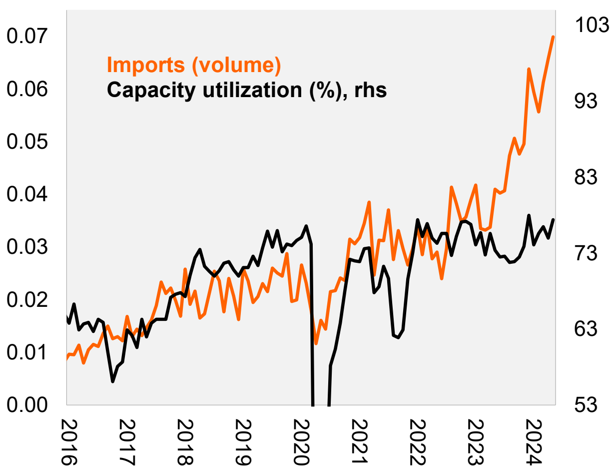
Clothing



Rubber and plastics



Vehicles



Historical correlation between imported volumes and capacity utilization, by sector

	Manufacturing	Intermediate goods	Consumption goods	Capital goods	Metallurgy	Chemicals	Rubber and plastics	Textiles	Clothing	Vehicles
All period (2014-2024)	0.30	0.42	0.59	0.20	0.43	-0.23	-0.14	0.15	0.17	0.26
2016-2019	0.29	0.38	0.17	-0.02	0.25	-0.23	0.20	0.20	-0.02	0.70
2022-2024	0.45	0.22	0.63	-0.08	-0.33	0.05	0.27	-0.10	-0.17	0.04

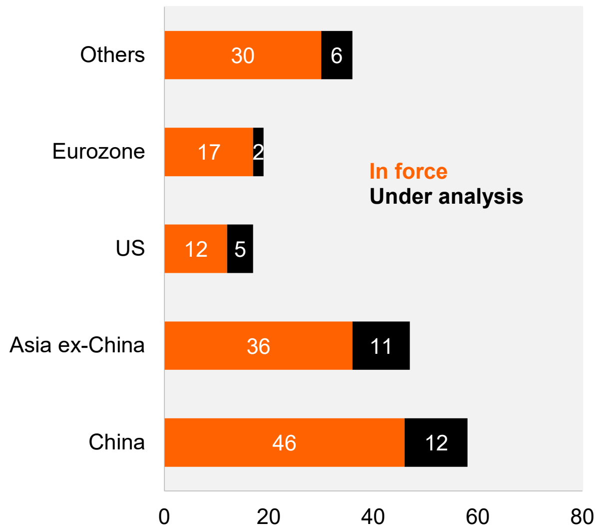
Source: MDIC, FGV, Itaú

5. The way forward: increasing competitiveness as a solution

Growing Chinese exports have prompted reactions from several countries, such as higher tariffs and non-customs barriers. The US announced tariffs on Chinese products such as electric vehicles (100% tariff), semi-conductors (50%) and photovoltaic cells (50%). The European Union also applied tariffs to electric vehicles (ranging from 18% to 36%). The Brazilian government recently adopted an import quota for steel products (but only for specific items) and taxed retail platforms for low-value imports.

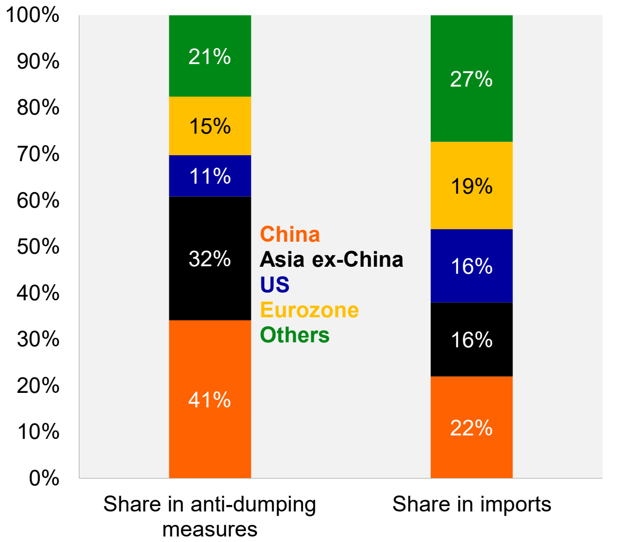
Brazil has been using alternatives to tariffs – such as unilateral actions at the World Trade Organization (WTO) – for an extended period. The graphs outline the number of anti-dumping measures by Brazil per trade partner. As the main source of imports into Brazil, China is naturally the target of a large share of such measures. Still, there are more actions in place than the share on the import list would suggest for China and Asia in general.

Anti-dumping measures in Brazil by country, up to Mar/2024



Source: Itaú

China is "over-represented" in anti-dumping measures



Source: MDIC, Itaú

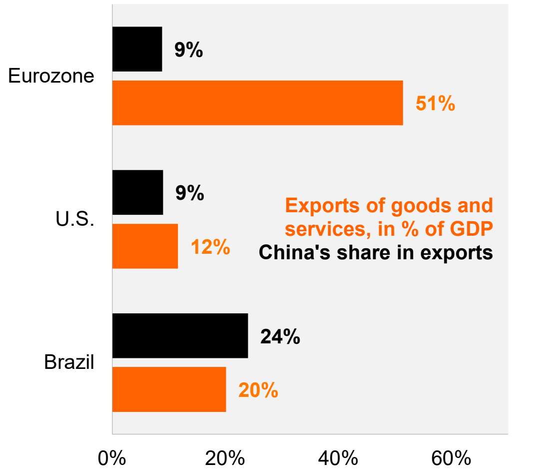
Anti-dumping measures in Brazil (vs. China), by sector (up to Mar/2024)		
Sector	**In force**	**Under analysis**
Metallurgy	15	5
Automotive tires	5	-
Chemicals and resins	7	2
House/office supplies	10	2
Textiles	3	1
Others	6	2
Total	46	12

Source: Itaú

Importantly, trade barriers tend to be more costly for Brazil than for other economies. China is Brazil's main trading partner and absorbs a large share of our output (graphs below), making protectionist strategies even less attractive than usual. Furthermore, Brazil comes from a stage of low trade openness, already imposing relevant costs on the domestic economy.

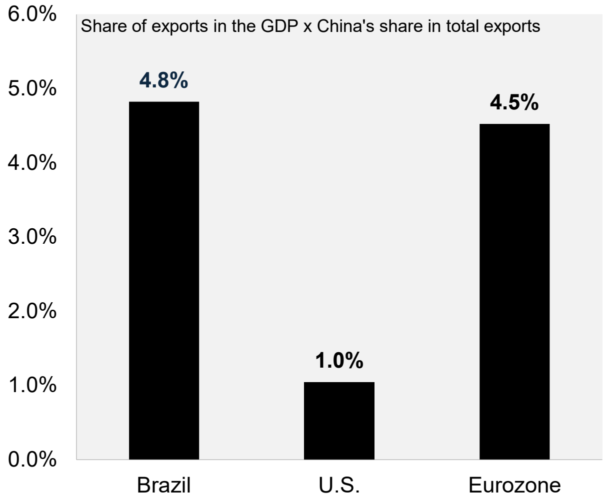
The penetration of Chinese products has provided a significant contribution to containing inflation in industrial goods prices in the country. Hence, protectionist measures tend to have inflationary impact, eroding households' purchasing power.

China's share in exports is bigger in Brazil, a fact even more relevant considering our small degree of trade openness



Source: World Bank, MDIC, Itaú

Proportionally, Chinese imports are also more relevant for the Brazilian GDP



Source: World Bank, MDIC, Itaú

In our view, the situation caused by the recent increase in Chinese imports underscores the need to advance with agendas aimed at improving the domestic business environment through structuring reforms, such as tax simplification (the recent tax reform was an important step), reduced bureaucracy, bolstered infrastructure, in addition to ensuring lasting macroeconomic stability. Embracing protectionism would likely have negative effects, benefiting a few sectors at the expense of the general population.

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