

## China-Spain-Latin America Triangulation in a Chinese Perspective (ARI)

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**Theme:** This paper looks at the prospects for triangulation between China, Spain and Latin America in the wake of the Sinopec-Repsol deal in Brazil.

**Summary:** The recent Sinopec-Repsol agreement in Brazil's energy sector is the result of China's massive 'going out' strategy and of Spain's increased role as a 'bridge'. This paper looks at the results and prospects of the China-Spain-Latin America triangulation, highlighting the challenges ahead for this promising instance of international cooperation.

**Key words:** China, Spain, Latin America, Sinopec, Repsol, Brazil, triangulation, China's outward investment.

**Analysis:** On 1 October 2010 it was announced that Sinopec, one of China's largest energy companies, would invest US\$7.1 billion in Repsol YPF Brasil, taking a 40% stake. The Brazilian company, which represents the interests of its Spanish parent, Repsol, in the Brazilian market, produces, exploits, transports and distributes crude and gas derivatives throughout Brazil. Its main products are gasoline, alcohol, biodiesel, NGV, diesel, fluids and motor lubricants.

### *A Treble-win Scenario*

Sinopec's cooperation with Repsol creates a treble-win scenario. For Sinopec, the investment can strengthen its foothold in Latin America's energy sector. It believes that this transaction will further enable it to achieve its strategic objective of building a stronger presence and operations in the region, accelerating its international growth strategy as well as optimising its offshore oil and gas asset portfolio.

For Repsol, the deal will enable it to acquire enough funds to develop its deposits in Brazil, one of the world's most important exploration markets since the discovery of massive pre-salt oil reserves off the Brazilian coast.

According to Reuters, on the day the deal was sealed, Repsol's shares rose 5.6% to a 2-year high of €20.00 while the construction firm Sacyr-Vallehermoso, which holds a stake of around 20% in Repsol, jumped 12.7%. Repsol's Chairman Antonio Brufau said in a statement: 'We are delighted to share the development of the Brazilian projects with a partner with recognised prestige in the sector like Sinopec'.

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The Sinopec-Repsol deal is also positive for Brazil, which has been looking for foreign capital to open up its resources. Before his visit to China in May 2009, President Lula said that Brazil would welcome Chinese investment in its infrastructure and energy sectors. He believed that China would become an important partner for Brazil when it attempts to tap its enormous pre-salt oil reserves.

On 4 January 2011, Sinopec's Chairman Su Shulin, who was accompanying the Chinese Vice Premier Li Keqiang during his visit to Spain, met Repsol Chairman Antonio Brufau in Madrid and they presided over the first joint meeting at the top corporate level between both companies following the agreements reached in Brazil. They agreed to create working groups to analyse new business opportunities world-wide. Antonio Brufau said, 'There are significant synergies between Repsol and Sinopec, and the relationship between both companies is ideal to continue reinforcing our alliance worldwide in new business areas'. Su Shulin also expressed satisfaction over their cooperation. He said, 'The successful co-operation between Sinopec and Repsol reflects the shared desire of both companies to start a long-term and extensive partnership. We are committed to making every effort to consolidate and develop this relationship with Repsol in the future'.

Cooperation between Sinopec and Repsol has attracted world-wide attention. The *Financial Times* believes that 'China and its big companies are eager to invest in natural resources in emerging markets such as Africa and Latin America. Repsol's assets in former Spanish and Portuguese colonies are a particularly tempting target'. According to the *Wall Street Journal*: 'The transaction gives China a piece of one of Latin America's largest foreign-controlled energy ventures. It is the latest sign of the country's growing prominence in the international energy sector as it expands both access to and ownership of raw materials needed to fuel the country's economic expansion'.

#### *China's "Going-out Strategy"*

The significance of the deal between Sinopec and Repsol is two-fold. First, it allows China to gain further influence in the global energy market. Secondly, efforts to push forward a China-Spain-Latin America triangulation have paid off.

Since China implemented the reform and open-door policies in 1978, its economy has been growing rapidly, creating a huge demand for resources, including energy. China itself has abundant resources, but in *per capita* terms it is quite poor. That is why China needs, on the one hand, to rely on external sources to sustain its economic growth and, on the other, to adjust its development model by reducing waste and raising its resource-utilisation efficiency.

In the late 1990s the Chinese government implemented its so-called 'going out strategy'. Its aim was to encourage Chinese enterprises to make more direct investments abroad so as to integrate China's economy more closely with the rest of the world, to secure the availability of external resources and to reduce the production overcapacity of some of the sectors of its economy.

According to official statistics, in 2009 China produced 189 million tons of crude oil, but net imports totalled 199 million tons, causing its dependence ratio –ie, its oil imports as percentage of total oil consumption– to exceed 50% for the first time, reaching 51.29%. Some Chinese economists predict that the dependence ratio, whose 'critical line' is believed to be below 50%, might reach 65% by 2015 and over 70% by 2020.

### *Spain's Role as a 'Bridge'*

Bilateral relations between China and Latin America have been developing steadily since the early 2000s. Apart from frequent exchanges of high-level visits, trade and investment have also been growing rapidly. Even strategic partnerships have been established between China and several Latin American countries such as Brazil, Mexico, Argentina and Peru.

China's presence in Latin America has aroused great concern and anxiety in the US Administration, the media and even the public. In fact, China's interest in Latin America is not to challenge the US dominance in the region, its 'back-yard', but to promote South-South cooperation in the economic sphere. Naturally, as a region with a large market and an abundance of resources, Latin America is highly complementary economically with China.

Unlike the US, Spain has been right to suggest that it can offer a helping hand to China to develop its relations with Latin America. It is important that, as early as the start of the new millennium, the Spanish government decided that the Spain-Latin America-Asia-Pacific triangulation was one of the priorities in its 'Asia-Pacific Framework Plan 2000-2002'.<sup>1</sup> In July 2005 the visiting Spanish Prime Minister, José Luis Rodríguez Zapatero, said to his Chinese hosts in Beijing that Spain would be ready to serve as a 'bridge' for China to develop its relations with Latin America. When President Hu Jintao visited Spain in November 2005, China and Spain issued a joint communiqué in which they expressed their willingness to cooperate around the globe, particularly in Latin America.

Speaking to the Chinese press in 2009, the Spanish Ambassador to Beijing, Carlos Blasco Villa, said that Spain would be happy to see China proceed with its investments in Latin America. When he was asked whether the interests of China and Spain were in competition, since China's relations with Latin America were moving closer, Blasco said, 'Just the opposite. I think closer relations between China and Latin America would contribute to the cooperation between them in making investments in Latin America'. The Ambassador also said that 'Spain would suggest that Latin America should not rely on the US so much, nor should it rely on EU'. He even offered an example of triangular cooperation: 'Huawei and Zhongxin have sold equipment to Spanish companies, which use the Chinese products to build telecom towers in Latin America'.

Spain is certainly in the right place to act as a 'bridge' between China and Latin America. Its affinity with the region in history, language and culture makes it have more common ground than China does. Since the 1990s, with the deepening of Latin America's economic reforms, including privatisation and tariff reductions, Spain has consolidated its economic relations with the region. Through the Ibero-American Summit, Spain's political relations with the region are also on very good terms.

### *Remarkable Progress*

China's first policy paper on Latin America, published in November 2008, might be a milestone in its relations with the region.<sup>2</sup> The paper not only makes China's diplomatic goals there more transparent, but also fills a gap in the country's foreign policy. It

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<sup>1</sup> Pablo Bustelo (2002), 'Prospects for Spain-Latin America-Asia-Pacific Triangulation', ARI nr 123/2002, Elcano Royal Institute, 20/XII/2002.

<sup>2</sup> China published its first policy paper on the EU in October 2003, followed by an African policy paper in January 2006.

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expresses for the first time the Chinese government's wishes to 'view its relations with Latin America and the Caribbean from a strategic height'.

The policy paper emphasises the importance of promoting bilateral trade and economic relationships and also confirms cooperation in 35 fields, including international affairs, judicial and police affairs, science and technology, education, medicine, climate change, disaster relief and exchanges between the military, legislatures, local governments, political parties and high-level officials.

If Spain intends to help China further develop its relations with Latin America, efforts need to be directed towards these 35 areas. Apparently, China hardly needs Spain's help in the political field. But in the economic sphere, Spain can make great contributions. Indeed, cooperation between Sinopec and Repsol is a very promising gesture towards this end.

Much of the Latin American countries' mineral reserves are located in remote areas or high mountains where infrastructures are nowhere to be found. So China and Spain can join hands to pool more funds to build infrastructures for the purpose of increasing access to the minerals.

According to China's 12th Five-Year Plan (2011-15) for economic and social development, the Chinese government will have a greater focus on transforming the country's economic development model. To facilitate the process, the government has vowed to boost domestic demand, promote scientific and technological innovations and take further measures to preserve resources and protect the environment.

Stimulating domestic demand, however, does not mean reducing the country's exports to the world market, including Latin America. Spain has well-established marketing networks in the region. Therefore, it can help China to expand its market share in the region.

China has increasingly recognised the importance of developing renewable energy. Spain, Brazil, Mexico and some other Latin American countries have a relatively advanced technology in the field, so there should be many opportunities for cooperation.

Language and cultural barriers pose challenges for China to expand its presence in Latin America. Although dozens of universities in China have Spanish-language courses and hundreds of students graduate each year, there is still a lack of professionals with fluent Spanish. Spain can offer assistance in this regard. The *Instituto Cervantes de Pekín*, founded in 1991, has done an excellent job by offering Spanish-language training courses. Furthermore, it also organises cultural activities in Beijing so as to enrich the Chinese people's understanding of the cultures of the Spanish-speaking nations.

Apart from technological cooperation between China and Spain in the Latin American market, such as with Huawei and Telefónica, triangulation has recently started to develop in other areas. In early 2010, for instance, Uría y Menéndez, a very prestigious Spanish law firm, opened an office in Beijing. It offers advice to Chinese clients on their investments in Latin America, where Uría has five offices and extensive experience advising foreign investors in the region. Undoubtedly, Uría y Menéndez's service will help Chinese investors to enter Latin America, a region where both political and legal uncertainties, along with cultural differences and geographical distance, are seen to be formidable barriers.

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So far Uria y Menéndez has participated in two of the most important Chinese investment transactions in Latin America announced in 2010: the acquisition of seven transmission lines by China's State Grid and the investment by the East China Mineral Exploration & Development Bureau in a mining project.

Financial services is another promising area where China and Spain can cooperate in Latin America, and the first steps seem to be quite fruitful.

In recent years, the social security system has finally come to the centre stage of China's reform programmes and it is believed that in this field China is modelling itself on Chile and other Latin American countries. In November 2010 China's CITIC Bank and BBVA signed a Co-operation Framework Agreement in the Pension Business to jointly advise on the structure of China's pension schemes. The agreement, valid for a period of 12 months, includes collaborative consultation on the structure of China's pension schemes, product design and customer services. Once the 12-month period comes to an end, both parties will evaluate the results of their collaboration and consider continuing co-operation further.

In January 2011 the China Development Bank (CDB), the country's largest banks by assets, signed an agreement with BBVA to foster cooperation between the two banks in business ventures outside China, mainly Latin America, in areas such as project and trade finance, commercial services, derivatives, corporate banking and bonds.

#### *Weak Points to Overcome*

There are more examples of successful triangulation between China, Spain and Latin America. On the Chinese side, pushing for triangulation is economically possible as it has accumulated huge reserves of foreign exchanges. In a strategic perspective, China would also wish to consolidate its presence in Latin America with Spain's help.

Spain has recognised the fact that the rise of Asia is a historically significant trend that will become the defining event of modern times. According to Spain's Foreign Ministry, as the eighth-largest economy in the world, Spain cannot afford to ignore the growing importance of this region on the international scene. In the age of globalisation, the political, economic, security and cultural interests of Spain are also dependent on Asia.

Prominent Spanish scholars, like Pablo Bustelo and Javier Santiso, along with Repsol and Uria y Menéndez, are among the pioneers in pushing for China-Spain-Latin American triangulation and initial progress has been achieved over a short period of time.

However, although both China and Spain have expressed their willingness to cooperate in Latin America, it seems that triangulation is not at the top of the agenda of their bilateral relations. For instance, when the Spanish Prime Minister José Luis Rodríguez Zapatero visited China in August 2010 he and Chinese Premier Wen Jiabao did not mention a word about their cooperation in Latin America. Wen only said that China and Spain should take more measures to promote trade and investment and jointly maintain the stability of the EU and world financial markets. He expressed the hope that China and Spain will closely coordinate and cooperate in the G20, stand firmly against protectionism and jointly push forward the reform of the international financial system. Rodríguez Zapatero only said that Spain would also like to see deeper bilateral cooperation in trade, investment, culture and tourism and would be ready to further promote strategic cooperation between



the EU and China by pushing for an early resolution to the major problems in EU-China relations.

In his article titled '*Trabajemos de la mano*' published in the Spanish daily *El País* (3/1/2011), Li Keqiang examined the ways and means of promoting bilateral cooperation, but he said nothing about China's cooperation with Spain in Latin America.

Consequently, if we want to see further development of the triangulation, the Chinese and Spanish governments should make bolder efforts to include it in their priority agendas for bilateral relations.

Another weak point is that most of China's public or private small- and medium-sized enterprises are not yet aware of the existence of the important role of Spain as a 'bridge' over which they might enter the Latin American market. Consequently, so far, only the giant state-owned companies have taken advantage of Spain's position. Both the Chinese and Spanish governments need to redouble their efforts to publicise triangulation.

There is one more weak point on the Latin America side. It seems that Latin America's reaction to triangulation is lukewarm and passive. The region is just waiting to be found by China and Spain in the triangulation game, though it cannot be denied that every country there endeavours to attract more foreign investment. Since triangulation involves three parties, active and spontaneous participation on the Latin American side would be extremely productive.

Finally, it must be understood that triangulation sometimes incurs third-party transaction costs. If a Chinese enterprise can find its partner in Latin America and vice versa, why use the Spanish 'bridge'?

**Conclusion:** The triangulation concept is used to indicate the interaction between three regional players, either a regional bloc of nations or individual nations. Even though they may compete in some cases and cooperate in others, the essential feature is the existence of shared interests and current or potential relations among them.

In recent years China's relations with Latin America have been proceeding rapidly. Unlike the US, Spain would be ready to help China develop its relations with the region. This should be interpreted as a very positive and benign offer.

In the political field of the China-Spain-Latin America triangulation, Spain's role as a 'bridge' is quite limited. In other areas, particularly investment and trade, the possibility of cooperation between China and Spain in Latin America is enormous and a very fruitful start has been made.

In order to achieve more progress, the Chinese and Spanish governments should make bolder efforts to include it into the priority agenda for their bilateral relations. Furthermore, efforts must be made to publicise Spain's unique position as a 'bridge' between China and Latin America so as to attract more and more Chinese public or private small- and medium-sized enterprises. At the same time, Latin America needs to be encouraged to take a more active and spontaneous attitudes towards triangulation.

The China-Spain-Latin American triangulation is part of the North-South and South-South issue. As cooperation and inter-dependence has become all the more important in the age of globalisation, the future of this new hybrid type of international relationship should be very promising.

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