

Agricultural trade linkages between Latin America and China

Conclusions and Future Priorities



FAO INVESTMENT CENTRE

WORKSHOP HIGHLIGHTS





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Summary report of an Expert Group Meeting
jointly organized by the World Bank and the
Food and Agriculture Organization of the United Nations (FAO)
FAO Rome, 27-28 September 2011



THE WORLD BANK



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of the United Nations

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Director
Investment Centre Division
FAO
Viale delle Terme di Caracalla, 00153 Rome, Italy
or by e-mail to: Investment-Centre@fao.org



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All workshop documentations are available online
<http://www.fao.org/investment/newsandmeetings/meetings-archive/en/>



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EXECUTIVE SUMMARY

The Workshop's purpose and program

The purpose of the workshop was to offer a forum for the exchange of information and ideas on the evolving agricultural trade links between Latin America (LAC) and China. It was oriented towards identifying critical issues and developing suggestions that could provide an enhanced framework for guiding interventions by FAO, the World Bank and other international development agencies in support of an effective policy dialogue and better focused investment projects in Latin America in cooperation with China.

The structure of the workshop's program (see Annex) included presentations on (a) recent trends in world agricultural trade and the role of China, (b) public policy and private sector initiatives in China and Latin America with lessons from selected experiences, (c) trade opportunities, risks and challenges of China as a force in agricultural trade and investment with Latin America, (d) a panel discussion on agricultural trade and growth prospects, and finally (e) a brief presentation on conclusions and the future, out of which this present note derives. The power point presentations of all sessions are available on the web site of the Workshop at the FAO Investment Centre's Meetings Archives for "Promoting agricultural trade linkages between Latin America and China."

One important consensus that emerged during the workshop was with regard to the importance of incorporating China in a partnership relation with the LAC region, where the World Bank and FAO could play a key role as facilitators, in addition to their lending operations.

Ultimately, the initiatives that emerged from the interactions during the workshop should contribute to the following:

- (i) The promotion of deeper integration and trade relationships in primary and agro-processed products between China and LAC, including a regular policy dialogue framework.
- (ii) The definition of areas of cooperation between the private sector in the LAC region and Chinese counterparts.
- (iii) The attraction of more active direct foreign investments, at least by China in LAC, and perhaps by LAC in China.
- (iv) The closer cooperation in technological innovations between the LAC region and China.



Section 1

The background facts

The discussion provided a clear overview of the recent trends in production, consumption and trade flows between LAC and China in agricultural products (mainly based on the presentation of D. Hallam, complemented by the presentation of Caballero and Amado). Beginning in the late 1980s as a small player in world agricultural markets, during the last two decades China has become the world's fifth largest single importer and the world seventh largest exporter of agricultural products. China's overall trade (exports and imports) with Latin America – more precisely with Mercosur countries and to a lesser extent from Peru and Chile – has expanded rapidly, growing at a higher rate than any other global region. The LAC region has been the fastest growing agricultural production region in the world, and Brazil has played the predominant role with the fastest growing agricultural sector, driven in part by China's import demand. LAC agricultural exports to China are concentrated in a few products, mainly grains and oilseeds; although at considerably lower levels there is also a growing Chinese demand for LAC meat and dairy products, fruits and vegetables, forestry products and fisheries. According to ECLAC's statistics, Argentina, Brazil, and Chile account for over three-quarters of all LAC exports to China, agricultural and non-agriculture. In exchange, China's total exports to LAC, primarily manufactured products, have also grown rapidly, faster than exports to the rest of the world.

In presenting agricultural commodity trends in the next decade, FAO/OECD world price projections suggest that global demand for agricultural commodities will remain firm, with projections of real international prices remaining above their pre-2007/08 levels. These expectations of rising world prices for the major commodities such as oilseeds, wheat, corn, sugar, pulp, do not yet extend to non-

commodity, high-value products, such fruits and vegetables, nor to traditional tropical products, such as coffee.

If we look, for example, at soybeans and soybean oil, the single most important agricultural export product from LAC (exported by Argentina, Brazil, Bolivia, Paraguay and Uruguay), in 2008 China alone imported 40% of Brazil's exports and 79% of Argentina's. Overall, China has become the principal export market for Mercosur members, the largest agricultural exporters in the LAC region. China is also becoming increasingly important for Peru and Chile in fruits, fisheries and forestry products. (Chile is already a large exporter of minerals to China.) Thus, the main players in the dynamic trends in agricultural export growth to China are Mercosur countries who have notably changed their trading patterns to accommodate Chinese demand. There has been no significant expansion in exports to China of tropical products from Central America, Colombia, Ecuador, and Venezuela. One non-Mercosur exception is cotton from Mexico, which exports nearly 20% of its total cotton exports to China.



Section 2

Questions, challenges, growth prospects and opportunities

During the workshop presentations and discussions, various questions and potential problems were identified, mainly focusing on the current high export growth rates from Mercosur to China. But there were other concerns as well. The following brief list is not exhaustive of potential issues, but highlights important questions discussed in the workshop.

Exports to China concentrated in a few products and from a few South American countries.

Certainly for Mercosur countries, what happens to Chinese agriculture and domestic food consumption will have direct repercussions for agricultural growth. And this also applies although to a much lesser extent for Peru and Chile. But at present the main focus of China-LAC agricultural trade is on a few products. And a key fact is that currently, outside of Mercosur, the rest of the LAC region is for the most part not involved in dynamic exchange in farm products with China. Why? Could this change in the future?

Various aspects of the workshop discussion centered on Mercosur's having developed a highly competitive oilseeds sector, not only in primary production of grains but also in processing and exports. LAC has abundant land and resources, complementary to land-scarce and labor-abundant China, which should allow Mercosur especially to continue expanding oilseeds and exports at current growth rates. This expansion could continue, certainly due to land conversion, mainly from grazing (some from forests), and perhaps from yield increases.

There are, however, possible adverse consequences from expanding soybean production. The two main concerns raised were (i) the environmental effects associated

with long-term impacts on natural resources (clearing forest land), and (ii) the reinforcement of a trend toward farmland concentration in a highly mechanized production system. Although not developed in detail in the workshop, concern was expressed as to the extent to which the soybean export boom in Mercosur might represent a risk in terms of its environmental sustainability. The implications in terms of sustainability associated with a monoculture farming system and the clearing of native forest land associated with the expansion of acreage in soybeans, and its potential implications for water sustainability were raised as a complex and important challenge for Brazil, Argentina and Paraguay, requiring more analysis. The trend toward farmland concentration and mechanization, at least in Paraguay but perhaps elsewhere, is displacing farm laborers previously employed in other more-labor-intensive crops and livestock. The policy response options to these two sensitive and important issues were not examined in detail during the workshop but should be part of future policy analyses, perhaps financed by FAO, the IDB and the World Bank. Individually countries might investigate these questions in more detail as well, but the magnitude of possible problems varies between Mercosur countries as well as between regions within each country (e.g. likely to be more important in the north of Argentina than in the pampas).

Why not other products, such as dairy and meats? How to identify potential exports to China?

What have we learned about China as a potential market for high-value products (non-commodity markets), and for dairy and meat products? This question is of special interest for non-Mercosur LAC countries. Aside from grains, China is also becoming a large importer from a few South American countries in other products, mainly

non-commodities such as fruits and vegetables. As Daniel Conforte and Li Xiande emphasized in their presentations at the workshop, China is experiencing a major change in food consumption patterns, which is most notable in terms of the growth in per capita consumption of milk products and poultry especially (and of beef to a lesser extent). Although China is rapidly developing its domestic dairy and beef sectors, it still relies heavily on imported feed grains, and the capacity of domestic production to supply national consumption is uncertain, leaving the door open for an expansion of imports.

The recent dynamism of Chinese agriculture has led to the country becoming a strong competitor in some world markets, particularly for fisheries, some fruits and other higher valued products. China is importing fruits and vegetables from South America, but is itself becoming a competitor and in only a few years has become the largest exporter of apples, citrus and asparagus.

To understand the potential for LAC agricultural exports to China, one must have better information about future consumption patterns and the resource constraints that would influence internal Chinese supply, and thus import demand. During the workshop, Li Xiande and Changsheng Zuo both presented a diagnosis of the limited potential for land and water resources dedicated to agriculture. The increasing relative scarcity of land has led to a high level of inputs per hectare, notably in the case of fertilizers. Profits from grain production have been falling, in part due to the increased costs of agro-chemicals, and perhaps of labor. Future growth sectors in farming will likely be those less land-intensive. And so grains and pasture-based animal production are likely to grow slower than other sectors, opening opportunities for more imports.

On the one hand, addressing the question of diversifying the LAC export base to include more products and countries requires a clearer understanding of policy development in China, with emphasis on factors that influence production, consumption and marketing policies. This is where international agencies such as FAO and the World Bank can make use of their economies of scale in research and market analysis. What are the challenges and constraints determining agricultural competitiveness in

the rest of the LAC region, beyond traditional exportables such as coffee and banana? The livestock sector merits special attention, considering the rapid growth in internal and foreign demand, but the product list is much broader, including fruits, vegetables, pulses, potatoes, cotton, and other products. To the extent that China pursues a self-sufficiency strategy, as in the case of wheat and rice, what might that mean for imports of soybean products? It is not clear whether China could expand simultaneously on all these fronts, but a strategy to do so would probably require a restrictive trade regime on imports, raising tariffs and/or quantitative restrictions, and therefore increased internal prices (and maybe decreased world prices). What is the possibility of China pushing toward self-sufficiency more generally and what is the scope for sustaining such a policy? The new environment of dialogue between China and LAC will help to resolve these questions.

Is there potential friction with LAC if China's moves to become more self-sufficient in food?

There were some opinions voiced that suggested that the "severe" imbalance in agricultural trade might be unsustainable. China is importing far more agricultural goods from LAC than it is exporting to the region, and in terms of all trade partners China's agricultural trade balance has turned from a surplus before 2004 to a deficit today. But China's 18 thousand million dollars agricultural trade deficit with LAC (Zuo) should be compared to the country's 40 thousand million dollars surplus in all merchandise trade going to the LAC region. Of the total merchandise export surplus, most is due to Mexico, South America's value of imports from China approximately equaling what it exports. China's agricultural imports represent approximately 5% of China's total imports. So it is difficult to accept the unsustainability of the agricultural trade deficit from the point of view of import capacity. The force of the argument must lie in non-economic objectives, such as a strategic desire to avoid dependence on foreign food sources beyond levels currently observed. Regardless of the motivation, might China pull back from its present engagement with the LAC region as its source of oilseeds? A signal of this move would be increases in Chinese import tariffs, which

would indeed lead to policy friction between China and its main LAC agricultural trading partners, Argentina and Brazil.

Is an emphasis on primary products discouraging innovation in LAC? Is it raising productivity?

There were some disagreements in the workshop discussions, but in the view of some participants (e.g. O. Rosales) there might be limited spillovers associated with increased LAC agricultural exports to China. Unlike the decades-old period of Japanese trade expansion into Southeast Asia, which created greater intra-industry trade, there is limited evidence that the current trade expansion between China and LAC has produced much technological diffusion or knowledge spillover in agriculture and agro-processing. But there are some specific cases, including soybean production systems in Argentina, Brazil and Paraguay, where modernization of the industry was facilitated by expanding into a large export market, China playing a principal role as the importer absorbing much of this expansion. One question, in the spirit of the literature on trade and endogenous growth theory, that should be examined with some care is, How would LAC countries take advantage of the Chinese market for squeezing out productivity gains either in the production of primary products or in downstream and related activities? What might be the role of governments in discovering opportunities for such spillovers, and what might be the role of China in participating in this process, along with international agencies and private investors?

The small farm sector in Mercosur has been left out of the commodity export boom.

For the most part, this perception is true. The soybean production system is the most revealing case – produced on medium and large scale farms, it is highly mechanized, tending to replace other farm activities such as other crops and dairy production. These other activities tend to be more labor intensive, and so soybean expansion might displace small farms and reduce employment demand for wage labor. The situation varies across countries and regions in Mercosur. For example, in soybean areas in Paraguay, it appears that labor displacement has

occurred. In other products, as in the case of fruits, wine, and vegetable exports from Chile and Peru, farm production systems most oriented towards exports also favor medium and large farms, but nothing the size of the extensive soybean estancias. The value chain in fruits and vegetables tends to be labor intensive, both in terms of on-farm production and in terms of post-harvest selection, packing, transportation. It is mainly seasonal labor, which has a notable presence of women, and – contrary to a common perception – the season lasts five months or more. (Farms also have adopted a product mix such that the peak labor demand periods for each crop follow sequentially, thus avoiding abrupt, sharp shifts in demand for seasonal workers.)

The role of bilateral free trade agreements (FTAs) as marketing tool

One question that was raised in the workshop was, Are FTAs only relevant for promoting the exports of non-commodities? The exporters of commodities with deep international markets, such as wheat, soybeans and copper, tend not to face high tariff and other restrictions to market access. Non-commodity exports tend to face higher levels of tariff and non-tariff protection. The workshop discussed the possible lesson that might be had from the FTA between China and Chile, the only agreement in the LAC region that has been functioning for several years (Valdes). (Peru and Costa Rica have recently signed agreements with China.) FTAs could reduce uncertainty about market access for LAC exports, and could play a role in facilitating the reduction of non-tariff barriers and the protectionist applications of SPS restrictions. As a general trend, several countries in the LAC region have signed FTAs with the US, Canada and the EU. Is this a trend that could extend to China? Given the emphasis on commodity exports, the incentives to do so are less for Mercosur. Moreover, negotiating with Mercosur as a bloc would be complicated. For other LAC countries, however, with a recent history of signing agreements, such as Colombia and Mexico, a FTA with China would seem to be a natural step. It is interesting that, to date, China remains outside of the current negotiations under the Trans-Pacific Partnership Initiative, which would promote trade expansion around the Pacific Rim and which involve several LAC countries.

Other concerns

Although not developed in more detail, there were questions raised regarding various topics of more immediate interest. For example, there were questions surrounding the potential impact of the current financial (and macroeconomic) turbulence in Europe and the US, and the possible implications for world trade, for China's own growth rates, and for trade flows with LAC. Climate change, another issue, was not examined during the workshop but was mentioned as a factor to consider for further analysis. Brought up in several discussion sessions in the workshop were the current trend and outlook with respect to the recent currency appreciation observed in some LAC countries, and the possible repercussions for LAC's impaired international competitiveness in agriculture.

The issue of Chinese investments in LAC farmland was mentioned. Although not addressed in formal terms, there was a discussion of the World Bank's interest in documenting land transactions in part motivated by concerns regarding a lack of transparency in the foreign direct investments in farmland in some countries. Some participants from Brazil expressed doubts that China would become an immediate direct player in LAC farm production, given the radical differences between farming systems in the two countries. But two initiatives were raised that might contribute to direct Chinese farmland investments and participation in production: the Peruvian initiative of competitive bidding in public land auctions to enhance transparency, and the success of a New Zealand model of share-farming in dairy and livestock, which could attract investment in enterprises without buying the land outright.

Finally, John Nash noted that China's impact on global food has become so large that an increase in its own production could reduce pressure on world prices. He asked, however, Where would the domestic resources come from to expand domestic agriculture? In contrast to Mercosur, China would be unlikely to gain significant production from bringing more land under production; but perhaps some gains could come from increased irrigation and more intensive farming, sustainable either by domestic higher prices or subsidies. There is also the question of whether or not food self-sufficiency is always a good thing, considering the trade-off between promoting production and higher food prices. To an economist, the question becomes one of opportunity costs. Cell phones or soybeans? More generally this raises the issue of a better understanding in LAC of the dynamics of policy adjustments in China.



Section 3

Some final remarks regarding a framework for FAO and World Bank activities

The workshop did not aim at identifying specific investment opportunities in various countries in the LAC region related to China's increasing role as a destination for agricultural exports. Nevertheless, the workshop did offer a timely review of several potentially important components of what could become a new development agenda of cooperation and integration between China and LAC's agricultural sectors beyond the Mercosur soybean complex. With respect to the possible contributions of FAO and the World Bank, one area would be in the formation of a LAC regional strategy for public policy and investment in agriculture that would enhance, in the context of deeper integration with China, competitiveness of the sector while preserving the natural resource base.

As part of such a strategy, would be the facilitation of stronger links at the institutional level (public and private) between China and LAC. Policy dialogue, exchanges of information and specialists and entrepreneurs, technological cooperation and joint ventures are components of an effort to forge these links. One outcome would be to improve the business climate for Chinese investments in the LAC region, especially along the supply chain, not only at the farm and firm level but in agro-processing and marketing. Beyond the supply chains of specific products, Chinese investors might also be interested in infrastructure collaboration and other projects with possible spillovers going beyond primary agriculture. Although directly motivated by facilitating agricultural, investments in ports, roads, other transportation projects, irrigation schemes, power generation, and perhaps R&D, would have positive impacts on other sectors. It is noted that within Latin America, the infrastructure of terrestrial transport and energy networks linking countries (and even linking regions within countries) is poorly developed relative to the region's resources and potential for enhanced trade, despite decades of public statements by various government officials promising to improve such communications.

In the final discussions of the workshop, various ideas concerning governments' roles were examined. Part of the development agenda should be to elicit complementary public and private sector initiatives. What would be the drivers to orient government policies and to promote investments? How might FAO and the World Bank identify and enhance such drivers? It would appear that the private sector and the formal stance of the public sector in LAC region are relatively open to trade and to listen to and accept investments from foreign firms and governments. Where international agencies might be of help, therefore, is to aid LAC governments to translate their official policies into efficient practice, especially with respect to clear sets of rules and regulations (such as in SPS and foreign ownership of land). Also with respect to China there are likely to be high returns to facilitating the penetration of Chinese markets by LAC exporters beyond oilseeds. As the marketing reach of Southern Cone fresh fruit exporters to the US extended beyond the ports and Philadelphia to dealing directly with supermarket chains and distributors, so might the reach extend into China. But this requires the development of much information and institutional collaboration, and FAO and the World Bank could act as facilitators, and FTAs could play a role in such a strategy, particularly in non-commodity products.



ANNEX: WORKSHOP PROGRAM

LCSAR/TCIO workshop 2011 (expert consultation) Agricultural trade linkages between Latin America and China

FAO-World Bank Expert Group Meeting
Rome, 27-28 September 2011

Background

Recent FAO and World Bank studies indicate that developing countries' share in world agricultural exports increased from 32% in 1990/91 to 42% in 2006/07. Most of this gain came from expansion of exports to other developing countries (about 12%) while the share of their exports to industrial countries declined.

According to OECD-FAO projections, Latin America is the fastest growing production region and Brazil has by far the fastest growing agricultural sector, expecting to grow by over 40% by 2019, when compared to the 2007-09 base period. As stated by OECD-FAO, the developing and emerging economies which are enjoying increasing affluence with rising per capita incomes over a number of years, with population demographics and continuing urbanisation to mega population centres also reinforcing demand, are leading to significant changes in consumption and dietary habits, which explains the trade trends indicated above. This involves a transition from traditional staple foods and grains to more processed and prepared food products and convenience foods, containing a greater proportion of animal protein and with more fruits and vegetables in national diets.

China in turn, from being a small agricultural importer (1.4% of world imports in 1990/91), became the fifth largest importer at 5.4% of world imports in 2006/07 (US\$ 4.8 billion to US\$ 52.3 billion). But China has also increased dramatically its agricultural exports from US\$ 8.0 billion in 1990/91 to US\$ 36.9 in 2006/07 at 3.7% of world exports (Aksoy and Ng, 2010). It is the seventh largest exporter of agricultural products, just after Brazil. "... China has a large agricultural sector and large food economy. The performance in these sectors is of great significance for future outcomes in the rest of the world. As such, what happens inside China's borders will also affect the actions of policy makers globally." China is both a competitor and a dynamic market for Latin American products.

Workshop objective and output use

The workshop is organised by the Investment Centre Division of FAO within the context of the Cooperative Programme FAO-World Bank. It is intended as a forum for exchanging knowledge and latest case study information on the evolving agricultural trade linkages between Latin America and China and on the opportunities and challenges for Latin American economies.

The workshops results will be used to develop an enhanced framework for guiding interventions by FAO, the World Bank and other international and national development actors in support of better focused investment projects.

Programme

27 September 2011

Session 1: Recent trends in world agricultural trade and role of China

Chaired by **Suzanne Raswant**,

Chief, Latin America, the Caribbean, East Asia and the Pacific Service, Investment Centre Division, FAO.

Major issues to be discussed during this session:

- new agricultural trade patterns: increasing participation of developing countries while share of industrialised countries remained stagnated or declined;
- China's rapid increase in world share of agricultural imports and exports during the last twenty years — impact of China's large agricultural sector and food economy;
- emergence and consolidation of commercial and economic linkages between China and Latin American countries;
- asymmetric performance among countries in Latin America.

Start	End	
9.00	10.00	Recent trends in world trade of agricultural and agro-processed food products. David Hallam, Director, Trade and Markets Division, FAO.
10.30	11.30	Developments and patterns of trade in agricultural commodities between China and Latin America. Zuo Changsheng, Deputy Director-general, Agro-Trade Promotion Centre, Ministry of Agriculture of China.
11.30	12.30	Trade and investment relations between Latin America and China with special reference to agri-products. Osvaldo Rosales, Director, International Trade and Integration Division, ECLAC.

Session 2: Public policy and private sector initiatives in China and Latin America: Lessons from selected experiences

Chaired by **Ethel Sennhauser**, Sector Manager, Latin America and the Caribbean, World Bank.

Major issues to be discussed during this session are:

- policy and investment strategies to boost productivity and quality;
- value chain integration;
- public-private partnerships;
- trade governance and private sector perspective;
- impacts on factor markets (labor, land, natural resources, etc.) that the Latin America-China trade expansion have brought so far.

Start	End	
14.00	15.30	China is a market for Latin American agricultural products and is a competitor in agricultural world markets: presentations and panel discussion. Soy industry: Argentina and MERCOSUR, Marcelo Regunaga, Academic Director of the Agribusiness Unit, University of San Andres, Argentina. Dairy/beef industry: Uruguay and MERCOSUR, Daniel Conforte, Senior Lecturer, Massey University, New Zealand. Asparagus Peru and China, Geoffrey Cannock, Managing Partner, Applied Economics, APOYO Consultoría S.A.C., Peru. The private sector perspective, Jorge Domínguez, Origination Manager, Molinos Río de la Plata SA.

28 September 2011

Session 3: Trade opportunities, risks and challenges, China as a force in agricultural trade and investment with Latin America?

Chaired by **Thomas Elhaut**,

Director, Asia and the Pacific, IFAD.

Major issues to be discussed during this session:

- China's public investments in land and technology in developing countries and in Latin America;
- food security and productivity/efficiency impacts of trans-national government led investments –versus profit oriented company investments;
- the extent to which trade agreements, both existing and potential, are likely to shape future changes in trade policy and hence trade patterns between the regions;
- risks and challenges for the Latin American agriculture.

Start	End	
9.00	10.00	Issues around the free trade agreements. Alberto Valdes, Research Associate, Universidad Católica de Chile.
10.00	11.00	China's public investments in land and technology in Latin America. Antonio Buainain, Senior Lecturer of Economics, Institute of Economics, University of Campinas - Unicamp, Brazil.
11.30	12.30	Prospects and challenges of agricultural trade between China and Latin America: analysis of problems and opportunities from the Chinese perspective. Li Xiande, Director, Professor and Ph.D. Advisor, Institute of Agricultural Economics and Development, Chinese Academy of Agricultural Sciences (CAAS).

Session 4: Agricultural trade and growth prospects

The objective of this session is to confront the issues raised from different standpoints -government, private sector and cooperation agencies- with a view to summarise the trade prospects and highlight the challenges, the growth opportunities, the sustainability and the risks for different Latin American countries.

Start	End	
14.00	16.00	Roundtable Discussion Chaired by Alberto Valdes Panel members: Jorge Caballero-Cerutti, John Nash, Osvaldo Rosales, Jose Dominguez, Changsheng Zuo, Daniel Conforti. Open discussion.

Session 5: Conclusions and way forward

Alberto Valdes

The conclusions from the workshop will provide guidance in the development of a framework for investment planning.

Please address comments and inquires to:

Investment Centre Division

Food and Agriculture Organization of the United Nations (FAO)

Viale delle Terme di Caracalla – 00153 Rome, Italy

investment-centre@fao.org

www.fao.org/investment/