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THE ROLE OF BRAZIL IN REGIONAL TRADE

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Brazil's participation in international trade has developed prominence over the recent past. In fact, across CARICOM, Guyana and St Kitts and Nevis already have partial scope agreements with Brazil. In light of Brazil's openness to trade and its geographical closeness with CARICOM, the region should explore tapping further into the Brazilian market for trade in goods and also in services for which it is renowned. Through detailed data and case study analysis, this paper examines any potential for further trade in goods and services between Brazil and ECCU member states. The paper concludes that the partial scope agreement with St Kitts and Nevis affords the opportunity for other ECCU member countries to be assented to the agreement. Consideration should be given to the negotiation of a collective agreement for the OECS or CARICOM to deepen trade relations with Brazil, which may provide the avenue for export expansion and economic growth.

Keywords: Trade, Brazil, agreement

JEL Classification: F1

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[1] The authors wish to acknowledge the contribution made to this paper by the Permanent Secretary, Mr Charleton Edwards, and Trade Policy Adviser, Mr Andrew Satney, in the Ministry of International Trade, Industry, Commerce and Consumer Affairs in St Kitts and Nevis.

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1.0 Introduction

Literature on globalization posits that as a country becomes more integrated into the global arena through trade openness; that country stands to benefit from a myriad of opportunities for growth and development. However, the extent to which the country gains from these opportunities is hinged on its willingness and ability to adequately take advantage of same. The CARICOM region has been looking for new initiatives to spur growth and as a result has been building stronger alliances with trading partners, who may be able to offer possible synergistic relationships.

Brazil's participation in international trade has developed prominence over the recent past albeit at a slower pace than the other emerging economies. This turnaround has been attributed in part to strong domestic demand and a more stable economy. There are avenues in which the CARICOM region and more so the countries of the ECCU, can tap into the Brazilian market, one of which is trade in goods and services. As Brazil's economy expands and reaches a sustainable level, the demand for commodities is expected to increase. This growing demand may be satisfied by supply from the region, if these countries are so positioned to do so. Thus far, very few ECCU countries have considered deeper trade relationships with Brazil and though a number of factors may be responsible for that position, it may be useful to assess the opportunities in that market and the feasibility of the region's participation in same.

Through detailed analysis of macroeconomic data including trade indicators with Brazil and ECCU, the researchers will bring to the fore any potential for trade in goods and services between those entities, assess the feasibility of these opportunities and identify the policy initiatives that may be necessary to allow the ECCU to take advantage of these prospects.

2.0 Literature Review

The neoclassical model of international trade suggests that trade liberalization can affect economic growth through three main channels (Indiana University South Bend, 2007). The first channel is referred to as gains or benefits from exchange. It explains that as trade barriers are reduced and markets become more liberal, consumers accrue a number of direct benefits, particularly through lower prices. Also, producers gain from the opportunities to source their inputs at cheaper prices. The benefits by both consumers and producers contribute to improvement in overall economic activity in both the importer and exporter countries. Secondly, lifting barriers to trade creates the enabling environment for businesses to venture into investments outside of traditionally protected sectors, which may be much more profitable. By so doing firms can focus on doing what they do best, benefit from resulting economies of scale and maximize returns in the areas of their competitive advantage. Businesses are forced to compete with a larger pool of firms and may either become more competitive or exit the market if they are unable to survive.

Gains from globalization and trade liberalization may not be dynamic in the near-term as the impact from the distortion in prices caused by a closed market may linger. However, in the long-run as firms and businesses become globally competitive, there is greater efficiency in resource allocation and consumers enjoy the benefit of lower prices. Firms are now exposed to the international market and adapt quickly to advancement in technology, hence the need for more highly trained employees and a complimentary demand on the labour market, which fosters greater human resource development in a developing country. Trade liberalization will minimize the existence of monopolies, which are prevalent in some developing economies. Avenues are created for private investment, which forces infrastructural development and boosts economic growth. Thirdly, opening of markets encourages the interaction of market forces, enhances private sector development and diminishes the likelihood of state intervention.

A plethora of literature exists on the relationship between trade liberalization and economic growth, many of which conclude that as countries become more open, the economy benefits from increased value added (Tchamourliyski, 2002). The growth question is high on the agenda of the ECCU territories and therefore further liberalization of their markets, albeit at a gradual pace can augur well for these economies.

The global economic crisis has shifted attention to emerging market economies such as Brazil, which have not only been able to grow while advanced ones are contracting, but have offered hope for recovery from the crisis. Brazil's economy remained resilient during the recent global economic and financial crisis and over the recent past a large proportion of its populace has progressed into the middle class. Brazil has managed to pull some 35 million people out of poverty since the mid-1990s and it also became a top market for foreign automakers, retailers, and telecom companies.[2] Brazil is the largest economy in Latin America and is one of the most dynamic emerging market economies in the global economy.

Brazil is categorized by the World Trade Organization (WTO) as a major trading economy - a country whose share of world merchandise trade exceeds 1.0 per cent. The Brazilian market presents an opportunity in trade for economies such as the ECCU which are experiencing little or no growth. In his remarks at the Caribbean Growth Forum in the Bahamas in June 2013, the President of the Inter-American Development Bank stated that new trading partners could be found in the faster growing Latin American neighbours. He further stated that "had Brazil been one of the Caribbean's trading partners during the recent global recession rather than the United States of America or Europe, economic growth in this region would have been nearly 3.0 percentage points higher."

In the Final OECS Construction Sector Strategy Report, it was highlighted that small island states such as the OECS have the advantage of the geographical relevance of proximity to five (5) G20 states - USA, Canada, Mexico, Argentina, and Brazil. According to the Report, this geographic advantage allows for access to technology and possible establishment of transportation links for goods and services. This means that valuable air and maritime connections can be established between OECS member countries and the G20 states.

[2] Reuters, March 2014. Retrieved March 2014, 12, from http://www.reuters.com/article/2014/03/12/us-brazil-economy-slowdown-analysis-idUSBREA2B0N820140312

3.0 An Overview of the Economy of Brazil

3.1 <u>The Historical Economic Performance of Brazil</u>

The economy of Brazil is the seventh largest in the world and the largest in Latin America. On an annual basis, GDP growth in Brazil averaged about 3.1 per cent from 1991 to 2014, peaked at 10.1 per cent in the first three months of 1995 and contracted by 3.2 per cent in the first quarter of 1992. A number of large and robust sectors such as agriculture, mining, manufacturing and services play a substantial role in the Brazilian economy. The most significant contributor to GDP in Brazil is the service sector, which accounts for approximately 69.0 per cent of the total value of the economy in 2014. The second largest contributor is industry, accounting overall for 26.0 per cent of GDP and the remaining 5.0 per cent originates from the agricultural sector. Manufacturing is the largest segment of the industry sector and accounted for 13.0 per cent of total GDP in 2014. Following a strong performance prior to the recent global economic and financial crisis, the economy of Brazil suffered a blow as internationally, the demand for commodity-based exports declined and the level of external credit fell. Notwithstanding that setback, Brazil was among the first emerging economies to experience a rebound in growth after the crisis.

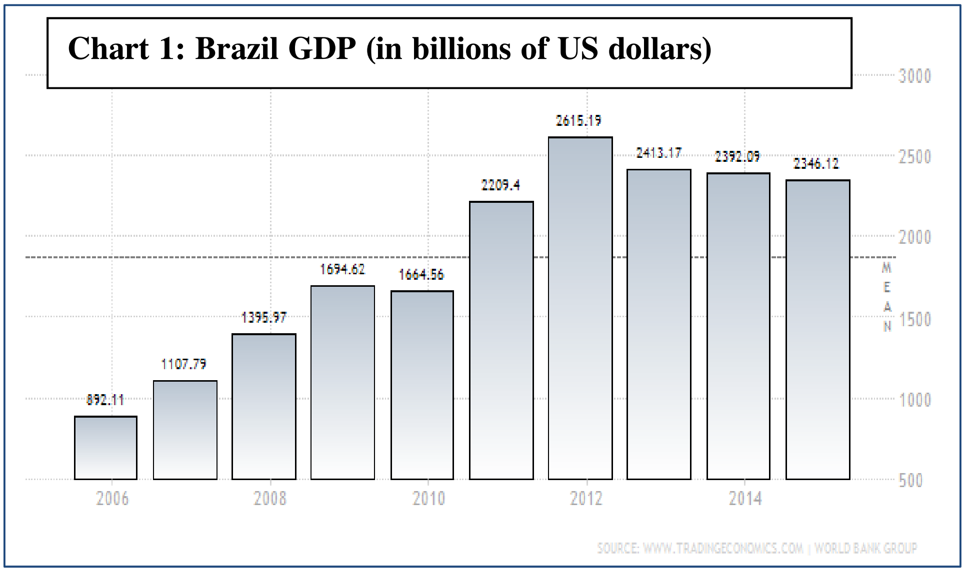


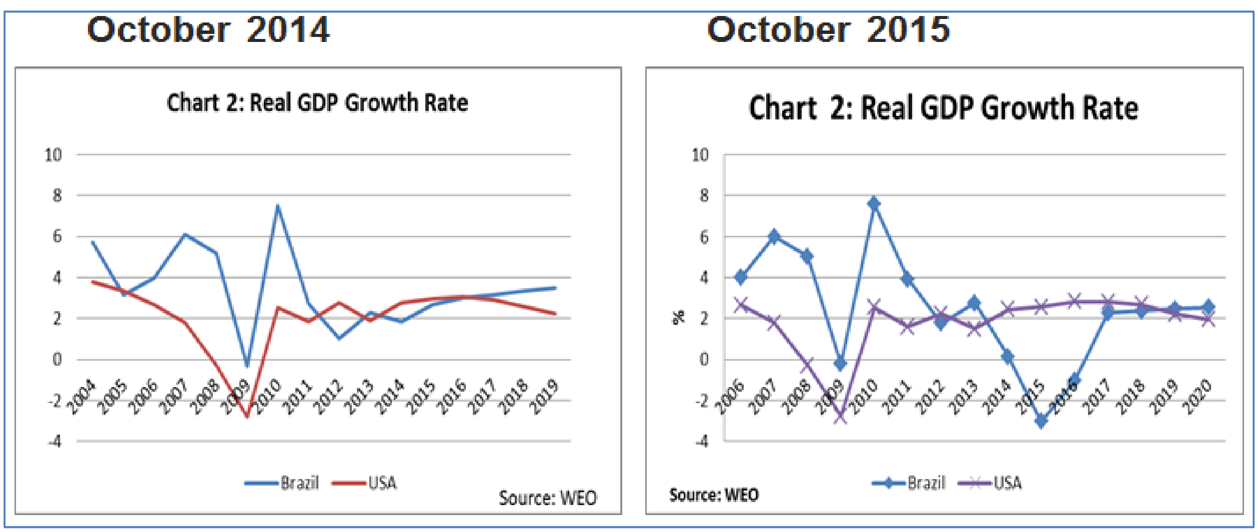
Chart 1: Brazil GDP (in billions of US dollars)

The Brazilian economy expanded by 1.9 per cent on an annual basis in the first quarter of 2014, following an increase of 2.2 per cent in the previous quarter, as a decline in investment was offset by an expansion in government expenditure. Agricultural production continued its increase from last quarter and registered 2.8 per cent acceleration as production of soybeans, rice, cotton and tobacco expanded. Industrial output contributed marginally, adversely affected by a decline in the manufacturing sector. The service sector most importantly recorded a second consecutive quarter of growth of 2.0 per cent.

Update: Economic activity in Brazil contracted by 2.6 per cent year-on year in quarter two of 2015, after recording a decline of 1.6 per cent in the first three months of the year. On a quarterly basis, activity fell by 1.9 per cent, the worst since 2008. The contraction was driven largely by a fall in investments (11.9 per cent). Household consumption and government spending fell by 2.7 per cent and 1.1 per cent, respectively. Also recording declines were manufacturing (8.3 per cent), construction (8.2 per cent), utilities (4.7 per cent) and services (1.4 per cent). By contrast, activity in mining and quarrying rose by 8.1 per cent and in agriculture by 1.8 per cent Notwithstanding the decline in overall activity, exports increased by 7.5 per cent in the April to June period, while imports decreased by 11.7 per cent.

3.2 Near Term and Medium Term Projections for Brazil

Chart 2: GDP Growth and Forecasts for the Brazilian Economy



When the growth performance of Brazil is compared with that of the USA, it is evident that real growth in the Brazilian economy has outpaced that of the USA, one of the main trading partners of the ECCU region. Brazilian growth seems to be generally moving in line with that of the USA, while remaining above, except for the years following the recent global economic and financial crisis; particularly in 2012 when growth in Brazil decelerated. Looking forward into the short to medium term, Brazil's growth rate stabilizes at just about 3.1 per cent on average, which is below that of the USA up to 2016, after which growth in the Brazilian economy is projected to be more robust than that of the USA. In this light, it is likely that demand will strengthen concomitant with economic growth and as a consequence a corresponding increase in imports into the Brazilian economy.

Update: As a result of weak economic performance in the first half of 2015, the International Monetary Fund – World Economic Outlook revised downwards its projections for the Brazilian economy for 2015 and 2016. Brazil is now expected to perform below the USA in these two years, but catch up by 2017. However, medium term prospects remain positive.

4.0 Profile of Trade in Brazil

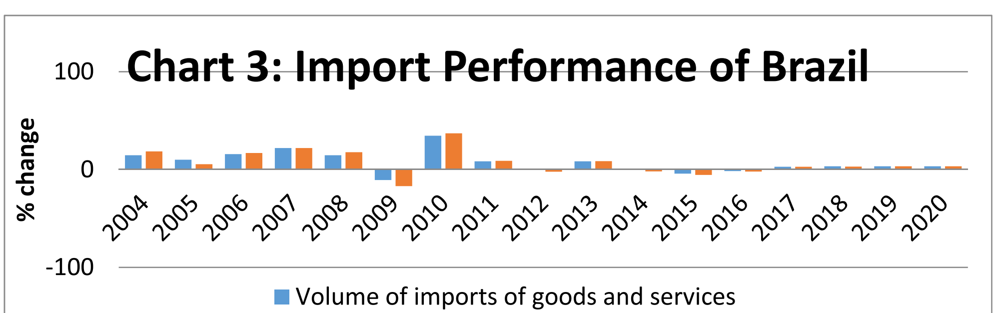
4.1 Trade Balances and Trade Partners

Brazil recorded surpluses on its merchandise trade balance (in goods) over the last decade (see Appendix – chart 11). In 2013, the merchandise trade balance recorded a relatively small surplus of US$2.6b. The largest merchandise trade balance was with MDG Latin America and the Caribbean at US$12.8b. The trade balance in services, however, has not fared that well. In 2012, there was a large trade in services deficit of US$41.0b (see Appendix – chart 13).

Brazil’s trade is diversified among its partners. Its main export and import partners are China, the USA and Argentina. These three countries accounted for 18.0 per cent, 12.1 per cent, and 6.3 per cent of total Brazil’s trade, respectively, in 2014.

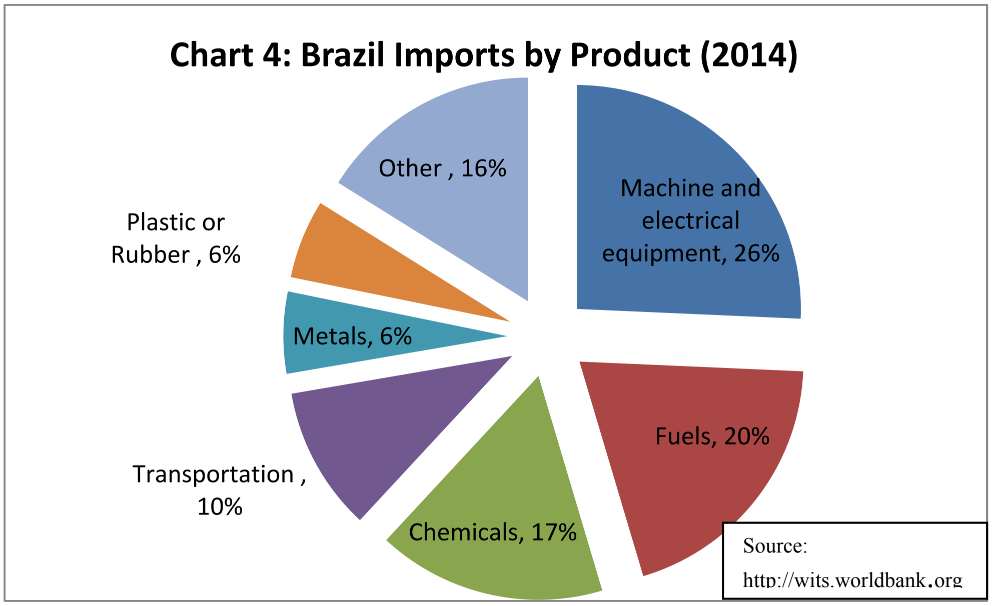
4.2 Imports

Over the last decade, the volume of imports of goods and services to Brazil has generally increased annually (see Chart 3). On the onset of the recent global economic and financial crisis, Brazilian imports of goods and services dipped in line with a sharp contraction



Source: IMF World Economic Outlook Database, October 2015 in economic activity in 2009 but recovered from 2010. Although contractions of 4.2 per cent and 1.5 per cent are forecasted in total imports for 2015 and 2016 respectively, import growth is projected following this two-year period, albeit at a slower pace than what existed prior to the crisis.

The products mainly imported by Brazil include machine and electrical equipment, fuels, chemicals, transportation, metals, plastic/rubber, clothing, food, vegetables, stone, glass and wood. In 2014, Brazil imported a total of 4,328 products from 215 trading partners. The most popular category of imports by Brazil in that year was machine and electrical equipment, which accounted for more than a quarter of the country's imports (see Chart 4) and was sourced largely from China and the USA.

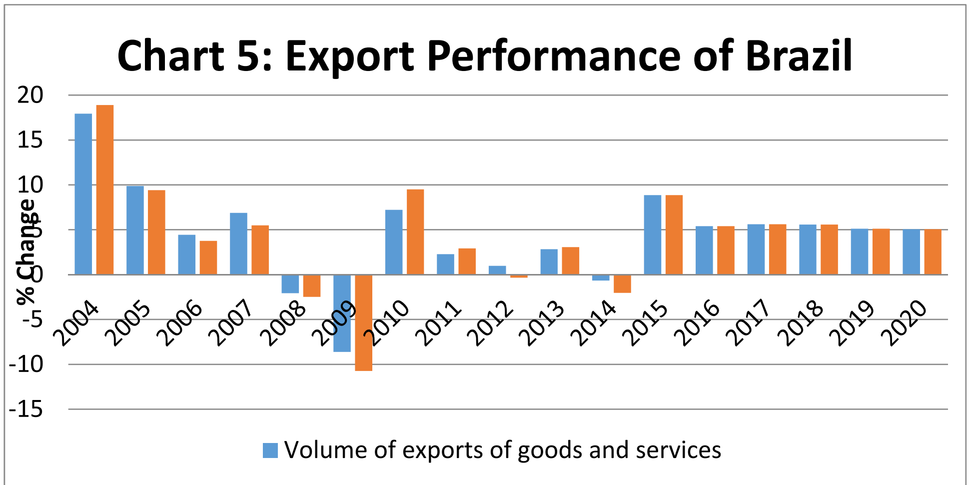


With respect to services, Brazil's imports seem to be concentrated in business and travel. "Other Businesses", and "Travel" were the two largest categories of services imported in 2012, accounting for 35.0 per cent and 27.5 per cent respectively of total services imported.[3]

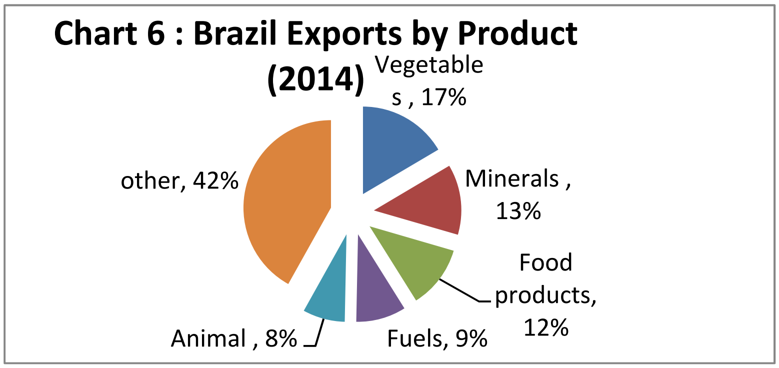
[3] Source: UN Comtrade and UN ServiceTrade

4.3 Exports

Over the last decade, the volume of Brazilian exports of goods and services has generally increased on annual basis. As a new export-oriented emerging economy Brazil has been able to gain access to a number of new markets. For the last five years, the volume of exports of goods and services has grown at an average rate of 2.5 per cent. The country experienced consecutive years of export growth in goods and services from 2004 to 2011 (see Chart 5), except in the years of the recent global crisis (2008-2009). Exports depend largely on shipment of raw material and intermediate products, which comprise over 60.0 per cent of total exports. A strong rebound - growth of 8.9 per cent - is anticipated in the volume of exports of goods and services in 2015. During the period 2016 to 2020, average annual growth of 5.4 per cent is anticipated in the volume of exports of goods and services.



Source: IMF World Economic Outlook Database, October 2015



Some of the major export products include aircraft, electrical equipment, automobiles, textiles, footwear, coffee, orange juice, soybeans and corned beef. In 2014, Brazil exported 4,036 products among 215 export partners. The single most popular category was vegetables which were exported mainly to China (see Chart 6).

In terms of services, "Other Businesses", and "Travel" have dominated trade. These were the two largest categories of services exported in 2012 accounting for 53.4 per cent and 16.7 per cent of exports respectively.[4]

4.4 Trade Environment and Policy

Brazil is a high income country which is fairly open to trade, although its openness is lower relative to other emerging market or developed countries (see Table 1). Its openness to trade indicator has remained relatively stable over time. The three year (2010-2012) moving average of openness to trade in Brazil was 19.8 per cent, relative to a moving average of 23.1 per cent recorded for the three year period 2003-2005.

Table 1: Openness to Merchandise Trade and GDP Per Capita for Selected Countries

Country	Openness to Trade (%)	GDP Per Capita PPP (in constant 2005 international $)
Brazil	27.6	14,555.1
Russia	50.9	23,564.2
India	53.2	5,238.0
China	50.2	11,524.6
USA	30.4	50,865.9
Canada	61.9	41,894.1

Sources: www.imf.org, http://wits.worldbank.org/openness-to-trade-visualization.html

Brazil's Hirschman Herfindahl index (a measure of the dispersion of trade value across an exporter's partners) was 0.09 in 2014, which means that that the country has a fairly diversified trade portfolio.[5] This score compares with that of China and the USA, which recorded 0.08 and 0.07 respectively, in that same year.

In terms of trading across borders (the ease of a business in Brazil to export and import goods), Brazil was ranked 123 among 189 countries in the World Bank's Group Doing Business 2015 report. This was lower than the regional average ranking of 86 for Latin America and the Caribbean. The ranking for Brazil was influenced by the total number of

[4] Source: UN Comtrade and UN ServiceTrade
[5] A country with trade (export or import) that is concentrated in very few markets will have an index value close to 1.

documents needed per shipment to import goods into the country (8); the time necessary to comply with all procedures to import these goods (17 days) and the cost of importing a container (US$2,323). In Latin America and the Caribbean, fewer documents are needed per shipment to import goods (7); more time is required to comply with all the procedures to import goods (18.7 days) and a smaller cost is incurred in importing a container (US$1,691.1).[6] Furthermore, in the Organisation for Economic Co-operation and Development (OECD) countries, some of which are the ECCU's major trading partners, fewer documents are needed per shipment to import goods (4); less time is required to comply with all the procedures to import goods (9.6 days); and reduced cost is incurred in importing a container (US$1,100.4).[7] This implies greater difficulty in trading with Brazil.

With respect to trade logistics, Brazil scored 2.94 in the World Bank's Logistics Performance Index (LPI) for 2014 on a scale of 1 to 5, with one being the lowest score and 5 the highest. Amid the categories of this ranking, Brazil scored higher on the timeliness of the shipment in reaching the destination within the scheduled or expected delivery time (3.39), but scored lower on the efficiency of the clearance process by border control agencies including customs (2.48).[8] The quality of the country's trade and transport related infrastructure (e.g. ports, roads, information technology) was ranked at 2.93 while its competitiveness and quality of logistics services (e.g. transport operations, customers brokers) ranked 3.05.

Overall, Brazil's business environment has improved over the last few years, which is a good sign for trade with other countries. The ease of doing business ranking moved to 120 in 2015 from 130 in 2013. Due to a number of trade agreements, trade facilitation improved in Brazil and has consequently increased opportunities for a number of countries.

Brazil is part of a number of preferential trade and free trade agreements since it places emphasis on its participation in the multilateral trading system to ultimately achieve socially inclusive economic growth. It is one of the WTO's most active participants and remains

[6] Source: http://www.doingbusiness.org/

[7] Source: http://www.doingbusiness.org/

[8]Source: http://lpi.worldbank.org/

committed to strengthening the multilateral trade system and also to successfully concluding the Doha Development Agenda (DDA), where it has presented, both independently and collaboratively with other delegations, a number of proposals related to, inter alia, agriculture, trade in services, intellectual property rights and trade rules. One of the country's objectives, as a founding member of the Southern Common Market (MERCOSUR), is to strengthen regional economic integration; and as such it has subscribed to preferential trade agreements with the Plurinational State of Bolivia, Chile, Colombia, Cuba, Ecuador, Mexico, Peru, and the Bolivarian Republic of Venezuela.[9] Brazil also has preferential trade agreements currently in force with India and Israel, separate and apart from those with other Caribbean countries.

The trade environment of Brazil is characterised by a combination of tariff and non-tariff measures. With regard to tariffs, Brazil had a total of 59 tariff agreements and a simple average tariff was 13.7 per cent in 2014. The number of non-tariff measures reached 57 in that same year. This level compares with the USA, a major ECCU trading partner, which, in 2014, had a total of 25 tariff agreements and a simple average tariff rate of 2.7 per cent.

5.0 An Analysis of the Partial Scope Agreement (PSA) with CARICOM Member States

5.1 The Case of Guyana

Brazil and Guyana signed a partial scope agreement in June 2001, which is the guiding principle for trade between these two countries. That original agreement expired in 2008 and prompted both countries to sign a protocol in August of that same year, which extended the Partial scope agreement indefinitely. That agreement took into consideration article 25 of the Treaty of Montevideo (1980), the Treaty of Chaguaramas (1973) and an MOU arrangement between MERCOSUR and Guyana (1999). The agreement aimed primarily at engendering bilateral trade between the two countries through tariff exchange preferences, trade cooperation and a higher level of private sector involvement in trade[10]. The two parties agreed to a number of articles on the agreement and to adhere to the terms as specified in these

[9] Source: https://www.wto.org/english/tratop_e/tpr_e/s283_sum_e.pdf

[10] Partial Scope Agreement between the Federative Republic of Brazil and the Cooperative Republic of Guyana

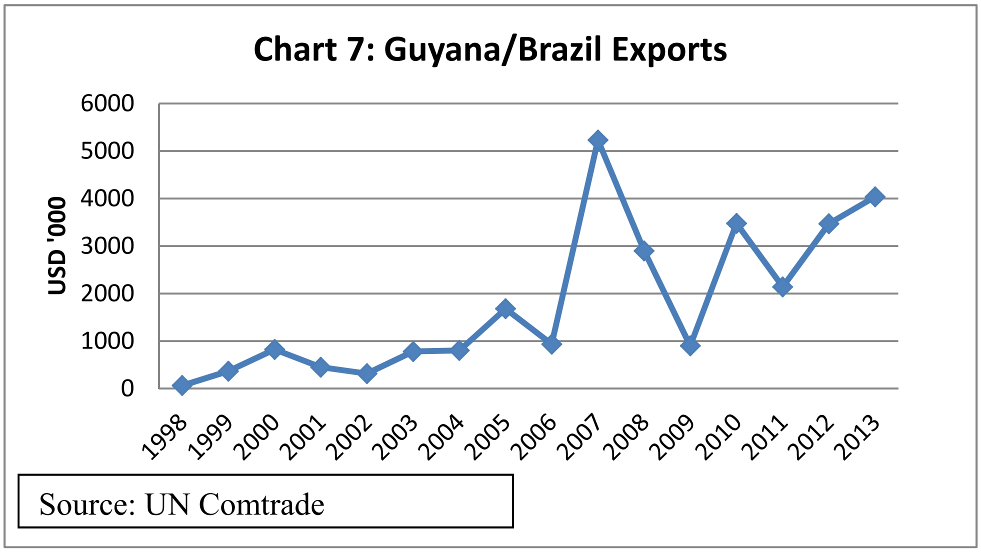
articles. Consequently, as stated in chapter three of the agreement, certificates of origin are required for each shipment of goods in order to determine its tariff preference.

Articles 24 and 25 allowed for the creation of partial scope as these portions addressed cooperation with a number of other countries and the level of access allowed. Article 25 made allowances for preferential treatment only in the case where the country's development was much less than that of Brazil, which created an advantage for Guyana. Therefore the agreement allowed Guyana 100 per cent preferential access to more than 100 tariff lines, including spices, meat wood products and corrugated cardboard. The reciprocal to Brazil was 837 lines of tariff to Guyana, which included meats, oil products and pharmaceuticals. Their degree of preferential treatment, however, ranged from 15.0 per cent to 100.0 per cent. The agreement became more relevant after the completion of the Takutu Bridge, linking the two countries (Guyana and Brazil) and consequently facilitating trade was completed in 2009.

A number of safeguard measures were also included in the agreement, which had to be renewed on an annual basis. These measures included suspension or reduction of preferences where it is believed that such preference can pose a threat to the domestic economy. Procedural guidelines for rules of origin of the products also formed part of the agreement. In order to originate from a territory, goods must be extracted, harvested or collected from that country or the country's economic exclusive zone, produced using raw materials found in the territory or materials from other countries but processed in the territory.

The partial scope agreement administered and managed by an Administrative Commission, established by both parties, with representatives from the Federative Republic of Brazil and the Cooperative Republic of Guyana, caters for future negotiations to include members of CARICOM. It forms part of Brazil's efforts to develop a better relationship with the region and have greater access to the regional market. According to Article 22, the Commission will inter alia, ensure compliance with the provisions of the agreement, provide recommendations for settling disputes, recommend amendments and encourage effective use of the agreement by the private sector.

Prior to the signing of the agreement between Brazil and Guyana in 2001, the value of Guyanese exports to Brazil averaged less than US$1m per annum. Major commodities exported were raw materials and stone and glass. Post signing of the agreement, Guyana's exports to Brazil more than doubled and continued on an increasing trend, notwithstanding the sharp decline recorded during the recent global crisis. An increase in export volume of the existing goods, coupled with the addition of a number of other commodities accounted for the improvement in exports from Guyana. Worthy of note is that Brazilian exports to Guyana more than doubled during the 2002 to 2012 period.



Source: UN Comtrade

5.2 The Case of St Kitts and Nevis

By 2009, the global economic and financial crisis forced manufacturing plants in St Kitts and Nevis to seek preferential access to new export markets, similar in size to their existing markets. Sales of the Federation's manufacturing sector had been impacted by the economic downturn in two of its major export markets, the USA and Europe. In light of its size and geographical location, Brazil seemed to be an ideal alternative export market. At that time, Brazil ranked highly among the emerging market economies poised for sustained growth, reflecting its potential as a viable export market.

Against this backdrop, St Kitts and Nevis successfully acceded to the existing Brazil - Guyana Partial Scope Agreement. The legislation which gave effect to and provide for the implementation of the Saint Christopher and Nevis, Guyana and Brazil Partial Scope

Agreement was passed on 15 July 2013.[11] The Agreement was ratified in 2014. It will become operational as the governments of Brazil and St. Kitts and Nevis prepare the administrative instruments to facilitate trade with the preferential concessions offered by the Agreement.

The main reason for negotiating this specific Agreement was the need for the Federation to increase its competitiveness in the world market. From the standpoint of St Kitts and Nevis, the goals of the Agreement were to have (a) access to South America's largest market for electronic goods produced in St. Kitts and Nevis and (b) an alternate import market base for high quality, reasonably priced goods, thereby reducing reliance on traditional imports from ageing and slowing markets such as North America and Europe.[12]

The accession to the existing agreement allows for Saint Kitts and Nevis to export (duty free) a number of items to Brazil, including agricultural crops, plywood, cardboard and nails. Although there is potential for St Kitts and Nevis to boost its exports of some agricultural goods and other items such as housing materials,[13] the Government of this country is however focusing on the development of the manufacturing sector, particularly increasing its exports of electronic items to Brazil with limited restrictions and cost-savings on freight. According to the Government of St Kitts and Nevis, there are 40 items to be accorded duty free treatment by Brazil to St Kitts and Nevis (see table 10 in the Appendix). These items include electrical components, coaxial cables and AC power controllers, some of which are produced in St Kitts and Nevis and are on Brazil's list of imported products. In addition to the indigenous manufacturers that produce some electronics (brushes, ballasts and other small electrical parts), there are four US owned manufacturing entities in St Kitts and Nevis. Together, the four US owned plants provide employment to approximately 913 employees.[14] All of these entities are engaged in the production of electronic components such as circuit boards, servo motors, cable television traps, resolvers, dimmer switches, and transformers. The parent company of the one of these four US owned firms in St Kitts and Nevis, already has a market presence in Brazil and is expected to expand exports to that market once the Agreement is finalised. As things stand currently, products from this company are shipped to the USA and

[11] Saint Christopher and Nevis, Guyana Saint Christopher and Brazil Partial Scope Agreement Act, 2013.
[12] The Working Draft of the National Manufacturing Strategy: 2012-2016, Federation of St Kitts and Nevis.
[13] National Manufacturing Strategy (2014-2020), Federation of St. Kitts And Nevis, July 2014
[14] National Manufacturing Strategy (2014-2020), Federation of St. Kitts And Nevis, July 2014

then to Brazil by the parent company. Upon implementation of the PSA, a direct consignment of goods to Brazil, with preferential treatment, is likely to yield reduced costs to manufacturers in St Kitts and Nevis.

St Kitts and Nevis stands to gain tremendous export revenue by tapping into this market - Brazil is the 16th largest importer of machine and electrical equipment in the world, importing US$58.9b worth of these products in 2014. An increase in export sales and employment creation seem to be the most significant benefits of the PSA in the short to medium term. When the PSA was under consideration in 2010, St Kitts and Nevis based exporters indicated the possibility to grow their international sales by a minimum of US$20m between 2011 and 2013 and create 125 new jobs within accession to the PSA.[15] The PSA can also lead to continuous growth in the manufacturing sector over time. Overall, the Agreement will directly impact the goods sectors as its provisions do not extend to services. Notably, services such as transportation; financial services; and wholesale and retail trade can be influenced through secondary multiplier effects.

Alternatively, the PSA also provides an import market to high quality, competitively priced goods from Brazil – in addition to sourcing goods from the traditional European and North American markets. St Kitts and Nevis already imports goods from Brazil such as poultry, wood, and furniture that attract little or no tariffs. In light of the reciprocity, the Agreement allows for Brazil to export goods to St Kitts and Nevis with tariff concessions ranging from 15 to 100 per cent. The goods which are expected to be agreed to for import by St Kitts and Nevis from Brazil are largely food items which already attract minimal tariff rates. Therefore, no significant revenue losses (from duties) are anticipated. In addition to the fiscal impact of the PSA, there is the threat that if Brazilian exporters divert a lot more of their global trade (including agricultural products) to St Kitts and Nevis then this can potentially lead to some displacements in the latter country's private sector. Table 2 outline some of the potential strengths, opportunities and threats of the Agreement to St Kitts and Nevis.

[15] Report provided by the Ministry of International Trade, Industry, Commerce and Consumer Affairs in the Government of St Kitts and Nevis.

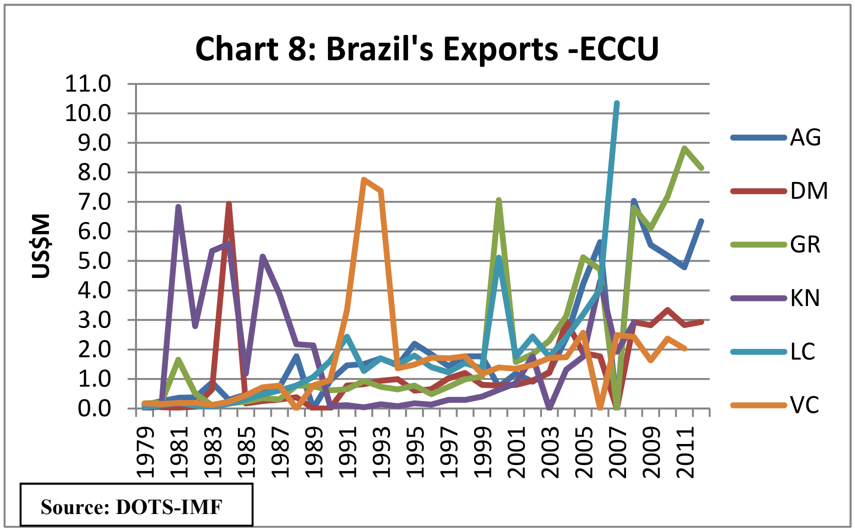
Table 2: The Strengths, Opportunities and Threats of Partial Scope Agreement to St Kitts and Nevis[16]

Strengths	Opportunities	Threats
- In line with the OECS Growth and Development Strategy. Manufacturing is a growth driver in the Strategy - Consistent with the current St Kitts and Nevis government focus on manufacturing led growth based on its 2015-2020 manifesto. - Promotes regional trade - In line with industrial policy in Brazil to promote the manufacturing sector.	- Provide a new market for enclave sector (foreign manufacturers) and indigenous manufacturers - Increase existing plant utilisation - Growth in domestic production; export sales; and foreign exchange inflows. Increase imports from Brazil in line with its projected increase in import demand over the medium term. - Expand plant facilities - Net employment creation - New products and technologies - Create significant linkages in the economy with the services sectors such as transportation, brokerage, and insurance. - Enhance the opportunity to attract new foreign companies and start new indigenous companies - Potential joint ventures between indigenous and Brazilian firms - Provide opportunities to expand carrier base and frequency - Could be used as a framework for future negotiations with MERCOSUR - Expansion of trade between Brazil and St Kitts and Nevis benefiting local producers and consumers. - Strengthen private sector cooperation between two countries. - Enhance profile for St Kitts and Nevis in International trade	- Risks tilted to the downside for Brazil economy. Downgraded forecasts for GDP growth and import growth in Brazil between October 2014 and October 2015 - Language barriers - Increasing cost of importing in Brazil - Increased competition from other suppliers of electrical components to Brazil such as China. - Greater complexity in the tax system for imports - Further depreciation in Brazil's currency, creating a more adverse impact on the demand for imports.

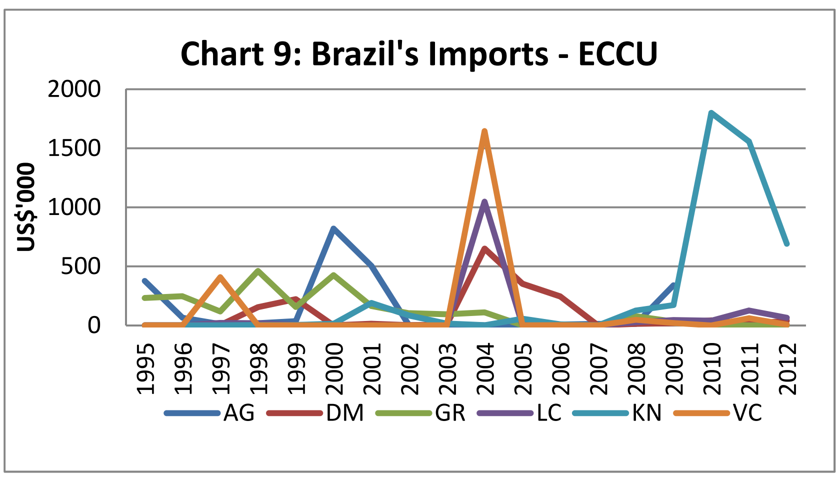
[16] Sources: "Overview of St Kitts and Nevis Manufacturing Sector", presented by Jose Rosa, General Manager, Kajola-Kristada Ltd, St Kitts and Nevis, 2012; and the Ministry of Trade in St Kitts and Nevis.

6.0 An Analysis of Trade Patterns between Brazil and ECCU Member Countries

6.1 Historical Trade Patterns



Trade relations between Brazil and the six independent members of the ECCU already exist from as early as 1976. Based on the Direction of Trade Statistics produced by the IMF, Brazilian export of goods to Grenada began in 1976, Antigua and Barbuda, Dominica and Saint Lucia since 1979, St Vincent and the Grenadines in 1980 and St Kitts and Nevis in 1983. Over the last three decades Brazilian exports to Antigua and Barbuda averaged about US$2.0m per annum, US$1.2m to Dominica, US$2.0m to Grenada, US$1.7m to St Kitts and Nevis, US$1.8m to Saint Lucia and US$1.6 to St Vincent and the Grenadines (chart 8).



On the import side, the ECCU territories started providing imports to Brazil in 1990, fourteen years after they began receiving goods from Brazil (chart 9). Brazilian imports from Antigua and Barbuda began (from DOTS) in 1995 and in the first three years imports averaged US$12.7m per annum[17]. From 1998, however, imports from Antigua and Barbuda started a decline and continued on that trend to average about US$0.2m between 1998 and 2012. Imports into Brazil from Dominica entered the records in 1997 and has since averaged US$0.1m per annum. IMF statistics also reveal that Brazilian imports from Grenada

[17] Data points for these first three years are not included in Chart 9.

officially began in 1990 and has averaged about US$0.1m annually up to 2012. Brazil imported from 1998, an annual average of US$0.3m from the economy of St Kitts and Nevis. Imports from Saint Lucia, which began in 1992, averaged US$0.5m over the period leading to 2012, with one abnormal year – 2004, having reported imports of over US$1.5m. When that anomaly is taken from the series imports into Brazil from Saint Lucia average just US$30,000 annually. St Vincent and the Grenadines from 1997 supplied Brazil with imports averaging US$0.4m per annum.

6.2 Potential Trade Relations

The trade complementarity index was used to determine the extent to which the export profile of the reporter, ECCU member countries and Guyana, match, or complement, the import profile of Brazil. A high index may indicate that two countries would stand to gain from increased trade, and may be particularly useful in evaluating the bilateral PSAs. The complementarity index can range in value from 0 to 100, with a score of 100 indicating ideal trading partners, while a score of 0 indicates that the two countries are perfect competitors. The mathematical definition of the index is as follows:

$$100 * \left[1 - \sum_k \left| \frac{m_{jk}}{M_j} - \frac{x_{ik}}{X_i} \right| \right]$$

Where x is the value of exports of product k from reporter country i, and X is country i's total exports. Partner country j's value of imports of product k is given by m, and its total imports value is denoted by M.

The results for the indices in Table 3 indicate that Saint Lucia and St Kitts and Nevis have the highest trade complementarity with Brazil in 2014.

Table 3: Trade Complementarity Indices for Independent ECCU Member States and Guyana with Brazil

Countries	Trade Complementarity Index for ECCU Territories and Guyana[18]		
	2012	2013	2014
Antigua and Barbuda	37.9	42.6	34.7
Dominica	57.5	60.1	47.9
Grenada	39.0	43.8	43.2
St Kitts and Nevis	50.2	61.0	51.4
Saint Lucia	58.7	50.4	59.6
St Vincent and the Grenadines	44.5	42.9	46.0
Guyana	32.1	33.7	29.7

Data Source: http://wits.worldbank.org

Although each individual country may not be equally successful with a Brazil trade agreement, in the context of a currency union, it may not be effective for each country to have a separate agreement with Brazil. The section in the initial agreement that allowed St Kitts and Nevis assent into a Partial Scope agreement with Brazil could be relooked with a view to making it a regional agreement. By doing so, countries will already have access to the Brazilian market in the event that they decide to strengthen their export base. Also, it may be possible to share production stages and collaborate to export final products to the Brazilian market from either St Kitts and Nevis or Saint Lucia[19]. It would therefore not be necessary for individual territories of the ECCU to renegotiate or to get the Brazilian authorities to agree to the necessary protocols. In that light, the authorities will have to decide in the production of which commodity or commodities that each country or a group of countries may have the competitive advantage and assign their export to Brazil accordingly.

[18] Authors' calculations using the Harmonized Commodity Description and Coding System 2012

[19] More thorough research needs to be done in that regard

An examination of the trade in goods shows that the ECCU is not positioned to produce most of Brazil's top imports and seemed very much aligned to import from Brazil in the future. Notwithstanding, ECCU member states can focus on commodities, such as consumer electronics, which are in high demand in Brazil and which they can provide without exorbitant initial outlays. According to the Euromonitor International of October 2014, consumer electronics in Brazil have performed well - sales of smartphones and tablets increased despite a deteriorating economy. The import demand for electronic integrated circuits, monolithic, analog or analog/digital, already exists in Brazil, and accounted for the fourth highest import of the country in 2013.[20] Demand for these goods is expected to be firm in the medium term, notwithstanding weakened prospects for the next two years. St Kitts and Nevis is already advanced in that it has the infrastructure in place for supplying these products to Brazil and tops the manufacturing sector in the ECCU. Consequently, the region should investigate how St Kitts and Nevis can partner with other ECCU member states to become a manufacturing bloc for these products. The success of this partnership will be dependent on the region's ability to achieve economies of scale and deal with issues such as high costs of labour and electricity.

The Federation of St Kitts and Nevis is already advanced in strengthening trade relations with Brazil. Since acceding to the PSA in 2014, St Kitts and Nevis has made all the necessary arrangements, including customs and excise administration, rules of origin, to qualify for tariff benefits into the Brazilian market. A number of manufacturers have expanded their existing plants in an effort to expand supply to meet the demands of the Brazilian market. The high quality of products being manufactured in St Kitts and Nevis sets the stage for standing to the competition in that market. A list of the products from St Kitts and Nevis to be accorded duty free treatment by Brazil is attached in the table 10 in the appendices. In spite of the forgoing efforts, a number of administrative delays in Brazil have hindered the completion of the agreement and therefore St Kitts and Nevis has not yet been able to accrue benefits from the PSA. In the meantime, Brazilian products like poultry/chicken, lumber and pesticides continue to enter the St Kitts and Nevis market. Notwithstanding these setbacks, the

[20] Source: UN Comtrade, 2015

authorities are positive that once Brazil's domestic issues are settled, St Kitts and Nevis stand to benefit tremendously from the PSA.

While awaiting the response of the Brazilian authorities, St Kitts and Nevis has been trying through bilateral discussions with the new administration and through the Brazilian Embassy to move the process forward. Since Guyana is currently experiencing some minor delays in specific areas, St Kitts and Nevis has also been partnering with Guyana to use their persuasive position to assist in ironing out the remaining issues. As a consequence, the authorities in St Kitts and Nevis are of the view that they should stick to the PSA for trade in goods only and could enter into another arrangement for services as time progresses. Their primary concern remains to grow the manufacturing sector as economic driver through greater penetration into new markets, cognizant that the older more traditional markets like the US, Canada and UK are maturing.

Transportation arrangements will also have to be considered with a view to getting the most efficient route/mode that would be convenient to all those involved. The countries within the ECCU with the transport infrastructure in place will have to consider serving as hubs to minimize transportation costs and maximise the benefits that can be gained from any agreement to export to Brazil. From the perspective of St Kitts and Nevis, the manufacturers have done intense marketing research and have partnered with shipping agents on achieving the more cost effective routes for the shipment of goods to the Brazilian market. The economy of Saint Lucia, which has a complementarity index of 59.6 per cent with Brazil in 2014, could also benefit from the manufacturing arrangements with St Kitts and Nevis. Saint Lucia's manufacturing sector has the capacity to expand supply in the short run and its exports of electrical products could be strengthened to facilitate a much needed boost in economic activity.

As noted, all the arrangements so far have involved trade in goods. Given the structure of the economies of the ECCU and the low trade complementarity indices of the other four independent territories with Brazil, consideration must be given to arrangements for trade in services. The service sectors account for a greater proportion of the region's gross domestic product, and therefore any negotiations for trade agreements, should seriously consider services. The potential exists to expand the scope to include services, particularly tourism, which has been identified as the lead transformational sector for the ECCU. Travel is one of Brazil's largest imports and ECCU member countries should try to capitalize on this source market. The Saint Lucia Tourism Authority has begun ground work for entering the Brazilian market, specifically targeting Brazil's off season. Progress has been made in the yachting sub-sector, and the Tourism Authority is positive that Saint Lucia stands to benefit from intensified marketing efforts in Brazil.

7.0 Main Policy Issues for Consideration

7.1 Trade Policy Considerations

Much potential exists in the ECCU to boost exports of a number of products, such as agricultural goods, indigenous manufactured products such as furniture, housing materials such as windows, railings, etc., condiments and confectionary; craft items; and traditional manufacturing exports. The operational phase of the PSA with Brazil would shed light on what exports will actually prove meaningful for the Brazilian market.

The potential for joint ventures under the PSA should also be favourably considered by all signatories to the trade agreement. The opportunity for joint ventures between indigenous firms in the region and Brazilian firms are worthy of pursuit.

The success of St Kitts and Nevis may not be easily replicated by other ECCU member states. Similar to St Kitts, the private manufacturing sector would have to play a leading role in increasing trade flows with Brazil. Furthermore, the public-private partnership cannot be overstated.

Negotiations on a one on one basis with each CARICOM member state and Brazil may not be desirable given the expense involved and length of time that may be required. Going forward, member states should investigate and work towards a CARICOM wide agreement with Brazil. If a CARICOM arrangement is not feasible, then an initial agreement between Brazil and OECS member states can be explored in light of the OECS Economic Union, with specific application of the experiences thus far of St Kitts and Nevis.

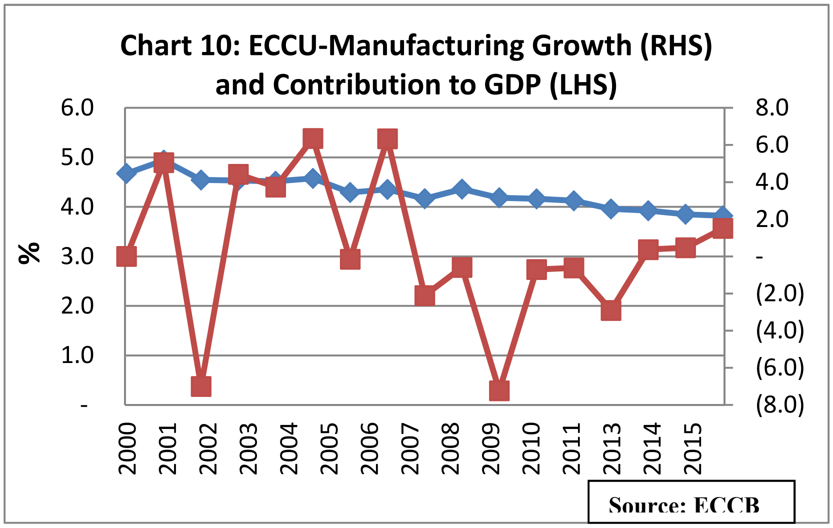
As South America's largest market, Brazil has the potential to open new doors to domestic and foreign-owned manufacturing facilities. Emphasis should be given to the enhanced trading opportunities that exist with exporting goods directly into Brazil with limited restrictions and cost-savings on freight. Consideration must also be given to the non-tariff barriers that inhibit trade between Brazil and the region.

It is noteworthy that the PSAs only involve goods, however, there exists opportunities for the Federation to leverage the current goodwill and deepen its ties with Brazil particularly in other sectors such as tourism.

7.2 Manufacturing and Growth Considerations

The ECCU has implemented a number of initiatives to spur growth following the global economic and financial crisis. While growth averaged about 3.5 per cent ex ante, the region has not been able to recover since the crisis and has grown on average by approximately 1.6 per cent. The initiatives have not taken root and authorities are left to relook existing policies in an effort to steer the economy on a sustainable growth path. The Commission on Growth and Development listed a number of features that were common to countries that were successful in achieving and maintaining high growth. Of these features is the ability to achieve rapid industrialization through deliberate policies that propelled the private sector to become more efficient and diversification in their manufacturing sector. It is important therefore to understand the channels through which growth in manufacturing impacts overall economic growth and the creation of jobs. Empirical research has shown a positive relationship between manufacturing growth and overall growth. South Africa experienced its highest growth in the 1970s, when its manufacturing sector grew at a higher pace than real GDP.

Manufacturing growth in the region has been rather volatile (See Chart 10), mainly negative, and therefore it is necessary to address manufacturing in the whole scheme of sustainable growth in the region. The opportunity to enter into agreements of that nature should be looked at in tandem with the need to grow the manufacturing sector, create employment and boost economic growth. Tapping into the Brazilian market should be seen as an opportunity for the region and should be taken in a holistic manner and negotiated at a regional level so that all members of the OECS economic union can benefit.



8.0 Conclusions and Recommendations

All the independent territories of the ECCU have existing trade relations with Brazil, some directly and some indirectly. These relationships can be strengthened to the benefit of trade and development in the OECS Economic Union. As an emerging economy, Brazil's middle income sector continues to expand in spite of a number of recent challenges. This expansion of the middle class creates a number of opportunities for the ECCU to deepen trade relations with Brazil and tap into what may be a lucrative market. The growing middle income sector in Brazil is also resulting in an increase in the demand for leisure. Additionally, the Brazilian market has a large appetite for the consumption of services, considering that the pace of expansion in the service sector increases annually. In that regard, services like tourism, the region's main transformational industry should be included in any agreement, whether PSA or otherwise, going forward.

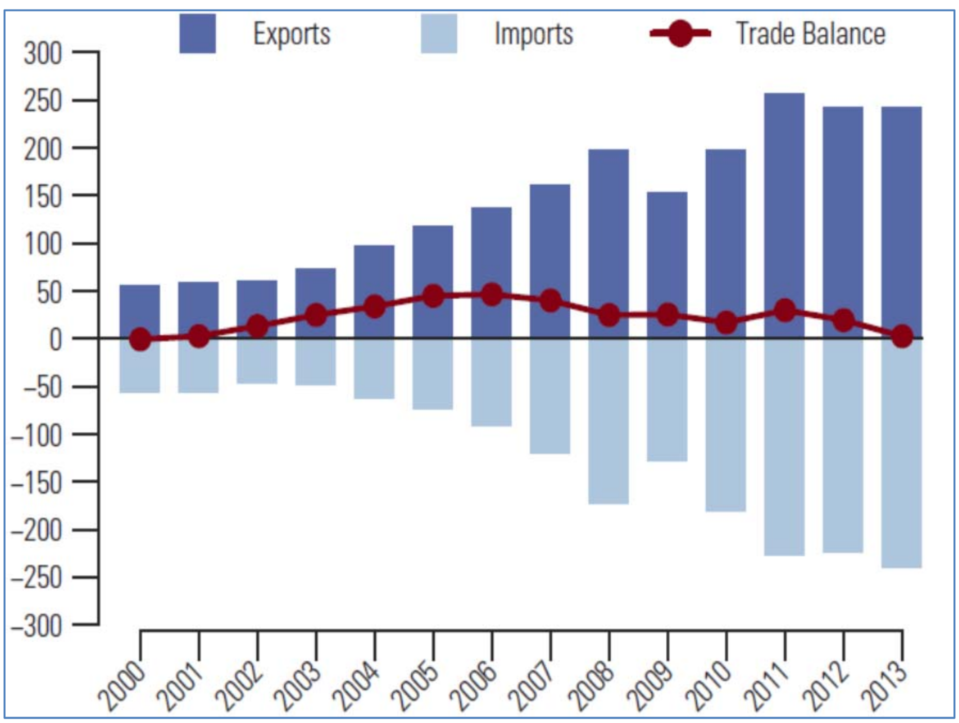
A number of the territories have been exploring opportunities for trade in services with Brazil. In the yachting sub-industry, for example, Brazilian yachts are becoming part of the annual yacht regatta held in Saint Lucia. Also, a number of trade expos have been organized in the

Brazilian market and as a consequence, yacht arrivals from Brazil to Saint Lucia have been on the increase and the tourism authorities are expecting improvement in the future. It may be possible to get these yachters to extend their stay in the region and visit other countries. Joint marketing and negotiations can be organized.

The groundwork is already in place and the ECCU needs to capitalize on any opportunities that may exist to strengthen growth in the region. The PSA with St Kitts and Nevis affords the opportunity for other ECCU countries to be assented to the agreement. In the effort to harmonize laws and regulations across the region, the authorities should negotiate a collective agreement for the OECS or CARICOM to deepen trade relations with Brazil and other countries or regions, which may provide the avenue for export expansion and economic growth. The region must learn from its past experiences and should therefore put the mechanisms and necessary framework in place for joint ventures as far as it's possible.

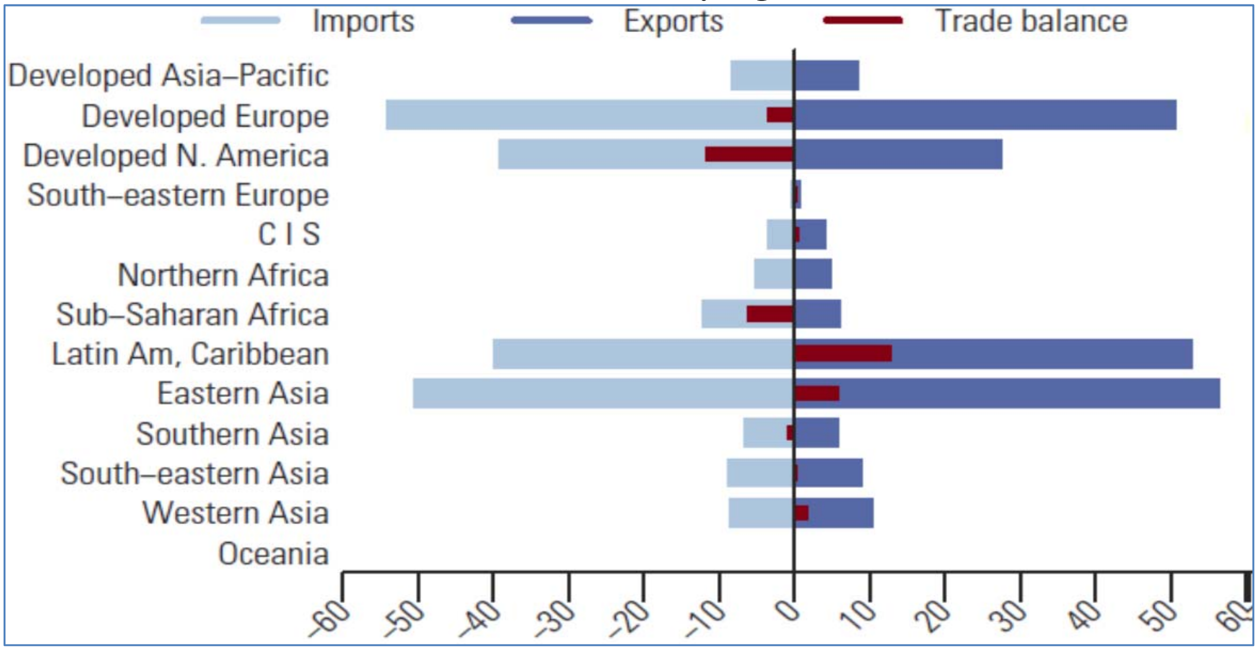
9.0 Appendices

Chart 11: Total Merchandise Trade in Brazil (in US$ billion)



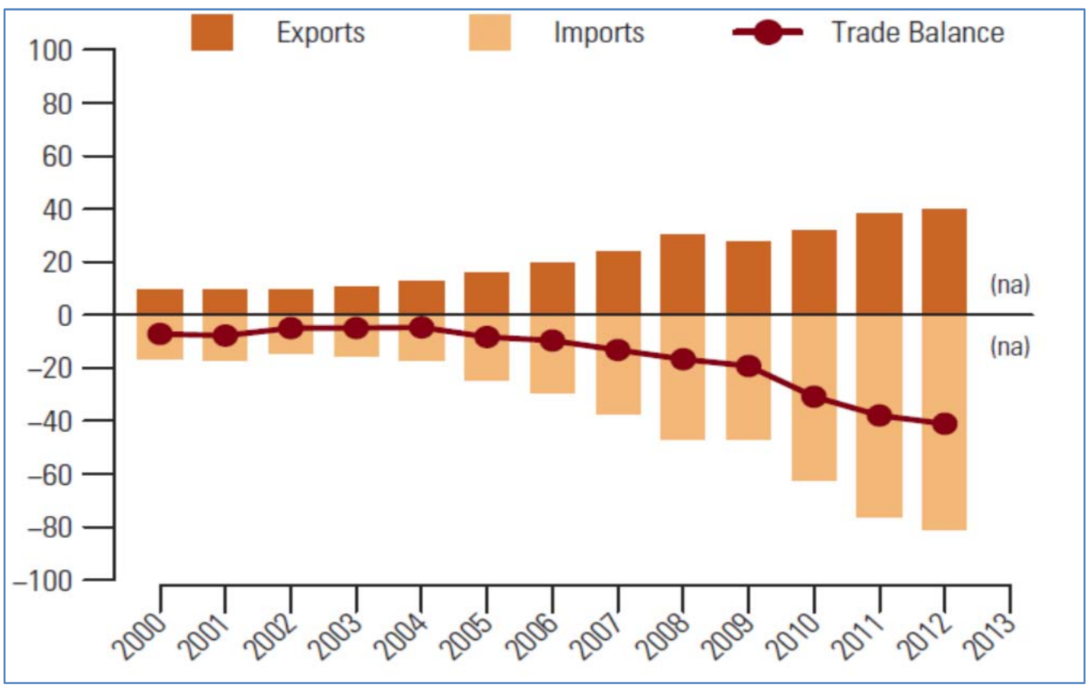
Source: UN Comtrade and UN Service Trade, February 2015

Chart 12: Merchandise Trade Balance in Brazil (by regions in US$ billion in 2013)



Source: UN Comtrade and UN Service Trade, February 2015

<u>Chart 13: Total Trade in Services in Brazil (in US$ b)</u>



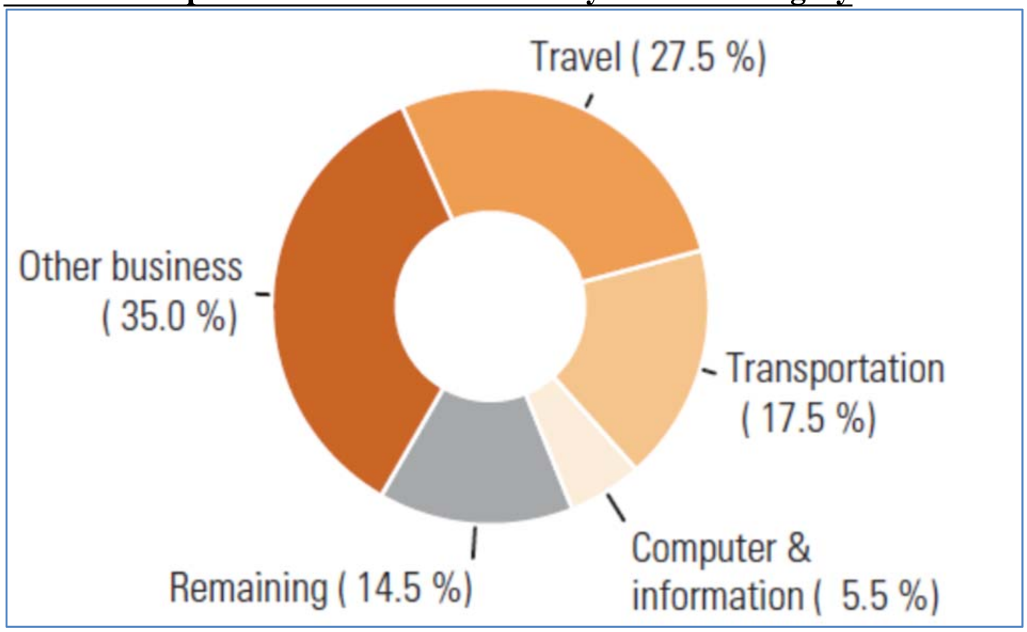
Source: UN Comtrade and UN Service Trade, February 2015

Table 4: Top 10 Import Commodities for Brazil from 2011-2013 (HS Code)

HS code	4-digit heading of Harmonized System 2007	Value (million US$) 2011	2012	2013
	All Commodities	226243.4	223149.1	239620.9
2710	Petroleum oils, other than crude	16905.1	16365.1	17757.0
2709	Petroleum oils and oils obtained from bituminous minerals, crude	14080.6	13405.8	16320.0
8703	Motor cars and other motor vehicles principally designed for the transport	11891.4	9566.7	9081.2
8708	Parts and accessories of the motor vehicles of headings 87.01 to 87.05	6317.6	6771.5	8296.7
2711	Petroleum gases and other gaseous hydrocarbons	4592.4	5959.6	7997.9
8517	Electrical apparatus for line telephony or line telegraphy	4599.6	3981.7	5036.2
8542	Electronic integrated circuits	4258.7	4139.3	4748.7
3004	Medicaments (excluding goods of heading 30.02, 30.05 or 30.06)	3490.5	3591.0	3734.3
8529	Parts suitable for use with the apparatus of headings 85.25 to 85.28	3448.5	3502.5	3565.7
3104	Mineral or chemical fertilisers, potassic	3533.0	3549.8	3356.1

Source: UN Comtrade and UN Service Trade, February 2015

Chart 14: Imports of Services for Brazil by EBOPS Category



Source: UN Comtrade and UN Service Trade, February 2015

Table 5: Brazil Imports by Sector 2009-2013

Sector	Average share of total imports 2009-2013
Chemicals	20.3 %
Minerals	18.8 %
Non-electronic machinery	14.2 %
Transport equipment	11.0 %
Basic manufactures	7.2 %
Electronic components	6.8 %
IT & consumable electronics	6.4 %
Miscellaneous manufacturing	5.0 %
Fresh food	3.1 %
Processed food	2.3 %
Textiles	1.9 %
Wood products	1.0 %
Clothing	0.9 %
Leather products	0.5 %
Unclassified products	0.0 %

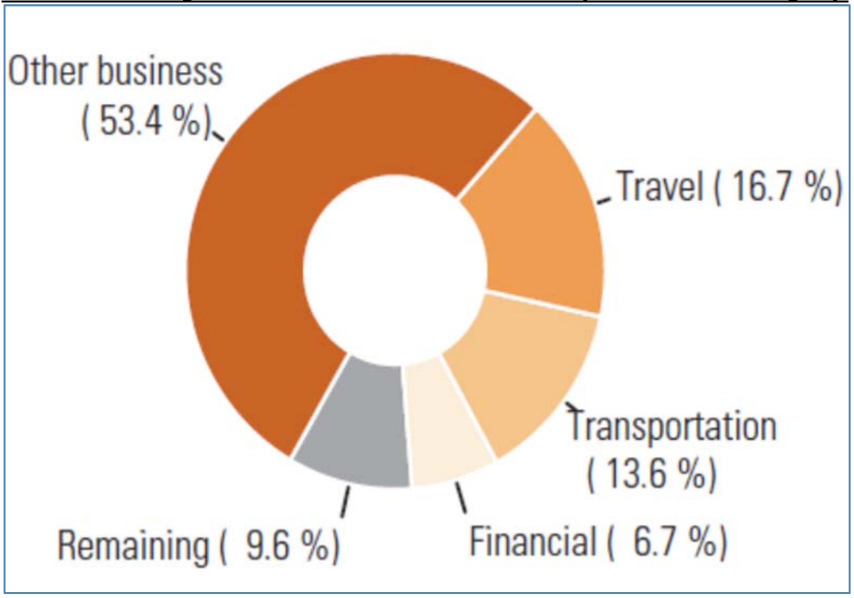
Source: International Trade Centre

Table 6: Top 10 Export Commodities for Brazil from 2011-2013 (HS Code)

HS code	4-digit heading of Harmonized System 2007	Value (million US$)			Unit value				SITC code
		2011	2012	2013	2011	2012	2013	Unit	
	All Commodities	256038.7	242579.8	242178.1					
2601	Iron ores and concentrates, including roasted iron pyrites	41817.3	30989.3	32491.5	0.1	0.1	0.1	US$/kg	281
1201	Soya beans, whether or not broken	16327.3	17248.3	22810.0	0.5	*0.5*	0.5	US$/kg	222
2709	Petroleum oils and oils obtained from bituminous minerals, crude	21603.3	20305.9	12956.6	0.7	0.7	0.7	US$/kg	333
1701	Cane or beet sugar and chemically pure sucrose, in solid form	14941.7	12650.8	11842.5	0.6	0.5	0.4	US$/kg	061
0207	Meat and edible offal, of the poultry of heading 01.05	7242.6	6948.0	7201.4	2.0	1.9	2.0	US$/kg	012
2304	Oil-cake and other solid residues	5697.9	6595.5	6787.3	0.4	0.5	0.5	US$/kg	081
0901	Coffee, whether or not roasted or decaffeinated	8026.4	5740.3	4598.1	4.5	3.8	2.7	US$/kg	071
9999	Commodities not specified according to kind	5067.9	5637.4	4837.8					931
1005	Maize (corn)	2716.4	5383.3	6307.6	0.3	0.3	0.2	US$/kg	044
2710	Petroleum oils, other than crude	4311.4	5367.8	4532.0	*0.7*	*0.7*	*0.6*	US$/kg	334

Source: UN Comtrade and UN Service Trade, February 2015

Chart 15: Exports of Services for Brazil by EBOPS Category



Source: UN Comtrade and UN Service Trade, February 2015

Table 7: Brazil's Top 5 Export and Import Partners in 2014

Market	Trade (US$ Mil)	Partner share(%)
China	40,616	18.04
United States	27,145	12.06
Argentina	14,282	6.34
Netherlands	13,036	5.79
Japan	6,719	2.98

Source: http://wits.worldbank.org

Table 8: Brazil's Top Exporters in 2014

Exporter	Trade (US$ Mil)	Partner share(%)
China	37,341	16.30
United States	35,299	15.41
Argentina	14,143	6.17
Germany	13,837	6.04
Nigeria	9,495	4.15

Source: http://wits.worldbank.org

Table 9: List of Manufactured Products to be Accorded Duty Free Treatment by Brazil in St Kitts and Nevis

No	Product Description
1	Resolvers
2	Electronic Inductors
3	Brush Block Assembly
4	Torquer Motor Assembly
5	Resolver Motor Assembly
6	Rotor/Stator Resolvers
7	Stator Bobbin Assembly
8	Rotor/Stator Lamination Assembly
9	Traps/Filters-KK
10	Export Trap Filters
11	Electrical Component
12	Import: Trap Filters
13	Coaxial Cable Connectors
14	Cyl Connectors
15	Connector Splices
16	Coaxial Cable
17	Cables w/ Phone Connectors
18	HDMI Cable
19	Fiber- Other
20	Speaker Wire
21	Digital Fiber Optic
22	Weather Seals – SUPS
23	Connectors
24	Jumpers
25	Jumpers Alternate
26	AK/Coaxial Cable Connector
27	Wireless Controls for Lighting/drapery
28	VMX Motor Starters
29	MVC Motor Starters
30	ABC Electronics Brakes
31	MWH Motor Heaters
32	RX Relays
33	AC Drives
34	AC Power Controllers
35	Conductors
36	Current Transformers
37	LV Transformers
38	MV Transformers
39	Fuse Tubes
40	Machined Heatsinks

Source: Ministry of International Trade - St Kitts and Nevis

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