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Special Economic Zone: A Path to Increase Brazil's Economic Position with Chinese FDI

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Abstract

This paper examines the creation of a Special Economic Zone (SEZ) in the city of Pouso Alegre (in the state of Minas Gerais, Brazil) as a way to attract Foreign Direct Investment (FDI) from China. The author's hypothesis is that Minas Gerais would receive more FDI if the right incentives were put into place. SEZs are such a tool to foster Pouso Alegre's economic and social development. This paper analyzes the micro and macro environments of the zone's strategic planning to understand the endeavor's viability and what this says about Pouso Alegre city's choice. The paper also presents Brazil's and Minas Gerais' economic backgrounds to showcase the investment opportunities already in place. This paper highlights how the economic measures necessary to implement the SEZ are a formidable route to reduce bureaucratic obstacles and promote international investment from places like China.

Keywords Special Economic Zone; Economic Development; Foreign Investment; Minas Gerais; Brazil; China.

Resumen

Este artículo examina la creación de una Zona Económica Especial (ZEE) en la ciudad de Pouso Alegre (en el estado de Minas Gerais, Brasil) como una forma de atraer Inversión Extranjera Directa (IED) de China. La hipótesis de la autora es que Minas Gerais recibiría más IED si se implementaran los incentivos adecuados. Las ZEE son una herramienta de este tipo para fomentar el desarrollo económico y social de Pouso Alegre. Este documento analiza los entornos micro y macro de la planificación estratégica de la zona para comprender la viabilidad del esfuerzo y lo que dice sobre la elección de la ciudad de Pouso Alegre. El documento también presenta los antecedentes económicos de Brasil y Minas Gerais para mostrar las oportunidades de inversión que ya existen. Este documento destaca cómo las medidas económicas necesarias para implementar las ZEE son una ruta formidable para reducir los obstáculos burocráticos y promover la inversión internacional desde lugares como China.

Palabras clave: Zona Económica Especial; Desarrollo económico; Inversión extranjera; Minas Gerais; Brasil; China.



1. INTRODUCTION

It is intriguing that Brazil, a highly regulated country full of potential investment opportunities, has not taken advantage of Special Economic Zones (SEZ) to improve its economic positioning while reducing the economic regime's inflexibility. Additionally, Brazil has unique resources that are not receiving adequate domestic investment due to either financial constraints or lack of technology. Furthermore, Brazil's economic and political instability entails a high regulatory risk level for foreign investors²⁴. This limits international financial investment. Overall, the country seems to be missing a chance to experiment with special jurisdictions and regulations which can increase prosperity, just like many countries around the world have already done. One of these countries is China.

China had enormous economic development in the past four decades due to testing economic policies in delimited areas, one by one. In a way, its experimentation was done as if it followed the Chinese saying "crossing the river by feeling the stones". Today, the government has learned from multiple policy experiments, even expanding the successful ones to the national level. The success of the initial four SEZs in Shenzhen, Xiamen, Shantou, and Zhuhai has led to the implementation of dozens of SEZs across the country. Despite Brazil giving its back to SEZs, China has proved to be a valuable commercial partner, even in moments of uncertainty. From 2008 to 2018, China's investment in Brazil amounted to USD 59.4 billion²⁵. Currently, there are several Chinese-led successful projects in action across Brazil, ranging from energy to industrial machinery production. Because Brazil has an extensive territory, and each of its regions boasts unique characteristics, Brazilian states

²⁴ "Foreign Investment in Brazil." Santandertrade.com, 2009, santandertrade.com/en/portal/establish-overseas/brazil/foreign-investment.

²⁵ "OEC - Brasil (BRA) Exportação, Importação, E Parceiro Comercial." oec.world. <https://oec.world/pt/profile/country/bra/>.



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have different needs and comparative advantages. Therefore, a one-size-fits-all solution for implementing SEZs would not work. For a country as diverse and large as Brazil, the Chinese experience of approaching investments with a regionalist strategy, understanding the needs and resources of specific states might be one that works.

This paper focuses on the state of Minas Gerais (MG), where Pouso Alegre is located, due to its significant economic and logistical advantages, its current positive growing trade with China, and the availability of natural resources frequently sought by Chinese companies. It is in this city where the Xuzhou Construction Machinery Group (XCMG) has decided to locate the Chinese lead, Pouso Industrial Park. Currently, some of Minas Gerais' biggest impediments for growth and further development are economic regulation, trade, and business tariffs. Hence, this paper argues for a robust and diversified approach to Special Economic Zones in Minas Gerais in order to mitigate these roadblocks. The creation of this SEZ can increase cash flow for the state and profitable opportunities for international companies and strengthen relations with China, the state's biggest trade partner.

Although Minas Gerais has relevant natural resources for Chinese companies (namely, minerals and renewable energy), the government could create a more favorable environment from the regulatory perspective, with tailored experiments for different regions within Minas Gerais, considering their comparative advantages.

This paper aims to study the viability of creating a SEZ in Pouso Alegre, a prosperous city in southern Minas Gerais, with China's Special Economic Zone expertise and its regional presence with Pouso Alegre Industrial Park. It concludes with recommendations on how to implement an Export Processing Zone in the state aimed at attracting more Chinese investment.

To elaborate on the project feasibility analysis and justify the city's choice and SEZ type, this article is divided into five macro sections: Special Economic Zones; Economic background; SWOT Analysis; Implementation of the new SEZ in Pouso Alegre; and Conclusion takeaways. The second section focuses on a historical perspective of SEZs and an



explanation of the concept. It also includes a discussion on the Chinese experience in the area, which elucidates China's background and unique know-how of using FDI to construct SEZs. The third section analyzes the Brazilian panorama, provides an overview of Minas Gerais State and Pouso Alegre City's Economic Potential. The strategic factors presented are based on economic, social, and political aspects. The fourth section elaborates a SWOT analysis of the city of Pouso Alegre. Lastly, the fifth section elucidates the process of creating the SEZ, justifies the choice for the specific type of SEZ here proposed for the city—an Export Processing Zone. Finally, the sixth section concludes with takeaways from the analysis.

2. SPECIAL ECONOMIC ZONES

The implementation of Special Economic Zones (SEZs) englobes public policy strategies, including various aspects of the region's social, environmental, and cultural life. A SEZ may have very different characteristics. Their structure and types are still a matter of intense academic discussion.²⁶ Generally, the main goal when creating a Special Economic Zone in a given country is not only to promote industrialization and structural transformation but also to attract foreign investment to achieve economic and social development. As per the definition of Thomas Farole, Senior Economist at the International Trade Department of the World Bank, SEZs can be generally described as:

...demarcated geographic areas contained within a country's national boundaries where the business rules are different from those that prevail in the national territory. (...) a business environment that is intended to be more

²⁶ Lotta Moberg. "The Political Economy of Special Economic Zones." *Journal of Institutional Economics* 11, no. 1 (2015): 167–90. doi:10.1017/S1744137414000241.



liberal from a policy perspective and more effective from an administrative perspective than that of the national territory²⁷.

The *Special* in Special Economic Zone derives from these extraordinary rules: extensive tax exemptions that tend to attract foreign and national investments. In doing so, they allow the economy within the Zone to flourish, with spillover effects. For example, new industries will employ several local citizens, the capital flow will enable the local progress, and logistical facilities will be improved, helping entrepreneurs move their products. The exceptions within the SEZ will depend on the type of SEZ, on whether the investment will be private, public, or a partnership, and on which sector of the economy will be contemplated. As per the table below, SEZs can increase FDI, foreign exchange, and exports:

Table 1: Potential Benefits Derived from SEZs

	Direct benefits	Indirect benefits
Foreign Exchange earnings	■	
FDI	■	
Employment generation	■	
Government revenue	■	
Export growth	■	
Skills upgrading		■
Testing field for wider economic reform		■
Technology transfer		■
Demonstration effect		■
Export diversification		■
Enhancing trade efficiency of domestic firms		■

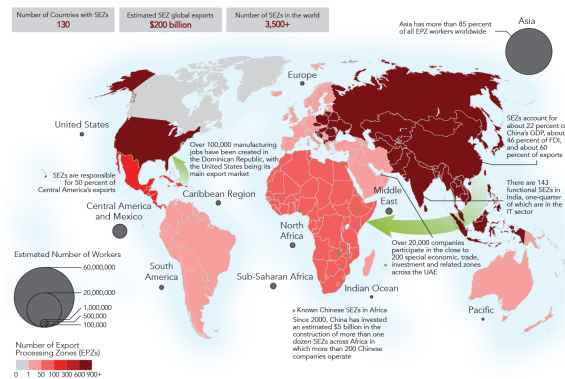
Source: Douglas Zeng, China’s Special Economic Zones and Industrial Clusters: Success and Challenges, 2012

²⁷ Thomas Farole and Akinco Gokhan, “Special Economic Zones Progress, Emerging Challenges, and Future Directions,” 2011, <https://openknowledge.worldbank.org/bitstream/handle/10986/2341/638440PUB0Exto00Box0361527B0PUBLIC0.pdf?sequence=1>.



A SEZ is frequently implemented in a location with some comparative advantage. This can be an abundant natural resource, a connecting area between highways and a cargo port or airport, or any component that can be exploited and refined. That advantage, along with local, geographical, and social assets, will influence the type of SEZ chosen. A given area can become more than one type of zone since they are not mutually exclusive.

Historically, Export Processing Zones (EPZ) were the first type of SEZ created to attract foreign investment in Europe. As shown in the map below, today, SEZs are present in Africa, Asia, the Americas, and Oceania. However, they are no longer limited to seeking FDI. SEZs can be used as small experiments for new public policies, as a way to foster systematic economic reforms, and as a complementary solution to encourage local employment.



World's Special Economic Zones. Source: Parag Khanna, "Special Economic Zones".

Globally, there are more than 5,400 SEZs, according to the 2019 World Investment Report. They have been studied and discussed already for 50 years. SEZs prosperity and development depend on their proper implementation. Currently, the most famous and economically successful Special Economic Zones are the ones located in China. These and other zones



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provide for worldwide excellent learning opportunities, which can be adapted to the national context, with careful and technical planning²⁸.

2.1. Chinese Experience

China was a closed and isolationist economy until Deng Xiaoping rose to power in 1976. To boost the economy, Deng Xiaoping implemented a series of far-reaching economic and political reforms. But Chinese growth mainly started when the government, focusing on increasing national production, began to allow controlled private initiative. In 1988, it was established that the private economy would be complementary to socialist doctrine. The state should protect the private sector's rights and interests by guiding, overseeing, and controlling the economy, a decision has proven to be a serious commitment to the country's economic growth. Finally, in 1993, it formalized the change from a “centrally planned economy” to a “market planned economy” and transformed State Enterprises into State-Owned Enterprises (SOEs), with independent operations and separate liabilities for profit and loss.

China started to shift from a mystery to foreign investors to an appealing destination for investment in the future. The reforms and the opening-up policies helped create the conditions that allowed China to become one of the fastest-growing economies in the world for decades and lift hundreds of millions of people out of poverty. Within this context, the SEZ's potential enhanced the demands for reforms, leading to more openness and internationalization.

Xiaoping's idea was to create SEZs as small-scale experiments within their territory. The government would then control their progress, constantly evaluating the next steps without threatening the national economy. There are valuable takeaways in the Chinese model, however, the conditions that made SEZs in China unique are hardly replicable

²⁸ UNITED NATIONS, “World Investment Report - Special Economic Zones,” 2019.



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elsewhere given the directives of the government: First, China showed the strength of a growing global economy and the focus on innovative models. Participating in the global economy was strategic and essential to China's growth, and SEZ was a great way to attract FDI. China needed to be inserted in the international scenario, which, in turn, forced the country to improve its productive sector, requiring a more skilled and efficient labor force. All those changes were boosted by the economic and technological development zones, free-trade zones, and high-tech industrial development zones implemented at the time. Second, envisioning a higher purchasing power and a better standard of living for the Chinese population the government focused on increasing productivity and maximizing economic incentives. Third, even with the adoption of a more open system, the Chinese Communist Party was still the ruling power in any instance, especially to continue to make the necessary adjustments. In other words, the Chinese government built the SEZs and provided the infrastructure that consequently attracted international companies and Foreign Direct Investment.

Hong Kong city is another compelling real-life case for a Special Zone, being a Special Administrative Region, and Deng Xiaoping noticed the economic success of this Chinese special administrative region governed by British laws and regulations. Much more open than the rest of Asia in general and China in particular, Hong Kong became an international hub for world companies and a pole of FDI.

In 1979, when the Chinese Central Government decided to create four Special Economic Zones in four coastal cities (Shenzhen, Xiamen, Shantou, and Zhuhai), the main goal was to attract foreign investment and make use of China's large reserve of labor. Despite the fact that the best implementation cases in the world were in China, not all the 2,543 Chinese zones were successful. Located right across Hong Kong's strait, Shenzhen is the most famous case; it developed from a village with 30,000 residents into a city of 1.2 million residents with the highest per capita GDP in China.



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The implementation of modernizing policies, such as SEZs, while taking China to a new level in the world market has also brought benefits to the Chinese population that are tangible to social inclusion, unemployment reduction, and Chinese per capita income growth. It is undeniable how this growth has in many ways been beneficial for many Chinese people. Today, many have better social conditions, increased life expectancy, higher purchasing power, and better employment rates.

- After profitably carrying out several SEZs nationally, China saw the possibility of investing in SEZs around the world. It started exploring creating SEZs in Africa. The Chinese government approved seven African SEZs to receive special funding as part of the global initiative's project, and six of them began construction in November 2009. But the Chinese government knew that SEZs should have different implementation processes. Therefore, Chinese officials considered favorable outcomes and issues from previous international implementations before creating new ones in Africa, resulting in more constructive relations.
- The Chinese government gave Chinese companies incentives to be the ones in charge of building and operating these zones for profit. However, these companies must compete for the government's subsidies. Additionally, it is their responsibility to invest their own money, decide the best location, and negotiate with the host government. As with many Chinese policy innovations, the zones are treated as an experiment, with a variety of approaches encouraged.²⁹

²⁹ Deborah Brautigam and Xiaoyang Tang, "China's Overseas Special Economic Zones: Aims and Objectives," December 5, 2011, <https://deborahbrautigam.files.wordpress.com/2013/04/2011-brautigam-chinese-investment-in-special-economic-zones.pdf>.



- In June 2019, as a result of this cooperation between China and different African countries, China announced more SEZs, strengthening the existing Overseas Economic and Trade Cooperation Zones³⁰. These movements exemplify China's interest in investing in various countries through SEZs, directly improving its economy and strengthening its international status. Chinese interest is often corresponded with by the recipient countries. Experts such as Douglas Zeng see the benefits of these models and recommend expanding these initiatives further, especially by Latin America employing domestic policies that favor skills improvement, technological adaptation, knowledge transfer, and innovative product development to materialize the benefits of China's investment

3. ECONOMIC BACKGROUND OF THE SEZ'S PROPOSED LOCATION

3.1. Brazilian Panorama

Brazil is the top destination for Chinese investment in Latin America. Since 2009, China has been Brazil's largest trading partner and the leading destination for Brazilian exports. According to data from the Brazilian Ministry of Industry and Foreign Trade and Services (MDIC), in 2017 Brazilian exports to China totaled USD 64.2 billion, while imports of Chinese products totaled USD 34.7 billion, resulting in a Brazilian surplus of USD 37.3 billion.³¹

As previously mentioned, obstacles when doing business in Brazil are excessive bureaucracy, high taxes, and heavy tariffs. These hinder not only Chinese investors as well as foreign and domestic ones. According to data from the World Bank, Brazil is one of the most bureaucratic countries in the world. It ranks number 124th (out of 190 countries) in the

³⁰ Aeabc, "China to Develop More Special Economic Zones in Africa," AEABC, June 9, 2019, <http://aeabc.org/china-to-develop-more-special-economic-zones-in-africa/>.

³¹ CEBC, "Comercio Bilateral Brasil- China 2018: Anos Recordes Balança Comercial," January 2019, http://www.cebc.com.br/arquivos_cebc/cebc-alerta/Ed%20108_2018_edi%C3%A7%C3%A3o.pdf.



Doing Business Index in 2019. On the other hand, China has been improving its position, ranking 31st in the same world ranking.³²

Brazil has one of the most complex taxation systems in the world.³³ It has over 60 types of taxes. According to the World Bank, Brazil ranks 184th among 190 countries in the Paying Taxes indicator³⁴. In 2018, a Brazilian citizen worked, on average, 153 days to pay the tax amount due. Recently, the population has been pressing for a revision and simplification of the system, which would immensely reduce the tax burden and represent a great victory for business. In 2019, a proposal was sent to the House of Representatives, and it is currently under revision. The 25th world's largest exporter in the world, Brazil is a competitive player in the commodity market, specifically in mineral extraction and agribusiness. These are areas in which Minas Gerais State excels. However, Brazil still has a long way to go to becoming an open global economy, despite its recent growth years. Creating special jurisdictions would result in more trade and promote access to international consumer markets and further FDI, all positive aspects for a country developing into a robust world economy. That said, Brazil's political risk has been a concern in the past for foreign investors, as government instability can harm profit and economic expansion. Simultaneously, heavy taxation also discourages new international capital flow. However, these taxes would not hinder SEZ, given the special concessions within zones for alternative taxation rules.

In economic aspects, Brazil's records and forecast trends display positive indicators. A strong GDP, coupled with growth expectations, assures Brazil's position among the top 10

³² "Ease of Doing Business in Brazil," Tradingeconomics.com (Trading Economics, October 8, 2019), <https://tradingeconomics.com/brazil/ease-of-doing-business>.

³³ "The Challenges of Tax Compliance in Brazil." International Tax Review. International Tax Review, September 25, 2017. <https://www.internationaltaxreview.com/article/b1f7n98fwrn4lj/the-challenges-of-tax-compliance-in-brazil>.

³⁴ "Paying Taxes - Doing Business - World Bank Group," www.doingbusiness.org, <https://www.doingbusiness.org/en/data/exploretopics/paying-taxes>.



in the GDP world ranking. In recent years, despite political and financial crises, Brazil has been experiencing a significant increase in its consumer market due to the swift change in the Brazilian social pyramid. Many Brazilian citizens moved from class D (total family income up to two minimum wages of around the USD 350) to class C (up to four minimum wages of around the USD 1,400). This social mobility has raised the purchasing power of class C and the middle class in general. Also, Brazil offers excellent operating conditions and a growing and young population. This would be appreciated by Chinese SEZ investors. A strong labor market is a key factor for decision-making concerning the Chinese SEZs outside of China.

3.2. Minas Gerais Overview

The state of Minas Gerais (MG) is the third richest state in Brazil, behind only the Sao Paulo (SP) state in first and Rio de Janeiro (RJ) state in second place. In Brazil's Southeast Region, these states collectively act as the industrial, agricultural, livestock, and service hubs. Minas Gerais is located in a privileged geographical position, with access to large consumer markets such as Sao Paulo and Rio de Janeiro. Neighboring the Center-West and Northeast Regions, it is the leading business corridor in Brazil. Also, MG has the most extensive road network and the second-largest rail network in Brazil.

Another focal point of MG's attractiveness is its easy access to Brazil's most important cities and ports. The state has forty-four airports and the largest road network in Brazil, 2,500 km or around 16% of the country's total. Minas Gerais used to have approximately 8,700 km of the railroad network, but now 6,200 km are unused and without any maintenance. Yet, this railroad carries the potential for future economic development with the right infrastructure improvements.

In southern Minas Gerais, Pouso Alegre's city acts as a strategic trade point, as it has been historically the main connecting area between Minas Gerais and Sao Paulo state. The



historic trade settlement that later became Pouso Alegre originated from the commercial exchange between the two states. Pouso Alegre is also one of the main trade routes between the two states and within other regions in MG.

3.3. Pouso Alegre Potential

Pouso Alegre is a prosperous city, having the main road interchange in southern Minas Gerais, cut by five highways, three state roads, and two federal roads. Pouso Alegre is only 110 km from the interstate that directly connects major consumer city centers. The city is strategically located 400 km from Belo Horizonte (capital of MG), 286 km from Sao Paulo city (capital of SP state), and 386 km from Rio de Janeiro city (capital of RJ state). These logistic and geographic considerations played an important role in picking the city to receive the XCMG Industrial Park. Industrial Parks are manufacturing and production areas planned and zoned for industrial development. In the combined efforts between the two countries, China supplies the financial investment, while Brazil provides a local labor force and a large consumer market. XCMG Pouso Industrial Park was the first Chinese machinery-oriented construction in Brazil, representing an exciting opportunity for all parties involved.

In June 2014, financed by FDI from Xuzhou Construction Machinery Group (XCMG), the Park started operations to encourage bilateral cooperation. The facilities link the industry, research & development areas, storage, distribution systems, nearby suppliers, and financial services. The XCMG Park has bridged investments from China and local companies, leading to economic and trade expansion. The Park is exclusive for XCMG, that is, it is not open to any other company interested in investing in MG.

In the past six years, the agreement has grown into a much larger partnership. In January 2020, the XCMG group decided to open an investment bank, the first investment



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bank in Brazil with 100% foreign capital, to further enable business in the area and sector.³⁵ The creation of the Pouso Industrial Park has also overcome some of the impediments that prevented economic growth in Brazil and Minas Gerais; since its special jurisdiction allowed for reduced bureaucracy and taxes.

Receiving substantial Chinese FDI has led to positive spillover effects in neighboring regions. XCMG Brazil has taken part in nearly 200 social welfare activities and projects ranging from disaster relief, education, and poverty alleviation.³⁶

Many national and international companies, such as the Indian ACG Worldwide, the multinational Unilever, and the Swiss Arysza, are attracted to the Pouso Alegre region because of logistical accessibility and strategic location. Yet, no company uses today the entire logistics chain advantage. These advantages bring about a significant opportunity that any company could take in the new proposed SEZ.

4. SWOT MATRIX

The fact that XCMG has implemented an Industrial Park in Pouso Alegre is per se a strong indicator of the valuable investment opportunity the city exhibits as a destination for FDI. As the paper proposes a more robust and open type of SEZ in Pouso Alegre to attract more

³⁵ “Grupo Chinês Anuncia Investimentos Em Minas Gerais,” agenciaminas.mg.gov.br (Agencia Minas, January 7, 2020), <http://agenciaminas.mg.gov.br/noticia/grupo-chines-anuncia-investimentos-em-minas-gerais>.

³⁶ XCMG. “XCMG Pouso Industrial Park in Brazil Becomes China’s First Construction Machinery-Oriented International Economic and Trade Zone.” [Prnewswire.com](https://www.prnewswire.com/news-releases/xcmg-pouso-industrial-park-in-brazil-becomes-chinas-first-construction-machinery-oriented-international-economic-and-trade-zone-300966761.html), November 29, 2019. <https://www.prnewswire.com/news-releases/xcmg-pouso-industrial-park-in-brazil-becomes-chinas-first-construction-machinery-oriented-international-economic-and-trade-zone-300966761.html>.



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Chinese investment and other Chinese companies to Minas Gerais, the SWOT Matrix will be used to explore the city's strategic factors.³⁷

The Strengths (S), Weaknesses (W), Opportunities (O), and Threats (T) matrix is based on the internal context for S and W, on the one hand, and the external environment for O and T, on the other. SWOT is a guideline for understanding the current reality to decide how to proceed with a strategy. It is a framework used to analyze from a company department to entire organizations, sectors of the economy, regions, countries, and continents³⁸.

The internal context (S and W) will consider Pouso Alegre and all factors that can directly impact or influence a new type of SEZ construction in the city. Strengths are positive aspects, which are critical for a successful SEZ construction. In short, they include all the competitive advantages, resources, and valuable assets that the city has to offer. Weaknesses are vulnerabilities and potentials that must be improved to provide adequate conditions for this undertaking such as excessive taxes and bureaucracy.

As for the external environment (O and T), where the city can influence but not directly impact, nearby towns and the surrounding region will be contemplated. Opportunities represent possibilities to invest and capitalize that have not been addressed, such as a new market niche, new customer demands, or loss of competitors. Threats, contrarily, are the roadblocks that could harm a SEZ's progress in Pouso and may affect the project's financial viability. Once the threats have been identified, they can be simply monitored or may require a counteraction.

³⁷ * All data used represents the most currently available indicator.

³⁸ Skye Schooley, "SWOT Analysis: What It Is and When to Use It," Business News Daily, June 23, 2019, <https://www.businessnewsdaily.com/4245-swot-analysis.html>.



4.1. Strengths

Pouso Alegre is an excellent place to do business, ranking 29th among the country's best cities to make investments. In the state of Minas Gerais, Pouso Alegre is second only to the capital, Belo Horizonte, according to the annual study carried out by Urban Systems that has 42 indicators and four focus areas: economic development (maturity and growth of the city), human capital (related to professional qualification and training of labor), social development (a social reflection of the development of the town) and infrastructure (essential for business development).³⁹

The business development in the region has attracted large pharmaceutical and logistics industries to Pouso Alegre, also due to the municipality's strategic location. Minas Gerais is the corridor of Brazilian cargo flow; within the state, Pouso Alegre has a uniquely well-located position, making it one of the six MG's dry ports - a Bonded Area and Inland Customs Unit (as shown in the map below). Bonded Areas are a type of SEZ closely related to Free Trade Zones as these commercial hubs receive and store (free of charge) products for exchange in the bonded warehouses. The central difference is that a Free Trade Zone is exempt from customs laws and regulations while a Bonded Area is not.⁴⁰

³⁹ "Melhores Cidades Para Fazer Negócios," Urban Systems (Revista Exame), <https://www.urbansystems.com.br/melhoresidadesparanegocios>

⁴⁰ Douglas Zhihua Zeng, "Special Economic Zones: Lessons from the Global Experience" (Private Enterprise Development in low-income Countries), <https://bityli.com/WhNmD>



Ports and Dry Ports in the Southeast Region. Source: Davyson Demmer and Fabio Alves, “Why Minas Gerais,” INDI

These logistic and geographic considerations played an important role in why the city was picked to receive the XCMG Industrial Park. Yet XCMG is not the only significant foreign company in the city. The Indian pharmaceutical multinational ACG Group opened a unit in Pouso Alegre in early 2019, and today it is the largest empty capsule manufacturing plant in Latin America and the most advanced in the world⁴¹. Brazilian companies also see the attractive logistics and distribution accessibility of Pouso Alegre. For example, in the second half of 2019, Cimed - the fourth largest national pharmaceutical industry - built a sizable facility near the Federal highway BR 381 road connecting Belo Horizonte to São Paulo city.⁴² For six years, the presence of XCMG and other foreign industries has transformed the lives of Pouso Alegre’s citizens, allowing greater international exchange and cultural assimilation, making the city a place where foreigners can easily adapt to life and work.

⁴¹ “Inauguração Da Nova Planta Da ACG Capsules,” India Brazil Chamber of Commerce, March 14, 2019, <https://www.indiabrazilchamber.org/post/inaugura%C3%A7%C3%A3o-da-nova-planta-da-acg-capsules>.

⁴² “Notícias CD,” Grupo Cimed, <https://cimedremedios.com.br/noticias/>.



Many characteristics favor foreign investment in Minas Gerais state, particularly in the Southern region. For example, MG's qualified labor force is much cheaper than that of neighboring São Paulo or Rio de Janeiro states. In fact, the base minimum wage in MG for 2020 is between BRL 100 to 200 lower per month than in SP state, resulting not in worse conditions for employees but rather in greater purchasing power within MG. Plus, according to the survey conducted in 2018 by the Brazilian Institute of Geography and Statistics (IBGE), Pouso Alegre was the wealthiest economy in Southern Minas, at the time with a representative GDP of USD 1.335 billion.⁴³ The value of the land for the SEZ future installations in this area is also another beneficial element. It is possible to acquire vast tracts of land for a reasonable price in Pouso Alegre and nearby areas, as prices are much more competitive than in São Paulo's cities.

4.2. Weaknesses

The city's fast industrialization, accompanied by rapid population growth, entailed a lack of sufficient and corresponding urban planning, generating an inadequate infrastructure in some city sectors. The United Nations Educational, Scientific, and Cultural Organization (UNESCO) indicated Pouso Alegre among the 30 safest cities for young people in Brazil in 2017, with the available indicators of 2015.⁴⁴ However, the city fell from number one in the country, in 2013, to 24th, two years later. Although the figures are outdated, they show an increase in violence. This is a widespread tendency in other metropolises in Brazil. Violence is

⁴³ "Produto Interno Bruto Dos Municípios - Pouso Alegre," Instituto Brasileiro de Geografia e Estatística - IBGE, 2017, <https://cidades.ibge.gov.br/brasil/mg/pouso-alegre/pesquisa/38/47001?tipo=ranking>.

⁴⁴ "Relatório Vulnerabilidade Juvenil - Violência," Forum Segurança (UNESCO, 2017), http://www.forumseguranca.org.br/wp-content/uploads/2018/10/FBSP_Vulnerabilidade_Juveni_Violencia_Desigualdade_Racial_2017_Relat%C3%B3rio.pdf.



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still an issue that needs to be addressed as it is a strong indicator of riskier investments, particularly among foreign investors used to lower crime rates.

4.3. Opportunities

The logistical and environmental potential are excellent opportunities that have not been fully seized in the region. There are currently no projects that explore the potential of ecological tourism, despite all the forests surrounding Pouso Alegre. Moreover, the region has excellent air quality and it is full of rivers and woods - circumstances favorable to attract foreigners and tourists, who would come at a greater flow to the city if it becomes a prosperous Special Economic Zone.

Yet, as stated above, no company uses today the entire logistics chain advantages, creating a major opportunity for any company in the new SEZ. Some benefits are storage in bonded areas and easy access to other states, without paying state taxes, to ship the production from nearby ports.

4.4. Threats

In order to initiate the implementation of a new SEZ in Pouso Alegre, there must be direct approval from the Minas Gerais state government. In this context, the main threat that could arise would be the local political struggle. The more scarce, specific, or essential the opportunity is, the more interested politicians will struggle to influence decision-making, create obstacles, and stop projects from approval when they fail to impose their agenda. In this example, the scarce resource would be the contribution of Chinese capital - the FDI that will be implemented with the specialized know-how to create a SEZ. Hence, the city that will receive the resources gains a considerable advantage by becoming a hub of economic attraction.



Nothing prevents new foreign investments from happening in other locations later. But one must consider that projects such as this SEZ are not focused on the short term. The priority of a SEZ should be global social improvement through commercial expansion and growth through economic development. With this goal in mind, it would be possible to envision a more competitive and efficient economic environment in the future, created by greater mobility of international capital.

5. IMPLEMENTATION OF THE NEW SEZ IN POUISO ALEGRE

Even though Brazil is a federal republic, individual states do not hold as much power to change legislation and make economic policies as they see fit. Establishing a SEZ in Minas Gerais would be an effective way to cut through red tape and reduce taxes as the Special Zone would have special taxation exemption and specific legislation. After careful consideration of all legal, economic, and political aspects in play, at the federal (Brazil), state (Minas Gerais), and municipal (Pouso Alegre) levels, this paper suggests that a viable route seems to be creating an Export Processing Zone (EPZ) in Pouso Alegre. One industrial project of a company interested in the EPZ and an economic feasibility study denote the location being suitable for exports. Creating it is possible under federal law. There is already a National Council of Export Processing (CZPE).

Export Processing Zones are a type of SEZ dedicated almost entirely (around 80%) to produce goods for exportation. To create one, it is necessary to provide a series of documents and fill an administrative request with the CZPE to implement an EPZ in Minas Gerais. The requirements for the enterprise are proof of land and availability of funds. The authorities also require a report stating the presence of minimum infrastructure; an indication of the legal model to be adopted; declaration by the competent environmental agency; and a term of commitment from the State or municipality's legal representative.



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Another positive factor for such creation is that the state's current government is pro-free market. It has worked to reduce excessive bureaucracy and it actively supports the creation of the Chinese bank by XCMG. Plus, the federal government guarantees for 20 years the right to an EPZ, as prescribed by the Brazilian EPZ regime.

An additional challenge faced by this type of SEZ to function is that the investment comes from the federal government in Brazil. Having part of the project financing coming from China via FDI could considerably minimize this issue for two reasons: First, part of the value would already be made available by the Chinese investment; And, second, the Brazilian government would be pressured to expedite its share of the investment. In this way, Brazil would be nationally committed to delivering not only to MG but also to China, its most significant international commercial partner.

Beyond the FDI to build the EPZ, a spillover effect is expected to expand to multiple cooperation areas, as was the case with the XCMG's bank, created because of the Industrial Park's success. However, unlike Pouso Park, the EPZ will not be restricted to one company, that is, other industries and businesses would be attracted.

6. CONCLUSION AND DISCUSSION

Doing business in and with Brazil is not a simple task. Even though the country receives plenty of FDI and has abundant natural resources, political and government matters do not facilitate financial transactions and efficient economic growth. Nevertheless, China has been steadfast in its investments in Minas Gerais, making it one of the top destinations among Brazilian states for Chinese FDI.

This paper argued that Minas Gerais and Pouso Alegre have the potential and capacity to receive and coordinate more Chinese FDI. Minas Gerais's geographic characteristics make it a strategically competitive area. Its logistical facilities enable a fast



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flow of products and outlets to all the country's larger consumer markets. Nevertheless, taxation and bureaucracy often come into play, preventing this free movement of foreign capital.

To mitigate both issues, the paper proposed creating an Export Processing Zone in Pouso Alegre. Many are the compelling reasons behind this suggestion, including how the state has the third-largest consumer market in Brazil. The paper used a SWOT analysis to raise relevant points and possible improvements that the state and municipal government could carry out for the EPZ to thrive. XCMG Industrial Park's success, cheaper land, and labor are excellent strengths that favor the city. On the other hand, the present infrastructure could be upgraded to meet the minimum infrastructure report requirements for the EPZ request. Furthermore, the EPZ could foster the use of the whole logistical chain present in the city.

Given that China has a record of directing the flow of FDI to locations where it has implemented a SEZ, carrying out an EPZ in Pouso Alegre will be a profitable strategy to systematize and increase foreign capital flow in Minas Gerais.

In summary, a Chinese-sponsored EPZ in Brazil would be appealing to both countries, which are often looking for more prominent bilateral partnership opportunities, according to the New BRICS Development Bank seminar regarding the negotiation of a Sino-Brazilian free trade agreement⁴⁵. If the Chinese market purchases the products from the EPZ for a reduced amount - given the tax incentive - this agreement can expand Minas Gerais - China's cooperation and efficiently guide Chinese foreign direct investment in Brazil. In conclusion, the Export Processing Zone in Pouso Alegre would be an instrument to promote Pouso Alegre, Minas Gerais, and Brazil's economic growth with Chinese FDI.

⁴⁵ "Guedes Fala Em Livre Comércio Com China: Veja Principais Produtos Negociados," globo.com (G1, November 12, 2019), <https://g1.globo.com/economia/noticia/2019/11/13/guedes-fala-em-livre-comercio-com-china-veja-principais-produtos-negociados.ghtml>.



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