

# CAPITULOS

## Trends in Latin America and Caribbean Integration



Sistema Económico  
Latinoamericano

Latin American Economic  
System

Sistema Económico  
Latino-Americano

Système Economique  
Latinoaméricain



# 49

JANUARY  
MARCH  
1997



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Just as in the next century the 1980's. will be remembered in Latin America and the Caribbean as the «lost decade» due to the difficulties that derived from the external debt burden, the 1990's. will be referred to as «the decade of regional integration».

Between 1990 and 1995 intra-regional trade grew at a more than 20% average rate . In the case of Central America, exports between countries of that sub region doubled, from \$750 to \$1600 million, during the same period. Similarly, in 1995, trade between the four MERCOSUR member countries increased 27%, a rate similar to the 1991-95 average.

Beyond figures, the dynamism of the regional integration process is a clear demonstration of a tendency to find in proximity and similar origins, situations and prospects, the starting point for the development of common economic, political, social and cultural projects.

Such dynamism has also been seen as an answer to the challenges of globalization, even though it does not exclude international norms and negotiations.

In this issue of Capítulos del SELA experts from different backgrounds examine the situation and prospects of regional integration agreements (MERCOSUR, Andean Community and Central American Common Market).

CARICOM's progress toward regional integration is reflected in the document approved at that organization's inter-sessional meeting held in February, 1997.

The process toward the creation of the Free Trade Area of the Americas (FTAA) is analyzed by SELA's Development Director, Dr. Mario Vacchino, and Jamaica's Ambassador to the USA, the Hon. Richard Bernal.

The overview of each integration process is complemented by articles that address more general issues such as which are the tasks that economic negotiators of the next century will have to face, and the questions raised by social issues and financial engineering.

Finally, in the Interviews section, the Secretary General of the Latin American Integration Association (ALADI), the engineer Antonio Antunes, expounds on the possibility of convergence of the different agreements, the probable ways to proceed toward the creation of the FTAA and the effects of globalization on regional integration.

**Economic Issues in the Next Decade: Handbook for Negotiations**

Even if the changes in the world economy and their impact on national economy are widely commented, little is said about the consequences of those changes for international economic negotiations. Similarly, little is said about the difficulties they imply for the negotiators, whose responsibilities are at least as important as those of other public officials.

Bearing in mind this concern, this article presents a futuristic exercise, where it identifies, on the basis of current trends of the international economic agenda, the crucial issues which will, in the next few years, will put to the test our negotiators' skills.

*Si bien se comentan mucho las transformaciones de la economía mundial y sus repercusiones a nivel de la economía nacional, poco se estudian las implicaciones de esos cambios sobre las negociaciones económicas internacionales y sobre la difícil tarea que le corresponde a los negociadores de nuestros días.*

*Con esta preocupación en mente, el presente artículo trata de hacer un ejercicio de futurología, identificando, con base en las tendencias actuales de la agenda económica internacional, los puntos neurálgicos que en los próximos años pondrán a prueba la capacidad de nuestros negociadores.*

*Bien qu'on commente beaucoup les transformations de l'économie mondiale et ses conséquences au niveau de l'économie nationale, les implications de ces changements –aussi bien pour les négociations économiques internationales comme pour la difficile tâche qui attend les négociateurs de nos jours– sont peu étudiées. Cependant, les responsabilités de ces derniers sont au moins aussi importantes que celles de ceux qui nous gouvernent.*

*Compte tenu de cette préoccupation, cet article essaye de faire un exercice de futurologie, en identifiant, sur la base des tendances actuelles de l'agenda économique internationale, les points déterminants qui, les prochaines années, mettront à l'épreuve l'habilité de nos négociateurs.*

*Embora se comente muito sobre as transformações da economia mundial e suas repercussões a nível da economia nacional, pouco se estuda sobre as implicações internacionais e a difícil tarefa que as mesmas enfrentam atualmente.*

*Com esta preocupação em mente, este artigo tenta fazer um exercício de futurologia, identificando, com base nas tendências atuais da agenda econômica internacional, os pontos neurálgicos que nos próximos anos porão à prova a capacidade dos nossos negociadores.*

# Economic Issues in the Next Decade: Handbook for Negotiations

↔ **Manuela Tortora**

*Director of Economic Relations, SELA's Permanent Secretariat\**

*«Because the short-term emergencies claim the attention of States, the long-term work on development priorities often goes unnoticed».*

B. Boutros-Gali

*«Is there any merit in being the messenger of ill news?».*

Addison

The effects of economic globalization on developing countries are today the subject of much prognostication. Generally, such analyses tend to warn us about new phenomena and, at times, to suggest to governments and businessmen, more or less successfully, possible strategies and actions.

On the other hand, little is being given in the way of advice to those in charge of international economic negotiations, who must balance their countries' development strategies with viable and beneficial commitments.

What will be the object of economic negotiations in the coming years? Even though, by definition, predictions always embody risks, it's worth attempting some on this issue, on the basis of a non-empirical, solely realistic methodology. Indeed, the current international economic agenda presents some basic characteristics that are shared by a majority of fora and issues which may be classified as general tendencies likely to continue in the coming years. Also, based on such tendencies it is possible to identify the key issues on which negotiators, particularly those from developing countries, will have to define a position.

## **I. Major Traits of the International Economic Agenda**

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All countries' foreign economic relations are characterized by such a variety of issues and fora that, at first sight, these may

\* *The opinions expressed in this article are solely of the author and do not reflect the Permanent Secretariat's position.*



appear as a disorderly medley that encumbers the identification of priorities, inhibits the follow up and evaluation of results in the capitals and in regional or international organizations, and whose only visible results are unmanageable schedules of meetings and all kinds of commitments.

In an attempt to systematize this agenda and separate from its present traits those that will underscore the coming years, four major tendencies may be pointed out:

### 1. The Exponential Growth in Issues and Negotiating Fora

Up until a few years ago, economic negotiations dealt with a limited and virtually static number of central issues: tariff and non-tariff measures; sub-regional integration; foreign debt and development financing; technology and technical cooperation transfers. Such issues were neatly departmentalized. Specific ministries, experts, regional or multilateral fora and, above all, well defined sectoral negotiating objectives dealt with each department.

Lately, and particularly since the Uruguay Round, we have witnessed the emergence in international economic fora of increasingly complex issues, as seen from a technical and political perspective. In the first place, multidisciplinary concepts and issues such as sustained development or intellectual property are being introduced which imply the definition and linkage of comprehensive national policies

on growth, industrialization, investment, clean technology and environmental control (1). Secondly, the range of issues open to negotiations has widened to include policies that until recently were exclusively of national concern, such as internal policies on competition or investments. Finally, all these issues are being considered simultaneously in various negotiating fora (bilateral, regional, hemispheric, multilateral). Such negotiations generate multiple legal commitments which are not always compatible, as well as economic implications that are difficult to evaluate.

These three tendencies, multidisciplinary, the encompassing of internal matters and simultaneity, cannot be reversed nor avoided since they result from the evolution of the global economic system and its by-products such as technological changes, the information network, the trade and foreign investments boom, the dynamism of regional economic blocs.

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*The range of issues open to negotiations has widened to include policies that until recently were exclusively of national concern.*

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## 2. The Harmonization of Rules Vs. Asymmetry: Making a Circle Square?

Trade, investment and technology are not the only issues that are being «globalized». The rules that regulate such issues are also being «globalized» or harmonized through the definition of multilateral regulatory frameworks that aspire to be universally enforceable, regardless of development levels.

In other words, the quest for the harmonization of trade regulations has outstayed concerns for the need to take into account the different levels of development among countries. Moreover, the harmonization quest is aimed primarily at issues of developed countries' interest (particularly those that are of their industry's interest, such as investments, trade in services, intellectual property) rather than at issues of more global interest such as the harmonization of rules on capital flows.

Indeed, as opposed to the past decade's modus operandi, transnational firms no longer must adapt to their country of operation's laws and policies, but rather it is the latter that has to cater to the company's needs lest it should become less attractive to foreign investments. Where before investors' behavior was regulated (at the national and also at the international level, through the Transnational Firms Code of Conduct), today it is the receiving country's behavior that is being regulated.

Undoubtedly, the opening of markets and economies requires a level playing field since, at least in theory, globalization should proceed without «distorting» obstacles to free enterprise (2). But in reality, structural differences between developed and developing countries inhibit uniform use of globalization's opportunities as well as uniform sharing of risk management. Moreover, those countries that are not successful in inserting themselves in the world economy in a viable and equitable manner become increasingly vulnerable as their exposure to the effects of globalization increases.

It is within this context that economic negotiators face the abolition of the «special and differential treatment» granted to developing countries during the 70's and its replacement by such concepts as reciprocity and «graduality». For instance, during the Uruguay Round identical commitments were agreed upon for all countries but with delayed implementation schedules for developing countries, thereby acknowledging the asym

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*The quest for the harmonization of trade regulations has outstayed concerns for the need to take into account different levels of development*

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metry between countries' development levels but ultimately reaffirming as primary objective the leveling of rules (3).

### 3. Multilateralism and Regionalism: Centrifugal vs. Centripetal Forces

The boom in regional integration mechanisms and, in general, the proliferation of free trade agreements or negotiations are positive results of the opening of the economy, not only in terms of goods, services, technology and capital flows, but also in terms of political, social and cultural bonds. At the same time, the economic strengthening of regional blocs is a consequence of and a reaction to globalization (4).

On the other hand and simultaneously, multilateralism appears as a centrifugal force in contrast with the consolidation of regional or sub-regional blocs. Its particular characteristic is the standardization of rules and regulations without regional distinctions.

On the negotiating table, both regional and multilateral forces become more specific every day, generating two dilemmas. In the first place, the dilemma of whether to strengthen or widen regional integration schemes. This arises when, due to its success, a scheme (for example, the European Union or MERCOSUR) attracts new partners that cannot meet immediately the obligations agreed upon by the founding members. Widening the integration scheme implies halting the strengthening of the process in order to grant new members the time and conditions necessary for their adap-

tation to the rules originally agreed upon (5).

The second dilemma deals not only with the judicial dovetailing of regional commitments with multilateral practices, but also with the merging of strategic priorities: is it more important and convenient for a country to strengthen its ties with its neighbors, or to support the harmonization of multilateral rules and institutions?

Once again, here lies the success or failure of any integration scheme, that which may swing the balance in favor of regional or multilateral –or even hemispheric– forces. For example, it is possible to think that MERCOSUR's success will stimulate United States' interest in FTAA's structuring process. At the same time, however, MERCOSUR's success will act as an increasingly stronger magnet for the remaining Latin American

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*Is it more important for a country to strengthen ties with its neighbors or to support the harmonization of multilateral rules and institutions?*

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countries and, therefore, for the consolidation of regional integration at the expense of a more dynamic hemispheric process.

#### **4. New Actors, New Management Problems for the World Economy**

Most globalization analyses point at the growing importance of non-governmental actors and their operations in the world economy (for example, the role of private capital in financial flows, the influence of non-governmental organizations on issues such as the environment, intra-firms trade, etc.). This is seen as diminishing the effective power of nations and even that of their «offshoots», i.e. regional and international organizations. Moreover, the economic boom experienced by some areas and sub-regions within particular states, or within a region that does not coincide with their borders, further debilitates the power of nations in the global arena (6).

Even if statistics seem to confirm its diminished role, it would be simplistic and hasty to assert that the State is no longer the fundamental actor in international relations. Indeed, even if trade, information or technology's integrating forces should succeed in erasing national barriers, the State cannot be replaced as the «basic unit of global policy». In the first place, none of the potential alternative actors ( firms, non-governmental organizations, investors) would be politically or legally viable as substitutes. In the second place, the State continues to be the «only holder of the magic formula without which no political structure could be maintained in the present world». (7)

State leadership tends to be increasingly shared, in the national and global economy. However, it is unlikely that this leadership will be relinquished completely in favor of non-state actors.

Within this context, government negotiators should be more concerned about taking the role played by other economic actors into account than about being replaced in their job. Consequently, the key question is not who will manage the world economy in lieu of the State, but rather how to insure that the State's untransferable responsibilities will not be curtailed by the inclusion of non state interests.

## **II. Major Issues for Future Negotiations**

From these general tendencies of the international agenda a number of priority issues can be derived which negotiators will

have to learn to deal with whatever the negotiating objectives or fora may be.

1. **The multidisciplinary character** of the international agenda requires, from a point of view of substance, understanding the links that may exist between one issue and another, as well as their implications. As far as procedures are concerned, the appropriate timing is a factor to consider when linking sectoral negotiations, thus allowing for crossed concessions. In those cases in which economic issues are connected with political or ethical criteria (as will probably happen with increasing frequency), it will become harder to identify national economic interests. For example, within the WTO, and at hemispheric level, it has already been established that the regulation of government procurement practices is related to the fight against corruption, and it is not hard to imagine that in a relatively short time span the functioning of the judicial system, as defined by multilateral norms, will be included into the market-access concept. In such cases, the negotiator will need to possess ample political sensitivity, besides sectoral, technical skills.

2. **The harmonization of rules on trade-related areas, i.e. the «new trade issues» that bear upon internal economic policies** and are well beyond the scope of traditional negotiations on tariff and non-tariff issues appears to be, in the short term, a foreseeable scenario. There will not be much time for internal technical preparations: issues such as competition, investments, double taxation and, with less probability for success, labor standards, are already on the agenda in several fora such as those concerned with regional integration and the hemispheric process. When dealing with all these issues, no matter what the national interest might be, negotiators should avoid three main risks: (i) that the harmonization of policies does not take into account the different levels of development among countries; (ii) that several of these «new» issues conceal new protectionist tendencies (as the link between trade and the environment, or trade and labor standards might warrant); and (iii) that these issues scatter the efforts of multilateral trade mechanisms thus endangering their effectiveness and credibility. (8)

3. Developing countries' negotiators should curb **the tendency to speed up or strengthen the implementation of multilateral commitments**, particularly the Uruguay Round agreements and those entered upon at the hemispheric level

(where the USA hopes to obtain stricter regulations than in the WTO). The risk here is that the legal and economic adjustments required by those agreements may be undertaken in a hurried and superficial manner, without the needed internal political consensus and institutional development. Within this context, developing countries will have to be prepared to withstand careful monitoring of their implementation of the Uruguay Round agreements by the industrialized countries. Faced with such monitoring these countries will find it difficult and expensive to follow up on the opening of developed markets and to identify export opportunities as tariff and non-tariff barriers are dismantled according to schedule.

**4. It is imperative to build up developing countries' potential for proposing their own agenda in all international economic fora.**

Issues such as raw materials, diminishing official assistance and development financing (9), the evaluation of international cooperation, technology transfer, how to deal with different levels of development and, above all, the administration of the global economy and the effect of industrialized countries' policies on developing economies, should be of priority concern not only in those fora where economic issues are the object of political debate (UNCTAD, the United Nations' General Assembly) but also, and above all, in those where participation in global trade and the distribution of financial resources is at stake (i.e. in multilateral financial institutions and the WTO).

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*Institutional issues will be of growing importance in multilateral and regional agendas.*  
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**5 . In the next decade, and more than ever before, negotiators will have to take their country's sectoral and global development strategies into account.**

Indeed, as the number of multilateral agreements of obligatory enforcement at the national level increases, countries will be able to determine their national interests only through precise and future-oriented internal assessments. For this, national assessments will be needed as well as a clear social and political consensus endorsing the strategies that may derive from such assessments . In this context, internal strategies regarding regional versus hemispheric or multilateral priorities are equally important .

**6. Institutional issues will be of growing importance in multilateral and regional agendas.** Within the WTO it will be necessary to reconcile the, at times, contradictory pressures in

favor of: (i) its political consolidation as overseer of world trade regulations (particularly through its disputes « settlement mechanism); (ii) the widening of its scope in order to begin economic negotiations and to administer the global economy together with the IMF, the World Bank and UNCTAD; and (iii) those that favor a small organization dedicated to specific technical functions. At the hemispheric level, FTAA's creation will pose the need to establish institutional mechanisms to follow up on the agreements and, probably, to administer the cooperation linked with the free trade area. At the Latin American and Caribbean level, the question of the effectiveness of regional institutions is only beginning to be considered in the Rio Group and it will not be dealt with easily. Also it will not be an easy task to provide integration's secretariats with the technical capacity they need to back progress at the sub-regional level. In all these scenarios, the experience of the OECD, the European Community and APEC will be referred to as good or bad examples, while no institutional project that could be applied automatically to our region's reality will derive from such examples.

**7. The need for international cooperation efforts** will be felt with increasing urgency, in view of the fears generated by an inequitable globalization that would not solve the problem of the different levels of development both within a country and between countries. Therefore, international cooperation in all its aspects (technical, financial, bilateral and multilateral) will continue to be a major issue in economic fora, in spite of donor countries' diminishing level of resources for development assistance. Negotiators will need to pay close attention to the evaluation of cooperation already received, as well as to the drafting and implementation of new cooperation initiatives in keeping with new needs. In this context, innovative cooperation efforts such as those aimed at the integration of economic and social issues; support to public sectors in their elaboration and supervision of regulatory measures; training of human resources and updating of congressmen and businessmen on the new international economic issues; the generation of internal savings; the link between technological research centers and companies; observance of environmental and technical rules in the production of exportable goods; the identification of trade and investment opportunities stemming from the Uruguay Round agreements; greater information on regional integration efforts in political and extra-regional economic circles; social and cultural integration, etc., will become priorities.

These tendencies, some of which are already a fact, and the focal points that will put developing countries' negotiating capacity to the test, demonstrate that foreign economic policies will need to change qualitatively within the next few years.

In the first place, regular consultations between the different branches of government and the public sector will have to be undertaken in order for the national position to rest on firm ground, particularly on multidisciplinary issues and on those where the state is not the only actor .

Deeper national evaluations will be needed of the issues to be negotiated, linking the «macro» (such as external competition or international trade and investment flows) and «micro» aspects of each issue (such as national firms' competitiveness or local effects of technological changes), together with long term perspectives as determined by countries' development strategies.

This comprehensive outlook may be applied not only to internal and international economic issues, but also to the constant transformation of the world's economic map. The dynamism of regional and sub-regional blocs, particularly in Latin America and the Caribbean, indicates that , as ECLAC has said, regionalism is not only «open» but, above all, flexible and changing. Consequently, it becomes harder to define privileged economic partners and to strengthen existing integration schemes.

Internal adjustments should be considered together and parallel with the necessary adjustments to the international economic system. Globalization should imply shared responsibility in the administration of the world economy by developing and industrialized countries. Similarly, the cooperation initiatives that it involves and those aimed at correcting the asymmetry may not be dealt with as secondary issues.

In summary, the international economic agenda requires for us to be competitive and innovative, not only in our productive capacity but also on the negotiating table and in the formulation of national strategies.

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*Globalization should imply shared responsibility in the administration of the world economy by developed and developing countries.*

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1. However, this new multidisciplinary modality is incomplete and biased as economic issues dominate over social ones. In international fora the issue of poverty, for example, is not treated with the same importance, nor is it granted the same instruments as that of international trade.

2. «If all regulations are considered arbitrary 'distortions', it follows that all these 'distortions' must be eliminated in order to improve efficiency. Taken to extremes, this would lead to the evaluation of the impact on competition of all public policies, ECLAC, **Trade Policies and Commitments within the World Trade Organization**. LC/R.1672, Santiago de Chile, July, 31, 1996, p.7.

3. See SELA, **Globalization and**

**Liberalization**. SP/RCC-IX UNCTAD/DT N°2, January 1996.

4. Nevertheless, Luciano Tomassini argues that regionalization efforts are not a counterbalance to globalization since the latter, finally, predominates. See Tomassini, Luciano, «Latin America: Tensions and Dynamics». **Revista del Convenio Andrés Bello**, Bogotá, N° 50-52, 1996, p. 66.

5. This is the risk faced by, for example, the European Union whose acceptance of new Eastern European members runs the risk of slowing down the strengthening of the integration process, already complex among the current 15 members.

6. For example, the axis that runs from San Diego to Tijuana;

Southern Germany's Lander; The River Tumén's delta in Northern China, which encompasses South Korea and Russia; in our region, for example, the State of Sao Paulo or the Colombian-Venezuelan border. See L Tomassini, *op.cit.*, p. 68.

7. «The Nation-State is Dead. Long Live the Nation-State», *The Economist*, Dec. 23-Jan.5. 1996, p. 17.

8. SELA, **Globalization and Liberalization**, *op.cit.*, p. 23.

9. «The questions to ask and to answer are: how much foreign capital is 'needed' for growth and (...) where is the foreign capital to come from?»; Morris Miller, «Where is Globalization Taking Us?», *Futures*, Vol. 27, N° 2, p. 134.

### **Paradigms and Economic Integration in Latin America**

Latin America has all the necessary features to build a stable and dynamic community. However, in practice, petty interests and short-term territorial aspirations have divided people of the region to such an extent that «the neighbor's syndrome» has characterized relations among them. Our countries find that political costs are lower when links are forged with nations from other continents rather than with their own neighbors. However, argues the author, the transforming potentials of integration are beginning to be felt in Latin America and the Caribbean. Eventually, the community of the South that will emerge from all current integration efforts will provide the groundwork for a new philosophy of life.

*América Latina ofrece todas las condiciones necesarias para construir una comunidad estable y dinámica. Sin embargo, en la práctica, intereses mezquinos y aspiraciones territoriales cortoplacistas han dividido a los pueblos de la región al punto en que lo que ha caracterizado las relaciones entre ellos ha sido «el síndrome del vecino». Nuestros países consideran que los costos políticos son menores cuando se forjan vínculos con naciones de otros continentes que cuando se forjan con los propios vecinos. Sin embargo, según el autor, los potenciales transformadores de la integración comienzan a sentirse en América Latina y el Caribe. La comunidad del Sur que surgirá finalmente de todos los esfuerzos actuales de integración servirá de base para una nueva filosofía de vida.*

*L'Amérique latine possède tous les atouts qu'il convient pour bâtir une communauté stable et dynamique. Cependant, dans la pratique, des intérêts mesquins et des ambitions territoriales à courte vue ont divisé les peuples de la région à un point tel que "le syndrome du voisin" a caractérisé leurs relations mutuelles. Nos pays trouvent que les coûts politiques sont moindres lorsqu'ils découlent de liens noués avec des nations d'autres continents que lorsqu'ils sont afférents aux relations avec leurs propres voisins. L'auteur indique toutefois que les forces potentielles de transformation de l'intégration commencent à se faire sentir en Amérique latine et dans les Caraïbes. En définitive, la communauté du Sud qui émergera de tous les efforts d'intégration en cours jettera la base d'une nouvelle philosophie de la vie.*

*A América Latina oferece todas as condições necessárias para construir uma comunidade estável e dinâmica. No entanto, na prática, interesses mesquinhos e aspirações territoriais, a curto prazo, têm dividido os povos da região a tal ponto que a característica das relações entre eles tem sido «a síndrome do vizinho». Nossos países consideram que os custos políticos são menores quando se forjam vínculos com nações de outros continentes que quando se forjam com os próprios vizinhos. Entretanto, segundo o autor, os potenciais transformadores da integração começam a fazer-se sentir na América Latina e no Caribe. A comunidade do Sul, que surgirá finalmente de todos os esforços atuais de integração, servirá de base para uma nova filosofia de vida.*

# Paradigms and Economic Integration in Latin America

→ **Gerardo Arellano**

*Advisor to the Venezuelan Ministry of Industry and Trade on integration issues.*

## I. Introduction

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Latin America has all the necessary features to build a stable and dynamic community, however, in practice, our people have lived separate from each other, with very little contact and, in some cases, very little communication.

Everything appears to indicate that some harmonizing element is missing, one that would stimulate the development, within the region, of a unifying process. To this end, economic integration would seem to be the lever that could set into motion the process for the creation of a Latin American community, since it holds very promising potentials that, in some cases, could be even revolutionary, as the experience of Western Europe has shown.

Indeed, Latin America appears before the world as a heterogeneous mixture in which our important heritage of values, traditions, resources and experiences are dispersed. Undoubtedly, our several years of common history, highlighted by the traumatic but successful emancipation process, constitute a decisive ingredient for the structuring of Latin America's unity. Nevertheless, it is important to point out that such emancipation process did not succeed in laying the foundations for the future consolidation of the idea of a Latin American community even though, at the time, it was successful in uniting efforts and in defining a far-reaching strategy for the region's integration into the world order. It also succeeded in forming a group of men capable of bravely confronting all adversities and limitations.

Petty interests and local and short-term territorial aspirations divided us to such an extent that the result has been the creation

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*Economic integration would seem to be the lever that could set into motion the process for the creation of a Latin American community*  
 ”

of something similar to a labyrinth. The barriers we built throughout our countries' geography, which we later sanctioned through countless cartographic interpretations, have become entrenched in our peoples' conscience and spirit. One could say that the divisionist effect has been so thorough that our common past, with its values and experiences, and our common language have been unable to suppress phobias and conflicts and to create a firm enough basis to support the project of Latin American unity envisioned by our forefathers.

## II. The Neighbor's Syndrome

Many years of rather scattered history yet to be evaluated do not allow us to draw conclusions on the possible structural circumstances that inhibit the consolidation of the idea of a Latin American community. Nor does our past provide us with solutions that might actively bind this group of heterogeneous and fractioned nations.

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*In relations between  
 countries of the region  
 conflict supersedes  
 cooperation*  
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«The neighbor's syndrome» is one of the concepts most widely applied to explain our complex Latin American heterogeneity. In practical terms this means that our countries find that political costs are lower when links are forged with nations from other continents rather than with their own neighbors. In relations between countries of the region conflict often supersedes cooperation.

Nevertheless, this cumbersome state of affairs is hardly Latin America's prerogative. As can be easily demonstrated this is, to a large extent, a general tendency among peoples. However, history has also demonstrated man's creative skill in altering reality.

History is not written. We build our reality and future with constructive and disciplined efforts. Within this context, many are the lessons and the achievements. Western Europe's experience is one of them.

In Europe's case the negative repercussions of the neighbor's syndrome led to two devastating world wars. Structural differences between the European nations deteriorated into conflict and lack of communication. A situation arose in which not only a country's gain was another country's loss but also a country's very existence was at stake. The common denominator was a dialogue among the deaf, with consequent collective failure.

With time, Europe would change. The world wars' bitter legacy, on the one hand, and some men's creative vision, on the

other, made it possible to discern among the tools offered by economic integration an alternative way to build a new philosophy of life.

The European experience clearly illustrates how it is possible to build an economic entity in which each citizen, in his/her daily tasks, contributes to the well being of a larger economic entity, be it the free trade area, a customs unions, or economic unity.

Within this context, economic integration has proven to be an effective foundation on which to build a new paradigm. Given its nature and dynamics, such paradigm may appear revolutionary as it tears down existing walls, but in practice it is progressive because it is based on daily, disciplined and persuasive work.

### III. The Transforming Potentials of Integration

This new paradigm's most significant outcome is the change it causes in the behavior of regular citizens, their view of the world and their decision-making process. Knowingly or unknowingly people begin to modify their traditional behavior which, to a great extent, has been molded by a first-rate rational egotism. The primary conceit by which an individual perceives that his personal good is in direct contradiction with the good of the community yields progressively, without much premeditation or traumatic effects. Individuals find it beneficial to resort to the tools integration may offer, thereby developing a cooperative behavior beneficial to society as a whole, without having planned it deliberately.

Europe's experience is rich with lessons that strengthen our thesis on economic integration's transforming potentials. Nevertheless, this does not mean that once integration is attempted all obstacles and limitations to the structuring of a firm and communal unit will disappear. On the contrary, in some cases more bitter conflicts have erupted. We must not forget that the building of integrated units implies relinquishing areas reserved for local sovereignty throughout centuries.

Notwithstanding the limitations and contradictions inherent in all economic integration processes, Europe's experience in this field is significant. Such experience should be our point of reference, since it is not a question of copying models or applying manuals blindly.

In Latin America's case, the issue of integration has been on

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*The building of integrated units implies relinquishing areas reserved for local sovereignty throughout centuries.*

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the region's political and economic agenda during several decades. This in itself, together with the fact that not much has come of it in practice, have won the issue few friends and, in the best of cases, marked skepticism.

At the beginning, many were the projects and ambitious the objectives; however, results did not meet expectations. The Latin American Free Trade Association (LAFTA) is an important experience that should be mentioned. LAFTA's objective (the organization was created by the 1960 Montevideo Treaty) was to establish a free trade area between the ten South American countries and Mexico.

However, the idea of building a Latin American economic area through LAFTA met with strong resistance. In those years of firm and flourishing protectionism no business sector was willing to accept, much less promote, tariff reductions on intra-Latin American imports.

This protectionist paradigm was compounded by our countries' different levels of development, a fact that became a rallying cry for the launching of vast projects and programs aimed at leveling such unbalance and eliminating injustice. In spite of the fact that this concept originated an ample theoretical debate, in practice the efforts it sparked joined the ranks of the many attempts at Latin American integration that have been shelved. This increased skepticism among the productive sectors of the region's so-called less developed countries (Bolivia, Ecuador and Paraguay).

As Dieter Sheengas points out in his work **Learning from Europe**, Latin America, in its recent history, particularly during the period of imports substitution policies, did not develop a rational and efficient protective strategy. We attempted to protect all sectors and this, in practice, led to the dispersion of efforts, the squandering of resources and the loss of our negotiating capacity, among other things.

It could be said that when we attempted to define development strategies and policies to insure our insertion into the international arena, a pronounced lack of rationality led to the creation of a highly contradictory environment in the enforcement of economic integration schemes. Such contradictions, or that which has been defined the dialectics of Latin American

integration, have been the object of a thorough and complex

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*When we attempted to define development strategies and policies to insure our insertion into the international arena, a pronounced lack of rationality led to the creation of a highly contradictory environment in the enforcement of economic integration schemes.*

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theoretical debate (see Juan Mario Vacchino, 1981, among others).

For some analysts the difficulties that have limited Latin American integration are of a structural nature. This means, broadly, that historical, macroeconomic and social behavior issues are at play. From this rigid perspective, it is not easy to progress toward the adoption of the changes made necessary by the economic integration process. To some extent, the structuralist view has masked with theory the little interest there was in opening markets to intra-Latin American competition.

The rhetoric of Latin American integration has been rich in doctrine but rather poor in results. Prolific political statements in favor of integration have been accompanied, in the private and public sector, by a localist and, to a good extent, mercantile manner of operating in which the emphasis is on selling rather than buying.

LAFTA's failure led to the creation of the Latin American Integration Association (ALADI), by the 1980 Montevideo Treaty. ALADI's objectives were less ambitious. Leaving aside the building of a Latin American free trade area, it would focus on negotiating bilateral agreements in which the parties would grant each other trade preferences for a limited list of products. Such preferences are quite varied and often rather limited.

Undoubtedly, ALADI's strategy was realistic, considering the prevailing apathy about and even rejection of integration. Its approach to integration was gradual. It attempted to rally friends, or at least sympathizers, for the integrationist project. Nevertheless, strong support and leadership were needed to be successful, and these were lacking during several years. This is why the eighties' decade is referred to as «Latin American integration's lost decade».

It is important to point out, however, that some of the initiatives carried out within ALADI's framework, particularly the active participation by some private sector associations in the negotiations on the Limited Scope Agreements, contributed effectively to creating a favorable environment for integration.

The Economic Complementation Agreements signed by Argentina's and Brazil's Governments are among ALADI's most significant achievements. With a view to strengthening their bilateral relations, between the years 1984 and 1989 Argentina and Brazil signed 24 bilateral protocols covering different areas. These envisioned the adoption of pragmatic and innovative trade

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 in results.*  
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policies that premiered compensation and administration formulae which facilitated the gradual phasing out of trade barriers and the creation of a favorable environment for integration efforts

#### IV. Andean Integration

The case of the Andean Pact is one that clearly illustrates the contradictions inherent in the protectionism and open markets paradigms, a process that could be defined as Latin America's integration dialectics. Established in 1969 by the Cartagena Agreement, the Andean Pact has experienced highs and lows. Chile's withdrawal from the Pact in 1973, the paralysis that led to Quito's Protocol in 1978 and Peru's special status, granted in 1991, are among the most significant difficulties faced by the Agreement.

Those who are most skeptical about Andean integration, have branded it as «entelechy or juridical spider web». Indeed, such definition is appropriate if we consider that by the end of the 1980's anyone interested in exporting from an Andean country to anywhere in the sub-region, faced the following situation:

–Countries had drawn lists of products that were to be excepted from free trade. Such lists varied from country to country and included a sizable number of goods. In most cases the entire textile sector was excluded.

–The Agreement envisioned a rather innovative scheme for the development of the sub-region's industrial capacity, called «Sectoral Industrial Development Program». The petrochemical, iron and steel, metal- mechanic, automotive, and fertilizers' sectors were selected for programming but, in practice, only the petrochemical program was implemented while the rest basically entered the exceptions lists.

–The industrial program included a *Nómina de Reserva* (reservation list) made up of a group of products whose status was to be defined but that, eventually, were added to the exceptions list. Products from the paper, aluminum and glass industries were among those included in the *Nómina*.

–The marginal percentage of free-trade products was further reduced by the «administered trade list» adopted by the Quito Protocol. The

few products that were freely traded were now to be subject to quotas.

The 1969 Cartagena Agreement's hope to establish a free trade area within ten years was left in limbo and, in practice, the

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*In the 1990's the transformation of the protectionist paradigm opens up new perspectives for regional integration.*  
 ”



productive sectors interested in integration faced a labyrinth.

In the 1990's the transformation of the protectionist paradigm opens up new perspectives for regional integration. It is important to point out that even though such paradigm made possible the creation of an important industrial infrastructure and the consolidation of several production projects, it also isolated the region from competitiveness and innovations.

#### **IV. Integration as a Way of Life**

The process toward the adoption of the new economic integration paradigm has begun. In this new context, and as opposed to previous decade's policies, priority is given to automatic mechanisms and to de-regulation of economic transactions, thereby insuring greater participation by economic agents. Additionally, tariffs are lowered and trade barriers progressively dismantled.

In the 1990's, parallel to the liberalization policies adopted by Andean Pact member countries, important changes are introduced in the Cartagena Agreement's judicial framework. The most important of these is the elimination of all exceptions through the creation of a lineal and speedy trade liberalization program. Improvements in the free trade area are coupled with the liberalization of air, land and multi-modal transportation services; the liberalization of regulations on investments, intellectual property, free competition and unfair competition.

This fast-paced and positive process of change occurring within the context of Andean integration has helped introduce the new paradigm that envisions the progressive consolidation of the Latin American community.

Andean integration, particularly Colombian-Venezuelan integration, begins to be an integral part of everyday life for people of the sub-region. To put it more formally, we could say that today Andean integration is an organic element of the civil society's functional dynamics. By this we mean that the common citizen has begun to view integration efforts as something he can benefit from. We are progressively edging towards the consolidation of the integration paradigm, just as it happened in Western Europe.

The signing, on March 26, 1991, of the Asunción Treaty by the Governments of Argentina, Brazil, Uruguay and Paraguay was another important landmark in the road toward Latin American integration. This agreement seeks the creation of the Common

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*Andean integration  
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Market of the South through a trade liberalization program, the coordination of macroeconomic policies and common external tariffs, as well as other trade regulatory instruments.

As studies and evaluations of MERCOSUR demonstrate, this integration scheme has been successful, in spite of the obstacles it has encountered. The program for the reduction and elimination of trade barriers is now at an advanced stage. Tariffs on the majority of goods have been reduced to comply with the levels established in the common external tariff code.

This decade's breakthroughs in economic integration prove that integration can provide effective and reliable tools for the consolidation of a Latin American community. Inter-Latin American trade figures are an indication of this.

An evaluation of ALADI's trade figures indicates that since 1990, intra-regional trade has been growing in a sustained and spectacular way, at an average annual rate of over 23%, reaching a level of over \$34 billion. This represents around 17% of member countries' total exports.

Trade among MERCOSUR countries has also increased progressively reaching, after a 30% surge in 1993 alone, \$8 billion per year. Since the end of the 1980's and the beginning of the 1990's, intra-MERCOSUR sales represent around 34% of total intra-regional sales. As for trade among Andean Pact members, it too has increased uniformly during the last years and it represents, today, 14% of regional trade.

Negotiations between the Andean Group and MERCOSUR are further proof of how economic integration can be a transforming force in the quest for a Latin American community. Even though this process was formally initiated only very recently, in November 1996, in reality it has its roots in the agreements negotiated within the framework of ALADI, which in the negotiating lingo are called the region's historical heritage.

This process of negotiations should culminate in a Latin American free trade area, the prized goal, during the 1950's, of some Latin American visionaries.

It is our opinion that from several points of view, particularly the political one, such negotiations are the greatest challenge the region must face. They will make possible the creation of a South American economic space which will contribute to the region's integration into a globalized world and will provide the groundwork

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 the community of  
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 of life.*  
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for a negotiating strategy on the creation of a hemispheric free trade area.

From an economic perspective, MERCOSUR represents for Andean Pact countries a two hundred million people market, with a \$700 billion Gross National Product, an imports' level that in 1994 reached \$60 billion and an international reserves' level greater than nine months of imports.

The definition of the legal basis for the creation of a South American economic space will increase our society's confidence in the region's resources and institutions. This will undoubtedly set into motion a slow but constant, therefore deep, transforming process. For Latin Americans the community of the South will provide the groundwork for a new philosophy of life in which the common citizen, in his/her daily work will build, without previous planning, a paradigm that will benefit the individual as well as society.

**MERCOSUR: Evaluation and Perspectives**

*The following article examines MERCOSUR's main characteristics. It reviews its origins, its institutional framework and the impressive strides made by its member countries toward trade liberalization. The new position on foreign direct investment is considered with some detail, together with the treatment granted to social issues. Finally, MERCOSUR's position vis-à-vis the rest of ALADI member countries and the importance of economic links with the European Union are examined. A reference is also made to negotiations on the FTA.*

*En el artículo siguiente se examinan las características principales de MERCOSUR, sus orígenes, marco institucional y los progresos impresionantes hechos por sus miembros en materia de liberalización del comercio. Se considera con cierto detalle la nueva posición en materia de inversión externa directa, así como el tratamiento que se le da a lo social. Por último, se examinan la posición de MERCOSUR con respecto al resto de los países miembros de la ALADI y la importancia de los vínculos económicos con la Unión Europea. También se hace referencia a las negociaciones relacionadas con el ALCA.*

*L'article ci-après examine les caractéristiques essentielles du Marché du Sud «MERCOSUR», traite de ses origines, de sa structure institutionnelle et des progrès impressionnants réalisés par ses pays membres sur la voie de la libéralisation du commerce. La position nouvelle en matière d'investissement étranger direct est examinée assez en détail tout comme le traitement réservé aux questions sociales. L'examen s'étend enfin à la position du Mercosur à l'égard des autres pays membres de l'ALADI et à l'importance de liens économiques avec l'Union Européenne. Référence est également faite aux négociations portant sur la zone de libre-échange des Amériques.*

*No artigo seguinte, examinam-se as principais características de MERCOSUL, suas origens, âmbito institucional e os impressionantes progressos alcançados pelos seus membros em matéria de liberalização do comércio. Considera-se com certo cuidado a nova posição em matéria de investimento externo direto, bem como o tratamento ao aspeto social. Finalmente, examina-se a posição de MERCOSUL em relação ao resto dos países membros da ALADI como também a importância dos vínculos económicos com a União Europeia. Faz-se referência, também, às negociações relacionadas com a ALCA.*

# MERCOSUR: Evaluation and Perspectives

→ **Armando Di Filippo**

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## I. Introduction

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The following article presents MERCOSUR's main characteristics and features. It examines the origins of the process whereby Argentina and Brazil were able to overcome their mutual disaccord and frictions in order to approve the Bilateral Common Market, and Paraguay's and Uruguay's later adherence to create MERCOSUR.

A brief description of MERCOSUR's institutional framework follows. The principle behind this framework is to avoid the creation of rigid and excessively bureaucratic bodies that do not originate from MERCOSUR's «real» growth.

The impressive strides made towards reciprocal trade liberalization, which culminated with the establishment of a common tariff, are then summarized.

The new position on foreign direct investment is considered with some detail. This is based on very liberal open policies even though an attempt is being made to reserve some preferential areas for intra-regional investments.

The fact that the Agreement, which favors economic issues, initially disregarded social matters is pointed out. However, the firm commitment to create a common market and an understanding of its effects on labor's international mobility, has resulted in an acknowledgment of the importance of social and labor issues and in the later revision of the Treaty.

Finally, MERCOSUR's position vis-à-vis the rest of ALADI member countries is examined, together with the strategic role it may play in the creation of a South American free trade area. Similarly, the importance of MERCOSUR's economic links with the European Union, its main trade and direct investment partner, is highlighted, together with the apparently favorable perspectives for the establishment of a free trade area between

\* *The opinions expressed in this article are solely of the author and do not reflect the Permanent Secretariat's position.*

both integration schemes. This section concludes with a reference to the negotiating strategies followed in the USA's initiative to create a hemispheric free trade area and to MERCOSUR's initial positions on this issue.

In the general conclusions, a small intellectual exercise is attempted with a view to stimulating the debate. A distinction is made between unidimensional or strictly economic integration and multidimensional or deep integration. The first is represented by NAFTA, or its more ambitious version aimed at creating a hemispheric free trade area. Deep integration, which includes market liberalization between its members, is represented by the European Union and its enormous efforts and achievements. The strictly economic hemispheric integration heralded by the United States is an option compatible with some far-reaching integration efforts being attempted in South America.

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MERCOSUR appears to be on its way towards a multidimensional and profound type of integration which, in the long term, could spread to South America as a whole.

## **II. MERCOSUR'S Origins**

During Latin America's period of authoritarian military governments national security was the prevailing ideology. This hindered efforts to overcome distrust and frictions among bordering countries.

Argentina and Brazil have been rivals throughout history because of competing geopolitical and geoeconomic interests. Both countries aspired to become South America's leading power and attempted to consolidate their military supremacy in, for example, the nuclear energy field. However, already during the military regimes important steps were taken to deflate some conflicts. For example, on the issue of who was to have access to the Paraná River's hydroelectric power Argentina objected to the signing, in 1973, of the Itaipú Agreement between Brazil and Paraguay. The controversy was settled in 1979 with the signing of the Tripartite Corpus-Itaipú Agreement.

This greater cooperation mode intensified when constitutionally elected civil governments came into power in Argentina (1983) and Brazil (1985), and a new disposition toward peace and cooperation began to emerge. In 1985, Argentina's President Alfonsín and Brazil's President Sarney signed the Foz de

Iguazú's Declaration in which they agreed to speed up bilateral integration efforts through the creation of a High Level Joint Commission.

Shortly thereafter, on July 1986 in Buenos Aires, the same two Presidents signed the Argentine-Brazilian Integration Act, which establishes the Economic Integration and Cooperation Program between Argentina and Brazil (known as EICP or ICPAB). During its first phase ICPAB approved twelve sectoral protocols. The Program placed much emphasis on the capital goods sector (Protocol 1), exploring the possibilities for within-industries complementation and for achieving balanced trade. Important agreements were also underwritten concerning wheat (Protocol 2, which improved Argentina's position in the Brazilian market), the iron and steel industry (Protocol 3) and foodstuffs (Protocol 23, which envisioned complementation efforts) and, above all, the automotive sector (Protocol 21, aimed at favoring reciprocal trade). With Protocol 13, ICPAB strengthened the existing cooperation on nuclear issues, a fact that had deep geopolitical meaning considering that these two countries had competed for hegemony in South America. In total, 24 protocols were signed.

In 1987 the implementation of the economic stabilization programs adopted by the two countries faced enormous difficulties, thereby increasing disagreements over the application of economic policies. In 1988 the growth rates of Argentina and Brazil reached -3% and 0% respectively. Nevertheless, in 1988 in Buenos Aires, both countries' Governments signed the Integration, Cooperation and Development Agreement aimed at creating a common market between the two countries. A period of ten years was agreed for the elimination of all trade and non-trade barriers between the two countries. The Treaty's second phase envisioned the gradual harmonization of policies needed to create a common market. In spite of the difficulties both countries faced, in 1988 bilateral trade grew by almost 20% sustaining a positive tendency the following three years.

With the change of government in both countries, Argentina's President Menem and Brazil's Collor de Mello signed in 1990 the Buenos Aires Act, aimed at moving the date for the creation of the common market to December 1994. During this period greater emphasis was placed on the use of trade liberalization mechanisms based on general tariff reductions, with limited exemptions' lists and stricter adherence to timetables. At the same time, government intervention in the sectoral agreements was scaled down. The neoliberal, open market approach began to take shape, particularly in Argentina.

At this point in the bilateral relation, it became evident that it was necessary to open up the agreement to two countries whose economic connection with Argentina and Brazil were of paramount importance: Uruguay and Paraguay. Uruguay's trade links with Argentina dated to 1974, when the Argentina-Uruguay Economic Complementation Agreement (AUECA) was signed; and its relations with Brazil to 1975, through the Trade Expansion Protocol (PEE). Both countries had closely followed developments in Argentina-Brazil relations.

On September 1990, representatives from Argentina, Brazil, Paraguay and Uruguay met in Buenos Aires and agreed to undertake the necessary steps to negotiate a four-party agreement to replace the bilateral one. Finally, after further contacts, on March 26, 1991, the Asunción Treaty was signed in Paraguay «for the creation of a common market between the Republic of Argentina, the Federal Republic of Brazil, the Republic of Paraguay and the Eastern Republic of Uruguay».

MERCOSUR encompasses a 200 million people market, that is, 44% of Latin America's population. Its Gross National Product is approximately \$700 billion, 51% of the region's total. Its territory represents 59% of the regional area.

As the Treaty explicitly states, MERCOSUR's aim is to achieve deep integration through the free circulation of goods, services and production factors; the establishment of common external tariffs and a common trade policy, together with the coordination of positions in regional and international economic and trade fora; the coordination of macroeconomic and sectoral policies in the foreign trade, agricultural, industrial, fiscal, monetary, exchange rate and capital, services, customs, transportation and communications' fields; and the commitment by member states to harmonize their legislatures in relevant areas.

On the other hand, social and labor issues are not treated satisfactorily in the Treaty's regulations. Nevertheless, by stating its commitment to create a common market where all productive factors would enjoy free mobility and right of establishment, the treaty implicitly includes all social and labor issues. Similarly, the agenda approved in the Working Sub-Group No. 11, whose work it is to analyze labor relations, employment and social security, encompasses these issues. Even so, the Treaty's fundamentally economic character is highlighted by the fact that the Working Sub-Group No. 11 was

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created in mid -1992, as a later addition to the other ten sub-groups established in 1991. Presently, this has been replaced by the Working Sub-Group No.10 which has similar responsibilities.

The Asunción Treaty was only the first step in the transition towards the establishment of the Common Market. Such transition ended on December 31, 1994. In order to ease the transition the Member States adopted a General Rule of Origins, a Disputes' Settlement Mechanism and a Safeguards Mechanism.

The transition phase concluded reasonably well and with the Ouro Preto Protocol, signed in 1994, a common external tariff that created an imperfect or flexible customs union was established thus mapping the road toward a better customs union. To this end, a so-called «adaptation regime» has been established to phase out some reciprocal tariffs still in force between the four countries. A timetable was also agreed for the elimination of some lists of exceptions to the common external tariff .

### **III. The Institutional Structure**

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The philosophy behind MERCOSUR's original institutional structure was to keep to the minimum the Treaty's rules and its constituent bodies. As opposed to the cumbersome institutional structures of other integration schemes such as ALADI or the Andean Pact, the idea was that the growth and complexity of the institutions would be determined by the «real» MERCOSUR's objective expansion . Such real MERCOSUR would emerge from the volume and intensity of reciprocal economic ties.

The four countries' Congresses ratified the Treaty within a very short period of time and practically without objections. The Treaty was then homologated before ALADI through the Economic Complementation Agreement No. 18, of January 21, 1992.

The Asunción Treaty established that, during the transition period, MERCOSUR's governing bodies were to be the following:

The Council (MC) is MERCOSUR's main body. It is responsible for providing political guidance and insuring that objectives are met. It meets at the Presidential level and at the level of Ministers of Economic and Foreign Affairs.

The Common Market Group (CMG) is the Agreement's executive body. Its members are ministerial representatives (Economy, Central Bank and Foreign Affairs) coordinated by each country's Foreign Ministry. It meets every three months while coordinators meet once a month. It operates in a simple and cost-effective manner, but it has proven to be very effective.

The Common Market Group's Administrative Secretariat has its headquarters in the city of Montevideo.

During the transition period, eleven Working Sub-Groups were also operating. These were in charge of studying trade and customs issues, technical rules, fiscal and monetary policies related to trade, land and maritime transportation, industrial and technology policies, agricultural policies, energy policies and the coordination of macroeconomic policies. As mentioned above, another sub-group in charge of studying labor relations, employment and social security was later added to these ten sub-groups. All of them mobilized hundreds of officials from diverse public administration bodies. Multiple actors from the academic and business world, as well as union representatives, technical experts from international and non-governmental organizations, all interrelate with the above groups.

After the Ouro Preto meeting the working groups were restructured and the following were created: Communications, Mining, Technical Reglamentations, Financial Issues, Transportation and Infrastructure, Environment, Industry, Agriculture, Energy, Labor Issues, Employment and Social Security. Additionally, meetings will be held on the issues of tourism and science and technology.

MERCOSUR also relies on a joint Parliamentary Commission comprised of representatives from the four national parliaments.

MERCOSUR's Industrial Council was created during the organization's first operational phase. Its members are Argentina's Industrial Union, Brazil's National Confederation of Industries, Paraguay's Industrial Union and Uruguay's Industrial Chamber. The Council's objective was to guide the dialogue between representatives of the business sector on integration issues of common interest, with emphasis on the issue of industrial competition. After the Ouro Preto meeting, this Council was replaced by the Economic and Social Consultation Forum.

Strictly speaking, a judicial body does not exist. Should controversies arise on the interpretation of the Asunción Treaty or on the fulfillment of its obligations, the system calls for obligatory ad-hoc arbitration. The rulings are also of a compulsory nature. It also protects the private sector from breach of legal commitments entered upon by MERCOSUR's Member States.

After the Ouro Preto meeting, MERCOSUR's Trade Commission (MTC) and the Economic and Social Consultation Forum (ESCF) were added.

The Trade Commission covers the implementation of common trade policy mechanisms within MERCOSUR and vis-à-vis third countries. It has the power to establish technical committees which may gradually absorb the tasks assigned to the trade working groups. Also, the Disputes Settlement System falls under its jurisdiction.

The fact that such significant responsibilities have been assigned to the MTC reveals the importance of internal and external trade relations, particularly the consolidation of the common external tariff, during this stage of MERCOSUR's development.

On the other hand, activities related to the promotion of the common market, particularly the social issues this involves, have only begun to be institutionalized through the creation of the Economic and Social Consultation Forum which engulfs MERCOSUR's Industrial Council. This consulting body represents the social and economic sectors and it will issue recommendations to be considered by the Common Market Group.

MERCOSUR's Administrative Secretariat (MAS), with headquarters in Montevideo, began operations on January 1, 1997. It is an international body within MERCOSUR, with structure and budget drawn from the four member countries and a Director appointed by the Common Market Council for a period of two years. MAS is MERCOSUR's official archives' depository. It publishes MERCOSUR's Newsletter and takes care of the official translations into Spanish and Portuguese.

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### III. Trade

A brief description of the boom in Latin America's reciprocal trade during the nineties will enable us to define South America's importance, particularly MERCOSUR's position within this process. Between 1990 and 1994, total exports from Latin America and the Caribbean increased from \$123 billion to \$181 billion, approximately a 47% surge. During the same period, exports between Latin American and Caribbean countries went from \$16 to \$35 billion, increasing by approximately 118%.

Total exports from ALADI member countries escalated, during this period, from \$ 111 to \$ 207 billion, an 86% increase, while reciprocal exports increased by 130%. Their participation within total trade figures surged from 11% in 1990 to 17% in 1994.

Excluding Mexico, in 1994 South America's inter-regional

exports as a percentage of total exports increased from 19% to 28%, while its exports to the USA decreased from 47% to 25% (ALADI figures). This discrepancy reflects the importance of Mexico's economy on global figures, and the fact that in 1994 only 4% of Mexican exports went to Latin American countries while 85% targeted the USA market. During the same period, the Central American Common Market's total exports grew by 75%, while exports to the region increased by 87%. Like Mexico, even though not quite, Central America's foreign trade is heavily dependent on the USA market, especially through the processing plants' areas and the maquiladoras that operate there. Mexico's trade dynamics, as well as that of Central American countries and the Caribbean, are very much dependent on the United States. Therefore, the intra-Latin American trade boom has occurred, basically, in South America.

Intra-South American trade depends, on the one hand, from the Andean countries' and MERCOSUR's performance and, on the other, from Chile who is not a full member of either integration scheme. During the 1991-1995 five year period, Andean Group countries' total exports increased from \$27 to \$40 billion, a 68% surge, while reciprocal exports grew by 167%. In 1991, the sub-region's reciprocal exports represented 6% of total exports and by 1995 they reached 12%. During the same period MERCOSUR's total exports grew from \$46 to \$72 billion, a 56% increase. Reciprocal trade flows, on the other hand, increased 210%. In 1991, exports between countries of the sub-region represented 11% of total exports and in 1995 they grew to 22%.

Therefore, the boom in intra-regional trade has occurred, basically, among MERCOSUR and Andean Group countries, with the addition of Chile whose contacts with MERCOSUR become closer by the day. Indeed, 22% of Chile's exports are to Latin America (1994) and during 1990-1994 these grew at a 22% annual rate (ECLAC, May 1996, Statistical Annex).

In view of these volumes, it is convenient to review briefly MERCOSUR's trade aspects during the transition period which began with the Asunción Treaty, and to glance at the new phase ushered in by the Ouro Preto Protocol.

Concerning the Treaty's trade clauses during the transition period, special reference should be made to the general system of rules of origins and to the trade liberalization program to which the signatory countries committed themselves firmly from the beginning. Other issues, such as the common external tariff, the coordination of macroeconomic policies and the approval of sectoral agreements required further negotiations.

The trade liberalization program was particularly broad and

comprehensive. It established progressive, lineal and automatic tariff reductions, together with the removal of any other type of non-tariff barrier or similar measure. The commitment to end 1994 with a zero tariff and full trade liberalization has been reasonably met. The lists of exceptions were also subjected to a calendar of automatic, 20% annual reduction of tariffs, beginning December 31, 1990.

The safeguard clauses on trade issues were designed to enter into force should imports surge greatly over a very short period of time. Such clauses do not limit the volume of total imports but only the quota subject to tariff preferences; the remainder may be imported subject to regular tariffs.

Sectoral agreements tend to strengthen intra-sectoral industrial trade within the integration process, but cannot invalidate any existing trade liberalization clause. At present their extension to Paraguay and Uruguay is being considered.

On the other hand, it should be mentioned that all trade preferences agreed upon between MERCOSUR's member states and other non-member countries were to cease after December 31, 1994. However, that date has been postponed several times in order to grant MERCOSUR more time for the new negotiations in which it participates as a bloc.

As of January 1995, the common external tariff was approved with a 0 to 20% range and an 11% average. It includes the lists of national exceptions and the basic convergence lists for the capital and informatics and telecommunication sectors. Exceptions represent 12% of the tariff system.

A 14% maximum tariff was established for capital goods, with ascending and descending convergencies (depending on whether previous tariffs were below or above such limit), with a 2001 time limit for Argentina and Brazil and 2006 for Paraguay and Uruguay. The common external tariff for informatics and telecommunications goods was set at a 16% maximum, with convergencies to be met by the year 2006.

Regarding the free trade internal area among member countries, lists of products subject to import tariffs during a definite period of time were agreed upon. Tariffs on the products included in these lists, less than 10% of total trade, will be reduced annually until their complete elimination. The time span is four years for Argentina and Brazil and five years for Uruguay and Paraguay. This system is called System of Final Adaptation to the Tariff Union, and annual reductions start from the nominal rate in force in each country on August 5, 1994.

It should be pointed out that the adaptation system does not authorize levying higher tariffs on products from MERCOSUR

than those levied on products from other countries. On this issue, the common external tariff operates as a ceiling.

The future of MERCOSUR's trade will depend on the strengthening of trade between industries. This will afford the group's smaller and economically weaker countries the opportunity to participate in a more balanced fashion. In trade between Argentina and Brazil, the manufacturing goods that have registered the most dynamic growth rate are: foodstuffs, chemical products and machinery and transportation equipments.

Between 60% and 70% of transnational firms' investments in Argentina and Brazil are in these products' industries. Therefore, trade in these goods has three major characteristics: it is the most dynamic; it occurs, to a great extent, between industries, and it receives a very high percentage of all foreign investments in Argentina and Brazil (Di Filippo, 1994).

## V. Foreign Direct Investment

During the 1990-1994 period MERCOSUR received a total of \$20.4 billion in direct investment flows. This represents 44.3% of the \$46 billion Latin America received from Europe, the United States and Japan (IDB-IRELA, 1996). If we exclude Mexico, the percentage of foreign investment that entered MERCOSUR increases to 63.1% of total flows.

Of MERCOSUR's foreign direct investment flows during this period 24.8% originated from Europe (23.5% from the European Union), 71.4% from the United States and 3.8% from Japan.

As for intra-regional investments within Latin America as a whole, figures indicate that they represent from less than 1% to more than 10% of total foreign direct investment flows. The importance of such investments within the total received is illustrated by Argentina's and Brazil's case. In 1992, 12.2% of Argentina's total foreign investment flows originated from the region, reaching a total of \$1.8 billion. In

1994, Brazil received from the region \$0.3 billion in foreign investments, with half a percentage point of total stock entered on that date.

We will now summarize briefly MERCOSUR's guidelines regulating foreign direct investment flows. Two protocols regulate the treatment of foreign investment. The first refers to investments originating in non-MERCOSUR countries, the second to member states.

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The Protocol on the Promotion and Protection of Investments originating in non-MERCOSUR countries states that these capital flows will not receive a treatment more favorable than that established by such protocol. Therefore, each party will not grant third countries more benefits or rights than those established by the Protocol's regulations.

In its substantive section the Protocol states that each member state will grant such investments full protection and a treatment no less favorable than that granted to local investments (national treatment) or to investments originating from other countries (most favored nation treatment).

However, investors from third countries will not benefit from any preferential treatment or privilege resulting from MERCOSUR member countries' participation in or association to a free trade area, customs union, common market or any similar regional agreement. Thus, a global preferential environment is created for any type of integration agreement in which MERCOSUR member countries participate either individually or as a group. Investors from non-MERCOSUR countries will also be excluded from international taxation agreements of which they are not signatories.

In summary, this Protocol addresses two major preoccupations. The first is to insure that no member state grants preferences that discriminate against other MERCOSUR members' rights or interests, in its eagerness to attract direct foreign investment. The second is to reserve for MERCOSUR members an area of special preferences granted within the framework of MERCOSUR's integration agreements as well as other agreements in which it participates. Third countries are not to have access to these preferences. To insure that these objectives are met, Article Three of the Protocol provides that «Member States agree to exchange information on future and ongoing negotiations on investments' promotion and reciprocal protection agreements with third countries, and will consult with each other before introducing any substantial modification to the general treatment agreed in Article Two of the present Protocol».

On the other hand, the Protocol for the Promotion and Reciprocal Protection of Investments in MERCOSUR states that «each Contracting Party will promote investments from other Contracting Parties and will allow them into its territory under conditions no less favorable than those granted to their own investors ( national treatment) or to third countries' investments (most favored nation treatment). This will not curtail each Party's right to temporarily retain limited exceptions on some of the sectors included in this Protocol's Annex».

As opposed to the Protocol on Investments Originating from Non-Member Countries, this one authorizes and, in a certain way, encourages member countries to grant more favorable preferential treatments. Indeed, Article 7 states that «when a Contracting Party's legal provisions or the international law obligations that are currently in force or may be established in the future, or an agreement between a Contracting Party's investor and the receiving Contracting Party, contain guidelines which grant investments a more favorable treatment than that established by the present Protocol, these guidelines will prevail over the present Protocol to the extent that they are more favorable».

In summary, the guidelines that regulate investments from outside MERCOSUR grant maximum preferences that may not be exceeded by member countries. On the other hand, the guidelines on investments from within the area grant minimum preferences that may be extended by each member country.

Also, MERCOSUR has a preferential system concerning joint enterprises. It was established by the Statute on Bi-National Enterprises signed on June 6, 1990 by Argentina and Brazil. Bi-national enterprises are those in which: i) 80% of the capital and votes belong to national investors from Brazil or Argentina, thereby granting them real and effective control over the firm; ii) each national investor holds at least 30% of the capital; and iii) national investors from each country have the right to elect at least one member of each of the firm's administrative and inspecting bodies.

Bi-national firms may engage in any economic activity allowed by the receiving country's laws and will adopt any of the legal formats approved by that country's legislations.

Amongst other preferences, bi-national firms will be granted: i) the same treatment granted or that may be granted to national capital firms, even if the majority of the social capital should belong to investors from the other country; ii) the above-mentioned «national treatment», which will cover local taxes; access to local credit; access to national, regional or sectoral promotion incentives; and access to public sector's purchases; iii) priority treatment for the goods and services they produce. This will be equal to that granted to local firms in the implementation by both governments of bilateral initiatives introduced during the economic integration and cooperation process; iv) the same treatment for their branches and subsidiaries; and v) the right to freely transfer profits from their investment to their country of origin, after due payment of taxes, and to repatriate their share of social capital in accordance with each country's



legal regulations. The same holds true for their branches and subsidiaries.

Another set of rules favors business agreements within the sub-region. This is Decision 3, approved on December 1991 by MERCOSUR's Council, regarding the terms of reference for sectoral agreements. As for the Decision's legal standing, suffice to point out that the Council is MERCOSUR's supreme body. Its role is to guide the Agreements' policies for the fulfillment of the objectives set forth in the Treaty of Asunción.

The said Decision regulates sectoral agreements. Its main objective is to facilitate integration among each country's sectors by promoting rationalization and complementation between markets and associations in order to compete efficiently within MERCOSUR and in other markets. The Decision also deals with environment's conservation and improvement issues, as well as with research and development in the field of products' and processing technology. The Decision's regulations cover different types of business associations, such as consortia, mergers and acquisitions, mixed ventures and others. (COSTA, 1993).

## **VI. The Social-Labor Dimension**

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As already mentioned, the Asunción Treaty did not fully incorporate social and labor issues into its guidelines. The issues of migrations and other labor issues were incorporated only by implication, as offshoots of future labor mobilizations resulting from the strengthening of the common market. However, very soon this situation was corrected and these issues began to be incorporated in the Treaty's guidelines.

On May 1991, just three months after the signing of the Asunción Treaty, the Labor Ministers from MERCOSUR member countries met in Montevideo. In the Declaration issued, they acknowledged the need to pay attention to MERCOSUR's labor and social issues in order for integration to improve labor conditions within the Treaty's signatory countries. On the same date, the creation of Working Sub-Group N° 11 was announced. This began operations by mid-1992.

The Ministers also accepted the possibility of studying the endorsement, within the Asunción Treaty, of «an instrument dealing with the unavoidable labor and social issues that will derive from the implementation of the Common Market of the South» Finally, they agreed to lend each other «all the cooperation needed in order to exchange information on each other's rules concerning employment, social security, professional train-

ing and individual and collective labor relations». Within the context of these commitments, on June 26, 1992, the Working Sub-Group N° 11 for the Study of Labor Relations, Employment and Social Security, was formally established in Las Leñas. Following the Ouro Preto meeting, this sub-group became No. 10 and was restructured as to the issues it would cover.

Given the stage of integration within MERCOSUR, the labor issues that have received privileged attention so far are those stemming from the establishment of a free trade area or a customs union. Of particular concern is how labor costs (salaries plus additional benefits) bear on the relative competitiveness of member countries, at the national, sectoral and business levels. This issue, by the way, has also been a cause of concern among developed countries in their trade agreements with developing countries. Witness, for example, the protocols on labor and the environment promoted by the United States within NAFTA.

Labor and social security problems will be detected with greater precision only as MERCOSUR's economic integration strengthens. The issues of adaptation, coordination and harmonization of labor, and social security policies will gain greater momentum as progress toward the common market brings them naturally to the negotiating table. The same thing will happen with the review of migration policies

or the comparative study of employment structures, recognition of academic degrees or the right to practice liberal professions in another member country.

As progress is made toward the creation of a free market where production factors and people circulate freely, the need will be felt, increasingly, for the establishment of a «social space» in which a minimum platform of rights and guarantees for MERCOSUR's peoples is honored. On this issue, the adoption of a Multilateral Agreement on Social Security, the drafting of which is well advanced, is being put on the fast track.

## VII. Relations with Countries from Outside the Sub-Region

Let us review briefly MERCOSUR's relations with countries from outside the sub-region, differentiating between those from Latin America, the hemisphere and outside the region.

The South American countries with the most dynamic and important ties with MERCOSUR are Chile and Bolivia. During

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the current nineties, Chile's and Argentina's trade, investment and physical integration ties have grown enormously. MERCOSUR countries have indicated to Chile that it would be welcomed into the group. However, MERCOSUR's common external tariff, which fluctuates between 0% and 20% with an 11.3% average, is an important obstacle to Chile's full membership. This country's common external tariff is set at the single 11% level. Another obstacle has been the Chilean economy's greater stability compared with that of its neighbors who are still struggling to achieve internal stability. Nevertheless, de facto integration between Argentina and Chile has reached such a high level that fluctuations in the first country's economy are felt in that of the second. Chile's investments in MERCOSUR and its physical integration with Argentina (highways, tunnels, railways, gas pipes, etc.), are increasingly strong. Chile's geographical position as transit route for MERCOSUR's economic relations with the Asia Pacific countries grant it strategic importance within the group. Therefore, even though it has not decided whether to join fully or not, Chile did decide to negotiate with MERCOSUR to preserve the trade preferences it had obtained and to work toward a comprehensive agreement covering services, investments and physical integration.

On June 1996, the Chile-MERCOSUR Agreement was signed, in spite of opposition from some internal sectors. Businessmen from the traditional agricultural sectors (wheat, corn, rice, etc.), in particular, have protested vehemently against the terms of the negotiations which set a definite timetable for them to improve their competitiveness in these products or reconvert. In spite of protests, the Chilean Government stood by its decision, with the support of the industrial chambers of commerce. Chile's decision to associate itself with MERCOSUR (even if not fully) gained momentum following the delays and doubts regarding its participation in the North American Free Trade Area.

Even though Bolivia is an Andean Group member, its trade relations with MERCOSUR, particularly with Argentina and Brazil, are very important. On December 1995, Bolivia signed its first agreement with MERCOSUR, on the so-called «historical heritage» (previously granted concessions). Presently, the second negotiating round on a Free Trade Agreement with MERCOSUR has been concluded. Even though Bolivia is a full member of the Andean Community its trade and investment interests are very much divided, at the regional level, between

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*Chile's investments in Mercosur and its physical integration with Argentina are increasingly strong.*

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the Andean Community and MERCOSUR. This poses keen strategic dilemmas for the Bolivian Government as to how to reconcile its position as an Andean country with its economic interests with MERCOSUR.

Bolivia's signing of the Free Trade Agreement renders its full membership within the Andean Community compatible with a preferential access to MERCOSUR. If Bolivia were to become a full member of MERCOSUR, it would have to renounce its affiliation with the Andean Community since MERCOSUR prohibits its members from belonging to any other sub-regional agreement.

In the Ouro Preto Protocol reference is made to resuming the negotiations on the partial agreements signed by MERCOSUR countries with other ALADI members. The aim is to progress toward the articulation and convergence of existing agreements.

As a way toward convergence, MERCOSUR suggests an approximation to the rest of South American countries based on Brazil's 1993 proposal to create a South American Free Trade Area. At the same time, negotiations are under way between MERCOSUR and the Andean Community to create a free trade area between both integration schemes. Should this second alternative come to fruition, a decisive step will have been taken in the network of negotiations needed to create a South American free trade area.

Reference must also be made to hemispheric relations. Following the December 1994 Miami Summit Meeting, the Denver Ministerial Meeting took place in mid- 1995. Its objective was to initiate the process toward the creation of a hemispheric free trade area by the year 2005.

On that occasion, MERCOSUR proposed the creation of five working groups in those areas where the beginnings of an agreement were underway (market access, investments, trade measures, customs procedures and technical guidelines). The United States, on the other hand, proposed the creation of eleven working groups including environmental and social issues. Finally, seven working groups were created dealing with: market access, investments, subsidies and trade sanctions, customs procedures and rules of origin, sanitary and phytosanitary measures and technical guidelines.

On March 21, 1996, the Second Ministerial Meeting on Trade took place in Cartagena de Indias. The mood at the meeting was less enthusiastic than on previous occasions. This was due, in part, to some frictions or stumbling blocks in the United States' relations with several Latin American and Caribbean nations (to

which we will return later) and, partly, to the hardening of MERCOSUR's negotiating position under the leadership, in this case, of Brazil.

One of the Ministerial Meeting's few concrete results was the creation of four more working groups: Government Procurement, Intellectual Property Rights, Trade in Services and Competition Policies. Nevertheless, the Meeting did not succeed in defining a minimum framework of terms of reference to initiate negotiations, at least in some sectors, toward the 1997 Ministerial Meeting to be held in Brazil. It was precisely Brazil's representation who pointed out the danger of taking «shortcuts» that might unduly speed up the creation of a Free Trade Area for the Americas, to the detriment of other commitments included in the timetables adopted by subregional integration agreements or the World Trade Organization. In summary, it is Brazil's position, supported by other MERCOSUR members, that hemispheric integration must be achieved through the strengthening and convergence of sub-regional agreements, and not through the adoption of new commitments which supersede those already approved at the sub-regional level and at the WTO level.

The increasing incorporation of new countries to NAFTA met with serious stumbling blocks during 1995, when the USA Congress denied the Executive the approval of the fast track for the negotiation of new trade agreements. This thwarted (or, to the least, postponed) Chile's joining of NAFTA. Also, throughout 1995 and 1996, several frictions and difficulties arose in United States' relations with NAFTA members and other Latin American countries. Mexico's economic crisis following the devaluation of the Peso (tequilazo) created uncertainty and friction between this country and the USA. Moreover, the tightening of the United States' embargo on Cuba was criticized not only by other Latin American countries but also by Canada, a member of NAFTA and an important investor in that Caribbean country. Finally, the so-called «de-certification» of Colombia also caused frictions with this country. These developments, together with the strengthening of isolationist tendencies opposed to Latinos' migration to the USA, have altered the environment of hemispheric relations, to the detriment of the objectives set forth at the Denver Summit. However, lately the Democratic Administration has begun to voice an interest in strengthening hemispheric

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integration efforts. Be that as it may, this political option still meets with strong internal political opposition.

It should be pointed out that NAFTA's participation in total MERCOSUR exports has decreased from 23.6% in 1990, to 16.9% in 1995 (IDB, 1995).

MERCOSUR's relations with the European Union have strengthened considerably. Relations between both blocs began in April 1991, when MERCOSUR's Ministers of Foreign Affairs formally notified the European Commission of the creation of the new Sub-Regional Agreement. On May 1991, a Joint Consultation Committee was established to provide technical assistance and institutional support from the EU to MERCOSUR. The idea of creating a free trade area between both blocs began to develop between 1994 and 1995. On December 1994, a memorandum of understanding was signed, aimed at liberalizing reciprocal trade, intensifying social and economic ties between both regions and bolstering European Union's technical and financial support to MERCOSUR.

The Inter-Regional European Union-MERCOSUR Trade and Economic Cooperation Framework Agreement was signed on December 15, 1995, in Madrid. It is the first inter-regional agreement signed by two customs unions based on the principle of reciprocity. This covers a wide range of commitments on trade and other economic issues as well as cultural and political issues.

The Agreement is based on the signatory parties' respect for democratic principles and for the fundamental human rights embodied in the Universal Declaration on Human Rights. Among other issues, the parties agree to: i) increase and diversify their trade flows; ii) promote economic cooperation in order to strengthen their international competitiveness and stimulate technological and scientific development; iii) support MERCOSUR's integration objectives; iv) seek closer cooperation between their respective institutional structures; v) strengthen cooperation ties on the issues of training, education and culture; fight drug traffic, etc.

As for the institutional structure, the Agreement creates a Cooperation Council responsible for supervising its developments. It is formed by members of the European Union's Council and Commission, on the one hand, and by members of MERCOSUR's Council and Common Market Group, on the other. This Cooperation Council will be assisted by a Joint Committee which will meet at least once a year, in Brussels and, alternately, one of MERCOSUR's member countries. The Joint Committee met for the first time in Brussels and was

presided by President Carlos Menem, as Argentina held MERCOSUR's pro-tempore presidency at the time.

A process has thus begun aimed at creating a free trade area by the beginning of the next century. To this end, a Joint Trade Sub-Commission was established in order to single out, with the assistance of several working groups, «sensible» products and prepare the agenda for the creation of the future free trade area. On November 1996, the Joint Trade Sub-Committee met for the first time in Brazil. The European Union' Common Agricultural Policy is the main difficulty that will have to be faced on the subject of trade liberalization.

It must be pointed out that the EU is MERCOSUR's main trade partner. MERCOSUR's trade relations with the EU are more important than its relations with the United States. Approximately 27% of MERCOSUR's trade is with the EU, compared with 17% with the USA. Similarly, MERCOSUR is the recipient of approximately 70% of European Union's investments in Latin America. Also the majority of MERCOSUR's direct investment stock, 36%, originates from the EU, compared with 32% from the USA. These numbers differ from those for Latin America as a whole. The region's trade data indicate a closer relationship with the USA due, partly, to Mexico's and Venezuela's (to a lesser extent) close trade links with their Northern neighbor. However, the volume of investment originating from the USA during the nineties is much higher than that of investment from the European Union, which would seem to indicate a relative weakening of economic ties with the EU, compared with the United States.

## VIII. Conclusions

The growing liberalization of hemispheric trade may possibly lead to «economic» Pan-American integration under USA leadership. Similarly, and much more probable, that integration process will occur between the United States and its immediate sphere of influence in Latin America, that is, Mexico, Central America and the Caribbean.

On the other hand, the profound integration process between Latin American and Caribbean countries will probably polarize them into two regions: South America on the hand and Central America, Mexico and the Caribbean on the other. The first such deep integration area would take shape around Brazil, the second

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*The deep integration process between Latin American and Caribbean countries will probably polarize them into two regions: South America on the one hand and Central America, Mexico, the Caribbean on the other.*

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around Mexico. The latter, however, would be subordinated to the United States market and, probably, would join NAFTA.

Finally, MERCOSUR's strategic role in South America's future integration explains the interest in an analysis of this integration scheme. The Argentina-Brazil axis generates a gravitational force which will pull along other South American countries. Brazil is the strategically decisive actor in South America's socioeconomic integration.

An economic integration agreement between Brazil and its South American neighbors –only Chile and Ecuador do not share a border with Brazil– through MERCOSUR requires the latter's full participation in order to balance Brazil's productive and negotiating power and to avoid creating a market area that mirrors the center-periphery type of relationship. Such scenario, improbable yet not impossible, would spoil the opportunity to turn South America's integration into an adventure amongst equals, the aim of which is shared development.

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**Which Mercosur Anyway?**

MERCOSUR is a member of the family of new regional pacts that have blossomed in Latin America with the liberalization that has taken place since the late 1980's. Contrary to some opinions, its intent is to expand and liberalize trade, both among members and with the rest of the world.

The following article argues that considerable liberalization, internal and external, has occurred in the MERCOSUR countries and such liberalization has benefited member and non-member producers- as well as MERCOSUR consumers.

MERCOSUR es miembro de la familia de nuevos pactos regionales que han florecido en América Latina con la liberalización ocurrida desde finales de la década de los ochenta. Contrariamente a lo que algunos opinan, su intención es expandir y liberalizar el comercio entre los miembros y con el resto del mundo.

En el artículo siguiente se afirma que en los países de MERCOSUR se ha dado un grado de liberalización considerable, tanto interna como externa, y que dicha liberalización ha beneficiado a los productores miembros y no miembros, así como a los consumidores de MERCOSUR.

Le Marché du Sud "Mercosur" est un membre de la famille des nouveaux pactes régionaux qui ont fleuri en Amérique latine dans la foulée de la libéralisation survenue depuis la fin des années 80. Contrairement à certaines opinions, il vise l'expansion et la libéralisation du commerce, ce à la fois entre ses membres et avec le reste du monde.

L'article ci-après fait état de la libéralisation considérable, au-dedans comme au-dehors, opérée au sein des pays dudit Mercosur et signale les avantages que ce processus a générés au profit des producteurs membres et non-membres, ainsi que des consommateurs du Mercosur.

MERCOSUL é membro da família de novos pactos regionais que florescem na América Latina com a liberalização ocorrida desde o final da década de oitenta. Contrariamente ao que alguns opinam, sua intenção é expandir e liberalizar o comércio entre seus membros e o resto do mundo.

No artigo seguinte, afirma-se que nos países do MERCOSUL tem-se observado um grau de liberalização considerável, tanto interna como externamente, e que a mesma tem beneficiado os produtores membros e não membros, bem como os consumidores do MERCOSUL.

# Which Mercosur Anyway?

➔ **Miguel Rodríguez Mendoza**

*Chief Trade Advisor, Organization of American States*

Over the past five years, the Mercosur countries exported to the United States and the European Union cars and car parts worth US\$ 3.4 billion. This, according to Mr. Alexander J. Yeats, a principal economist at the World Bank, could not have happened, as these «are highly capital intensive goods which (Mercosur) members have not been able to export competitively to outside markets». The fact that these goods are increasingly traded between Mercosur countries, Mr. Yeats argues, can only be explained by the high trade preferences that they have granted to each other in the auto sector. He presents this as «the most convincing, and disturbing, evidence produced so far concerning the welfare reducing effects of regional trade arrangements».

Focusing on the relatively rapid growth of intra-regional exports in the high-growth, relatively capital intensive auto sector, Mr. Yeats, in a draft Working Paper<sup>1</sup> which has been widely cited in the press, concludes that Mercosur diverts trade from patterns «expected on the basis of efficiency conditions and comparative advantage» by keeping tariffs and nontariff barriers much higher on imports from non-Mercosur countries than among members. Ultimately, the study argues, this will hurt the member countries by allowing producers to hide behind relatively high protectionist walls and focus on the comfortable Mercosur market—and thus remain globally uncompetitive. His findings, says Mr. Yeats, constitute a «smoking gun» that regional trade arrangements have an adverse impact on the world economy.

These conclusions may surprise analysts who have been following the evolution of the Mercosur. By focusing almost exclusively on intra-Mercosur exports, Mr. Yeats gives us only a partial picture of the trade pact. Reading his paper one has the impression that there is a «fortress» Mercosur whose main accomplishments could only be explained by its protected trade walls. No analysis is provided of the structure of protection in the Mercosur countries and the liberalization schedule which has been followed over the past five years. Nor does he mention the impact of protection on imports from third countries, an element

which is critical to any analysis of the world welfare effects of regional arrangements. One cannot focus only on the export side of the equation. Moreover, Mr. Yeats' conclusions on Mercosur rest solely on his analysis of the auto sector—one of the two sectors where Mercosur negotiations remained ongoing and where agreed rules did not yet apply during the time studied. The sector continued to be regulated by national industrial policies, only loosely coordinated at the regional level. It is perhaps on those policies rather than on Mercosur that Mr. Yeats should focus his concerns.

### **I. The Political Economy of Mercosur**

Mercosur can hardly be characterized as a protectionist trading arrangement. It is a member of the family of new regional pacts that have blossomed in Latin America in parallel with the liberalization that has taken place since the late 1980s. In contrast to the regional arrangements which existed in the 1960s and 1970s, whose purpose was to protect internal industries and

to isolate the economies from outside competition, the new arrangements are not constructed to shelter economies behind high tariff walls. Rather, their intent is to expand and liberalize trade, both among members and with the rest of the world, not to insulate themselves from outside competition.

And, indeed, considerable liberalization—internal and external—has occurred in the Mercosur countries. As can be seen in Table 1 the Mercosur tariff levels for all categories of products in 1986 were much higher than the ones that resulted from the implementation of

the Mercosur Common External Tariff (CET) in early 1995. The driving force behind this shift in tariff protection is the unilateral trade liberalization that started in Argentina in 1987 and in the other Mercosur countries at the beginning of the present decade. This new trend in trade policies influenced the nature and scope of Mercosur protection vis-à-vis the rest of the world. In most cases the CET was set at the lower prevailing rates in the national schedules. It has been estimated that Argentina reduced 40 percent of its tariff lines as a result of the CET<sup>2</sup>. Brazil agreed to accept lower tariff rates in the capital goods and the informatics sectors even though it had sought higher rates of protection.

Admittedly, the full CET will not be implemented until the year

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Table 1. Tariffs in the Mercosur

Tariffs and other border taxes in Mercosur, 1986-95

	Tariffs + other border taxes						Applied rates*			CET Mercosur
	1986						1995			
	Argentina	Brazil	Paraguay	Uruguay	Argentina	Brazil	Paraguay	Uruguay		
0 Food and animals	35,3	84,8	23,7	40,8	11,0	11,1	10,9	11,2	11,0	
1 Beverages and Tobacco	38,0	118,6	34,9	43,5	17,9	18,0	16,6	17,6	18,0	
2 Crude materials except fuels	37,9	56,6	20,9	30,3	5,3	5,2	5,3	5,1	5,3	
3 Fuels and lubricants	36,5	28,7	3,1	41,2	0,7	5,4	0,5	0,6	0,7	
4 Animal and vegetable oils	35,5	79,8	23,7	29,4	8,2	8,0	8,2	8,1	8,2	
5 Chemicals	33,8	66,9	10,6	28,8	8,9	8,8	8,2	8,3	9,0	
6 Manufactured goods	44,9	88,1	22,1	40,6	13,8	13,0	12,7	12,9	13,1	
7 Machinery and transport equipment	46,6	81,8	15,2	31,4	10,6	16,8	6,9	6,6	13,9	
8 Miscellaneous manufactures	44,6	99,6	27,7	41,4	16,8	16,6	14,8	15,3	16,2	
9 Others	28,1	74,2	30,0	21,9	7,1	7,1	7,1	7,1	7,1	
Average	40,9	79,8	20,1	35,8	10,9	12,0	9,6	9,7	11,3	

\* In January 1995 the Mercosur countries implemented the Common External Tariff (CET) on 85 percent of all goods. Each country has maintained a number of exceptions to the CET, which will be eliminated on a linear basis by 2006.

Source: Juan José Echavarría, « Tariffs, Preferences and Trade Expansion in the Mercosur », forthcoming.

2000—but the trend is clear: Mercosur is moving toward lower, not higher, levels of trade protection. As a result, imports, a major component of trade—and an area not addressed by Mr. Yeats—have increased noticeably. The reduction of barriers to trade has encouraged a flow of goods—both from partner countries and from the rest of the world. As shown in Chart 2, total imports by the Mercosur countries have increased by a yearly average of 22

percent between 1991 and 1995. Intra MERCOSUR imports grew at an average rate of 25 percent, imports from the European Union increased at a similar rate, and imports from the United States and the rest of Latin America grew at 21 and 20 per cent, respectively.

This is clear and convincing evidence that Mercosur is no trade fortress. On the contrary, since the establishment of the trade pact in 1991, the Mercosur's most important trading

partners have been able to increase their sales to the region at similar or only slightly lower rates than the Mercosur countries themselves. This reflects that trade liberalization in Mercosur has benefited member and non-member producers—as well as Mercosur consumers. This, again, is fully consistent with the new orientation of regional agreements in Latin America which are based on market reforms and trade liberalization. Mercosur has succeeded in eliminating tariffs and other trade restrictions for the bulk of trade among its member countries. At the same time, it has kept pace with trade liberalization vis-à-vis the rest of the world. This explains the behavior of the import sector.

It is true, as pointed out by Mr. Yeats, that intra-Mercosur exports have grown at rates well above exports to the European Union, the United States and the rest of Latin America (see Table 3). This is good news, and something that can be expected of countries that liberalize their reciprocal trade, especially two economically powerful countries such as Brazil and Argentina which were previously separated by significant trade barriers. Latin American integration arrangements have been criticized in the past for failing to increase trade among the participating countries. It seems ironic that they now be questioned for producing the opposite results. In fact, what Charts 2 and 3 show is that ever since the inception of Mercosur, the economic interdependence of its member countries has been growing steadily.

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*Trade liberalization in Mercosur has benefited member and non-member producers—as well as Mercosur consumers.*

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## Table 2. Mercosur Imports

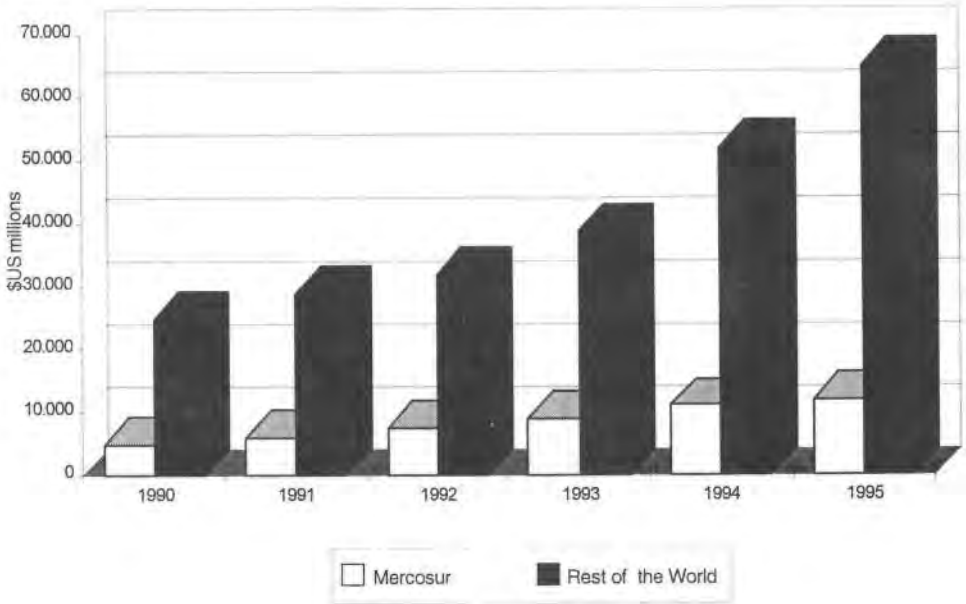
### Mercosur - Imports of goods, 1990-95

(\$US billions and percentage)

	1990	1991	1992	1993	1994	1995	Average Annual Growth 1990-95
From World	29	34	39	49	64	78	22%
From United States	6	7	9	11	14	16	23%
From EU	7	8	9	11	16	21	25%
From MERCOSUR	4	5	7	9	12	13	25%
From other LAC	5	5	6	7	8	11	20%
From Rest of World	8	9	8	10	14	16	15%

### Chart 2

#### Mercosur imports, 1990-95



Source: International Monetary Fund, Direction of Trade Statistics Yearbook 1996.

## II. The Auto Sector

Central to Mr. Yeats' analysis is the rapid growth of intra-regional trade in the relatively capital intensive auto sector, which he attributes almost exclusively to higher-than-average Mercosur trade barriers. Indeed, trade barriers continue to exist in this sector. Still, they do not by themselves explain what has happened in the auto sector, nor do they lead to the conclusion that regional trading arrangements are welfare reducing. At least three points are worth making. First, the auto sector, during the time period analyzed by Mr. Yeats, was excluded from Mercosur rules. Thus, it is at least inappropriate to attribute to Mercosur the faults of a sector where the rules of the game do not apply. Second, the policies that regulate the auto sector are *less*, not more restrictive than those applied a few years ago and have led to a surge of car imports from all sources, not just from the Mercosur countries. Third, the preferences that Mercosur countries have granted to each other in the auto sector are not much more significant than preferences in the other sectors and thus cannot explain the trade deviation claimed by Mr. Yeats.

It is managed trade, not free trade, that governs auto trade in the Mercosur countries. Both Brazil and Argentina apply a combination of tariffs, local content requirements and import quotas<sup>3</sup>. Mercosur rules will not apply to the auto sector until the year 2000, when tariffs will be set at 20 per cent and intra-Mercosur trade will be duty free. So it is not because of Mercosur, but rather in spite of it, that intra-Mercosur trade in automobiles has boomed in recent years. In general, existing policies in the sector are geared towards influencing investment decisions. In this sense, they have been very successful. As pointed

out in a recent survey by *The Economist*, «the modernization and expansion of the motor industry has been Mercosur's most visible business achievement. But it has not been due only to free trade. Industrial policy too has played a part. Unsurprisingly: governments the world over tend to regard an industry so big as too important to be left wholly to market forces».

Policies regulating the automobile sector are more liberal than they used to be. That is why the Mercosur countries have continued to expand their purchases of vehicles and vehicle parts from the rest of the world. Non-Mercosur originating imports of this sector increased from \$691 million in 1990 to \$6.1 billion in 1995. This represents an average annual increase of 69

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**Table 3. Mercosur Exports**

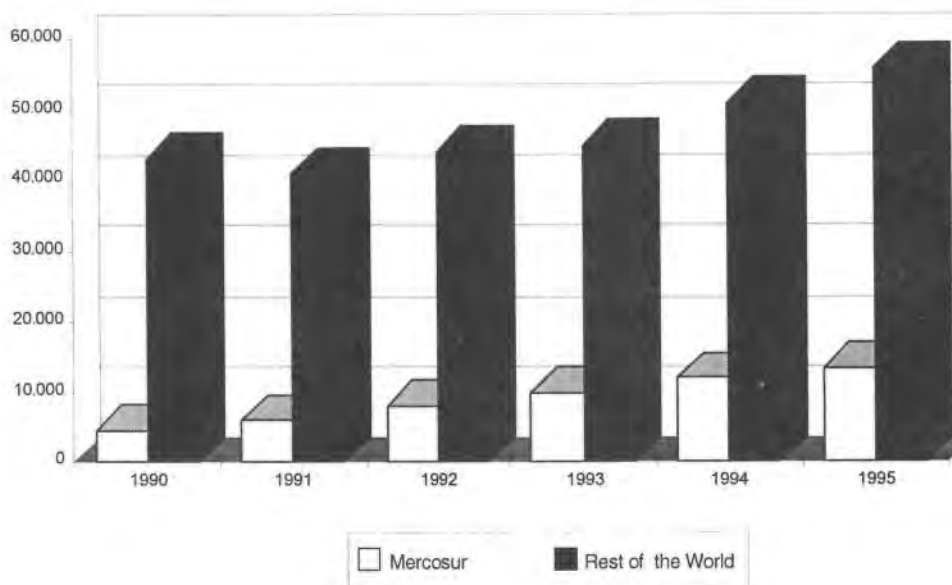
**Mercosur - Exports of goods, 1990-95**

*(in \$US billions and percentage)*

	1990	1991	1992	1993	1994	1995	Average Annual Growth 1990-95
To World	47	46	50	54	62	69	10%
To US	10	8	9	10	10	11	3%
To EU	15	15	16	15	17	18	5%
To Mercosur	4	5	7	10	11	13	32%
To other LA/C	4	5	6	6	7	8	18%
To Rest of World	14	13	12	14	17	20	9%

**Chart 3**

**Mercosur exports, 1990-95.**



Source: International Monetary Fund, Direction of Trade Statistics Yearbook 1996.

percent in imports from the EU, a 55 percent average annual increase in imports from the NAFTA countries, a 50 percent increase in imports from Japan and a 75 percent increase from other Latin American countries. So it is not only intra-Mercosur trade that is growing in the auto sector, it is trade from all sources. Mr. Yeats may be correct in his assessment that efficiency patterns in Mercosur auto trade are not optimal, but, if anything, gauging by recent trade and investment trends and the expected application of Mercosur rules to the automobile trade, there is hope for the continued trade *expansion* in this important sector.

Finally, an examination of the size of tariff preferences for the capital goods sector relative to tariff preferences in all other sectors does not indicate an explicit policy of promotion of this sector. Looking at the preferential margins given by the Mercosur countries to their partners, the evidence is inconclusive. Although preferential rates for the capital goods sector are higher than for other goods, the differential is not large enough to conclude that this preference is trade diverting. The preferential rate given by the Mercosur countries to their partners for all sectors other than capital goods in 1995 was 9.4 percent, countries and the rate of preference for the capital goods sector was 9.8 percent. Whether a difference of 0.4 points in absolute tariffs could cause such a large expansion of trade in capital goods among the Mercosur countries is highly questionable.

### **III. Mercosur: Stumbling Block or Stepping Stone?**

Although the concern expressed by Mr. Yeats in his study—that the new regionalism will divert attention from the multilateral negotiation process—is a legitimate one, this has not materialized. He assumes that trading nations are unable or unwilling to

pursue the objective of trade liberalization in more than one forum at a time. The fact that major trade liberalization initiatives such as Europe 92 and the Maastricht Treaty, the North American Free Trade Agreement, the Asia Pacific Economic Forum and Mercosur were all concluded in parallel with the ultimate success of the Uruguay Round of trade negotiations contradicts such a view. Also relevant is the fact that the majority of Latin American countries have undertaken large *unilateral* strides towards trade liberalization. They have reinvigorated their trading arrangements and committed themselves to further trade liberalization in the context of the Free Trade Area of the Americas Agreement—whose prepa-

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The majority of Latin American countries have undertaken large unilateral strides towards trade liberalization.  
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mitted themselves to further trade liberalization in the context of the Free Trade Area of the Americas Agreement—whose prepa-

ratory process is well advanced— while actively participating in the multilateral trading system.

Consistent with this approach, Mercosur has been reaching out to other countries, has concluded free trade agreements with Chile and Bolivia, and is currently negotiating with the Andean Group. In December of 1995 it signed a framework trade agreement with the European Union. As such, the Mercosur can be seen as a stepping stone on the route to further free trade. In addition, the economic links forged by Mercosur have strengthened political bonds of benefit beyond the trade arena. This was in evidence earlier this year when the solidarity of Mercosur members in opposition to the attempted military coup in Paraguay helped keep that country on the path of democracy.

Mr. Yeats is right in pointing out the need for the WTO to tighten its rules on regional arrangements. The Uruguay Round understanding on the interpretation of GATT Article XXIV, and the recent establishment of the Committee on Regional Agreements are moves in that direction. More surveillance by the WTO may lead to greater transparency in the functioning of regional arrangements. And greater transparency may help trade policy analysts to take a broader and more positive view of the impact of regional agreements on the world economy.

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*The economic links forged by Mercosur have strengthened political bonds of benefit beyond the trade arena.*

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## Notas

1. Alexander Yeats, «Does Mercosur's Trade Performance Justify Concerns About the Global Welfare Reducing Effects of Regional Trading Arrangements? YES!», unpublished World

Bank paper.

2. Bouzas, Roberto: «Mercosur and Preferential Trade Liberalization in South Americas: Record, Issues and Prospects», FLACSO,

May 1995.

3. Such policies have led some countries to express concerns in the WTO context, leading to the initiation of consultations on this issue.

**Economic Integration and Trade Relations in Central America**

*The Central American integration process is treated by this author as an integral part of the changes experienced by the subregion over the past ten years, marked by the return of peace, the implementation of a new development strategy, and the search for greater international insertion.*

*Within this setting, the author proceeds to analyze the challenges of Central American economic integration, the wide variety of trade negotiations under way, and most particularly, the ties to the United States of America.*

*El autor inserta el proceso de integración centroamericana en los cambios experimentados por la subregión en los últimos diez años que se caracterizaron por la conquista de la paz, la instrumentación de una nueva estrategia de desarrollo y la búsqueda de una mejor inserción internacional.*

*Sobre este telón de fondo, analiza los desafíos de la integración económica centroamericana, las variadas negociaciones comerciales en curso y, particularmente, los vínculos con los Estados Unidos.*

*L'auteur replace le processus d'intégration centraméricain dans les changements survenus dans la sous-région ces dix dernières années qui ont marqué la conquête de la paix, la mise en place d'une nouvelle stratégie de développement et la recherche d'une meilleure insertion internationale.*

*Sur cette toile de fond, il analyse les défis de l'intégration économique de l'Amérique centrale, les multiples négociations commerciales en cours et notamment les liens avec les États-Unis.*

*O autor insere o processo de integração centro-americana nas transformações sofridas pela região nos últimos dez anos, que se caracterizaram pela conquista da paz, pela instrumentação de uma nova estratégia de desenvolvimento e pela procura de uma melhor inserção internacional. Dentro desse panorama, analisa os desafios da integração econômica centro-americana, as diversas negociações comerciais em curso e, particularmente, os vínculos com os Estados Unidos.*

# Economic Integration and Trade Relations in Central America

↔ **Haroldo Rodas Melgar**

*Secretary General, Permanent Secretariat of the General Treaty for the Economic Integration of Central America*

*Lecture delivered at the II US-Central America Forum, held on March 12-13, 1997, in Guatemala.*

## I. Central America Today

The integration of Central America is a process subject to permanent evolution in terms of the conditions existing in the countries of the region as well as in the international context. Thus, it has learned to renew and redimention itself in order to face the realities of the new international trends in the political, economic and social fields. This explains how, after an extremely difficult decade, the Central American countries, acting as a bloc, succeeded in establishing the basis for a sustained model of development, achieving a new consensus among them, as well as regional strategies within the integration process.

In the second half of the eighties, the issue of economic integration in Central America acquired again a central position in the political agenda of this region. The Esquipulas Process, launched by the Central American Presidents with the purpose of obtaining a «firm and durable peace», signified an overwhelming effort to find an autochthonous solution to regional problems, and it has culminated in the recent subscription of the Peace Agreements that ended the Guatemalan conflict.

The nineties started with a positive outlook. The pacification of the region and the strengthening of democracy made possible processes of reform and reorientation of economic and social policies. In this sense, the process of economic integration matches converging national projects and an international context to which the region must adequate. Thus, in June 1990, the Central American Presidents reached an agreement to restructure, strengthen and reactivate the integration process, as well as its institutions, with the purpose of dynamizing and facilitating their adaptation to the new strategies of economic liberalization and modernization.

## 1. Overcoming Hard Times with a New Strategy for Development

In terms of economic policies, Central American countries have adopted, in the last years, new strategies of development aimed at obtaining a better position in international trade. These strategies grant priority to the rearrangement and modernization of the economies and imply the adoption of stabilization and structural adjustment programs and measures.

As the following economic data indicate, at the beginning of the nineties the Central American economies faced difficulties:

- A 2% growth of their Gross Domestic Product.
- An inflation rate of 37%.
- A fiscal deficit equivalent to 7% of the GDP.
- High rates of devaluation: Costa Rica with 23%, Guatemala with 47%, Honduras with 124%, El Salvador with 25% and Nicaragua with more than 1000%.

This situation could be explained by an inadequate allocation of resources, as well as by inefficient production and important external imbalances. Consequently, the Central American Governments developed stabilization and structural adjustment programs to eradicate these distortions. The purpose of stabilization was to reduce and eliminate the most obvious imbalances, while the purpose of adjustment was to modify the economic structure, eliminating once and for all the major deficiencies of the economic system. The results, by the mid nineties, are apparent in the following figures:

- A 4.2% growth of the GDP.
- An inflation rate of 14%.
- A fiscal deficit equivalent to 2.4%.
- Low rates of devaluation: Costa Rica with 19.1%, Guatemala with 2.3%, Honduras with 10%, El Salvador with 0% and Nicaragua with 13.4%.

Economic adjustment policies have resulted in the general stabilization of the economy and in an increase in production and exports. The Gross Domestic Product grew, in the previous decade, at negative rates, while in the nineties it exhibits positive grow rates. In 1996, the GDP amounted to US\$ 40 billion, which is higher than that of most Latin American countries.

The Governments of Central America are making major efforts to further the liberalization of their economies and to achieve their

successful insertion into international trade. This renewed vision of economic strategies and of public administration has allowed for convergence of national macroeconomic policies and has facilitated the consensus between Central American countries on fundamental economic issues.

## 2. A Better Position in the New International Order

The Central American effort to obtain a better position in the world economy is coherent with the deep structural changes that have occurred in international relations during the last decade. The end of the Uruguay Round and the creation of the new World Trade Organization, WTO, which is aimed at the regulation of multilateral trade relations, has resulted in the regulation of issues that include agriculture, textiles and apparel as well as services, government procurement, rules of origin and intellectual property. The evolution of multilateral trade relations will broaden WTO's field of action. This will have to deal with crucial issues like trade and environment, investments, and competitiveness policies.

Since 1995, all the Central American countries members of the Central American Common Market, are also members of the WTO (Costa Rica and Honduras since January 1<sup>st</sup>, El Salvador since May 7, Guatemala since July 21, and Nicaragua since September 3). Thus, Central American countries have had to modify their trade regulations in order to comply with their commitments within this new multilateral framework. Some countries have adopted general laws to apply the WTO agreements, while others have created ministerial level working groups to support the processes aimed at their implementation.

This new multilateral system is coherent with regionalism, that is, the strengthening and creation of economic blocs like the European Union, the MERCOSUR, the CARICOM, the Andean Pact, NAFTA and the Central American Common Market.

Globalization is the result of accelerated technological progress and of the internalization of production, technology, services and finances. Foreign investment and the world organization of trade and production acquire more importance in this context the modernization of the economies becomes urgent in order to improve their position in the world economy. That is, to partici-

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*The Central American effort to obtain a better position in the world economy is coherent with the deep structural changes that have occurred in international relations during the last decade*  
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pate in the global economy, economies and private sectors must become more efficient and competitive.

Within in the framework of regionalization and globalization, trade and investment are central elements for economic policy. Trade liberalization, increased exports, elimination of trade barriers and related measures, are policy instruments to achieve the modernization of the economies and an efficient access to the international market.

## **II. Economic Integration of Central America: the Tasks Ahead**

### **1. A New Integration**

The process of Central American economic integration must evolve within a context of international relations, the major poles of which are the United States, the European Union and Japan. It is around these that developing countries seek a better position in the rearrangement of international markets. This is the main task of the Central American Common Market.

To promote the integration of Central America implies considering several factors:

- The economic stabilization of each country, seeking regional convergence of macroeconomic and sectoral policies.
- Perfecting the Central American free trade area.
- Common external tariffs.
- Customs modernization.
- Infrastructure.
- Investment.
- Finance, and
- Coordination, harmonization and implementation of a common trade policy.

With regard to macroeconomic stabilization, distortions have been eliminated and the convergence of macroeconomic and sectoral policies is on its way.

Exchange systems are either more flexible or free. Monetary policy is closer to anti-inflationary policies and all the Central American countries have adopted a policy of zero net credit to the public sector. There have been qualitative changes in the use of instruments of monetary control; generally, open market operations are favored instead of portfolios limitations or fixed interest rates.

In terms of taxing, reforms have been undertaken with regard



to the main taxes (income, value added) and advances are being made for regional fiscal harmonization.

The Central American countries are implementing, with different intensities, policies aimed at the reduction of the relative size of the State and of its degree of intervention in economic activities.

The improvement of the free trade area can be seen in:

- The suppression of most trade barriers.
- The reduction of the number of goods subject to exceptions from the free trade regime, and
- The increase in trade between the Central American countries, which grew from US\$ 650 million in 1990 to US\$ 1600 in 1996.

The Central American free trade area is a way to advance toward strengthening the position of regional exports in terms of quality, opportunity and efficiency, as these conditions are harder to achieve individually.

Negotiations toward a common external tariff have progressed. So far, 95% of import tariffs are uniform; 2% are being harmonized; and only the remaining 3% refer to national tariffs with an important fiscal weight.

With regard to customs, modernization programs are being implemented. A new Central American Customs Code has been subscribed and personnel is being trained in specific areas.

Central America is directing efforts at the rehabilitation and extension of infrastructure in other sectors: land, air and sea transportation; customs facilities; ports; airports; and communications. At the same time, investments in the energy sector are being promoted as well as investments for productive activities. The modernization of financial services is coherent with this strategy.

With trade in services becoming more important every day, Central American countries are aware of the importance of adapting their legislation to the basic principles of the General Agreement on Trade in Services, GATS. With this purpose, discussions on a regional Project of Regulations on Trade in Services, which contains the proposal for gradual liberalization, are currently underway.

In terms of finance, the Central American Bank for Economic Integration plays an important role, both attracting and lending

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resources. Currently, CABEL has been declared eligible to perform joint operations with the European Investment Bank. Special projects of CABEL have supported, technically and financially, several programs such as: small and medium business in Central America (the PAPIC I and II programs); regional exports through a Fund for the Strengthening of Central American Exports, FOEXCA, which provides financial resources and technical support to modernize, expand, transform and rehabilitate exporting firms; the exports of Honduras and Nicaragua, through a Special Fund for the Promotion of Exports.

Strong impulse has been given to liberalizing and deregulating the financial system. The system of control and auditing has been strengthened in order to prevent practices that may destabilize the system. Moreover, the integration of insurance institutions and stock markets is being promoted with the support of the Central American Stock Exchange.

## 2. The Project on «Central American Competitivity»

Strengthening the economic integration process allows for the development of competitiveness through economies of scale made possible by the complementarity of national economies. In this sense, the project on Central American competitiveness undertaken by Mr. Michael Porter with the University of Harvard and INCAE, is playing an important role. The project is based on three areas:

- competitiveness,
- macroeconomy, and
- environment management and governability.

The project will deal with these areas in the fields of public policies for trade and competence; incentives for production protection (protection to investment, reform of the State, etc.); improvement of regional infrastructure (transportation, communications, energy, higher education, integration of financial markets, of communications and information); regulations (environment management) and governability (improvement of the regional institutions and development of a strategy of communications).

Many of these tasks have already been undertaken by Central American countries within the framework of the integration process, so that there is a close coordination between this project and SIECA.

Central America is involved in several trade negotiations aimed at facilitating access to other markets and creating adequate conditions for foreign investment.

Relevant negotiations include:

#### 1. Free Trade Area of the Americas

As a result of the Hemispheric Summit of December 1994, Central America, like the rest of the countries of the Hemisphere, started negotiations for a free trade area that will include all the countries from Canada to Argentina and the Caribbean. So far, two meetings have taken place in Denver, Colorado, in June 1995, and in Cartagena de Indias, Colombia, in March 1996. A third meeting will take place in May 1997 in Belo Horizonte, Brasil. Within this process, eleven working groups have been established:

- Access to markets.
- Customs regulations and rules of origin.
- Investment.
- Standards and technical trade barriers.
- Sanitary and phytosanitary measures.
- Subsidies, antidumping and countervailing duties.
- Smaller economies.
- Government procurement.
- Intellectual property rights.
- Services, and
- Competitiveness policies.

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*Central America is involved in several trade negotiations aimed at facilitating access to other markets and creating adequate conditions for foreign investment*  
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The working groups in charge of Access to Markets, Investment and Intellectual Property are coordinated by Central American countries.

#### 2. Mexico

Costa Rica signed a free trade agreement with Mexico in January 1995 and the other four countries are negotiating with this country. After these negotiations are over, parties will converge in order to subscribe a single agreement with Mexico.

### 3. Other Negotiations

The Governments of Central America have given high priority to negotiations with the United States of America, Panama, the Caribbean Common Market and Chile. Within this context, proposals are being prepared.

## IV. Relations Between Central America and the United States of America

### 1. A Mutually Beneficial Partnership

The United States is the major trade partner of the Central American region. It represents more than 55% of Central American trade, not taking into account assembly activities or maquila.

This implies a deep relationship between this region and the United States, particularly if we consider its links with the US in other fields –services, investment and financing. Even more, migration flows to that country and the transfer of resources to the Central American countries are also an important those part of this relationship.

On the other hand, Central America has a special importance for the United States, since its trade flows with the region are higher than those with other larger Latin American countries. Data from the United States Trade Department show that, in 1995, the United States exported US\$ 6000 million in goods to Central America, which places this region in the third place among Latin American countries, after Brazil and above Colombia, Argentina and Chile, among others. If Mexico, which benefits from NAFTA, is excluded, Central America is holds the second place after Brazil.

#### United States

#### Trade with Latin American Countries, 1995

*(Thousands of millions of dollars)*

Country	Exports	Imports
Mexico	45.5	61.7
Venezuela*	4.6	9.7
Brazil	11.4	8.8
Central America	6.0	5.7
Colombia	4.6	3.7
Argentina	4.2	1.8
Chile	3.6	1.9

Includes oil exports.

Source: United States Trade Department.

With regard to imports, Central America is in third place among Latin American countries, Mexico excluded, with only Brazil and Venezuela (which exports mostly oil) above it.

Central American exports to the United States include, mostly, textiles, garments and sugar. Central America is the second exporter of sugar to the United States in Latin America, after Brazil. This product is the second in importance for the region in terms of currency income.

Trade relations with Central America favor the United States. Between 1992 and 1995, the trade balance has been positive for the United States to up to US\$ 1800 million, though there is a clear trend of decreasing surpluses—from US\$ 500 million in 1992 to US\$ 300 million in 1995.

## 2. Preferential Regimes

As part of its trade policy, the United States grant preferential treatment to imports from Central American countries through two regimes: the General System of Preferences, GSP, and the Caribbean Basin Initiative, CBI. Products not included in these regimes are subject to regular tariffs. In 1994 the total value of commodities imported from Central America was US\$ 4746.9 million, of which 47% was affected by either the Most Favored Nation treatment, the CBI or were goods with zero tariff.

### United States Imports from Central America by trade regime, 1994

*(Millions of dollars and percentages)*

Regime	Value (Millions of US\$)	Share (%)
Subject to no tariffs	2,228.7	47.0
Subject to tariffs	2,518.2	53.0
<b>Total exports</b>	<b>4,746.9</b>	<b>100.00</b>

## 3. The Impact of NAFTA

When the NAFTA agreement was signed, approximately 85% of Mexican exports to the United States, which already benefitted from the MFN regime, were automatically exempted from import tariffs. This put Central America at a disadvantage with regard to Mexico. Besides losing the advantages of the CBI, Central

American exports lost competitiveness with regard to Mexican products, especially textiles and apparel.

The CBI has been useful to intensify trade relations between Central America and the United States, as well as to develop free market economies with an export vocation.

The fact that NAFTA grants Mexico better commercial preferences to access the United States market has resulted in the formulation of proposals intended to find mechanisms to improve Central America's conditions of access to that market, the most important for the region.

The importance of the products affected by NAFTA, especially textiles and apparel, is obvious. Central American exports of these products to the United States have been increasing consistently throughout this decade. In 1995 they represented 52% of total exports to the United States. In total, apparel imports in

the United States represent a market of US\$ 3600 million. The share of traditional exporters to the United States market has changed significantly. Hong Kong, China and Taiwan reduced their share sensibly between 1990 and 1995 (from 40.5% to 30%), while Mexican and Central American exports increased their share.

#### 4. The Future of Trade Relations

Central American countries are designing a new framework of trade relations with the United States, based on the strategic objective of reaching, by the year 2005, a Free Trade Area of the Americas which, as mentioned before would include many issues beyond the trade of goods.

Within this context, there are at least two options to follow.

One is the possibility of negotiating a project of «extended parity» which, besides including those products covered by the current CBI, would include those excluded and subject to preferential treatment for Mexico in NAFTA. The implementation of such a proposal would have fiscal implications for the United States. Thus, the Clinton Administration would have to make provisions for it in the Federal Budget.

Another option would be to sign a third generation free trade agreement between Central America and the United States. To do this, the Government of the United States would have to

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*Central American countries are designing a new framework of trade relations with the United States, based on the strategic objective of reaching a Free Trade Area of the Americas by the year 2005*  
 ”

obtain authorization for the fast track which authorizes the President to negotiate bilateral or multilateral trade agreements.

Both options are not reciprocally exclusive, but are, rather, complementary and both constitute temporary mechanisms to reach, by the year 2005, the Free Trade Area of the Americas.

## **V. A final message**

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Central America is a region of peace, democracy and constant growth, a fertile field for foreign investment. The possibilities of integration and liberalization are broad, as the trade negotiations undertaken by Central America will open large markets ready to benefit from investments in this promising part of the world.

**Integration and Competitivity in a Globalized World: Outlook for the Andean Community**

*The Andean Group is still an enigma among recent Latin American integration agreements. As any integration process, it has had its highs and lows, however, at least in the field of trade, de facto integration between Andean Community members has grown. Within the context of a more globalized world, trade among AC countries has a bearing on the development of the region's economy, particularly on the development of its exports' competitiveness.*

*The article reviews the evolution of integration processes in Latin America and the role the Andean Community plays within such process. The AC trade flows with the region are then examined, as well as the effects of integration on competitiveness.*

*El Grupo Andino sigue siendo un enigma entre los acuerdos recientes de integración en Latinoamérica. Como cualquier proceso de integración, ha tenido sus altas y sus bajas; sin embargo, por lo menos en el terreno del comercio, la integración de facto entre los miembros de la Comunidad Andina ha aumentado. En el contexto de un mundo cada vez más globalizado, el comercio entre los países de la CA repercute en el desarrollo de la economía de la región, particularmente en el de la competitividad de sus exportaciones.*

*El artículo pasa revista a los procesos de integración en América Latina y al papel que la Comunidad Andina desempeña dentro de dichos procesos. Se hace un examen de los flujos comerciales de la CA con la región, así como de los efectos de la integración en la competitividad.*

*Le Groupe andin reste une énigme au regard des récents accords d'intégration latino-américaine. Comme toute processus d'intégration, il a eu ses hauts et ses bas, mais, au moins dans le domaine du commerce, l'intégration s'est en fait développée entre les membres de la Communauté andine. Dans le contexte d'un monde toujours plus globalisé, le commerce entre pays de la Communauté andine a une incidence sur le développement de l'économie de la région et notamment sur celui de la compétitivité de ses produits d'exportation. L'article rend compte de l'évolution des courants d'intégration en Amérique latine et du rôle qu'y joue la Communauté andine. Les flux commerciaux de la Communauté andine avec la région y sont examinés, tout autant que les effets de l'intégration sur la compétitivité.*

*O Grupo Andino continua sendo um enigma entre os recentes acordos de integração na América Latina. Como qualquer processo de integração, tem tido seus altibaixos; no entanto, pelo menos na área do comércio, a integração entre os membros da Comunidade Andina, de fato, tem aumentado. No contexto de um mundo cada vez mais globalizado, o comércio entre os países da CA repercute no desenvolvimento da economia da região, principalmente no da competitividade de suas exportações.*

*O artigo faz uma revisão nos processos de integração na América Latina e no papel que a Comunidade Andina desempenha dentro desses processos. Examinam-se os fluxos comerciais da CA com a região, bem como os efeitos da integração na competitividade.*



# Integration and Competitiveness in a Globalized World: Outlook for the Andean Community

## ♦ Mercedes Araoz

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*This article is based on the paper with the same title presented during the SELA/CEFIR Seminar «Regional Integration and the Challenge of Competitiveness and Convergence», which took place in March, 1997 at SELA's Headquarters, in Caracas.*

## I. Introduction

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The Andean Group (GRAN) is still an enigma among the recent Latin American integration agreements. When, on March, 1996, the VIII Andean Presidential Council met in the city of Trujillo, Peru, it injected new life into the Group by creating the Andean Community (CA) and the Andean Integration System. This is a more dynamic and agile structure aimed at boosting market liberalization and promoting greater cooperation among member countries. However, there is still a certain degree of uncertainty regarding some issues, particularly Peru's position on the free trade area and the customs union.

The fact that this integration process has had its back and forths is not new, nor is this the exclusive prerogative of the AC. The highs and lows are to be seen as the logical outcome of a negotiating process involving different interests. Nevertheless, it is interesting to point out that, at least in the field of trade, de facto integration between Andean Community's members has indeed grown. Within the context of a more globalized world, trade among AC countries has a bearing on the development of the region's economy, particularly on the development of its exports' competitiveness.

## II. The Evolution of Integration Processes in Latin America

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During the first half of the century, the level of trade among

Latin American countries was very low. In 1938, it represented only 7% of total exports and by 1954 it had increased to 10,4%. Trade links between the region began to strengthen only recently, in the sixties and seventies. This was due to the fact that Latin American countries began a process of regional association aimed at stimulating industrialization in order to decrease Latin America's dependence on the rest of the world and to increase its economic growth. (1)

During the eighties, the foreign debt crisis, the fall in prices of Latin America's main exports and the implementation of populist economic policies, originated a recession in the region's economies which lowered inter-regional trade. ALADI member countries' inter-regional trade as a percentage of total exports fell from 13,7% in 1980 to 8,4% in 1985 (Table 1). This fall was even greater among Andean Group countries.

The beginning of the nineties saw a shift in the region's integration processes. On the political side, the consolidation of democratic governments, the political commitment to open markets and the existence of similarities among the region's policies demonstrated that the process was politically viable. In addition, the success of the Free Trade Agreement between the US, Canada and Mexico, as well as the creation of the European Community injected new life into sub-regional and regional integration agreements. (2) This is apparent if we consider the great number of agreements signed within the region during this decade.

**Table 1**  
**Share of Inter-Regional Trade in Each Group's Total Trade**  
(in %)

	1965	1980	1985	1990	1992	1995 *
ALADI	9,9	13,7	8,4	12,1	16,7	17,5
CACM	17,8	25,4	15,5	16	19,8	24,5**
GRAN	1,2	4	2,6	4,2	7,9	11,9
MERCOSUR	14,5	8,5	9,8	14,5	18,4	22

\* Calculations based on partial estimates.

\*\* 1994 figures.

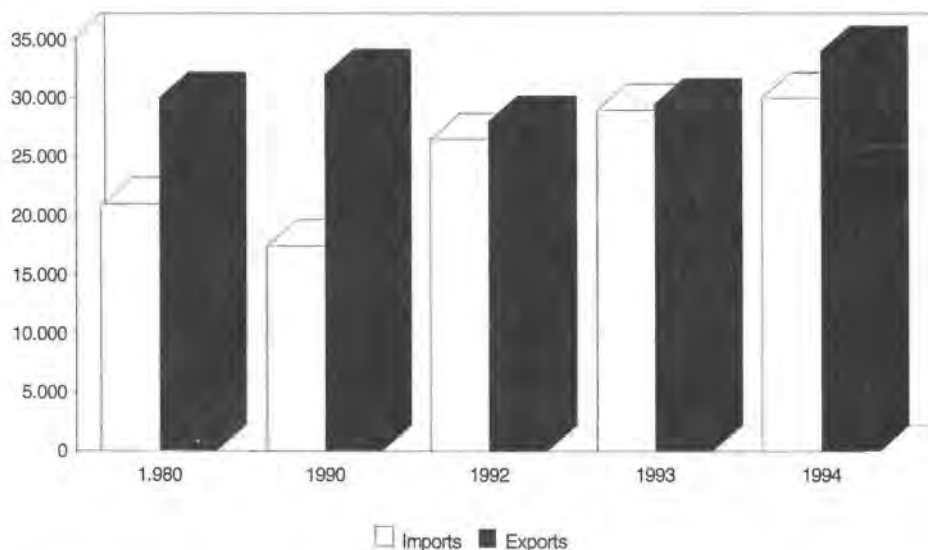
Source: ECLA. CIMTRADE Data Base, United Nations.  
Calculations made by the author.

Thanks to the implementation of political and economic reforms and to the proliferation of bilateral and multilateral trade agreements, inter-regional trade has increased significantly since the beginning of the nineties. In 1995, inter-ALADI exports accounted for 17,5% of the region's total exports, compared with 8,4% in 1985. (See Chart 1).

Another important trait of regional trade is that trade within integration groups has also grown significantly. In this context, trade among Andean Group countries has been the most dynamic (3), followed by MERCOSUR. Inter- group trade in these schemes has more than doubled its participation with respect to total exports (Table 1).

Exports of manufactured goods have increased within inter-regional trade. In 1985 these accounted for 45% of total exports to the region, while in 1992 this percentage had increased to 62,2%. However, Latin American exports of manufactured goods to the rest of the world have not been very dynamic, even though they have grown in recent years. In this context, the competitive position of dynamic sectors did not exhibit significant growth between 1980 and 1993.

**Chart 1**  
**Evolution of Andean Group's Trade Flow with the World\* (1980-1994)**



\* Includes Latin America and the Caribbean.

Source: ECLA. Calculations made by the author.

However, closer trade links between integration groups is not reflected in trade flows between such groups. In this context, trade links between the Atlantic Basin countries and those on the Pacific Basin have not strengthened enough. In Latin America, relatively close trade relations occur only among neighboring countries, while they tend to disappear among countries distant from each other. This is made worse by the little importance some Latin American economies attach to the region's market.

### III. The Andean Community's Trade Flows

According to ECLA figures, in 1995 Andean Group exports reached \$40 billion. This is a 40% increase compared with exports at the beginning of the decade. This huge rise is a result of the sub-region's trade liberalization process and the significant boost in inter-regional trade. Between 1992 and 1995 inter-regional trade doubled to \$4,7 billion, 11,7% of GRAN's total world exports.

The Andean Group's world trade flows register a surplus (Chart 1). The Group's world exports more than offset its growing imports as a result of open market policies and the new growth rate of the region's economies. However, an analysis of trade flows in manufactured products with the rest of the world

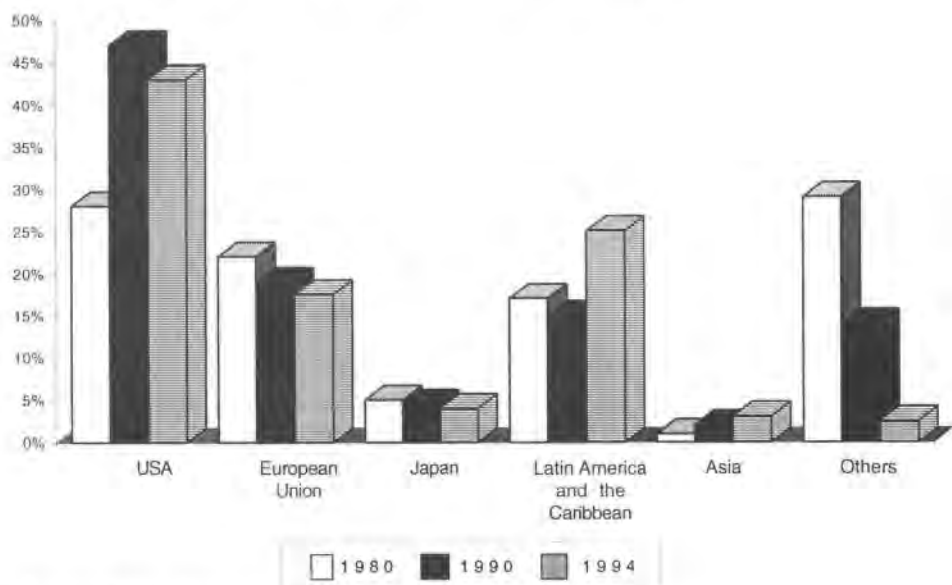
indicates that GRAN is a net importer of such products, even though its manufactured goods' exports have risen slightly. This is because GRAN's exports to the world consist mainly of light industrial products, whereas its imports from developed countries are in high technology products and capital goods.

Given that manufactured products are the most dynamic component in world trade, the region has a long road to travel to be competitive in such sectors. Perhaps integration among similar countries could stimulate the development of higher value added products by taking advantage of the benefits offered by economies

of scale.

In spite of its growth, GRAN's inter-group trade by no means reaches the level of such groups as MERCOSUR. In 1995 trade among MERCOSUR countries doubled compared with 1990, reaching a total of \$15,8 billion, i.e. 22% of total MERCOSUR exports. Granted the differences in both markets's scales, it would be interesting to evaluate to what extent inter-regional trade within the Andean Group may reach the levels of

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*Given that manufactured products are the most dynamic component in world trade, the region has a long road to travel to be competitive in such sectors*  
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**Chart 2****Destination of Andean Group's Exports (1980-1996)**

Source: ECLA. Calculations made by the author.

MERCOSUR, considering the importance in such flows of manufactured goods.

A change has occurred in the structure of the Andean Group's export markets (Chart 2). In 1980, the United States was the main market, receiving a little less than 30% of total AG exports, followed by the European Union with close to 22%. By 1990, 46% of total exports went to the United States, while exports to other markets decreased, with the exception of exports to Asia, which grew to 2% of the total. However, by 1994, exports to the US decreased to 43%, as was the case with other regions except Asia which received 3% of total exports, and Latin America and the Caribbean, whose participation grew considerably from 16% in 1980 to 25% in 1994.

As far as imports are concerned, the United States is the Andean Group's main provider, even though its relative participation in this market has decreased from 43% in 1980 to 34% in 1994. Latin America's and the Caribbean's share, on the other hand, has increased from 13% in 1980 to 25% in 1995, while that of the Asian countries surged from 2% to 5% during the same period. This illustrates the growing importance of the Latin American market for the region's exports. In the case of the

Andean region, it is significant to note that Latin America represents a growing market as well as a growing provider. This indicates that the sub-region's neighbors are a natural market for its trade.

Nevertheless, in Latin America relations between groups of countries are only beginning. The Andean Group receives only a little over 4% of MERCOSUR's exports, while only 3,6% of GRAN's exports go to MERCOSUR. The MERCOSUR-GRAN trade balance is negative for the latter. Also, the products traded are the same as those which GRAN trades with the rest of the world. Primary products -fuel, metals and minerals and agricultural products- are the major exports, while manufactured goods, followed, at a much smaller scale, by agricultural products are the major imports. As for GRAN's trade with other regional groups, in the case of the Central American Common Market (CACM) fuel is the major export, followed by manufactured products.

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 countries are only  
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In the case of trade between countries belonging to a group the situation is different. For MERCOSUR, trade in manufactured and agricultural products is more important. In the case of GRAN, trade in fuel is rather high (21%), but without it manufactured products represent 60% of inter-regional exports, i.e. 47% of the total. The export share of manufactured products has grown during the last years, followed by that of agricultural goods. On the other hand, the share of fuel, metals and minerals and other raw materials in inter-regional trade has decreased in terms of relative importance.

By 1994, industrial inputs, mainly mineral, chemical and pharmaceutical products and agricultural and livestock industrial products, were the major inter-regional exports, followed by transportation vehicles, transportation equipments, fuels and agricultural products. These exports reached a total of \$2,4 billion and accounted for 68,6% of the region's total exports.

On the other hand, Venezuela and Ecuador are the main exporters of oil and other fuels. Colombia's exports of these products have also risen in recent years, due to the discovery of new deposits. As for trade in products for the livestock industry, the major ones are soja and its by-products, from Bolivia; sugar and related products, from Colombia and Bolivia; cotton and cereals also from Bolivia, among others. Mineral products originate mainly from Peru and Bolivia. These are: zinc, tin, silver, lead and copper. Fish flour is another important export.

Peru is the main exporter of fish flour, followed by Ecuador, which entered the market in 1994. Colombia is the main exporter of pharmaceutical products.

Exports of apparel and other textile goods have decreased noticeably within the region, due to competition from Asia. Peru's exports in these items are the most affected, resulting in a sharp drop in production.

At the beginning of 1995 the common external tariff entered into force. It envisions five tariff brackets with a 20% maximum tariff level depending on the product's percentage of added value; that is, the higher the processing the higher the tariff. This common tariff replaces 95% of all tariffs. However, Peru and Bolivia decided to maintain their lower tariffs and to continue their bilateral negotiations on tariff preferences. Therefore, Venezuela, Colombia and Ecuador are the only countries to which the common external tariff applies. They all have signed bilateral industrial and trade complementation agreements.

As for the share of Andean countries' exports to the sub-region, Colombia and Venezuela participate strongly, followed by Peru and Ecuador, while Bolivia only covers 5,7% of such trade (Table 2). In 1991 Colombia became GRAN's main trading partner. Its exports to the group went from 14% of total exports, to more than 40% in later years. However, beginning in 1993 Colombia's GRAN market share began to decrease, while Venezuela's improved slowly. Nevertheless, in 1995 this situation changed substantially, as Colombia recovered its position in this market to the detriment of Venezuela, whose exports fell as a result of the country's economic crisis.

**Table 2**  
**Evolution of Share in Total Exports to GRAN by Member Countries**

(in %)

	1990	1991	1992	1993	1994	1995 *
Bolivia	4,5	4,6	4,5	4,2	5,7	4,8
Colombia 1/	28,0	42,9	45,5	39,7	32,4	38,8
Ecuador	14,2	11,2	8,0	10,3	11,3	7,8
Peru	16,1	14,9	12,1	9,4	9,0	8,9
Venezuela	37,1	26,4	29,9	36,4	41,6	39,7

\* Preliminary figures to September, 1995. 1/ 1995 figures are preliminary to August 1995.

Source: JUNAC. Calculations made by the author.

Ecuador's exports have behaved more erratically as far as share of total exports is concerned. This is around 11%. In 1995 Ecuadorian exports were affected by the conflict with Peru, but later they surged again thanks to price increases on all its exports.

On the other hand, the decrease in Peru's share of the Andean market, in spite of the increase in prices of its main exports, is a significant development. Data show that Peru has not benefited from Andean integration. The country lost the opportunity to increase its competitiveness through access to a greater market, as a result of which its industries have been left out of future hemispheric integration initiatives such as the Free Trade Agreement of the Americas (FTAA).

#### **IV. Integration as a Tool to Increased Competitiveness**

Often when we speak of competitiveness we are referring to its simpler concept: the total or partial increase of productivity in the factors of production of exportable goods. This definition is very narrow and, possibly, confusing, since it equates the concept of comparative advantages with that of absolute advantages. But we all know that trade occurs as a result of relative or comparative advantages. However, there is a wider definition. It refers to an economy's capacity for reaching increasingly higher standards of living, that is, a country's potential growth given its relative development level.( 6)

This kind of competitiveness implies more than an increase in productivity. It is the result of a complex web of economic, geographical, social and political factors that make up the structural basis of a nation's development. The decision to join a regional economic bloc may contribute to determine a nation's competitive level and, therefore, its ability to converge, in terms of economic growth, with relatively more developed countries.

The benefits derived from a customs union are usually evaluated in terms of the extent to which it creates or diverts trade. In general, greater benefits will depend on the degree of trade complementarity which exists before a country joins a trade union. As a general rule a small country should not join a trade union since the diversion of trade could be greater. Therefore, it would be best for it to stick to a wider multilateral liberalization.

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*The decision to join a regional economic bloc may contribute to determine a nation's competitive level*  
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This rule, however, is static and short term, since it does not take into account the effects of trade policy and market structures other than those with perfect competition.

It is precisely these last two factors which will determine the extent to which Latin American countries may benefit from preferential trade agreements. In the first place, it is true that in some cases the initial costs of integration may be greater than the benefits, since some uncompetitive industries may lose in the process. However, as time goes by, the benefits will become apparent. The more evident benefits are those related to economies of scale. Wider markets allow for reductions in production costs per unit and for increased production of related goods. This is more evident in the case of industries whose market structure is based on imperfect competition. (7) Generally, these are manufacturing industries. The most significant result is the expansion in variety and quality of products, which is a direct benefit for the consumer, and output and employment growth in participating economies.

The benefits derived from economies of scale are not only those a firm accrues internally but also those obtained from international yields, that is, from a company's specialization in particular sectors of the chain value. (8) Regional integration allows for better international distribution of labor among countries of the region. It also stimulates demand for production and commercialization services.

Additional benefits are those derived from outward-oriented economies which may be easily internalized through the creation, within the sub-region, of industrial conglomerates. Geographical unity, therefore, becomes another competitive advantage for members of the integration union. In fact, many long-distance transaction costs decrease as countries integrate physically. Transportation and communications costs diminish, customs transactions are simplified and many trade and distribution costs lessen.

In short, the dynamic effects of integration among countries with similar levels of development are potentially high. This increases significantly the level of competitiveness of member countries. The new regional unity implies complementarity between bilateralism and multilateralism and the hypothesis that an increase in inter-regional exports will result in an increase in the region's total world exports.

Technological innovations and the growth of industries which, spurred by the new competitiveness, expand the variety and

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quality of their products, reveal the temporal dimension of regional integration. (9) This indicates the need to cooperate in the development of the region's human capital.

The dimension and institutionality of regional agreements must also be taken into account. For example, De Melo, Panagariya and Rodrik (1993) (10), evaluate the behavior of non-cooperative lobbies in the integration process and point out that the establishment of common institutions within the region weakens their capacity to influence decisions by the regional group. Moreover, the creation of regional blocs affords some kind of insurance against possible reverses in the macroeconomic and market liberalization policies. (11)

Finally, in the case of the Andean Community, reference should be made to the advantages a customs union offers, compared to a free market agreement. The effects of all these aspects, particularly the strategic and institutional ones, become greater when a customs union is created. They also increase the group's negotiating capacity vis-a-vis other trade blocs. The common external tariff renders competition homogeneous and insures the even distribution of the benefits and opportunities created by integration. Without the common external tariff, very clear and transparent rules of origin would be needed. These are often difficult to enforce and allow for discretionality. A tariff measure is always better than a non-tariff measure. Therefore, the creation of a customs union is a step toward greater competitiveness.

## **V. Final Conclusions**

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»Open regionalism«, as this new integration stage has come to be known, poses many questions as to whether a true regional integration is viable. Within Latin America, the integration process has emerged with renewed strength due to trade liberalization policies and structural changes based on free market policies. In spite of the positive evolution of trade flows within the region, particularly inter-group manufactured exports, the different regional groups are still negotiating. For example, MERCOSUR still needs to solve the problem posed by the gap in the scale of its members' economies. On the other hand, the Andean Group lacks political will and the high transaction costs inhibit the consolidation of the customs union.

Nevertheless, as the Andean Group's inter-regional trade flows demonstrate, the potential benefits of the customs union are rather high. The present lack of definitions is the result of short term pressures. Eventually, the region's common inter-

ests, pointed out in the Trujillo Act, should prevail. This will generate an irreversible hysteresis which will lead the group toward greater global competitiveness.

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## Notas

1. The integration process in Latin America began with what L. Bhagwati (1993) called «first regionalism» and was stimulated by the European experience, as well as by the post-vinerean customs unions' theory developed, during the sixties, by Cooper and Massell (1965a, 1965b), Johnson (1965) and Bhagwati (1968). These authors argued that developing countries with small markets could decrease their industrialization costs by exploiting the economies of scale resulting from the

creation of wider markets by free trade areas or customs unions.

2. J. Bhagwati (op. cit.) calls this resurgence of regionalism «the second wave of regionalism». He argues that this wave will last longer than the first due to a shift in US foreign policy aimed at stimulating the creation of regional blocs. Witness, for example, its participation in NAFTA, APEC and the Initiative for the Americas. However, J.E. Garten points out that the US has not abandoned

multilateralism but changed its outlook.

3. As explained, mostly, by trade between Colombia and Venezuela.

4. Mortimore, M.(1995), «América Latina Frente a la Globalización», *Desarrollo Productivo* series No. 23). (LC/G. 1867), Santiago de Chile, ECLA.

5. Based, partially, on the author's article «Los Flujos Comerciales en el Contexto Regional Andino», *Política Internacional* 43, Lima. January-March 1996.

6. *World Economy Forum (1996) The Global Competitiveness Report*. WEF, Geneva.

7. For example, see Krugman P. (1981) «Intraindustry Specialization and the Gains from Trade», *Journal of Political Economy*, pp. 959-973.

8. On this issue, see Ethier W. (1982) «National and

*International Returns to Scale in the Modern Theory of International Trade*». *American Economic Review* 72. pp. 389-405.

See, for example, Grossman G. and E. Helpman (1993) *Innovation and Growth*, MIT Press, Massachusetts.

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**Hemispheric Negotiations: Questions and Options**

*After closely examining the creation of regional integration spaces, the author proceeds to carefully explore the process leading to the establishment of the Free Trade Area of the Americas (FTAA) from a tridimensional viewpoint encompassing background events, advances in the Working Groups, and likely impacts.*

*In light of the last meeting of the FTAA Undersecretaries of Trade, the author sets forth the important queries and possible options open to the 34 countries currently participating in the process of creating a hemispheric free trade area.*

*Tras analizar la creación de espacios de integración regional, el autor examina en profundidad el proceso de establecimiento del Área de Libre Comercio de las Américas (ALCA), desde la triple perspectiva de sus antecedentes, avances en los Grupos de Trabajo y probables efectos.*

*A la luz de la última reunión de viceministros de Comercio del ALCA, plantea los principales interrogantes y las posibles opciones que se abren para los 34 países que participan en el proceso de conformación de la zona de libre comercio hemisférica.*

*Après avoir analysé la création d'espaces d'intégration régionale, l'auteur examine en profondeur l'aménagement de la Zone de libre-échange des Amériques (ZLEA) dans la triple perspective de ses antécédents, des progrès au sein des groupes de travail et leurs probables effets. A la lumière des conclusions de la dernière réunion des vice-ministres du commerce de la ZLEA, il expose les principales inconnues et les choix possibles devant lesquels se trouvent placés les 34 pays participant à la mise en forme de la zone de libre-échange continentale.*

*Após analisar a criação de espaços de integração regional, o autor examina com profundidade o processo de estabelecimento da Área de Livre Comércio das Américas (ALCA) a partir da triple perspectiva de seus antecedentes, avanços nos Grupos de Trabalho e prováveis efeitos. À luz da última reunião de vice-ministros do Comércio do ALCA, coloca as principais interrogações e as possíveis opções que se apresentam para os 34 países que participam no processo de conformação da zona de livre comércio hemisférico.*

# Hemispheric Negotiations: Questions and Options

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## I. Introduction

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Latin America and the Caribbean are living through a crucial moment. On a global level, it would seem that never before has the world progressed so much toward globalization, as a result of the world-wide, fast paced and unified development of the capitalist system. The World Trade Organization and its new trade regulations are the starting point for the set of norms to be applied in the future. These will be more transparent and predictable. At the same time, regional groupings have increasingly emerged, as an answer to the need for shelter from the asymmetric traits and difficulties which have characterized the world economy. Such groupings also translate into concrete actions the tendency to find in neighbors with similar origins, situations and prospects, the starting point for the development of common projects on different issues. (1)

The emergence of regional integration groupings is compatible with economic globalization and the efforts toward a better insertion in the international economy. Indeed, global tendencies enrich the integration process by incorporating into its agenda a wide range of new issues. In turn, preferential liberalization of trade in goods and services in integrated areas has become a crucial strategy for a better participation in the world economy. Within this context, it can be argued that the multilateral commitments resulting from the Uruguay Round tend to stimulate integration in as much as they establish a set of common minimum rules, thus counteracting the development of closed protectionist blocs. In turn, integration schemes and agreements tend to complement multilateral efforts toward overall liberalization.

Under present international and regional circumstances, characterized by an infrequent dynamism, the countries of the region, spurred by a new vision of themselves and by their development models and external relations, have drawn a multi leveled plan of action. This covers several areas and may be seen as a set of

strategic, interrelated options of varying degree of intensity. These are: sub-regional (including the new type of bilateral schemes), regional, hemispheric, inter-regional and international relationships. (2)

## **II. Regional Coordination**

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Integration commitments and the fast-paced growth of intra-regional trade have become valuable tools to promote greater competitiveness among firms, stimulate liberalization and the implementation of de-regulation policies, and diversify the risks posed by a more open and globalized economy. (3) Nevertheless, as a region, Latin America faces a crucial challenge, the convergence of the different integration schemes. This would consolidate the ongoing trend toward outward-oriented and more stable, from a macro perspective, economies, with more competitive production structures and greater negotiating power. (4)

ALADI's institutional and operational framework did take into account the need to initiate a process of cooperation and convergence that would allow to project, at the multilateral regional level, the achievements reached within the limited scope agreements, including the agreements with other Latin American and Caribbean countries. However, multilateral mechanisms did not succeed in fomenting this process, nor in stimulating gradual and progressive cooperation between different integration schemes and agreements, with a view to progressing from the current system of economic preferences to a superior level of integration. (5)

However, as ALADI member countries have opted for indirect strategies, whereby steps are taken in a gradual and sequential manner, regional cooperation and convergence will depend on the initiative and goodwill of sub-regions.

In point of fact, ever since Brazil proposed the creation of a South American Free Trade Area (SAFTA, or an enlarged MERCOSUR), a proposal later adopted by MERCOSUR, the rest of the South American countries have found the idea very attractive; even Central America and Caribbean countries appear to be interested. Presently, Chile and Bolivia have completed wide ranging negotiations aimed at improving their adherence to MERCOSUR, determining future free trade areas and developing other issues. All these are positive steps toward regional cooperation and convergence.

The Andean countries, pursuant to Decision 321 of the Cartagena Agreement's Commission, have made strides in their negotiations with MERCOSUR on ALADI's historical heritage



(previous commitments), and are expected to sign free trade agreements during 1997. On this issue, and notwithstanding the commitments and declarations agreed upon, there are some doubts as to the possibility of negotiating a joint Andean Group - MERCOSUR agreement or of signing individual agreements between MERCOSUR and each of the Andean countries.

Chile has succeeded in forming a vast network of bilateral free trade agreements, thereby becoming the first country member of ALADI to establish a free trade area with the other member countries (the only agreement pending would be one with Bolivia).

Progress in the negotiations would spur the development of a network which, starting from MERCOSUR as the nucleus of a South American free trade area, could be strengthened by a growing number of links and agreements with the other Latin American and Caribbean sub-regional groups, thus advancing toward the creation of a regional integration system. (6)

### **III. The Establishment of the FTAA**

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#### **1. Background**

In the Summit of the Americas, held on December, 1994, in the city of Miami, thirty four Heads of State and Government committed themselves to the preservation of democracy, the eradication of poverty and discrimination, insuring sustained development and promoting prosperity through integration and free trade. In this context, they agreed to sponsor the creation of a Free Trade Area of the Americas (FTAA). Negotiations on this issue were set to conclude by the year 2005.

At present, two Ministerial Meetings have been held (Denver, June 1995 and Cartagena de Indias, March 1996) and eleven Working Groups created, whose work will be evaluated in the next Ministerial Meeting to be held, in May 1997, in Belo Horizonte. At that meeting, and in preparation to the next Summit to be held in March 1998, in Santiago de Chile, criteria and guidelines will have to be agreed with regard to the launching of negotiations on the establishment of the Free Trade Area of the Americas.

The following are some of the criteria that will guide the creation of the FTAA, as drawn from declarations issued by Presidents and Trade Ministers:

- The FTAA will be based on existing sub-regional and bilateral agreements, the regulations of which will have to be made compatible in order to widen and deepen relations.

## OPINIONS

- The FTAA should be a hemispheric agreement negotiated by all participating countries and should coexist with existing bilateral and sub-regional agreements.
- Reciprocal commitments should take into account existing differences in sizes and levels of development, this with a view to facilitating the integration of smaller economies and increasing their development level.
- Hemispheric trade liberalization and environment protection policies should support each other, as a way to sustained development.
- The dynamic and efficient movement of goods, services, capital, information and technology requires the establishment of a hemispheric infrastructure, with the participation of the private sector and financing from international financial institutions.
- The creation of the FTAA should discourage the creation of new institutions. To this effect, Latin American institutions and the private sector should play a role in the follow up and promotion of the commitments agreed upon. (7)

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*Progress has been uneven among working groups, depending on the importance of common interests*  
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### 2. The Working Groups' Progress

From the unfolding of the preparatory stage previous to the negotiations, a number of conclusions may be drawn on the progress made by the working groups on the different issues covered.

- Progress has been uneven among working groups, depending on the importance of common interests. Less progress has been achieved on issues such as market access, subsidies, anti dumping and countervailing duties, smaller economies, government procurement and services.
- Differences in points of view have not been determined so much by the «classic» dichotomy US vs. Latin America and the Caribbean as on the type of issue being negotiated and, to a lesser extent, on sub-regional interests.
- The preparatory stage has progressed successfully, with the support of multilateral organizations and without complex institutional mechanisms. To avoid some coordination, information and overlapping problems, the working groups' coordinators and the trade vice-ministers have met regularly.
- However, it has not been possible to reach an agreement on the issues which the FTAA should cover; its rules and disciplines vis-à-vis those of the WTO; and the acceptance of preferential treatment as an acknowledgement of the existence

of different levels of development among participating countries.

### 3. Possible Effects of the FTAA

What are the costs and benefits of the FTAA, from the point of view of Latin America and the Caribbean?

a. The following are among the potential advantages of hemispheric trade liberalization:

- greater access to the North American market. This could lead to the consolidation of liberalization and to greater foreign direct investment flows;
- a greater market and the consolidation of macroeconomic policies would stimulate investments;
- the «country's risk» classification would be lower;
- greater access to other Latin American markets not included in the FTAA integration scheme;
- the negotiating power of its members would increase vis-à-vis other areas and third countries.

b. Disadvantages may result from the following:

- The higher adjustment costs and the need to speed up industrial reconversion, considering the higher tariffs, different price structures and more segmented financial and labor markets;
- the loss, to the benefit of the United States and Canada, of preferences now enjoyed under sub-regional schemes and between Latin American countries;
- the difficulties to be encountered when attempting the liberalization of the agricultural sector and the elimination of subsidies in the US and Canada;
- the need to change some internal policies such as those on labor regulations, the environment and competitiveness;
- stricter rules of origin requirements, similar to those adopted by the NAFTA;
- limitations on the development of national trade and industrial policies;
- stricter rules on investment and intellectual property rights. (8)

To date, only a few quantitative estimates have been attempted on the benefits and costs for Latin America of a hemispheric free trade area.

### IV. Present Situation, Prospects and Questions

During the FTAA's Vice-Ministerial Meeting held on February

25-27, 1997, in Recife, Brazil, key issues such as the negotiations' modalities, content and timetable, were discussed. The position of the main groups of countries on these issues was more apparent.

### 1. Nature of the Negotiations and Participation

The general consensus was that the FTAA should be a hemispheric agreement that would coexist with existing sub-regional and bilateral agreements and would be negotiated by all participating countries. This reflects an important change from the position that prevailed at the beginning of the negotiations, when one of the preminent options was to widen the FTAA progressively.

Also, it was accepted that countries could participate in the FTAA negotiations individually or as a group. MERCOSUR and CARICOM members stated that they will negotiate as a group, while the US and Canada will do so individually.

### 2. Content, Focus and Timetables

During the recent Recife Vice-Ministerial Meeting the debate that took place in the previous Cartagena Meeting resurfaced. This brought to light the existence of different opinions regarding the appropriate way to proceed toward the creation of the FTAA and on the timetables for the beginning of negotiations.

Regarding the issues, the Meeting agreed that the FTAA should consider the issues mentioned in the Plan of Action issued at the Miami Summit. These are being analyzed by the different working groups created by the Denver and Cartagena Ministerial Meetings, to which the Working Group on Disputes Settlement, to be created by the Belo Horizonte Ministerial Meeting, should be added.

As for the negotiations' calendar, several positions prevailed. The United States and MERCOSUR argued that the negotiations should proceed in consecutive stages, whereas Canada and CARICOM suggested that all issues be discussed simultaneously.

– The calendar proposed by the US would envisage a negotiation in two stages: one during 1998-99 and another beginning in the year 2000. During the first stage the issues to be negotiated would be: investments, services, government procurement, standards, sanitary and phyto-sanitary rules, customs proce-

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*To date, only a few quantitative estimates have been attempted on the benefits and costs for Latin America of a hemispheric free trade area*  
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dures and intellectual property. The second stage of the negotiations would cover subsidies, anti-dumping and countervailing duties, safeguards, competitiveness and dispute settlement.

On the other hand, MERCOSUR proposes a «gradual and progressive» negotiation in three stages: a) trade facilitation issues (1998-99), b) rules and disciplines (2000-02), and c) market access in goods and services and the total elimination of subsidies and tariffs. Within this context, the hemispheric free trade area that would emerge from the negotiations would include transition periods and exceptions for sensitive products. At the same time, MERCOSUR argues that economic liberalization should be reciprocal and that the US should include all products that are subject to restrictions in its market. (9)

- The Canadian proposal suggests that all issues should be discussed simultaneously and that negotiations should conclude by the end of the year 2004, in order to allow for the legislatures of the countries involved to ratify the agreements during 2004 and for the FTAA to enter into force by 2005. (10) Even though it was agreed that negotiations should begin at the next Santiago de Chile Summit (March, 1998), there was disagreement as to the actual date in which negotiations ought to commence. The US, Canada and CARICOM proposed a date, while MERCOSUR proposed another.

Finally, on the question of differences in levels of development, CARICOM and Central America argue that smaller economies should be granted longer transition and grace periods, in addition to receiving technical and financial assistance, in order to enable them to take advantage of the Free Trade Area of the Americas. (11)

### 3. Prospects

Given the nature of the FTAA negotiations and the different interests involved, definite results are not to be expected in the short term. Nevertheless, it is possible that in the next Meeting of Ministers of Trade, to be held in Belo Horizonte, the parameters of the negotiations might be established with greater precision. Meanwhile, as some experts are suggesting, different alignments may occur around the two main negotiating poles: the US, with NAFTA, in the North, and Brazil, with MERCOSUR, in the South.

On the one hand, negative comments on MERCOSUR are on the rise in the US. Several sectors in that country are clamoring

for their Government to resume leadership in the hemisphere through the approval of the fast-track to begin negotiations with Chile on its incorporation into NAFTA and hasten negotiations on the establishment of the FTAA. In this way, a policy of selective access to NAFTA would be combined with the creation of a hemispheric free trade area, from Alaska to Tierra del Fuego.

On the other hand, MERCOSUR countries insist on an indirect, step by step strategy, which envisions concentric areas (12) and the establishment of exceptions lists and other restrictions, so as to allow for the development of their own areas of economic activity (particularly high technology industries). Within this context, business organizations from MERCOSUR countries have begun to express their solidarity with the positions adopted during the recent Vice-Ministerial Meeting. (13) For MERCOSUR, the creation of the FTAA will depend on «acceptable time-frames» to shelter its member countries from an abrupt trade liberalization that would dramatically affect their industries' competitiveness and their economies.

Between both of these positions there are others advocated by other groups of countries with greater economic links with the US and whose future depends on continued access to the US market, in the best possible terms.

Within this context, the final outcome will depend on the capacity of the region's countries to coordinate their positions, in view of the difficult negotiations with the US awaiting them in the near future.

### Notes

1. *The following considerations reflect the analysis developed by the Permanent Secretariat in its document «the Process of Regional Convergence and the Establishment of the FTAA», presented at the III Meeting of Trade Policy Government Representatives of Latin America and the Caribbean, held on October 21, 1996, in Montevideo, within the framework of the activities related to the XXII Latin American Council Meeting (ALADI /*

*ECLA / SELA / III / RGPC / DT No.4)*

2. *For more details see our article «In the Globalization Era. Integration Options», Capítulos, SELA, No.45, January-March, 1996.*

3. *In addition to their specific modalities, the geopolitical perspective of integration agreements is determined by geographical considerations, existing infrastructure, business links and the circulation of*

*people, goods, services and capitals between the countries involved.*

4. *In this context, the weak trade and economic relations between integration schemes is an obstacle that has to be conquered. The weakness of such links is apparent in the case of MERCOSUR and the Andean Community; the Andean Community and the CACM; ALADI member countries and CARICOM or between Central America and*

CARICOM.

5. It seems to us that, under current Latin American conditions, convergence implies the coordination of sub-regional agreements and schemes and must be seen as a multidimensional concept ( legal, political and economic) which comprises the formal aspects and the structural conditions needed in order for countries to interact within a wider institutional and regulatory framework. Moreover, it is our opinion that the disparities that exist between Europe's and Latin America's notion of convergence are due to both region's different levels of integration -economic and monetary union in the European Union, the creation of free trade areas for goods and services or customs unions in Latin America- than to conceptual differences.

6. In this context, besides existing relations between ACS countries, of particular importance are recent contacts between MERCOSUR member states and Caribbean countries such as, for example, Uruguay's Minister of Foreign Affairs' participation in the CARICOM Summit Meeting held last February in Antigua.

7. Following the Miami Summit, the OAS-

IDB-ECLA institutional cooperation mechanism was reactivated. This was established in 1960 to provide the Working Groups with technical support. Also, the Working Groups' Coordinators were given the authority to summon the support of other organizations. SELA was invited to participate in the Working Group on Smaller Economies, to prepare a technical cooperation program for such economies. ALADI participated in the Working Group on Origins and Customs Procedures.

8. See the publication *El Area de Libre Comercio de Las Américas* of Argentina's Centro de Economía Internacional, Buenos Aires, January, 1997.

9. On the issues discussed and the preliminary agreements reached at the Recife Meeting, see declarations by Miguel Rodriguez Mendoza, Special Advisor to the OAS on Trade Issues, in IPS, March 15, 1997.

10. See Brazil's Minister of Foreign Affairs' declarations to the international press on the occasion of the III Meeting of Trade Ministers from the Americas, held, on February, 1997, in Recife, Brazil.

11. Of the remaining countries, the Andean Group will propose a model for negotiations. This is

being prepared.

12. As a contribution to the work of the Working Group on Smaller Economies, coordinated by Jamaica, SELA's Permanent Secretariat was asked to analyze the technical assistance mechanisms currently in place and to identify technical assistance needs in order to facilitate the participation of smaller countries in the negotiations and creation of the FTAA. Accordingly, the Secretariat presented at the V Meeting of the Group (Caracas, November 13-15, 1996) the document «Guidelines for a Technical Cooperation Program for the Smaller Economies: Proposals of SELA's Permanent Secretariat», and , at the VI Meeting of the Group (Georgetown, February 13-14, 1997), the document «Identification of Technical Assistance Needs in the FTAA Process».

13. Considering that MERCOSUR and other South American countries are 'global traders', such spheres of influence cover bi-regional relations (as in the case of the European Union) and multilateral relations (strengthening of the WTO).

14. See press notes reviewed in SELA's *Síntesis Informativa*, Monday, March 11, 1997.

### **Path to the Free Trade Area of the Americas**

The countries of the Western hemisphere have announced their intentions to form a hemisphere-wide free trade area, to be known as the Free Trade Area of the Americas. However, they have not designed nor agreed upon a path to commencement of the operation of the FTAA. In the absence of a single path different paths are evolving, while a process of consultation and preparatory work unfolds. This is taking place in a context in which there has been an increase in the number of regional and bilateral arrangements, accompanied by the rapid expansion of trade and investment flows. Existing trade arrangements and the proliferation of new initiatives might hinder or contribute to the creation of the FTAA. A consensus must be reached on a single process leading to the FTAA.

*Los países del Hemisferio Occidental han anunciado su intención de formar un área de libre comercio que comprenda todo el hemisferio, denominada «Área de Libre Comercio de las Américas» (ALCA). Sin embargo, aún no han diseñado o acordado una vía para poner en ejecución esta iniciativa. Ante la ausencia de un proceso único, han surgido diferentes vías, en forma paralela al proceso de consulta y el trabajo preparatorios. Esto se plantea en un contexto en el que ha ocurrido un aumento de los acuerdos regionales y bilaterales, concomitante con la rápida expansión de los flujos de comercio e inversión. Los acuerdos comerciales existentes y la proliferación de nuevas iniciativas podrían obstaculizar la creación del ALCA o contribuir con el proceso. Resulta necesario lograr un consenso en cuanto a un proceso único conducente a la puesta en práctica del ALCA.*

*Les pays occidentaux ont annoncé leur intention de constituer une zone de libre-échange continentale dite des "Amériques". Ils n'ont toutefois arrêté aucun plan en vue de la mise en route de ce projet. Au lieu d'un plan unique, on en a élaboré différents, tandis qu'un processus de consultation et de travaux préparatoires est en cours. Il s'agit-là d'un contexte dans lequel on a assisté à un accroissement du nombre d'accords régionaux et bilatéraux accompagné d'une expansion rapide du commerce et des flux d'investissement. Les accords commerciaux existants et la prolifération de nouvelles initiatives pourraient entraver ou contribuer à la création de la zone de libre-échange des Amériques. Un consensus doit se faire autour d'un processus unique conduisant à sa réalisation.*

*Os países do hemisfério ocidental anunciaram que têm a intenção de formar uma área de livre comércio que abranja todo o hemisfério, denominada «Área de Livre Comércio das Américas» (ALCA). No entanto, ainda não delinearão uma via para pôr em marcha esta iniciativa. Face à ausência de um processo único, têm surgido diversas vias, de forma paralela, no processo de consulta e trabalho preparatórios. Isto se coloca num contexto no qual se observa um aumento dos acordos regionais e bilaterais, concomitantemente com a rápida expansão dos fluxos de comércio e investimento. Os acordos comerciais existentes e a proliferação de novas iniciativas poderiam obstaculizar a criação do ALCA ou contribuir ao processo. É necessário alcançar um consenso relativo a um processo único conducente ao andamento do ALCA.*



# Path to the Free Trade Area of the Americas

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*This paper benefitted from comments by George Fauriol, Sidney Weintraub, Steve Lande, Peter Hakim, Carol Wise, Peter Morici, Robert Delvin, Alister McIntyre, Don Mackay and Gerald Helleiner.*

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## Introduction

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The countries of the Western Hemisphere have announced their intention to form a hemisphere-wide free trade area to be known as the Free Trade Area of the Americas (FTAA). The creation of a free trade area encompassing the democratic countries, in the Western Hemisphere, (excluding Cuba) was agreed upon in the Summit of the Americas, in Miami, in December, 1994. This goal is embodied in the Summit of the Americas Declaration Principles and Plan of Action as the Free Trade Area of the Americas. The governments committed to (1) begin immediately to construct «The Free Trade Area of the Americas» (FTAA) in which barriers to trade and investment will be progressively eliminated<sup>1</sup>, (2) conclude the negotiations no later than 2005, (3) make concrete progress toward the attainment of this objective by the end of this century.<sup>2</sup> However, they have not designed or agreed upon a path from the present situation to commencement of the operation of the FTAA nor what will constitute the FTAA, although the implicit assumption is that the commitments would have to go beyond those of the Uruguay Round of the WTO.

In the absence of a single path to the Free Trade Area of the Americas, different paths are already evolving simultaneously, and are likely to continue. Meanwhile, a process of consultation and preparatory work has been set in motion. This is taking place in a context in which there has been an increase in the number of regional and bilateral trade arrangements, accompanied by the rapid expansion of trade and investment flows.

Concomitant with the FTAA process, several regional and bilateral initiatives are now being discussed or negotiated. Existing trade arrangements and the proliferation of new initiatives might hinder or contribute to the eventual creation of an FTAA. There is an urgent need to evaluate the alternative paths to the FTAA, both those which are evolving and those contemplated, with a view to selecting one, and if not, then ensuring their complementarity. Ideally, there must be consensus on a single process leading to the FTAA.

## **I. The Current Situation**

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The main features of the present context are:

### **A. Resurgence of Regional Trade Agreements**

Trade in the hemisphere is characterized by a trend towards the regionalisation of trade as intra-regional trade is growing faster than hemispheric and global trade. This reflects the impact of liberalization policies and the resurgence of regional trade arrangements. There are five major regional trade agreements and economic integration schemes, namely, the North American Free Trade Area (NAFTA), the MERCOSUR, the Central American Common Market (CACM), the Caribbean Common Market (CARICOM), and the Andean Pact.<sup>3</sup>

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The share of intra-regional trade in total trade of the hemisphere has increased significantly in recent years. Intra-regional exports as a share of total exports between 1990 and 1994 increased by 243% in the Andean Group, 215% in MERCOSUR and 24% in the CACM.<sup>4</sup> There was a doubling of intra-NAFTA exports with a marginal decline in CARICOM. While these figures reflect expansion from a low base, they indicate momentum in intra-regional trade.

regional trade.

In addition to the five principal regional trade agreements (NAFTA, MERCOSUR, CACM, CARICOM, AND AP) there are five preferential trade arrangements. These are the Caribbean Basin Initiative (CBI), the CARIBCAN, Andean Trade Preference Act, Venezuela/CARICOM Agreement, and the Colombia/CARICOM Agreement. There are also some regional initiatives which are in various stages of implementation, namely, the

## B. Trade Promiscuity<sup>5</sup>

There has been a scramble by countries to develop links to member states of NAFTA and to the MERCOSUR which has led to the emergence of arrangements with the United States Mexico and Brazil as hubs with an increasing array of spokes. The implications of a hub and spoke pattern<sup>6</sup> is that only the hub has preferential market access to all countries, while the spoke countries have liberalized access only to the hub but not to other countries. This can cause a distortion in investment flows, with a concentration of investment likely to occur in the hub country. This hub and spoke pattern might be detrimental to the kind of regional cooperative initiative which the FTAA is intended to be.

Several countries have sought to establish bilateral trade agreements with the United States, Mexico and Brazil, as a way of linking with NAFTA AND MERCOSUR or with the principal export market, e.g., the U.S. market for the Caribbean and the Mexican market for Central America. Attempts by countries to negotiate free trade agreements with individual NAFTA countries started even before the conclusion of NAFTA. This was prompted by the worry that securing a free trade agreement with or joining NAFTA would be difficult after NAFTA ratification because the member countries may want to wait for a period in order to evaluate NAFTA's progress<sup>7</sup>. Some countries may also have been «put off» by the necessity of meeting NAFTA's high level of trade and investment discipline. Some countries may have mistakenly viewed an agreement with Mexico as a «back-door» to enter NAFTA. Countries are prevented from benefitting from access to the NAFTA market even if they entered into an agreement with Mexico as existing NAFTA rules prevents the extension of FTA benefits to third countries. Strict origin rules means that components produced in Mexico's FTA trade partners, even if completed in Mexico, would still not be treated as eligible NAFTA products when entering the United States. Indeed, the NAFTA rules of origin are intended to prevent non-NAFTA parties from deriving NAFTA benefits.

The United States, as the largest economy in the hemisphere, is a natural growth pole and the likely core of a hemispheric free

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trade area. It is already a hub with several important spokes, including NAFTA (with Canada and Mexico), the Caribbean Basin Initiative (with the Caribbean and Central America), and the ANDEAN Trade Preference Act (with Bolivia, Peru, Ecuador, and Colombia). Quite naturally, a frequently discussed proposal is that NAFTA would constitute the core of an expanded trading bloc by admitting additional countries.

Mexico which is currently a member of NAFTA, is also a participant in the group of three with Colombia and Venezuela and has signed (1992) an agreement to promote free trade with Central America. Mexico also has bilateral agreements with Uruguay (1986), Argentina (1986), Peru (1987), Chile (1991), Costa Rica (1994), and Bolivia (1994). Mexico plans to complete negotiations with the rest of Central America and Peru by the end of 1997. It will then have free trade agreements with all hemispheric countries with the exception of MERCOSUR and the CARICOM countries. The emergence of

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*The coexistence of numerous agreements has created a confusing array of rules of origin and regulations.*  
 ”

Mexico as a node of catenation creates uncertainty, which is likely to continue until there is a clear schedule of accession to NAFTA.

Brazil is playing a leadership role in MERCOSUR which is beginning to expand its membership e.g., Chile and Bolivia. In early December, 1995 Bolivia signed an accord with the MERCOSUR which aims to eliminate trade barriers in 10 years<sup>8</sup>. The Chile-MERCOSUR negotiations concluded in June 1996<sup>9</sup>, and the agreement went into effect on October 1, 1996. Discussions with the Andean Pact, Ecuador, Peru, Venezuela, and Colombia are proceeding and there is outreach to Europe and Japan<sup>10</sup>.

In addition, to the matrix of trade agreements emanating from the United States, Mexico and Brazil, there numerous bilateral arrangements between other countries and several more have been announced or are being negotiated. Bilateral trade agreements seek to liberalize and facilitate trade, however, the proliferation of agreements is making it more complex as exporters and importers can never be sure which regime governs their operations. The coexistence of numerous agreements has created a confusing array of rules of origin and regulations. This overlapping of agreements is hindering trade rather than promoting it. Simplification, which should come from a single hemispheric free trade, would be a significant benefit.

The Western Hemisphere encompasses countries vastly different in size and level of development<sup>11</sup> Size ranges from Canada (9.9 million sq.km) and Brazil (8.5 million sq.km) to Montserrat (102 sq.km). Gross National Product GNP differs between the U.S. with \$8,291 billion to Antigua Dominica, Grenada, Montserrat, St. Kitts, St. Lucia and St. Vincent each of which have a GDP of less than \$500 million. Population varies from 258 million in the United States to 11,000 in Montserrat. Per capita GNP ranges from \$24,750 in the United States to \$450 in Haiti.

Substantial liberalization has been achieved in the majority of countries in Latin America and the Caribbean. The state of preparedness to participate in and benefit from the FTAA varies widely among the countries of the hemisphere<sup>12</sup> The average tariffs were fourteen (14) percent in 1995 ranging from 6.6.% in the United States to 17.9% in Honduras. In addition there has been a substantial reduction in the number of items which attracted tariffs<sup>13</sup>

By the early 1990's a «new Latin American consensus» had emerged<sup>14</sup>. Based on competitive markets, macroeconomic stability through reduction of public sector deficits, opening of the external sector to foreign competition and reducing the role of the state by privatization and deregulation. The extent of trade liberalization reflects a variety of structural economic features, policy orientations, political perspectives and psychological dispositions. Further complications arise from limited and tentative political support for economic reform and liberalization<sup>15</sup> partly due to the fact that these policies were prompted from the frustration with import-substitution and protectionism during the profound economic crisis of the 1980's<sup>16</sup> The circumstances in which the more complex stages of liberalization have to be implemented are made difficult by the more unequal distribution of income<sup>17</sup> and an increased incidence of poverty<sup>18</sup> which have accompanied economic reform and liberalization. The recent experiences of Venezuela and Mexico<sup>19</sup> reveal the fragility of the process.

Whether the Latin American and Caribbean economies are able to take advantage of access to the larger hemispheric

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market or to larger regional groupings to expand exports depends not only on the policies of Governments, but also on the readiness and ability of the private sector to compete effectively. Even where these economies have a comparative advantage it could, as in the past, be offset by the lack of a competitive advantage<sup>20</sup> by both locally-owned and foreign firms. The expansion of exports will depend on a combination of both comparative and competitive advantages. Economic reform, liberalization, and adjustment are prerequisites for participation in the FTAA, therefore trade liberalization is a necessary but not sufficient condition. Governments will have to address the economics (macro-economic and micro-economic), social and political difficulties of adjustment if the goal of hemispheric free trade is to be realized<sup>21</sup>.

## **II. Alternative Paths to the FTAA**

Five alternative paths to the FTAA can be conceived of:

### **A. NAFTA as the Core**

The Enterprise for the Americas Initiative (EAI), which was launched in June 1990 by President Bush consisted of three interrelated components: trade liberalization, debt relief, and investment promotion measures. The objective of trade liberalization was the creation of a hemispheric free trade area, stretching from Anchorage, Alaska to Tierra del Fuego, in Chile. The establishment of free trade would be achieved by the expansion of the North American Free Trade Agreement (NAFTA) (between the U.S., Canada, and Mexico) to include other countries<sup>22</sup>. This view of NAFTA as the core is shared by Canada. Prime Minister Chretien of Canada, during a recent visit to Chile and MERCOSUR countries, reiterated that «We see NAFTA as the foundation for eventual free trade throughout the Americas»<sup>23</sup>. Apart from the shared conception by the NAFTA partner, NAFTA undoubtedly will have substantial pull because it includes the largest economy and most powerful country, the U.S.A. and it represents about 75% of hemispheric trade<sup>24</sup>. President Clinton on succeeding President Bush, reiterated the vision of NAFTA as a core agreement, which would be expanded to eventually encompass all the countries of the hemisphere that undertake the commitments to free trade. More recently, the U.S. has indicated that NAFTA accession is one of several ways to create the FTAA<sup>25</sup>.

The NAFTA accession clause neither sets out eligibility

criteria for new members nor application procedures for interested countries. Article 2204 of the NAFTA merely provides that any country or group of countries may accede to the NAFTA «subject to such terms and conditions»<sup>26</sup> as may be agreed to between those countries and the NAFTA Free Trade Commission comprising Cabinet level officials from Mexico, Canada and the United States. Apart from the vagueness of the accession clause, it is important to resolve the issue of sequential accession versus accession by blocs or groups. Bloc accession is preferable to the «piecemeal» expansion by a series of individual accessions because it avoids adverse implications for both the FTAA process and existing regional trade groups<sup>27</sup>.

In mid-1994, the Clinton Administration indicated that Chile was the only country it regarded as ready to assume the disciplines required by the NAFTA. In December 1994, at the Summit of the Americas, the NAFTA partners announced that Chile would be the first country to be allowed to accede to NAFTA and negotiations would start in early 1995. Negotiations with Chile for accession to NAFTA, according to then U.S. Trade Representative Mickey Kantor, is the first step towards building a Free Trade Agreement of the Americas<sup>28</sup>. A number of meetings were held in 1995 but the process is now in recess. Canada and Chile commenced discussion on a free-trade accord, which is intended to «provide a bridge to a full NAFTA accession for Chile and will be folded into the NAFTA once the accession negotiations are eventually completed»<sup>29</sup>.

The major obstacle to NAFTA expansion is the lack of fast track authority which effectively freezes negotiations for NAFTA entry. The Clinton Administration commenced efforts to secure passage of fast-track authority immediately after the Presidential Election in November<sup>30</sup>. The outcome is uncertain as the November congressional elections did not change the political configuration in Congress. Protectionist and NAFTA opponents will continue their opposition to NAFTA expansion and possibly the FTAA, as the large and growing U.S. trade deficit with its NAFTA partners appears to vindicate their gloomy predictions<sup>31</sup>. Strong opposition can be expected from environmental organizations and unionized labor<sup>32</sup> who attribute job losses to NAFTA<sup>33</sup>. Perhaps the most difficult obstacle is that 57% of U.S. residents «don't want the U.S. government to approve new trade agree-

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*The major obstacle to NAFTA expansion is the lack of fast track authority which effectively freezes negotiations for NAFTA entry.*

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ments with Latin America» as 51% believe these agreements will result in loss of U.S. jobs<sup>34</sup>.

Another major problem is the differences among the NAFTA partners on when and how fast to expand NAFTA. The U.S. has not yet made up its mind, Mexico wants to proceed slowly and Canada is ready to move ahead as soon as possible. Canada questions the resolve of the U.S. to play a leadership role in trade liberalization in the Western Hemisphere<sup>35</sup>. Meanwhile, Canada and Chile concluded a bilateral trade agreement which will come into effect in June, 1997<sup>36</sup>. In addition there have been several trade squabbles between the NAFTA partners, (including differences over the Helms-Burton Bill), which does not make for an atmosphere conducive to NAFTA expansion. There is an urgent need to improve relations between Washington, Ottawa and Mexico City. Indeed, an editorial in the *Journal of Commerce* departed from its tradition of sobriety to state that «Mr. Kantor poisoned relations with Mexico by pandering to special interest<sup>37</sup>.

In response to the concerns articulated by the Governments of the small developing countries of Central America and the Caribbean<sup>38</sup>, the Clinton Administration and CBI supporters in Congress sought unsuccessfully to have congressional approval for a unilateral extension of most NAFTA benefits for products currently excluded from CBI duty-free treatment. The proposal, known as parity, would have addressed the diversion of trade and investment<sup>39</sup> which is resulting from NAFTA. This is particularly evident in apparel exports<sup>40</sup>. The proposed program provides enhanced access to the U.S. market in the form of NAFTA-like tariff and quota treatment for particular categories of apparel. It was hoped that the parity program would be included first in NAFTA implementing legislation, in the Uruguay Round implementing legislation and then in the trade legislation introduced in the 104th Congress.

## **B. MERCOSUR as a Pole**

Brazil is proposing to extend MERCOSUR to create the South American Free Trade Area (SAFTA), which eventually could be in a position to amalgamate with NAFTA<sup>41</sup>. The idea of a free trade area encompassing all the countries of South America is not new. It dates back to the First International Conference of the American States in 1889<sup>42</sup>. The Latin American Integration Association (ALADI) was started in 1980 and replaced the Latin America Free Trade Association, which was created in 1960. The membership of ALADI includes Mexico and the countries of South America. Support is growing for a Brazilian-campaigned



concept of a South American Free Trade Area. Already MERCOSUR membership has been expanded to include Bolivia and Chile<sup>43</sup>, and negotiations are in progress with the Group of Three. At the end of August, negotiations for a FTA between Mexico and MERCOSUR began with a projected completion date of early 1997<sup>44</sup>. At the Rio Group meeting in September, it was announced that negotiations would commence between the Andean Pact and the MERCOSUR. These developments indicate that the creation of SAFTA is a possibility which, if realized, could lead to a bi-polar hemisphere divided between NAFTA and SAFTA.

The possibilities of the MERCOSUR becoming the core of a SAFTA or one of two poles for hemispheric free trade derive not only from a particular vision of Brazil's emergence as a regional «power»<sup>45</sup> but from MERCOSUR's size in relation to Latin America. The MERCOSUR represents almost 50% of Latin America's GDP, more than 40% of its population and about 33% of its foreign trade<sup>46</sup>. The possibilities of the MERCOSUR becoming the core of SAFTA or FTAA derive not only from the extent of integration but from MERCOSUR's size in relation to Latin America. In addition, intra-MERCOSUR trade is growing rapidly e.g. from \$ 10 billion in 1993 to \$ 12 billion in 1994<sup>47</sup>. While MERCOSUR's size is still much less than that of NAFTA and it will not displace U.S. dominance or leadership, nevertheless it does have momentum in its favor. Its willingness to expand its membership and network of trade accords at a time when the U.S. Administration is immobilized by the lack of fast track authority makes the MERCOSUR appear as a more feasible and/or immediate option for some South American countries. Some countries which were hoping to join NAFTA are turning in frustration to links with MERCOSUR<sup>48</sup> and even to links with Asia and the European Union<sup>49</sup>. Membership in MERCOSUR is not a substitute for participation in NAFTA but represents a very different option, especially given large differences in the size of the respective markets.

### C. Bi-Polar Amalgamation<sup>50</sup>

The MERCOSUR, at the instigation of Brazil, has tried to initiate discussions with NAFTA which could lead to some type of MERCOSUR-NAFTA agreement<sup>51</sup>. In October 1995, U.S. Trade Representative, Mickey Kantor and Brazil's Foreign Trade Minister Luiz Felipe Lampreia agreed to «explore with the other parties to our respective sub-regional trade arrangements this possibility, which we strongly endorse»<sup>52</sup>. In November 1995, the

U.S., with the acquiescence of Canada agreed with MERCOSUR to hold their first meeting prior to the meeting of Western Hemisphere Trade Ministers scheduled for March 1996, in Colombia<sup>53</sup>. However, strong Mexican opposition has so far

prevented this group from convening<sup>54</sup>. It has also been suggested that «Brazil seeks to avoid any specific hemispheric-wide negotiations until MERCOSUR is in a stronger bargaining position vis-à-vis NAFTA»<sup>55</sup>. Hence, the consolidation and expansion of the MERCOSUR will be Brazil's priority between now and the end of the century<sup>56</sup>.

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*There are different perspectives on whether the convergence of regional trade groups has to be preceded by a phase of consolidation.*  
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While most Governments in the hemisphere would not support a bi-polar negotiation process, «many trade analysts see the talks generally coming down to a U.S.-led bloc negotiating with a Brazil-led bloc, with Caribbean countries fighting to avoid being forged in the process».<sup>57</sup>

It is not clear if NAFTA-MERCOSUR inter-bloc discussions will emerge as a parallel track to the FTAA process. Brazil and the U.S. have a long history of different perspectives on trade issues as was revealed during the Uruguay Round in which one observer noted that the U.S. and Brazil «haggled» over almost every issue of substance in the GATT negotiation<sup>58</sup>. Nevertheless, Lampreia and Kantor came to a common understanding on the Ministerial Declaration during a plane trip from Brazil to Cartagena. The other member states refused to rubber stamp their version of the declaration and the final Ministerial Declaration reflected a cross section of other views.

#### **D. Convergence of Regional Trade Groups**

It is frequently suggested that regional trading groups/agreements can constitute building blocks for the FTAA by fostering increased trade liberalization among their member countries<sup>59</sup>. The five principal regional trade groupings, namely, NAFTA, MERCOSUR, CARICOM, the Central America Common Market (CACM), and the Andean Pact could engage in a negotiated convergence or cooperation on a common integration goal. It might be easier and quicker to have the five main regional trade groups negotiate the FTAA than 34 countries. The disparities in economic size between the various regional groups would be a concern since this could translate into leverage for the NAFTA countries. The disparities are enormous e.g. NAFTA's popula-

tion is 372 million compared to 6.2 million in CARICOM. NAFTA's GDP is 10 times larger than the next biggest group, the MERCOSUR<sup>60</sup>. There is also the question of the inclusion of countries not currently members of any regional group, e.g. Haiti, the Dominican Republic, and Panama.

There are different perspectives on whether the convergence of regional trade groups has to be preceded by a phase of consolidation. Brazil has proposed that a period of consolidation of regional groupings is a prerequisite of hemispheric free trade, however, the United States has stated firmly that the FTAA «cannot wait for regional groupings to consolidate»<sup>61</sup>.

## E. Hemispheric Negotiations

Another way to proceed is to forge an agreement on «WTO plus» standards towards which all countries in the hemisphere would move in accordance with a designated schedule. This must involve a schedule for concerted effort to develop these common standards for hemispheric trade in goods and services and the movement of capital flows in ways which foster compatibility between the various trade blocs. This approach is similar to that being followed by the Asia Pacific Economic Cooperation group (APEC).

The trade component of the Summit of the Americas process embodies this strategy: (1) the system of Working Groups that has been established is engaged in an intensive process of examining relevant issues. By the time of Belo Horizonte, seven of eleven working groups will have been engaged for a period of 18 months (June 1995 to May 1997), while four of the working groups will have been engaged for a period of 14 months (March 1996 to May 1997). The negotiation agenda is being identified and confirmed. (2) By Belo Horizonte Ministerial Meeting in May, 1997, Ministers Responsible for International Trade will have met three times in the 29 months since the Miami Summit. During that same period, Vice-Ministers will have met much more frequently for a total of 8 times. The working groups will have had a total of 52 meetings, most lasting at minimum one and a half days. In addition, the FTAA and its prospects will have been discussed in numerous meetings, visits or conversations as Ministers and senior officials from national governments exchange views and ideas. Such a process indicates that the countries have sufficient political and bureaucratic will to launch the negotiations.

### **III. Advantages of a Single Path**

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The coexistence of the different paths to the FTAA raises some fundamental issues which must be addressed e.g., the problem of the proliferation of regional, sub-regional and bilateral trade agreements which could complicate the process of creating the FTAA. Ideally, the governments of the hemisphere should agree on a single path to the FTAA because this would: (1) Avoid the confusion, duplication of effort and delays which will result from the coexistence of different paths. This will slow down the process of creating the FTAA. (2) An unfocussed FTAA process with no clear end in sight will reduce the commitment of governments to the FTAA. They will be tempted to concentrate on regional agreements and initiatives, including those outside the hemisphere. Canada, the US, Mexico and Chile are members of APEC and could make this a priority over Western Hemisphere trade. The Caribbean countries could divert resources from the FTAA process to negotiating an agreement with the European Union to succeed the present LOME convention.

### **IV. Towards a Hemispheric Round**

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The path to the FTAA will involve two phases: (1) a preparatory phase, and (2) the actual negotiations. The preparatory phase will involve (a) a broad discussion among countries to define the content of the negotiations and the principles on which negotiations will proceed, e.g. right of withdrawal balanced by the right of remaining parties to continue the negotiations; (b) a determination of a sufficient level of political will exists to justify launching formal negotiations. The FTAA process which commenced after the Miami Summit appears capable of ensuring that both aspects of the preparatory process can be accomplished. However, the question which remains is the form and conduct of the negotiations. The first step in this process is to arrive at a consensus on the best option from the alternative paths.

There are four criteria which any path to the FTAA should meet. These are:

(a) Facilitate full participation by all 34 countries, designated as eligible by the Summit of the Americas.

(b) Ensure equanimity of participating governments regardless of size and level of development, i.e., all governments have the same formal rights in the decision-making process.

(c) Strive for simplicity in the form, logistics and administration of the process.

(d) Ensure maximum transparency in the preparatory and negotiations phases in order to increase understanding, inform discussions and maintain credibility.

The path of hemispheric negotiations would be preferable to the other four possibilities. Both because it best meets the four criteria and poses less difficulties than the alternative path.

(1) The creation of the FTAA by NAFTA expansion can only be contemplated because the disciplines involved are the most far-reaching, and the coverage of issues is the most comprehensive among the regional arrangements in the Hemisphere. However, participation in decisions on fundamental issues would be confined exclusively to the NAFTA partners and therefore lack equanimity and transparency. The obvious simplicity of the small number of governments decreases as countries accede to membership. Another serious drawback is the fact that a decision by NAFTA to provide sequential admission, either for individual countries or blocs, could set off very damaging trade and investment diversions for those countries or blocs which come later in the schedule of expansion.

Hemispheric negotiations whether on a comprehensive or scaled-down agenda would be preferable to NAFTA expansion because the majority of countries are small and are unlikely to be among the countries given early accession and this could result in a serious erosion of their exports to NAFTA markets. This is clearly demonstrated by the inability of the U.S. Government to expand the membership of NAFTA. The uncertainty about if and when NAFTA will be expanded, will reduce the prospects of this being chosen as the single path to the FTAA.

(2) Similar problems are likely to occur if MERCOSUR becomes a pole from which the FTAA could evolve, namely narrow participation with the attendant lack of transparency and equanimity. In particular the establishment of the FTAA could be delayed beyond 2005 because the MERCOSUR is focused on the creation of SAFTA, before the FTAA. There has been little contact or in-depth discussion between the smaller economies and MERCOSUR despite the fact the half the membership of MERCOSUR, namely, Paraguay and Uruguay could be viewed as smaller economies. It should also be borne in mind that Bolivia's admission to associate status in MERCOSUR was held up because of an unwillingness to provide «special» consideration, which would take account of Bolivia's size and level of development. All of this is confirmed by the marginal nature of small country participation in the Rio Group.

(3) If the FTAA is to emerge from bi-polar negotiations between the NAFTA and MERCOSUR, the question arises of how the interest of countries which are not members in either agreement will be taken account of in the negotiations. If the goals, design, and schedule of the FTAA were presented to the rest of the hemisphere as a *fait accompli*, or with perfunctory subsequent consultations this would obliterate participation, equanimity and transparency.

(4) The convergence of regional trade groups as a path to the FTAA has a deceptive conceptual simplicity. However, in reality it would be a very difficult path to the FTAA as it would involve intra-regional consensus building as a prerequisite to agreement at the hemispheric level. The ability to forge consensus and adhere to it within regional groups varies considerably between the various trade groups. The process could become very complex as trade groups might not only negotiate simultaneously, but may also conduct bilateral discussions. If all groups were involved, this would be tantamount to hemispheric negotiations but with the additional constraint of regional trade arrangements. There is also the problem of how to ensure the participation of countries which are not members of regional groups, for example, Haiti, the Dominican Republic, and Panama. If these countries are to participate in this format they would have to be attached to some regional group for negotiation purposes. This raises the possibility that the regional groupings may not conform to existing regional trade arrangements. If this principle was accepted, a range of regional configurations could emerge, e.g., SAFTA, Central America and the Caribbean or Small Economies. This path can provide participation and transparency, but in a cumbersome two-tier process which could leave most governments with the feeling that their particular concerns were not satisfactorily represented as national interests were subsumed in a regional consensus.

A hemispheric round of negotiations avoids the difficulties and complexities of the other paths. It would provide full and direct participation by all countries, hence providing equanimity and transparency. The process is also relatively simple and one to which governments of the hemisphere have become familiar over many years in various hemispheric organizations such as the Organization of American States, and more recently the fora of the Summit of the Americas. This path has the added advantage of being a single undertaking thereby allowing trade-offs among countries which could facilitate the emergence of consensus. Furthermore, it is the path most likely to maintain the

focus of attention on the FTAA. The benefits of this path extend beyond the negotiations as it generates greater legitimacy and commitment which make for stability of the final agreement.

The majority of the countries in the Western Hemisphere are small, developing economies and are not likely to be a major determinant of what constitutes the FTAA, the path to FTAA and the schedule for negotiations and the commencement of the FTAA. The interests and concerns of small, developing countries must effectively be taken into account by a hemispheric round. Ensuring the participation of these countries is essential for the formation of the FTAA, otherwise, the ultimate objective of the FTAA, a seamless hemispheric economy hemispheric economy, will not become reality.

## Notes

1. *Summit of the Americas, Declaration of Principles at 3.*
2. *Ibid.*
3. *Details of these agreements can be found in, «Trade and Integration Arrangements in the Americas: An Analytical Compendium».* (Washington D.C.: Trade Unit, Organisation of American States, September, 1996).
4. «*Toward Free Trade in the Americas*» (Washington D.C.: Trade Unit, Organisation of American States, 1995) p.2.
5. *Trade promiscuity refers to «signing agreements with anyone and everyone who is willing, most likely their neighbors».* See Moises Naim and Robin King, «Hemispheric Economic Integration: Big Bang, Gradual Evolution, or Fading Hope?» (Prepared for presentation to Latin America 2010 Seminar, at the National Defense University) September, 1996.
6. See Yung Chul Park and Jung Ho Yoo, «More Free Trade Areas: A Korean Perspective» in Jeffery Schott (ed.), *Free Trade Areas and U.S. Policy* (Washington D.C.: Institute of International Economics, 1989) pp. 141-158, and Ronald J. Wonnacott, *The Economics of Overlapping Free Trade Areas and the Mexican Challenge* (Toronto and Washington D. C.: C.D. Howe Institute and National Planning Association, 1991).
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16. Dani Rodrik «The Rush to Free Trade in the Developing World: Why So Late? Why Now? Will it Last?» in Stephen Haggard and Steve B. Webb (eds.), *Voting for Reform. Democracy, Political Liberalization and Economic Adjustment* (Oxford: Oxford University Press, 1994) pp.61-88.
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18. "The Backlash in Latin America», *The Economist*, November 30, 1996 pp. 19-21.
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20. Michael Porter, *The Competitive Advantage of Nations* (New York: The Free Press, 1990).
21. Manuel Pastor Jr. and Carol Wise «Western Hemispheric Integration: Free Trade is Not Enough», *SALS Review*, Vol. XV, No. 2 (Summer-Fall, 1995) pp. 1-16.
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SISTEMA ECONÓMICO LATINOAMERICANO  
LATIN AMERICAN ECONOMIC SYSTEM  
SISTEMA ECONOMICO LATINO-AMERICANO  
SYSTÈME ECONOMIQUE LATINOAMÉRICAN



# Coordinación y Cooperación PARA AMERICA LATINA Y EL CARIBE



ENGLISH VERSION

| INDICE |

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### **The Social Dimension of Integration**

*In spite of the level of economic growth achieved by Latin America, as opposed to other developing regions, its income distribution is hugely uneven, the poverty index is very high, the middle class is increasingly poorer and social problems are harder to solve. The author argues that the reason for this is to be found in the unconditional manner in which the economic model adopted in recent years has been applied. In the quest for economic liberalization social policies have been left somewhat behind. Also, the region's integration agreements have viewed social issues as marginal. But for policies to be effective they must translate economic growth into development. This, argues the author, will be the only way to increase the social well-being of the majority.*

*Es un hecho reconocido por todos que América Latina, a pesar del importante ritmo de crecimiento económico alcanzado comparado con otras regiones en desarrollo, sobre todo en los años noventa, mantiene enormes desigualdades en la distribución del ingreso, elevadísimos índices de pobreza, depauperización acelerada de la clase media y acuciantes problemas sociales cada vez más difíciles de resolver.*

*Por supuesto que son múltiples y complejas las causas de este fenómeno, pero tal vez la razón fundamental se encuentre en la forma incondicional de aplicar el modelo económico que se ha seguido en los años recientes, sobre todo en los dos últimos lustros.*

*En dépit du niveau de croissance économique atteint par l'Amérique latine en comparaison d'autres régions en développement, la répartition de son revenu est extrêmement inégale, l'indice de pauvreté très élevé, les classes moyennes vont s'appauvrissant et les problèmes sociaux sont toujours plus difficiles à résoudre. De l'avis de l'auteur, cela tient à ce l'application incondionnelle du modèle économique adopté ces dernières années dans l'optique d'une libéralisation de l'économie a relégué au second plan les politiques sociales. Les accords d'intégration régionale n'ont réservé aux aspects sociaux qu'une place marginale. Mais, pour être effectives, les politiques doivent rapporter la croissance économique au développement. C'est, selon l'auteur, le seul moyen d'accroître le bien-être du plus grand nombre.*

*Apesar do nível de crescimento econômico alcançado pela América Latina, em comparação com o de outras regiões em desenvolvimento, a distribuição da receita é enormemente desigual; o índice de pobreza é sumamente alto, a classe média é cada vez mais pobre e os problemas sociais tornam-se cada vez mais difíceis de se resolver. O autor afirma que isso se deve à maneira incondicional em que se tem aplicado o modelo econômico adotado nos últimos anos. Em nome da liberalização econômica tem-se abandonado, de certa maneira, as políticas sociais; do mesmo modo, os acordos de integração da região têm considerado o aspecto social de uma maneira marginal. Entretanto, para que as políticas sejam efetivas, é necessário que o crescimento econômico se traduza em desenvolvimento. Esta será, segundo o autor, a única maneira de promover o bem-estar social da maioria.*

# The Social Dimension of Integration

⇒ **Telasco Pulgar**

*Coordinator in Chief of Integration Permanent Secretariat, SELA.*

## I. Introduction

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It is a well known fact that, in spite of the level of economic growth achieved by Latin America as opposed to other developing regions, particularly during the nineties, its income distribution is hugely uneven, the poverty index is very high, the middle class is becoming increasingly poorer and urgent social problems are harder to solve.

Obviously, this phenomenon is due to multiple and complex causes. However, perhaps the fundamental reason for this is to be found in the unconditional manner in which the economic model adopted in recent years has been applied, particularly during the last ten years.

## II. The Development Model

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Just as the world economic situation changed significantly as a result of globalization and the new tecno-production paradigm, so have the Latin American countries' development policies experienced an important turnaround during the last years, particularly since the mid-eighties. Almost all countries, some later than others, were faced with the need to adopt heroic measures to stabilize their economies and to meet their onerous foreign debt obligations. The inward oriented development model was replaced by the outward oriented model, based on liberalization policies which were introduced after more than half a century of protectionism. The neo-liberal school of thought provided the theoretical foundations for the new approach. This prescribed that greater priority should be given to market forces as resources' allocators and that the State should abstain from, or limit its role in the administration of the economy. Far reaching economic and trade reforms, some hurried and abrupt, were introduced with different levels of intensity and speed. They were part of a wider program aimed at surrendering to market forces the majority, if not all, of economic decisions, without contemplating any income redistribution mechanisms.

That economic model was to lead, at a later stage, to a new type of economic expansion, based on international competitiveness. This, in turn, would eventually result in increased social well being. Unfortunately, the transition toward that second stage was never achieved and appears every day harder to reach as the so-called social deficit increases by the day. A quick look at the latest reports from the international agencies that deal with statistics on social issues is enough to become aware of the sad reality faced by Latin America.

Halfway through the nineties, close to 200 million Latin Americans, 46% of the total population, are not able to meet their basic needs, while almost 100 million live in extreme poverty. Real salaries have dropped to levels well below those achieved in the eighties. In spite of renewed economic growth in most countries, poverty continues to climb and indigence has increased significantly in the region.

The decline and backwardness of the Latin American economies' food producing sectors tend to aggravate this situation. Indeed, since the beginning of the eighties, Latin America has ceased to be a net producer and exporter of foodstuffs to become a heavy importer of these products as well as of the raw materials and inputs needed to produce them. And these deficits are growing. Self sufficiency in cereals, vegetables and milk has decreased considerably. According to studies on this issue, by the year 2000, when the Latin American population will be close to 600 million, self sufficiency in cereals, vegetables, milk and meat will have decreased even more.

The following opinions express clearly Latin America's harsh social reality: «Our economic model makes production growth possible, but does not imply employment growth. Latin America is growing, but not its work force. This situation is a cause of grave concern to the region's Governments» (Moneta, interview in *Economía Hoy*, 1997, Caracas).

«In a situation of market globalization, industrial investments are aimed at reducing costs, rather than increasing employment. In the years 1990-1995 the Gross Internal Product (of Argentina) grew by approximately 30%. However, such growth increased global employment by only 3% (Rocca, Argentine business leader, 1997).

«Today Latin America is the world's most inequitable region. This is reflected in the fact that the accomplishments derived from economic growth do not reach the poor sectors. Nor does

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*In spite of renewed economic growth in most countries, poverty continues to climb and indigence has increased significantly in the region*  
 ”

a wide sector of the middle class benefit from them. While in some societies such as Switzerland the middle class represents 60% of the population, in several Latin American countries it is less than 20%. Inequity locks the wealth distribution mechanisms» (Kliksberg, Chile, 1995).

«The more favorable evolution of economic growth has not resulted in employment growth. On the contrary, data on the year's (1996) first three quarters indicate that unemployment kept growing after a considerable increase in 1995. In 1996, urban unemployment reached the highest level in the decade» (ECLA, Balance 1996).

Nevertheless, the long period of neoliberal and macro-economic adjustment policies, under the tutelage of international economic and financial institutions (WB and IMF), has taught us three basic lessons: First, that economic growth does not automatically generate social well being, on the contrary, it may create poverty. Second, that equitable public policies are needed, in particular those aimed at the redistribution of growing income, so that such income may reach the more disadvantaged sectors of society and thus complement and support open market policies. Third that extremist positions are not effective in economic policy just as they are not in politics. Effective policies are those that translate economic growth into development, the only way to increase the social well being of the majority.

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 majority*  
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### III. The New Social Agenda

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In view of the situation described above, it became imperative to take into account social issues when formulating development policies, particularly integration policies. Slowly, the need was felt to coordinate economic policies and social policies that could transcend national boundaries.

Indeed, little by little Chile's social policies, for example, have gone beyond local regulations to enter into the realm of international negotiations on the most diverse issues (Gretschmann, Chile, 1995). The most significant achievements within this context were the Social Clause resulting from the Uruguay Round which links international trade with social issues, and the Copenhagen World Social Summit, which internationalized issues such as poverty reduction, competitiveness training and coordination of economic and social policies. To these initiatives

we must add previous worthy efforts in this field by UNESCO, UNICEF and UNDP.

In Latin America, ECLA developed an integrated approach to economic policies that placed much emphasis on social issues, the concept of «productive transformation with equity». UNDP produced instructive reports on this issue and developed the concept of «human development». IDB declared the social question a central issue in its development programs for the region. An important part of IDB's financing for the region has been earmarked for investments in the social sector and the Inter-American Institute for Social Development has been created.

On the political level, the importance that is now being assigned to social issues is demonstrated by declarations and mandates issued at high level meetings such as the Group of Rio Presidential Meeting, the Ibero-American Summits, the Miami Summit, and SELA's Latin American Council Meetings.

In this context, we should refer to the coordination of efforts undertaken by the Latin American Centre for Development Administration (CLAD), ECLA and SELA. This has given rise to the project «Coordination of Economic and Social Policies», began in 1995. The project's aim is to present to those responsible for the formulation and implementation of economic and social policies, a number of suggestions for a better development of integrated policies. The first phase of the project has concluded. Its task was to research and prepare documents for experts' workshops on the issue. The second phase has already begun. Its aim is to analyze specific problems previously identified, compare the experience of several countries of the region in this field and organize training seminars for government officials, as well as meetings and other activities to inform on the results achieved.

#### **IV. Integration as a Social Project**

The social issue has also become a part of the new efforts to restructure the integration modalities prevailing since the sixties. These did not, as a whole, deal with two issues crucial for integration. The first is the social dimension of integration. That is, the problems related with health, education, culture, the free movement of people, migrations, the training of human resources to face successfully the new techno-production paradigm, and the progressive adaptation of labor conditions to the increasing demands of a wider work environment. All of these are necessary ingredients if integration is to translate into concrete



deeds and in order for it to consolidate itself at the institutional level. The second issue refers to the actions needed to confront and attenuate the impact of economic integration on the societies of participating countries, particularly on labor intensive productive sectors, border areas specifically affected and some social groups who may feel left aside.

In other words, the achievement of an equitable integration would appear to be the next stage in the process that has been unfolding since the beginning of the nineties. Such process was aimed at strengthening integration through the adoption of open market policies that would insure the region's participation in the world economy on competitive terms.

In reality, the social question has always been present when entering into integration commitments (ECLA, Social Policies Series, 1996). The cultural (Andrés Bello), health (Hipólito Unánue) and social-labor agreements (Simón Rodríguez) approved by the Andean Group in its first year of life are an example of this. However, the Andean Social Chart, underwritten in 1994, is, undoubtedly, the most important example of the incorporation of social issues into integration efforts.

In ALADI, important resolutions aimed at creating a common market of cultural and educational assets were approved.

Within the framework of the Central American integration process, important agreements were signed dealing with pressing social problems such as disabled minors, housing and human settlements, the circulation of cultural assets and the development of human resources, among others. The most significant achievement in this context was the signing, in 1995, of the Central American Social Integration Treaty.

More recently, within the framework of MERCOSUR, the Ouro Preto Protocol established the Economic and Social Consultation Forum, which includes workers and consumers. The Forum complements the activities of the Working Sub-Group 11, which has been studying labor, employment and social security issues. MERCOSUR countries are well advanced in the negotiations on a social security agreement. Nevertheless, with the exception of some trade and tariff commitments, Latin American integration agreements have viewed social issues as marginal, as some kind of a sub-product. They have not created mechanisms, nor allocated resources to deal with the social aspects of integration,

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*Latin American  
 integration  
 agreements have  
 viewed social issues  
 as marginal,*  
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to decrease economic disparities, nor to support the social sectors most affected by economic integration.

However, «it is methodologically very difficult to differentiate the social effects of integration from those resulting from insertion in the global economy, especially if we consider that the latter is accompanied by deregulation of local markets» (Pareja, F., Cartagena, 1996).

Therefore, in order for integration to achieve a social dimension it is necessary to concentrate efforts on very specific social issues. From the studies and debates undertaken by ECLA, CLAD, IDB, CEFIR, the Integration Secretariats and SELA, and above all by the joint seminars and meetings that are being organized, it is possible to deduce that efforts are being made at drawing a «social agenda of integration» that includes, at least, the following issues: (i) cooperation between organizations and countries on problems related to the free movement of people, the mutual recognition of educational degrees, labor laws, migration, regulations in the social security field (health, retirement, among others); and (ii) policies and measures to alleviate integration's negative social effects such as labor retraining, training of human resources for the modernization of production, support for geographical border areas, support for key productive sectors, among others.

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***Intra-Latinamerican Financial Engineering***

*The improvement of financial services in Latin America and the Caribbean has begun within the framework of trade and foreign investment liberalization, originating two parallel phenomena: the surprising increase in international capital flows to the region and the strengthening and expansion of integration between the capital markets of Latin American and Caribbean countries.*

*Nevertheless, the region's financial sector still exhibits structural weaknesses which inhibit a faster modernization pace and the full exploitation of the opportunities offered by regional and international trade.*

*La reforma de los servicios financieros en América Latina y el Caribe, iniciada en el contexto de la apertura al comercio y a la inversión extranjera, dio lugar a dos fenómenos paralelos: el sorprendente aumento de los flujos de capitales internacionales hacia la región y la profundización de la integración entre los mercados de capital de América Latina y el Caribe.*

*Sin embargo, el balance global de las reformas financieras aún adolece de debilidades estructurales que le impiden avanzar más rápido en la modernización y aprovechar plenamente las oportunidades que brindan el comercio y la integración regional.*

# Intra-Latinamerican Financial Engineering

→ SELA's Permanent Secretariat

## I. The Opening of Financial Services: Positive and Negative Factors

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The improvement of financial services in Latin America and the Caribbean has begun within the framework of trade and foreign investment liberalization, originating two parallel phenomena: on the one hand, the surprising increase in international capital flows to the region and, on the other, the strengthening and expansion of integration between the capital markets of Latin American and Caribbean countries.

This process takes place within the wider framework of trade and financial globalization. The huge increase in foreign direct investment flows is easily confirmed. During the ten years prior to 1993, investment flows throughout the world multiplied by four, reaching a total of \$ 200 billion per year. Similarly, in the last forty years, trade flows multiplied by 15 and production increased sixfold. In addition to this, the market has grown tremendously: in the coming years 2 billion people from developing and transition economies will enter the world market.

As for Latin America's position within the international financial system, in a period of 10 years it has changed from one of foreign indebtedness to one of «emerging region» in which several countries are privileged recipients of foreign capital. According to ECLAC's preliminary estimates, last year total capital flows to Latin America reached approximately \$ 50 billion , a level comparable with that of 1993 and 1994, before the 1995 recession. For example, it is estimated that in 1996 Brazil alone received a total of \$ 8 billion, three times the 1995 level.

This means that those pessimistic forecasts announcing that many years would pass before the region would become attractive once again for foreign investments, did not take into account the fact that, as in many other aspects of today's economic life, changes- be they positive or negative- occur at a much faster pace than in the past.

Something similar is happening with the progress in economic and trade integration between the countries of the region.

Reality has exceeded the most daring predictions not only regarding the growth in intra-regional trade, but also in reference to capital flows between countries of the region. For the first time in history, a tangible relationship has been established between commercial and financial integration. In some countries, such as Argentina, more than 12% of total foreign direct investment originates from the region.

Sub-regional agreements are, in some cases, directly responsible for intra-regional investment operations such as those between Colombia and Venezuela, or those among MERCOSUR countries which, among other instruments, created the National Banks of the South network (Banasur), whose members are the

Banco de la Nación Argentina, Banco do Brasil, Banco de Fomento de Paraguay and Uruguay's Banco República.

Conversely, in other cases, such as with Chile, capital exports toward other countries of the region preceded any trade agreement (as MERCOSUR's Economic Complementation Agreement) due to several reasons, among these:

1. The development and consolidation of Chilean companies relatively too large for a narrow national market.
2. High local savings rates.
3. The need to minimize risks by diversifying export markets.
4. The increase in exports' flows, the commercialization of which originates investments in the importing countries' financial institutions.

In this way, for example, Chile's Banco O'Higgins bought 87% of Banco Popular Argentino, for \$40 million; the Luksic Group bought, for \$75 million, Argentina's Credit Lyonnais Bank. Furthermore, in what could be a growing tendency in the future, Chilean Pension Funds and insurance companies invested \$45 million in Argentina.

In Perú as well financial enterprises accompany and strengthen investments in goods and services' producing firms. Witness, for example, the investments in Chile by the Errázuriz Group, the Santa Cruz Group, Financiera Cordell, Banco de Osorno, etc., and the new flow of investments towards Bolivia.

This process is further defined by mutual investments between Argentina and Brasil, between Colombia, Venezuela and México (G-3) and by Mexico's investments in Central America.

Hence, statistics prove what international economics textbooks state, namely, that trade and financial liberalization, when

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*Reality has exceeded the most daring predictions not only regarding the growth in intra-regional trade, but also in reference to capital flows between countries of the region*

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combined, as is the case in our region, nurture each other and create an attractive environment for both, international investments and intra-regional investment flows.

Nevertheless, the transformations undergone by the region's financial sector within the last few years were not completely positive. This sector still presents structural weaknesses which inhibit a faster modernization pace and the full exploitation of the opportunities offered by the dynamics of regional and international trade.

The basic weakness that affects the further development of the financial sector in Latin American economies can be summed up with the word «instability» which, to a greater or lesser extent, derives from external and internal factors.

A recent IMF study analyzes the roots of instability in «growing markets», in the light of their fast-paced internal financial liberalization and the growing freedom of movement for foreign capital flows. Within this context, the study attempts to evaluate to what extent the volatility and predictability of investments in emerging and in developed markets differ (1).

The paper's conclusions are, to some extent, surprising. The IMF points out that it would be inaccurate to state that «all» emerging markets are unstable, or that they have become more unstable recently as a result of growing capital flows. The study affirms that such generalization is incorrect and that, in many cases, the roots of some emerging markets' instability were already in place before foreign investors found these markets attractive.

The IMF document points out several factors that should be analyzed in the light of national traits. All of these are relevant for the Latin American and Caribbean financial sector :

—In the first place, the general instability of emerging markets, compared with developed markets, does not seem to have increased much in the last few years. However, the danger of «speculation bubbles» cannot be dismissed.

—In the second place, the document confirms that, in a process of growing liberalization, excessive capital flows may cause an unjustified raise in the exchange rate, unsustainable current account deficits and speculation «bubbles». All of these are particularly dangerous in a developing economy lacking

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*The basic weakness that affects the further development of the financial sector in Latin American economies can be summed up with the word «instability» which, to a greater or lesser extent, derives from external and internal factors.*

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adequate supervision and regulation mechanisms for the banking sector.

Therefore, the IMF points out that the risks involved in the liberalization of emerging markets' financial services may be minimized as long as «strict supervision and prudent reclamation» is established in order «to grant support to the appropriate policies and reduce damage to the minimum should variations arise» in capital flows. Moreover, «in some cases, perhaps it would be convenient to proceed to a progressive liberalization», in order for emerging markets to develop the capacity needed to absorb the amount of capital they attract.

## II. The Way Ahead

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The region's liberalization and financial integration process is uneven not only because it poses both benefits and risks, but also because it succeeded more in attracting international capital than in achieving full and productive integration between the regional commercial and financial sectors.

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*To date, extra-regional  
 investors are the  
 greatest beneficiaries of  
 our countries' trade and  
 financial liberalization.*  
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In point of fact, to date, extra-regional investors are the greatest beneficiaries of our countries' trade and financial liberalization. World Trade Organization's most recent figures estimate that, today, direct investments among Latin American countries represent, approximately, less than 5% of total foreign direct investment in the region. Considering how

recent this phenomena is, such percentage is significant, however, it is still very small compared with the potentials for investment inherent in the growing economic relations between countries of the region.

In other words, even though it was well conceived and planned since the beginning of the regional and sub-regional economic integration process, the financial integration of Latin America and the Caribbean is still an unfinished task.

Let us consider some of the steps that, in this Secretariat's opinion, are essential for the modernization and strengthening of financial links within the Latin American region.

The first step that is required is a change in mentality. Foreign trade growth, both within and without the region should be backed by sound coordination between commercial banks, regional and sub-regional financial institutions and governmental institutions in charge of trade integration. For this to occur, financial integration should hold a position similar to that held by trade and



economic integration between Latin American and Caribbean countries, in the public and private sectors' external economic strategies. Along these lines, and based on criteria formulated by both, public and private sector, it would be useful to undertake a comprehensive evaluation of existing regional and sub-regional financial institutions, in order to determine if their policies and operations meet the needs created by local financial liberalization and by the strengthening of trade integration between countries of the region.

The second step toward greater regional financial integration has to do with the harmonization of rules on financial services in countries of the region, at least at the minimum common denominator level. In effect, liberalization has proceeded along different criteria and at varying speed depending on the country, even though the pattern has been generally the same. Within the framework of the World Trade Organization, the negotiations on trade in financial services, began in 1995, will lead, in the medium term, to the harmonization, at the multilateral level, of rules on, for example, financial institutions' right of establishment and their local market operations, or on stock markets performance. It would be convenient for those in charge of the region's financial sector at the public and private level to insist, within the framework of intra-regional integration mechanisms and agreements, that rules be harmonized in accordance with the realities created by liberalization policies and by financial movements in Latin American countries. In this context, they could, for example, explore the possibility of negotiating a regional agreement on prudential rules (on the basis of the Basilea Agreements) in order to ensure stability and harmony among financial systems within the region.

In the third place, it is important that the banking community and the public sector increase contacts and exchange experiences in order to identify the problems faced by Latin American bankers, businessmen and merchants when resorting to intra-regional integration mechanisms and agreements. By the same token, other regions' integration experiences, such as the European Union's integration of financial services, may enrich our own.

Finally, we need to envision and explore new formulas to engage the region's private capital in the financing of infrastructure projects needed to foster trade growth between our countries. The bio-oceanic corridors (SELA, The Rome Club) are

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*We need to envision and explore new formulas to engage the region's private capital in the financing of infrastructure projects needed to foster trade growth between our countries.*

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examples of projects that successfully combine long term financing with economic profitability. Here again, the key element is coordination between private banking and regional or sub-regional financial institutions, through strategic alliances that may allow ample mobilization of long term resources, together with proper management of the financial risks involved.

The consolidation and strengthening of regional financial integration cannot be postponed, otherwise we run the risk not only of leaving the liberalization process vulnerable to fluctuations in international capital flows, but also of allowing extra-regional capital to benefit from the opportunities created by trade and the integration process between our countries.

### **Notas**

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## **Antonio de Cerqueira Antunes: Latin America is Evolving Toward a New Type of Trade**

Antonio Antunes is a civil engineer with a specialization in economic and social development and industrial planning.

In March, 1990, he was appointed Deputy Secretary General of ALADI and played an important role in redirecting that organization's work and introducing new cooperation issues such as environment, science and technology, standards and others.

On March 16, 1993, he was appointed Secretary General of ALADI for the term 1993-1996, the first Brazilian to head that Organization's technical body.

In 1996, Antunes is reelected Secretary General of that Organization. In his new triennial term he will set in motion the restructuring of the Organization. Among the General Secretariat's initiatives aimed at adapting its work with the needs of ALADI eleven member countries at this point of the integration process, is that of granting the Organization enough flexibility to deal with the dynamics of negotiations and intra-regional and international relations.

In Brazil, Antunes held high positions in the Ministries of Finance, Industry and Trade, Transportation and in the Planning Office of the Presidency. He represented these ministries in several inter-ministerial commissions, including the commission responsible for designing, during 1985-1990, a modern industrial policy for Brazil, replacing the old imports substitution policies.

Previously, he worked as an international civil servant in the Latin American Institute for Economic and Social Planning of the United Nations (ILPES), with Headquarters in Santiago, Chile, where he contributed to the drafting of development strategies for several Latin American countries such as Venezuela, the Dominican Republic, Costa Rica, Ecuador, as well as for the Northern region of Chile and Minas Gerais in Brazil. He also worked on studies for the Andean Group.

Antunes is the author of several works on economic and industrial development, infrastructure and transportation and regional integration.

**1. Regional integration has experienced significant changes in the nineties. It exhibits greater dynamism and diversity -customs unions, trilateral trade areas (G3 and ALCA), multiplicity of economic complementation agreements- and the growing participation of business in the process. All these transformations raise questions on the traditional role of integration organizations. What measures has ALADI taken to adapt to this new reality?**

—During the last meeting of ALADI's Ministerial Council (Ninth Meeting, December, 5-6, 1995) a number of measures were adopted to consolidate, at hemispheric level, the process of regional integration, to adapt the General Secretariat's institutions and administration to the new needs, and to back the competitiveness of relatively less developed countries. The widening and strengthening of bilateral, subregional and regional agreements signed within the framework of the 1980 Montevideo Treaty, are some of the measures undertaken. The aim is to progress toward higher levels of regional integration. In this context, the Association has agreed to promote negotiations between member countries and, when the case arises, with subregional groups of the Association's members countries and Central American and Caribbean countries. The final objectives encompass the consolidation of regional integration, particularly through intra-regional trade liberalization, the widening of markets and the growth of regional investment.

ALADI clearly understands that such negotiations must contribute to the convergence of existing bilateral and subregional schemes and to growth in reciprocal trade, as well as to the development of different types of cooperation and complementation in other areas and specific sectors.

The Secretariat's role was strengthened when the Council of Ministers requested that it grant technical support to the above-mentioned negotiations, catering to the specific needs of the participating countries. At the same time, the Association adopted a work programme, for which the Secretariat will prepare comparative studies of bilateral and subregional agreements existing within the framework of the 1980 Montevideo Treaty, with a view to converge toward the consolidation of regional integration and keeping in mind that such agreements form the basis for the creation of the Free Trade Area of the Americas (FTAA).

**2. Within a period of only five years (1990-95), trade among Latin American and Caribbean countries increased from \$16**

**billion to \$43 billion, while intra-Latin American participation in total exports grew from 13% to 19%. Granted the unquestionable success these figures demonstrate, there is an interest for integration to move beyond the merely commercial sphere. What measures should the region adopt to insure a more «integrated» coverage of integration?**

– In relation to the need for ALADI to cover the widest possible range of integration's issues and sectors, I should mention that the subjects of transportation's infrastructure, cultural activities, science and technology, environment, standards, tourism and many others have been incorporated in the Association's work programme.

Moreover, on many of these topics agreements have been reached, signaling that we are moving toward a wider coverage of integration.

**3. Experts' analyses have coincided in pointing out that «the process of convergence of the different integration agreements has proven to be a harder than imagined task» In light of ALADI's experience, which characteristics should the process of regional convergence have? How can present obstacles be overcome? Which are the best time frames?**

– ALADI's experience demonstrates that the region is moving toward a heterodox type of free trade. There are ten free trade agreements: subregional agreements, comprising the Andean Group, the Group of Three and MERCOSUR; bilateral agreements, comprising Chile's agreements with Venezuela, Colombia and Ecuador; and Mexico's agreements with Chile and Bolivia. A great percentage of trade has been freed by these accords. By the year 2007, all trade covered by each of these agreements will be liberated. This represents 77 % of intra-regional trade, which, in 1995, reached a total of \$35.5 billion.

By that year, the 52 bilateral relations envisioned in those ten agreements, among the eleven countries members of ALADI, will have established a free trade system.

Negotiations are taking place between MERCOSUR and the Andean countries and Mexico; Mexico and Ecuador and Chile and Peru. MERCOSUR's negotiations with the Andean countries (Colombia, Ecuador, Peru, Venezuela) seek to establish a type of free trade similar to that envisioned in MERCOSUR's agreement with Chile.

Consequently, negotiations on regional convergence are

coming through and will continue, in our opinion, as preexisting agreements are added.

Evidently, the 2005 deadline for the culmination of negotiations on the FTAA represents a point of reference and a challenge for converging ALADI's bilateral and subregional agreements, even though no such deadline has been set for convergence.

It is possible that the negotiations between Colombia, Ecuador, Peru, Venezuela and MERCOSUR will conclude by the end of this year or the beginning of the next. Probably, such agreements will originate, among ALADI members, a number of questions related with their simultaneous participation in different agreements. Such participation may be harmonized by establishing families of agreements on basic issues, thus affecting the public and private actors involved in the execution of the whole set of agreements in each participating country.

It is not possible to anticipate the time frames for convergence of such agreements. A clearer picture of these will emerge at the end of the above-mentioned negotiations.

**4. During the hemisphere's Meeting of Vice- Ministers for Trade, held at the end of February in Recife, two strategies were identified for the establishment of the Free Trade Area of the Americas. The United States proposed that negotiations be accelerated in order to obtain zero tariff by the year 2005. On the other hand, MERCOSUR countries held that negotiations should begin in 2005, once regional integration had been strengthened, and that sensitive products should continue to be excepted. What is your opinion regarding the FTAA's time frames and characteristics? Which previous conditions should exist, from the point of view of Latin America and the Caribbean? Which are the points of convergence and divergence between the FTAA and regional integration?**

— The creation of the FTAA will not dismiss the fact that it must be conditioned to the coordination of bilateral and sub-regional agreements. National and transnational actors have concrete reasons to support such convergence, just as there are reasons for improving the negotiating power of the countries benefiting from this process. Hence, even if negotiations between ALADI members and Central American and Caribbean countries, and negotiations on the FTAA are simultaneous, this will undoubtedly imply different time frames to allow for the creation of groups where closer relations are envisioned which are not incompatible with hemispheric liberalization.

More important than time frames will be the intensity of relations between different areas that will become compatible. In order for this complex scheme to become a reality, the pace of the negotiations has to be accelerated.

While no conclusions are reached on how to build the FTAA, no definition may be arrived at concerning convergence or divergence between the FTAA and regional integration schemes. Such schemes are already a reality, whereas the FTAA is still a subject whose methodology of negotiations is being discussed.

The natural process of convergence into bilateral and sub-regional agreements, and the inevitable need for liberalization to be gradual will provide countries more advanced in such liberalization the strength to carry out their policies in this field.

**5. At the WTO Ministerial Conference held in Singapore, it was agreed «to facilitate world and regional trade liberalization processes that support each other». Which concrete actions should countries undertake in order for regionalism and multilateralism to be not only compatible but complementary?**

—Regionalism and multilateralism are compatible because the configuration of blocs is part of the globalization process. The challenge for Latin American countries is to meet their obligations and obtain better results in the WTO negotiations, rather than to seek complementarity between regionalism and multilateralism. Also, countries of the region should intensify the fulfillment of bilateral and subregional agreements, as well as their convergence and articulation, in order to play a greater role in world trade and thus gain more negotiating power.

**6. Sub-regional agreements such as MERCOSUR and the Andean Community are becoming stronger at their own pace, following time frames and priorities defined by their members. The pace of globalization, on the other hand, is imposed by external phenomena. How can countries counteract globalization's negative effects and take advantage of its potential? What should Latin America and the Caribbean do in order to make the effects of globalization compatible with their integration objectives?**

—Making MERCOSUR compatible with the Andean Community and with Central American and Caribbean countries through bilateral and sub-regional agreements is a way to stimulate those

countries to integrate into the global process in a more competitive manner.

In order for countries to take advantage of the opportunities globalization may offer and to reduce its negative impact, regional agreements will have to be strengthened and made to converge.

In the process of convergence among Latin American and Caribbean countries it is important to create groups that are not mutually exclusive in such a way that each of these groups harmonize trade regulations and agreements' rules, devise flexible liberalization projects and establish the necessary links between their transportation, energy and communications systems and develop inter-regional and extra-regional production and trade.



# **Communique of the Eighth Inter-Sessional Meeting of the Conference of CARICOM Heads of Government**

The Eighth Inter-sessional Meeting of the Conference of Heads of Government of the Caribbean Community took place in Antigua and Barbuda from the 19-21 February, 1997.

Eleven of the 14 CARICOM Heads of Government attended the meeting, while The Bahamas was represented by the Minister of Foreign Affairs, the Hon. Janet Boswick; Guyana by the Ambassador to Belgium and the European Union, H.E. Dr. Havelock Brewster, and Grenada by Dr. the Hon Raphael Fletcher, Minister of Legal Affairs and Local Government.

The President of the Dominican Republic, H.E. Leonel Fernández and of Haiti, H.E. Rene Preval also participated in the meeting. In their address at the Opening Ceremony both Presidents referred to the changing dynamics of Caribbean external economic relations, and in particular the likely changes in respect of the Lome arrangement with the European Union.

During the Opening Ceremony, the Secretary General of CARICOM, Dr. Edwin Carrington, signed with Mr. Athanassios, Deputy Director General of the Development Directorate of the European Commission, the Second Financial Protocol of Lome IV which permits the use of ECU 90M for regional projects over the next 5 years.

The opportunity was also taken to sign the Charter of Civil Society which consolidates various undertakings by CARICOM countries in respect of good governance and respect for civil, political and economic rights, and the Protocol amending the Organs, Institutions and Procedures of the Community.

## **Signing of the Protocol Amending the Treaty Establishing the Caribbean Community and of the Charter of Civil Society**

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On 19 February 1997, the Heads of Government participated in a special ceremony to execute the Charter of Civil Society and

the Protocol Amending the Treaty Establishing the Caribbean Community whose entry into force will constitute a significant first-step in the establishment of the Caricom Single Market and Economy. The Protocol, which establishes a number of New Organs, Institutions and Procedures of the Caribbean Community, is the first in a series of instruments being elaborated in accordance with decisions adopted by the Conference of Heads of Government at its Special Meeting in Port-of-Spain, Trinidad and Tobago, in October 1992, to revise the Treaty of Chaguaramas. This Protocol confirms the status of the Community as an association of sovereign states, reaffirms the status of the Conference as the Supreme Organ of the Community, establishes more efficient and flexible procedures for decision-making and rationalises the organizational structure of the Community. Consonant with the perception of the West Indian Commission which recommended its development and adoption, the Charter of Civil Society is declaratory and does not itself create legally binding obligations. However, it consolidates various obligations and undertakings assumed by CARICOM States in relation to good governance, including respect for civil, political and economic rights and the rule of law.

### **The Caribbean Regional Indicative Programme**

The Caribbean Regional Indicative Programme (CRIP) under the Second Financial Protocol of the Lomé IV Convention was signed by Mr. Edwin Carrington, Secretary-General of the Caribbean Forum (CARIFORUM) of African, Caribbean and Pacific States and Mr. Athanassios Theodorakis, Deputy Director-General, Directorate General for Development, Commission of the European Union.

The Agreement, whose duration extends to the year 2000, will provide for the financing of regional projects under the Second Financial Protocol of the Lomé IV Convention. The financial resources to be provided by the EU for the CRIP amount to some ECU 90 million (US\$ 110m).

An additional sum of ECU 14 million from other European Commission sources would be made available to assist in financing some aspects of the Action Plan for Drug Control in the Caribbean which was adopted in Barbados in 1996. The new Agreement would ensure more timely implementation of projects.

Mr. Theodorakis conveyed to the Government and people of Montserrat, the continuing solidarity of Commissioner Pinheiro in connection with the threat posed by the Soufriere Hills volcano.

The satisfaction of the EU with the development of closer relations between the Caribbean Community and the Dominican Republic and the Republic of Haiti was highlighted as were, *inter-alia*, the role of the Caribbean in the restoration of democracy in the Republic of Haiti, the accomodation of Cuba in the Association of Caribbean States (ACS) and the participation of the Caribbean in wider hemispheric activities in the spirit of open regionalism.

The total allocation to national indicative programmes of CARIFORUM Member States, amounting to ECU 543 million (\$ 685m) represented a significant effort in comparison with the efforts of other international donors. There was also the possibility of concessional funds from the European Investment Bank. In the ensuing three years, the representative of the EU indicated, emphasis will be placed on efficiency, transparency and performance-oriented cooperation, as well as on the concentration of resources on a limited number of sectors with a view to securing a greater level of balance among programmes.

### **The Post-Lomé IV Caribbean-EU Relationship**

The Heads of Government of the Caribbean Community, together with the President of the Dominican Republic and the President of the Republic of Haiti, held a Retreat at Jumby Bay, Long Island, to consider the Caribbean approach to the relationship with the European Union after the Expiry of the Lomé IV Convention. The participation of the Dominican Republic and the Republic of Haiti signals the involvement of all CARIFORUM Member States in the preparation process. These two Governments pledged to be part of the process which CARICOM had initiated with respect to the preparation for the negotiations of a successor agreement to Lomé IV. Heads of Government reaffirmed that the Caribbean placed significant importance on the Region's relationship with the EU and that they were determined to maintain and enhance that relationship following the expiry of Lomé IV.

They also reaffirmed the Region's intention to maintain solidarity with the wider ACP Group as a single, cohesive entity in their future relationship with the EU and restated the commitment of the Caribbean countries to work for a new ACP-EU arrangement that reflects their needs and interests as well as those of other ACP countries.

The Heads of Government acknowledged that the increasing globalisation of the world economy and hemispheric developments, including the initiative towards the creation of a Free

Trade Area of the Americas, could, conceivably, have implications for the Region's future relationship with the European Union. They expressed their determination to enter into any economic or political relationship that would enhance or contribute to the development of the Region. In that regard, they did not consider their various relationships with Europe, with the proposed ALCA or with any other grouping to be mutually exclusive. They decided on policy guidelines for the formulation of Caribbean positions for negotiating the ACP-EU relationship following the expiry of the Lomé IV Convention.

The Heads of Government expressed the view that any further ACP-EU relationship following the expiry of the Lomé IV Convention, should safeguard the Sugar, Rum and Banana Protocols, as well as to protect and improve the trade arrangements for rice.

They further expressed the view that the *post*-Lomé arrangements should contain provisions to facilitate development in new and critical areas, including the services sector and the enhancement of the Region's competitiveness in order to deal with the new circumstances arising from global liberalization in respect of the trade in goods and services.

The Heads of Government acknowledged the direct financial support extended by the European Union to Caribbean ACP States under successive Conventions. They noted that the EU was the largest source of grant aid to the Region. *Post*-Lomé arrangements should seek to preserve these gains.

They recognised that in addition to the debt burden of many Caribbean ACP countries, the changes in the global economy would require adjustments at considerable cost to their fragile economies. To enhance the capability of Caribbean countries to successfully undertake those adjustments, the Heads of Government agreed to explore within the context of the negotiations for a successor ACP-EU Agreement, all possibilities for enhanced financial support from the European Union through existing and new instruments.

The Heads of Government determined that the Caribbean preparatory process for negotiations on the future arrangements would involve, in addition to governments, the Associated States and the social partners.

### **Progress Towards the Establishment of the Single Market and Economy**

The Heads of Government welcomed the fact that implementation of the CARICOM Single Market and Economy (CSME) had

accelerated. The First Protocol signed by Member States and which established the organs, institutions and procedures for the Community provides the part of the legal framework for the CSME. The Second Protocol providing for the Provision of Services, Rights of Establishment and the Movement of Capital is in the process of being finalised for the consideration of the relevant Ministerial bodies.

Arrangements for the free movement of goods are almost completely in place with unauthorised barriers remaining on no more than five items involving three Member States. The intra-regional Double Taxation Agreement is in operation among seven Member States. The Social Security Agreement, providing for the transfer of social security benefits, has entered into force for four Member States who have signed. The legal arrangements for free movement of graduates have been introduced in eight Member States with additional provisions for the movement of other skills in three of these Member States. Eighth Member States now accept identification other than passports at points of entry.

Heads of Government agreed that Member States, during the intervening four months prior to the next Meeting of the Conference, would, *inter-alia*, complete the implementation of Double Taxation Agreement, the Social Security Legislation, the free movement of graduates, the facilitation of travel and the machinery for national consultations. Further, the Conference agreed that the Region would give priority, during 1997, to the creation of an enabling investment climate, an effectively functioning regional capital market, the expansion of the Region's productive capacity and the enhancement of competitiveness of regional production.

The Conference agreed to work towards completing the implementation of the major elements of the CSME by 1999.

### **The Regional Transformation Programme for Agriculture (RTP)**

The Conference reviewed the status report on the Regional Transformation Programme for Agriculture, which it had mandated in the Special Session dedicated to Agriculture in the context of its Seventeenth Regular Meeting.

The Conference emphasized the critical role to be played by the private sector, the NGOs and labor for the effective establishment of Agriculture as an internationally competitive business and agreed that the public sector must ensure the creation of the

requisite climate to attract investment into competitive production in the Region.

The Conference endorsed the thrust and mechanisms being used to implement the RTP with a view to achieving international competitiveness of the agricultural sector for the Twenty-First Century.

The Conference committed itself to put in place vigorous promotion and public education programmes, so as to inform all levels and sectors of our society and also to promote their widespread involvement in various aspects of the RTP with a view to achieving international competitiveness of the agricultural sector for the Twenty-First Century.

The Conference endorsed the regional initiatives being taken to strengthen the biological control of the Pink Mealy Bug in the Region and in that context also endorsed the adoption of measures to facilitate trade in fresh produce. The Conference noted the offer of the Government of Trinidad and Tobago to provide technical training and biological agents for assisting in controlling the Pink Mealy Bug.

### **Mechanism for Negotiation**

The Heads of Government recalled their decisions to establish a structure to enhance the coordinating and execution of external negotiations and agreed to invite Sir Shridath Ramphal to undertake the assignment of Chief Negotiator.

### **Proposed CARICOM-United States of America Summit**

Heads of Government expressed pleasure at the acceptance by President Clinton of their invitation to meet with them. They agreed that this Meeting, which is scheduled in Barbados, in May 1997, will provide an excellent opportunity to set the tone for CARICOM-US relations into the Twenty-First Century.

The Heads of Government agreed on the major issues which the Caribbean Community would wish to discuss with the President of the United States and accepted the offer of President Clinton to send a senior advisor to the Caribbean in March 1997 to advance preparations for the Summit Meeting. They mandated a high-level group under the coordination of the Prime Minister of Barbados to meet with the senior advisor in Barbados to discuss the proposed Agenda to begin the preparatory process for the Summit. They also agreed that the Governments of

Barbados and Jamaica and the CARICOM Secretariat would constitute the core of a planning group for the Summit.

The Heads of Government reaffirmed that CARICOM-US relations will remain a central element in the Region's external relations into the Twenty-first Century and that the upcoming Summit should strengthen the mutual respect and understanding of the United States and CARICOM as sovereign partners.

### **The Situation in Montserrat**

The Conference of Heads of Government received an update on the situation in Montserrat noting, in particular, the need to relocate families to the Deep Zone in the North of the island; to address as a matter of urgency the growing social problems; and the urgency of developing well-designed projects in order to access available funding.

The Meeting underscored its commitment to provide support to Montserrat and agreed to work with the Government in mobilizing and providing financial and technical support.

The Chief Minister of Montserrat expressed the appreciation of the Government and people of Montserrat for the support received so far which included not only financial support, but accommodation for children during the holidays.

### **Movement of Nuclear Waste and Other Hazardous Materials Through the Caribbean**

The Meeting considered the movement of nuclear waste and other hazardous materials through the Caribbean Sea and reiterated that the Community remained implacably opposed to the transshipments of such materials.

### **Meeting with the Emissary of the Southern Cone Common Market (MERCOSUR)**

The Heads of Government received the Emissary of the Southern-Cone Common Market (MERCOSUR) and Minister of Foreign Affairs of Uruguay, the Hon. Alvaro Ramos Trigo.

The Minister expressed his appreciation for the invitation that had been extended to him to address the Conference and indicated that his acceptance of that invitation had also been in the context of strengthening relations between Uruguay and the Region which was considered a natural partner of Latin America.

The evolution of MERCOSUR was outlined, together with the

role of Uruguay in that sub-regional integration process. The achievements of MERCOSUR, its structure, as well as its policy of outreach, including to Central America and the Caribbean were also reviewed. The Emissary also indicated that MERCOSUR supported greater coordination efforts towards the consolidation of integration between both blocs, in order to promote economic and social development and to acquire greater strength and bargaining power for hemispheric and international negotiations with third parties. The Emissary expressed the intention of Uruguay to open a diplomatic mission in the Caribbean and to pursue a process of permanent dialogue with the Region through this medium as well as through the diplomatic representations in Washington among other channels.

The Minister of Foreign Affairs of Trinidad and Tobago and the Prime Minister of Jamaica responded on behalf of the Caribbean Community.

The Minister of Trinidad and Tobago welcomed the presence of the Emissary of MERCOSUR as well as his positive statement on the perspective for the future development of relations between Uruguay and Member States and CARICOM, as well as between MERCOSUR and CARICOM. The Foreign Minister drew attention to the shared features of Uruguay and the Member States of CARICOM in the integration process by reference to the relative size of the respective economies and the determination to implement economic reform in recognition of the contemporary global realities. The basic objective, he postulated, was to ensure that the hemispheric integration process was effectively concluded for the benefit of all. The role being played by MERCOSUR as a major pole of hemispheric integration was recognised.

The Prime Minister of Jamaica remarked on the historical coincidence by virtue of which the Emissary of MERCOSUR to CARICOM had come from Uruguay, given the commonalities in size, economic potential and economic policies of the respective countries.

The opportunity for direct dialogue among the respective countries as a result of their own initiatives as evidenced by the present encounter was to be accorded very high value. Cooperation induced by this kind of interaction would be an asset as both sub-regions sought to engage in meaningful dialogue towards the implementation of the FTAA.

The Prime Minister welcomed the intention of the Government of Uruguay to establish bridges of cooperation through, *inter-alia*, the institutionalization of a diplomatic presence in the Caribbean and through existing arrangements for similar representation,



particularly in Washington Perspectives, on technical cooperation in areas such as human resource development, education, science and technology, health and cultural and youth exchanges were articulated. The Prime Minister wished to be associated with the welcome that had been extended to the Emissary and expressed the hope that the result of this initial meeting will be substantial in historical perspective.

The Deputy Permanent Secretary of the Latin American Economic System (SELA), which facilitated the development of contacts between CARICOM and MERCOSUR, expressed satisfaction at having been invited to witness the historic encounter aimed at intensifying relations between CARICOM and MERCOSUR. He traced the antecedents of the encounter to certain recent events which had at least been co-sponsored by SELA or for which a SELA activity had provided an appropriate environment.

CARICOM and MERCOSUR were viewed as dynamic participants in the hemispheric integration process and, at the sub-regional level, could pursue cooperation in, inter alia, investment, transfer of technology and security issues, including the production, traffic and use of illicit drugs.

### **Proposed US-EU Zero for Agreement on Distilled Spirits**

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The Heads of Government of the Caribbean Community, the President of the Dominican Republic and the President of the Republic of Haiti meeting in caucus at Jumby Bay on 20 February 1997, made proposals with regard to the US proposal for the *zero for zero* treatment for rum in the upcoming negotiations between the US and the European Union in regard to an International Telecommunications Agreement and a *zero for zero* agreement on distilled spirits. The Heads of Government made this proposal in the context of implied or expressed requests from both sides to come up with a recommendation, specific to rum to be included in the *zero for zero* agreement, after Prime Ministers Arthur and Patterson had both rejected a blanket inclusion of rum in the distilled spirits agreement and for a subsequent price brake mechanism being proposed by the USA's representative of the United States Trade Representative.

The following were agreed by the Group:

(i) that zero for zero treatment on rum be limited to the historic Caribbean producers which listed the Members of CARIFORUM (CARICOM plus the Dominican Republic and the Republic of Haiti), Puerto Rico, the British and US Virgin Islands and the

French DOM, which includes Guadeloupe, Marie Galante, Martinique, Reunion and Guyana.

It was recognised:

(i) that this proposal was consistent with workers rights and obtained by the two sides (CBI/USA, Lomé/EU) under the WTO.

(ii) that this proposal would in no way take from any third country any privileges (GSP or otherwise) which they now possess.

This proposal has been agreed by all the industries involved in the process and in fact emanates from Meetings held by the industry.

### **Appreciation**

The Heads of Government expressed their profound gratitude to the Government and people of Antigua and Barbuda for the excellent hospitality extended to their delegations and for the arrangements which ensured a successful Meeting.

### **Arrangements for the Eighteenth Regular Meeting of the Conference of the Heads of Government of the Caribbean Community**

The Heads of Government confirmed their decision to convene the Eighteenth Regular Meeting of the Conference of the Heads of Government of the Caribbean Community in Montego Bay, Jamaica, during the period 30 June to 4 July 1997.

# Keys to Latin America and the Caribbean

Since the beginning of the 90s, that is, in less than ten years, the Latin American and Caribbean economy has undergone a radical change evidenced in higher growth rates, a sharp drop in inflation, sustained export increases, and high levels of foreign capital flows.

Recovery levels have varied among most countries as a direct result of different combinations of opening policies, stabilization of macroeconomic factors—particularly prices, public finances and external accounts— and the renewed impulse given to regional integration.

«Keys to Latin America and the Caribbean», prepared by the Permanent Secretariat of the Latin American Economic System (SELA), sketches the main characteristics of the region's economic evolution explaining its recent performance on the basis of fiscal, monetary, trade, and financial policies, and analyzes the current situation and the prospects



vis-à-vis two crucial factors, namely regional integration and foreign investment.

Far from being a statistics compendium or a theoretical treaty on the region's economics, «Keys to Latin America», as its name clearly suggests, is a work tool and practical reference for potential foreign investors, government officials of extraregional countries, international organizations, research centres, experts, as well as for anyone interested in getting a better grasp of the fast-paced changes that are changing the face of the Latin American and Caribbean region and the trends to be expected for the XXI century.

**Keys to Latin America and the Caribbean may be accessed free of charge through SELA's WWW on the Internet at:**  
<http://lanic.utexas.edu/~sela>

**The Challenges of International Cooperation**

*The President of Suriname described the panorama currently prevailing in his country as a result of the changes in the international scenario determined by the globalization process and pleaded for an increase and renewal of international cooperation.*

*El Presidente de Suriname expuso la situación de su país en el contexto de los cambios producidos en el escenario internacional como consecuencia del proceso de globalización y abogó por una mayor y renovada cooperación internacional.*

*Le président du Suriname a exposé la situation de son pays dans le contexte des changements survenus sur la scène internationale dans la ligne du processus de mondialisation et exhorté à une coopération internationale plus étendue et novatrice.*

*O Presidente do Suriname expôs a situação do seu país no contexto das transformações ocorridas no cenário internacional como consequência do processo de globalização e exortou uma maior e renovada cooperação internacional.*

# The Challenges of International Cooperation

❖ **Dr. Jules Albert Wijdenbosch**

*President of the Republic of Suriname*

*Conference given on February 26, 1997, at SELA's Headquarters, in Caracas, before Representatives of the Diplomatic Corp and Venezuelan dignitaries.*

Although I am officially a guest of President Caldera I thought it expedient, during my State visit to the Republic of Venezuela, to visit SELA of which my country has been a member for years and which Suriname has developed prosperous relations with since its entry into this organization. On behalf of my delegation I would like to thank you for the opportunity to address you.

At the conclusion of the nineties, dynamic developments in the international community are taking place. Technology, trade flows, financial and economic programmes and valid collaboration have now undergone a transformation that has fundamentally changed international relations. The process of globalization and liberalization of world trade that has manifested itself in recent years, the consequences of which have not gone unnoticed by any country, has emphasized the need for more intense cooperation between aligned countries.

Apart from the fact that cooperation on an international level is taking place, the tendency for strengthening mutual cooperation on a regional level is at the same time noticeable. More and more countries participate herein by entering into integration relations with countries in their immediate vicinity departing from the viewpoint that integration can best prosper in a natural environment. Examples are the European Community, NAFTA, CARICOM, ASEAN, MERCOSUR, and ACS. These trade blocs are characterized by an internal regime of freedom of movement of goods, services and persons on the one hand, and protection by way of high tariffs on the other.

Except in the field of economics mutual cooperation is even imperative in cases where borders are being crossed, the approach of which demands a multinational response, regional or international. Crime on a global level, harm to the environment, violation of human rights, undermining of democracy and the

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*The process of globalization and liberalization of world trade that has manifested itself in recent years has emphasized the need for more intense cooperation between aligned countries.*

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constitutional state, and drug-related crime, can not be effectively suppressed by tackling them individually and, therefore, demand a collective approach.

For countries such as Suriname, with a relatively large developmental potential of natural resources, a small population and a still fragile and vulnerable economy, it is of paramount importance to follow these developments very closely and to respond in such a responsible manner that the national interests are served to the utmost. My country has not been spared the effects of these developments and can not afford to idly stand by. Against this background we have become a member of CARICOM and of the Association of Caribbean States and we have committed to the agreements of the «summit of the Americas» which will result in the realization of a hemispheric free trade zone on the American continent in the year 2005.

Since international relations as a whole show strong dynamics and demand a constant monitoring, my Government is now in the process of adjusting international cooperation. At the core hereof is the implementation of a foreign policy aimed at protecting the national sovereignty, at employing economic diplomacy as an instrument for economic development, at the actual integration into the region on a bilateral as well as on a multilateral level, at the diversification of the developmental and international cooperation in the sustainable exploitation of our natural resources, the concept of sustainable human development being an important guiding principle in the developmental cooperation strategies.

In a 1995 World Bank report, my country was indicated as being the seventeenth richest country in the world with regard to the presence of natural resources, the available human resources, and the resulting developmental potentials. My Government's policy is aimed at creating those necessary conditions to make these natural resources available in such a way that they contribute to the realization of a sustainable economic growth. In this developmental concept man will be at the centre point, and not only the macroeconomic indicators, but also the effects on the social-economic low income groups will be scrutinized.

At present the Suriname people suffer from the negative effects of a structural adjustment programme that was not geared to the Surinamese situation. Consequently, the purchasing power of the average Surinamese citizen has dropped drastically since 1990, the unemployment percentage has increased, the economic activities have strongly decreased and

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*Since international relations as a whole show strong dynamics and demand a constant monitoring, my Government is now in the process of adjusting international cooperation.*

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the interest rate has increased in such a manner that investments fail to occur.

Therefore, my Government, since its inauguration, has introduced a National Reconstruction Programme in which attention is given to the development of man, the struggle against poverty and the increase of national production take priority, the necessary conditions to promote national and international investment are created, and the use of natural resources in a sustainable manner will take place without causing any permanent damage to the environment. For that purpose the Government is in the process of taking organizational measures to guarantee financial and economic stability in Suriname, which is to be considered the most important condition to attract investors. It is also the opinion of my Government that a decisive and vital private sector is an essential condition for the development of the Surinamese economy; accordingly, this sector must be provided with as many facilities as possible. The Surinamese Government will strive for the private sector to also participate in the implementation of its developmental strategies, limiting its role in economic matters to regulations and control.

The Republic of Suriname and SELA can take pride in a prosperous cooperation and it is our intention to strengthen this relation. In recent years this organization, has proven to be an important instrument for member countries in their struggle to better adjust their national economies to regional and international development. Suriname is aware of the important task of SELA to improve the economic development of its members, and we are of the opinion that the achievements up till now have proven the organization's right to exist. I would therefore like to express my appreciation for the positive contribution of SELA in strengthening the economy of the members enabling them to better face the challenges at the eve of the Twenty-First Century.

I have indicated briefly the effects which the Surinamese economy has to deal with and how the Surinamese government intends to tackle them. Suriname is fortunate to be able to make use of the experiences of SELA, and in presenting solutions, when necessary, will not hesitate to appeal to you. After all, this organization is responsible for the development and integration of the economies of the Latin American countries which relate to our policy to further integrate into the region.

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*In recent years  
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economies to  
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development.*

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**CARICOM-MERCOSUR: The Benefits of Greater Integration**

*The Minister of Foreign Affairs of Uruguay portrays the present situation and prospects of his country, particularly its role as a member of MERCOSUR, while also pointing out the interest that his government has in launching closer links between this scheme and CARICOM.*

*El canciller de Uruguay reseña la situación actual y las perspectivas de su país, particularmente en lo que respecta a su papel dentro del MERCOSUR, a la par que expresa el interés de su gobierno en impulsar una mayor vinculación entre este esquema de integración y la Comunidad del Caribe (CARICOM).*

*Le ministre uruguayen des Affaires étrangères résume la situation actuelle et les perspectives de son pays, notamment en ce qui concerne le rôle de ce dernier au sein du MERCOSUR et fait part de l'intérêt de son gouvernement d'oeuvrer en faveur d'un raffermissement des liens entre cet organisme d'intégration et la Communauté des Caraïbes (CARICOM).*

*O ministro das relações exteriores do Uruguai expõe a situação atual e as perspectivas do seu país, particularmente no que se refere ao seu papel dentro do MERCOSUL, ao mesmo tempo que expressa o interesse do seu governo de impulsionar uma maior vinculação entre esse esquema de integração e a Comunidade do Caribe (CARICOM).*



# CARICOM-MERCOSUR: The Benefits of Greater Integration

→ **Alvaro Ramos Trigo**

*Minister of Foreign Affairs of the Eastern Republic of Uruguay*

*Lecture delivered at the Conference of CARICOM Heads of State and Government, held in Antigua and Barbuda, on February 21, 1997.*

Our presence here today is not a coincidence but an expression of will. We are aware that the relations between Uruguay and the Caribbean region in the past have been well below their potential. We feel that this is not only a diplomatic omission but also against our common interests.

Therefore, we are in Antigua today, and will be visiting a number of Caribbean countries in the coming days, as part of our government's strategy, aimed at strengthening Uruguay's relations with this region, which we consider a natural partner of Latin America.

Let me assure you that this is not a rhetorical statement. It reflects, rather, both a commitment and a goal that I have set myself as Foreign Minister, based on the firm belief that we face similar problems and challenges, and a shared understanding of the need for international cooperation and integration.

It should come as no surprise, then, that we are following a similar strategy for development; just as your countries have been doing since 1973 within CARICOM, Uruguay is now in the process of consolidating a customs union with Argentina, Brazil and Paraguay, within MERCOSUR.

It must be stressed that both integration schemes have essentially the same objectives: to improve the economies of our countries by enlarging their markets and by harmonizing their economic sectors, thus making them more efficient and competitive.

Within MERCOSUR, Uruguay, as the smallest country of the bloc, has stressed the advantages of wide and outward-looking integration, open to investment from, and trade with, all regions of the world. Therefore, we are fully committed, not only to the openness of MERCOSUR, but also to world-wide economic liberalization.

Furthermore, what is a remarkable aspect of MERCOSUR is

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*Within MERCOSUR, Uruguay, as the smallest country of the bloc, has stressed the advantages of wide and outward-looking integration, open to investment from, and trade with, all regions of the world.*

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*We welcome the positive dialogue that has recently been established between MERCOSUR and CARICOM in the context of the negotiations towards a Free Trade Area of the Americas.*

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that, besides eliminating tariffs between member countries, the bloc has also lowered its external barriers, opening the region to the rest of the world, and complying with World Trade Organization principles, particularly with regard to the avoidance of non-tariff barriers.

As a result, the consolidation of MERCOSUR has brought with it a substantial increase in trade with the rest of the world; exports from the bloc to non-member countries have been growing at a yearly rate of 11% since 1990, while imports from the rest of the world have been increasing 19% a year.

The non-discriminatory design of MERCOSUR is also reflected in the recent Association agreements of MERCOSUR with Chile, Bolivia and the European Union, and the comprehensive negotiations we are currently pursuing with the Andean Pact countries and Mexico. In our opinion, the next steps in this process should include the Caribbean and Central American countries.

For I must stress that –with Uruguay’s full support and encouragement– Mercosur has become a path of no return for all parties involved.

As such, we welcome the positive dialogue that has recently been established between MERCOSUR and CARICOM in the context of the negotiations towards a Free Trade Area of the Americas. We support greater coordination efforts towards the consolidation of integration between both blocs, in order to promote economic and social development and to acquire greater strength and bargaining power for hemispheric and international negotiations with third parties.

However, our firm intention is to complement these regional efforts with the development of closer ties between the Caribbean and Uruguay on a bilateral basis.

We base our commitment to this objective on the belief that, besides our historical differences and present day disparities, there is much common ground for progress, particularly considering the role of Uruguay within MERCOSUR.

With only 177,000 square kilometers of surface, and 3.2 million inhabitants, Uruguay faces, like the nations of CARICOM, the challenge to overcome the weaknesses that all small countries share; our mutual dilemmas should permit us to learn from each other in the political, economic and social fields.

Fortunately, we hold similar views on a significant number of subjects, based upon the common values of democracy, peace and human rights, and our commitment towards disarmament, a nuclear weapons ban and the principle of shared responsibility in the fight against the production, trafficking and consumption

of illicit drugs. Our common standpoints also include support for greater economic cooperation and integration within the Americas, and global trade liberalization, in the framework of sustainable human development.

But, as important as they are, these affinities cannot sustain, by themselves, a whole strategy for closer integration; potential economic partners must provide each other with business opportunities and that is why Uruguay has been involved in a process of economic reforms since the early seventies.

Today, with its strategic location within MERCOSUR and its sound economic policies, the country has the distinct advantage of being the gateway to this, one of the world's largest trading blocs, with a global G.D.P. of nearly one trillion dollars.

Our country is at the crossroads of the most important routes that connect Argentina with Brazil; its highly efficient communications and business infrastructures have made it the administrative center of MERCOSUR and the ideal commercial access point to and from the rest of the world.

Uruguay's liberal policies have enabled it to become one of the most dynamic and open economies in the region. This degree of openness is reflected in a legal framework that permits foreign companies to be established freely. Also unrestricted is the transfer of capital, the repatriation of profits and the contracting of services, labor and goods. There are no foreign exchange controls, no personal income tax, and banking secrecy has become an accepted asset of our financial markets. Off-shore operations are not taxed.

Moreover, in recent years, the country has undertaken an impressive process of reforms in order to address the daunting task of adjusting the economy to the rhythm of MERCOSUR, a market of nearly 200 million consumers.

The social security system, which had become a severe financial burden, has been reformed, extending the age of retirement for men and women, and at the same time, introducing a private system for pension fund management.

In a further effort to improve fiscal balances, Parliament has passed a major reform of the public sector, reducing the number of budget executing units, des-centralizing non-essential services, eliminating positions and, in general, creating a results-oriented environment.

Knowing that monopolies constitute a major obstacle for close integration, we have dismantled them: the insurance market, alcohol production, port services and housing credit monopolies were successfully opened up. In order to develop

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*Uruguay's liberal  
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more secure capital markets, new legislation on mutual funds and stock markets has recently been approved.

And last, but really not least, an ambitious reform process is well on its way to improving our already first rate education system, easing the transition to labor markets and consolidating continuing education programs.

This framework explains why investment has become such an important element in our economy's overall performance in the last ten years, when sectors like tourism, forestry and housing, among others, have seen rapid growth rates. And this, of course, explains why the Uruguayan economy has grown at an average annual rate of 3.5% in the same period.

We believe that this experience of structural reforms opens up a vast field for horizontal cooperation, by which I mean, a joint search for the expansion of our economic and social capabilities. Likewise, the exchange of scientific, technological and cultural human resources and information, as well as the field of environmental protection, provide an ample framework for a closer relationship among our countries.

Accordingly, I am pleased to inform you today of Uruguay's intentions to open an embassy in the Caribbean in the near future, as a basis for a more direct and permanent dialogue with this important region.

Meanwhile, we have given instructions to our Embassy to the Organization of American States in Washington DC, to strengthen its relations with the Caribbean Embassies in that capital, and we have recently appointed a high level diplomatic staff member specifically for that purpose.

We intend to pursue a process of permanent dialogue and consultations from there, and will organize periodic visits of relevant Ministers to this region, on a yearly basis, to ensure we gradually become partners in development.

Let me close by saying that it has been a privilege to have this opportunity to share with you our objectives and our dreams with regards to your region.

Your invitation has been greatly appreciated and valued. I am convinced it will contribute to the strengthening of our relations in the very near future.

You can rest assured of my dedication towards that goal.

**INTEGRATION BULLETIN**  
for Latin America and the Caribbean

SELA Permanent Secretariat 20' E. February 1997



**CARICOM studies strategies for the Twenty-first Century**

**EDITORIAL**

With the monthly publication of the Latin American and Caribbean Integration Bulletin, the Permanent Secretariat of SELA aims to assist in promoting a deeper awareness of the objectives, concrete actions, and principal achievements of the regional integration processes.

The Bulletin is published in both Spanish and English, and is available to all Member States of SELA. It is also available to interested parties outside the region.

The Bulletin is published by the Permanent Secretariat of SELA, which is located in the city of Havana, Cuba. It is published by the Permanent Secretariat of SELA, which is located in the city of Havana, Cuba.

All Member States of CARICOM are invited to participate in the 20th Anniversary of the Caribbean Community and Caribbean Integration Process. The Caribbean Community (CARICOM) was established in 1973 and has since then been a major force for regional integration in the Caribbean.

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**How CARICOM relates with the WTO**

As a result of the Caribbean Community's (CARICOM) efforts to integrate the Caribbean region, the Caribbean Community has been able to negotiate a series of trade agreements with the World Trade Organization (WTO).

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- Integration

*iNEW!*

**Integration Bulletin for Latin America and the Caribbean**

- With the monthly publication of the Latin American and Caribbean Integration Bulletin, the Permanent Secretariat of SELA aims to assist in promoting a deeper awareness of the objectives, concrete actions, and principal achievements of the regional integration processes.
- This Bulletin in fact forms part of the activities provided for in the «UNESCO-SELA Agreement on Communication for Latin American and the Caribbean Integration» and has funding from the International Programme for Communications Development (IPCD).
- This bulletin, published in both Spanish and English, will be transmitted via fax and Internet (<http://lanic.utexas.edu/~sela>), to a wide specter of users including government officials of the 27 SELA Member States, networks grouping parliamentarians, and academic centers, business associations, international organizations, and the media in general.

# Singapore: the Day After

→ Permanent Secretariat, SELA

## I. General Results of the Singapore Meeting

According to WTO's by-laws adopted in the Uruguay Round, the Organization's members should meet at the ministerial level every two years. As the Singapore meeting was the first one of this kind since the conclusion of the Round, in principle the effort should have been focused on the implementation of the commitments entered upon after seven years of multilateral trade negotiations. However, more attention was given to WTO's role in the «new» issues than to the follow-up and evaluation of the Round's results.

This does not mean that the Singapore meeting did not fulfill its objectives or that the «broadening» of the issues came as a surprise. While it is too early to evaluate the Round's results with any precision, since the majority of the agreements will be implemented from 5 to 10 years hence (in this respect, there will be more elements for evaluation in the next bi-annual meetings), the «new» issues which were not dealt with in the Round already formed part of the context and perhaps it would have been unrealistic to exclude them from the meeting.

However, before the next Ministerial Meeting in 1998, it would be advisable to reflect on the balance which should be maintained in WTO's agenda between traditional and new issues. We run the risk that, detrimental to compliance of the commitments entered upon, the new issues take center stage as they embody greater political and economic priorities for the industrialized countries than for the developing ones. In future, it will be necessary to prevent the bi-annual meetings from becoming regular «mini-Rounds», whose political content could threaten to erode WTO's credibility. The active participation of Latin America and the Caribbean both in WTO's routine activities in its role as overseer of the multilateral trade system and in the preparation of proposals for the handling of new issues could constitute a key element to achieve a situation of balance more in keeping with the region's interests.

As highlighted in the Meetings of Government Officials Re-

sponsible for Trade Policy convened by SELA, ALADI and ECLAC, a determining factor in the definition of SELA Member States' position in the WTO is that the region's trade agenda is not only multilateral but hemispheric and regional or subregional as well. Therefore, the treatment of new issues in the WTO can not be isolated from, for example, the treatment of those same issues in the hemispheric process or in integration schemes.

Traditionally, trade in textiles and apparel and agricultural products has been the most protected. After tough negotiations, the Uruguay Round managed to liberate it by deciding on the progressive dismantling of national quotas and producers' subsidies.

The Ministerial Declaration of Singapore includes very detailed recommendations on the fulfillment of commitments in the area of textiles and apparel, and renews commitments adopted by the Uruguay Round on agricultural products. For the moment, in industrialized countries, liberalization is taking place mainly in the least sensitive products. This gradual liberalization should be the object of careful monitoring by the exporting countries. It would be advisable to develop an information mechanism which would allow exporters to be informed on the new conditions for access to the industrialized markets as opportunities arise as a result of progressive liberalization. In addition to watching over liberalization and taking advantage of it, it is important to prepare for the negotiations on agricultural trade which are to be held in 1999.

## II. The Prospects of Negotiations on Services

The Ministerial Declaration of Singapore states that the results of the negotiations on services held to date «have been below expectations». It reiterates the determination to liberalize that trade «with the appropriate flexibility» for developing countries, in the negotiations under way as well as in those which will begin in the year 2000. See SELA, **Trade in Services: The Post-Uruguay Round Negotiations** (ALADI/ECLAC/SELA/III/RGPC/DT No. 3), Montevideo, Oct. 96.

The Declaration states that the objective is the most-favoured-nation treatment based on better access to markets and national treatment, and in this respect it establishes that:

- Negotiations on basic telecommunications will be concluded in February, 1997;
- Negotiations on financial services will be resumed in April, 1997;

- It is hoped to successfully conclude the negotiations on maritime transport in the next round of negotiations on trade in services;
- As regards professional services, it is hoped to complete the work on accountancy services towards the end of 1997, in order to draft multilateral disciplines and guidelines;
- Negotiations on safeguards should be completed by the end of 1997, with the support of additional analytical work on emergency safeguard measures, government procurement in services and subsidies.

Despite the political will expressed in Singapore, the future of negotiations on services will not be free of obstacles. To date, the position of the United States has been a determining factor in the paralysis of the negotiations on financial services (because the liberalization offers of the other countries are considered insufficient) and maritime transport (traditionally a very protected sector in many nations). Trade in professional services will be liberalized very punctually, due to its link with the issue of migrations, and prospects for the telecommunications sector are seemingly good.

To date, the participation of Latin American and Caribbean countries in the negotiations on services has been limited (only 10 countries in the region have presented offers). At the national level, the situation of the services sector must be examined in depth in order to define the negotiating position of countries, both individually or collectively.

### **III. Labor Regulations: Ethical Concerns and Commercial Interests**

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The paragraph relative to this issue was undoubtedly the most discussed in Singapore. Indeed, «social dumping» is an issue that unleashes controversies and pressures that are both ethical and economic and which, in the field of international trade, translates into proposals to sanction exports from countries accused of being lax with labour regulations and conditions. See SELA, **Social Dumping: Social Policy as Trade Policy** (SP/CL/XX.O/Di No. 4), Mexico, 30 May 1994.

The Declaration of Singapore specifies WTO's policy in this area, establishing boundaries and principles:

(i) The International Labour Organization (ILO) is the competent body in this area;

(ii) «The use of labour regulations for protectionist purposes» is rejected;



(iii) The questioning of «the comparative advantage of countries, particularly low-wage developing countries» is rejected; and

(iv) It was noted that the Secretariats of the WTO and the ILO will continue their existing collaboration.

Despite the clarity achieved in Singapore, and in view of the labour regulations/trade links' record (which dates from 1919, when the ILO was created), it can be assumed that the issue has not been solved definitively and that some industrialized countries (especially, the United States of America and France) will continue to press for its introduction in the negotiations' agenda or as a condition for unilateral economic concessions such as GSP, multilateral loans, development aid, etc.

#### **IV. Investments and Competition: In Search of Multilateral Standardization**

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As regards investments and competition, what was agreed in Singapore is limited compared with many countries' expectations (in the first place the European Union and the OECD, but also several developing countries) due to opposition, especially from India and Malaysia. See Strategic Issues Number 24: «The Treatment of Foreign Investment: Towards International Regulations?» (July, 1996) and Number 27: «The Discreet Charm of Competition» (December, 1996).

The Declaration refers to the commitments adopted in the Uruguay Round on these issues, and decides, without prejudging future negotiations, to establish two working groups: one «to examine the relationship between trade and investment», and another «to study issues raised by Members relating to the interaction between trade and competition policy, including anti-competitive practices, in order to identify those areas that may merit further consideration in the WTO framework.» This decision will not bar the OECD from its plans to conclude, in 1997, the formulation of a Multilateral Investment Agreement (MIF), open to adherence by non-OECD members.

Countries opposed to negotiating investments within the WTO put forth two prevailing arguments: (i) The need to preserve each country's sovereignty in the definition of the treatment of foreign investment; and (ii) that bilateral or multilateral investment agreements are not factors that determine a country's attractiveness for foreign investment. Concerning the issue of competition, several industrialized countries wish to avoid «distortions» generated by differing or even non-existent national legislations.

## V. The Dilemma Stirred by Regionalism

This politically-sensitive issue, virtually absent from discussions in Singapore, arouses conflicting interests. On the one hand, efforts must focus on insuring that integration schemes do not become protectionist «fortresses»; on the other hand, the members of the several schemes wish to avoid having an entity monitoring their joint policies.

The contradiction is evinced in the conciliatory tone, on this issue, of the Declaration of Singapore which encourages the facilitation of «mutually supportive processes for the liberalization of global and regional trade». The difficulty lies in defining WTO's role in this context and the criteria for the linkage of regionalism with multilateralism (see **Strategic Issues No. 18** «Regionalism and Multilateralism: Forced Relations», November, 1995). In the medium term, the dispute between the advocates of multilateralism and the upholders of regionalism will be one of the major issues to be dealt with by the WTO.

## VI. Treatment of Developing Countries

As was the case with GATT, the participation of developing countries in world trade creates the need for the WTO to embody provisions and implementation terms adapted to the asymmetries that exist between developed and developing countries.

In this respect, the Declaration of Singapore points out:

- That the problem exists of «marginalization of lesser-developed countries and the potential marginalization of certain developing countries»;
- That the WTO Agreement embodies provisions conferring «differential and more favourable treatment for developing countries, including special attention to the particular situation of less developed countries»;
- That the commitments undertaken by developing countries are «new and significant» and acknowledges «the range and complexity of the efforts that they are making to comply with them»;
- That «the availability of technical assistance must be improved»;
- That the agricultural reform programme could have «possible negative effects on least -developed countries and net food-importing developing countries».

The Declaration likewise refers to the adoption of an Action Plan for less developed countries. Other paragraphs mention

developing countries' needs regarding trade in textiles, services, regional agreements.

## VII. The Latin American-Caribbean Agenda within the WTO

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As preparations for the Singapore Meeting and the work of the WTO point out, countries of the region need to focus their technical and political efforts on improving their **capacity to propose and ,consequently, to negotiate both individually and collectively**, within the framework of the Organization, particularly as regards the following substantive and institutional issues:

### **Development of proposals for:**

- The implementation of GATS' Article IV (concerning the participation of developing countries in trade in services);
- The treatment of investment and competition issues (taking account of UNCTAD's activity in this area);
- The follow-up of agricultural commitments and support to food-importing developing countries;
- The rules applicable to regional agreements.

**Broadening and strengthenin of technical assistance provided by the WTO**, in coordination with other international and regional organizations;

**Transparency of decision-making processes** and the equal participation of all members in the WTO;

**Follow-up of WTO cooperation with the Bretton Woods Institutions (IMF and World Bank) and UNCTAD**, so as to consider needs of developing countries are duly considered.

# Gone With the Wind? Special Treatment for the Developing Countries

→ **SELA, Permanent Secretariat**

## I. Asymmetries: A Problem as Old as International Relations

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The differences between nations as regards their size, population, wealth, culture and development have always been determinant in international relations. At the present time, with the recognition of the juridical equality within the States, the matter can be raised in different terms from those of hegemony and protection which predominated in the past. Nevertheless, the differences –asymmetries– still exist and are acknowledged in the activities of the international community.

The distinction between developed and developing economies, and any differences between economies that fall in the latter group have been taken into account in the international cooperation efforts of the past decades and are present in the design of new international norms and types of association between States.

The objective of achieving a harmonious global economy encounters an obstacle in the profound differences in the degree of development and possibilities of growth of regions and countries. In this context, the establishment of norms commonly applied to nations faced with different conditions from the structural point of view could lead to situations of inequity.

In practice, the way in which the aforementioned differences have been dealt with has differed depending on the area of activity or the group of countries to be considered, and no consensus has been reached as regards the scope and significance of the asymmetries between countries. The lack of a general frame of reference for the treatment of asymmetries has led to the application of unilateral and changing criteria, and sometimes to the establishment of conditions which could be considered arbitrary. Owing to the lack of clarity regarding the

subject, the positions have moved between extremes. According to one of them, special and differential treatment for the developing countries should be eliminated, according to the other, it should be general, automatic, permanent and non-reciprocal.

The generalized tariff reduction resulting from the Uruguay Round, from the integration agreements and unilateral actions of the developing countries, has shifted the focus of attention from international economic relations to matters which transcend the customs domain and affect policies which were previously considered as the exclusive jurisdiction of each nation. Monetary and fiscal policies, policies related to investment, intellectual property policies or those aimed at preserving the environment are all examples of subjects included in the international agenda in which the problem of asymmetries still remains to be considered.

## **II. The Asymmetries in Multilateral Relations**

The contrast between juridical equality and economic diversity among the states is reflected in the decision-making processes of international organizations. In the United Nations and the World Trade Organization each country has the right to one vote. In the Bretton Woods financial institutions (International Monetary Fund and World Bank) the right to vote is proportionate to the capital contributed. In the activities of each of said organizations, however, criteria are used to differentiate between developed and developing countries.

The principle of special and differential treatment and the concept of developing countries itself was realized institutionally and operatively with the creation of UNCTAD in 1964. Among the instruments designed within the framework of UNCTAD to deal with the asymmetries, the Generalized System of Preferences (GSP), in 1968, is worthy of note, according to which the industrialized countries grant non-reciprocal trade preferences to the developing countries. However it has been applied in a partial, temporary and conditional fashion. At the onset in GATT, and now in the World Trade Organization (WTO), there is «a differential and more favourable treatment for the developing countries», which consists basically of the granting of more extensive time frames for the adoption of general rules and the establishment of some exceptions for less developed countries (with a per capita income of less than US\$1,000) or very small countries. This principle was incorporated in the Agreement establishing the WTO and stems from two ministerial decisions

of the Uruguay Round, one related to measures in favour of less developed countries and the other related to measures regarding the possible negative effects of the reform programme in less developed countries and in developing countries net importers of foodstuffs.

The financing organizations do not acknowledge juridical difference between developed and developing countries. The World Bank, however, only grants financial support to those members who «cannot obtain loans in favourable conditions within prevailing market conditions». In practice, this is currently equivalent to the developing countries and the so-called «economies in transition». In another sense, it means that when a member manages to obtain access to the capital markets in favourable conditions it may be «graduated». That is to say, it loses access to the bank's resources. On the other hand, the International Development Association (IDA), affiliate of the World Bank which grants financing in concessional terms, lends exclusively to countries with lesser incomes. Also in the case of the IDA a country can be «graduated» when its income increases. The World Bank distinguishes statistically between «high income» countries (39); «medium income» countries (111); and «low income» countries (per capita GNP up to US\$725). The regional banks follow similar procedures. The International Monetary Fund makes no juridical differentiation between developing and developed countries. Nevertheless, in the past twenty years it has not granted financial assistance to any developed country. For statistical purposes, the IMF groups the economies in industrial (23); developing (132); and in transition (23). In the treatment of the external debt, more favourable conditions are also established for the «highly indebted» countries.

### **III. The Asymmetriess in Relations Between Nations: Some Examples**

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Agreements by groups of countries reflect a wide variety of situations. Traditionally, the regional economic integration agreements were entered into between countries with relatively similar degrees of development. Hence, special and differential treatment was an exception destined to compensate some unusual circumstances.

– This was the case, for example, of the European Common Market, the Constitutive Agreement of which, in 1957, established between the six (6) founding members, financial mecha-

nisms and special programmes taking such asymmetries into account, particularly so for the less developed countries, e.g. the Southern region of Italy. The Maastricht Treaty of the European Union continues to evidence the asymmetries and corresponding support mechanisms. Something similar has been witnessed in the integration systems among countries of our region.

– The process of decolonization initiated after the second World War led to the establishment of special conditions for the former colonies or areas of influence. The most important aspect in this respect is the Lomé Convention. This provides access, exempt from tariffs, to the markets of the European Union for products coming from African, Caribbean and Pacific States, in addition to providing technical and industrial assistance and a special guarantee for these countries' exports. The Lomé Convention IV is currently in force and will supposedly expire in 1999.

– The Special Generalized System of Preferences of the European Union, intended to support the struggle against the production of and trade in drugs, is an extension of the aforementioned GSP to the Andean countries. Under this scheme, the preferences of the GSP have been extended to a list of export products of Colombia, Peru, Bolivia and Ecuador since 1991, and to Venezuela since 1995. A limited list of products was granted to the Central American countries.

– In the United States' relation with the Latin American and Caribbean countries the most important programme has been the «Caribbean Basin Initiative (CBI), whereby the U.S.A. grants exemption from tariffs to a wide universe of products from almost all the countries of the Caribbean Basin. It entered into force in 1984 and in 1990 was declared indefinite. It is a programme which has had a different level of impact on the beneficiary nations of Central America and the Caribbean. Canada, by means of the CARIBCAN system, has also established non-reciprocal preferential mechanisms for trade with the Caribbean countries, complemented by mechanisms for the promotion of investments and systems of cooperation.

– The North American Free Trade Agreement (NAFTA) does not contain any specific provisions regarding special and differential treatment. Nevertheless, the agreement prescribes a different treatment between the parties as a result of the process of negotiation.

#### IV. The Asymmetries in Latin America and the Caribbean

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The Montevideo Treaty of 1960, which created the Latin American Free Trade Association (LAFTA), contemplated special treatment for the «relatively less developed countries with insufficient market». The Montevideo Treaty of 1980, which replaced the previous one and created the Latin American Integration Association (ALADI), distinguishes for the same purpose, «countries of medium development» (Colombia, Chile, Peru, Uruguay and Venezuela) and «relatively less developed countries» (Bolivia, Ecuador and Paraguay) from the rest of the countries (Argentina, Brazil and Mexico), establishing a system which differentiates between three levels of development.

In the Common Central American Market, the first Treaty of which was signed in 1960, no specific reference is made to the concept of special and differential treatment depending on the level of development. Nevertheless, mechanisms have often been introduced for the purpose of gradually reducing the differences between the relatively more and relatively less developed countries. In particular, special regimes have been established for Nicaragua and Honduras.

The Cartagena Agreement of 1969, today the Andean Community, was conceived from the point of view of the differences of relative development between the members of LAFTA: this agreement grouped countries of medium development and relatively less developed countries in order to make the benefits of the integration which it was hoped would be achieved within the framework of LAFTA more equitable. A preferential regime was contemplated for the relatively less developed countries on trade and industrial development. Although the elimination of the Programme of Joint Industrial Development and other modifications have eroded the preferences granted to the relatively less developed countries, the general principle of special and differential treatment is one of the conceptual bases of the Andean Community.

Likewise, the Caribbean Community (CARICOM) incorporates the concept of special and differential treatment depending on the level of development and applies it in its operational mechanisms. The CARICOM treaty establishes three categories of countries and contemplates special measures to avoid the concentration of economic benefits in the relatively more advanced countries. Special attention is paid to the members of the Organization of Eastern Caribbean States (OECS).

In MERCOSUR no explicit reference is made to the concept



of special and differential treatment. Nevertheless, Paraguay and Uruguay (the two smaller economies of the group) are granted special conditions.

Just as in MERCOSUR, numerous free trade treaties and recent trade agreements between countries of the region have implicitly recognized the matter of asymmetries in the content of their negotiations, particularly in the trade liberalization programmes.

Systems of non-reciprocal generalized preference have also been established for relatively less developed countries, such as the 1980's Partial Scope Agreements of ALADI member countries of ALADI with Central American Countries and, more recently, the CARICOM Agreements with Venezuela and Colombia. Furthermore, there are systems of financial cooperation between relatively more developed countries and smaller economies, such as the San José Pact, whereby Mexico and Venezuela guarantee the supply of petroleum and allocate a percentage of the respective bills to the financing of trade and to economic development projects of the Central American and Caribbean countries.

#### **IV. The Asymmetries in the Hemisphere**

One of the 11 Working Parties created to prepare negotiations on the Free Trade Area of the Americas (FTAA) deals with the «Smaller Economies», a novel term different from the categories based on the levels of development already established among the Latin American and Caribbean countries.

The objective of the mandate entrusted by the Ministers to that Working Party is the identification and evaluation of: the factors which affect the smaller economies' participation in the FTAA; the means of facilitating this participation; and the support that IDB, ECLAC and the OAS and other pertinent institutions can grant in that process.

To date, the Working Party on Smaller Economies has held six meetings, which, in addition to the representatives of the 34 countries parties to the FTAA, have been attended by representatives of the «Tripartite Commission» (IDB, ECLAC and OAS). In the last three meetings of the Working Group, SELA's Permanent Secretariat has been asked to support its work and to prepare analyses of the «smaller economies'» technical cooperation needs.

Despite the progress made by this Working Party, there has been an obvious difficulty in defining what «small economies» are, which countries must be included in that definition, and how

to reflect in the FTAA the considerable differences in the levels of development and in the size of the economies recognized by the Presidents of the hemisphere.

## **V. The Asymmetries and the Latin American and Caribbean Development Agenda**

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Everybody is aware of the fact that the subject of asymmetries is definitely the subject of Development, an issue related to the structural deficits of less industrialized countries.

In this respect, the problems of the less developed countries are not limited to the discussion of the graduality of the time frames for the fulfilment of multilateral or regional commitments, and the trade preferences granted by the developed countries to a more or less long list of export products of the less developed countries, regardless of the importance of both subjects.

The subject needs to be taken a step further in terms of the queries to be answered. These would include, for example:

What differences exist at present regarding degrees of development and growth potential and how can they be overcome?

Within the present context of globalization, in what categories could countries be classified to account for the differences between them? Do the existing differences require special and differential treatment in accordance with the categories established?

Must the special and differential treatment be limited to support in the adaptation to a development model (which would be the responsibility of the country concerned), or must it include active policies whereby industrialized countries directly promote development?

Is it necessary to establish «graduation» policies for those countries which pass from one category to another?

Is it advisable to use the same categories for different sectors of activity (trade, finance, investments, technical assistance)? or, on the contrary, would not special and differential treatment be more adequate if applied by sector of activity or taking into account the overall effect of the different sectors on the asymmetric situation of each economy?

To what extent can a multilateral, hemispheric, regional or group of countries' action nullify differences which have been recognized previously? In the process of creating a FTAA, what will be the role assigned to the treatment of asymmetries or of the «smaller economies»? How does the non-recognition of asymmetries affect the development of international relations?

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