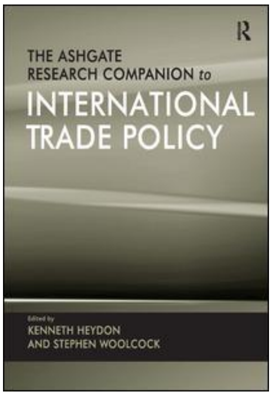


# The Ashgate Research Companion To International Trade Policy

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## Trade Policymaking in Latin America

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# Trade Policymaking in Latin America

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## Introduction

This chapter focuses on the evolution of trade policy in Latin America in the last two decades. The first section briefly describes the region's trade policies since the early twentieth century. The second section examines some recent trends in the region's trade. The third section discusses Latin America's economic integration efforts, including through negotiations with extra-regional partners. The fourth section looks at Latin American countries' participation in the multilateral trading system and the fifth section concludes.

## Historical Overview

At the turn of the twentieth century, and up to the Great Depression, Latin America was highly integrated into the world economy. The region's economies were relatively open and derived most of their export income from primary products (such as wheat, meat, nitrate, rubber, sugar and coffee), while the industrial sector was little developed. The devastating effects of the Great Depression, compounded by the disruption of supplies during the Second World War, encouraged industrialization policies across the region. These included high tariff and non-tariff barriers to imports and the provision of credit by the state to selected industries. This strategy of import-substitution industrialization (ISI) prevailed in most of the region until the 1980s.

[1] The opinions are the personal responsibility of the authors and do not represent the views or positions of the United Nations Economic Commission for Latin America and the Caribbean (ECLAC) and the World Trade Organization (WTO), respectively.

As Latin American countries were transitioning from predominantly agrarian to mostly urban societies, the emerging working and middle classes – made up largely of industrial workers and state employees – supported the new ISI strategy and prevailed over the interests of the region's traditional exporting sectors, agriculture and mining. ISI was also underpinned by proposals from the United Nations (UN) Economic Commission for Latin America and the Caribbean (ECLAC), created in 1948.

The ISI strategy was instrumental in the creation of several basic industries such as steel and cement, as well as in absorbing the workforce that left the farms for the cities. However, it hampered the absorption of new technologies and knowledge embodied in imports, thus impacting negatively on overall efficiency and productivity levels. It also led to the development of numerous uncompetitive industries across the region, which could nevertheless survive in the absence of international competition. Overvalued exchange rates were common and resulted in a severe anti-export bias, which was compounded by policies selectively channelling credit to industry to the detriment of agriculture and mining. As will be seen in the third section of this chapter, some attempts were made at overcoming these limitations through economic integration.

By the mid-1970s, most Latin American economies had restrictive trade policies, characterized by high average tariffs, a large variance in tariff levels and numerous non-tariff barriers, complemented by price controls and multiple exchange rate regimes. Partly as a result of the inefficiencies created by ISI, Latin America failed to achieve sustained growth and significantly reduce income inequality and poverty (Corbo 2008).

The debt crisis that hit the region in 1982 prompted the abandonment of ISI.[2] Faced with a severe reversal of capital inflows and the loss of access to international private capital markets, many Latin American countries underwent dramatic falls in gross domestic product (GDP), coupled with currency and financial crises. For some, international financial institutions like the International Monetary Fund (IMF) and the World Bank became the main sources of capital. These institutions thus acquired increased leverage to promote market-led policy reforms that went beyond restoring macroeconomic stability.

Along with the privatization of state-owned enterprises and a deregulation of economic activity, the reduction of trade barriers was a key component of the reforms of the 1980s. The reduction of the anti-export bias of ISI was made more pressing by the need to increase export income to service the region's high foreign debt. Table 25.1 illustrates, for the seven largest Latin American economies, the deep reduction of import tariffs that has taken place since the mid-1980s across the region.

[2] The exception is Chile, which abandoned ISI in the mid-1970s, under the military dictatorship that took power in 1973 (Herreros 2009).

**Table 25.1 Simple average most-favoured-nation applied tariffs in selected LAC countries (in percentages)**

| | 1985–1989 | 1990–1994 | 1995–1999 | 2000–2004 | 2005–2008 |
|---|---|---|---|---|---|
| Argentina | 27.5 | 13.9 | 14.7 | 14.0 | 10.7 |
| Brazil | 45.8 | 21.0 | 15.1 | 14.7 | 12.5 |
| Chile | 18.0 | 11.8 | 10.7 | 7.0 | 6.0 |
| Colombia | 29.4 | 16.6 | 12.7 | 12.2 | 11.2 |
| Mexico | 16.7 | 12.8 | 14.1 | 16.1 | 7.9 |
| Peru | 45.8 | 17.2 | 13.9 | 11.0 | 7.5 |
| Venezuela, BR | 31.1 | 15.8 | 13.0 | 13.0 | 12.3 |

*Source*: Data on Trade and Import Barriers, World Bank.

As a result of these reforms, including those aimed at attracting foreign direct investment (FDI), Latin American economies generally became more open. This is especially the case in Chile, Peru and Mexico that have gone furthest in trade liberalization (see Table 25.2).

**Table 25.2 Merchandise trade (exports plus imports) as a percentage of GDP in selected LAC countries**

| | 1980 | 1985 | 1990 | 1995 | 2000 | 2005 | 2008 |
|---|---|---|---|---|---|---|---|
| Argentina | 24 | 14 | 12 | 16 | 18 | 38 | 39 |
| Brazil | 19 | 18 | 12 | 13 | 18 | 22 | 24 |
| Chile | 38 | 42 | 51 | 45 | 50 | 63 | 77 |
| Colombia | 26 | 22 | 31 | 26 | 26 | 29 | 32 |
| Mexico | 21 | 25 | 32 | 54 | 60 | 53 | 57 |
| Peru | 31 | 25 | 22 | 25 | 27 | 38 | 48 |
| Venezuela, BR | 46 | 39 | 53 | 42 | 42 | 55 | 46 |

*Source*: World Development Indicators, World Bank.

The bulk of trade liberalization in Latin America has been unilateral. Reciprocal trade agreements have become an important factor since the 1990s, first with a renewed momentum in regional integration along with the results of the Uruguay Round of multilateral trade negotiations and later as several countries engaged in preferential trade agreements (PTAs) with extra-regional partners.[3]

[3] PTAs form a very broad category in terms of their product, sectoral and thematic coverage as well as the depth of the commitments undertaken by their members. They include Free Trade Agreements (FTAs) as well as more limited agreements. Henceforth the FTA acronym will be used to refer only to agreements specifically described as such by their signatories.

During the past decade, there has been an erosion of support for trade liberalization in some Latin American countries. Most notably, in 2004 Cuba and Venezuela formed the Bolivarian Alliance for the Peoples of Our America (ALBA), adopting an openly critical stance towards capitalism in general, including free trade. Subsequently, other countries joined ALBA: Bolivia in 2006; Nicaragua in 2007; Dominica in 2008; Antigua and Barbuda in 2009; Ecuador in 2009; and St. Vincent and the Grenadines in 2009. ALBA is not a 'classic' trade agreement as it is largely based on voluntary cooperative undertakings by its members, such as barter of oil for agricultural products or even medical services.

Disenchantment with trade liberalization seems to be part of a broader erosion of support for market-based reforms. This has happened despite the fact that between 2003 and 2008 the region's GDP grew at an average 5 per cent a year, its strongest performance since the 1970s, along with a reduction in poverty (from 44 per cent to 33 per cent) and unemployment (from 11 per cent to 7.4 per cent) (Barcena 2010). It has been argued that an important reason for this is that large segments of the region's population did not feel included in the benefits from growth (Rojas-Suarez 2010). In fact, despite its recent good performance, Latin America continues to be one of the world's most unequal regions (Barcena 2010). In contrast, successful reform in other countries has translated into political support allowing for further liberalization, whether unilateral or based on reciprocal arrangements, as shown by Mexico, the Central American countries, Colombia, Peru and Chile.

## Latin America's Trade at a Glance

The past decade has seen the share of Latin America and the Caribbean (LAC) in world merchandise trade register a small decrease, whereas its share in world trade in commercial services fell more sharply. This stands in contrast with the significant gains made by developing countries as a whole and especially by developing Asia during the same period. In the case of merchandise trade, Latin America's weak performance is explained almost exclusively by the substantial drop in the share in world trade of Mexico, the region's largest exporter. This loss was compensated by the gains made by Brazil and all other major economies in the region. In the case of trade in commercial services, Mexico's share also fell, but so did those of other major Latin American economies (although not Brazil's) (see Table 25.3).

The stagnation of Latin America's share in world merchandise exports mirrors the loss of dynamism of the region's exports during the past decade when compared to the previous one. Consistent with the results in Table 25.3, this trend is reversed – and the region's export performance shows an improvement – if Mexico is excluded (see Figure 25.1)

While LAC exports of primary products (measured by value) grew much faster in the past decade as compared to the 1990s, the opposite happened with the region's exports of manufactures. This result is heavily influenced by both the high prices registered by several commodities during most of the past decade and the

**Table 25.3 Shares of developing economies, regions and selected countries in world trade, 2000 and 2008 (in percentages)**

| | Share in world merchandise trade | | | | Share in world commercial services trade | | | |
|---|---|---|---|---|---|---|---|---|
| | Exports | | Imports | | Exports | | Imports | |
| | 2000 | 2008 | 2000 | 2008 | 2000 | 2008 | 2000 | 2008 |
| Developing economies | 30.6 | 38.1 | 27.8 | 34.1 | 24.5 | 27.3 | 27.6 | 31.6 |
| LAC | 5.8 | 5.7 | 5.9 | 5.7 | 4.1 | 3.4 | 4.9 | 4.1 |
| *Brazil* | 0.9 | 1.3 | 0.9 | 1.1 | 0.6 | 0.8 | 1.1 | 1.3 |
| *Mexico* | 2.7 | 1.9 | 2.8 | 2.0 | 0.9 | 0.5 | 1.2 | 0.7 |
| Developing Europe | 0.6 | 1.1 | 1.1 | 1.8 | 1.7 | 1.6 | 0.7 | 0.8 |
| Africa | 2.4 | 3.5 | 2.0 | 2.9 | 2.1 | 2.3 | 2.6 | 3.5 |
| Middle East | 4.3 | 6.5 | 2.5 | 3.6 | 2.3 | 2.6 | 3.4 | 4.8 |
| Developing Asia[a] | 17.6 | 21.3 | 16.3 | 20.2 | 14.3 | 17.4 | 16.0 | 18.4 |

*Note*: [a] Excluding re-exports and imports for re-export by Hong Kong, China.
*Source*: WTO (2010).

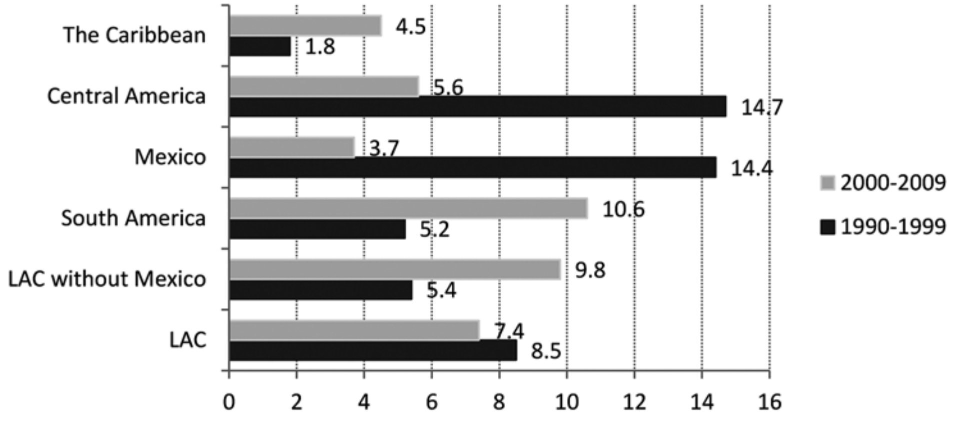


**Figure 25.1 Evolution of total LAC merchandise exports by value, 1990–1999 and 2000–2009 (average annual growth rates)**
*Source*: ECLAC (2010).

dramatic fall (of almost 90 per cent) in the average rate of expansion of Mexican manufacturing exports, a phenomenon that also affected Central America (see Table 25.4).

**Table 25.4 LAC: Evolution of exports of primary products and manufactures by value, 1990–1999 and 2000–2009 (average annual growth rates)**

| | Primary products | | Manufactures | |
|---|---|---|---|---|
| | 1990–1999 | 2000–2009 | 1990–1999 | 2000–2009 |
| LAC | 2.6 | 11.4 | 14.7 | 5.3 |
| South America | 2.7 | 13.0 | 6.4 | 8.3 |
| Mexico | 1.8 | 6.3 | 27.3 | 2.9 |
| Central America | 6.4 | 4.9 | 19.8 | 7.8 |
| The Caribbean | -1.4 | 12.2 | 4.8 | 2.9 |

*Source*: ECLAC (2010).

As a result of the divergent paths followed by LAC exports of primary products and manufactures, the share of the former category in the region's total exports by value increased by more than ten percentage points during the last decade, reaching nearly 40 per cent. If resource-based manufactures are added, their combined share in total LAC exports approaches 60 per cent (see Table 25.5).

**Table 25.5 LAC: Breakdown of exports by value according to technological intensity, 1981–1982 to 2008–2009 (in percentages of total exports)**

| | 1981–1982 | 1985–1986 | 1991–1992 | 1995–1996 | 1998–1999 | 2001–2002 | 2005–2006 | 2008–2009 |
|---|---|---|---|---|---|---|---|---|
| Primary products | 51.5 | 48.4 | 39.5 | 32.5 | 26.7 | 27.6 | 35.1 | 38.8 |
| Resource-based manufactures | 25.5 | 25.0 | 23.5 | 21.7 | 18.4 | 16.6 | 19.3 | 20.2 |
| Low-technology manufactures | 8.2 | 9.2 | 11.5 | 12.0 | 12.9 | 12.2 | 9.3 | 7.6 |
| Medium-technology manufactures | 11.6 | 13.6 | 20.1 | 24.4 | 26.7 | 26.8 | 23.9 | 21.5 |
| High-technology manufactures | 3.2 | 3.8 | 5.4 | 9.4 | 15.3 | 16.8 | 12.4 | 11.9 |

*Note*: Based on Sanjaya Lall's classification and 3-digit Standard International Trade Classification (SITC) categories.
*Source*: ECLAC (2010).

The clear shift in LAC exports towards primary products is consistent with the more dynamic performance of South America as compared with Mexico and Central America. Both elements are in turn directly related with a third major shift in LAC's trade: the emergence of Asia – and China in particular – as a key trade partner. As Table 25.6 shows, during the last decade, Asia's share in LAC exports tripled from 5 per cent to 15 per cent, whereas its share in the region's imports more than doubled from 11 per cent to 25 per cent. These gains have been mostly at the expense of the United States, which nevertheless continues to be the region's main individual trade partner.[4]

Asia's economic dynamism has resulted in sustained demand and high prices for commodities such as copper, iron ore, crude oil, wheat and soybeans, which are mostly exported by South American countries. On the other hand, the loss of dynamism of Mexican and Central American exports of manufactures is largely explained by increased competition from Asia (especially from China) in those countries' main market, the United States. The erosion of Mexico's and Central America's competitive position in the United States has occurred despite the trade preferences that both enjoy in that market as a result of FTAs.

**Table 25.6 Share of main partners in LAC's trade, 2000 and 2006–2009 (in percentages)**

| **Share of partners in LAC exports** | | | | | |
|---|---|---|---|---|---|
| | **2000** | **2006** | **2007** | **2008** | **2009** |
| LAC | 19.0 | 16.4 | 17.2 | 18.4 | 17.2 |
| Asia | 5.0 | 9.7 | 11.3 | 11.8 | 14.5 |
| China | 1.1 | 3.4 | 4.6 | 5.0 | 6.9 |
| US | 61.0 | 47.6 | 44.0 | 41.4 | 39.8 |
| European Union | 11.8 | 12.8 | 13.8 | 13.7 | 12.8 |
| **Share of partners in LAC imports** | | | | | |
| | **2000** | **2006** | **2007** | **2008** | **2009** |
| LAC | 15.1 | 18.9 | 19.1 | 18.9 | 18.8 |
| Asia | 10.9 | 22.2 | 23.0 | 23.5 | 24.9 |
| China | 1.8 | 8.4 | 9.6 | 10.4 | 11.8 |
| US | 55.0 | 32.4 | 30.3 | 29.0 | 29.2 |
| European Union | 12.1 | 12.8 | 13.3 | 13.5 | 13.8 |

*Source*: ECLAC (2010).

While Latin America's trade with regions such as Asia and Europe is mostly inter-industrial (that is, the region exports natural resources and imports manufactures), its intra-regional trade has a much larger intra-industry component, as the region's countries export manufactures to each other. However, intra-regional trade accounts for just 18 per cent of total Latin American trade, a much smaller share

[4] This trend was reinforced by the recent global financial crisis, as LAC exports to the United States and the European Union fell much more dramatically in 2009 than those to Asia.

than in Asia and Europe, thus limiting its potential to upgrade the technological content and otherwise increase the value-added of the region's exports.[5]

## Latin America's Main Trade Integration Efforts

### The Latin American Free Trade Association

Latin American integration has, since independence, been an aspiration that has taken many shapes and forms. Besides the political rhetoric, since the 1960s the shortcomings of ISI provided the rationale to seek enlarged – yet still protected – markets through regional integration. At the time it was thought that freer trade within the region, coupled with high tariffs vis-à-vis third parties, would facilitate the achievement of economies of scale, thus overcoming the restriction imposed by the small size of most LAC economies.

In 1960, seven Latin American countries signed the Treaty of Montevideo establishing the Latin American Free Trade Association (LAFTA) with the long-term aim of becoming a common market.[6] Initially, a free trade area was to be established over 12 years through annual tariff cuts. This plan never went beyond the first instalment because of the resistance of sensitive sectors to external competition and the wide disparities in development levels among LAFTA members. However, LAFTA allowed some increase in the amount of intra-regional trade covered by preferences, while providing a temporary legal cover under the General Agreement on Tariffs and Trade (GATT).[7]

In 1980 LAFTA was replaced by the Latin American Integration Association (LAIA).[8] LAIA is essentially an umbrella agreement that provides a GATT cover to bilateral or plurilateral agreements among its members.[9] It also provides for limited regional preferences for some goods which have been largely superseded

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5 Even among Central American countries, which are the most commercially integrated, the intra-regional trade ratio does not exceed 25 per cent.

6 LAFTA members were Argentina, Brazil, Chile, Mexico, Paraguay, Peru and Uruguay. By 1970, Bolivia, Ecuador, Colombia and Venezuela had also joined.

7 As an increasing number of Latin American countries acceded to the GATT, it became more necessary to justify their departures from the most-favoured-nation (MFN) obligation enshrined in GATT's Article I. LAFTA provided such justification by way of the exception to MFN granted to free trade areas and customs unions in GATT's Article XXIV.

8 The legal instrument establishing LAIA is the Treaty of Montevideo 1980. LAIA is better known by its Spanish acronym ALADI.

9 In 1979 the GATT contracting parties approved a decision, the 'Enabling Clause' (a Brazilian initiative), whereby developing countries may conclude preferential agreements that do not meet the requirements of Article XXIV.

by bilateral agreements. It has therefore not played a significant role in LAC efforts towards the liberalization of intra-regional trade over the last two decades.

## The Andean Community (AC)

By the end of the 1960s the LAFTA was all but abandoned, as reflected by the creation in 1969 of the AC. Its founding members were Bolivia, Chile, Colombia and Ecuador, while Venezuela joined in 1973. Originally the AC was intended to become an economic union beyond the confines of trade policy. For example, it included sectoral industrial policies allocating specific lines of production to member states, as well as a common – but restrictive – foreign investment and intellectual property regime. Chile withdrew from the AC in 1976, following the military coup that resulted in a shift in its economic policies towards a market-driven approach (Herreros 2009).

The AC languished during the remainder of the 1970s and through the 1980s, while its member states experienced the severe effects of Latin America's 'lost decade' following the outbreak of the debt crisis in 1982. In the early 1990s, the AC was revamped, against the backdrop of the market-led reforms they had started implementing since the late 1980s. A free trade area for goods was established in 1993 and a common external tariff (CET) in 1995.[10] In 2006 a free trade area in services was attained, providing for national treatment and market access in most sectors.

The trade policy stances of AC members have diverged in recent years. While Colombia and Peru have maintained open trade policies and individually or jointly pursued FTAs with extra-regional partners, Bolivia and Ecuador have joined ALBA. Both countries have also enacted new constitutions that restrict their ability to include issues such as trade in services, investment, intellectual property and government procurement in trade negotiations.[11] Following Colombia and Peru's decisions to negotiate FTAs with the United States, Venezuela withdrew from the AC in 2006 and applied to join the Common Market of the South (MERCOSUR).[12] Against this background, AC members have focused their cooperation efforts on issues other than trade liberalization, thus straying from the goal of forming a customs union with a common trade policy.

[10] Peru did not participate in the CET, while the other members enjoyed some exceptions. The CET did not prevent individual governments from concluding their own bilateral agreements with other Latin American countries.

[11] In December 2009 Bolivia denounced its FTA with Mexico, which had been in force since 1995, due to the incompatibility between its new constitution and the agreement's chapters on services, investment, intellectual property and government procurement. The FTA was replaced by a new agreement covering only trade in goods.

[12] At the time of writing, Venezuela's accession to MERCOSUR still had to be approved by Paraguay's Congress.

## The Common Market of the South (MERCOSUR)

MERCOSUR was established in 1991 by Argentina, Brazil, Paraguay and Uruguay. Among its goals is the free circulation of goods, services and factors of production, along with the establishment of a CET and a common trade policy. By 1995 both duty-free trade among MERCOSUR members and the CET were achieved. However, tariffs remain for intra-MERCOSUR trade in the automotive sector and sugar. Moreover, trade remedies and non-tariff barriers such as non-automatic import licenses continue to be used, especially between Argentina and Brazil. As to the CET and common trade policy, they are somewhat undermined by national exceptions and the conclusion by individual MERCOSUR members of bilateral FTAs with other Latin American countries (for example the Uruguay–Mexico FTA). Some progress has been made towards liberalization of trade in services, a process foreseen to be completed in 2014. On government procurement, a protocol was agreed in 2004 providing for most-favoured-nation (MFN) and national treatment. However, as of March 2012 it is not yet in force. Trade disputes within MERCOSUR are often subject to diplomatic negotiations (with outcomes not necessarily based on the legal obligations binding the parties) rather than being settled through MERCOSUR's dispute settlement mechanisms.

MERCOSUR has concluded PTAs with all other South American countries. However, it has mostly refrained from seeking negotiations with its main extra-regional partners, except the European Union (EU).[13] This has largely been influenced by the strong defensive sensitivities of Argentina and – to a lesser extent – Brazil in the industrial sector. MERCOSUR has privileged trade agreements with developing partners such as India, Egypt and the South African Customs Union, or small economies like Israel. However, some of those agreements are limited in so far as tariffs are reduced – not eliminated – for a limited number of products and issues such as services and government procurement are not covered. It is often argued that these agreements have little commercial interest and respond mostly to foreign policy considerations (Marconini 2009).

## The Central American Common Market (CACM)

Founded in 1960 by Costa Rica, El Salvador, Guatemala, Honduras and Nicaragua, the CACM has been successful in achieving free trade among its members and eliminating other barriers to trade. Most notably, Central American countries plus the Dominican Republic were able to negotiate a comprehensive FTA with the United States in 2005, the DR-CAFTA, covering trade in goods, services,

[13] Negotiations towards an Association Agreement between MERCOSUR and the EU (including an FTA) were launched in 1999 and suspended in 2004, mostly due to the EU's agricultural sensitivities and those of MERCOSUR in industry. Negotiations resumed in June 2010 and are still ongoing.

investment and several other areas.[14] This agreement also applies between the Central American countries, thus superseding the corresponding provisions of the CACM.

In 2010 the CACM, this time along with Panama, also completed successfully negotiations towards an association agreement with the EU, which includes a comprehensive FTA. CACM members have equally been able to negotiate individually FTAs with other countries such as Canada, Chile, China, Mexico and Singapore.

## Regionwide Initiatives

The early 1990s mark a turning point in trade policy and integration in Latin America. Democratic regimes coincided with the adoption of market-led economic policies across the region. This alignment of politics and economic policies resulted in a renewed interest in strengthening trade links between Latin American countries. It is within this context that MERCOSUR was created in 1991 and a free trade area established within the AC in 1993.

In 1991 Mexico and Chile concluded a free trade agreement (FTA), with very few products excluded. This was the first real FTA in the region, and it set a model for future negotiations by these and other Latin American countries. More importantly, it quickly led to agreements with and among other countries in the region. Exporters of countries not party to any such agreements pushed their governments to also conclude bilateral or plurilateral accords and thus avoid losing markets.

As a result of the dynamics set in motion in the early 1990s, today trade among Latin American countries is conducted mainly through a vast web of bilateral and plurilateral agreements (Table 25.7). While these pacts reflect an interest in freeing up intra-regional trade, the absence of a unified single market imposes significant transaction costs, including those derived from different regulatory regimes and rules of origin. Several initiatives to achieve convergence among these different agreements and integration schemes have been tried, with little success so far

The most ambitious economic integration project so far in the Americas was the US initiative to establish the Free Trade Area of the Americas (FTAA), encompassing North, Central and South America as well as the Caribbean.[15] The preparatory process that began in 1993 and concluded with the launching of negotiations in 1998 suggested a consensus on the FTAA's scope and objectives. However, this consensus unravelled when new governments in some countries (Brazil, Venezuela and Argentina, among others) challenged the inclusion of issues such as investment, services and intellectual property. In addition, the United

14 CAFTA entered into force for its members between 2006 and 2009 depending on the completion of their domestic approval procedures.

15 There were 34 participating countries in total. Within the western hemisphere, only Cuba was excluded (on political grounds).

**Table 25.7 PTAs in force, under negotiation or announced among Latin American countries (as of November 2010)**

| | Andean Community | MERCOSUR | CACM | Chile | Mexico | Panama |
|---|---|---|---|---|---|---|
| Andean Community | | MERCOSUR–Bolivia PTA<br>MERCOSUR–Peru PTA<br>MERCOSUR–Colombia–Ecuador–Venezuela PTA | Colombia–Northern Triangle PTA[a]<br>Peru–Central America–Panama FTA (currently in negotiations) | Chile–Bolivia PTA<br>Chile–Ecuador PTA<br>Chile–Colombia FTA<br>Chile–Peru FTA | Bolivia–Mexico PTA<br>Colombia–Mexico FTA<br>Peru–Mexico FTA (currently in negotiations) | Colombia–Panama FTA (currently in negotiations) |
| MERCOSUR | | | | MERCOSUR–Chile PTA<br>Venezuela–Chile PTA | MERCOSUR–Mexico Framework Agreement<br>MERCOSUR–Mexico automotive agreement<br>Uruguay–Mexico FTA<br>Brazil–Mexico economic integration agreement (negotiations announced) | |
| CACM | | | | Central America–Chile FTA | Costa Rica–Mexico FTA<br>Nicaragua–Mexico FTA<br>Northern Triangle–Mexico FTA | Central America–Panama FTA |
| Chile | | | | | Chile–Mexico FTA | Chile–Panama FTA |
| Mexico | | | | | | |

*Note*: [a] The term Northern Triangle refers to El Salvador, Guatemala and Honduras.
*Source*: Authors, based on Organization of American States, Foreign Trade Information System. Available at: www.sice.oas.org.

States was unwilling to negotiate away agricultural subsidies – except in the WTO – or anti–dumping measures, posing additional difficulties to reach an agreement. The negotiations were eventually terminated in 2005, after which the United States began a strategy of bilateral negotiations with individual Latin American countries.

Following the failure of the FTAA, the project to create a South American Free Trade Area comprising the AC, MERCOSUR and Chile was launched in 2005 within the context of the recently created South American Community of Nations. However, it was subsequently abandoned, and today it is not in the agenda of the Community's successor, the Union of South American Nations (UNASUR). This reflects the wide divergences that exist among the region's governments in terms of their approaches to development, including the role of trade liberalization.

Notwithstanding the above, there has been some progress on convergence at the subregional level. For example, since 2009 Mexico and the CACM have been working towards unifying the three FTAs currently linking them (Table 25.7). This offers a good potential to further integrate these six economies, reducing transaction costs and fostering the formation of value chains spanning several countries. Work has also been undertaken since 2008 towards convergence of the FTAs that link Mexico, Central America, Panama, Colombia, Ecuador, Peru and Chile, within the so-called Latin American Pacific Basin Initiative (LAPBI). This effort aims, among others, at harmonizing rules of origin and verification procedures, and at allowing cumulation of origin among the 11 LAPBI members.

In November 2010 the governments of Brazil and Mexico announced their decision to start negotiations towards a comprehensive 'economic integration strategic agreement', covering not only tariffs but also services, government procurement, investment and intellectual property, among other topics. This negotiation may have substantial implications for the whole Latin American integration process, as it involves the region's two largest economies and its two largest exporters of goods and services. Moreover, if successful it could lead to a Mexico–MERCOSUR FTA, which in turn could pave the way for the gradual creation of a Latin American free trade area.

## The Negotiations with Extra-regional Partners

Mexico pioneered Latin America's efforts to develop preferential trade ties with extra-regional partners when it proposed to the United States to begin negotiations for what would become the NAFTA. Chile followed suit in 1997 with its FTA with Canada.[16]

During the past decade the majority of Latin American countries have followed Chile's and Mexico's steps and engaged in FTA negotiations with extra-regional

[16] Chile was invited to join NAFTA in 1994, but negotiations failed when the Clinton Administration was unable to obtain Fast Track Authority from Congress. Instead, Canada and Chile negotiated a bilateral FTA which, at the time, was viewed as an interim arrangement until Chile became a NAFTA partner.

partners. Most of them have been conducted with the United States and the EU, Latin America's most traditional foreign markets. However, in recent years, some countries have also entered FTA negotiations with Asia–Pacific partners such as Japan, China, India and Korea. The countries that have been most active in this effort are Chile, Peru, Mexico, Colombia and Costa Rica (see Table 25.8).

**Table 25.8 FTAs between LAC and integration schemes and selected extra-regional partners (as of September 2010)**

| | USA | EU | Japan | China | Korea | India |
|---|---|---|---|---|---|---|
| MERCOSUR[a] | … | Currently in negotiations | … | … | … | Partial scope agreement[b] |
| Central American Common Market | FTA (CAFTA-DR) | FTA negotiations concluded | … | … | … | … |
| Costa Rica | | | … | FTA signed | … | … |
| Colombia | FTA signed in 2006, not yet in force | FTA negotiations concluded | … | … | Currently in negotiations | … |
| Peru[c] | FTA | FTA negotiations concluded | FTA negotiations concluded | FTA | FTA negotiations concluded | … |
| Chile[d] | FTA | FTA | FTA | FTA | FTA | Partial scope agreement[b] |
| Mexico[e] | FTA (NAFTA) | FTA | FTA | … | FTA negotiations suspended in 2008 | … |

*Note:* [a] It also has an FTA in force with Israel and one signed with Egypt; [b] A partial scope agreement is one that covers trade in goods only, with a limited product coverage and in which tariffs are reduced rather than eliminated (see Chapter 22); [c] It also has FTAs in force with Canada and Singapore, and one signed with the European Free Trade Association (EFTA); [d] It also has FTAs in force with Australia, Canada, EFTA and Brunei Darussalam, New Zealand and Singapore (the latter three in the context of the Trans-Pacific Strategic Economic Partnership Agreement), plus FTAs signed with Turkey and Malaysia and ongoing FTA negotiations with Vietnam; [e] It also has FTAs in force with Canada (NAFTA), EFTA and Israel.

*Source*: Authors, based on Organization of American States, Foreign Trade Information System. Available at: www.sice.oas.org.

## Latin America in the GATT/WTO

Until the Uruguay Round (1986–1994) participation in the GATT had not resulted in much liberalization on the part of Latin American countries, having been rather passive participants in tariff negotiations.[17] As the region's economies opened up unilaterally, the multilateral trading system became more important to both lock-in trade policy reform and pursue offensive interests such as disciplines and liberalization of agricultural trade.

In the Uruguay Round most participating Latin American countries bound all their tariffs but usually at levels substantially higher than the actual applied rates (Table 25.9).[18] The commitments negotiated by Latin American countries under the General Agreement on Trade in Services (GATS) were few and limited to binding totally or partially the status quo, very much in line with what other countries did.

There has been no unified Latin American stance in the ongoing Doha Round negotiations. Indeed, not even the region's main integration schemes have articulated common positions. On the contrary, differences between members of the same integration scheme have not been infrequent. This has been the case, for example, with differences between Costa Rica and the other Central American countries on agricultural market access (with the former adopting a much more offensive position than the latter) or among Andean Community members (replicating the same split which has become evident in preferential negotiations). In sum, negotiating positions in the WTO tend to be largely national and replicate Latin American countries' overall trade policy stances.

Despite being all developing economies, LAC countries pursue widely different objectives in terms of special and differential treatment, with some attaching much more importance to this concept than others. The one interest common to the entire region is reducing as much as possible the trade-distorting agricultural subsidies provided by developed countries.

As to coalitional activity, it is mostly issue-specific and based on common interest, rather than along regional lines. Thus Latin American countries participate with developed countries and with developing countries from other regions in issue-specific groups such as the Cairns Group, G20, G33, Friends of Fish, Friends of Anti-dumping Negotiations, etc.

Brazil is by far the most influential Latin American country in the Doha Round, being part – together with the United States, EU, China and India – of the core group of members in the negotiations, the so-called G5. This leading role reflects the vast size and strong dynamism of the Brazilian market, but has also been underpinned, among other factors, by the proven technical expertise of its negotiators and by the

17 This is a reflection not only of the ISI strategy but also of the fact that until the Uruguay Round tariff negotiations were carried out on the basis of request and offer, and thus only the main suppliers of a product got involved, reducing Latin American participation to very few tariff lines.

18 Chile had been the first GATT signatory to bind 100 per cent of tariffs (at 35 per cent) in the Tokyo Round (1973–1979) even though its applied rate at the time was 10 per cent.

**Table 25.9 Latin American countries: tariff profiles (2009)**

| Country | Average bound rate (%) (1) | Average applied rate (%) (2) | Binding overhang (%) (1)–(2) | Binding coverage (%) |
|---|---|---|---|---|
| Argentina | 31.9 | 12.6 | 19.3 | 100.0 |
| Bolivia, Plurinational State | 40.0 | 10.3 | 29.7 | 100.0 |
| Brazil | 31.4 | 13.6 | 17.8 | 100.0 |
| Chile | 25.1 | 6.0 | 19.1 | 100.0 |
| Colombia | 42.8 | 12.5 | 30.3 | 100.0 |
| Costa Rica | 42.9 | 5.4 | 37.5 | 100.0 |
| Cuba | 21.3 | 10.7 | 10.6 | 30.9 |
| Dominican Republic[a] | 34.0 | 7.1 | 26.9 | 100.0 |
| Ecuador | 21.8 | 11.2 | 10.6 | 100.0 |
| El Salvador | 36.6 | 5.9 | 30.7 | 100.0 |
| Guatemala | 41.2 | 5.6 | 35.6 | 100.0 |
| Honduras | 31.8 | 5.6 | 26.2 | 100.0 |
| Mexico[b] | 36.1 | 11.5 | 24.6 | 100.0 |
| Nicaragua | 40.7 | 5.6 | 35.1 | 100.0 |
| Panama | 23.5 | 7.1 | 16.4 | 100.0 |
| Paraguay | 33.5 | 10.3 | 23.2 | 100.0 |
| Peru | 29.3 | 5.5 | 23.8 | 100.0 |
| Uruguay | 31.6 | 10.5 | 21.1 | 100.0 |
| Venezuela, Bolivarian Rep. | 36.5 | 12.5 | 24.0 | 100.0 |

*Note:* [a] Corresponds to 2008; [b] In January 2009 Mexico started a programme of unilateral tariff reduction, to be implemented over five years. Tariffs will be lowered for practically all non-agricultural items whose applied MFN tariff is not already zero.
*Source*: World Trade Organization, World Tariff Profiles 2010.

clear political commitment Brazil has made to the Doha Round as its main concern in terms of trade negotiations. Proof of this is Brazil's leading role – along with India – in the creation of the G20 agricultural coalition of developing countries.

Several Latin American countries have made extensive use of the dispute settlement system of the WTO, scoring important victories in landmark cases. Among these are the complaint by Central American countries, plus Ecuador and Colombia, against the EU's import regime for bananas; and Brazil's victories on cotton subsidies versus the United States and on sugar against the EU.

## Conclusion

Today Latin American countries are much more open and integrated into the world economy than they were 30 or even 20 years ago. However, this general assessment overlooks important differences. At the risk of oversimplifying a regional landscape that is full of nuances, today there appear to be three main approaches to trade within Latin America. Those countries with coasts on the Pacific Ocean (with the exception of Ecuador) tend to show the most open trade policies and actively seek to improve their links with the global economy, including through the negotiation of PTAs with their main partners within and outside the region. At the other end of the spectrum are those countries within ALBA. MERCOSUR members fall somewhere in between, although with important variations among themselves.

The erosion of support for trade liberalization in some countries has not resulted in massive tariff increases, even in the face of the recent world economic crisis. By and large, Latin American countries have not used the large space to raise tariffs allowed by their ceiling bindings at the WTO. Indeed, most countries in the region have not increased trade barriers at all, regardless of their public discourse on trade. Nevertheless, in recent years some countries have made use of non-tariff barriers such as non-automatic import licenses, minimum custom values, exchange controls, dual exchange rate regimes for foreign trade, an increased use of managed trade and outright import bans.

In the coming years, the role of trade policy in Latin American countries' overall development strategies will surely differ from the one it had at the start of trade reforms in the 1980s. Despite some backtracking in recent years, Latin America has achieved trade opening levels roughly equivalent to those of East and South East Asia. Although further reduction of trade barriers could have a positive impact on the region's overall competitiveness, the gains are likely to be smaller than those reaped as a result of the reforms of the 1980s and 1990s.

Trade agreements, particularly those concluded within the region and with other developing countries, will need to be reinforced in several aspects. First and foremost is the need to abide by the obligations established in these international treaties. There is often, among countries in the region, too much tolerance when a party disregards or does not properly enforce the commitments entered into in trade agreements. This creates problems for governments when resisting domestic protectionist pressures. Moreover, legal security and predictability are key elements of good governance. Second, trade agreements need to provide better disciplines and transparency for trade in services, investment and government procurement. A third issue that needs to be tackled at both national and regional levels is competition policy, so as to prevent uncompetitive behaviour by private firms in an environment characterized by fewer barriers to trade and foreign investment.

A recurrent concern is how to improve Latin America's export performance. South American countries are still largely dependent on exports of natural resources. Although they have benefitted in recent years from a strong Asian demand for commodities, this export structure has generally resulted in insufficient value addition, weak links with the rest of the economy and vulnerability to sudden declines in commodity prices. Moreover, several of the extractive industries in which South America has become specialized (for example mining) are capital-intensive, with little employment creation, and also pose important environmental challenges. An additional problem is that the large foreign currency inflows associated with high commodity prices push towards real appreciation of local currencies, hurting the international competitiveness of other export and import-competing sectors and thus reinforcing commodity dependence.

For their part, the Central American countries and Mexico, which show a larger component of industrial products in their export basket, face a different problem: the loss of share in the US market due to Asian competition in low and medium-technology manufactures. In the Mexican case, this is compounded by its excessive export dependence on the US market.

Brazil appears as a relative exception to the region's trade predicament. Besides being one of the world's main commodity exporters, it has displaced Mexico as the region's main exporter of commercial services. It is also a successful exporter of manufactures in some medium and high-technology segments, most notably aircraft. This is the result of a number of factors, including a higher spending on research and development (as a percentage of GDP) than the Latin American average, an abundant provision of credit from the powerful state-owned national development bank (BNDES) and large FDI inflows. The sheer size of the Brazilian market (with almost double the population of Mexico) has most likely also played a part, by enabling Brazilian companies to develop scale and learning economies that can later be exploited in international markets. However, because of the particularities of the Brazilian case, it is unclear that other LAC countries could upgrade their productive capacities simply by following its example.

Against this background, it seems that Latin America's main challenges lie in areas other than trade policy understood in a narrow sense. The region does not sufficiently participate in the global value chains that today dominate international trade, and where it does is generally in their least sophisticated segments. Addressing this requires increasing the value and knowledge content of the region's exports, including those of natural resources (or based on them). Over the coming years it will also be important to reduce the vulnerability of LAC exports to climate change-related trade measures in third markets, by reducing their 'carbon footprint'. Addressing these challenges will require changes in a wide range of policies such as those dealing with innovation, science and technology, education and training, environmental management and the attraction of FDI. The nature of those adjustments lies beyond the scope of this chapter.

Notwithstanding the above, there is at least one area where trade policy should play a very important role in increasing the region's international competitiveness: the promotion of intra-regional trade. Progress towards the establishment of a unified economic space along the lines of the EU's Single Market would greatly contribute to raising Latin America's low levels of intra-regional trade, in turn fostering the development of intra-regional value chains and increasing the value content of the region's exports. While such an ambitious goal does not appear feasible in the short term due to political differences, especially in South America, it should nonetheless remain as a top priority for the region's governments in the coming years.

Looking in perspective at the last two decades, what Latin America has achieved in terms of increased openness to trade and investment represents a good basis to continue building a trade architecture that underpins better and deeper integration across the region. Incremental progress towards that end looks much more promising than the very ambitious – yet ultimately unsuccessful – integration initiatives the region has often embarked upon in the past.

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