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# Options for a Hemispheric Trade Order

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## SYMPOSIUM

OPTIONS FOR A HEMISPHERIC TRADE  
ORDER†

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## I. INTRODUCTION

The constellation of trade arrangements has its own bright stars, red dwarfs, and black holes. The hugely successful European Community is a brilliant star; the problematic Uruguay Round at this writing is a red dwarf;<sup>1</sup> the U.S.-Mexico talks represents a young star, while the erstwhile Latin American Free Trade Area is a black hole. The question ahead is whether a shining new galaxy

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1. See *infra* note 8 and accompanying text for a discussion of the Uruguay Round.

can be created for the Western Hemisphere.

In Parts One and Two, this Article reviews the Enterprise for the Americas Initiative<sup>2</sup> and its Latin American response. Parts Three and Four examine the main trade arrangements among countries in the Western Hemisphere, and Parts Five and Six conclude this Article by speculating on the configuration of a new Western Hemispheric trade order.

These conclusions are straightforward. Past attempts at forging free trade agreements within Latin America failed because they did not meet certain obvious preconditions. These preconditions are now coming into place for selected Latin American countries, and the Enterprise Initiative makes possible trade agreements with the United States. The result, in the first instance, will be a hub-and-spoke architecture dealing with the most obvious border barriers.<sup>3</sup> Eventually, this will be superseded by a "hub-spokes-rim" architecture, and the agreements will be extended to reach behind the border barriers to domestic economic issues. As companion instruments to the trade agreements, social pacts will likely be devised, calling for better enforcement of existing health, safety, and environmental standards and requiring a gradual improvement in standards over time.

The timing of trade agreements will largely depend on external events. Unless and until the crisis in Iraq is successfully resolved, President Bush will have neither the time nor the negotiating clout — neither with foreign nations nor with the U.S. Congress — to mount major new initiatives. Beyond that, the Uruguay Round must come to a conclusion, and the proposed U.S.-Mexico Free Trade Agreement must be worked out,<sup>4</sup> before far reaching trade talks are possible with other Latin American nations.

## II. ENTERPRISE FOR THE AMERICAS INITIATIVE

On June 27, 1990, President Bush offered proposals for closer economic relations within the Western Hemisphere with his Enter-

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2. See *infra* note 5 and accompanying text for a discussion of President Bush's Enterprise for the Americas Initiative.

3. See R. WONNACOTT, U.S. HUB-AND-SPOKE BILATERALS AND THE MULTILATERAL TRADING SYSTEM (C.D. Howe Inst. Commentary No. 23, 1990).

4. For further discussion on the proposed U.S.-Mexico Free Trade Agreement, see *infra* text accompanying notes 89-94.

prise for the Americas Initiative (Initiative).<sup>5</sup> The Initiative is broadly designed to support democratic governments and market-oriented reforms through a program that will promote investment, help reduce debt, and cut trade barriers.

In the investment arena, the Initiative seeks wholesale reform. According to Treasury Undersecretary David Mulford, only two or three Latin American and Caribbean nations currently maintain what the United States would consider an open investment regime.<sup>6</sup> In the debt arena, the Initiative basically combines self-help with a modest amount of U.S. assistance.

The trade arena is the centerpiece of the entire Initiative, with the ultimate goal being the creation of a Western Hemisphere free trade zone. Assuming this goal is widely accepted in the United States and Latin America, the key issues are how long it will take to reach it and the tactics by which it will be achieved.<sup>7</sup>

#### A. Trade

At this juncture, the Enterprise Initiative is short on trade specifics, but its general goals are clear. First, the Initiative seeks worldwide trade integration under the presumption that the Uruguay Round will succeed.<sup>8</sup> The successful completion of the talks would likely increase the "integration of the Latin nations into the global trading system."<sup>9</sup> According to the Bush Administration, the Initiative "is not an attempt by the United States to set up a regional trade bloc, but it is an effort to lower trade barriers in the region to the benefit of all trading nations."<sup>10</sup> Within the framework of the Uruguay Round, the United States has offered to assist

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5. For the text of the President's statement, see *President Bush's Address on "Enterprise for the Americas" Proposal and Accompanying White House Fact Sheet, Released June 27, 1990 (Text)*, Daily Rep. for Execs. (BNA) No. 125, at M-1 (June 28, 1990) [hereinafter Bush Initiative].

6. Inside U.S. Trade, Oct. 5, 1990, at 2.

7. Crigler & Lande, *Toward a Hemispheric Strategic Economic Alliance: Consideration by the Council of the Americas*, Manchester Trade, Feb. 14, 1990; and *Trade Policy Proposals Under the Enterprise for the Americas Initiative*, Manchester Trade, Aug. 20, 1990.

8. The Uruguay Round describes a series of talks, designed to negotiate agreements on tariffs to services and intellectual property, which began in 1986 in Uruguay between member countries of the General Agreement on Tariffs and Trade (GATT). See *Draft Final Act Embodying the Results of the Uruguay Round of Multilateral Trade Negotiations*, MTN.TNC/W/35/Rev. 1, Dec. 3, 1990.

9. See Bush Initiative, *supra* note 5, at M-1.

10. Inside U.S. Trade, *supra* note 6, at 2.

Latin American countries in addressing specific trade issues, and has pledged support for tariff cuts on products of vital interest to Latin American exporters.

Second, the Initiative seeks to open up a free trade zone throughout the entire Western Hemisphere "stretching from the port of Anchorage to Tierra del Fuego."<sup>11</sup> State Department policymakers have declared "that intra-regional trade barriers must fall and trade volume among Latin American countries and the Caribbean must jump before any country in the hemisphere other than Mexico and Chile will be ready to enter free trade talks with the United States."<sup>12</sup> As a first step to this goal, however, the United States has begun to negotiate bilateral framework agreements on trade and investment in piecemeal fashion with a number of countries in the region. Seven countries — Bolivia, Chile, Colombia, Costa Rica, Ecuador, Honduras, and Mexico — already had signed such agreements by the end of 1990;<sup>13</sup> talks are proceeding with Venezuela and the Southern Cone countries (Argentina, Brazil, Paraguay, and Uruguay); and the Andean Pact<sup>14</sup> might well negotiate a framework agreement with the United States in 1992. The existing free trade agreement (FTA) with Canada<sup>15</sup> and the agreement now under discussion with Mexico<sup>16</sup> presumably will serve as models for substantive content when the framework agreements are succeeded by full-fledged trade agreements.

### B. Investment

The Enterprise Initiative seeks to "help Latin American countries to compete for capital by reforming broad economic policies and specific regulatory systems."<sup>17</sup> To promote these objectives, the Initiative contains proposals for two new programs to be administered by the Inter-American Development Bank (IDB).

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11. Bush Initiative, *supra* note 5, at M-1.

12. Inside U.S. Trade, Nov. 30, 1990, at 3.

13. *Bush Hails Possibility of Hemispheric Free Trade Zone During South America Trip*, Int'l Trade Rep. (BNA), No. 48, at 1324 (Dec. 5, 1990).

14. Agreement on Andean Subregional Integration, May 26, 1969, Colombia, 8 I.L.M. 910 (1969) [hereinafter Cartagena Agreement]. For more discussion on the Andean Pact, see *infra* text accompanying notes 42-60.

15. Free Trade Agreement, Dec. 22, 1987, United States-Canada, 27 I.L.M. 281 (1988) [hereinafter U.S.-Canada FTA].

16. Understanding Regarding Trade and Investment Facilitation Talks, Oct. 3, 1989, United States-Mexico, 29 I.L.M. 36 (1990) [hereinafter U.S.-Mexico FTA Proposal].

17. Bush Initiative, *supra* note 5.

First, the Initiative proposes that the IDB create a new investment sectoral loan program to provide both technical advice and financial support for privatization efforts and liberalization of investment regimes — possibly coordinated with the World Bank. This program would enhance both IDB and World Bank sectoral lending facilities.

Second, the administration has proposed a multilateral investment fund to which the United States, the European Community, and Japan would each contribute \$100 million annually over the next five years beginning in 1992. Additional contributions from other countries could boost the fund total to \$2 billion.<sup>18</sup> The proposed multilateral investment fund would provide annual grants tied to investment reforms, support efforts to privatize government-owned industries, and finance worker training, education, and health programs. The fund is designed to create a climate favorable to investment in Latin America, thereby attracting increased amounts of private capital, including Latin flight capital now residing in the United States and Europe, and to promote investment reforms in the region.

### C. *External Debt*

Overall, Latin America's debt situation is still precarious.<sup>19</sup> The external debt outstanding at the end of 1990 totalled \$423 billion.<sup>20</sup> Most countries in the region have not kept current on their debt service and consequently ran up \$12 billion in arrears in 1990.<sup>21</sup>

To deal with these debt issues, President Bush's "Enterprise for the Americas Initiative Act of 1990" (EAI Bill)<sup>22</sup> proposes that

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18. This sum is comparatively small relative to the task at hand. The Initiative's diagnosis thus appears to be that policy reform is more important than cash. To quote the President, "[P]rosperity in our hemisphere depends on trade — not aid." *Id.*

19. For most Latin countries, sharply higher oil prices in the wake of the Persian Gulf crisis have curtailed the prospects for economic growth, at least through the first half of 1991. Mexico and Venezuela are big winners (perhaps together by \$18 billion at an annual rate), but other countries are losers (Brazil by nearly \$4 billion at an annual rate). See Tucker, *Big Winners and Many Losers Watch the Price of Oil*, Overseas Development Council, Nov. 20, 1990; see also *World Economy: Global Growth Slowing in 1991; Recession Can Be Avoided*, Daily Rep. for Execs., (BNA), No. 9, at S-27 (Jan. 14, 1991).

20. U.N. ECONOMIC COMMISSION FOR LATIN AMERICA AND THE CARIBBEAN, PRELIMINARY OVERVIEW OF THE ECONOMY OF LATIN AMERICA AND THE CARIBBEAN (1990).

21. *Id.*

22. H.R. 5855, 101st Cong., 2d Sess., 136 CONG. REC. 16,827.

an Enterprise for the Americas Facility (Facility) be administered by the Treasury Department in order to address debt reduction, investment reform, and environmental protection. The Facility will support debt reduction programs for countries that meet certain eligibility requirements set out in the EAI Bill that are designed to promote a favorable investment climate. Each country should: 1) establish an International Monetary Fund (IMF) standby arrangement or an arrangement under the structural adjustment facility, and institute an IMF monitored program or its equivalent in exceptional circumstances; 2) receive structural or sectoral loans from the World Bank or the International Development Association; 3) either establish major investment reforms in conjunction with an IDB loan or implement an open investment regime; and 4) negotiate a satisfactory financing program with commercial banks, including debt and debt service relief if appropriate.<sup>23</sup>

When all these conditions are met, the United States would provide new payment terms for outstanding debt "extended under the Foreign Assistance Act of 1961 and credits extended pursuant to the Agricultural Trade Development and Assistance Act of 1954 (PL 480 Aid)."<sup>24</sup> The agency whose loans or credits are affected will exchange — at the direction of the Facility — new obligations for obligations outstanding as of January 1, 1990. The principal and interest would be payable to the United States in U.S. dollars.

However, under the EAI Bill, interest at concessional rates may be paid in local currency if the eligible country enters into a framework agreement establishing an Environmental Fund. This Fund would be jointly administered by the respective country and the U.S. government to support local environmental projects. In the absence of an environmental agreement, interest would be paid in U.S. dollars into a special account.<sup>25</sup> The Initiative also provides for the sale, reduction, or cancellation of Export-Import Bank (Ex-Imbank) loans and Commodity Credit Corporation (CCC) loans, provided the eligible country confirms that debt relief assistance will be used to carry out debt-for-equity or debt-for-nature swaps.

As President Bush noted in his Enterprise for the Americas Initiative, Latin American countries currently owe \$12 billion to

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23. *Id.*

24. *Id.*

25. The EAI Bill is ambiguous as to whether the account might be conditionally earmarked for the paying country. *Id.*



the U.S. government.<sup>26</sup> The Overseas Development Council has calculated that the total extent of the U.S. debt initiative would, at maximum, amount to a savings in interest payments of about \$400 million annually, if the total \$12 billion were forgiven.<sup>27</sup> If other countries of the Paris Club join the plan, this amount might rise to \$1.6 to \$2.3 billion — a fraction of the current annual net resource transfer out of Latin America but significant in relation to what the Brady Plan<sup>28</sup> has delivered so far.<sup>29</sup>

### III. LATIN AMERICAN RESPONSE

The Bush Initiative was warmly received throughout Latin America and the Caribbean. This reception reflects a fundamental change of economic and political thinking in Latin America. Economic policies of import-substitution and regulated markets are rapidly being replaced by policies of freer trade, hospitality to foreign investment, and extensive deregulation.

For example, Bolivia, Mexico, and Jamaica have dramatically and unilaterally liberalized their trade restrictions; Colombia and Costa Rica have made significant progress; and Argentina and Venezuela have recently initiated radical liberalization programs.<sup>30</sup> Even Peru and Brazil have now taken first steps to open their economies under new leaders elected in 1990. As a result of these reforms, more and more countries in the region have become able and willing to join the General Agreement on Tariffs and Trade (GATT).<sup>31</sup>

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26. See Bush Initiative, *supra* note 5.

27. *Hearings on H.R. 5855 Before the Subcomm. on International Development, Finance, Trade and Monetary Policy of the House Comm. on Banking, Finance and Urban Affairs*, 101st Cong., 2d Sess. (1990) (statement of Richard Feinberg, Exec. V.P. and Director of Studies, Overseas Development Council) [hereinafter *Hearings*].

28. The Brady Plan, named for Treasury Secretary Nicholas Brady and put forth by him in a March 1989 speech, describes a proposal to relieve Latin American debt through certain debt-for-equity exchanges. Under these programs the U.S. purchases a country's foreign debt at a discount price, the debt is then converted into local currency by that country's central bank, and the currency is then invested back into that country's local enterprises.

29. *Hearings*, *supra* note 27.

30. These trade policies complemented domestic stabilization policies in the second half of the 1980s that sought to dampen inflationary pressures by cutting excessive government expenditures and to increase efficiency in production through privatization and deregulation. See Williamson, *The Progress of Policy Reform in Latin America*, INST. FOR INT'L ECON., at 24-26 (Washington, D.C., Jan. 1990).

31. General Agreement on Tariffs and Trade, *opened for signature* Oct. 30, 1947, 61 Stat. (5), (6), T.I.A.S. No. 1700, 55 U.N.T.S. 188 (entered into force Jan. 1, 1948). The cur-

The Initiative is viewed as a chance to reap the benefits of recent economic reforms by expanding trade and improving economic efficiency. The Initiative is further seen as a welcome change of U.S. policy from an emphasis on military assistance and security considerations to an emphasis on closer economic relations.<sup>32</sup> Finally, some Latin American nations support the Initiative as a defensive strategy to cope with the perceived risk of U.S. protectionism (as did Canada), the feared decline of GATT authority, and the possible rise of an inward-looking European bloc.<sup>33</sup>

Despite this general atmosphere of enthusiasm, there are concerns about the Initiative's shortcomings and intentions. For example, Colombia's Finance Minister, Rudolf Hommes, speculated that the Initiative could "introduce new economic inefficiencies" by leading "to a specialization of the productive basis of [Latin American and Caribbean] countries that is determined by the competitive advantages that may exist with relation to the U.S. or Canadian economies, but could not necessarily exist with respect to the economies of the rest of the world."<sup>34</sup> Hommes criticizes the overall proposal as not going far enough to facilitate the free movement of people and the investment fund for being too small (compared, for example, to the European Bank for Reconstruction and Development capitalized at \$12 billion).<sup>35</sup> Other observers fear that the whole Initiative could become hostage to the bargaining strategies of commercial banks.<sup>36</sup> Furthermore, the environmental part of the

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rent version is at 4 GENERAL AGREEMENT ON TARIFFS AND TRADE, BASIC INSTRUMENTS AND SELECTED DOCUMENTS (1969), reprinted in J. JACKSON, *WORLD TRADE AND THE LAW OF GATT* 799 (1969). Chile, Peru, Argentina, Brazil, and Jamaica were already GATT members by 1979. Colombia joined in 1979; Mexico joined in 1986; Costa Rica became the 100th GATT signatory in November 1990; and ratification of Venezuela's protocol of accession is expected shortly.

32. *Caution Urged on Bush Plan; SELA's Experts Produce a Wary Report*, Latin Am. Weekly Rep., Sept. 20, 1990, at 6.

33. See, e.g., *Latin America, Mexico: Bush Seen Pushing Hemispheric Trade Plan*, Daily Rep. for Execs. (BNA), No. 11, at 5-10 (Jan. 16, 1991).

34. *Five Latin Ministers Embrace Free Trade*, Wall St. J., Sept. 13, 1990, at A-16. See also *Fin. Times*, Sept. 6, 1990, at 6 (wherein the Latin America Economic System (SELA) expresses similar concerns).

35. *Five Latin Ministers Embrace Free Trade*, *supra* note 34, at A-16.

36. See *Hearings*, *supra* note 27. During President Bush's five-nation trip to South America in early December 1990, the United States, Europe, and Japan cut off all new loans from the Inter-American Development Bank to Brazil until the Collor government makes significant progress with its commercial creditors. *Officials Say Bush Is Either Reflecting New Reality or Missing Opportunity*, N.Y. Times, Dec. 5, 1990, at A-16, col 6. Brazil has not paid interest on its commercial debt in fifteen months and is now \$8 billion in arrears. *Id.*

Initiative has received scant notice, partly because interest payments to the Environmental Fund would, at best, amount to about \$50 million annually.

Overall, the trade part of the Bush Initiative has incited the most interest. The vision of a Western Hemisphere free trade zone is perceived as a remarkable advance in U.S.-Latin American relations, overshadowing the investment and debt pillars. This approaching free trade zone, however, will compel a close assessment of the many pre-existing and emerging Latin American trade agreements.

#### IV. EXISTING ECONOMIC INTEGRATION AGREEMENTS IN LATIN AMERICA

If a new trade order is to emerge for the Western Hemisphere, it must draw on the lessons of existing trade arrangements. Economic integration is a perennial topic in Latin America, and the list of bilateral and multilateral agreements is extensive. Owing to an array of economic and political obstacles, none of the initiatives has yet fulfilled its promise. There is no parallel within Latin America to the European Community or even to the European Free Trade Area.

However, beginnings of integration within Latin America are now emerging. Argentina and Brazil first embarked on sectoral trade integration and then entered into agreements aiming at overall trade integration.<sup>37</sup> Mexico signed trade pacts with Chile and Venezuela in 1990.<sup>38</sup> Existing trade groups, like the Andean Pact and the Caribbean Community (CARICOM),<sup>39</sup> expanded earlier agreements.<sup>40</sup>

However, only within the Southern Cone has intra-regional trade growth been impressive, and that growth (68% between 1983 and 1989 (Table 1)) largely took place before association talks began. Inside the Andean Group, trade declined by 12% between

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37. *Mexico's Salinas Pushes Free Trade in Central, South American Tour*, Christian Sci. Mon., Oct. 5, 1990, at 4.

38. *Id.*

39. For further discussion on CARICOM, see *infra* notes 65-78 and accompanying text.

40. The Latin American Integration Association (LAI), formed by the Treaty of Montevideo in 1980, created an umbrella organization for the Andean Pact and the emerging group of Southern Cone countries. The LAI members represent approximately 90% of Latin American population and GNP, and about 80% of exports. The main countries outside LAI are the Central American countries.

1983 and 1989; within the Central American Common Market, trade decreased by 17% (Table 1).<sup>41</sup> For some countries, the intra-regional export market in the late 1980s was of great importance — for example, Bolivia (46%), Paraguay (30%), and Uruguay (26%) (Table 1) —but for most countries Latin markets are far less important than North American and European markets. As integration among these areas begins to take hold with the advent of increased agreements, these markets are likely to increase in importance.

#### A. *The Andean Pact*

In 1969, five Andean states — Bolivia, Columbia, Chile, Ecuador, and Peru — signed the Agreement on Andean Subregional Integration (Cartagena Agreement),<sup>42</sup> thereby forming what is known as the Andean Pact.<sup>43</sup> This agreement arose out of growing dissatisfaction with the existing Latin American Free Trade Area (LAFTA), which dated from 1960.<sup>44</sup> The Andean Pact is now composed of Bolivia, Columbia, Ecuador, Peru, and Venezuela.<sup>45</sup>

Unlike LAFTA, which sought with little success to reduce tariffs on a product-by-product basis, the Andean Group has freed 3,000 items from tariffs for intra-bloc trade.<sup>46</sup> Although a common external tariff has not been implemented, a degree of tariff harmonization was achieved through a minimum common external tariff. A 1990 study of the trade effects of the Andean Pact over the period 1968 to 1977 found annual trade creation of about 18.4% of total import values, offset by annual trade diversion of about 16.7% in the value of external imports.<sup>47</sup> The calculated net positive effect was thus only 1.7% annually, a fairly modest result.

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41. The figures cited here refer to import growth. For various reasons, export statistics for intra-group trade differ from import statistics. Correspondingly, trade growth stated in terms of export data would be different, but the picture of stagnation would remain much the same.

42. Agreement on Andean Subregional Integration, May 26, 1969, Bogota, 8 I.L.M. 910 (1969) [hereinafter *Cartagena Agreement*].

43. Khazen & Clark, *A Case Study of Effects of Developing Country Integration on Trade Flows*, 22 J. LATIN AM. STUDIES 317 (1990).

44. *Id.*

45. *Id.* at 318. Venezuela entered the Andean Pact in 1973. Final Act of the Negotiations on the Entry of Venezuela into the Cartagena Agreement, Feb. 13, 1973, 12 I.L.M. 344 (1973). Chile left the Pact in 1976. Khazen & Clark, *supra* note 43, at 318.

46. Khazen & Clark, *supra* note 43, at 318-19.

47. *Id.*

Looking at the performance of the Andean Pact, two phases can be observed. From 1970 to 1981, trade among member states grew at an average rate of 22% annually, reaching \$1.2 billion. After 1981, however, trade declined within the region, and in 1989, intra-Andean imports amounted to about \$800 million (excluding illicit drugs). Bilateral trade between Colombia and Venezuela accounted for 58% of that total. By contrast, trade with the United States in 1989 was about ten times greater than intra-Andean bloc trade (see Table 1).

Historically, Andean Pact policies toward foreign direct investment (FDI) have been less than liberal. The Andean nations placed special emphasis on a common policy toward FDI and technology transfer, fearing that the process of integration would promote geographic concentration of various industries disproportionately benefiting the advanced members. To counteract this anticipated result, particular industries were assigned to each country for the first ten years. Backing up the diversification policy, the Andean Pact's foreign investment code (Decision 24)<sup>48</sup> aimed at spreading the activities of multinational enterprise across all Andean members.<sup>49</sup> Decision 24 tried to allocate foreign investment to predetermined areas and industries through a myriad of guidelines.<sup>50</sup> As a consequence of these regulations, investing firms, whether domestic or foreign, were not allowed to seek the highest prospective returns.<sup>51</sup> This contributed to an already weak investment climate resulting from macroeconomic mismanagement and political instability.<sup>52</sup>

The latest policy initiatives coming to the Andean region include: (1) U.S. and E.C. attempts to promote legitimate commerce

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48. The foreign investment code, formally entitled the "Common Regime for Treatment of Foreign Capital and of Trademarks, Patents, Licenses and Royalties," is more commonly referred to as Decision 24 of the Commission of the Cartagena Agreement, promulgated December 31, 1970. Decision 24 has since been replaced by Decision 220 as of May 18, 1987. See Weisenfeld, *Decision 24 and Decision 220 of the Commission of the Cartagena Agreement (Andean Foreign Investment Codes)*, Introduction, in 1 BASIC DOCUMENTS OF INTERNATIONAL ECONOMIC LAW 581 (1990).

49. Khazen & Clark, *supra* note 43, at 319-20.

50. Weisenfeld, *supra* note 48, at 582.

51. *Id.*

52. The Quito Protocol of May 25, 1988 attempted to make Andean investment procedures and regional industrial programming more flexible. See Weisenfeld, *supra* note 48, at 591. Progress was also made in lifting non-tariff barriers. *Id.* However, the scope of the Quito Protocol was nowhere near as ambitious as the La Paz Agreement of November 1990. See *infra* text accompanying notes 57-60.

to deflect interest and participation in the drug trade under the scheme of the Generalized System of Preferences (GSP); and (2) the La Paz Agreement signed by five presidents, vowing to eliminate most of the interventionist provisions of the original Andean Pact.<sup>53</sup>

In late 1990, the European Community agreed under the GSP to open unilaterally its market for certain Andean tropical products.<sup>54</sup> The United States likewise agreed to give unilateral tariff preferences to most goods exported from Bolivia, Ecuador, Peru, and Colombia and to help farmers in the region reach global health and safety standards, improve certification procedures and meet certain labeling requirements.<sup>55</sup> However, after a seven month U.S. tariff review, only sixty-seven products — accounting for \$27 million of merchandise exports — were made eligible for special tariff status under the GSP.<sup>56</sup>

At a summit in La Paz on November 29-30, 1990, the five Andean Pact nations agreed to accomplish a true regional free trade area by 1992 by abolishing internal tariffs under the La Paz Agreement.<sup>57</sup> The Andean countries have further agreed to establish common external tariff rates during 1991 and implement these rates by 1995, when a Andean customs union will be established.<sup>58</sup> Meanwhile, all products will be eligible for tariff-free trade within the Andean area by December 31, 1991, and administered trade regimes will be abolished by 1992.<sup>59</sup> Limits on private investment in strategic industries are to be eliminated by June 30, 1991. Regulations governing foreign investment, particularly those that prevent foreign investors from taking advantage of the free trade area, are to be modified before March 31, 1991.<sup>60</sup> These sweeping initiatives are designed not only to create a unified Andean economy for its own sake, but also to act as a substantial partner in negotia-

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53. *Andean Pact to End Internal Tariffs Before 1992*, Reuters, Nov. 30, 1990.

54. J. Com., July 24, 1990, at 11-A. See also, *GSP Benefits Are Expanded*, Int'l Trade Rep. (BNA), No. 30, at 1145 (July 25, 1990).

55. J. Com., July 24, 1990, at 11A.

56. *Id.*

57. *Andean Pact to End Internal Tariffs Before 1992*, Reuters, Nov. 30, 1990. The agreement is formally known as the Agreement Regarding the Consolidation and Rescheduling of Certain Debts Owed to, Guaranteed by, or Insured by the U.S. Government and Its Agencies. *Treaty Actions — Jan. 1991*, U.S. Dep't of State Dispatch, Feb. 11, 1991.

58. *Andean Pact to End Internal Tariffs Before 1992*, *supra* note 53.

59. *Id.*

60. Unclassified Cable 16915 from U.S. Embassy at La Paz (Dec. 3, 1990) (available at the U.S. State Dep't).

tions with the United States.

### *B. Central American Common Market*

The Central American Common Market (CACM) achieved some results at its inception in the 1960s, but collapsed in the late 1970s.<sup>61</sup> Lately the CACM has been more of a paper creation than a force for integration.<sup>62</sup> The CACM members include El Salvador, Guatemala, Costa Rica, and Honduras.<sup>63</sup> Three of these countries — El Salvador, Guatemala, and Costa Rica — provide the bulk of total CACM trade, accounting for 92% of all exports within the area and for 84% of all imports from other member states. In the 1980s, ravaged by civil war and regional conflict, Central American economic integration retrogressed.<sup>64</sup> Between 1984 and 1986, intra-regional trade decreased sharply (36%). Although trade flows have recovered somewhat, the 1989 level of trade (\$2.2 billion) was still below the 1983 level (\$2.3 billion) (Table 1).

CACM exports to the other two trade associations, the Andean Pact and the Caribbean Community and Common Market (CARICOM),<sup>65</sup> were lower in 1989 than 1983 (Table 1). By contrast, trade with the United States has grown sharply and accounts for almost half of the region's total trade (Table 1). Between 1983 and 1989, CACM exports to the United States rose from \$1.6 billion to \$2.3 billion, while CACM imports from the United States more than tripled from \$1.5 billion to \$4.8 billion (reflecting sharply higher military purchases) (Table 1).

As their latest initiative, CACM members agreed, in January 1991, to negotiate sectoral free trade pacts with Mexico as part of a broader program (including concessional oil sales) to strengthen bilateral economic relations.<sup>66</sup> These negotiations are expected to lead to increased access to a wider range of products among these nations.<sup>67</sup>

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61. Kaston, *Capitalism from the Ashes*, Policy Review, No. 48, at 72 (Spring 1989).

62. *Id.*

63. Nicaragua joined in 1956, giving the group nominal membership of the entire region except Panama and Belize.

64. *Id.*

65. Treaty Establishing the Caribbean Community, signed July 4, 1973, 12 I.L.M. 1033 (1973) (entered into force Aug. 1, 1973) [hereinafter CARICOM].

66. Coone & Doulton, *Mexico Signs Central American Free-Trade Accord*, Fin. Times, Jan. 15, 1991, at 7.

67. *Id.*

### C. Caribbean Community

The Caribbean Community (CARICOM), founded in 1973, includes thirteen English-speaking Caribbean nations with a population of 5.5 million.<sup>68</sup> From 1981 to 1986, persistent shortages of foreign exchange, due to weak export prices and volumes for petroleum, bauxite, and sugar, prompted a considerable decline in intra-regional trade.<sup>69</sup> However, member trade has expanded since 1987, increasing by 20% in 1989 to reach \$317 million.<sup>70</sup>

In a meeting in October 1990 in Kingston, Jamaica, the leaders of CARICOM continued to emphasize further economic integration as a means to deal with emerging regional trading blocs in North America, Europe, and Southeast Asia.<sup>71</sup> CARICOM may enlarge by accepting new members, such as Haiti, Surinam, and the Dominican Republic.<sup>72</sup> Leaders also agreed on a Common External Tariff, effective April 1, 1991, with special provisions worked out for vulnerable sectors.<sup>73</sup> Moreover, in 1991, new rules will allow duty-free and restriction-free movement of CARICOM-produced goods between the member states.<sup>74</sup> Finally, the CARICOM Stock Exchange is scheduled to open by January 1, 1992. By 1994, leaders expect to achieve currency alignment among member states.<sup>75</sup>

U.S.-Caribbean trade relations have not yet fulfilled the expectations that were raised by the Caribbean Basin Initiatives of President Reagan (CBI I) and President Bush (CBI II).<sup>76</sup> These initiatives essentially promised one-way free trade, but nearly all products of current commercial interest to the Caribbean nations were excluded.<sup>77</sup> Since 1983, total exports of the Caribbean Community to the United States have in fact been halved from \$4.6 billion to only \$2.3 billion annually. Other factors were also at

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68. See CARICOM, *supra* note 65. CARICOM replaced the Caribbean Free Trade Association, CARIFTA, which was founded in 1965.

69. J. Com., June 5, 1990, at 6-B.

70. *Id.*

71. *Id.*

72. Update information was provided by the Eastern Caribbean Investment Promotion Service (ECIPS).

73. J. Com., *supra* note 69, at 6-B.

74. *Id.* The rule of origin provision requires "substantial transformation" for goods made with foreign materials to qualify for free movement to other CARICOM countries.

75. *Id.*

76. President Bush recently signed the revised Caribbean Basin Initiative (CBI II) into law as part of the Customs and Trade Act of 1990. See *Region Assesses Impact of CBI-II*, Latin Am. Reg. Rep.: Caribbean, Oct. 4, 1990, at 4.

77. *Id.*



work,<sup>78</sup> but the two CBIs did not noticeably help the Caribbean states overall to increase their exports to the United States. The Caribbean Community still seeks duty-free and quota-free concessions on exports to the United States of so-called "sensitive" items: textiles and apparel, leather products, sugar, and fruits and vegetables.

#### D. Southern Cone

The Southern Cone — comprised of Argentina, Brazil, Paraguay, and Uruguay — appears to be in the process of reformation. In April 1988, the leaders of the two primary Southern Cone countries, Presidents Sarney of Brazil and Alfonsín of Argentina, signed an industrial complementary agreement in April 1988 to coordinate policies in their auto, food, aircraft, and other industries. Since then, the pace of integration has increased, and new bilateral and multilateral agreements are in the making.

In July 1990, the new leaders of Argentina and Brazil, Presidents Carlos Menem and Fernando Collor de Mello, respectively, agreed to form a common market by the end of 1994.<sup>79</sup> Recently, Uruguay and Paraguay indicated that they would be interested in joining an integrated Southern Cone Market.<sup>80</sup> These announcements came only a few days after President Bush proposed the Enterprise for the Americas Initiative.

Chile has been mentioned as a possible member of the Southern Cone subregion. However, Chile is more likely to "go it alone" through negotiations with the United States. Chile has outpaced all the other countries in the region in the speed of its economic reforms<sup>81</sup> and prefers to negotiate a FTA with the United States

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78. For example, the worldwide drop in oil prices in the mid 1980s caused reduced exports of oil from Trinidad & Tobago, the Bahamas and the Netherland Antilles. *See id.*

79. *Brazil-Argentina Common Market in 1995*, Latin Am. Reg. Rep.: Brazil, Aug. 16, 1990, at 4.

80. *Collor and Menem Take Pragmatic Line on Common Market*, Fin. Times, Sept. 21, 1990. On March 26, 1991, two months after this symposium, the Presidents of Argentina, Brazil, Paraguay, and Uruguay signed an agreement in Asunción, creating a future Southern Cone common market known as Mercosur. *Southern Cone Governments Sign Mercosur into Existence*, Latin Am. Weekly Rep., Apr. 4, 1991, at 1. The Treaty of Asunción aims to reduce intra-regional export tariffs down to zero by the end of 1994. *Id.*

81. From 1983 to 1989, Chile's imports from and exports to the Southern Cone grew by 172% and 113%, respectively, while the Southern Cone's intra-regional imports grew by 129% (Table 1). The Southern Cone's imports from the Andean Pact and CARICOM decreased by 46% and 3%, respectively (Table 1). However, Chile boosted its export trade to

far more quickly than would be possible if it had to wait for its neighbors to catch up.<sup>82</sup> Chilean efforts seem to be bearing fruit. During his visit to Chile in December 1990, President Bush put prospective FTA talks on the near-term agenda, and U.S. Trade Representative Carla Hills reinstated Chile as a beneficiary under the U.S. generalized system of preferences (GSP).<sup>83</sup>

#### V. U.S.-CANADA FREE TRADE AGREEMENT<sup>84</sup>

The United States' free trade agreement with Canada (U.S.-Canada FTA)<sup>85</sup> will inevitably serve as a reference point both for talks with Mexico and for wider hemispheric negotiations. Given the disparities in income between the United States and Latin American countries, however, one should not expect bold progress on trade liberalization comparable to the U.S.-Canada FTA. Moreover, based on the Canadian precedent, Latin American nations should not expect an FTA to come into place quickly or to instantly solve their economic ills.

The United States and Canada had substantial economic ties before entering bilateral trade negotiations. In 1986, U.S. merchandise exports to Canada accounted for 25% of total U.S. exports, and U.S. imports from Canada accounted for 19% of total U.S. imports.<sup>86</sup> Trade ties were even more substantial from the Canadian perspective. Canadian merchandise exports to the United States accounted for 77% of Canadian exports, and imports accounted for 67%.<sup>87</sup> Comparable dependence on U.S. commercial ties is evident for Mexico (see Table 2). For Chile and the Southern Cone of Latin America, trade with the United States is about

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the United States by only 49% as compared with an export increase of more than 60% between the Southern Cone and the U.S. (Table 1).

82. *Bush Hails Possibility of Hemispheric Free Trade Zone During South American Trip*, Int'l Trade Rep. (BNA), No. 8, at 1824 (Dec. 5, 1990).

83. *Chile Seeks Closer U.S. Trade Ties*, Wall St. J., Jan. 8, 1991, at A10, at col. 4; *Fin. Times*, Dec. 11, 1990, at 14.

84. For a more detailed discussion of this topic, see Schott, *United States-Canada Free Trade: An Evaluation of the Agreement*, PA 24, INST. FOR INT'L ECON. (April 1988); Schott & Smith, *The Canada-United States Free Trade Agreement: The Global Impact*, INST. FOR INT'L ECON. (1988).

85. U.S.-Canada FTA, *supra* note 15. The United States also has a free trade agreement with Israel and a preferential trading arrangement with the Caribbean. These agreements, however, have a very small fraction of the economic impact of the U.S.-Canada agreement.

86. Schott, *supra* note 84; Schott & Smith, *supra* note 84.

87. Schott, *supra* note 84, at 10-11.

20% of total trade, while for the rest of Latin America the figure approaches 50% (see Table 1).

The Shamrock Summit between President Reagan and Prime Minister Mulroney in March 1985, in Quebec City, set both countries on the track toward bilateral trade liberalization. The broad goal was to establish a climate of predictability and confidence for both Canadian and United States firms to plan, invest, grow, and compete more effectively with one another and in the global market. After more than a century of false starts, U.S.-Canadian FTA negotiations began fourteen months after they were first broached and then took another seventeen months to conclude;<sup>88</sup> even then, some issues still proved so sensitive that the agreement fell short of expectations (notably, in transportation services, intellectual property, and "unfair" trade remedies).

Any trade agreements between the United States and Latin American countries will likewise take time to negotiate, and, inevitably, difficult and sensitive issues will arise. The following paragraphs summarize key elements of the U.S.-Canada FTA.

#### A. *Tariffs*

The U.S.-Canada FTA seeks to eliminate all tariffs between the two countries over a ten-year period. Tariffs on some products were eliminated immediately, but most tariffs were scheduled to be eliminated over five to ten years in equal annual installments. However, since the FTA went into force, both countries have agreed to accelerate tariff cuts on a broad range of products during two subsequent tariff reviews. The FTA has thus fortified the momentum for trade reform. The U.S.-Canada pattern of tariff liberalization sets a good standard for a broader Western Hemisphere compact, although in many cases the cuts would need to be phased asymmetrically, meaning larger cuts in the early years by the United States.

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88. The talks opened in May 1986; a draft agreement was initialed on October 3, 1987; the final text was completed on December 11, 1987; it was signed by President Reagan and Prime Minister Mulroney on January 2, 1988. Subsequently, after a bruising political battle in Canada, the FTA was ratified by each legislature and entered into force on January 1, 1989.

### *B. Government Procurement*

The FTA expanded on obligations that both countries had already undertaken in the GATT Code on Government Procurement. It also lowered the threshold of the contract value from \$171,000 to \$25,000 for the application of competitive bidding procedures and other GATT rules.

### *C. Energy*

The FTA contains commitments not to impose restrictions on imports and exports — including quotas, taxes, or price requirements — with limited exceptions for national security and short supply circumstances. It thereby guarantees market access for Canadian producers and reliable supplies for U.S. consumers. This issue will undoubtedly take on added importance in the aftermath of the Persian Gulf crisis.

### *D. Agriculture*

The FTA eliminated agricultural tariffs and removed some non-tariff barriers, but major farm policies in each country were left unchanged — supposedly to be reformed through Uruguay Round talks. The inclusion of agricultural liberalization in future regional trade pacts will depend importantly on the extent of reforms reached in GATT talks.

### *E. Investment*

The FTA eliminated the screening requirements for most U.S. greenfield investments and indirect U.S. acquisitions in Canada. By 1992, the threshold for screening direct acquisitions will be increased, so that it will only apply to the top 600-plus Canadian firms. Moreover, the FTA bars the introduction of new trade-related performance requirements. However, important exemptions to several of these provisions limit their application to the energy and cultural sectors.

### *F. Automotive Trade*

Under the FTA, Canada agreed to eliminate immediately its export-based duty remission scheme, to phase out its production-

based incentive scheme by 1995, to remove its embargo on used car imports within five years, and not to extend the benefits of the Auto Pact to new companies that establish assembly plants in Canada. The FTA also increased somewhat the North America content rule that must be met for a company to benefit from bilateral duty-free trade.

#### *G. Resolution of Subsidy/Countervail and Antidumping Problems*

Much to the disappointment of Canada, no new rules were reached on the application of countervailing duties (CVD) and antidumping duties (ADD). The FTA committed both countries to continue negotiating a harmonized regime on subsidy/CVD and ADD over a five to seven year period. The FTA also established ex post procedures to resolve disputes about the consistency of final CVD and ADD orders with existing national laws and GATT obligations. Disputes on subsidy/CVD and ADD issues are subject to binding arbitration.

#### *H. Services*

The FTA established a framework of rights and obligations regarding national treatment, establishment, and licensing and certification procedures. In addition, FTA provisions facilitate the temporary cross-border movement of professional workers (the only provisions relating to trade in labor services). Most existing restrictions were "grandfathered," although significant liberalization was achieved in the financial services sector. The FTA removed restrictions on U.S. banks — notably the 16% limit on total banking assets that foreign subsidiaries may hold in the Canadian market — and relaxed a restrictive rule on U.S. insurance groups operating in Canada.

#### *I. Dispute Settlement*

The FTA established a Canada-U.S. Trade Commission, composed of trade ministers and their representatives, to supervise the operation of the FTA and to resolve all disputes except those relating to subsidy/CVD and antidumping matters (which are handled through their own arbitration mechanism) and financial services (which are handled through a consultative system between the

U.S. Treasury and the Canadian Department of Finance).

## VI. THE ROAD TO A NORTH AMERICAN FREE TRADE AREA

The announcement that the United States and Mexico will begin negotiations on an FTA breathes political life into the idea of a North American Free Trade Area (NAFTA). Coming on the heels of the U.S.-Canada FTA (ratified in 1989), the U.S.-Mexico trade and investment pact (signed October 1989),<sup>89</sup> and the recent Canada-Mexico framework agreement (signed in March 1990), the prospective U.S.-Mexico talks have broad implications for economic relations between the three countries of North America. Negotiations between the United States and Mexico will likely begin in Spring 1991, assuming Congress consents to the applicability of fast-track procedures to implement the prospective pact.<sup>90</sup> An agreement would probably be ready by Spring 1992. Canada will also be actively involved in the talks, though (as of late January 1991) a decision had not been taken whether its role will be as an active participant or merely consultative.<sup>91</sup>

A two-part process could furnish the modalities to secure the interests of the United States, Mexico, and Canada, if trilateral negotiations do not supersede the bilateral U.S.-Mexico talks. First, a separate agreement focusing both on tariffs and sectoral issues (e.g., autos, pharmaceuticals, and energy) will likely be negotiated between the United States and Mexico. This would answer Mexico's interest in the rapid conclusion of a bilateral FTA and would avoid the complications of trilateral negotiations. Second, a separate North American steering group comprised of the three countries could begin to plan for a NAFTA — by harmonizing U.S.-Mexico provisions (in a technical sense) with the provisions of the Canada-U.S. FTA and by devising ways to develop common rules of origin, administrative provisions, and dispute settlement procedures.

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89. Mexico-United States Understanding Regarding the Joint Committee for Investment and Trade, Oct. 3, 1989, Washington, D.C., 29 I.L.M. 36 (1990).

90. *Latin America, Mexico: Bush Seen Pushing Hemispheric Trade Plan*, Daily Rep. for Execs. (BNA) No. 11, at S-10 (Jan. 16, 1991).

91. *Id.*

### *A. Goals of the Partners*

Mexico, Canada, and the United States each have their own reasons for pursuing a North American Free Trade Area. The extent of mutuality will largely determine the scope and pace of talks.

#### 1. Mexico

As the smallest and most protected economy, Mexico has the most to gain over time from a NAFTA. An agreement would reinforce and accelerate the pace of domestic reforms currently underway and would guarantee access to the broader North American market. Further, an open trade policy could help alleviate Mexico's crippling debt service burden and help finance the current account deficit by encouraging foreign direct investment and the return of flight capital (statistics on Mexican trade patterns appear in Table 2).

#### 2. Canada

Canadian interests in a NAFTA are more defensive than Mexican interests. Canada wants to maintain its position as a player in the dialogue between Mexico and the United States, to safeguard Canadian rights under the U.S.-Canada FTA, and to deal with such questions as trade in automobiles and parts and natural gas flows. In some instances, Canada and Mexico may find common commercial interests juxtaposed with the United States.

#### 3. United States

U.S. interests lie both in the political and economic areas. Economic growth should promote a stable and democratic regime in Mexico, providing a good model for other countries in the region. The FTA would reinforce ongoing trade and investment reforms in Mexico, and thus likely contribute to increased economic growth. Many Fortune 500 manufacturing firms are looking to the global advantages of safe investment and production in Mexico. A prosperous Mexico would become a thriving market for U.S. exports, providing a particular boost to the economies of border states such as California, Texas, New Mexico, and Arizona. At the same time, growth in the Mexican economy would create new jobs and in-

crease wages in Mexico and thus help stem the tide of illegal immigration. Finally, in the face of a rapidly integrating European Community, a North American Free Trade Area has political appeal in showing that "we can do it, too."

For both Canada and the United States, however, an economic partnership with a low-wage country with nearly ninety million people could have enormous consequences. Labor-intensive and machine-driven industries in Canada and the United States — fruits and vegetables, textiles, automobiles and parts, household equipment, and consumer electronics — could significantly contract over a period of ten or fifteen years. On the other hand, Canada and the United States should gain greatly from increased exports of sophisticated products and services to Mexico and from the ability to draw on Mexican labor and resources to compete in world markets.

### *B. Impact on Third World Countries*

Estimates indicate that, over a five year period, trade creation of a U.S.-Mexico agreement, coming on top of the U.S.-Canada FTA, will greatly outweigh trade diversion.<sup>92</sup> Eliminating U.S. tariffs on Mexican products would increase Mexican exports to the United States by about \$1.4 billion in the early 1990s, and eliminating both tariff and non-tariff barriers (NTBs) would increase Mexican exports by about \$2.8 billion. Mexican exports of clothing, machinery, transportation equipment, and fruit and vegetables will especially benefit from the trade pact. Total trade diversion would probably not exceed \$0.4 billion. The diversion effect on Central and South America is estimated, at worst, at under \$0.2 billion. If sector-specific deals on NTBs come at the expense of third country suppliers, however, the diversion effect could become much more pronounced.

### *C. Agenda*

The agenda for both the bilateral U.S.-Mexico agreement and the trilateral NAFTA will likely follow the model of the Canada-U.S. FTA, including negotiations on specific sectoral issues. Broader economic issues such as monetary integration and labor

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92. The figures in this paragraph are based on data provided by Sam Laird, International Economics Division, World Bank.



mobility will be excluded from an agreement. However, U.S. labor unions and environmental and consumer groups are pressing for the inclusion of social issues involving environmental, workplace, health, and safety standards, as well as drug trafficking.

### 1. Tariffs and Quotas

Mexico has reduced its average weighted tariff to about 10%, set a maximum rate of 20%, and has substantially harmonized its tariff schedule. The United States already extends tariff preferences to Mexico under the General System of Preferences and HTS categories 9802.00.60 and 9802.00.80 (formerly TSUS 806.30 and 807.00, provisions that underpin maquiladora operations). Non-tariff barriers likely to be targeted for liberalization include U.S. steel quotas (in case they do not expire as scheduled in March 1992), Mexican local content and export requirements in the auto industry, and both U.S. and Mexican quotas in agriculture and textiles and apparel. These sectors, of course, will also be targeted by opponents of trade liberalization in an effort to derail trade talks entirely or at least exempt the sectors from coverage. In addition, questions remain concerning the timing of tariff phase-outs and special treatment for impacted industries.

### 2. Agriculture

This sector is beset by layers of barriers in the form of tariffs, quotas, and phytosanitary regulations. The United States has a wide number of specific duties on fruits and vegetables, which range up to 38% ad valorem. Both the United States and Mexico also impose extensive import licensing controls on agricultural products. The U.S. quotas are hard on sugar, fruits and vegetables (fourteen commodities are subject to marketing orders with a strong seasonal component); Mexican quotas are hard on U.S. grain exports, especially during the Mexican harvest season. The United States is worried both about Mexican pests and animal diseases making their way north and about pesticide levels on crops.

### 3. Energy

The energy sector holds the greatest promise for big new U.S. investment, but is politically explosive for Mexico. Ownership and control of the energy sector has been reserved for the government

since 1938. Mexico desperately needs foreign capital to upgrade aging machinery and gain technology to exploit difficult new fields. With rising domestic consumption and flat or declining production, Mexico would become an oil importer by the year 2000 in the absence of major new investments. The recent \$1.5 billion Eximbank loan — possibly expanding to \$6.5 billion over the next few years — gives American oil-service companies access to Mexican oil-development projects.<sup>93</sup> However, it remains an open question whether Mexico can attract participation by foreign companies with the advanced technologies needed to explore and exploit its oil reserves. American oil companies rankle because they are still prohibited from direct equity investment in the Mexican oil industry.

#### 4. Automotive Industry

Mexico has a highly regulated automobile industry. FTA negotiators are likely to discuss issues such as safety standards in factories, import restrictions under the 1989 Mexican Auto Decree (which limits imports to 15% of domestic sales in 1991 and 1992), export requirements (exports must be a multiple of imports, 1.75 by 1994), value added requirements (36% local content to be supplied by locally owned firms), and investment limitations. The 1989 Decree has been applauded by auto producers, but is disliked by U.S. and Canadian auto parts manufacturers. The interaction between the U.S.-Mexico FTA and the U.S.-Canada Auto Pact raises fears in Canada that the whole industry will move south. The key element in the negotiations will thus involve the establishment of common rules of origin.

#### 5. Services

An agreement on services would build on the model of the U.S.-Canada FTA and on the provisions of the prospective General Agreement on Trade in Services (GATS) that is being developed in the Uruguay Round. The GATS will likely contain a framework of rights and obligations that stress transparency of regulations and the application of the national treatment principle and that liberalize trade through an evolutionary process, sector by sector, start-

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93. *Bush Makes Progress on Trade Issues in Mexico, Gains Supports for Gulf Policy*, Wall St. J., Nov. 28, 1990, at A24, col. 2.

ing from the baseline of existing policies. All this is facilitated by Mexican privatization of its banking and telecommunications sectors.

## 6. Maquiladora

Maquiladoras<sup>94</sup> have drawn criticism from factions both within the United States and Mexico. Problems include low average wages in Mexico, exploitation of young and female workers, low unionization, and inadequate health and safety standards in the workplace. These are all issues likely to be revisited in prospective U.S. negotiations with other countries or regions in the hemisphere. However, maquila operations offer two benefits for the United States: maquila imports are an alternative to goods from East Asia and lead to a larger backflow of U.S. exports to Mexico, and maquilas reduce emigration to the United States, by providing jobs for about 440,000 Mexicans.

## 7. Countervailing Duty and Antidumping Laws

Prospective results in the Uruguay Round do not hold great promise for reforming the multilateral GATT rules that govern national countervailing duty (CVD) and antidumping (ADD) proceedings. Given the experience of the U.S.-Canada talks, bilateral and regional pacts will likewise only be able to make small, incremental reforms. An agreement on CVD and ADD could start, however, by including a dispute settlement procedure along lines similar to the U.S.-Canada FTA procedures. Over time, the ADD regime could be supplemented and eventually supplanted by a common competition policy standard. In the distant future, it might be possible to negotiate a NAFTA code limiting domestic subsidies, as well as export subsidies, so that CVD proceedings dwindle in number and importance.

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94. Maquiladoras are export manufacturing firms located in Mexico which are foreign-owned but do not pay tariffs on the component parts they import for assembly, thus reducing the overall cost of manufacturing and exporting goods to the U.S. See Mulligan, *International Trade: What Does the Future Hold?*, TEX. LAW., Jan. 21, 1991, at 24; *Latin America, Mexico: Bush Seen Pressing Hemispheric Trade Plan*, Daily Rep. for Execs. (BNA) No. 11, at S-10.

## VII. LESSONS FOR THE HEMISPHERE

The successes and failures of past trade agreements suggest various lessons for new efforts to achieve free trade within the hemisphere. Those lessons can be grouped under three headings: preconditions, timing, and subject matter.

*A. Preconditions for a Trade Agreement*

More often than not, free trade agreements are concluded between countries with similar levels of per capita income. Many social conditions correlate with per capita income: for example, general wage levels, minimum wage legislation, health and safety rules for the workplace, social safety nets (old age, health, and welfare assistance), environmental controls, and educational standards. When such social conditions are similar, the trauma of economic integration is much reduced. In two major instances of pronounced social disparities, the richer partner agreed to help the poorer partner with very substantial flows of financial assistance. Thus, when the European Community was enlarged to include Greece, Spain, and Portugal, a massive regional assistance program was inaugurated to improve the infrastructure in poorer parts of Europe. Likewise, when the German Democratic Republic was reunited with the Federal Republic, the Federal Republic committed huge amounts of money to a broad reconstruction program.

Obviously, per capita income disparities between the United States and Latin American nations are great — more than a factor of ten in the case of the United States and Mexico. It is most unlikely that large-scale financial assistance programs will be devised to bridge the ensuing social disparities. Other solutions will have to be devised.

In addition to finding imaginative solutions to ease concerns about vast social disparities, five preconditions will need to be met before worthwhile trade agreements can be negotiated between the United States and single Latin nations or groups of countries. When those conditions are met, a trade agreement can act as an archstone holding together the pillars of a functioning, growth-oriented economy.

The first precondition is a reasonable degree of monetary stability. Experience teaches that high *average* inflation rates, year-to-year, are also *highly variable* rates, year-to-year. Highly variable

inflation wrenches and twists the economy: not all prices and wages rise and fall at the same rate. In particular, with high and variable inflation, enormous shifts in the real exchange rate are bound to occur (Table 3), which alternately exposes the traded goods sector to mania and depression. In manic episodes, partner countries will inevitably complain about unfair trade subsidized by a cheap exchange rate; in depressive moods, home country industries will certainly seek, and often obtain, protection against imports. This was the experience of the United States in the first half of the 1980s, when a rapid fall in inflation and a superstrong dollar led to a wave of protection in automobiles, steel, and other products. It is a recurring experience in Latin America.

The second precondition is a willingness to accept the tenets of a market economy and to reject the teachings of statism. Possibly the most important effect of lowered trade barriers is increased competitive pressure on domestic industry. Such pressure is stoutly resisted by state-run firms, which are usually the victim of two forces. First, employees and managers come to think of themselves as tenured workers. In turn, this makes it necessary to maintain output, even when the goods are rejected by the market; and it makes it hard to introduce efficiencies that entail staff layoffs. Second, cozy relations develop with domestic supplying industries, and these relations virtually equate to buy-national preferences. When a large part of industry operates under state control, free trade is at best a nuisance. Neither on the production side nor on the purchasing side do state enterprises wish to respond to market signals, and their first line of defense will be to block those signals by undermining the trade agreement.

On an index from zero (backsliding toward statism) to four (embrace of private markets), some Latin countries may be scored as follows for their performance in the 1980s. In the category of 4: Chile and Mexico (the amazing transition from Lopez Portillo to Salinas); in the category of 3: Costa Rica, Jamaica, Bolivia, Venezuela, and Argentina; in the category of 2: Colombia; in the category of 1: Brazil; in the category of zero: Peru.<sup>95</sup> A more recent report card on government policies and officials, based on evaluations of corporate executives and analysts, leads to the following scores for 1990: Chile and Mexico, 3; Brazil, Colombia and Vene-

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95. Williamson, *The Progress of Policy Reform in Latin America*, PA 28, INST. FOR INT'L ECON., at Table 10 (Jan. 1990).

zuela, high 2; Argentina, Peru, Ecuador and Uruguay, low 2.<sup>96</sup> Evidently, 1990 elections in both Brazil and Peru installed new regimes that moved each country up the scale.

The third precondition is an ability and willingness of the government to look to other revenue sources than imposts on international transactions. When import tariffs and export taxes form a large part of government revenues, it will be very difficult for governments to accept even the first step in any trade agreement which looks to the phase-out of these charges. As Table 3 shows, Latin countries vary enormously in their dependence on import tariffs and export taxes.

The fourth precondition is trade linkage. At least one of the partner countries needs to depend significantly on trade with the other. This dependence establishes the *raison d'être* for the negotiation: to receive preferential trade treatment in order to secure and expand access to the partner's market. The clearest examples of this point are in North America, where both Canada and Mexico rely on the U.S. market for the preponderant share of their trade.

The final precondition, vital in any trade agreement with the United States (or the European Community, for that matter), is a functioning democracy. Within the United States, there will always be economic opponents to a free trade agreement. These opponents will usually be able to carry the day against proposed concessions to a dictator or a military government. Moreover, the United States has a long history of applying economic sanctions against Latin nations (twenty-five cases since the Second World War).<sup>97</sup> A trade agreement with a dictatorship will often be at risk of interruption by the United States.

Sometimes, as in the U.S.-Canada agreement or the Australia-New Zealand agreement, these five preconditions have been in place for a very long period before the trade agreement was reached. But that need not always be the case. The idea of the European Economic Community gathered force in the early 1950s, only a few years after the Second World War and the rule of fascism in Germany and Italy. In Europe, the Treaty of Rome was seen as the archstone of a democratic peaceful continent and a way to lock-in liberal economic and political institutions. Similarly, the U.S.-Mexico FTA, if it succeeds, will come into place when mone-

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96. See Latin Finance, Dec. 1990, at 36-37.

97. HUFBAUER, SCHOTT & ELLIOTT, *ECONOMIC SANCTIONS RECONSIDERED* (2d ed. 1990).

tary stability is a recent achievement in Mexico, and just as statism is being dismantled.

This Article takes the view that a long record of democracy, free markets, and monetary stability is not required. Instead, the focus should be on recent events and on *trends* as much as *levels*. Even so, conditions are radically different from country to country, which brings us to issues of timing.

### B. *Timing*

In his June 27, 1990 speech launching the Enterprise Initiative, President Bush stated that he is willing to negotiate with every single country on a bilateral basis or, if possible, with groups of countries.<sup>98</sup> Not everything can be done at once. There are two main timing issues. The first is the time sequence between hemispheric negotiations and U.S.-Mexico and NAFTA negotiations. The second is the priority of countries or country groups in their negotiations with the United States. Taken together, timing considerations point, in the first instance, to a "hub-and-spoke" model rather than a "hub-spoke-rim" model.<sup>99</sup> In a "hub-and-spoke" model, the United States is the "hub" while Canada, Mexico, and later individual Latin American countries are the "spokes." Only when the "spokes" join together will there be a "hub-spoke-rim" system.

In the best of all possible worlds, free trade would be achieved through a single plurilateral trade agreement rather than separate bilateral pacts between the United States, Canada, Mexico, and other countries in the region. Ronald Wonnacott argues that the bilateral approach will create a "discriminatory, inefficient, hub-and-spoke trading structure" that would benefit the United States (the "hub") more than its trading partners (the "spokes"), and could erode prospects for future multilateral liberalization.<sup>100</sup>

However, Wonnacott's argument is a case of the best being the enemy of the good. The logic for starting with a hub-and-spoke system is the "drop-lock" argument. At different times, different Latin countries will meet the preconditions for a worthwhile agreement. If the moment is not seized, there may well be policy retro-

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98. See Bush Initiative, *supra* note 5.

99. R. WONNACOTT, *supra* note 3.

100. *Id.*

gression. Moreover, it is unlikely that the preconditions will be met for a large group of Latin countries at a single point in time in the near to medium term.

There is much to be said for delaying substantive hemispheric trade talks until the U.S.-Mexico FTA is wrapped up sometime in 1992, and the shape of a broader NAFTA is articulated.<sup>101</sup> This short delay, while framework agreements are being implemented<sup>102</sup> will allow countries in Latin America a better opportunity to achieve the preconditions for a meaningful trade agreement. Moreover, in political terms, the United States can only digest so much trade liberalization within a two-year time frame. U.S.-Mexico talks are sure to provoke the U.S. fruit and vegetable and textile industries, and other U.S. industries, notably petroleum and automobiles, will be watching carefully to see whether they are getting from Mexico as much as they "deserve." The political circuits might well be overloaded by the simultaneous negotiation of free trade agreements with additional Latin countries.

This does not mean a halt to diplomatic initiatives for the next two years. Seven Latin American nations have already signed bilateral trade and investment agreements with the United States; Brazil, Argentina, Paraguay, and Uruguay are wrapping up the remaining details for similar framework agreements;<sup>103</sup> the CARICOM countries have experience with two Caribbean Basin Initiatives; and the Andean Pact might negotiate a framework agreement in 1992. These agreements are essential precursors for trade negotiations. The question ahead is the priority sequence of countries and country-groups for full-fledged talks. There are two that stand out in readiness terms: Chile and the CARICOM nations.

As a single medium-sized country, Chile is the most obvious candidate. Chile has expressed a keen interest in talks with the United States. Democracy, free markets, monetary stability, and low reliance on tariffs all characterize Chile. In his December 1990 visit to Santiago, President Bush proclaimed that "Chile has moved further, faster than any other nation in South America toward real free-market reform" and declared the country a prime

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101. This timetable requires that President Bush emerge victorious, in both military and international political terms, from the crisis in Iraq.

102. See *infra* text accompanying notes 105-06.

103. Inside U.S. Trade, Nov. 30, 1990, at 3.



candidate for debt relief under the Enterprise Initiative.<sup>104</sup>

The CARICOM group is also eager for a free trade arrangement. The main obstacle is U.S. reluctance to grant duty-free concessions on U.S. imports of "sensitive products" — textiles, petroleum products, footwear, and leather goods — as part of the revised Caribbean Basin Initiative (CBI II). These issues are still on the table and the Caribbean nations are also seeking an expansion of the U.S. quota for sugar.<sup>105</sup> A further obstacle within the CARICOM nations is its high revenue reliance on taxes on international transactions (see Table 3). With these sizeable caveats, the CARICOM group meets the preconditions for a trade agreement.

### C. Subject Matter

Broadly speaking, the U.S.-Canada FTA provides the best guide to the *ultimate* content of trade agreements negotiated between the United States and Latin nations. What is actually achieved in the U.S.-Mexico agreement will probably provide the best guide to the *first stage* of future agreements with Latin countries.

In the first stage, tariffs will be phased-out over periods not longer than ten years, but in some cases the cuts will be asymmetric (that is, faster for the United States) and extended in duration, to perhaps fifteen years. Predictably, once the phase-out is agreed, accelerations will be negotiated. Quotas will also be liberalized, but here idiosyncratic formulas with ample safeguards will be negotiated sector by sector. In addition, the first stage will establish a framework for dispute settlement, common rules of origin, and administrative procedures, consistent with the U.S.-Canada FTA.

Beyond that, other items may be postponed to later stages, but not indefinitely. In large part, the United States agenda will consist of unfinished business from the Uruguay Round: intellectual property protection, rules against distortions to investment (local content and export performance requirements), national treatment for services, and better discipline on subsidies.

On a longer time table, the negotiators will address key social

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104. *Bush Lauds Free-Market Economy in Chile, Promises Closer Relations*, Wash. Post, Dec. 7, 1990, at A-53, col. 6. Other official U.S. statements single out Chile for talks right after Mexico. See *Chile Seeks Closer U.S. Trade Ties*, *supra* note 83 at A-10, col. 4.

105. *Region Assesses Impact of CBI-II*, *supra* note 76, at 4.

issues: environment, wages, and labor standards.<sup>106</sup> Already now, on the eve of U.S.-Mexican FTA negotiations, American fears are focused on the maquiladoras in Mexico. Lower wages and lax health and safety standards are luring companies into border plants. The environmental issues of hazardous waste disposal, sewage treatment by border cities such as Tijuana, local air pollution and greenhouse gases, and saline water flowing from the United States to Mexico cannot be indefinitely postponed. It appears that, if trade agreements go forward with Mexico and other Latin nations, they will be accompanied by social pacts. At this stage, the prospective content of these pacts is nebulous, but the pacts will at least call for increased enforcement of existing social and environmental legislation, higher standards, and regular monitoring.

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106. The Lome Conventions between the European Community and former colonies in Africa, the Caribbean and the Pacific, might serve as a useful model. African, Caribbean and Pacific States — European Economic Community Convention, Dec. 15, 1989, 29 I.L.M. 783 (1990). The Lome Conventions established an institutional framework for regular public and private sector contacts on a wide variety of issues, including the environment, education, and infrastructure. See generally I.K. Minta, *The Lome Convention and the New International Economic Order*, 27 How. L. J. 953 (1984).

Table 1. Regional trade flows in Latin America, 1983 and 1989 (millions of dollars)

	1983				1989				% change from 1983 to 1989	
	Imports	% of Total	Exports	% of Total	Imports	% of Total	Exports	% of Total	Imports	Exports
<b>SOUTHERN CONE<sup>a</sup></b>	22,410	100	31,021	100	26,265	100	55,358	100	17	78
Intra-regional	2,010	6	2,395	8	4,599	18	4,244	8	129	77
Central America	0	0	69	0	5	0	185	0	n.a.	169
Andean Pact	1,397	5	970	3	755	3	1,527	3	(46)	57
CARICOM <sup>d</sup>	78	0	85	0	76	0	189	0	(3)	123
United States	3,670	12	6,098	20	6,276	24	9,741	18	71	60
Mexico	321	1	799	3	449	2	632	1	40	(21)
Canada	674	2	430	1	694	3	1,094	2	3	154
Chile	302	1	415	1	700	3	1,010	2	132	143
All other	13,959	45	19,761	64	12,712	48	36,737	66	(9)	86
<b>CENTRAL AMERICA<sup>b</sup></b>	4,608	100	3,847	100	6,406	100	4,513	100	39	17
Intra-regional	684	15	749	19	571	9	723	16	(17)	(3)
Southern Cone	48	1	9	0	221	3	9	0	360	0
Andean Pact	281	6	114	3	423	7	37	1	51	(68)
CAPRICOM	175	4	54	1	35	1	37	1	(80)	(31)
United States	1,494	32	1,584	41	2,532	40	2,277	50	69	44
Mexico	442	10	31	1	375	6	30	1	(15)	(2)
Canada	73	2	29	1	86	1	181	4	17	517
Chile	7	0	1	0	11	0	0	0	51	(67)
All other	1,403	30	1,277	33	2,152	34	1,219	27	53	(4)
<b>ANDEAN PACT<sup>c</sup></b>	14,785	100	23,428	100	16,601	100	24,825	100	12	6
Intra-regional	909	6	809	3	796	5	1,130	5	(12)	40
Central America	56	0	267	1	38	0	407	2	(32)	52
Southern Cone	1,110	8	1,087	5	1,427	9	738	3	29	(32)
CARICOM	189	1	328	1	24	0	1,190	5	(87)	263
United States	5,924	40	8,654	37	6,432	39	11,732	47	9	36
Mexico	228	2	36	0	346	2	128	1	52	256
Canada	576	4	655	3	422	3	524	2	(27)	(20)
Chile	187	1	303	1	267	2	419	2	43	38
All other	5,606	38	11,289	48	6,849	41	8,557	34	22	(24)
<b>CHILE</b>	2,968	100	3,850	100	6,496	100	8,191	100	119	113
Southern Cone	421	14	292	8	1,146	18	630	8	172	115
Central America	0	0	0	0	0	0	12	0	n.a.	n.a.
Andean Group	324	11	156	4	502	8	354	4	55	126
Caribbean E.C.	120	4	0	0	13	0	0	0	(89)	n.a.
United States	704	24	1,083	28	1,283	20	1,616	20	82	49
Mexico	17	1	1	0	88	1	28	0	422	n.a.
Canada	61	2	60	2	142	2	56	1	133	(7)
All other	1,321	45	2,257	59	3,322	51	5,496	67	151	144

<sup>a</sup> Argentina, Brazil, Paraguay, and Uruguay<sup>b</sup> Costa Rica, El Salvador, Guatemala, Honduras, and Nicaragua<sup>c</sup> Bolivia, Colombia, Ecuador, Peru, and Venezuela<sup>d</sup> 13 Caribbean countriesSources: IMF, Direction of Trade Statistics, Yearbook 1990, Country Tables  
US Department of Commerce, US Trade 1990

*Table 2. Mexico's Regional Trading Partners,  
1980 and 1990 (% of total trade)*

	1980	1989 <sup>a</sup>	1980	1989 <sup>a</sup>
United States	64.7	63.3	61.6	67.0
Canada	0.8	2.4	1.8	1.8
Japan	4.3	7.1	5.1	5.3
Other industrial countries	15.6	16.3	17.3	16.3
Latin America and Caribbean	6.9	5.2	4.2	4.2
Other developing countries	5.8	3.6	1.6	2.4
Other <sup>b</sup>	2.0	2.1	8.3	3.1

<sup>a</sup>Estimated

<sup>b</sup>USSR and other non-members

Source: IMF, Direction of Trade Statistics,  
Yearbook 1987, and 1990.

*Table 3. Quantitative Indicators of Preconditions for Entry into a Free Trade Agreement*

	Average Inflation Rate 1987-89	Average Absolute change in the real effective exchange rate 1987-89	Taxes on International Transactions late 1980s (% of total revenue)
United States	2.8	5.4	1.7
Canada	3.3	9.7	3.8
Australia	6.0	9.0	4.6
New Zealand	5.4	6.2	2.8
European Community			
Belgium	1.5	4.2	0.0
Denmark	3.4	4.4	0.1
France	2.2	2.7	0.3
Germany	1.4	0.6	0.0
Greece	13.9	1.7	3.3
Ireland	2.2	n.a.	3.6
Italy	4.3	2.3	0.0
Luxembourg	1.6	0.5	0.1
Netherlands	0.6	2.2	0.0
Portugal	9.5	3.2	1.9
Spain	4.6	4.6	2.8
United Kingdom	4.7	4.8	0.1
Mexico	over 100.0	11.9	3.4

Andean Pact (ANCOM)			
Bolivia	48.0	4.6	12.6
Colombia	29.9	3.5	11.2
Ecuador	94.5	18.4	n.a.
Peru	over	14.3	21.5
	100.0		
Venezuela	66.0	14.0	23.4
Central American Common			
Market (CACM)			
El Salvador	22.5	n.a.	21.1
Guatemala	12.0	n.a.	37.2
Honduras	5.3	n.a.	n.a.
Costa Rica	17.8	6.0	21.1
Nicaragua	n.a.	20.3	16.9
Southern Cone			
Brazil	over	16.8	1.6
	100.0		
Argentina	over	13.2	10.3
	100.0		
Uruguay	over	5.1	13.6
	100.0		
Paraguay	29.4	14.1	12.0
Chile	16.3	4.3	9.9
Selected Caribbean			
Economia Community (CARICOM)			
Bahamas	3.7	1.8	58.0
Barbados	4.0	n.a.	13.8
Caymen Islands	n.a.	n.a.	42.1
Guyana	27.8	25.6	10.0
Jamaica	9.7	n.a.	4.1
Netherlands Antilles	2.3	3.9	24.4
St. Kitts & Nevis	1.8	n.a.	26.0
St. Lucia	1.9	4.1	33.6
St. Vincent	n.a.	3.1	43.6

Source: IMF, Government Finance Statistics Yearbook 1990;  
 JP Morgan, World Financial Markets, July 1990  
 IMF, International Financial Statistics, November 1990