

EXPECTED IMPACT OF FTAA ON LATIN AMERICAN COUNTRIES

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The Free Trade Area of the Americas (“FTAA”) is proposed to become effective in January 2005. The viability of this major regional economic integration project has been widely debated over the past decade since the idea was first presented at the Miami Summit of the Americas in December 1994. The idea was developed through subsequent Summits in Santiago, Chile in 1999 and Quebec, Canada in 2001, as well as through several Ministerial Meetings that took place in between these Summits. By the end of 2003 the question of gaining approval of a free trade area by the region’s national governments had advanced to the point of questions arising regarding the detailed contents of the agreement and debating possible exceptions to the free trade rule, rather than whether or not an agreement would be reached. It is expected that an agreement will be achieved; therefore, this article explores some of the implications of such an agreement.

The broad intent of the FTAA is to create a regional economy rivaling the European Union, and one that unites the industrial leaders—the United States (“US”) and Canada—with emerging markets from Mexico to Argentina. This intent indicates the expected scope and significance of the impact of the FTAA. Far from focusing only on the traditional elements of a free trade area—creation and diversion of trade based on tariff reductions—the FTAA is to bring with it additional elements including: the elimination or reduction of non-tariff barriers to trade; similar elimination or reduction of barriers to trade in services; expansion of foreign direct investment; and generation of increased confidence in the economies of Latin America and the Caribbean.

This article examines the expected FTAA and its potential impact on Latin American and Caribbean countries that are eligible to join the FTAA. The expected impact on the US has been studied elsewhere,¹ and is not included in

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¹ See, e.g., Council of the Americas. *FTAA: Blueprint for Prosperity*. Washington, D.C.: Council of the Americas, 2001.

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this analysis; however, reference is made to Brazil throughout this article. It should be recognized at the outset that the FTAA cannot parallel the European Community model too closely, since the nature of the countries involved is significantly different. Namely, with regard to the FTAA, the United States constitutes approximately 85% of the regional income, and provides the market for more than half of the exports everywhere in the Western Hemisphere, other than the Southern Cone countries (For Brazil and Argentina, the US absorbs only about 20-25% of their exports, while the European Union takes in slightly more).² Thus, the bargaining situations of the countries are different between countries in the Western Hemisphere and Europe, since Europe has had more balanced dealings at least among the larger countries (i.e., France, Germany, and Britain). And the level of economic development is quite different between the US and Canada on one hand, where gross domestic product (GDP) per capita was more than US \$30,000 per person in 2002, and Latin America and the Caribbean countries where GDP per capita was less than US \$7,000 in 2002.³

Conceptual View of the FTAA's Overall Impact on Latin America

The negotiations for a Free Trade Area of the Americas cover far more than tariff barriers. The additional items on the agenda include standards and technical barriers, rules of origin and customs procedures, intellectual property protection, and regulation of trade in services.⁴ The negotiations also relate to other activities of international firms, such as foreign direct investment. An analysis of the expected impact of the FTAA must include consideration of the added policy issues that will appear in the Agreement (or as side agreements⁵). A full evaluation of the expected impact includes the following items:

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Elements of the Agreement	Countries & Products
Generalized reduction/elimination of tariffs with a timetable	All FTAA countries and most products
Separate reduction or non-reduction of tariffs on some specific items	Brazilian auto parts, perhaps in exchange for US steel; Brazilian information technology products, possibly in exchange for US orange juice
Specific reduction of existing quota barriers	US quotas on textiles and sugar

² International Monetary Fund, *Direction of Trade Statistics*. Updated monthly and available on CD-ROM at <http://www.imf.org/external/pubs/cat/longres.cfm?sk=16063.0>.

³ International Monetary Fund, *International Financial Statistics*. Updated monthly and available on CD-ROM at <http://ifs.apdi.net/imf/about.asp>.

⁴ See, e.g., the FTAA draft agreement at http://www.ftaa-alca.org/FTAADraft03/Index_e.asp [hereinafter FTAA draft agreement].

⁵ That is how NAFTA was negotiated among the US, Canada, and Mexico. A number of issues, including labor rights and environmental protection, were treated in separate 'side agreements' attached to the main free trade agreement among those three countries in 1993. Intellectual property protection was treated in a separate chapter of the actual agreement.

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on certain products	
Specific reduction of subsidies on existing products (especially agricultural)	US subsidies on many agricultural products
National treatment of Multinational Enterprises (MNEs) in the region	All Latin American countries where this principle is not already achieved
Rules on some service sectors	Greater opening of financial markets in Latin America
Other harmonized rules on business	Foreign direct investment in all sectors and countries

The elimination of tariff barriers is likely to be agreed upon relatively easily in the FTAA discussions, because tariffs on non-critical products tend to be low, and therefore a point of negotiation that is not particularly contentious. In contrast, tariffs on certain agricultural products can be difficult to negotiate, and, therefore, may never be eliminated by the FTAA. Given the approximate average tariff of 10-20% ad valorem across Latin America,⁶ it seems reasonable to assume that eliminating such “barriers” will not be too difficult, since the existing protection is fairly limited. This is also true regarding the US, where the average tariff is less than three percent ad valorem.⁷ These kinds of restrictions tend to be the easiest to reduce or eliminate in regional and global free trade talks, since their impact is so visible and small.

A second part of the FTAA will, necessarily, be negotiation toward the reduction or elimination of tariffs on specific, highly-restricted goods, such as agricultural products. This area, as well as textiles and clothing, are the greatest sources of conflict in the FTAA negotiations. The United States, in particular, imposes tariffs on several key Latin American and Caribbean export products, particularly sugar, orange juice, and tobacco. If the United States does not agree to eliminate or reduce the levels of these tariff barriers, then a major source of gains from free trade will be lost.

A third part of the FTAA will be the attempted elimination of quotas and other non-tariff barriers, such as quotas on textiles and clothing imposed by the United States. These barriers are generally placed on the most important exports from Latin American and Caribbean countries, and thus, cause tremendous trade diversion away from the efficient producers. The US lobbies for these sectors are powerful and may be capable of stopping any progress on dismantling these barriers. Nevertheless, the quotas in clothing and textiles are scheduled to be eliminated through the global Multifibre Arrangement by the end of 2004,⁸ so

⁶ See, e.g., Interamerican Development Bank, *Integration and Trade in the Americas*. Washington, D.C.: IDB, at 11 (Jan. 2004).

⁷ See, e.g., World Trade Organization, *Trade Policy Review – United States*, WT/TPR/G/126 at 7 (Dec. 17, 2003) [hereinafter *Trade Policy Review – United States*]. This document points out that the average US tariff on a simple basis was 3.6%, but that including other preference schemes, the trade weighted average tariff was about 1.6%.

⁸ The Multifibre Arrangement was formally replaced by the WTO “Agreement in Textiles and Clothing” (“ATC”) in 1994, with a ten-year term during which the textile and clothing quotas would be eliminated progressively. The ATC ends at the end of 2004. See <http://www.wto.org/>

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this issue probably will not be negotiated within FTAA, but still should be resolved simultaneous with FTAA.

A fourth part of the FTAA will be the elimination of subsidies (that disallow or harm imports), such as those on agricultural products in the United States. This issue does not appear likely to be resolved within the FTAA discussions, since the US has taken the position that agricultural subsidies will need to be considered at the World Trade Organization (“WTO”) instead.⁹

A fifth part of the FTAA will cover the treatment of foreign multinational companies. The most common way of treating such companies under regional free trade agreements is to handle them in accordance with each country’s treatment of non-national firms. This issue may be resolved because it has not been a source of major conflict in FTAA negotiations and, actually, may have an important role in economic benefits being generated from the FTAA. If US firms are treated by the Argentine government the same as Argentine firms, and Argentine firms are treated like US firms by the US government,¹⁰ then a major step will have been taken to stimulate business investment throughout the region.

Expected Impact on Foreign Direct Investment by the FTAA

The empirical analysis of expected impacts covered by this article begins with a look at foreign direct investment (“FDI”), which differs from the usual discussions of regional economic integration in general and free trade areas. FDI is investment in controlling ownership of companies by foreign companies, whether the investment is by establishing a new plant or other facility, or by the acquisition of an existing company. Foreign direct investment into Latin America in 2002 was approximately US \$56 billion, relative to regional GDP of approximately US \$1,673 billion.¹¹ Thus, FDI was about 4% of regional GDP.

This example emphasizes that, no matter what tariff reductions are established as part of the FTAA, there will be a significant impact on FDI if an overall agreement is reached among the countries of the region. Even if negotiations to reduce barriers to imports into the US (especially on agricultural and textile products) in exchange for barrier reductions on imports into Latin American countries do not achieve much progress, a FTAA that does include provisions for national treatment of non-national companies, and for transparent regulation of companies, will be likely to have a major impact on FDI.

This impact can be seen in the context of Mexico joining the US and Canada in NAFTA in 1994. By formally agreeing to follow rules on business (e.g., incorporation rules, ownership rules, intellectual property rules)—and by pursuing other policies of economic openness—Mexico attracted very large inflows of FDI after entering NAFTA. The average annual value of FDI flows

english/docs_e/legal_e/16-tex.wpf.

⁹ See the FTAA draft agreement, *supra* note 4.

¹⁰ Foreign firms already receive national treatment in the US, and this principle is affirmed in the multilateral OECD agreements among industrial-country members of that organization.

¹¹ UNCTAD, World Investment Report 2002. Geneva: UNCTAD, 2003.

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into Mexico during 1990-1993 was US \$4 billion, while the average annual inflow of FDI during 1995-98 was US \$11.5 billion.¹² Although a crude indicator, this would mean that, because FDI into the rest of Latin America (without Mexico) averaged US \$69 billion during 1999-2002, the average FDI for Latin American countries would leap to US \$198 billion per year during 2006-2009 *ceteris paribus* with an FTAA in place. These numbers are excessively simplistic since they do not account for other events such as the Argentine crisis of 2002, the dot com crisis of 2000-2002, and other phenomena that affect FDI activity. Even so, this example points up the very significant impact that may be anticipated in FDI if the FTAA is similarly able to generate investor¹³ confidence in the rest of Latin America, as NAFTA did with Mexico.

Expected Impact of FTAA on Trade in Goods

In addition to FDI, the Free Trade Area of the Americas will impact the economies of Latin American and Caribbean countries in several different ways. The main focus of analysis of gains and losses from regional economic integration is traditionally trade in goods. When tariffs are reduced on exports within the region, the resultant lower cost of delivering goods from one country to another will stimulate added trade at the margin. For example, if tariffs are decreased from 10% ad valorem to zero, export and import activity between member countries will be stimulated by a certain percentage based on the elasticity of price, hence demand, for imports in each country, as well as the amount of imports to each country. This idea is sketched graphically in Figure 1.

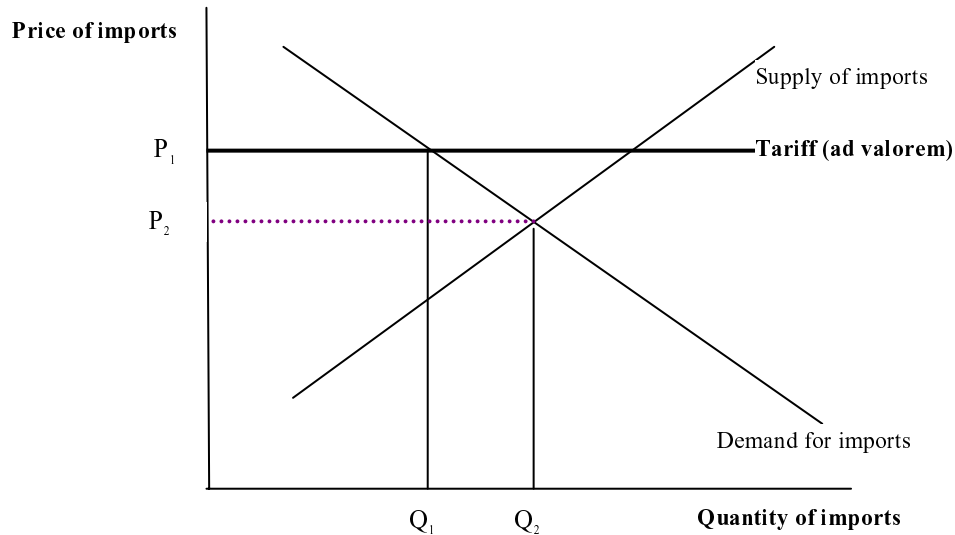
¹² These data are available from the US Department of Commerce at <http://www.bea.gov/bean/di/usdiacap.htm>.

¹³ This applies to portfolio investment as well as direct investment. Greatly increased investment into stocks, bonds, real estate, and bank deposits should be expected from a successful negotiation of FTAA, just as what occurred in Mexico under NAFTA.

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Figure 1

GAINS FROM TRADE BY REDUCING INTRA-REGIONAL TARIFFS



The gains from eliminating a tariff barrier are shown as the shift in the total quantity of the exported product (from Q_1 to Q_2), and a reduction in the price paid by consumers of the product from P_1 to P_2 . The government of the importing country loses tariff revenue as a result of this policy change, but overall welfare rises because the “dead weight loss” from overpricing the product is eliminated.

This picture fails to account for the problem of trade diversion, which is the reduction in imports from non-member countries whose exporters lose out because the tariff reduction is not applied to their products. Thus, more efficient producers in non-member countries will lose the opportunity to supply the most efficiently produced products into the free trade area if the tariff cost made the difference in cost competitiveness. In principle, trade diversion exists to prohibit the export of products from non-member countries (e.g., from the European Union or from other emerging markets) into FTAA member countries.¹⁴

How high the original tariff barriers were and how price elastic the demand was for traded products is a crucial consideration to determine actual trade creation produced by the implementation of the FTAA. As shown in Figure 1,

¹⁴ Trade diversion occurs initially if tariff barriers preclude the third-country imports. Thereafter, if within-region tariff reductions make regional trade cost-competitive, such tariff reductions continue to exclude third-party exports. Thus, trade diversion exists *a priori* due to the tariffs on imports into individual countries (i.e., local producers take the market due to protection). Then, with regional barrier reductions, regional producers come to dominate the market based on cost competitiveness.

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the demand is somewhat price-elastic near the intersection with the supply curve, with some gain in total revenue from price reduction due to tariff elimination. If the demand curve were very steep, then tariff reduction would have relatively little impact on the amount of importing. Similarly, a very steep supply curve would produce relatively little impact on imports. Conversely, a price-elastic demand for the product would produce a very large increase in imports if tariffs were eliminated.

Tariff Barriers in Latin America, 2003

Tariffs in Latin American countries varied greatly in 2003. A brief list of products that have been highly protected is given in Table 1 below.

Table 1
SELECTED TARIFF RATES IN THE AMERICAS, 2002

Country/ product	Product #1	Product #2	Average tariff, 2001
Argentina	Leather Goods 21.5%	Carpets 21.5%	9.2%
Brazil	Automotive vehicles and parts 23.5%	Shoes & Footwear 23.5%	11%
Chile	Live Animals 7%	Meats 7%	8%
Colombia	Meats 20%	Prepared Foods 20%	11%
El Salvador	Arms and Ammunition 30%	Meat and Fish Preparations 27.3%	6.4%
Mexico	Sugar and Confectionary 92.7%	Meats 82.1%	15.4%
Trinidad & Tobago	Edible Fruits and Nuts 33.4%	Fish and Shellfish 29.2%	4.6%
United States	Tobacco 90.7%	Shoes and Footwear 14.1%	1.8%
Venezuela	Meats 20%	Prepared Foods 20%	13.5%

Tariff protection varies widely across countries and among products. Tariffs in Latin American countries currently average from ten to twenty percent, whereas the average tariff in the United States is less than three percent.¹⁵ Tariffs on agricultural and food products tend to be highest everywhere, especially on tobacco, fish, and meats. This is true in the United States as well as in Latin American and Caribbean countries.

Non-Tariff Barriers in Latin America, 2003

Latin American countries are relatively open to trade as far as non-tariff barriers are concerned. Nevertheless, there are important sectors, such as media and energy, where local businesses are favored. Additionally, foreign products in some sectors are limited by quotas and health restrictions, just as in the United

¹⁵ *Trade Policy Review – United States, supra note 7.*

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States. Table 2 lists selected non-tariff barriers in Latin America in the early 2000s.

Table 2
SELECTED NON-TARIFF BARRIERS IN THE AMERICAS, 2002

Country	Product #1	Product #2	Comment
Argentina	Autos	Paper and Pulp; Footwear	Permanent and temporary quotas and import licensing
Brazil	Agricultural Chemicals	Aircraft	Import licensing requirements; local content requirements
Chile	Pharmaceuticals	Weapons	Import licensing required
Colombia	Fresh and Frozen Poultry & Parts	Powdered Milk	Import licensing required
El Salvador	Seditious Books and Other Printed Matter	Coffee Trees and Coffee Seeds	Prohibited
Mexico	Basic Agricultural Products	Petroleum	Import licensing required
Trinidad & Tobago	Poultry	Sugar	Import licensing and surcharges
United States	Sugar	Clothing	Quotas; subsidies
Venezuela	Pork	Cigarette Paper	Prohibited

Note that this list does not differ too much from the list of tariff restrictions. The main types of products that are restricted through quotas, subsidies, and import licensing requirements are food and clothing items.

The FTAA's Expected Impact on One Country—Brazil

Reduction of Trade Barriers in the United States

Brazil would benefit significantly from a reduction of tariffs in the United States in key sectors. Of Brazil's US \$60 billion in annual exports, about 25% go to the United States.¹⁶ Brazil is an important producer of orange juice, tobacco, sugar, steel, and soybeans, and the US currently has significant restrictions on trade in all of these sectors. With the advent of the FTAA, the US may agree to eliminate or significantly reduce its barriers to trade in at least some of these areas. One estimate is that if the US were simply to eliminate barriers to trade on just four products—orange juice, steel, meat and soy products—Brazil's annual exports would increase by US \$2 billion.¹⁷

¹⁶ Economist Intelligence Unit, *Country Forecast: Brazil*, ECONOMIST, Aug. 2003.

¹⁷ Roger Burbach, "Incoming Brazil President Adept at Checkmating Bush," ALAI, *America Latina en Movimiento*, December 13, 2002, available at <http://www.redress.btinternet.co.uk/rburbach16.htm>.

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An analysis of two representative sectors, orange juice and sugar, shows how a reduction of US trade restrictions would increase exports and employment in those sectors in Brazil. Increased direct employment would have significant related effects, such as indirectly generating jobs in other areas, therefore, the overall impact would be greater than the estimates provided here. However, in this analysis, only potential increases in direct employment are considered.

Orange Juice

Brazil is the world's foremost producer and exporter of orange juice by which it generates US \$1.5 billion in revenues annually.¹⁸ In 1992, 90% of orange juice imported into the US came from Brazil.¹⁹ By 2001, however, Brazil supplied only 46% of the orange juice imported to the US, having lost market share to Mexico and Costa Rica, which had preferential trade arrangements with the US.²⁰ Another reason for the decline in Brazilian exports of orange juice to the US is that the US has imposed significant restrictions on orange juice imports in the form of tariffs and subsidies.

The current US tariff on Brazilian orange juice is 29.7 cents per gallon.²¹ The Brazilian embassy reported in 2002 that the tariff was 7.85 cents per liter of reconstituted orange juice, which it estimated was equivalent to a 60% value added tariff. In addition to this tariff, the US imposes an "equalization tax" of 2.7 cents per gallon.²²

The orange juice sector currently employs 400,000 people in Brazil.²³ Because approximately seven percent of the sector's exports, and therefore seven percent of the jobs employing 28,000 people, are currently dedicated to the US, a doubling of these exports could result in a proportional increase in jobs—from 400,000 to 428,000.²⁴

Sugar

As with orange juice, Brazil is a major producer of sugar but confronts barriers to the US market in the form of quotas, subsidies, and tariffs. In 1981, the US imposed a strict quota on sugar imports, which eliminated 90% of Brazil's sugar exports to the United States. The US imposes a 244% tariff on any

¹⁸ U.S. BARRIERS TO BRAZILIAN GOODS, SERVICES AND INVESTMENT, 33-34, available at http://www.brasilemb.org/trade_investment/Barr2002_english.pdf (Brazilian Embassy, Washington, D.C., Oct. 2002) [hereinafter U.S. BARRIERS TO BRAZILIAN GOODS, SERVICES AND INVESTMENT].

¹⁹ *Id.*

²⁰ *Id.*

²¹ Laura Layden, *To Florida Citrus Growers, Keeping Tariff on Brazilian Orange Juice is Priority at WTO Talks*, NAPLES NEWS, available at http://www.ussugar.com/sugarnews/trade/keeping_tariff.html (Sept. 10, 2003).

²² U.S. BARRIERS TO BRAZILIAN GOODS, SERVICES AND INVESTMENT *supra* note 18.

²³ Abecitrus, The Brazilian Association of Citrus Exporters, at <http://www.abecitrus.com.br> (last visited Mar. 8, 2004). Also available at <http://www.arabbrazil.com/orange.htm>.

²⁴ *Id.*

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imports above the quota. As a result of this restriction, Brazil exported only 150,000 tons of its total worldwide sugar exports of 13 million tons to the US in 2002.²⁵ At a price of US \$617 per ton, this means that Brazil exported US \$92.6 million worth of sugar to the US—just 1.2% of its total exports—while selling a total of over US \$8 billion on the global sugar market.

With a reduction in trade barriers Brazil could easily double its annual sugar sales to the US, from 150,000 to 300,000 tons. This would have a significant impact on jobs in Brazil. One source estimates that for every 500,000 tons of sugar grown in Brazil, 30,000 jobs are created.²⁶ Nine thousand jobs could be created in Brazil, assuming an increase in sales to the US of 150,000 tons as a result of a reduction in sugar tariffs. This assumption greatly underestimates the potential impact of a FTAA Agreement that would eliminate US trade restrictions on sugar imports altogether.

Reduction of Trade Barriers in Brazil

Brazil also has a number of trade barriers which may be reduced with the advent of the FTAA. Key sectors that Brazil has sought to develop by means of such barriers include the capital goods, information technology, automobile, and telecommunications industries. Only capital goods and information technology are considered here.

Machine Tools/Capital Goods

For segments of the capital goods industry that have no local production in Brazil, tariffs were already reduced to four percent in 2000. However, the average tariff is 14% in segments of this industry in which there is local production.²⁷ In 2000, the total market for machine tools in Brazil was US \$809 million. Brazil imported US \$52.3 million of this total from the US, giving the US a relatively small 6.5% share of the Brazilian market.²⁸

Assuming a doubling of imports from the US with the elimination of tariffs, the US share of the market would increase to 13%. In the unlikely event that the entire increase would come at the expense of local producers, Brazil could potentially lose a proportional number of jobs in that sector. This would result in a 6.5% decline in employment in this sector. However, this is not a realistic assumption because some, if not all, of this increase in market share would come at the expense of other countries that export to Brazil, rather than from local

²⁵ Jon Jeter, *Brazilians Soured by U.S. Sugar Tariffs*, THE WASHINGTON POST, Sept. 10, 2003, at A12, available at <http://www.washingtonpost.com/ac2/wp-dyn/world/americas/southamerica/post?start=60&per=20> (Sept. 10, 2003).

²⁶ *Id.*

²⁷ Patrick Levy, United States and Foreign Commercial Service Market Research Reports, Industry Sector Analysis, *Capital Goods Industry Grows*, Apr. 9, 2001, available at www.stat-usa.gov.

²⁸ INTERNATIONAL BUSINESS STRATEGIES, *Machine Tool Industry in Brazil*, Aug. 2001, 5, available at <http://www.internationalbusinessstrategies.com/page/IBS/PROD/BRAZIL/1945> (last visited Mar. 8, 2004).

production alone.

Information Technology Sector

Brazil has maintained significant barriers to trade in this industry since at least the mid-1980s when the Brazilian government established an “Informatics Law,”²⁹ implementing the “market reserve” policy. This law codified an existing policy reserving the Brazilian personal computer and software market for local producers.

In 1991, the Brazilian government liberalized its policies and modified this law, allowing imports, albeit at tariff rates in the 30% range, as well as foreign investment in the sector. However, the government continued to promote local production by providing a number of subsidies in the form of tax incentives to companies that produced in Brazil, and met other prescribed conditions. The main benefits the government provided to such companies were exemption from Brazil’s industrialized products tax (“IPI”) [a 15% tax on the final cost of production of industrial goods], and preference in government procurement for Brazilian-made IT goods, provided that their prices were competitive with imported equivalents.³⁰ In order for companies to get these benefits, they had to invest at least five percent of their revenues from IT hardware products on research and development within Brazil. Companies also had to manufacture some portion of the end product in Brazil. For example, personal computer manufacturers built the motherboards in Brazil in order to qualify for the tax breaks.

In January 2001 another modification of the Informatics Law went into effect. The most important change in the new law was that it enacted a gradual elimination of the IPI exemption for local manufacturers to a 95% exemption in 2001, 90% in 2002, 85% in 2003, 80% in 2004, 75% in 2005, and 70% from 2006 to 2009, when it will be eliminated altogether.³¹ Changes in tariff rates have also occurred. In 2003 the government reduced the import tariff on personal computers from 26% to 16%, a rate that is supposed to remain in place until 2006. The current tariff on imported software is 15%.³²

Currently, the most rapidly growing part of the information technology industry in Brazil is the computer software sector.³³ An analysis of the effects of the elimination of tariffs in this sector indicates that the impact on Brazil could be significant. Currently, the total Brazilian market for software is US \$5.5

²⁹ ROY C. NELSON, *INDUSTRIALIZATION AND POLITICAL AFFINITY: INDUSTRIAL POLICY IN BRAZIL* 20-23 (New York and London: Routledge Press) (1995).

³⁰ Genard Burity, *Software Market: Brazil*, U.S. & FOREIGN COMMERCIAL SERVICE MARKET RESEARCH REPORTS, INDUSTRY SECTOR ANALYSIS (Feb. 2, 2003), at www.stat-usa.gov [hereinafter U.S. & FOREIGN COMMERCIAL].

³¹ *Id.*

³² *Id.*

³³ *Id.*

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billion per year.³⁴ Of this amount US \$2.5 billion, or approximately 46%, is imported.³⁵ The US alone provides US \$2 billion—80%—of Brazil's total software imports.³⁶ If Brazilian tariffs on imports of software from the US were eliminated, US software imports could double in value to US \$4 billion. In this event—if we assume that foreign competitors would be shut out of the market altogether—Brazilian production of software would shrink to only US \$1.5 billion.³⁷

This amount is only half of the current Brazilian production in this sector of US \$3 billion. Assuming that jobs would be lost proportionally to the decline in sales, the current 116,800 employees in this sector in Brazil would be reduced by half, to only 58,400. This is an unlikely outcome, given that protection of the Brazilian software sector is presently obtained by a tariff of 15%, which probably restricts a fairly small percentage of potential imports. The impact here would probably be small, unless the elimination of software tariffs signaled to the world market that Brazil was committed to open competition in this sector, thus leading to greater imports as a result.

In any event, a decline in local software production would have a significant impact on Brazil in terms of the related negative effects of so many jobs being lost in a key sector that provides its employees with relatively high wages. At the same time, however, the numerous sectors that make use of software in their business activities would now be unimpeded by import restrictions on software from the US. Therefore, Brazilian businesses would be able to make more efficient use of their resources by purchasing the most relevant and efficient software for their specific needs, regardless of its national origin. Thus, the net effect of reducing barriers to the importing of software to Brazil would not, necessarily, be to reduce Brazilian employment.

Another factor is that these overall numbers do not indicate how a reduction in tariffs would affect specific segments of the Brazilian software industry. Any jobs lost as a result would be in the weakest segments of the industry, rather than in areas such as banking automation software, in which Brazilian firms have special strengths and have developed their own niche. In such areas, the FTAA would very likely result in an increase in exports from Brazil and, therefore, an increase in jobs.

The “market reserve” policy in place in the informatics sector throughout the 1980s and early 1990s is now widely viewed as a mistake. For over a decade it hindered the development of numerous other sectors that relied on information technology. Continuing restrictions in this manner would only prolong this earlier mistake. Although some jobs in some segments of the software industry might be lost in the short run if the remaining trade restrictions are lifted, jobs

³⁴ *Id.*

³⁵ Author's calculations.

³⁶ U.S. & FOREIGN COMMERCIAL. *Supra* note 30.

³⁷ *Id.*

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elsewhere would be created from more efficient use of this technology, and the Brazilian economy would grow overall. This, in turn, would generate more jobs in other areas.

Obstacles to the Agreement: Points of Contention Between the United States and Brazil

Clearly, Brazil has much to gain from the FTAA. Nevertheless, the Brazilian government has expressed a number of concerns about the US stance toward the agreement. Brazil's main concerns are that the US does not want to discuss its agricultural subsidies and antidumping laws in the context of the FTAA negotiations.³⁸ The US position is that these issues should be discussed in the WTO.³⁹ Additionally, Brazil is concerned about the US insistence that the FTAA should go beyond reductions in tariffs to include implementation of harmonized rules throughout the hemisphere on intellectual property rights, government procurement, and investment.⁴⁰ Brazil believes that these issues should be addressed in the WTO rather than in the FTAA.⁴¹ In this section, we analyze both countries' positions on these issues, and highlight some sectors in both countries that would benefit most from a FTAA Agreement that did address these issues.

U.S. Agricultural Subsidies and Antidumping Laws

Agricultural Subsidies

Many developing countries are frustrated by agricultural subsidies in developed nations such as the US, the EU, and Japan, which severely limit the ability of developing countries to export to these developed countries. The current Doha round of the WTO is intended, in part, to reduce such subsidies in developed countries. As a major exporter of agricultural products, Brazil is strongly opposed to such subsidies and, as a result, led a group of 22 developing nations (the G22) at the 2003 ministerial meeting of the WTO in Cancún to oppose them.⁴² The Brazilian government's position is that negotiations on other issues should not continue until the developed countries make concessions on agricultural subsidies.⁴³ Since substantive concessions were not forthcoming in Cancún, the talks there broke down.

This reluctance on the part of the US to reduce its agricultural subsidies

³⁸ Paul Blustein, *Trade Talks End in Vague Accord; Framework for Americas Less Than Had Been Envisioned*, WASH. POST, November 21, pat. E01.

³⁹ *Id.*

⁴⁰ Brink Lindsey, "The Miami Fizzle: What Else But Cancun Redux?", WALL ST. J., November 29, 2003, pat. A9.

⁴¹ *Id.*

⁴² *Between Rivalry and Cooperation: Latin America and the United States*, THE ECONOMIST, Nov. 29, 2003, at 67 [hereinafter *Between Rivalry and Cooperation: Latin America and the United States*].

⁴³ *Id.*

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explains why Brazil is so determined now to make sure that this is part of the FTAA. It is likely that the Brazilian government does not want to make concessions if the US will not make concessions of its own. The US, however, does not want to reduce its agricultural subsidies in the FTAA, because that will not require any similar reduction on the part of the EU or Japan, which is why the US wants to continue to negotiate such reductions in the context of the WTO.

Antidumping Laws and Section 201

The US has domestic laws that allow it to retaliate against “dumping” (selling in foreign markets at prices below the cost of production in the home market). Brazil’s concern is that the US definition of what constitutes “dumping” is too broad, and that this legislation is frequently used purely for protectionist purposes.⁴⁴ Section 201 of the 1974 Trade Act is also of concern to Brazil. This law allows the US to impose tariffs against all countries if it determines that a domestic industry is being damaged by a large volume of imports.⁴⁵ While Section 201 is consistent with the WTO’s “safeguards” provisions, Brazil’s concern is that the US may be too willing to impose such safeguards purely for protectionist purposes, as many believed to be the case when the Bush Administration used Section 201 to impose steel tariffs in 2001.⁴⁶

Brazilian Policies on Investment, Government Procurement, and Intellectual Property Rights

Investment Liberalization

Brazil has yet to fully dismantle its barriers to investment in service industries, specifically the insurance industry. This is an important area of US concern. Nevertheless, liberalization of this sector would be consistent with Brazil’s overall trend toward market-oriented reforms, which Brazilian President Luiz Inacio Lula da Silva has maintained.⁴⁷ While a concession from the Brazilian government would seem likely, Lula is likely to use this issue as a bargaining chip to win further concessions from the US.

Government Procurement

A competitive bidding process for government contracts is consistent with the current administration’s emphasis on transparency as well as its overall emphasis on market-oriented policies consistent with WTO principles.⁴⁸ Although the Brazilian government may well be inclined to adopt the changes the US seeks, this area, too, serves as a useful bargaining chip.

⁴⁴ *Id.*

⁴⁵ Susan Rosegrant, *Standing up for Steel: The U.S. Government Response to Steel Industry and Union Efforts to Win Protection from Imports (1998-2001)*, Kennedy School of Government, 2002.

⁴⁶ *Between Rivalry and Cooperation: Latin America and the United States*, *supra* note 42.

⁴⁷ Economist Intelligence Unit, *Country Forecast: Brazil*, *ECONOMIST*, Mar. 2003.

⁴⁸ *Id.*

Intellectual Property Rights

Brazil's legislation is now consistent with WTO (and US) standards.⁴⁹ The issue is enforcement. The difficulty here is not ideological opposition to the policy but the difficulty of enforcing existing legislation.

Conclusion with respect to Brazil

The US is already Brazil's principal export market, accounting for 25.1% of Brazil's US \$60.3 billion worth of exports in 2002, followed closely by the EU at 24.9% (China was the destination of only 4.2% of Brazil's exports, followed by Argentina, Mexico, and Japan, which each received 3.9% of the total).⁵⁰ On the other hand, the EU is Brazil's principal source of imported goods, supplying 27.6% of Brazil's US \$47.2 billion worth of imports, while the US supplied 26%. Argentina, Brazil's neighbor, supplied only ten percent, followed by Japan at five percent, and China at 3.3%.⁵¹

With the FTAA, trade between Brazil and the US, which is already sizeable, will become even more significant. Nevertheless, the US will continue to hold the dominant position when it comes to winning on issues of contention between the two countries. For this reason, Brazil's chief concerns are unlikely to be substantively addressed before the 2004 US presidential campaign, during which domestic issues will take precedence. Because the current administration in Brazil seems unlikely to make concessions without getting something in return, Brazil—if only for pragmatic bargaining reasons—is also unlikely to make concessions in the short term. As will be explained in the conclusion to this article, it is likely that the FTAA will be negotiated successfully in some form by the December 2004 deadline. Final resolution of some of the more complex and controversial issues currently in dispute, however, may take considerably longer.

Lessons from a Study of Free Trade with Colombia

Based on a series of studies examining the potential impacts of free trade between Colombia and the United States,⁵² a number of useful insights can be made into the goal of understanding broader, regional free trade. The most striking findings of estimates of the impact of eliminating trade barriers between Colombia and the US were that: (1) with free trade, agricultural exports from Latin America would boom and would produce lower prices and greater availability of sugar, soybeans, orange juice, and other farm products in the US;⁵³ (2) competition from China and potentially other Asian countries would

⁴⁹ *Id.*

⁵⁰ BACKGROUND NOTE: BRAZIL, available at <http://www.state.gov/r/pa/ei/bgn/1972.htm> (U.S. Department of State, Jun. 2003).

⁵¹ *Id.*

⁵² Evan Tanner & Robert Grosse (eds.), *North American Journal of Economics and Finance* Special Issue on "Free Trade Between Colombia and the United States" (Spring 1994); Ochoa, Hector (ed.), *Estudio para la Negociacion de la Zona de Libre Comercio entre Colombia y Estados Unidos*. Cali, Colombia: ICESI, 1994.

⁵³ *Id.*

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continue to pose a huge competitive challenge to Latin American exporters of clothing, shoes, and other manufactured goods into the United States, despite free trade in the Americas;⁵⁴ and (3) barriers to the import of foreign goods, services, and companies have been declining since the late 1980s, and there is no reason to expect a change in the direction of deregulation—with or without free trade agreements.⁵⁵

The study of the sugar industry was one example of possible gains from free trade that have been disallowed by quotas and tariffs in the United States. The trade barriers with regard to sugar have resulted in sugar prices in the US that are about three times higher than in Latin America, and in trade diversion.⁵⁶ This example, though less visible publicly than US barriers to steel and auto imports, is one that could be addressed in FTAA negotiations and could produce important benefits to US consumers. In the study of Colombia, the impact would be to create several thousand jobs in Colombia in the areas of sugar cane growing, sugar milling, and distributing of sugar.

In the early 1990s free trade in sugar would have generated gains to US consumers of approximately US \$680 million resulting from lower cost, greater availability of sugar, and a reduction in producer losses of about US \$450 million from output lost to imports from Colombia.⁵⁷ The new Colombian sugar exports would come from sugar previously exported elsewhere in the world, sugar previously sold in Colombia, and new production spurred by the market growth. Under the FTAA, this same kind of impact would take place in other major sugar growing countries in the region, including Brazil, Mexico, Argentina and Guatemala.

A different kind of impact would result in the Colombian clothing and textile industry. While the broad picture was similar, with US quotas on Colombian exports of clothing and textiles, the impact of elimination of these barriers was much less due to competition from Chinese producers.⁵⁸ While Colombian producers would be positively impacted by eliminating quota limits, Chinese products would continue to enter at much lower prices, despite tariffs and quotas on such products, thus posing a continuing challenge to Colombian exporters.⁵⁹ Since the global Multifibre Arrangement governs the system of quotas on clothing and textiles into industrial countries of Europe, Japan and the US from emerging markets, bilateral free trade with Colombia in these products was seen as unlikely to remain bilateral. And once China obtains open access to the US market, the Colombian producers would have to search for market niches, such as high quality and/or high fashion clothing to compete.

⁵⁴ *Id.*

⁵⁵ *Id.*

⁵⁶ *Id.*

⁵⁷ *Id.*

⁵⁸ *Id.*

⁵⁹ *Id.*

Some Conclusions on FTAA and its Potential Impact on Latin America and the Caribbean

The successful conclusion of a Free Trade Area of the Americas among the 34 countries of the region would clearly bring overall economic benefits to the members of the group. Conceptually, dropping “artificial” barriers to international trade will allow for gains from specialization where producers in each member exporting country are more efficient than their competitors in the importing country. The overall gains from trade will benefit all participating countries, under reasonable assumptions about production costs, demand patterns, and institutional factors. However, no one expects the FTAA to achieve free trade across all products, so the real questions are: how large will the gains be in products that are deregulated and how will those gains be distributed?

Another major consideration that has not been raised, and that will be a key outcome of achieving a free trade agreement, is the credibility that will be attached to a country’s linking itself to the United States. Regardless of the specifics of the agreement, the fact that a country such as Mexico has linked itself legally to the United States in NAFTA has largely increased investors’ confidence in Mexico. That is, investors now believe that the rules of the game in Mexico are more credible and less subject to arbitrary changes than in previous times. Because Mexico has trade rules—and other rules on, for example, labor, environmental protection, and intellectual property protection—established in a formal agreement with the United States, investors perceive greater likelihood that those rules will be followed and not changed arbitrarily. This expectation of legal stability has contributed very profoundly to the large increase in US and other industrial country FDI into Mexico since 1994.⁶⁰

A similar impact can be expected in other Latin American countries that join in a free-trade agreement with the United States whether through the FTAA or bilaterally. The impact may be numerically smaller since no other Latin American or Caribbean country with the exception of Brazil, approaches the economic size of Mexico. Chile may be a good example of this impact because it recently entered into a free trade pact with the US and is expected to enjoy the kind of impact asserted here. The impact should appear not only in foreign direct investment, but also in portfolio investment [i.e., purchase of local financial instruments] from the US, EU, and Japan. The effect of these investments may ultimately dominate the overall impact of the FTAA, just as they do in the case of Mexico with NAFTA.

⁶⁰ A recent study of NAFTA by the World Bank stated: “The report’s main conclusion regarding NAFTA is that the treaty has helped Mexico get closer to the levels of development of its NAFTA partners. The research suggests, for example, that Mexico’s global exports would have been about 25% lower without NAFTA, and foreign direct investment (FDI) would have been about 40% less without NAFTA.” See Daniel Lederman, et. al, *Lessons from NAFTA for Latin American and Caribbean (LAC) Countries: A Summary of Research Findings*. THE WORLD BANK, available at <http://web.worldbank.org/WBSITE/EXTERNAL/NEWS/0,,contentMDK:20146331~menuPK:34479~pagePK:34370~piPK:34424~theSitePK:4607,00.html> (Dec. 2003).

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Overall, it is expected that the FTAA will be successfully negotiated by the countries of the hemisphere, and probably on the timetable agreed—namely by the end of 2004.⁶¹ The actual content of the agreement will probably fail to satisfy many people, especially those who want to see major tariff and non-tariff barrier reductions. Some industrial sectors will certainly remain protected. Even so, the very important benefits of having a more credible policy regime in countries of the region, due to joining with the United States, should be considerable, primarily from new direct and portfolio investment into Latin America and the Caribbean.

⁶¹ This was the date originally agreed at the Miami Summit of the Americas in 1994, and subsequently reaffirmed throughout the negotiations of FTAA. *See, e.g.*, the FTAA website at http://www.ftaa-alca.org/alca_e.asp.

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