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What's New in the New Regionalism in the Americas?

Robert Devlin
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WHAT'S NEW IN THE NEW REGIONALISM IN THE AMERICAS?

Robert Devlin *
Antoni Estevadeordal *

I. INTRODUCTION

The centrifugal forces of economic globalization in the 1990s ran parallel with centripetal forces of regionalization. While seemingly pulling in opposite directions, the two forces reflected complementary dimensions of dynamic capitalist market development (Oman [1998]). The completion of the Uruguay Round and growing membership in the World Trade Organization (WTO) was accompanied by a situation in which regional integration schemes became commonplace; indeed, practically all WTO members are now party to one or more regional accords (WTO [1995]).

Latin America is a good example of these dual forces. Between the mid-1980s and 1990s the region unilaterally reduced its average external tariff from over 40% to 12 %. The region also actively participated in the Uruguay Round and by the end of the decade all Latin American countries were members of the WTO. Meanwhile, there was a parallel wave of new reciprocal free trade and integration agreements, around twenty in number (Table 1). These trends were accompanied by a strong average growth of international trade in the 1990s (especially on the import side, the value of which expanded by 18% per annum until the Asian crisis), and a marked increase in intraregional trade (intraregional exports rose from 13% of the total in 1990 to 20% towards the end of the decade).

Regional integration in Latin America is not new; indeed, such initiatives span its history since independence. Originally, these were motivated largely by political objectives (Townsend [1988]). However, in the Post-War era economic development became the central goal. In the 1950s there was much discussion of creation of a Latin American Common Market. Following a decade of negotiations and debate, the Latin American Free Trade Association (LAFTA), comprising the South American countries and Mexico, and the five member Central American Common Market (CACM) were officially launched in 1960. The Andean Group (AG) was founded later, in 1969. While these agreements experienced some success (especially the CACM), it was short lived. By the second half of the seventies all of them were in difficulty, falling into open crisis in the 1980s (Orrego Vicuña [1977]).

Many trade theorists, following the Vinerian framework on the welfare effects of preferential trade arrangements, viewed these early Post-War initiatives with skepticism. Some of this same skepticism has reemerged during the current wave of New Regionalism. The major concerns are trade diversion and the undermining of the multilateral system. Other analysts, however, have argued that the New Regionalism is really new and demands a much broader framework

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for evaluation than the static trade creation/diversion analysis of Viner (Ethier [1998]). This paper attempts to substantiate that Latin America's recent wave of regional integration is indeed a New Regionalism, quite different from the old, and hence merits a more comprehensive perspective than in the past.

Section II of the paper examines some stylized facts of the Old Regionalism and is accompanied by an Appendix, which outlines the Andean Group's early Post War initiative, which probably approximated the theoretical ideal of the era. Section III compares the New Regionalism with the Old, drawing distinctions regarding the key features of regional integration and development policy. In Section IV, these differences are expanded by briefly considering some indicators of New Regionalism trade patterns. Section V outlines how some of the Old Regionalism characteristics linger on in the New Regionalism, and is followed by some concluding remarks in section VI.

II. THE OLD REGIONALISM

Some Stylized Facts

Some of the stylized facts about the old Post-War economic integration initiatives are:[1]

- The central objective of the agreements was to support the prevailing state-led import substitution industrialization (ISI) model of development. The model was expressive of export pessimism, skepticism regarding private markets, and great concern about the presence of, and dependence on, foreign firms. The goal was to industrialize by substituting imports behind high levels of national protection (effective protection could be 150-200%) *cum* state planning and direct public sector intervention in markets. The model prospered for a number of decades, but began to falter in the 1950s. The prevailing opinion in the region was that this was due to the small size of domestic markets.

- Given the policy objective, regional integration was to overcome the limitations of the ISI model through the creation of a regional market. The approach was to eliminate internal barriers to trade and to maintain or increase, high levels of external protection and expand industrial planning to the regional level. The explicit goal was to divert third party imports to intrarregional production and export. The sustainability of the initiatives depended on successfully opening national markets to intraregional trade.

- The basic development model of the region was inward-looking and so too was regional integration. The effects of integration on commercial links with the industrialized countries' markets and the multilateral system were not a central policy issue in view of the export pessimism of the times and the perceived "virtues" of protection. In the first episode of integration only a handful of Latin American countries were even active members of the GATT. Moreover, ideological concerns about foreign dependence created ambivalence, or outright restrictions, regarding foreign direct investment's (FDI) participation in regional schemes.

- Reflecting the primacy of national protection, the old integration's liberalization mechanisms tended to be based on multiple positive lists, the full definition of which typically emerged only after protracted step-by step negotiations (the exception was Central America). Consequently, schemes had an extremely high degree of selectivity, further complicated by complex arrangements for special and differential treatment for the lesser developed members. This, coupled with the creation of costly bureaucratic architecture inspired by the European experience (LAFTA was the exception) *cum* sectoral industrial programming, eroded credibility with the private sector.

- In terms of liberalization and trade, the old schemes generally did not succeed in meeting their most basic objectives. Negotiations and liberalization schedules bogged down quickly. Hence, effective liberalization was limited and growth of intraregional trade modest (Central America was the exception). Other disciplines often did not go beyond paper accords. The primacy of national protection in the ISI model - which, ironically, undermined the very

[1] The appendix of this paper presents a synthesis of the Andean Group Agreement. For a detailed analysis of the period see Devlin, Estevadeordal and Katona [2001].

instrument (regional integration) that had emerged to rescue it -, as well as authoritarian regimes, inefficient bureaucratic interventions, perceptions of asymmetric gains among partners, and economic and political instability all contributed to the old integration's failure to take off, or caused it to stall relatively quickly.

- Of the three initiatives, only Central America achieved substantial liberalization: 95% of all tariff lines were fully liberalized for several years. A common external tariff (adjusting rates upward) was established. Regional exports grew significantly, to peak at 26% of the total exports, until serious political problems emerged in the Group in the late 1960s and stalled the process.

III. THE NEW REGIONALISM

The Resurgence of Regionalism in the 1990s

The debt crisis of the 1980s and consequent balance of payments problems induced a deep recession in Latin America and with that a severe contraction of imports. Since intraregional imports are the other side of intraregional exports, the collapse in the Latin American economy also induced a collapse of intraregional trade and open crisis in the already flagging formal integration agreements. The general economic paralysis in the region, coupled with the emergence of a new development strategy based on market opening, correct relative prices and privatization/deregulation seemed to some to be the final deathblow for regional integration. However, to the surprise of many observers, new regional initiatives began to appear in the second half of the 1980s and a true resurgence materialized in the decade of the 1990s.

While the earliest agreements in this new wave were relatively unsophisticated and very limited in scope, the later accords of the 1990s were comprehensive, with some at the technological edge of regional integration.

The initial arrangements were negotiated as Economic Complementary Agreements (ACE) under the framework of the Latin American Integration Association (ALADI in Spanish), which was created in 1980 as the successor to LAFTA. ALADI eschewed the grand objectives of the 1960s in favor of limited agreements confined to market access via the exchange of partial or full preferences on trade in specific products with accompanying rules for use of safeguards, rules of origin, etc.

The limited scope ACE agreements in the Southern Cone evolved into the birth of MERCOSUR (Brazil, Argentina, Paraguay and Uruguay) in 1991. The MERCOSUR customs union agreement began to evolve towards greater levels of integration, with the goal of becoming a common market. It also incorporated Bolivia and Chile as associate free trade area members. Meanwhile, a Presidential initiative in the Andean Group drove the member countries to free trade in the early 1990s and to form an imperfect customs union among three of them (Colombia-Venezuela and Ecuador). The agreement changed its name to the Andean Community and set out the objective of a common market by 2005. A similar initiative relaunched integration in the Central American Common Market.

While the first ACE Agreements in ALADI were being negotiated, Canada and the United States launched free trade negotiations in 1986 that would radically transform the landscape of international trade negotiations. The agenda was vast and introduced pioneering issues vis-a-vis the multilateral trading system. For at least ten years, the U.S. had been pushing with little success to expand the GATT agenda to include trade in services, investment, government procurement, and other “new issues”. Lacking consensus at the multilateral level, the U.S. opted to pursue bilateral trade agreements in which disciplines in these areas could become a reality and influence the conduct of multilateral negotiations. Not only did the Canada-U.S. Negotiations establish model disciplines in a whole range of areas, but also new approaches to older issues, such as rules of origin and dispute settlement. On a larger level, what made the Canada-U.S. free trade area such a watershed was that negotiations moved beyond market access barriers at the border to traditionally sovereign policy areas related to how societies regulate their domestic economies.

The subsequent NAFTA negotiations were built on the innovations of the Canada-U.S. accord. NAFTA was historic because it represented the first time a Latin American country would link up with an industrialized partner. Moreover, it became a prototype for other new initiatives in the Americas during the decade. A series of new Mexican bilateral free trade areas (FTAs) throughout the region as well as one between Chile and Canada followed the NAFTA model.

Other bilateral FTAs were promoted by Chile; they first followed a more traditional market access in goods approach, but later increasingly adopted many NAFTA-like characteristics. Meanwhile, the major subregions pursued "deep" integration involving larger commitments in terms of loss of commercial sovereignty that one finds in an FTA.

This renewed activity continues today. MERCOSUR has been negotiating with the Andean Community to create a free trade area in South America and with the European Union for a transpacific FTA. Mexico recently negotiated a free trade area with the EU and is, along with Chile and Peru, a member of APEC. Chile is negotiating as well with South Korea, the EU and the US, while Costa Rica just finished negotiating an FTA with Canada. Finally, 34 countries of the hemisphere are quite advanced in negotiating a Free Trade Area of the Americas (FTAA) agreement, which is scheduled to emerge in 2005.

By looking at the objectives and modalities of the New Regionalism, clear differences with the Old Regionalism can be highlighted.

The Objective

The objective of regional integration in Latin America has shifted with the region's shift to a new overall strategy for development. In essence, the New Regionalism of the 90s is an integral part of the broad-based structural reforms that have been underway in Latin America since the mid-1980s. The central features of today's strategy include an opening to world markets, promotion of private sector initiative and withdrawal of the state from direct economic activity.

The New Regionalism's link to the structural reform process is most clearly observed in trade liberalization. In effect, regional integration is the third tier of a three-tiered process. As mentioned in the introduction, Latin America's average external tariff was radically reduced between 1985-95 (>40% to <12%). The average maximum tariffs in the region fell from more than 80 percent to 40 percent with only two countries presently applying maximum tariffs of up to 100 percent on a small number of products. Tariff dispersion, on average, has declined from 30 percent in the mid-1980s to a low of 9 percent today. Both the highest average rate and the highest dispersion rate, as measured by the standard deviation, are currently under 15 percent.[2]

The second tier is at the multilateral level. A decade of multilateral Uruguay Round negotiations ended in April 1994 with the signature in Marrakesh of the Final Act. That Round was concerned with two basic issues regarding market access: (i) reducing obstacles to trade in goods and services and (ii) making the new levels of market access legally binding under tougher WTO regulations and procedures. In the area of tariff liberalization, this latest round of the GATT

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[2] There are still, however, some important peak tariffs. On average, approximately 22 percent of tariff lines are subject to rates above 20 percent. Moreover, there are still some countries with maximum tariffs above 70 percent.

negotiations implied a very substantial commitment on the part of Latin America to dismantle import barriers and adopt new disciplines. The central obligation with respect to tariffs required countries to "bind"' them to a specified maximum. The latest round resulted in a significant increase in this commitment. In the case of developed countries, the increase went from 22 to 72 percent; and in the case of countries in transition, it went from 78 to 98 percent. Latin America as a whole agreed to bind practically *all* tariff lines (albeit, above applied rates).

Liberalization at the unilateral and multilateral levels has helped to better incorporate Latin America into the world economy. In the 1990s, extraregional imports grew at a relatively high average rate of 18 percent per annum, more than tripling to $280 billion. This was 50 percent faster than the growth of extraregional exports. The region's extraregional import coefficient (respect to GDP) rose as well, from 21 percent in the late 1980s, to 34 percent 1997.

For a region with a modern history of closed economies, this two-level opening was clearly dramatic. While bringing benefits of more competition, lower input costs and enhanced consumption possibilities, the opening also introduced new difficulties. These included important fiscal costs, real resource costs from capital and labor made newly redundant, as well as political costs due to shifting domestic economic coalitions and the real or perceived threats of globalization. The large and rapid external liberalization during the decade could initially lean on considerable "water" in national tariff schedules, while needed fiscal adjustments were quite straightforward. But with tariffs having moved closer to differential margins of competitiveness between home and abroad and fiscal options narrowing, the political economy of trade liberalization became considerably more challenging during the course of the 1990s.

Government authorities have used support for regional integration as a signal of their continued commitment to liberalization even when political or economic conditions for further unilateral opening are difficult and when reciprocal multilateral initiatives are in a transitional phase, as has been the case since the end of the Uruguay Round.

In this context, regional integration has become a vital third tier of liberalization that has helped ensure continued momentum in the process. The fiscal implications of preferential liberalization among Latin American neighbors are less burdensome because typically levels of trade are initially small due to history as well as the legacy of protection. Political resistance to regional integration also can be less entrenched. It takes place within a delimited and familiar market space which reflects more symmetric competition than is found in the international arena. Moreover, there is a compensatory element of reciprocal exports in tandem with reciprocal imports, making for a potentially more balanced fallout of short-term costs and benefits. Regional opening can even be politically popular due to domestic receptiveness to "getting together" with certain neighbors (Devlin and Ffrench-Davis [1999]).[3]

Hence, today regional integration is being used as an effective policy tool to deepen liberalization, further reduce average levels of protection, and reinforce the winds of competition. Figure 1 illustrates for the MERCOSUR partners, Argentina and Brazil, how regional commitments are working in tandem with unilateral and multilateral processes to create more open economies.

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[3] This can be because you love your neighbor, or because you are tired of conflicts with your neighbor and hope trade will support a broader political initiative for peace.

Regional based rules and peer pressure are also useful to "lock-in" liberalization commitments that under unilateral policy alone might be more easily reversed. It is true that some countries, largely in response to severe fiscal or balance of payments shocks, have temporarily increased protection during the 1990s. However, such measures have usually exempted regional integration partners, due to trade treaty obligations. Customs unions like that found in MERCOSUR have made it difficult (but not impossible) for any member country to raise tariffs on third parties since a plurilateral consensus must be reached.[4] The lock-in effects of regional schemes (in combination with WTO bindings) have contributed to anchoring the trade liberalization process and retard backpedaling.

From the above it is clear that, instrumentally, the new regional integration is dramatically different from the older schemes. However, the New Regionalism contrasts with the old in the other dimensions as well.

- Attracting foreign direct investment (FDI). The old fears of dependence on FDI have evolved into an appreciation of FDI's contribution to enhanced international competitiveness and access to export markets. In an era of globalization there is an intensive worldwide competition for this type of capital. Today the creation of a regional market like MERCOSUR are being deployed not as a way to restrict, or program, FDI as in the past, but rather as a way to distinguish countries from the world pack and attract FDI (Ethier [1998]). Agreements which have successfully created a regional trademark, such as NAFTA and MERCOSUR, have become successful beacons for attracting this type of capital (ECLAC [2000]).

- Intraregional trade. The creation of a regional market has promoted trade and investment activity that is generating dynamic transformation effects in productive sectors. This is something that the old integration sought, but largely did not achieve due to, among other things, domestic price and regulatory distortions and the inability to open the regional market. With respect to international markets, the strong growth of intraregional exports reflects a more diversified product mix, a greater participation of differentiated, knowledge-based manufactured goods, and expanding specialization and scale economies through intra-industry trade[5]. Firms have reoriented their marketing, investment and strategic alliances to exploit the regional market. Moreover, trade in some sectors, such as dairy and textiles, is a welcome outlet given severe protection in international markets. These dynamic transformation effects are contributing to more competitive economies which can face the challenges of globalization.[6]

- Geopolitics. The outward orientation of Latin American policies has raised demand for more active and strategic participation in hemispheric and world forums. Regional integration has allowed countries to cooperate and be more effective global players. In the Free Trade of the Americas process, for example, the MERCOSUR, Andean and Caricom countries now each

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[4] Mexico has exempted NAFTA partners from some recent increases in protection. In MERCOSUR, community obligations initially made it more difficult to extend protection to their partners and third parties, although the recent crisis in Argentina overwhelmed the discipline of that group's common external tariff.

[5] In 1996, manufactured goods exports in intra bloc trade was considerably higher than their share in total trade: CACM (70% vs. 30%); Andean Community (63% vs. 21%) and MERCOSUR (61% vs. 48%) (IDB [1996b]).

[6] For analysis that captures some of the dynamic sectoral effects of regional integration in Latin America see Hasenclever *et. al.* [1999]; Nofal and Wilkinson [1999]; Echavarría [1998] and Gereffi and Martínez [1999].

negotiate as a bloc, giving them more impact in the negotiations than if each country had acted alone. Regional integration and trade also has helped democratic countries seal hard won peace on frontiers with a tradition of military conflict. It moreover has set up a solidarity network (through democratic clauses) to protect the region's still young democracies. MERCOSUR's experience is a good example on both accounts: its formerly conflictive borders are now the most pacified and heavily trafficked in Latin America. The old integration was not able to achieve this because the primacy of protection blocked growth of commercial trade between neighbors, while many of the sponsors of the initiatives were often nationalistic authoritarian regimes with a vested interest in restricted borders, territorial disputes and non-democratic processes.

Finally, the new face of regionalism is well exhibited by a phenomenon that would have been inconceivable just ten years ago: Latin America linking up in reciprocal trade agreements with the U.S. and other industrialized nations. These "big market" agreements have more formidable costs and challenges than intra-Latin American agreements. The liberalization is sharply asymmetric because the industrialized economy is already very open. Given that the more developed country is already a major trading partner, the loss of tariff revenue and resource transfer for the Latin American country is important. The ensuing competition moreover is world class. Why do it? Because an agreement with a credible industrialized country provides a powerful anchor that greatly magnifies many of the aforementioned positive effects of integration on structural reform, such as lock-in and signaling, attraction of FDI, productive transformation, protection of democracy, etc. The agreement is also a way to eliminate peak protection in sensitive sectors of the industrialized partner and create binding rules-based legal mechanisms for access to the industrialized market and dispute settlement. In sum, these types of agreements are seen as an especially powerful tool of economic and political transformation.

Modalities

Liberalization Mechanisms of Recent Agreements

- Tariffs -

This subsection will outline some of the most relevant features of the structure of the liberalization process emerging from the agreements of the 1990s. Given the very large number and diversity of agreements during this period, a core group of representative accords has been selected in order to derive from them some general stylized features of the New Regionalism. The analysis will focus more on the intraregional liberalization of selected agreements than on the formation of common external trade policies.

The new generation agreements in Latin America, following in many respects the NAFTA model, moved towards tariff phase-out programs that are based on straightforward preprogrammed schedules at the outset, which are relatively quick, automatic, and nearly universal. This contrasts quite sharply with the laborious step by step development of positive lists of LAFTA and the byzantine schedules of the AG with its important exceptions.

In the new integration agreements a high percentage of products are liberalized immediately, and for products regarded as "sensitive", special phase-out periods are agreed to, or lists of

exceptions established. The negotiations usually started with an agreement on a base rate or base level from which phase out schedules are applied. Those base rates usually coincide with the MFN applied rates to third parties at the time of negotiations. This has been the case, for instance, with NAFTA after initial discussions about using GATT bound rates were rejected. In other cases, such as the G3 (Mexico-Colombia-Venezuela) negotiations, it was necessary to take into account previous preferences negotiated under other agreements in order to establish the initial base rate. These rates also could be negotiated so that phase out schedules would begin from lower rates. In a second stage, parties defined several tariff elimination programs or phase out schedules to bring base rates to zero in a specified time period.

There has been very little empirical analysis of the depth and the effects of this new preferential liberalization in Latin America. The degree of liberalization achieved to date can be illustrated in Figure 2. It shows the average level and dispersion of the preferential margins, by sector, resulting from bilateral preferential negotiations between Latin American countries in two benchmark years: before the new regionalism started and for the year 1995.[7]

In 1985 most of the region still had relatively high MFN tariffs. This is because the process of unilateral liberalization had not yet begun and the multilateral negotiations of the Uruguay Round had not yet been completed. At the same time, most of traditional preferences negotiated under the ALADI framework and other subregional agreements had eroded over time and had not been renegotiated, partly due to the trauma of the debt crisis. As a result, the degree of preferential liberalization among countries was quite low, with the average values of margins of preference being below 5 percent.

The picture changes dramatically ten years later. The MFN tariffs had already been reduced through unilateral and multilateral policies. However, parallel to this, most preferential relations had been renegotiated under the new agreements, lowering preferential tariffs even more than the substantial drop in tariffs to third parties. Thus despite sharp MFN tariff reductions, average levels were somewhat higher than before, just around 5 percent. However, the most important difference is the higher dispersion for maximum values, meaning that there is more variance in the discriminatory policies pursued by countries for at least selected sectors. It is beyond the scope of this paper to attempt an evaluation of the effects of these tariff policies on trade patterns, particularly the variance across sectors, but in some cases they probably are not of a second order.

Table 2 presents the degree of trade liberalization achieved by 1995 for a number of agreements as well as an estimate (assuming zero elasticity of imports to tariff liberalization) of the percentage of imports by product in ten years time when full liberalization is reached. First, it is important to note that the table reconfirms what was stated earlier, i.e., in many cases the levels of bilateral imports subject to liberalization were a relatively low share of total imports. Meanwhile, although most programs will eliminate internal tariffs for almost all products by 2006, the internal structure of the phase-out programs varies widely across agreements. As for

[7] For each product category, defined at the ISIC 5-digit level of desaggregation, the margin of preference (MP) is computed for a selected number of the bilateral preferential relations among countries in the region. Then, for each product the maximum, the minimum and the average MP levels in all those bilateral relations are selected. Finally, the distribution of these maximum, minimum and average values across agreements are plotted for an aggregated sector defined at the ISIC 2-digit level.

the average percentage of exceptions, it is low, around five percent, which contrasts favorably with most of the old agreements.

Figure 3 normalizes the phase-in of internal liberalization of all agreements (for which the authors have data) as if all had started on the same date. It then presents the percentage of items and bilateral trade that will be subject to dismantling of tariffs over a ten-year time period, the usual GATT consistent framework for creation of a free trade area.[8] What is evident from the figures is the different built-in speeds of each agreement. For some agreements, more than fifty percent of the products become free of tariffs during the first year of implementation of the agreement. For others, those percentages will not be reached until the 5th year or later. Four patterns are observed. First, there are the U.S. and Canadian sides of NAFTA *vis-a-vis* Mexico, the Mexico-Costa Rica FTA and the Mexican side of its FTA with Bolivia, all which liberalize a high percentage of trade the first year. Then there are the Chile bilaterals and the Bolivian side of its Mexican FTA, which achieve high levels of liberalization by year five. A third pattern is the Mexican side of NAFTA, which undertakes the bulk of its opening between years 5 and 10. Finally, the G-3 did not undertake much liberalization at all until after year five. The figure also displays a relatively high degree of reciprocity in liberalization schedules with the notable exception of NAFTA and the Mexico-Bolivia FTA.

The picture changes when considering how much of bilateral trade will be affected by the elimination program. Even with the caveat that the projections are based on the import structure of the initial period and therefore assume an unrealistic null elasticity of imports vis-a-vis tariff elimination, the data in the bottom half of Figure 3 reflect a much higher degree of variance and no discernable pattern regarding the speed of the programs and the levels of reciprocity. When the examination of the same agreements is done sectorally (not shown), one observes that the intra-sectoral dispersion among the agreements is quite marked and that agricultural products generally have the most gradual liberalization schedules. Finally, with few exceptions, most of the bilateral trade in the selected agreements is fully liberalized within a ten-year period.

-Rules of Origin (ROO)-

It is important to note that tariffs are only part of the story. Because of its discriminatory nature, a preferential free trade agreement must distinguish “non-member originating” from “member originating” products in order for a good to be granted the preferential access. The importance of this rises when there are multiple preferential agreements with several partners. Indeed, the growth of international trade in goods that are not manufactured in a single country has raised the issue of the rules for determining the “origin” of traded goods into one of the most important and complex areas of preferential market access negotiations. The economic analysis of rules of origin has been relatively limited in both formal modeling as well as empirical testing. It has been argued, from an analytical point of view, that the way in which rules of origin are defined and applied within modern preferential agreements plays an important role in determining the degree of protection they confer and the level of distortionary trade they produce.[9]

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[8] In reality, of course, the phase-in programs are discrete in time rather than continuous. However, for visual purposes the figures smooth out the discrete phases with a continuous fitting line.

[9] For some of the more analytical work in this area see Garay and Quintero [1999]; Garay and Estevadeordal [1996], and Cordoba [1996].

Although one of the key features of the New Regionalism that contrasts with the old processes is the very general application of automaticity and universalism in the tariff elimination programs, it has also introduced an extremely selective procedure through the discretionary application of rules of origin. In the old agreements, mostly under the ALADI framework, there was a general rule applied across-the-board based on a change in tariff classification at the heading level or, alternatively, a regional value-added rule of at least 50 percent of the f.o.b. export value.[10] In the New Regionalism, mostly attributable to agreements that follow the NAFTA model of rules of origin, one finds a system of general rules plus additional product-specific rules negotiated at the 6 digit level of the Harmonized System (HS).

There are two basic criteria to determine origin. The criterion of "wholly produced", where only one country enters into the consideration of origin, and the criterion of "substantial transformation", where two or more countries have taken part in the production process. The first criterion applies mainly to natural resources which have been entirely extracted from the soil or harvested within the country, or manufactured there from any of these products. Such products acquire origin by virtue of the total absence of the use of any second country components or materials. Even a minimal content of imported components will imply losing its status of "wholly produced".

The "substantial transformation criterion" has been more vague, leaving discretion in its application to national customs authorities. The negotiations of rules of origin under NAFTA were mostly concerned with giving more precision to ROO through the use of three methodologies: (i) a change in tariff classification, requiring the product to change its tariff heading (chapter, heading, sub-heading or item) under the HS in the originating country; (ii) a domestic content rule, requiring a minimum percentage of local value added in the originating country (or setting the maximum percentage of value originating in non-member countries); and (iii) a technical requirement, prescribing that the product must undergo specific manufacturing processing operations in the originating country.

Table 3 measures the degree of specificity provided in ROO, computing the percentage of tariff lines that use a specific pattern. It is important to note that there are significant differences among the rules when patterns of rules of origin are compared across agreements. The FTA between the United States and Canada already had an important degree of specificity. However, NAFTA rules are even more complex when one considers the degree of exceptions introduced at different changes in tariff classification. Also, and this is not reported in the table, the specificity introduced in NAFTA is much greater when one takes into account the methods of computing regional value content, or other administrative provisions in implementing the system. The NAFTA model was exported to the G3 agreement, Mexico's bilaterals with Costa Rica, Nicaragua and Bolivia as well as Chile's recent bilaterals with Mexico and Canada. Meanwhile, rules introduced under the MERCOSUR and MERCOSUR bilaterals with its associate members (Chile and Bolivia), as well as the Central America Common Market's rules of origin, can be considered intermediate models between the two extremes of ALADI and NAFTA.

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[10] However, the old ALADI framework was only loosely enforced.

From one angle, the New Regionalism's deployment of ROO is a step backwards from the simpler arrangements in the old regional agreements. The growing use of complex rules of origin highlights the fact that modest specificity in the tariff phase out programs of the New Regionalism has been at least partially offset by a built-in selective instrument through product specific rules of origin. In NAFTA there is empirical evidence of selective protection through the agreement's rules of origin (Estevadeordal [1999]). If the protectionist and investment diverting effects of rules of origin are serious, one could indeed face effects equivalent to the very distortionary tariff-based instruments under the old regionalism**.** The spread of rules of origin also raises the issue of transparency and transaction costs. On the other hand, as we have noted, the New Regionalism is much more than trade as such. To the extent that agreements are supportive of overall structural reform, ROO could be considered endogenous protection that guarantees both the achievement and sustainability of an agreement. In any event, to draw firm conclusions in this area one must undertake difficult empirical evaluations of the degree of "bite" in the region's ROO systems[11] and weigh that cost against other benefits derived from the agreement.

Other modalities

Aside from the generally more rapid and universal nature of liberalization, coupled with use of more specific ROO, there are several other distinguishing features of the New Regionalism vis-à-vis the old.

- Market driven. The expansion of the regional market is being driven primarily by the private sector and market-based decisions on intraregional export and investment. Any transformation effects derived from regional integration are being achieved without the state planning and programming that characterized earlier initiatives.

- Special and Differential Treatment (S&D). In the agreements of the 1990s there has been relatively little attention to S&D for the least developed countries. Arrangements are modest, if they exist at all. The most typical arrangement is an extended phase-in of one or more disciplines. For example, in MERCOSUR, Paraguay and Uruguay received an additional year to complete the tariff elimination of sensitive products, while Paraguay was allowed to place 25 percent more product categories on a temporary list of exceptions to the agreement's common external tariff, with six additional years to incorporate them. Permanent derogations also exist --for example, Bolivia is outside of the Andean CET-- but they are not common.[12]

- Cascading. With the discovery of new markets and positive experience, strategic considerations have led to cascading effects in which one agreement leads to another with upgrading of liberalization beyond the old integration's traditional free trade in goods to include so-called new issues. One example is Chile. It began by integrating with Mexico in a

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[11] Garay and Quintero [1999] and Cordoba [1996] have made advances in this area.

[12] For a complete summary of special and differential treatment in the new regional accords, see OAS [1996]. For the old accords, see Lizano [1979] and Devlin, Estevadeordal and Katona [2001].

simple ALADI-type FTA. After signing a number of similar agreements with other countries in the region, it attempted to enter the more comprehensive NAFTA. When this failed due to the U.S.'s lack of Fast Track authority, it signed a NAFTA-like agreement with Canada. Chile then upgraded its simple Mexican FTA to NAFTA-like standards and is currently engaged in new negotiations with the U.S. Good experiences in the hemisphere also led to negotiations with South Korea and the E.U.

- Scaled Down Architecture. The old integration arrangements tended to prematurely foster a complex and costly institutional structure. The new agreements tend to promote minimalist intergovernmental arrangements. Moreover, traditional agreements such as the Andean Community and the CACM have reformed the over-sized institutional structures inherited from the past.

- The resurgence of regional integration appears to be more sustainable than the early Post War experience. The commitments to liberalization processes have, on the whole, been effectively implemented and have stayed on track with little backpedaling, even during the difficult economic conjuncture of 1998-99. This is a major contrast with the old integration which was big on agreements but short on implementation and sustained commitments.

IV. TRADE INDICATORS

There are some additional structural differences between the early Post-War period and more recent integration initiatives that are revealed by looking at selected trade indicators. The measures presented below are, as usual, open to interpretation and can only offer some hints of possible trends, or underlying forces, behind the implicit dynamics of any trade agreement. It is also difficult to separate causality between periods, although in this case one can take advantage of the 1980s debt crisis, which served as a kind of "laboratory trick", equivalent to a temporary shutdown of regionalism to be restarted again few years later. Attention is focused on two areas. First, is an evaluation of the existence of some ex-ante "anticipatory effects" on trade flows even before the agreement was implemented. Second, the two periods of regionalism are examined in terms of the "intensity" of regional integration achieved through time.

Anticipatory Effects

This type of analysis compares the agreements in terms of the presence of the so-called anticipatory effects in the trade pattern. We follow Freund and McLaren [1999] in order to examine the existence of trade ratios with an "S" shape pattern, indicating an accelerating and then decelerating growth of intraregional trade around the formation of a trade agreement.[13]

Freund and McLaren found an "S"-shaped curve for some agreements (EU, EFTA, MERCOSUR and NAFTA). The interpretation is that, when the initiative is credible, as the date of accession looms near, a country and its private sector will accelerate trade with its future partner countries, and after accession, trade with the said members should flatten out. Recent theoretical work on the existence of sunk investments made in anticipation of accessions supports this view. Given the different scope, modalities and credibility of the older versus the new agreements, those effects may be of different magnitude, much stronger in the case of the new agreements, partly because of the greater credibility and domestic receptiveness to the openness of the New Regionalism.

For the purpose of this paper, it is interesting to note that in general, countries entering "old" agreements exhibited the "S" behavior to a lesser degree than when the same countries entered into "new" agreements (Devlin, Estevadeordal and Katona [2001]). Mexico is a striking example

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[13] The share of a country's total trade with the members of a given block is defined as follows:

$tr^{t}_{i,j} = trade^{t}_{i,j} / trade^{t}_{i,world}$

where

$tr^{t}_{i,j}$ = share of country i's trade with block j at time t;

$trade^{t}_{i,j}$ = i's imports from j plus i's exports to j at time t;

$trade^{t}_{i,world}$ = i's imports from the world plus i's exports to the world at time t;

The indices are computed as the difference between actual shares at time t with respect to the share at the time when the agreement is implemented using aggregate trade data from the IMF's DOTS database.

of this (Figure 4). This may reflect the fact that the "old" regionalism was used as a means of extending the domestic import substitution industrialization (ISI) model to the regional level rather than enhancing trade among partners as such. The exception is the CACM (Figure 4), perhaps because some of the features of its 1960 intraregional liberalization scheme approximated the commitment structure of the New Regionalism. In any event, significant anticipatory effects can be observed in most cases of New Regionalism, indicating that the current regional liberalization processes are perhaps more credible: they are integrated into the three tier liberalization process described earlier and form an integral part of commitments to structural reform.

Trade Intensity

To measure the degree of regional integration over time one can deploy two regional intensity ratios, one based on exports and another based on imports. The regional intensity indexes that we have used were theoretically developed by Anderson and Norheim [1993] and are defined as the share of a country's exports (imports) to region j relative to the share of region j's imports (exports), net of country i, in world imports (exports), net of country i.[14]

Trade intensity indices are a better measure of reorientation than trade shares because they control for the overall growth in members' trade relative to world trade as well as for the number of members in the accord by controlling for the size of the block. The index describes how much a country trades with other members of the agreement relative to how much it trades with the rest of the world. A trade intensity index of unity implies that country i's share of trade with the other members of the agreement is identical to the partner's share of trade with the rest of the world. When the index takes on values above (below) unity the countries have greater (smaller) bilateral trade than would be expected based on the partner's share in world trade.

Devlin, Estevadeordal and Katona [2001] report the intensity indexes for all countries in Latin America during 1960-98, with respect to their immediate sub-regional agreements as well as LAFTA/ALADI (except for Central American countries). In order to illustrate the potential effect of regional trade agreements, the analysis depicted the development of the index for each country for all years, even though not all of them participated in the specific agreement during the whole period (i.e., Chile in the Andean Group and MERCOSUR).

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[14] The import and export intensity indexes, respectively, are as follows:

$IM_{ij} = x_{ij}/m_j$

where

x_{ij} = the share of country i's exports to the region j

m_j = the share of the region j in worlds imports (net of country i's imports)

$Ix_{ij} = m_{ij}/x_j$

where

m_{ij} = the share of country i's imports from the region j

x_j = the share of the region j in worlds exports (net of country i's exports)

The index is very useful in order to analyze the long run dynamics of intra-bloc trade, since implicitly one is controlling for factors such as relative income growth, distance, language and other factors, which would be typically included in a Gravity model.[15] Then, examination of trade intensity indices over time accomplishes the same purpose as estimating a Gravity equation in a more parsimonious way (See Freund and McLaren [1999], for an analytical derivation of trade intensity indices using a gravity equation).

For some countries, the effect of the new regional initiatives seem to have been very important; particularly noteworthy are the cases of the major trading partners in the South American agreements, i.e. Argentina and Brazil in the case of MERCOSUR (illustrated in Figure 5), and Colombia and Venezuela in the case of the Andean Community. Moreover, the fact that there is a co-movement of the import and export series indicates that there is not a systematic bias between the two, and therefore less concern for potential systematic trade diversion effects. Other studies also have suggested that the New Regionalism in Latin America and elsewhere has, in general, not been substantially trade diverting (Soloaga and Winters [1999]; Robinson and Thierfelder [1999]; Nagarajan [1998]; and Devlin, Estevadeordal and Katona [2001]).

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[15] Assuming that the elasticities of trade with respect to income and distance are constant over time, the gravity equation defines the movements in excess trade over time as those movements that cannot be explained by income growth since distance does not change. There are of course other factors that can explain those movements, among others, the real exchange rates. However, we take the view that some of those price effects will be more important in the short to medium run rather than long-run lasting factors. In other words, we interpret the long run trends in the indices as due more to structural factors in the way different economies are linked through formal trading arrangements, while short-to-medium run fluctuations can be attributed to variables such as exchange rate movements.

V. SOME "OLD" FEATURES OF THE NEW REGIONALISM

Notwithstanding the advances of the New Regionalism, it still exhibits some lingering "old" characteristics, which could be undermining the full potential dynamic and non-traditional effects of the new approach to regional integration:

- Latin America still often makes excessive use of "irregular" unilateral measures to deal with disruptive trade imbalances in their regional agreements. This is sometimes due to the fact that the agreements have made no provision for safeguard clauses, indeed even during periods of tariff phase out (Table 4). Although there have been some signs of improvement,[16] there has been insufficient attention to the use of formal dispute settlement. Past practice in Latin America was to settle disputes in back rooms through diplomatic channels. The diplomatic route is still excessively used today. This approach perhaps made sense when the state was the primary economic actor in the region. However, today integration is market driven; growth of private sector investment in the regional markets would be enhanced by a more modern and transparent rules-based systems.

- The old regionalism was characterized by significant selectivity in its tariff liberalization process. While the New Regionalism is more universal and automatic in this regard, there is considerable sectoral selectivity in some product specific tariff phase outs and preferences across different partners. Another source of selectivity is the increasing use of product-specific rules of origin. Moreover, rules of origin lack the transparency of a tariff. All the above --but especially rules of origin-- are contributing to a "spaghetti" bowl of agreements which contributes to transaction costs and reduced transparency. There clearly is a need to empirically evaluate the effects of rules of origin. The WTO could help by putting rules of origin under the umbrella of Article 24 and expanding its development of a system of non-preferential rules of origin to include the preferential type (Serra *et. al.*, [1996]). Meanwhile, creation of an FTAA in 2005 would help to clean out and harmonize many of the more shallow FTA's in the hemisphere.

- One solution to the rules of origin problem is the formation and consolidation of a customs union. The old regionalism encountered tremendous difficulties in establishing and maintaining a common external tariff. It has proved difficult in the New Regionalism too. The common external tariffs in all subregions were "imperfect" when established in the early 1990s and some have suffered serious perforations since then. In Central America, the CET established in the 1990s began at 95 percent of the tariff universe, but now involves only 50 percent, or 70 percent if Nicaragua is excluded (Granados [1999]). MERCOSUR started out with a CET on 88 percent of the tariff universe (INTAL [1996]); however, a significant number of perforations have occurred in recent years, i.e., the recent withdrawal of Argentina from the CET. In the Andean Community about 85 percent of the tariff lines were incorporated in the CET; exceptions were to be eliminated in 1999, but this was postponed. Meanwhile, aside from a significant number of items outside the CET, rules of

[16] For example, the AG Tribunal was created in 1984, but went unutilized until 1996. Starting in this latter year activity has increased significantly, with some 30 cases of non-compliance being sent to the Tribunal (authors' communication with the Andean Community Secretariat, 1999).

origin are also necessary because no subregion has a common system for collection of tariff revenue.

- Notwithstanding 15 years of market-oriented economic reforms, the Latin American economies still suffer from major bouts of instability (Mexico, Brazil, Ecuador, Argentina, etc.), with consequent negative effects for regional integration.

- The dream of a common market still captures the imagination of Latin America. However, the dream, even though perhaps still difficult to realize, is now often more realistically cast in terms of geographical blocs that have, at least in the medium term, potential strategic economic and political potential for effective future development.

VI. CONCLUSIONS

The New Regionalism contrasts fundamentally with the old. Its instrumental role is geared to supporting structural reforms to make economies more open, market based, competitive and democratic. Given that regional liberalization has worked in tandem with unilateral and multilateral trade opening and a liberalized economic environment for the private sector, the new trade agreements enjoy a credibility that the old regionalism did not due to the latter's underlying vocation for protection and state intervention. The scope of liberalizing disciplines in the New Regionalism tends toward a comprehensive, more rapid, universal and sustained system in terms of effective application. The New Regionalism also is designed to attract foreign investment, not restrict or control it. Moreover the New Regionalism has more functional and cost effective institutional arrangements. Finally, the new initiatives better support important non-economic objectives such as peace, democracy and effective participation in international forums.

Regional integration, like any major structural transformation, has costs -- many of which are up front -- that must be assumed and should be minimized to the extent possible. But with the new role of regional integration in Latin America, the matrix of objectives and expected benefits have changed dramatically. In this sense Ethier [1998] is correct in arguing that the simple Vinerian approach to the evaluation of regional schemes is overly narrow and development of a broader conceptual framework is needed.

Many theoretical static Vinerian critiques are especially limited. They typically derive negative conclusions about regionalism, while ignoring key features such as parallel reduction of external and internal tariffs, product differention, competition and market shares, investment and learning by doing, externalities etc, all of which are central economic dynamics of the New Regionalism. Costs, such as the trade diversion and redistributive effects of lost tariff revenue are consequently stressed and the benefits underestimated. Risks for the multilateral system are also exaggerated because regionalism and multilateral negotiations aim at entirely different outcomes(the former feeds on the objective of eliminating barriers among some countries while the latter proffers reduced barriers among all countries). Moreover, the two processes are increasingly interacting and mutually support each other. For example, an FTAA will be difficult to realize without advances in multilateral negotiations on agriculture, which in turn, probably requires the initiation of a new round.

To assess regional integration it is necessary to increase analytical capacity for the effective evaluation of events in this broader framework. This will require, among other things, much better empirical observation and analysis than we have today about what is actually happening on the ground (i.e. sectoral developments that capture the dynamic impacts) in Latin America's regional integration processes.

APPENDIX TO SECTION II

An Example of the Old Regionalism: The Case of the Andean Group (AG)

1. The Background

In the region's negotiations during the 1950s, there were serious discussions about forming a common market in Latin America. Consensus was not reached, however, and LAFTA was one of the compromised outcomes. The agreement originated at the initiative of Argentina, Brazil, Chile and Uruguay in the late 1950s, and incorporated Bolivia, Colombia, Mexico, Paraguay, Peru, and Venezuela as well. Although some countries had hoped it would evolve into a deeper region-wide common market (Urquidi [1960]), the agreement set out the immediate expressed goal of establishing a free trade area within twelve years.

The proponents of integration never considered LAFTA an ideal arrangement. It was a relatively weak agreement as it compromised depth for the sake of breadth of membership. It involved states with a wide variety of levels of development, size, political interests and with geography yet untamed by an effective transport and communications infrastructure. The large countries, such as Argentina and Brazil, were focused on securing a ready market for their existing trade in goods, while the smaller countries were more interested in creating new industrial development through programming and concessions for creating favorable conditions for their development within the region. The interests of the larger countries generally prevailed in the final agreement.

As a result, LAFTA was merely an agreement on a *framework* for the subsequent negotiations to free trade among the member countries. There were also provisions for industrial sectoral agreements. At the time of its signing no trade was liberalized. Governing bodies were intergovernmental and voting was by two-thirds majority, but every delegation possessed a veto. In addition, there was a weak secretariat.

Trade liberalization in LAFTA was based on the principle of developing positive lists for reciprocal trade concessions. It was hoped that, through bilateral horse-trading, countries with widely divergent interests could find mutual benefit through concessions that fit each country's priorities. With these benefits in hand, it would be a more simple matter to extend the concessions group-wide. The system, however, required free trade to be negotiated line-by-line. Progress, therefore, was only achieved if one country was interested in claiming other member countries' markets for a particular product or sector.

The emphasis of LAFTA was on regional free trade in goods. The relatively less developed member countries in the Andean area perceived themselves to be at a disadvantage with the larger, more industrialized countries of the region. The agreement's premise that development would take place in all economies in LAFTA proved to be unrealistic; most of the benefits from increased industrial trade accrued to the larger countries, which ran favorable trade positions. As early as 1966 the Presidents of Colombia, Chile, Venezuela, Ecuador and Peru highlighted these smaller countries' dissatisfaction with LAFTA and outlined principles for accelerating the integration process, including the creation of an Andean common market. As a response, the Andean countries set up the Cartagena Agreement in 1969 including as members: Bolivia, Chile, Ecuador, Colombia and Peru. Venezuela joined in 1973 while Chile left in

1976. The Andean Group was the fullest expression of the old integration's instrumental support of Latin America's ISI development model.

2. The Agreement

In the Andean Group strategy the role of the public sector was paramount. The key assumption was that a centralized political apparatus not only could ensure equitable development, but that it was necessary in order to overcome market bottlenecks. It would require strong institutions and a high degree of policy coordination in many areas, not limited to strictly economic issues. In that way, it was hoped that competition between members could be managed.

The Group's institutions were made up of the Commission (ministerial level) and the Junta (or Board) which was to be completely independent of the member country governments, made up of three individuals picked by the Commission. The Junta was a permanent body granted with executive and research functions, and could make proposals and suggest initiatives. It oversaw a large independent technical staff. These characteristics and the legislative mandate of the Commission gave the AG a powerful supranational character. Each country had one vote and enjoyed a veto, with decisions requiring a two-thirds majority to pass. The agreement also made provision for the creation of an arbitration tribunal. A regional development bank was created just prior to the agreement.

The key elements of the agreement reflected the negative experience with LAFTA. All countries were to actively participate (planning was therefore necessary), with special preferences for the smaller, less developed countries (Bolivia and Ecuador); the process was to be swift and clear; trade was to be liberalized not on a product-by-product negotiating basis, but rather with a significant presence of automatic lists.

The trade liberalization was to be completed by 1980 (all exceptions eliminated by 1990). Some 2,000 items, or roughly one third of all goods, were reserved for possible inclusion in sectoral industrial development programs (SIDPs). The idea was to have various members involved in making components for products that would be traded within the group. Factories for goods not yet produced in the region were to be reserved for the less developed members. These programs were to be recommended by the Junta and negotiated and approved by the Commission by December 1973. Overall, these and other deadlines and objectives were enormously ambitious.[17]

One of the most controversial policies was Decision 24, which governed foreign capital. As mentioned, foreign ownership was controversial in Latin America and especially in the Andean area where there were a number of major international investment disputes. The agreement banned foreigners from investing in activities that would compete with existing firms, and strict controls were imposed on foreign ownership as well as the level of profit remittances.

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[17] The Agreement=s deadlines called for a common system of treatment of foreign capital, trade markets, patents, licenses, and royalties to be approved by December 31, 1970; a uniform system governing Andean multinationals, by December 31, 1971; harmonization of industrial promotion legislation, December 31, 1971; unification of foreign trade regulations, December 31, 1972; and procedures and mechanisms for coordination and harmonization of exchange, monetary, financial and fiscal policies, industrial programming, agricultural development, and the planning of physical and social infrastructure were to be approved by December 31, 1970.

The official treaty goal for trade liberalization was the total elimination of tariffs and other "trade restrictions" by December 31, 1980. The latter were to be eliminated outright by December 31, 1970, except for those applicable under the sectoral industrial development programs (SIDPs), and a high degree of flexibility was granted to Ecuador and Bolivia.

The trade liberalization program was a complex formula. The overall Andean intra-regional tariff universe was divided into five main groups of products: (a) those subject to a schedule of automatic reductions; (b) the liberalization already agreed to in LAFTA; (c) goods reserved for industrial programming; (d) products not produced within the region, some of which were reserved exclusively for development in Bolivia and Ecuador; and (e) lists of exceptions.

List (a): this was the largest group of these five categories. These products were bound to automatic tariff reductions following a ten-year phase-out schedule. The list was made up of some 3,470 items-- representing around 50 percent of tariff lines-- and was generally made up of goods being produced to satisfy regional demand of goods for which industrial programming was considered impractical. Products originating from Bolivia and Ecuador were subject to more accelerated tariff reduction.

The elimination process began by identifying the common initial tariff level, or PID (*Punto Inicial de Desgravación*); i.e., the lowest national tariff between Chile, Colombia and Peru for each product, not exceeding 100 percent *ad-valorem* at the time of the signing of the agreement. On December 31, 1970, all tariffs higher than the PID were reduced to that common base level, and on December 31 of each subsequent year, the base tariff rate was scheduled for a 10 percent automatic reduction until it reached zero at the end of 1980.

Intra-regional tariffs on those goods originating from Bolivia and Ecuador were reduced at a greatly accelerated pace, with annual cuts (beginning December 31, 1971 and based on the PID) of 40, 30 and 30 percent, thereby achieving free intra-regional trade in those products by December 31, 1973. Before March 31, 1971, the Commission had authorization to establish additional preferential margins and timeframes for goods in the group (a) product category that might be of special interest to Bolivia and Ecuador. Meanwhile these two countries were not required to begin tariff reductions until December 31, 1976, reaching zero by 1985 through a series of annual 10 percent tariff cuts. Moreover, these reductions were to be based on the existing original national tariff levels, not the lower PID.

List (b): the common list of tariffs that the LAFTA countries had previously agreed to eliminate by 1973 were to be liberalized completely one hundred and eighty days after the agreement came into force. Meanwhile, Bolivia and Ecuador were allowed to follow the original LAFTA schedule.

List (c): by December 31, 1970, the Commission had to reserve a group of goods for possible inclusion in the SIDPs. The Commission then was required to approve programs covering the reserved items by December 31, 1973, or by 1975 if the Junta approved an extension. Reserved goods not selected for a sectoral program by this time were subject to a liberalization schedule that would eliminate the tariff by 1980. Goods that were included in the approved SIDPs were subject to the specific terms of each industrial program, although they would eventually have to be subject to tariff elimination. Goods produced in Bolivia and Ecuador under an SIDP program, however, were to be completely free of restrictions as soon as the SIDP program was approved.

List (d): industrial products not produced in the subregion and not reserved for the SIDPs were to be drawn up on a list and were to be allocated to either Bolivia or Ecuador for future development (or, in special cases to any of the others). Tariffs on these products were to be eliminated by February 28, 1971, and only those countries to which each product was allocated could take advantage of the liberalization. After four years, if the designated country had not begun, or at least planned, the development of the item, the privileges were forfeited and it became subject to immediate and full liberalization.

List (e): exceptions. On December 31, 1970, each country was required to release a list of exceptions to the free trade program. These exceptions were to last until 1985 (1990 for Bolivia and Ecuador). The only restrictions on exceptions were on those that could be staple exports for Bolivia and Ecuador. The maximum number of exceptions allowed for each country were 600 in the cases of Bolivia and Ecuador, 450 for Peru, and 250 for Chile, Colombia and Venezuela.

The Common External Tariff (CET) was to be in place by December 31, 1980. The first step was to be the approval of a Minimum Common External Tariff (MCET) before December 31, 1970, followed by the approval on December 31, 1973 of a draft CET proposal, which the AG would begin to implement one year later. The process was not well defined in the Agreement. Meanwhile, the MCET was to have been fully in force by December 31, 1975, following annual linear movements towards the MCET level. The products covered by SIDPs were subject to the specific rules of each program, and products not produced in the region could remain under the import rules of individual states until production began. Bolivia and Ecuador were allowed numerous exceptions, but were required to abide fully with the CET by 1985.

The complex trade liberalization scheme set out in the Cartagena Agreement was imperfectly implemented. Neither a free trade area nor a customs union was achieved. However, the highly protected Andean markets did experience more sub-regional openness in the decade following the Agreement. In 1969, the year of the accord's signing, the tariff rates between Peru, Colombia, and Chile averaged some 92 percent ad-valorem with high degrees of dispersion. In addition, other, less quantifiable, but severe, restrictions on intra-regional imports were in place. By December 31, 1978, the highest intra-regional tariff on goods subject to the liberalization program was 32 percent, with an average rate of 10 percent. Twenty five percent of the tariff universe was traded freely. This did not include Bolivia and Ecuador which never began the trade liberalization process. On the other hand, eighty percent of the intra-regional exports *from* these countries were free of tariffs.

As mentioned above, the number of exceptions to the liberalization program was to be phased-out entirely by 1985 (1990 for Bolivia and Ecuador). The negotiations mandated by the Agreement for 1974 to schedule these reductions were not held (a 1976 protocol pushed the time frame back several years). Ten years after they were originally formulated, the items on the list of exceptions had only been reduced by 10 percent. The total number of items reserved for the SIDPs on exceptions lists in the AG was very significant: some 40 percent of the total five-country Andean tariff universe.

Problems mounted with disagreement over the industrial plans springing from the central bureaucratic institutions. There was increasing polarization between the more developed countries (Colombia, Chile) and the others. The Petrochemical program was approved in 1975, but in 1976 Chile withdrew from the Andean Group. With the troubles in implementing the tariff

liberalization program and the industrial programming, it is not surprising that intraregional trade showed little growth: intraregional exports as a percentage of the total rose from 2% in 1970 to only 4% at the end of the decade.

The countries never completed their CET. The transitional MCET was in place by December 31, 1970. External tariffs of member countries (excluding Bolivia and Ecuador) could not be lower than that MCET, which averaged 40 percent ad-valorem. The range of the MCET ran the gamut from 0 to 120 percent, with 97 per cent of the items equal to or less than 80 percent. The MCET was not only high, but also very incomplete, as an abundant number of items were excluded, as were the SIDP products and the products in the regional "not produced" reserved list. Nor did it apply to Bolivia and Ecuador. Moreover, the MCET *was a minimum not a maximum*; hence, in all cases the average national nominal tariffs of the member countries were far higher than the MCET. Bolivia, the country with the lowest external tariffs, averaged 54 percent, and Chile was the highest with 172 percent (unweighted sector averages).

In 1975, a new proposal called for a maximum effective protection of 90 percent. In 1976, the MCET was revamped, lowering the average minimum external tariff level to 29 percent, but it had a maximum level of 110 percent. The sectors for which the MCET was reduced the most were mostly final consumer goods. Meanwhile, the formation of the CET was postponed until December 31, 1983 for Colombia, Venezuela and Peru, and to 1989 for Bolivia and Ecuador. By this time, of course, an external debt crisis was not conducive to consolidation of the CET.

Problems with the implementation of the liberalization program were legion. There was instability in the economies of the member countries. The extremely centralized process, where the Andean institutions were responsible for planning and preparing politically sensitive and technically difficult economic and trade programs, did not accommodate the capacity of the states to implement them. Customs personnel, for example, were not always equipped with the resources to interpret the myriad lists, exceptions and decisions of the Group. Furthermore, securing the authorization to implement trade barrier reductions through the respective state institutional process could be problematic. Even authorizations to begin implementing the automatic reductions outlined in the Cartagena Agreement could take more than a year.

Furthermore, non-compliance was frequent. The Andean safeguard and dispute settlement systems were ineffective. The safeguard clause was used only twice in the first decade (Chile and Peru once each), revealing reluctance on the part of member countries to deploy the official machinery. Instead, countries far more often took recourse to unofficial methods to circumvent Andean obligations. Common complaints from the Andean countries concerned non-compliance with the MCET and additional restrictions placed on products on the reserved and exceptions lists. Non-tariff barriers were also widespread.

TABLE 1
TRADE AGREEMENTS IN THE AMERICAS IN THE 1990s

AGREEMENTS IN FORCE	Date of Signature	Entry Into Force
Caribbean Community (CARICOM)[1]	1973	1973
Chile-Mexico[2]	1991	1992
Central American Common Market (CACM)[3]	1960	1961
Chile- Venezuela	1993	1993
North American Free Trade Agreement (NAFTA)	1992	1994
Colombia-Chile	1993	1994
Southern Cone Common Market (MERCOSUR)	1991	1995
Costa Rica-Mexico	1994	1995
Group of Three (G-3)	1994	1995
Bolivia-Mexico	1994	1995
Chile-Ecuador	1994	1995
Andean Community[4]	1969	1969
Chile-MERCOSUR	1996	1996
Canada-Chile	1996	1997
Bolivia-MERCOSUR	1996	1997
Mexico-Nicaragua	1997	1998
Chile-Peru	1998	1998
CACM-Dominican Republic[5]	1998	1999
CARICOM-Dominican Republic[5]	1998	1999
Mexico – European Union[5]	1999	2000
CACM – Chile[5]	2000	2001
Mexico – Northern Triangle[6]	2000	2001

SELECTED AGREEMENTS UNDER DISCUSSION

Regional: Free Trade Area of the Americas (FTAA); Andean Community-Panama; CACM-Panamá; Chile-Panama; Mexico-Ecuador; Mexico-Panama; Mexico-Peru.

Extra-Regional: MERCOSUR-EU; Chile-EU; Chile-US; Chile-South Korea; CARICOM-EU (post-Lomé IV); APEC; Mexico-Japan.

Notes:

1. CARICOM is now updating its founding treaty in order to establish the legal basis for moving towards a single market.
2. The parties have substantially revised and upgraded this accord; a new agreement is in force since August 1, 1999.
3. The Presidents agreed to re-activate CACM in 1990 (Montelimar Summit) and opted to definitively pursue a customs union in 1993 (Protocol of Guatemala).
4. The 1988 Protocol of Quito calls for amendments to the group's founding treaty. In 1996, the Group's name was changed to the Andean Community and its institutional structure was revised (December Declaration of Trujillo).
5. Awaiting (sufficient) legislative approval.
6. Northern Triangle Includes El Salvador, Guatemala, and Honduras.

Source: Integration, Trade and Hemispheric Issues Division, IDB.

TABLE 2

NEW REGIONALISM: SELECTED TRADE LIBERALIZATION PROGRAMS IN THE AMERICAS

Agreement	Bilateral Imports As % Of Total Western Hemisphere Imports	Bilateral Imports As % of Total Imports	% Liberalized Items	
	1995	1995	1996	2006
CHILE-MEXICO (1992)				
Chile-Mexico	7.3	3.9	95.5	98.4
Mexico-Chile	0.9	0.7	95.0	98.2
CHILE-VENEZUELA (1993)				
Chile-Venezuela	2.7	1.5	0.7	96.6
Venezuela-Chile	1.7	1.2	0.7	95.7
CHILE-COLOMBIA (1994)				
Chile-Colombia	1.7	0.9	4.1	91.3
Colombia-Chile	2.1	1.4	5.3	91.3
CHILE-ECUADOR (1995)				
Chile-Ecuador	2.5	1.4	3.9	96.4
Ecuador-Chile	4.1	2.7	5.1	96.1
G3 (1995)				
Mexico-Colombia	0.2	0.1	7.6	90.9
Colombia-Mexico	4.9	3.3	4.1	90.8
Mexico-Venezuela	0.4	0.3	2.4	76.4
Venezuela-Mexico	4.8	3.4	0.4	76.8
MEXICO-COSTA RICA (1995)				
Mexico-Costa Rica	0.0	0.0	86.4	99.3
Costa Rica-Mexico	5.3	4.0	73.2	97.8
MEXICO-BOLIVIA (1995)				
Mexico-Bolivia	0.0	0.0	61.8	96.5
Bolivia-Mexico	2.2	1.4	59.2	96.4
MERCOSUR (1995)				
Argentina-Mercosur	44.1	22.7	96.6	99.9
Brasil-Argentina	31.3	13.8	99.4	99.9
Paraguay-Mercosur	71.1	40.4	92.8	99.9
Uruguay-Mercosur	73.6	46.1	86.3	99.9
MERCOSUR-CHILE (1996)				
Argentina-Chile	5.0	2.6	4.4	94.7
Chile-Argentina	16.8	8.9	4.4	95.0
Brasil-Mercosur	5.0	2.2	4.4	94.7
Chile-Brasil	14.5	7.7	4.4	97.6
Uruguay-Chile	2.7	1.7	4.4	94.8
Chile-Uruguay	0.5	0.3	4.4	95.4
Paraguay-Chile	4.6	2.6	4.4	95.0
Chile-Paraguay	0.7	0.4	4.4	93.5
MERCOSUR-BOLIVIA (1997)				
Argentina-Bolivia	0.5	0.3	5.4	97.1
Bolivia-Argentina	14.1	8.8	7.3	92.2
Brasil-Bolivia	0.1	0.1	5.6	97.1
Bolivia-Brasil	19.5	12.1	7.3	92.2
Uruguay-Bolivia	0.1	0.1	4.8	97.1
Bolivia-Uruguay	0.5	0.3	7.3	92.2
Paraguay-Bolivia	0.1	0.1	5.0	97.1
Bolivia-Paraguay	0.1	0.1	8.7	92.3

Source: IDB, Integration, Trade and Hemispheric Issues Division.

TABLE 3

NEW REGIONALISM: STRUCTURE OF RULES OF ORIGIN IN SELECTED AGREEMENTS

		FTA US-CA	NAFTA	G-3	Mexico-Costa Rica	Mexico-Bolivia	Canada-Chile	MERCOSUR-Chile	MERCOSUR-Bolivia
RULES OF ORIGIN BASED ON CHANGE OF CHAPTER	**CC**	**16,7**	**27,0**	**20,0**	**27,8**	**20,9**	**26,5**		
	CC/E		5,8	6,0	5,8	6,7	5,3		
	CC/OR	8,4		5,5		6,3			
	CC/E/OR		5,7	6,7	5,8	6,2	7,9		
	CC/RC/OR			2,7		1,2			
	CC or CH/RC					1,0			
	CC or CH/E/RC		1,3				2,0		
	CC or CS/RC	12,8							
	CC or CS/E/RC		1,1				1,0		
	CC/E or CH/E	16,2							
	CC/E or CH/RC	2,5							
	CC/E or CS/E/RC		11,2						
	SUBTOTAL	*56,6*	*52,1*	*40,9*	*40,4*	*41,3*	*42,7*	*0,0*	*0,0*
RULES OF ORIGIN BASED ON CHANGE OF HEADING	**CH**	**21,1**	**7,9**	**14,8**	**14,9**	**15,2**	**8,9**		
	CH/E	6,3	14,2	13,2	16,3	13,9	14,6		
	CH/RC	5,8	3,1	2,0	2,6	2,2	3,4	10,0	11,9
	CH/OR			1,0				20,0	21,2
	CH/E/OR	5,8				1,7			
	CH/RC/OR			8,1		10,0		24,0	22,3
	CH/E/RC/OR			4,9					
	CH or RC				1,0			46,0	44,6
	CH or CH/RC								
	CH or CS/RC		6,9	1,0	1,1				
	CH or CS/E/RC				7,4		7,5		
	CH/E or CS/E/RC						1,1		
	CH/E or CH/RC								
	CH/E or CH/E/RC		1,9		2,6		2,5		
	SUBTOTAL	*39,0*	*34,0*	*45,0*	*45,9*	*43,0*	*38,0*	*100,0*	*100,0*
RULES OF ORIGIN BASED ON CHANGE OF SUB-HEADING	**CS**	**1,1**	**1,3**	**1,0**	**1,6**	**1,7**	**11,0**		
	CS/E				1,3	1,3	1,6		
	CS/RC			4,6	4,2	4,2			
	CS/E/OR								
	CS or RC				1,3	1,3			
	CS or CS/RC								
	CS/E or CS/RC								
	SUBTOTAL	*1,1*	*1,3*	*5,6*	*8,4*	*8,5*	*12,6*	*0,0*	*0,0*
	TOTAL	**96,7**	**87,4**	**91,5**	**94,7**	**92,8**	**93,3**	**100,0**	**100,0**

Notes: Only percentages above 1% of the total are reported. The following abreviations are used (see text): CC - Change of Chapter; CH - Change of Heading; CS - Change of Subheading; CI - Change of Item; E - Change of Tariff Classification including Exceptions; OR - Other Technical Requirements; RC - Regional Value Content Criteria.

Source: Author's calculations.

TABLE 4

AVAILABLE UNILATERAL TRADE MEASURES APPLICABLE TO INTRA-AGREEMENT TRADE

MEASURES	ALADI	ANDEAN COMMUNITY	CACM	CARICOM	GROUP OF THREE	NAFTA	MERCOSUR	MERCOSUR Bilaterals with	
								Bolivia	Chile
Increase in tariffs[1]		No[2]	No[3]	No[5]	No	No	No	No	No
Import Surcharges	No	No	No[4]	No	No	No	No	No	No
Minimum import prices	WTO[6]	WTO	No		No	No	WTO	WTO	WTO
Anti-dumping tariffs	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Countervailing duties	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Safeguards									
General rules	Yes	Yes	No	Yes	Yes	Yes	No	Yes	No
Sector-specific rules	No	No	No	No	No	Yes[7]	No	No	No[8]
Safeguards or other measures triggered by balance-of-payments problems	Yes	Yes	No	Yes	No	No	No	No	

[1] Other than under a safeguard clause.

[2] Exceptions for Bolivia and Ecuador

[3] However, products can be removed from the free-trade list. In that case the MFN tariff is applied.

[4] Nicaragua is applying a temporary protection tariff (ATP) to intra-regional trade that will be eliminated in 1999, except for some products for reasons of fiscal revenue in 2001.

[5] Can be raised to MFN level with consensus of all CARICOM states.

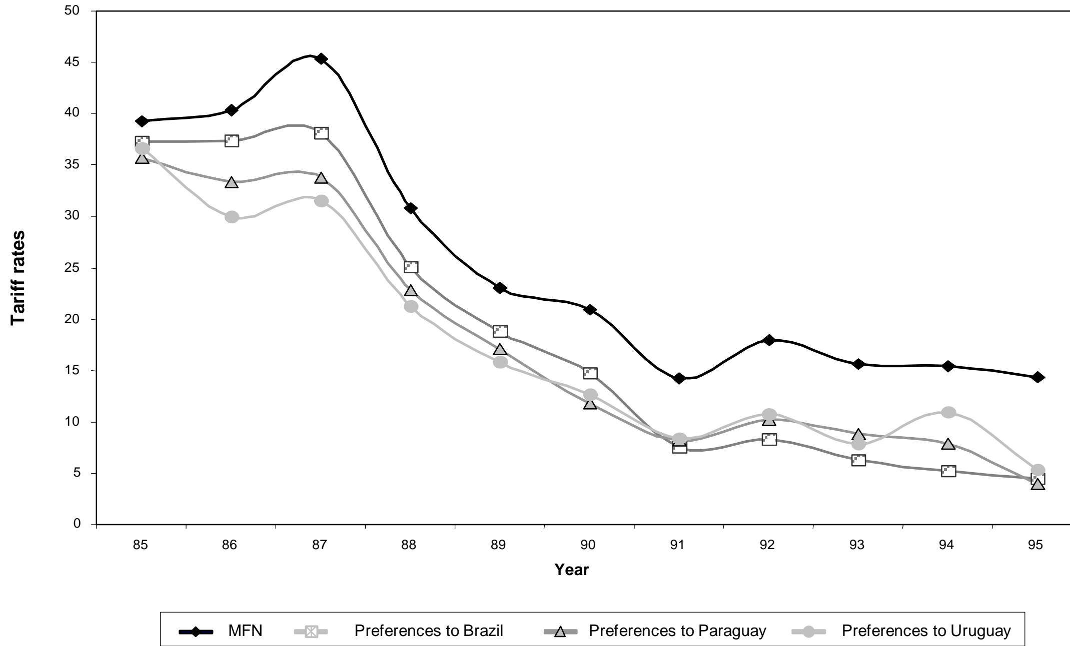
[6] WTO rules are utilized.

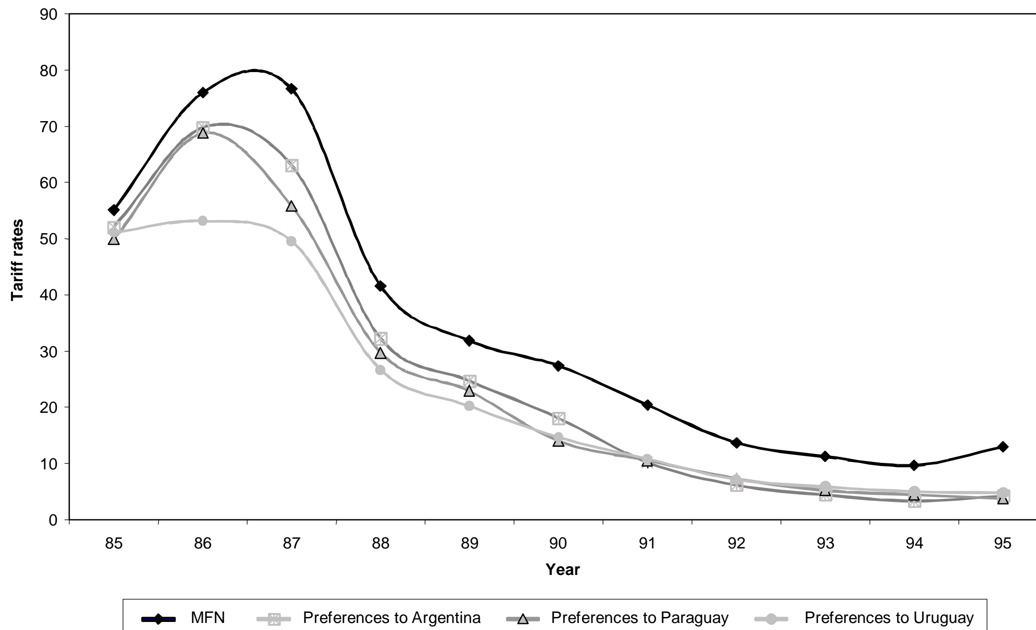
[7] Textiles and apparel goods.

[8] Under negotiation.

Source: OAS [1996]; IDB [1999].

FIGURE 1
EVOLUTION OF EXTERNAL AND INTERNAL TARIFFS IN MERCOSUR COUNTRIES



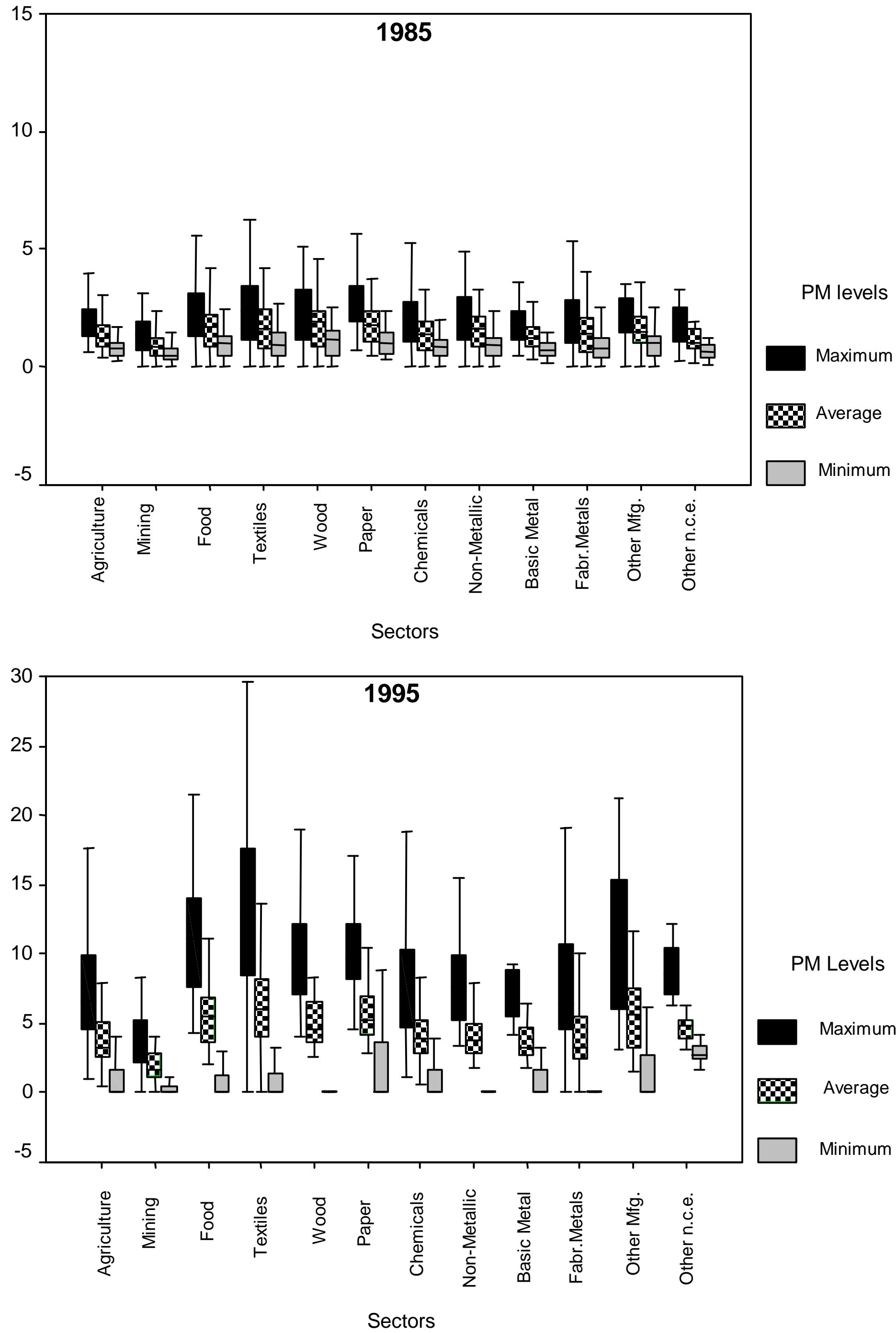


Source: Estevadeordal, A., J. Goto and R. Saez [2000].

FIGURE 2

PREFERENTIAL MARGINS IN LATIN AMERICAN AGREEMENTS

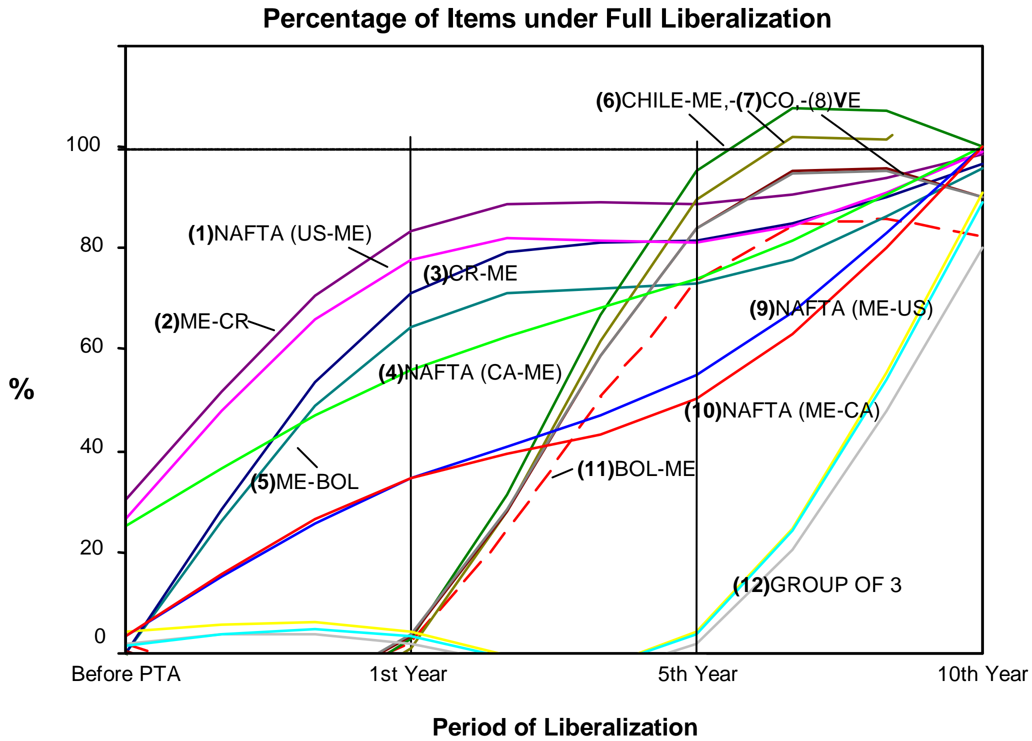
DISTRIBUTION OF MAXIMUM, MINIMUM, AND AVERAGE LEVELS

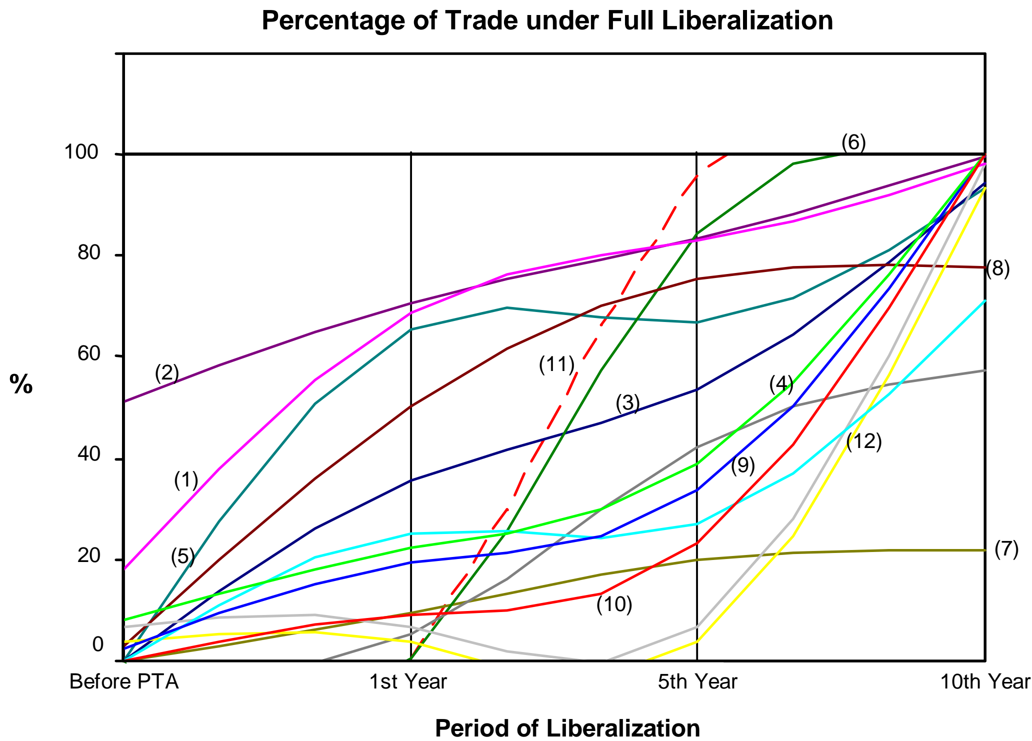


Note: As a measure of relative dispersion we use boxplots representing the interquartile ranges. The line in the middle of the box represents the median or 50th percentile of the data. The box extends from the 25th percentile ($x_{[25]}$) to the 75th percentile ($x_{[75]}$), the so-called interquartile range (IQR). The lines emerging from the box are called the whiskers and they extend to the upper and lower adjacent values. The upper adjacent value is defined as the largest data point less than or equal to $x_{[75]}$ + 1.5 IQR. The lower adjacent value is defined as the smallest data point greater than or equal to $x_{[25]}$ + 1.5 IQR. Observed points more extreme than the adjacent values are individually plotted.

FIGURE 3

NEW REGIONALISM: SPEED OF INTRAREGIONAL TARIFF LIBERALIZATION



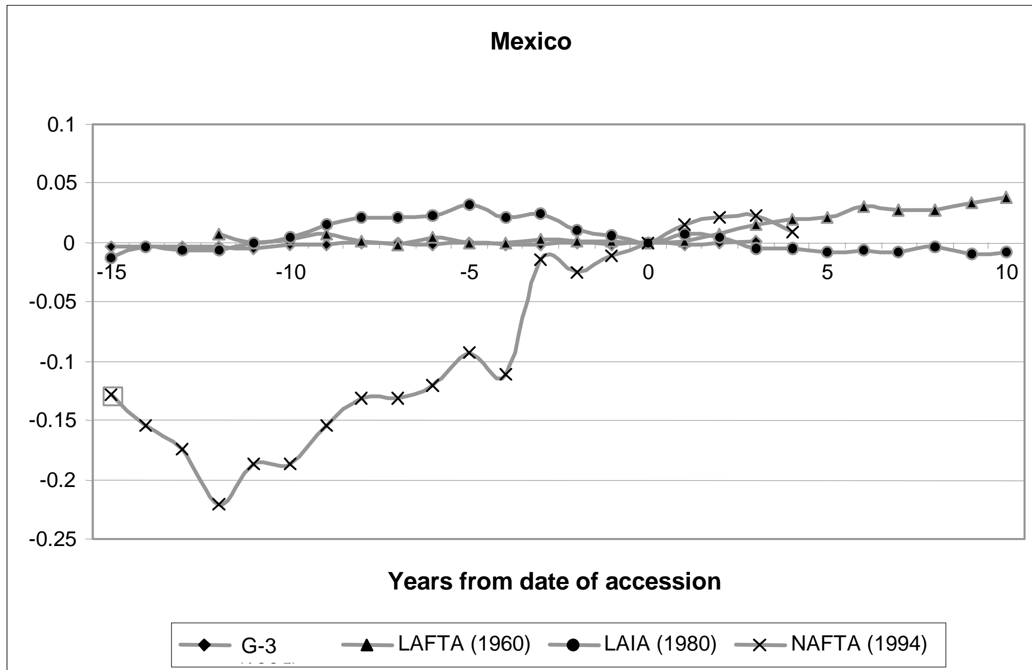


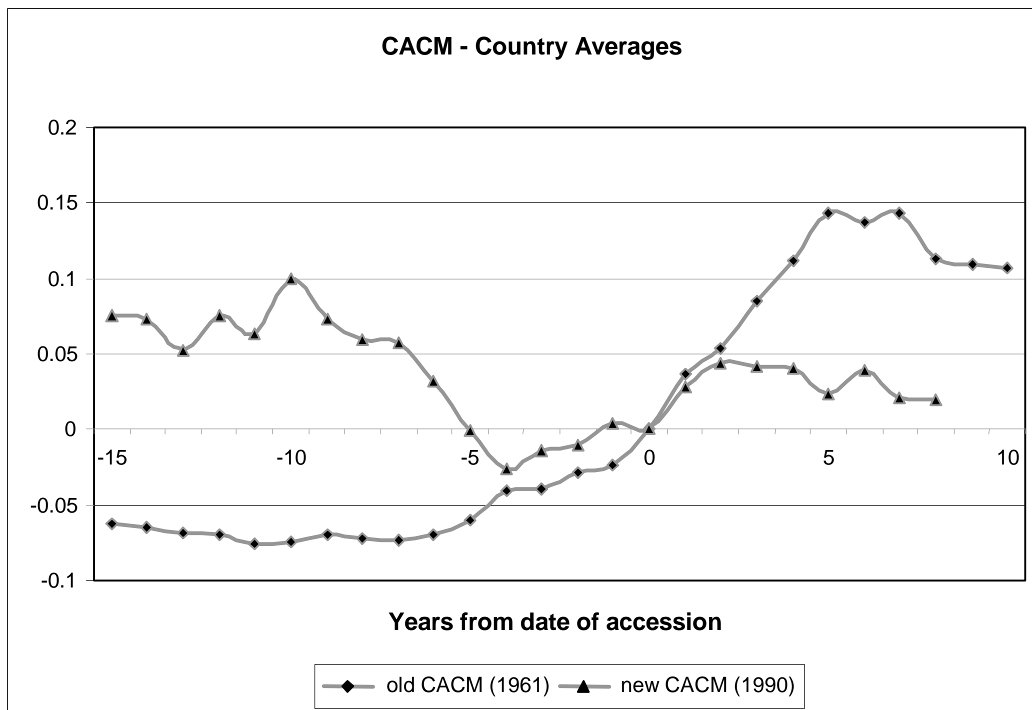
Source: Author's calculations.

FIGURE 4

OLD AND NEW REGIONALISM: ANTICIPATORY EFFECTS

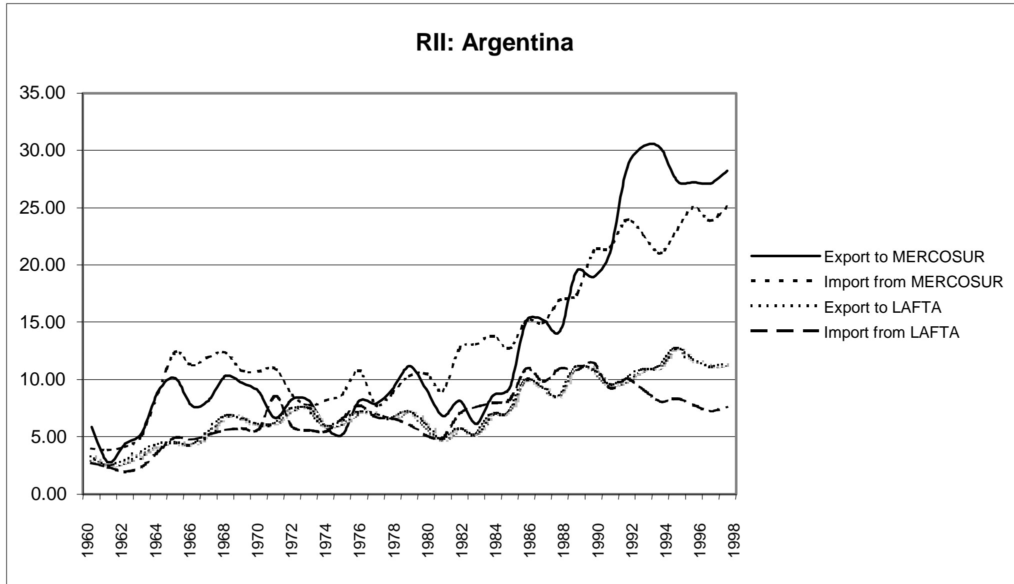
Trade shares normalized with respect to the year of implementation

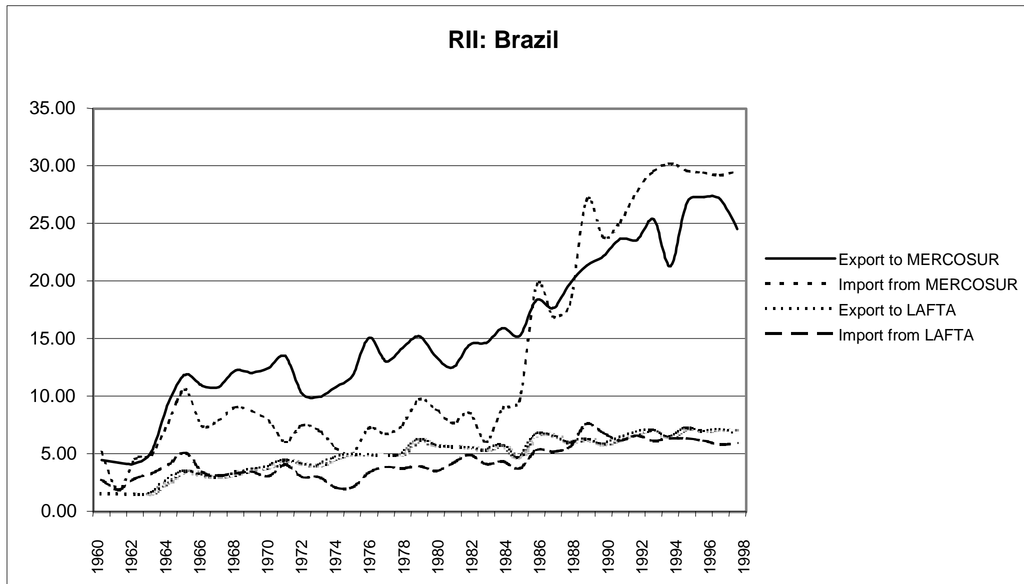




Source: Division of Integration, Trade, and Hemispheric Issues, IDB, based on data from IMF DOTS Database.

FIGURE 5
OLD AND NEW REGIONALISM: REGIONAL INTENSITY INDICES, 1960 TO 1998
MERCOSUR Countries





Source: Division of Integration, Trade and Hemispheric Issues, IDB.

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