

# Preferential Trade Agreements in the Western Hemisphere

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## Resumen

En este trabajo se analiza la proliferación de acuerdos comerciales preferenciales en el continente americano, las principales razones económicas y políticas que motivan la suscripción de estos acuerdos, y los cambios ocurridos desde la década de los sesenta en los modelos de integración y países que han liderado el proceso de regionalismo en el continente. El artículo detalla los principales logros de este proceso durante la década de los noventa, tanto en el plano comercial y de inversiones como en términos de convergencia hacia compromisos de apertura y liberalización amplios y estables. En tal contexto se examina la evolución de las negociaciones para el ALCA y se hacen planteamientos de mucha actualidad sobre las implicancias de esas negociaciones y las de los acuerdos bilaterales o plurilaterales con Estados Unidos, respecto a la construcción de la zona de libre comercio continental y a la coexistencia de esta con acuerdos subregionales de integración más profunda, con acuerdos comerciales regionales en otras partes del mundo y con el sistema multilateral de comercio.

## Abstract

This article analyzes the proliferation of preferential trade agreements in the Western Hemisphere, the main economic and political motivations behind them and the changes that have occurred since the sixties in integration models and countries leading the regionalism process in the hemisphere. The article scrutinizes the main achievements of this process both at the level of trade and investment flows and patterns as in terms of a convergence towards wide and stable commitments to openness and liberalization. In such a context, the evolution of FTAA negotiations is examined and relevant suggestions are made on their

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implications and those of bilateral or plurilateral agreements with the US regarding the building-up of the hemispheric free trade zone and its coexistence with sub-regional agreements for deeper integration, with regional trading agreements elsewhere in the world, and with the multilateral trading system.

## 1. A HUGE WEB OF AGREEMENTS

Table 1 lists the 26 Preferential Trade Agreements (PTAs) in force in the Western Hemisphere (WH) as of 30th June, 2001. From that total, four are sub-regional PTAs, each aimed at becoming a common market and now trying to complete the customs union stage<sup>1</sup>. These are the Central American Common Market (CACM), the Andean Community (before named Cartagena Agreement or "Andean Group"), the Caribbean Community and Common Market (CARICOM), and the Common Market of the South (MERCOSUR). This latter *one* emerged in the early 1990s, whereas the first three are the oldest sub-regional PTAs existing in the WH and all three modernized and deepened their integration process during the nineties<sup>2</sup>.

At the other end of the spectrum, there are four PTAs of Partial Scope (PS), in the sense that they are agreements mostly limited to tariffs and which the phasing out of barriers to goods trade is either negotiated on a product-by-product basis or covers all products but is not complete. These characteristics put them in the category of the so-called "old generation" of LAFTA (Latin American Free Trade Association)/LAIA (Latin American Integration Association-LAIA) agreements<sup>3</sup>. Two of them have the additional feature of being non-reciprocal, that is, the least developed parties either do not have to reciprocate the tariff preferences (CARICOM-Venezuela agreement) or are bound by "postponed reciprocity" on an agreed list of products (CARICOM-Colombia agreement)<sup>4</sup>.

In between, there are 18 PTAs (10 bilateral, 7 plurilateral and 1 sub-regional) aiming at completing the free trade area (FTA) stage only, but differing among themselves in the type of FTA pursued. The most advanced in this kind is the comprehensive ("full") type of FTA envisaged by the sub-regional North American Free Trade Agreement (NAFTA), which goes beyond the elimination of tariffs and reduction of various non-tariff measures (NTM) in goods trade. It also includes advanced rules and provisions on most disciplines (services,

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1. The Inter-American Development Bank (IDB) publishes a Periodic Note, *Integration and Trade in the Americas*, containing background information and updated briefings on progress in these and other PTAs of WH countries (see, for instance, the December 2000 issue, part II, pp. 28-54). In addition, the IDB Institute for the Integration of Latin America and the Caribbean (INTAL) publishes a wide range of research reports, newsletters and reports on PTAs in the WH (see the IDB-INTAL web site quoted in the References to this paper). For a recent review made at INTAL, see Taccone (2001).
  2. For a recent review of sub-regional PTAs in the WH aiming at becoming Customs Unions, see Salazar-Xirinachs and Wetter *et al.* (2001).
  3. The Treaty of Montevideo of 1980 transformed LAFTA (which was born in 1960) into LAIA, a semi-regional framework for integration including 11 member countries: Argentina, Bolivia, Brazil, Colombia, Chile, Ecuador, Mexico, Paraguay, Peru, Uruguay and Venezuela. LAIA members therefore include all five members of the Andean Community, the four members of MERCOSUR and a NAFTA member country.
  4. For a recent review of PS-PTAs in the WH, see Steinfatt (2001).

**Table 1**  
**Preferential Trade Agreements in the Western Hemisphere**

Agreements in Force (as of June 30, 2001)	Year Signed	Year Entry into Force	PTA stage being pursued	Format
1. CACM (Central American Common Market) <sup>1</sup>	1960	1961-1963 <sup>a</sup>	Customs Union	Subregional
2. Andean Community (thus named since 1996) <sup>2</sup>	1969	1969	Customs Union	Subregional
3. CARICOM (Caribbean Community and Common Market) <sup>3</sup>	1973	1973	Customs Union	Subregional
4. MERCOSUR (Common Market of the South) <sup>4</sup>	1991	1995	Customs Union	Subregional
5. Chile - Mexico	1991/1998 <sup>b</sup>	1992/1999 <sup>b</sup>	FTA, NAFTA-type <sup>b</sup>	Bilateral
6. Chile - Venezuela	1992	1993	FTA, LAIA-type	Bilateral
7. CARICOM - Venezuela	1992	1993	PS-NR	Plurilateral
8. NAFTA (North American Free Trade Agreement) <sup>5</sup>	1992	1994	FTA, "full" type	Subregional
9. Colombia - Chile	1993	1994	FTA, LAIA-type	Bilateral
10. CARICOM - Colombia	1994	1995	PS-NR	Plurilateral
11. Group of Three (Colombia-Mexico-Venezuela)	1994	1995	FTA, NAFTA-type <sup>c</sup>	Plurilateral <sup>d</sup>
12. Costa Rica - Mexico	1994	1995	FTA, NAFTA-type	Bilateral
13. Bolivia - Mexico	1994	1995	FTA, NAFTA-type	Bilateral
14. Chile - Ecuador	1994	1995	FTA, LAIA-type	Bilateral
15. Chile - MERCOSUR	1996	1996	FTA, LAIA-type	Plurilateral
16. Canada - Chile	1996	1997	FTA, NAFTA-type	Bilateral
17. Bolivia - MERCOSUR	1996	1997	FTA, LAIA-type	Plurilateral
18. Mexico - Nicaragua	1997	1998	FTA, NAFTA-type	Bilateral
19. Chile - Peru	1998	1998	FTA, LAIA-type	Bilateral
20. Central America - Dominican Republic	1998	1999	FTA, NAFTA-type	Plurilateral <sup>d</sup>
21. CARICOM - Dominican Republic	1998	2000 <sup>e</sup>	FTA, NAFTA-type	Plurilateral
22. Central America - Chile	1999	2001 <sup>f</sup>	FTA, NAFTA-type	Plurilateral <sup>d</sup>
23. Brazil - (Colombia/Ecuador/Peru/Venezuela)	1999	1999	PS, LAIA	Plurilateral
24. Argentina - (Colombia/Ecuador/Peru/Venezuela)	2000	2000	PS, LAIA	Plurilateral
25. Mexico - Northern Triangle (El Salvador/ Guatemala/ Honduras)	2000	2001	FTA, NAFTA-type	Plurilateral
26. Canada - Costa Rica	2001		FTA, NAFTA-type	Bilateral

Abbreviations: FTA = Free Trade Area; LAIA = Latin American Integration Association; PS = Partial Scope; NR = Nonreciprocal

1/ The 5 members of CACM are: Costa Rica, El Salvador, Guatemala, Honduras and Nicaragua.

2/ The 5 members of Andean Community are: Bolivia, Colombia, Ecuador, Peru and Venezuela.

3/ The 13 members of CARICOM are: Antigua & Barbuda, Barbados, Belize, Dominica, Grenada, Guyana, Jamaica, St. Kitts and Nevis, St. Lucia, St. Vincent and the Grenadines, Suriname, Trinidad and Tobago and Montserrat. (UK Overseas Territory). Haiti will become a member once it deposits its instruments of accession. The Bahamas, the British Virgin Islands and the Turks and Caicos Islands are associate members.

4/ The 4 members of MERCOSUR are: Argentina, Brazil, Paraguay and Uruguay. Bolivia and Chile are associate members.

5/ The 3 members of NAFTA are: Canada, Mexico and United States. Before, a bilateral Canada-USA FTA agreement was signed in 1988 and entered into force in 1989.

a/ It entered into force in 1961 for El Salvador, Guatemala and Nicaragua; in 1962 for Honduras and in 1963 for Costa Rica.

b/ The NAFTA-type FTA agreement was signed in 1998 and entered into force in 1999 replacing a bilateral LAIA-type FTA agreement signed in 1991 and that had entered into force in 1992.

c/ Between Colombia and Venezuela. It applies the Andean Community goals and rules.

d/ It applies bilaterally with each Central American country.

e/ A protocol to implement the agreement was signed that year.

f/ The process of legislative approvals is yet to be completed.

Sources: ASCUP, based on data from IDE - Integration and Regional Programs Department, and OAS Trade Unit.

investment, intellectual property, competition policy, government procurement, dispute settlement) needed for the functioning of a common market, though without the commitment to adopt supranational institutions and mechanisms similar to those of the European Union<sup>5</sup>.

This NAFTA-type of FTA is the model now being pursued elsewhere in the WH through 11 agreements (6 bilateral and 5 plurilateral). These have been the result of the following initiatives: bilateral negotiations of two NAFTA members (Canada and Mexico) with Chile and Costa Rica, respectively; negotiations of Mexico with three Andean countries and four Central American countries, either bilaterally (with Bolivia and with Nicaragua) or plurilaterally (with Colombia and Venezuela on one side, and on the other with El Salvador, Guatemala and Honduras); Chile's plurilateral negotiations with the five CACM members; and the Dominican Republic's plurilateral negotiations with CACM countries as well as with CARICOM members<sup>6</sup>.

On the other hand, there are seven agreements (five bilateral and two plurilateral) following a LAIA-type of FTA, which provide for the elimination of tariffs and reduction of many NTM in most product lines, and also include rules on some other disciplines not confined to goods trade. These belong to the so-called "new generation" agreements under the LAIA framework, and are those emerged during the 1990s from bilateral negotiations between Chile and each of the Andean Community members, as well as from the plurilateral negotiations of Bolivia and of Chile, each one with the four MERCOSUR countries, as part of their respective incorporations as associate members of this sub-regional agreement. In all these cases, the new agreements have replaced the respective bilateral PS-PTAs before existing under the LAFTA/LAIA frameworks, and have considerably upgraded the liberalization and cooperation processes between the named parties<sup>7</sup>.

It thus follows that there are two main types of FTA agreements in the WH, the majority of which have NAFTA as the model sought for. Mexico has been an active and consistent promoter of the dissemination of the NAFTA-type FTA in the WH, particularly through its

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5. For a thorough analysis of NAFTA, see Hufbauer and Schott (1993).

6. For a recent review of NAFTA-type FTA agreements in the WH, see Robert (2001a).

7. LAIA (or ALADI, its acronym in Spanish) inherited from its predecessor (LAFTA) a huge number of mostly bilateral PS-PTAs, though not only tried to make them converge but it also stimulated the covering of trade-related matters left aside in the old PS-PTAs. From this effort started to emerge during the 1980s a first version of "new generation" agreements (named in Spanish *Acuerdos de Complementación Económica* -ACEs), 13 of which were already signed in 1990. See ALADI (1990: 1). During the 1990s the second version of ACEs emerged, FTA-oriented in tariff matters and including many of the relevant trade-related disciplines listed in Table 1.

dealings with Chile and agreements signed with countries in the Andean and Central American sub-regions. Chile, in turn, has implemented a two-tier strategy: it has adopted the NAFTA-type FTA for its agreements with countries in the North American and Central American sub-regions and, at the same time, it has used the LAIA-type FTA at the South American level, for its agreements with Andean countries and with the MERCOSUR sub-region.

From all the above, it can be shortly said that:

- a) The existing web of PTAs within the WH is very big indeed, and their proliferation is a recent phenomenon. Their overwhelming majority (23 out of 26) emerged during the nineties.
- b) There is a complex co-existence of overlapping Common Market (European-inspired) and NAFTA-FTA models of integration within the Andean, the Central American and the Caribbean sub-regions.
- c) The "Common Market Model" still officially prevails in the two South American sub-regional agreements (Andean Community and MERCOSUR) with relatively strong supranational institutions in the Andean case. Yet the "NAFTA Model" has already made important inroads within the Andean sub-region.
- d) A sort of "Greater NAFTA" zone comprising NAFTA, Chile, Central America and Caribbean seems to have significant progress.

### **1.1 Other Trade Agreements and Preference Programs**

And yet table 1 does not tell us the whole story. As detailed right below, even more PTAs are now in the making, both within WH countries and between some of them and countries outside the Hemisphere. At the same time, some developing economies in the Americas do benefit from nonreciprocal trade preferences awarded by the two developed countries of the WH, as well as by the European Union and Japan.

- a) Formal negotiations or pre-negotiation consultations are proceeding for establishing the following PTA agreements within the WH (Devlin and Estevadeordal 2001: 29, Table 1; Salazar-Xirinachs 2001b: 3, Table 1).

- Free Trade of the Americas (FTAA)
  - Andean Community–MERCOSUR
  - CACM–Panama
  - Chile–USA
  - Mexico–Ecuador
  - Mexico–Panama
  - Mexico–Peru
  - Mexico–Trinidad and Tobago
- b) There are also three Generalized System of Preferences (GSP)-type of nonreciprocal preferential programs (Steinfatt 2001: 109-15).
- The Caribbean Basin Initiative (CBI), enacted by USA in 1983 and subsequently extended in time and expanded in product coverage in 1990 through the Caribbean Basin Economic Recovery and Expansion Act (CBBERA) and in 2000 through the Caribbean Basin Trade Partnership Act (CBTPA). It now applies to 24 CBI countries potentially eligible as beneficiaries subject to specific criteria. It is to remain in effect until the earlier of two dates: September 30, 2008 or the date the FTAA enters into force.
  - The Andean Trade Preference Act (ATPA), enacted by USA in 1991. Four Andean countries (Bolivia, Colombia, Ecuador and Peru) are potentially eligible as beneficiaries subject to specific criteria. Compared to CBI, ATPA is a narrower program in key products coverage and NTM benefits. Andean countries are currently lobbying for an ATPA extension in time and product coverage expansion.
  - The CARIBCAN program, enacted by Canada in 1986. It covers an extensive list of products originated from 18 eligible Caribbean countries or territories, not subject to specific criteria for qualifying as beneficiaries.
- c) On the other hand, WH countries are also involved in the following preferential arrangements with parties in other regions of the world (Salazar-Xirinachs 2001b: 3):
- Regarding Europe, already in force are the Mexico–European Union FTA agreement (2000) and the Mexico–European Free Trade Association FTA agreement (2001). In the negotiation stage are the possible Chile–European Union and MERCOSUR–European Union FTA agreements.
  - Regarding Asia–Pacific economies, negotiations are underway for a Chile–South Korea FTA agreement, a Chile–New Zealand FTA agreement and a Mexico–

Singapore FTA agreement, while other possible bilateral agreements are at the study or consultation stages.

- Each of the three NAFTA countries also have bilateral FTA agreements with Israel, in force since 1985 in the case of USA, since 1997 in the case of Canada and since 2000 in the case of Mexico.
- Under negotiation there is a MERCOSUR-South Africa FTA agreement.
- Finally, Andean countries, as well as Central American and Caribbean countries also benefit as groups from different nonreciprocal preferential treatment granted by the European Union and Japan through their respective GSP-type programs.

## 2. ORIGINS AND RADICAL TRANSFORMATIONS

### 2.1 Competing Integration Models and Changes in Leadership

Since its modern (post-WWII) origins in 1960, the integration process among Latin American countries harbored two models of economic integration: the FTA model, first adopted by LAFTA, and the Common Market model, first adopted by the CACM sub-regional grouping. This latter has the European integration staged program as source of inspiration, and calls for going beyond the stage of FTA in goods trade up to the formation of a Customs Union plus the free circulation of production factors, the harmonization of trade policy and other trade-related policies, all this with increasing levels of supranational mechanisms and institutional governance. As for the FTA model, its call has been confined to the complete liberalization of trade in goods until NAFTA came into the scene representing, as said before, the pursuit of a comprehensive ("full") version of FTA encompassing the complete liberalization of most barriers to trade in goods and services, as well as the inclusion of advanced rules and provisions on most disciplines needed for the functioning of a single enlarged market. Yet all this is to be accomplished without the commitment to adopt supranational mechanisms and institutions.

During the 1960s<sup>8</sup>, concrete steps toward fulfilling those models were either limited in scope and depth (the LAFTA case) or stalled shortly after a rapid initial progress (the CACM case), due to political and macroeconomic instability as well as to the highly protectionist and inefficient Latin American version of the import-substitution development strategy. LAFTA gave birth to numerous bilateral PS-PTAs (signed by each member with each one of

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8. See Salazar-Xirinachs and Wetter *et al.* (2001) for a summary on the origins and initial achievements of CACM (pp. 46-8), the Andean Community (pp. 56-7) and CARICOM (pp. 66-8).



the other members), whereby efforts to liberalize trade were often stalled by an exhausting method of product-by-product tariff-cutting negotiations on a limited list of goods usually involving unimportant sectors. It was so that, disappointed with very slow progress in LAFTA and determined to counterweight the influence of its largest members (Argentina, Brazil and Mexico), five medium and small countries created the "Andean Group" (1969) and shaped it along the lines of the Common Market model (Moran 1970: 20-2). A few years later, the Caribbean economies created CARICOM (1973), following a similar pattern.

Thus, the European-inspired Common Market model reigned in the three sub-regional PTAs existing in the Latin American and Caribbean (LAC) region in the 1970s. During that decade, the named model made its way to progressively replacing the FTA model embodied in LAFTA as the Integration Vision for the region as a whole. This was so because, even though the "Andean Group" and the CARICOM versions of the Common Market model also suffered from some of the same constraining factors which had previously slowed-down the pace of integration in the CACM, all the three sub-regions achieved integration results substantially larger than LAFTA's and progress was particularly impressive within the "Andean Group"<sup>9</sup>. As a consequence, the "Latin America Common Market" emerged as a superior integration vision for the region, and so it was made explicit in the Treaty of Montevideo (1980) that transformed LAFTA into LAIA.

Unfortunately, economic integration among LAC countries was abruptly reversed during the first half of the 1980s by the sequels of the debt-driven crisis. Intra-regional trade as well as inside each PTA decreased more than total LAC trade, as widespread recessions sharply curtailed import demand and the urgent need for foreign currency focused LAC countries on hastily increasing their primary exports directed mainly to industrialized economies outside the region. Mounting balance of payments deficits made most LAC countries return to protectionist and "managed trade" measures. In such a context, an important buffer role was accomplished by the LAIA Reciprocal Payments Compensation Mechanism in preventing intra-regional trade from an even worse fall<sup>10</sup>.

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9. For a detailed account of the progress achieved by the "Andean Group" during its first ten years, see a report issued in 1970 by its secretarial board, then named *Junta del Acuerdo de Cartagena* and today named *Secretaría General de la Comunidad Andina*, quoted in the references as *Comunidad Andina - Secretaría General* (1970). This has been recently complemented by Maldonado (1999).

10. This mechanism allows each LAIA member to make foreign currency payments only for the difference between its imports from and exports to another LAIA member when there is a deficit in the respective bilateral trade account. It contemplates payment facilities when the deficit mounts over the years.

But the slump in the region's integration process did not last too long. Signs of an LAC economic integration revival appeared in the mid-1980s, with the signing of the bilateral Program of Integration and Economic Cooperation between Argentina and Brazil in 1986. Although it was cautiously initiated under a sector-by-sector approach, the success of some of the ensuing sectoral protocols made both countries upgrade their bilateral integration efforts through the signing of a more embracing Treaty of Integration, Cooperation and Development in 1988<sup>11</sup>. This was, and perhaps not coincidentally, the same year the Canada–USA bilateral FTA agreement came on the scene. Later on, with the addition of Paraguay and Uruguay, the "Treaty of Asuncion" signed in 1991 replaced the 1988 Treaty and gave birth to MERCOSUR, the latest Common Market-aimed sub-regional agreement in the WH.

The Argentina–Brazil integration process exerted a significant "demonstration effect" all over the Americas. It played an important influential role in the revival of the Andean Group, which started with the approval of the "Quito Protocol" (1987) instructing for the removal of "managed trade" practices and that a few years later became a comprehensive agreement thanks to the formulation and implementation of the "Strategic Design" approved by the Andean Presidential Council in 1989, which modernized the Andean sub-regional integration process and put the program on the fast track for the accelerated completion of its FTA stage though keeping it as part of a more ambitious Customs Union mandate (González Vigil 1994: 217ss.). At the same time, integration events between Argentina and Brazil, together with the Canada–USA FTA agreement, were also very influential in Mexico's approaches towards the USA, first to sign in 1987 a bilateral framework agreement which resulted in a number of sectoral trade negotiations (Schott 1989: 47), and then during 1989–1990 about negotiating an FTA agreement. Somehow privy in advance to the Mexico–USA talks Chile lobbied intensively to be advantageously considered in the outcome.

It was so that in 1990 the USA launched the Enterprise for the Americas Initiative (EAI) embracing three components on trade, investment and debt-relief. The trade component had as its ultimate goal the progressive building-up of a WH-wide free trade area (WHFTA), through a gradual process of bilateral FTA agreements with LAC countries the USA deemed

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11. Argentina and Brazil signed between them 24 sectoral protocols during 1986–1990 and in their 1988 Treaty announced the decision of becoming a Common Market (See Magariños 2001: 2).

ready<sup>12</sup>. Among these, Chile was the only other LAC country besides Mexico officially mentioned by the USA government when it launched the EAI. That is, the USA adopted in the EAI a bilateral "hub-and-spoke" approach which meant that the WHFTA building-up would be implemented sequentially and by means of a possibly arbitrary "picking-the-winners" selection method.

Such a full incursion of the USA in the integration process among countries in the WH brought about two crucial consequences:

- a) The emergence of the WHFTA (subsequently renamed as FTAAs) as a new economic integration vision for the Americas, thus larger in scope than the previous vision confined to only the LAC region. Moreover, the new vision adhered to an FTA model of integration, different to the Common Market model prevailing in all the sub-regional PTAs existing in the named region. The ensuing possible incompatibilities notwithstanding, most LAC countries welcomed the new vision.
- b) But the bilateral "hub-and-spoke" approach, then chosen by the USA for building up the WHFTA and which was the official approach until the end of the Bush Administration, generated a proliferation of bilateral and plurilateral FTA-type agreements then conceived as platforms for the projected WHFTA. These agreements threatened with destabilizing the LAC sub-region's on-going efforts to configure their respective Customs Unions, and made for them very difficult to find out ways to constructively co-exist, as a group, with the announced WHFTA.

In such respect, the credibility of the Andean Group countries commitment with the Customs Union goal was severely hurt when Mexico launched talks in 1991 with Colombia and Venezuela about a "Group of Three" FTA agreement (which finally was signed in 1994). In 1991 also, Chile initiated with Venezuela a series of bilateral talks that gradually resulted in FTA-type agreements between that country and each of the Andean Group members (González Vigil; Abugattas and Cuba 1992: 130; see also González Vigil 1994: 246-49). A similar path was followed by Mexico with CACM members during the second half of the 1990s. As for MERCOSUR, although this sub-region managed to keep united before bilateral moves by Chile and Mexico, Argentina and Brazil clearly had different

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12. For those LAC countries judged by the USA as not yet ready, the EAI envisaged a sort of preparatory stage through the signing of framework agreements establishing consultative fora and mechanisms in order to discuss trade and investment matters of mutual interest. By early 1992, the USA had already signed 16 of those framework agreements with 31 countries in the LAC region (See United States 1992: 8). This official document offers an account of progress in implementing all EAI components, from the USA point of view. For an analysis of the EAI from a LAC perspective, see SELA (1991).

views on how to react to USA invitations to bilateralism embodied in its "hub-and-spoke" approach towards the WHFTA (Bouzas 1996: 69).

All the above notwithstanding, in practice none of the four Common Market modelled sub-regional PTAs was abandoned. On the contrary, all four continued working to create their respective Customs Unions. Moreover, by the mid-1990s two of them (the Andean Community and MERCOSUR) had made considerable headway in the matter, to the point that Chile had to change its mind and concluded a LAIA-type FTA agreement with MERCOSUR in 1995 and became its Associate Member ever since. A year later Bolivia followed suit and led the subsequent process of negotiations between Andean Community and MERCOSUR members<sup>13</sup>. These developments can be attributed to two sets of factors:

- a) With the arrival of the Clinton Administration, USA changed its ways to make real the new Hemispheric integration vision, replacing the bilateral "hub-and-spoke" approach for what may be called the "Western Hemispheric Round" (WHR) approach, which since the Miami Summit of the Americas (1994) convoked at once all countries in the Hemisphere but Cuba.
- b) Economic and political motivations for economic development and integration advised LAC countries to accelerate and make deeper their sub-regional PTAs at the same time that they participated actively in the construction of a Hemisphere-wide integration agreement. The motivating rationale is discussed below.

## 2.2 The Political and Economic Motivations

The proliferation of PTAs in the WH during the 1990s and the somehow astonishing cohabitation of 'old' and 'new' regionalism in the Americas resist any attempt at a single-minded explanation. They have rather been the result of a combination of factors, *a priori* not necessarily congenial among them but which the American countries have so far been able to melt in a way that has so far made them de facto accomplices of a very lively and fruitful regionalism exercise. Particularly important among those factors are the following ones:

- a) *The Impact of Market-based Economic Reforms*  
A radical change in development strategy, from a highly-protectionist and inefficient LAC version of the import-substitution strategy to an outward-oriented strategy,

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13. For an analysis of main events and results of LAC countries integration efforts in the 1990s, see CEPAL (2001b: 173-200).

relying on private initiative as growth engine and to this aim implementing deregulation, privatization and the opening of trade and capital accounts (in a context of plentiful and cheap foreign savings), brought about a bold unilateral liberalization process. The average tariff in the LAC region declined from 45% in the mid-1980s to 12% in 1999, together with a sharp decrease in tariff dispersal. At the same time, many NTMs have been either dismantled or adjusted in compliance with Uruguay Round commitments (Ocampo; Bajraj and Martin 2001: 32 and Table 2.1).

And yet, though market-based reforms do account for unilateral liberalization by themselves they do not give birth to negotiated liberalization. In fact, most WH countries do not rely solely on unilateral liberalization but rather on a three-tier liberalization approach, which combines unilateral with multilateral and regionalism-led liberalization measures (Devlin and Ffrench-Davis 1998: 9-11). Additionally, in most of LAC countries the economic reform packages were not implemented before the early- or even mid-1990s (Edwards 1998: 9-10; see also Stallings 2001: 9). Thus, when trying to explain the revival of PTAs in the LAC region from the mid-1980s onwards and the subsequent incursion of North America in PTA-making, one has to add up into the account the workings of some important factors specific to regionalism.

b) *Regionalism-specific factors: political motivations*

There is widespread consensus in the relevant literature (See, for instance, Serra *et al.* 1997) that countries "feel" the need to get closer and group themselves for far more than just market economy rationality, especially when they are neighbours or belong to the same geographically-shaped region. This is not only due to the need of increasing their bargaining power internationally and ensure for themselves a better and respected place in the world arena, but also because usually centripetal forces rooted in common heritage, culture and language tend to prevail, in the long run, over centrifugal forces coming from national rivalries or the sometimes dividing influence of powers outside the region.

c) *Regionalism-specific factors: sustainable trade liberalization*

A reciprocal agreement of circumscribed scope (either regional or sub-regional or even some important bilateral agreements) usually meets less political resistance and provides a more predictable and controlled environment for sustained liberalization. Not only does it add a compensatory ingredient to import liberalization by fostering reciprocal exports in tandem with reciprocal imports, but it also does so with unfavourable effects on fiscal income much lesser than liberalization of imports from the world at large. It also reduces the level of protection compared to its pre-

agreement level, thereby creating trade, raising competition and promoting specialisation within the enlarged market provided by the agreement (Devlin and Ffrench-Davis 1998: 14).

d) *Regionalism-specific factors: investments attraction*

It follows from the above that regionalism-led liberalization serves to lock-in open economy policy reforms by allowing a more balanced dose of their positive and negative effects on economic activity, and thereby sending good signals to investors. This is particularly important regarding investors in modern manufacturing and services industries that tend to cluster and locate together due to externalities and agglomeration economies. Given such a trend, the enlarged market resulting from the agreement is expected to stimulate inflows of foreign investment by improving the location advantages of the member economies as a group, though not necessarily for each of them (Venables 1999: 16-17).

e) *Regionalism as a strategic tool for industrialization and competitiveness*

Economic integration can assist national efforts to diversify export supply and upgrade output towards goods and services with more value-added and longer learning curves. This will be so if the enlarged market induces new domestic investment and is more attractive to foreign investors, provided it facilitates greater specialization through economies of scale and agglomeration, enhances competition and accelerates information flows specifically focused on the regional or sub-regional opportunities and potential. As a result, the larger market may encourage new exports of goods and services, as well as new exporters, incubated under the preferential access to similar and more familiar neighbouring markets with shorter learning curves, thus playing as a sort of platform for better reaching less familiar and more exigent markets elsewhere in the world (Ffrench-Davis 1980: 41-8). All the above implying that the agreement may function as a tool for a progressive upgrading of the group's industrialization level and international competitiveness.

*In sum*, when considering the five set of factors combined, it can be hypothesized that:

- Before the 1990s, when liberal economic reforms (factor a) were unpopular and trade liberalization (factor c) did not rank high in the LAC regional agenda, political and strategic motivations (factors b and e) prevailed and made the Common Market model look superior to the FTA model, as the latter does not contemplate common mechanisms to temper asymmetries among participant countries by giving to the

weaker ones the means to ensure themselves that their national development and industrialization goals will not be hindered by the stronger partners.

- Since the 1990s, the wave of liberal reforms in foreign trade and domestic markets, in a context of rising globalization of production networks and corporate operations, has not only increased the importance of unilateral and negotiated liberalization (factors a and c) but has also given a great urgency to attracting investment (factor d) and, even more significantly, has radically changed the contents of and the strategies for materializing the political and economic development goals of nations which underlie factors b and e, yet seemingly without demoting them neither in national country nor in some PTAs' agendas<sup>14</sup>.
- As a consequence, during the 1990s liberalization proceeded at an accelerated pace administered in three-tier (unilateral, multilateral, regional) strategies, and while the USA-led FTAA (and its predecessor the WHFTA) was mostly welcomed, many LAC countries kept alive (in words at least though not always in deeds) their Common Market-aimed PTAs and strived for "deep" integration (and not just liberalization) at that sub-regional level as a precaution against the potential inequity intrinsic to the FTA model. In short, the fundamental rationality behind the "old" LAC regionalism is not dead but it lives transformed in consonance with the imperatives of the "new" and "open" regionalism now reigning in the WH as a whole<sup>15</sup>.

### 3. MAIN ACHIEVEMENTS IN THE 1990S

This section highlights two important sets of achievements of regionalism in the Americas during the 1990s. One is the increasing convergence of rules and work agendas among WH PTAs, despite varying specific traits. This convergence reflected the general consensus in favor of open economies, and liberalization of trade and investment flows, together with the basic framework for trade negotiations provided by the post-Uruguay Round multilateral system. It can be attributed to the common challenges posed by globalization and to the strong leadership exerted by the USA in the modeling of the 'new' regionalism in the Americas, with the ensuing spreading of NAFTA-style FTAs in the continent.

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14. For a conceptual discussion on how development aspirations and free trade goals interact with each other as basic ingredients of the economic and political rationale for regionalism, see Gonzalez Vigil (2000: 5-7).

15. For an illustrative contrasting of 'new' with 'old' regionalisms in the LAC region, see Devlin and Esteveordal (2001: 3-9; 19-20).

Such a convergence not only facilitated the cohabitation of sub-regional PTAs pursuing the Common Market Model with –mostly bilateral– PTAs adhering to the FTA Model, but it also triggered synergies among most of the existing PTAs which, their competitive and at times quite tense juxtaposition notwithstanding, have made them all together contributed to another and even more important set of achievements in terms of growth and diversification of trade and investment attraction.

### 3.1 Key Characteristics Common to PTAs in the WH

Most of the main PTAs now existing in the WH, even those attached to different models of integration, share among themselves the following key features:

a) *Deep goods trade liberalization*

Tariff lines provide universal or near universal coverage, with few exceptions usually in the agriculture, energy and automotive sectors (Mackay; Robert and Plank-Brumback 2001: 127–8), and the envisaged tariff elimination process is very rapid. Most tariff lines have been totally liberalized up front, i.e. bringing them down to the zero tariff level right since the date of the PTA's entry into force. For the rest, the scheduled tariff reduction program is typically completed within a 10-year period. Negotiated exceptions rarely exceed 6% of total tariff lines. All the above implying that the bulk of intra-PTA trade within the WH will already be at zero tariff level by around 2005, the agreed year for the approval of the Treaty that will give birth to the FTA (Devlin and Estevadeordal 2001: 11 and Figure 3). At the same time, as already said before, average external tariffs have sharply declined, though some remain at levels above 20% specially in few sectors excepted by or under special regimes, such as the three mentioned at the beginning of this paragraph.

In addition, many NTMs (import prohibitions and surcharges, quotas) have also been dismantled up front. The rest (usually safeguards, some subsidies) are being phased out gradually under agreed PTA schedules or adjusted according to WTO commitments. But, on the downside, rules of origin have become more complex in NAFTA and NAFTA-type agreements, because the absence of common external tariffs makes of those rules the main mechanism for preserving the functioning of FTAs, and the use of this mechanism is rendered as even more crucial when FTAs aim at being comprehensive and/or when there are multiple PTAs involving several partners. In turn, more complex rules of origin open the way for discretionary administrative



procedures which may have diverting effects on trade and investment greater than relatively high external tariffs<sup>16</sup>.

b) *WTO – Plus Liberalization of Trade in Services*<sup>17</sup>

From the standpoint of GATT principles, all PTAs contain basic obligations about National Treatment. All but CARICOM do so with regard to MFN treatment as well, either in an unqualified form (Andean Community, MERCOSUR) or with some country-specific exceptions (NAFTA-type FTAs) to be specified at federal, state or province levels. Likewise, all adhere to the principle of Transparency and contain rules on the matter.

As for market access provisions, all PTAs cover the four modes of service supply, thereby including investments (commercial presence), though the treatment of people movement varies. All PTAs aim at universal coverage of sectors, though exceptions typically included are air transport, education, health, and also financial services in some NAFTA-type FTAs.

The right of countries to have their own domestic regulations is certainly acknowledged, but all PTAs state that such regulations should not include measures restricting the service supply under any mode (though NAFTA-type FTAs tend to narrow this to cross-border supply only); contain obligations to achieve mutual recognition of licenses and certifications of service suppliers; prohibit (MERCOSUR) or request notification (NAFTA-type FTAs) of new non-discriminatory quantitative restrictions and, in order to qualify the denial of benefits right, extend (all but MERCOSUR) the definition of beneficiary service supplier to a legal entity conducting substantial business operations in the territory of any WTO member.

c) *More Investment-friendly Legal and Regulatory Regimes*<sup>18</sup>

Coverage of investment chapters or provisions includes, in all PTAs, investments made before the agreement entered into force. The definition of investment is asset-based in most PTAs, including portfolio and intangible assets though with qualifications to avoid coverage of non-investment related (purely monetary or speculative) flows. When defining the investor, citizenship is the basic criterion for individuals, sometimes including permanent residents. The criterion varies for corporations. Whereas NAF-

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16. For a good comparative analysis of rules of origin in NAFTA, Group of Three and the Mexico–Costa Rica bilateral FTA, see Garay and Esteveordal (1996: 12–20 and Appendix).

17. The following three paragraphs on Services trade are largely based on Stephenson (2001a; 2001b).

18. The following four paragraphs on Investment rules are largely based on Robert (2001b; 2001d).

TA-type FTAs citizenship is determined by the site of incorporation while MERCOSUR prefers the seat or location of management.

Regarding principles, all PTAs provide for National Treatment and all but Andean Community and CARICOM for MFN treatment as well. There are, however, some important limitations in NAFTA-type FTAs, which usually qualify the granting of those treatments to "in like circumstances" and make reservations for non-conforming measures at federal and sub-federal levels.

Yet on the upside, all PTAs include the right of establishment with no admissions provision but often with a list of country-specific exceptions. Thus, WH PTAs add a market-access component to the protection element that is typical of investment agreements.

Another WTO-Plus feature refers to specific performance requirements, prohibited in NAFTA-type FTAs for both goods and services. Although this does not apply to export promotion, foreign aid programs, state enterprise procurement, and rules of origin include certain qualifications. Moreover, subsidies or investment incentives can be granted to locate production, provide a service, employ and train workers, construct or expand facilities, and carry out R&D.

*In sum*, from the above account of characteristics common to current PTAs in the WH it can be said that these PTAs are compatible parts of a modern rules-based system and are committed to economic openness and liberalization of goods and services flows. This, together with the obvious incentive provided by the exchanged preferences in market access, have undoubtedly contributed to the trade and investment results examined below.

### 3.2 Effects in Trade and Investment

#### a) *Salient trends in the 1990s*

Table 2 shows that total exports of the Latin American and Caribbean (LAC) region taken as a whole grew at an average annual rate of 8,4% during the 1990-1999 period, compared to 6,4% in the eighties<sup>19</sup> and higher than the 7,5% growth rate recorded by total exports of the entire WH over the same period. The export performance of the each of the five WH sub-regions shown in the table ranged from 11,9%

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19. Figures for the eighties are not shown in table 2, but are based on the same data sources.

**Table 2**  
**Western Hemisphere: Total and Intra-Regional Trade, 1990-1999**  
(Millions of US\$ and percentages)

	Exports			Imports		
	1990	1996	Annual Avg. Growth 1990-1999*	1990	1996	Annual Avg. Growth 1990-1999*
<i>Western Hemisphere</i>	632.702	1.071.955	7,5	744.149	1.213.204	8,3
Extra-Hemispheric	330.379	496.479	4,4	442.285	651.197	7,0
Intra-Hemispheric	302.322	575.475	10,3	301.864	562.008	10,1
Intra / Total	47,8	53,7		40,6	46,3	
<i>NAFTA</i>	537.226	918.077	8,0	676.970	1.053.426	8,2
Extra-NAFTA	307.297	485.698	5,2	449.865	636.292	6,8
Intra-NAFTA	229.930	432.379	10,9	227.104	417.134	10,8
Intra / Total	42,8	47,1		33,5	39,6	
<i>Latin America &amp; Caribbean</i>	136.177	249.332	8,4	111.970	247.943	11,3
Extra-LA & C	119.260	203.074	8,0	95.346	202.019	11,2
Intra-LA & C	16.917	46.257	11,1	16.424	45.925	11,6
Intra / Total	12,0	18,6		14,7	18,5	
<i>CACM</i>	4.096	7.778	11,9	6.538	12.300	11,9
Extra-CACM	3.388	6.192	11,3	5.897	10.739	11,5
Intra-CACM	658	1.586	14,9	641	1.561	15,7
Intra / Total	16,3	20,4		9,8	12,7	
<i>CARICOM</i>	4.647	5.439	3,7	5.526	7.708	8,2
Extra-CARICOM	4.156	4.568	2,9	5.056	6.922	8,0
Intra-CARICOM	491	872	9,5	469	786	10,4
Intra / Total	10,6	16,0		8,5	10,2	
<i>Andean Community</i>	31.751	45.687	3,5	17.315	36.965	8,2
Extra-AC	30.427	40.996	2,9	16.139	32.067	7,6
Intra-AC	1.324	4.691	12,9	1.176	4.898	14,9
Intra / Total	4,2	10,3		6,8	13,2	
<i>MERCOSUR</i>	46.402	74.998	5,4	29.293	83.217	11,8
Extra-MERCOSUR	42.275	57.960	3,8	25.053	66.124	11,1
Intra-MERCOSUR	4.127	17.038	15,6	4.240	17.092	15,4
Intra / Total	8,9	22,7		14,5	20,5	

\* The annual average growth rates of CARICOM were calculated from for the 1990-1997 period.  
Source: IDB Statistics and Quantitative Analysis Unit, based on official country data

in the CACM to 3,5% in the Andean Community, but in all cases trade growth recovered significantly in the 1990s compared to the 1980s.

The same table also shows that total imports grew even faster: at a 11,3% rate for the LAC region in 1990-1999, compared to only 4,1% in the eighties and much higher than the 8,3% rate for the whole WH in the nineties. Import growth rates were quite similar among the five WH sub-regions, and in all cases but CACM higher than the respective export growth rates.

Faster import demand, plus the fact that extra-LAC region exports and each of the extra-(sub-regional) PTA exports grew all at rates higher than in the 1980s, means that LAC integration was in the 1990s characterized by one of the traits typical of the Latin American version of an "open regionalism" process<sup>20</sup>. Such trait was present in the LAC sub-regional PTAs as well, and even among the more vocal followers of the Common Market model: the Andean Community and MERCOSUR. This important feature implies that these sub-regions were successful in their efforts of rendering themselves consistent with the open-economy development strategy then prevailing in the region.

At the same time, intra-PTA trade growth was experienced in all sub-regions and in all cases (intra-PTA exports and intra-PTA imports) it was higher than total trade growth during the 1990s. The same holds true for the entire LAC region and the WH as a whole, given the trade weight of the five sub-regions shown in table 2. Since there can be little doubt that integration as such has been the main factor behind the significant dynamism of intra-PTA trade, it can be fairly said that "PTA-led trade growth"<sup>21</sup> has been an important component of the positive trade performance of WH countries during the last decade. What makes this result even more noteworthy is the fact that it went along with the also positive performance in extra-PTA trade already mentioned in the preceding paragraph.

In qualitative terms, the contribution of integration to growth of manufactured exports has been much more significant, as it was considerably higher than total export growth and particularly so in the cases of NAFTA, the Andean Community and MERCOSUR. As

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20. For a useful comparative analysis of the original Asia Pacific version of open regionalism with the version implemented in the Latin American region, see Kuwayama (1999).

21. Or "agreement-led growth in trade", using the words of Devlin and Ffrench-Davis (1998: 7).

a result, the share of manufactures in intra-PTA trade increased during the 1990s<sup>22</sup>, very sharply so in the case of Mexican exports to NAFTA. In the Andean Community and MERCOSUR cases, the predominance of manufactures in their respective intra-exports has to be underlined. This is a truly remarkable feature given the dominant primary composition of total exports from most of their member countries (table 3).

**Table 3**  
**Intra-Regional Trade of Manufactured Goods, 1990-1997**  
(Millions of US\$ and percentages)

	Exports			Imports		
	1990	1996	Annual Avg. Growth 1990-1997	1990	1996	Annual Avg. Growth 1990-1997
<i>Mexico</i>	13.032	80.304	32,5	32.221	76.997	16,6
Extra-NAFTA	2.624	9.868	22,5	7.654	16.061	15,0
Intra-NAFTA	10.408	70.436	34,5	24.567	60.936	17,1
% manufactures intra-trade	49,4	80,6		82,3	85,5	
<i>Andean Community</i>	4.495	9.187	10,3	15.216	30.705	13,5
Extra-AC	3.854	6.350	5,9	14.574	27.868	12,8
Intra-AC	641	2.837	25,9	641	2.837	25,9
% manufactures intra-trade	51,1	56,7		51,1	56,7	
<i>MERCOSUR</i>	22.562	37.516	9,3	20.553	70.444	22,4
Extra-MERCOSUR	20.347	26.695	4,6	18.339	59.623	21,2
Intra-MERCOSUR	2.215	10.821	30,2	2.215	10.821	30,2
% manufactures intra-trade	59,1	59,1		51,6	59,1	

Source: United Nations Statistics

Due to the dominant weight of the USA market, most of the manufactured products exported by LAC sub-regions have traditionally gone to the WH. This has continued to be a fact during the 1990s, and increasingly so except for the CACM case (table 4). But the novel trend has been that, within the WH, the LAC region has gained importance as a destination market for the manufactures exports of not only almost all of the LAC sub-regions (the CACM being again the exception) but for those of NAFTA as well. When total

22. In addition, it seems that the share of intra-industry trade in total intra-PTA trade, of manufactures especially, has also tended to increase. For evidence on the matter in the Andean Community, see Echavarría (1998).

**Table 4**  
**Destination of Manufactured Exports**  
 (Percentage of total manufactured exports)

	NAFTA			CACM		
	1990	1996	Avg. 1990-1999	1990	1996	Avg. 1990-1999
Western Hemisphere	50,3	55,5	49,0	95,0	92,4	92,3
Intraregional	45,1	48,8	43,2	48,7	45,3	46,9
European Union	21,4	16,0	16,1	3,2	5,4	4,4
East Asia <sup>1</sup>	15,1	19,1	14,9	0,3	0,4	1,4
Rest of World	13,2	9,5	10,0	1,5	2,3	1,8
	Andean Community			MERCOSUR		
	1990	1996	Avg. 1990-1999	1990	1996	Avg. 1990-1999
Western Hemisphere	70,5	83,6	81,9	52,2	70,3	66,0
Intraregional	14,5	38,5	32,6	10,5	34,2	26,7
European Union	15,2	9,0	9,7	22,5	16,2	17,5
East Asia <sup>1</sup>	5,6	3,1	3,4	10,8	6,0	6,8
Rest of World	8,8	4,3	5,1	14,5	7,5	9,7

1/ Hong Kong, Indonesia, Korea, Japan, Malaysia, Philippines, Singapore, Taipei-China and Thailand.  
 Source: IDB Integration and Regional Programs Department

**Table 5**  
**Western Hemisphere - Direction of Trade**  
 (Percentage of total exports or imports by region)

NAFTA	Exports to			Imports from		
	1990	1996	Avg. 1990-1999	1990	1996	Avg. 1990-1999
Andean Community	1,4	1,6	1,7	2,5	2,1	1,9
CARICOM	0,5	0,4	0,4	0,3	0,3	0,3
CACM	0,6	0,8	0,8	0,5	0,7	0,7
MERCOSUR	1,4	2,3	2,1	1,8	1,3	1,4
Latin America & Caribbean <sup>1</sup>	4,9	6,4	6,1	5,8	5,0	4,9
NAFTA	42,8	47,1	48,0	33,5	39,6	38,5
Western Hemisphere	47,7	53,5	54,1	39,3	44,6	43,4
European Union	20,7	15,8	16,8	18,2	15,9	16,5
East Asia <sup>2</sup>	17,7	20,1	17,8	24,5	25,2	25,0
Rest of World	13,9	10,6	11,2	18,0	14,3	15,1

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<i>CACM</i>	Exports to			Imports from		
	1990	1996	Avg. 1990-1999	1990	1996	Avg. 1990-1999
Andean Community	0,8	1,7	1,5	9,2	6,5	6,6
CARICOM	1,1	0,7	0,7	0,1	0,3	0,4
CACM	16,3	20,4	20,9	9,8	12,7	12,5
MERCOSUR	0,2	0,2	0,2	2,6	2,1	2,3
Latin America & Caribbean <sup>1</sup>	21,4	26,5	26,7	24,0	24,9	25,0
NAFTA	45,3	43,2	44,6	46,2	52,5	52,1
Western Hemisphere	66,7	69,7	71,3	70,2	77,4	77,1
European Union	25,1	23,8	21,4	13,6	9,9	10,0
East Asia <sup>2</sup>	3,3	2,4	3,3	8,6	6,8	7,6
Rest of World	5,0	4,0	4,0	7,6	5,9	5,3
<i>CARICOM</i>	1990	1996	Avg. 1990-1997	1990	1996	Avg. 1990-1997
Andean Community	1,1	2,2	2,0	4,8	7,8	5,8
CARICOM	10,6	16,0	13,9	8,5	10,2	9,2
CACM	0,1	0,4	0,5	0,5	0,7	0,7
MERCOSUR	1,3	1,0	1,6	3,7	2,1	2,3
Latin America & Caribbean <sup>1</sup>	14,1	21,5	19,7	17,8	21,4	18,7
NAFTA	40,8	44,0	41,8	49,0	49,8	50,9
Western Hemisphere	54,9	65,5	61,5	66,8	71,2	69,6
European Union	21,6	19,1	20,8	17,4	16,0	16,0
East Asia <sup>2</sup>	2,0	2,4	2,2	5,6	7,0	7,4
Rest of World	21,6	13,1	15,6	10,1	5,7	7,0
<i>Andean Community</i>	Exports to			Imports from		
	1990	1996	Avg. 1990-1999	1990	1996	Avg. 1990-1999
Andean Community	4,2	10,3	9,8	6,8	13,2	11,0
CARICOM	0,9	1,1	1,4	0,4	0,3	0,4
CACM	1,6	1,7	1,8	0,2	0,3	0,3
MERCOSUR	2,8	3,6	3,6	8,7	7,2	7,7
Latin America & Caribbean <sup>1</sup>	13,7	20,7	20,6	19,1	24,3	22,4
NAFTA	49,0	49,3	47,3	42,7	42,2	41,8
Western Hemisphere	62,7	70,0	67,9	61,8	66,5	64,2
European Union	19,1	15,9	16,5	23,8	18,7	19,1
East Asia <sup>2</sup>	5,1	4,5	4,6	7,5	9,8	10,4
Rest of World	13,1	9,6	11,0	6,9	6,4	6,2

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MERCOSUR	Exports to			Imports from		
	1990	1996	Avg. 1990-1999	1990	1996	Avg. 1990-1999
Andean Community	3,1	4,2	4,4	3,3	2,4	2,3
CARICOM	0,3	0,2	0,2	0,2	0,1	0,1
CACM	0,3	0,3	0,4	0,0	0,0	0,0
MERCOSUR	8,9	22,7	19,5	14,5	20,5	19,5
Latin America & Caribbean <sup>1</sup>	15,3	31,8	28,5	20,5	25,1	24,2
NAFTA	23,9	17,4	19,3	22,3	24,5	24,6
Western Hemisphere	39,2	49,2	47,8	42,8	49,6	48,8
European Union	31,8	24,4	26,8	22,6	26,4	26,4
East Asia <sup>2</sup>	11,1	10,9	10,0	9,1	10,5	10,9
Rest of World	17,9	15,5	15,5	25,4	12,1	13,9

1/ Excludes Mexico.

2/ Hong Kong, Indonesia, Korea, Japan, Malaysia, Philippines, Singapore, Taipei/Taiwan-China and Thailand.

Source: IDB Statistics and Quantitative Analysis Unit, based on official country data.

exports are considered and Mexico is excluded from the total LAC figure (as in table 5), a similar trend regarding the rising importance of LAC as a destination market applies, and this time without sub-regional exceptions<sup>23</sup>. Such a trend was only partially reversed during the crisis years (1997-1999).

Another interesting feature of LAC sub-regional PTAs is the concentration of their respective exports in the two largest economies belonging to each PTA. During the 1990s, Jamaica and Trinidad & Tobago have on average accounted together for almost 80% of total CARICOM exports, Colombia and Venezuela for about 40% of intra-Andean Community exports. The dominant weight of Argentina and Brazil together in MERCOSUR trade (Steinfatt and Contreras 2001: 16-7, 22-4) is clear<sup>24</sup>.

Regarding investment flows, the positive signals sent by economic reforms and open regionalism made both the Andean Community and MERCOSUR countries more attractive as recipients of FDI inflows in the 1990-1997 period, though the subsequent crisis years sharply reduced the respective share of the Andean Community (table 6). Within the Andean Community, the main recipients of FDI inflows during the 1990s have been Colombia, Venezuela and Peru, and within MERCOSUR, Brazil and Argentina. In explaining the preferred country locations of FDI, the size of the market has continued to be the dominant motivation, though in the 1990s the target market has increasingly been not just the country's domestic

23. For similar findings, see Kuwayama (2001: 1-6 and Table 1).

24. For earlier evidences of the country concentration in the LAC region trade flows, see ALADI (1991).



but the extended market provided by PTAs. Countries that most benefited in this regard were those that chose to include the expected advantages of an extended market as an important objective of their macro-economic and trade policy mix. These were the cases of Colombia and Venezuela in the Andean Community's sub-regional market, and of Brazil in MERCOSUR's. Meanwhile, privatization programs (of public utilities and services activities, especially) have weighted relatively more in explaining FDI inflows to Argentina and Peru<sup>25</sup>.

**Table 6**  
**Share of FDI Inflows by Western Hemisphere Subregion**

Subregion	1990	1997	1999
NAFTA	91,7	71,5	80,3
Andean Community	1,8	7,9	2,0
MERCOSUR	4,6	15,3	14,2
CARICOM	0,6	0,9	0,4
CACM	0,1	0,2	0,2

Source: OAS Trade Unit, based on UNCTAD data.

Simultaneously, economic reforms and open regionalism have also allowed for LAC becoming the developing region with the highest increasing rate in FDI outflows (table 7), most of which have been invested within the same LAC region, very often in order to take advantage of the opportunities given by privatization and deregulation measures (See Ocampo, Bajraj and Martin 2001: 39-52, 57-86).

**Table 7**  
**FDI Outflows**  
(Millions of US\$ and Shares)

Region	1991	1999	1991-1999 % Change
World	198.143	799.928	303,7%
Developed countries	95,8%	91,5%	285,6%
Developing countries	4,2%	8,2%	688,5%
Africa	0,5%	0,1%	-22,8%
Latin America and the Caribbean	0,3%	3,4%	3.996,7%
Developing Europe	0,0%	0,0%	
Asia	3,9%	4,7%	376,3%
Pacific	0,0%	0,0%	850,0%
Central and Eastern Europe	0,0%	0,3%	6.727,0%

25. For data and case-study evidence supporting the statements in this paragraph regarding the Andean Community countries, see Gonzalez Vigil (2001a: 29-37 and Annexes); and regarding MERCOSUR countries, see Chudnovsky *et al.* (2001: 5-22).

b) *Some relevant implications*

There can be no doubt that the reviewed trends referring to the manufactured goods's component of intra-PTA exports and to investment flows are, to some extent, the result of trade and investment-diverting effects typical of most PTAs. Available studies point clearly to restrictive rules of origin as the main source of such effects in the case of NAFTA<sup>26</sup>, whereas for the MERCOSUR case, there is a debate on the matter. While relatively high tariff preference margins have been signaled as the main source of similar diverting effects in MERCOSUR, other studies have analyzed evidences rather indicating the existence of important trade creation effects<sup>27</sup>.

But the aforementioned trends do show the contribution of PTAs to their members' objectives of industrialization and economic development. Such contribution helps in understanding one of the key strategic reasons behind LAC countries' strengthening their sub-regional integration efforts instead of neglecting them, their interest on the new vision of Hemispheric integration notwithstanding.

The concentration of trade and investment flows recorded within each PTA (intra-PTA flows included) in a couple of member countries raises concern about the possible devastating effects of the bilateral "hub-and-spoke" approach to free-trade in the WH, in terms both of the ensuing realignments in the location of investments and in the directions of trade within the WH, as well as of the possibilities of survival left to the sub-regional agreements.

#### 4. THE FTAA PROCESS

In all fairness, what it is really going on in the WH is a "FTAA cum summitry" process, as Richard Feinberg correctly defines it when he explains that

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26. Gilmore (2000) discusses on pp. 395-8 the evidence showing how NAFTA's stingy rules of origin have diverted trade and investment away from third countries in favor of Mexico. See also Esteveordal (1999).

27. Yeats (1997) considers tariff preference margins in MERCOSUR as high and on pp. 18ss. arrives at the conclusion that much of the increase in its intra-exports has been in products which have not been successfully exported to third countries, such as automobiles. Nagarajan (1998) has a different view, and on pp. 16-24 shows that intra-MERCOSUR imports are dominated by products which embody standard or intermediate technology, while its imports from industrialized countries, which have also grown strongly, continue to be composed mostly of high technology products. In turn, Esteveordal and Goto and Saez (2000), with the help of a Krugman-type trade model based on imperfect competition and product differentiation, arrive on p. 33 at the conclusion that MERCOSUR integration creates trade and increases the the welfare of members and non-members alike.

from its inception the FTAA has been embedded in the broader process of the summits of the Americas (...). Free trade is just part—albeit a critical part—of the comprehensive economic, social and political mandates issued at the Americas' summits (...) the trade initiative is deeply embedded in a much broader Hemispheric agenda (Feinberg 2000: 4).

This agenda was set out in the *Americas Plan of Action* approved at the I Summit of Heads of State and Government (Miami, December 1994), which points out four fundamental objectives: preserving and strengthening the community of democracies; promoting prosperity through economic integration and free trade; eradicating poverty and discrimination; and, guaranteeing sustainable development and conserving the natural environment for future generations. In order to implement the plan, 23 cooperative initiatives with over 150 action items were included: 8 initiatives dealing with democracy, 12 with poverty and 3 with sustainable development. All of them together amounting to a truly strategic agenda for interdependence and cooperation for development in the WH (Salazar-Xirinachs 2001a: 294–5), which ties umbilically with the trade initiative become more visible when in their III Summit (Quebec, April 2001) the leaders of the Americas adopted a “democratic clause” making the commitment to democratic government a condition to participate in the summitry process, a condition that would likely apply to the FTAA (sub-) process as well (Robert 2001c: 12).

The scope of this paper, focused on PTAs, justifies the concentration of the discussion that follows on the trade component (FTAA) of such a comprehensive hemispheric agenda.

#### 4.1 FTAA: Progress made (as of May 2001)

It is useful to distinguish three phases in what has happened thus far since the FTAA process was launched at the I Summit of the Americas<sup>28</sup>. First there was a *preparatory phase*, elapsed from December 1994 until the II Summit (Santiago, April 1998), during which the mechanisms for the negotiations were implemented. These being the Ministerial Meetings; a Trade Negotiations Committee (TNC); nine Negotiating Groups (on market access; agriculture; investments; services; government procurement; intellectual property rights; subsidies, antidumping and countervailing duties; competition policy; and dispute settlement); three non-negotiating committees (on smaller economies, participation of civil society, and electronic commerce); and a Tripartite Committee, in

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28. This paragraph, plus the following two, are largely based on Salazar-Xirinachs (2001a: 281–90). For another analysis on what it was achieved in the FTAA process up to the year 2000, see Bouzas and Svarzman (2001: 2–16). The basic information on the FTAA process can be obtained through the respective official web page: [www.alca-ftaa.org](http://www.alca-ftaa.org)

charge of providing technical and logistical support to the negotiations and composed by the Organization of American States (OAS), the Inter-American Development Bank (IADB) and the United Nations Economic Commission for Latin America and the Caribbean (ECLAC).

Trade ministers exercise the ultimate oversight and management of the Negotiations, while the TNC —composed of the Trade vice-ministers— plays a central role in managing the negotiations and has the responsibility of guiding the work of all the aforementioned groups and committees. Their workings along the preparatory phase generated comprehensive databases and compendiums of laws and regulations in WH countries and PTAs, as well as other background information and technical analysis useful for the upcoming negotiations.

Then came the *second phase*, elapsed from April 1998 until the III Summit of the Americas (Quebec, April 2001), where the substantive negotiations actually started, and which main achievements can be summarized as follows: the preparation of a first complete draft of the FTAA agreement (with brackets where no consensus was reached) for it to serve as the text for negotiations thereafter; the decision to implement 18 specific business facilitation measures, eight of these customs-related and 10 transparency-related<sup>29</sup>, and significant increases in the supply of trade-related technical cooperation and capacity-building activities, in face of growing demand for them propelled by the on-going and programmed negotiations.

Since the III Summit, the FTAA process has entered into its *third phase*, where the "real action" will likely heat on<sup>30</sup>. Early on April 2001, the VI FTAA Ministerial Meeting held at Buenos Aires adopted the first complete draft of the FTAA agreement, released it to the public in a demonstration of transparency and communicative attitude towards the civil society, and instructed the TNC to prepare (between May 2001 and October 2002) a second version of the draft agreement trying to eliminate the brackets to the maximum extent possible. At the same time, the ministers agreed on a deadline for the negotiations on market access, by which they instructed the related negotiating groups to submit to the TNC their recommendations on methods and modalities by April 1, 2002 and to start these negotiations no later than May 15, 2002. They also established the Technical Committee on Institutional Issues (TCI) with the mandate of making recommendations on the overall architecture of the FTAA agreement, in view of the preparation of the chapters on general and institutional aspects to be included in the second version of the draft.

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29. The progress on business facilitation in the FTAA process is analyzed by They (2001).

30. This paragraph and the next one are largely based on Robert (2001c: 11-6).

The above issues were endorsed a few weeks later by the Leaders of the Americas in Quebec. There, besides adopting the "democratic clause" already mentioned and calling for the drafting of a "democratic charter", they agreed that the FTAA negotiations should be concluded no later than January 2005 and to seek the entry into force of the FTAA Treaty no later than December 2005. They also restated that the agreement should be comprehensive, WTO-consistent and balanced. Closely linked to this latter concept, the Leaders stressed the importance that the agreement should take into account the differences in size and development levels of the participant economies, and requested the Tripartite Committee to consider favorably the technical assistance needs related to FTAA issues of the smaller economies in particular. As for the procedure to reach the agreement, the Leaders confirmed that it should constitute a single undertaking, i.e. a single package where nothing is agreed until everything is agreed. In this regard, it is very pertinent to take due notice that in Buenos Aires the ministers had stated the right of any delegation to present proposals on any issue it deemed relevant, which seems to pave the way for the inclusion in the bracketed draft of issues thus far contentious such as labor and environmental standards.

#### 4.2 FTAA Prospects: some desirable outcomes

As said before, the "real action" in the FTAA process is just starting. There are, in principle, various sorts of prospective exercises that could be applied in order to figure out the possible alternative scenarios ahead<sup>31</sup>. But, for the purposes of this paper, it seems preferable to limit the reflections on the matter in a way closely linked to the issues analyzed in the previous sections of the paper. Concretely, this means discussing about the potential outcomes in the FTAA process from two specific angles: first, the desirable incremental contribution FTAA should bring to the WH as a whole on top of the important contributions already made by the existing PTAs during the 1990s (as seen in Section III); and second, the difficult interaction between the Hemispheric free trade zone being built and the sub-regional PTAs adhering to a Common Market model in the WH (as seen in Section II).

##### a) *FTAA's desirable value added*

Given the undeniably substantive contribution made by the existing PTAs within the WH to the progress already achieved in the Americas during the 1990s, in terms of accelerated liberalization, convergence of rules and disciplines, and growth and

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31. For example, Scollay (2000a) first advances in pp. 33-36 a qualitative exploration on alternative scenarios of possible regional configurations in the WH and Asia Pacific, and then together with Gilbert and Bora (2001) assesses quantitatively, using a Computer General Equilibrium (CGE) model, the potential impact of those possible configurations to participants and third economies.

diversification of trade patterns and investment attraction, what value added should be expected from FTAA? Evidently, there is no one but many possible answers. What may be deemed as a desirable outcome varies depending on the relative levels of development of the participant economies, their bargaining capabilities at the negotiations, the technical skills and ideological inclinations of the relevant actors, and so forth.

The list of desirable outcomes that follows, therefore, is just *one* answer expressing nothing else than a personal point of view, which of course reflects somehow a particular perspective proper to a native of an Andean developing economy, but which does not have pretend any representative authority, even though it takes into account the opinions of business people and experts on the matter<sup>32</sup>.

- *On market access*: simultaneous yet differentiated tariff reduction schedules according to relative development levels; consolidation of ATPA and CBTPA programs, with enlarged product coverage; effective dismantling of non-WTO conforming NTMs and equitable treatment of the remaining ones according to their impact on trade, production and factors intensity; a simple and transparent rules of origin regime, with non-discretionary administrative procedures.
- *On investment, services and competition disciplines*: an agreement that the provisions on services should not discriminate against non-member economies, similarly to prior decisions on investment; to reduce the remaining divergence in most relevant rules and disciplines (especially on investment regulation, all modes of service supply, enforcement of intellectual property rights and related technology development issues); cooperation for the development of competition policy laws and agencies across the Hemisphere, and concrete steps towards the inclusion of criteria to deal with trans-border effects in competition rules and their enforcement procedures.
- *On business facilitation*: effective concerted measures to remove obstacles so the private sectors of all the participant economies can profitably take advantage of business opportunities in the whole Hemisphere

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32. The WH private sector is organized in the Business Network for Hemispheric Integration in order to reach consensus in the business sector on each one of the negotiation issues and to channel them to the FTAA's Trade Ministers. The results of this private sector involvement in the FTAA process, including the proposals prepared in each of the Americas Business Forum (ABF) that have taken place thus far back-to-back each of the FTAA Ministerial Meetings, can be consulted at [www.bnhi.org](http://www.bnhi.org). Experts are involved on a permanent basis, and so far there have been two Academic Colloquiums of the Americas. The reflections and proposals presented at the second colloquium held in Buenos Aires (April 3-4, 2001) just before the VI ABF (April, 5-6) and the VI Ministerial Meeting (April 6-7), including those quoted in Gonzalez Vigil (2001b), can be consulted at [www.iadb.org/intal](http://www.iadb.org/intal)

- *On technical and economic cooperation*: to guarantee a sustained commitment toward liberalization through effective human, physical and institutional capacity-building needed to benefit from liberalization
- *More generally*: to provide for a decisive "lock-in" of market, corporate and public policy reforms, by exponentially raising the potential benefits of liberalization and economic integration, supported by reduced political costs and social imbalances through the other components of the Summitry Plan of Action for the Americas.

b) *FTAA and sub-regional PTAs*

In Section II it was explained that tensions between the Common Market-type sub-regional PTAs and the projected Hemispheric FTA subsided from 1994 onwards, when the USA approach changed from the bilateral "hub-and spoke" to the "Western Hemispheric Round" (WHR) one. Although the lack of fast-track authority was a factor explaining such a change, high credits should be granted to the Clinton Administration for adopting an approach such as the "WHR" that, in the first place, democratically gave to almost all (but Cuba) countries and territories of the Americas the possibility of simultaneously participating in a process of substantive repercussions for the future well-being of their peoples and that, secondly, allowed the FTAA Ministers to agree that the FTAA will co-exist with "FTAA-Plus" sub-regional and bilateral PTAs of the WH<sup>33</sup>.

To the extent that this latter is a decision that must be validated through acts and not just words, it can be assumed that LAC countries will likely keep trying to strengthen their sub-regional Common Market-type PTAs and even some of their bilateral or plurilateral FTA-type agreements, in order to render them "FTAA-Plus" and so be able to count on them in addition to the FTAA. Given the positive role some existing PTAs are playing as tools for industrialization, trade and investment flows, if eventually that decision does not find its way to implementation, it is not hard to imagine a potentially conflictive situation as more than just a few FTAA participants would feel caught in a sort of "prisoner's dilemma" facing highly uncertain strategic options<sup>34</sup>.

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33. As it follows from paragraph 5(b) of the statement issued by the III FTAA Ministerial Meeting (Belo Horizonte, May 16, 1997). Da Motta Veiga (1997: 3-4, 7-9) explains how this and other results of that ministerial meeting chaired by Brazil were reached in a context of conflicting rhetoric and contention between the named country and the USA.

34. Devlin; Esteveordal and Garay (1999: 27-36), elaborate skilfully on this matter and suggest some criteria for a smooth co-existence of the FTAA implementation with existing PTAs in the WH.

In fact, tensions may arise again as a consequence of recent events signaling the coming back of the "hub-and spoke" approach. It is so that in December 2000 Chile and the USA started to negotiate a bilateral FTA, a move that made MERCOSUR halt its review of the full membership requested by Chile in July 2000, a request that had been warmly received in MERCOSUR countries and others of South America as well. (See, for instance, Taccone and Nogueira 2000: 82-3). A few months later (April 2001), a Colombia, Mexico and Venezuela Presidential Summit was convened to give new momentum to the "Group of Three" agreement, a move that perhaps would increase doubts about the Andean Community's capability of consolidating its still imperfect Customs Union.

In such new context, the following seems desirable:

- a) The USA should continue to give top priority to the "WHR" as the main approach for the building-up of the FTAA.
- b) In addition, if for the purpose of accelerating the FTAA building process, the USA feels necessary to complement the "WHR" negotiations with "hub-and-spoke" inroads, it may do so (either bilaterally or, even better, together with its NAFTA partners) through FTA negotiations with each of the Common Market-type sub-regional agreements existing in the WH.
- c) This procedure would not only cause less trade and investment-diverting effects –negative for LAC sub-regions– than the bilateral "hub-and-spoke" approach, but it could also work in favor of the progressive networking of a pro-industrialization division of labor ("flying-geese style") within the WH.
- d) In the event that such a procedure may raise concern in Mexico about the ensuing potential losses of its NAFTA-status privileges in front of countries such as Argentina and Brazil, North American partners could always have the possibility of deepening their NAFTA agreement through many devices, including (why not?) the incorporation of more Customs Union-type instruments and regulatory procedures<sup>35</sup>.

## SOME CONCLUDING REMARKS

A PTA such as the FTAA will unquestionably have enormous repercussions on the world economy at large. On its prospected member economies of the Americas, the effects will

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35. According to Weston (1996: 92), there are already a number of activities (computers, computer parts and local area networks) where NAFTA would appear to operate as a Customs Union. For an earlier assessment considering these as good precedents, particularly when contrasted with NAFTA's intricate rules of origin for the automobile and textiles and apparel sectors, see Hufbauer and Schott (1993: 7).



greatly depend on what the on-going negotiations finally produce in terms of what it has been already said about a suitable value added in some of the main issues being negotiated. Those effects will also greatly differ depending on what approach —“WHR” or “hub-and-spoke”— finally dominates the process. To a large extent, the same applies when thinking on the possible effects of FTAA in non-member economies. Since in this case there is also the additional and fundamental question of the level of discrimination towards non-members, and given that the European Union plus other major players in the global arena certainly have the means to defend their interests at home and globally, the multilateral trading system has the imperious task of quickly adopting or updating the preventive measures aimed at duly protecting the world welfare<sup>36</sup>.

In such view, the WTO should constructively overcome the vagueness nested in Article XXIV, particularly in order to improve the operational review process with the help of multilaterally agreed criteria built on strong empirical foundations. There is also a need for better multilateral guidelines to broaden the common base among PTAs and so reduce the costs caused by the “spaghetti bowl” of discrepant arrangements in the WH and elsewhere in the world<sup>37</sup>.

The above obviously applies also to, and it is obviously a source of concern for, the non-FTAA members of APEC, considered individually. But as for APEC as a whole, to some extent it can be said that FTAA should not represent a problem for it. Open regionalism can co-exist with PTAs, and as yet APEC as such has had no problems with the European Union. But the novelty, of course, is the partially overlapping memberships of FTAA and APEC. Given this, it would be desirable that:

- a) FTAA be born containing rules of origin less restrictive than NAFTA's, as well as investments and services chapters the least discriminatory as possible
- b) APEC could arrive at an agreement on the principles about its members' PTAs that would be helpful keeping them compatible with open regionalism<sup>38</sup>.
- c) In view of some APEC members' recent interest on establishing PTAs with WH countries, APEC may effectively promote that such trans-Pacific negotiations be with LAC sub-regional agreements instead of bilateral ones.

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36. For a detailed review of the issues entailing possible complex interactions between the FTAA and WTO, see Granados (1999: 12ss.).

37. For a lucid discussion of main loopholes in Article XXIV giving too wide room for almost any PTA to claim its “WTO-consistency”, see Scollay (2000b: 3-7). Findlay (2000: 21-5) coincides and extends the discussion to GATS (V) as well.

38. See, for instance, the guiding principles proposed by Elek (2000: 18-21).

- d) APEC could actively encourage trans-Pacific initiatives of wide-scope membership, such as the recent EALAF (East Asia and Latin America Forum) and the ADB-IDB co-sponsored TBN (Trans-Pacific Business Association) and LAEBA (Latin America/Caribbean and Asia/Pacific Economic & Business Association).

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