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Trade Integration in the Americas

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Summary

Since the 1990s, the countries of Latin America and the Caribbean have been a focus of United States trade policy, as demonstrated by the passage of the North American Free Trade Agreement (NAFTA), the U.S.-Chile free trade agreement (FTA), and, more recently, the Central America-Dominican Republic Free Trade Agreement (CAFTA-DR). The Bush Administration has made bilateral and regional trade agreements important elements of U.S. trade policy. The United States currently is in the process of completing trade negotiations with Andean countries for an FTA and on reactivating talks for a U.S.-Panama FTA and a Free Trade Area of the Americas (FTAA). The FTAA is an on-going regional trade initiative that was first discussed in 1994 and formally started in 1998. The last FTAA trade ministerial meeting was held in Miami in November 2003, but the talks are currently stalled.

The efforts of the United States in regional trade integration in the Americas are significant for Congress because U.S. entry into any free trade agreement may only be done with the legislative approval of the Congress. U.S. supporters of trade integration in the Americas believe it helps U.S. economic and political interests in several ways. Proponents believe that the movement towards trade integration of the Americas is beneficial for U.S. prosperity, and also serves to strengthen democratic regimes and support U.S. values and security. Forming closer economic relations with countries in the region is seen by some as a means to improve cooperation on other issues such as the environment and anti-drug efforts. U.S. opponents of trade integration proposals are mainly concerned that hemispheric free trade would lead to a loss of jobs in the United States through increased import competition or as a result of U.S. companies shifting production to lower-wage countries with weak labor standards.

The number of regional trade agreements in the Americas has been increasing since the 1990s. Major trade arrangements include NAFTA, CAFTA-DR, the Southern Common Market (Mercosur) in South America , the Andean Community (CAN), the Caribbean Community and Common Market (CARICOM), the Central American Common Market (CACM), and the Latin American Integration Association (ALADI). With a total of 12 trade agreements involving over 40 countries, Mexico is one of the countries with the highest number of agreements. Supporters note that if countries in the Western Hemisphere ultimately establish an FTAA, it could have as many as 34 members and nearly 800 million people, nearly twice the population of the European Union.

Trade integration in the Americas is of interest to policymakers because of the implications for the United States. Issues under debate include the pros and cons of deepened trade relations with Latin America and the Caribbean, and whether the current focus on bilateral and regional FTAs is the most appropriate trade policy. Some analysts do not believe that such a policy is a good idea because it is creating a complicated network of trade agreements throughout the region could slow down the FTAA process. Others believe that regional trade agreements lead to the consolidation of regional trade areas into larger free trade areas, and although a slow process, may eventually lead to a hemispheric free trade area.

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The efforts of the United States in regional trade integration in the Americas are significant for Congress because U.S. participation in any free trade agreement may only be done with the legislative approval of the Congress. Trade is a controversial issue for Congress. This report provides background information and analysis on U.S. trade policy with Latin America.

What Are Regional Trade Agreements?

Regional trade agreements (RTAs) are trade arrangements under which member-countries grant each other preferential treatment in trade. RTAs may be categorized as bilateral, multilateral, or sub-regional. With no formal definitions, these terms are sometimes used loosely to describe various groupings. A bilateral trade agreement is usually an agreement between two countries to reduce tariffs and quotas on items between themselves. While this definition seemingly indicates an agreement between just two countries, it is sometimes used to describe trade agreements involving more than two countries.

There are a number of types of arrangements including free trade agreements, customs unions, common markets, and economic unions.[1] Free trade agreements (FTAs) are the most common form of regional economic integration in which members of a group remove tariffs and some nontariff barriers to trade among

[1] In addition to the trade arrangements described in this section in which member countries extend *reciprocal* preferential treatment, there are trade arrangements under which one party agrees to extend nonreciprocal preferential treatment to the imports of a country or group of countries unilaterally. Such arrangements primarily involve developed countries extending nonreciprocal preferential treatment to the imports from developing countries.

member countries.[2] At the same time, each member retains its independent trade policy, including its tariffs, towards nonmember countries. FTAs are those in which member countries agree to eliminate tariffs and nontariff barriers on trade in goods within the free trade area, but each country maintains its own trade policies, including tariffs on trade outside the region. FTAs account for 84% of all RTAs in force in the world, and 96% of those that are pending. The likely reason there are more FTAs than customs unions is that they can be concluded more quickly and require less policy coordination among members. In an FTA, member countries maintain their own trade policy vis-a-vis non-member countries.[3] The U.S.-Chile free trade agreement is an example of a bilateral FTA.

Customs unions are agreements in which members conduct free trade among themselves and maintain a common trade policy towards non-members. These agreements require the establishment of a common external tariff and harmonization of external trade policies. Such agreements imply a greater loss of autonomy over the parties' commercial policies and require longer and more complex negotiations and implementation periods. Geographical considerations play an important role in defining the objective of economic, and sometimes political, integration among the member countries.[4] The Southern Common Market (Mercosur) in South America is an example of a customs union.

Common markets are those in which member countries go beyond a customs union by eliminating barriers to labor and capital flows across national borders within the market. The European Union is the most prominent example of a common market.

In economic unions, member countries merge their economies even further than common markets by establishing a common currency, and therefore a unified monetary policy, along with other common economic institutions. The 12 members of the European Union that have adopted the euro as a common currency is the most significant example of a group of countries that has gone from a customs union to an economic union.

Growth of Regional Trade Agreements

Between January 2004 and February 2005, the World Trade Organization (WTO) received notification of 43 new RTAs, "making this the most prolific RTA period in recorded history".[5] A WTO discussion paper reported in May 2005 that the number of world RTAs in force totaled 170, with 20 additional RTAs due to enter

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[2] For the impact of Free Trade Agreements, see CRS Report RL31356, *Free Trade Agreements: Impact on U.S. Trade Policy*, by William H. Cooper.

[3] World Trade Organization, *The Changing Landscape of Regional Trade Agreements*, by Jo-Ann Crawford and Roberto V. Fiorentino, Discussion Paper No. 8, 2005.

[4] Ibid.

[5] Pruzin, Daniel, "Challenges Posed to Developing nations by Upswing in Regional Trade Agreements," *International Trade Reporter*, May 26, 2005.

force pending domestic ratification, and a further 70 under negotiation or consideration. RTA activities have intensified in all world regions "particularly in the Western Hemisphere and Asia-Pacific."[6]

Motivations for Forming Regional Trade Agreements

While economic motivations may be a major driving force, countries form RTAs for a number of reasons. Political and security factors also play a role in forming RTAs. Countries usually enter into trade agreements to improve their country's or region's bargaining position in global negotiations, attract foreign direct investment to increase economic growth, achieve economies of scale, and expand export markets. Countries also see RTAs as building blocks for further trade liberalization under the World Trade Organization (WTO) or for forming larger free trade areas such as the FTAA.

Expanding market access is probably the primary motivation for entering into trade agreements. RTAs give the signatories trading preferences in each other's markets while excluding other nations from the same privileges. These preferential trade arrangements reduce tariffs and other trade barriers among trading partners, providing partners with broader market access for their goods and services. Trade liberalization allows countries to achieve economies of scale as they are able to expand their export market. Smaller countries benefit from trade agreements because producers in these countries can lower their unit costs by producing larger volumes for regional markets in addition to their own smaller domestic markets.[7] When more units of a good or a service can be produced on a larger scale, companies will have a better chance to decrease cost of production.

Attracting foreign direct investment (FDI) is another reason for forming RTAs, especially for developing countries. The lowering of foreign investment restrictions through trade agreements improve investor confidence in a country, which helps attract FDI. Multinational firms invest in countries to gain access to markets, but they also do it to lower production costs. One of the motivating factors in Mexico's interest in forming NAFTA was to attract FDI. It was also a motivating factor for Central American countries and the Dominican Republic in the CAFTA-DR.

The slow progress in multilateral negotiations may also contribute to the increasing interest in regional trade blocs. Some countries may see smaller trade arrangements as "building blocks" for multilateral agreements. For example, the United States recently ratified CAFTA-DR and is moving forward on negotiations with Panama and the Andean countries as part of its overall trade strategy for free trade in the Americas.

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[6] Crawford, Jo-Ann and Roberto V. Fiorentino (Crawford and Fiorentino), "The Changing Landscape of Regional Trade Agreements," *World Trade Organization (WTO) Discussion Paper No. 8*, May 2005, p. 1.

[7] For more information on the costs and benefits of regional trade agreements, see Cohen, Stephen D., Robert A. Blecker, and Peter D. Whitney, *Fundamentals of U.S. Foreign Policy*, Westview Press, 2003, pp. 49-79.

Some countries form RTAs for political reasons. Governments may seek trade agreements as a way to promote peace or increase regional security. Countries may want to demonstrate good governance by locking in political and economic reforms through trading partnerships. Larger countries may use RTAs to forge new geopolitical alliances and strengthen diplomatic ties, which could ensure or reward political support. For example, the United States formed RTAs with Israel and Jordan as a way of reaffirming U.S. support of these countries and to strengthen relations with them. Some analysts believe that the choice of RTA partners is increasingly based on political and security concerns and not so much on economic rationale.[8]

The Americas and Regional Trade Agreements

The formation of RTAs throughout the world has intensified in the last few years with countries in the Americas forming a notable share of the world's total. Thirty-nine of the 170 agreements in force around the world involve countries in the Western Hemisphere. Europe has the greatest concentration of RTAs in the world, with the European Union and the European Free Trade Association as the "main continental hubs." The WTO reports that in the Western Hemisphere, RTA dynamics are more diverse than they are in Europe with "several major players engaged in multilayered RTA processes and not necessarily sharing similar objectives."[9]

Trade liberalization has been a central component of structural reform process in Latin America and the Caribbean since the mid-1980s when countries were implementing unilateral measures to liberalize trade. After NAFTA, countries began taking a more regional approach through the formation of regional trade agreements. Some of the major trade arrangements in the Americas are described in Table 1 below. By adopting a more regional approach, countries have been able to go beyond that which was attainable or desirable at the unilateral and multilateral levels. Most of the regional integration to date has involved trade in goods and has not advanced as far in other areas such as trade in services or intellectual property rights. In this regard, Mexico's liberalization has been the most comprehensive through its implementation of NAFTA.[10]

NAFTA has the largest market size of all regional trade blocs in the Americas, encompassing a market of 430 million people with a nominal GDP of $13.4 trillion (see Table 2). In South and Central America, the largest markets are formed by Mercosur, with a population of 227 million and a nominal GDP of $778 billion; and the Andean Community, with a population of 121 million and a nominal GDP of $314 billion.

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[8] Crawford and Fiorentino, p. 16.

[9] Crawford and Fiorentino, p. 10.

[10] *Beyond Borders: The New Regionalism in Latin America (Beyond Borders)*, Inter-American Development Bank, Economic and Social Progress in Latin America 2002 Report, p. 4.

Table 1. Major Trade Arrangements in the Americas

Agreement	Description/Status
North American Free Trade Agreement (NAFTA)	Member countries: Canada, Mexico, United States. The free trade agreement was signed in December 1992 and entered into force on January 1, 1994.
Central America-Dominican Republic Free Trade Agreement (CAFTA-DR)	Signatory countries: Costa Rica, Dominican Republic, El Salvador, Guatemala, Honduras, Nicaragua, United States. The free trade agreement was signed on August 5, 2004. As of September 2005, the agreement had been ratified by six countries. Costa Rica has not ratified. The agreement is expected to enter into force in January 2006.
Southern Common Market (Mercosur)	Member countries: Argentina, Brazil, Paraguay, Uruguay. Associate Member Countries: Venezuela, Colombia, Ecuador, Bolivia, Chile, and Peru. The treaty was signed in 1991. The goal of the treaty is to form a common market. The program has progressively removed trade barriers and established a common external tariff structure with selected national exceptions.
Andean Community (CAN)	Member countries: Bolivia, Colombia, Ecuador, Peru, Venezuela. The 1969 founding agreement was a step forward in creating a customs union with a longer term goal of creating a common market. Over the years, member countries have taken adopted a number of measures towards trade integration and have committed to the creation of a common market by the end of 2005.
Caribbean Community and Common Market (CARICOM)	Member countries: Antigua&Barbuda, Bahamas, Barbados, Belize, Dominica, Grenada, Guyana, Haiti, Jamaica, Montserrat, Trinidad & Tobago, St. Kitts & Nevis, St. Lucia, St. Vincent & the Grenadines, and Surinam. The original treaty was signed in 1973. In 1989, member countries agreed to create a CARICOM Single Market and Economy (CSME). Efforts are being made to establish the CSME by end of 2005.
Central American Common Market (CACM)	Member countries: Costa Rica, El Salvador, Guatemala, Honduras, and Nicaragua. Panama has observer status. Original treaty signed in 1960 and 1963 but although most intra-regional trade is duty-free, integration process continues. The goal was to establish a common market but integration was delayed to political and economic challenges in the region.
Latin American Integration Association (ALADI)	Member countries: Argentina, Bolivia, Brazil, Chile, Colombia, Cuba, Ecuador, Mexico, Paraguay, Peru, Uruguay, and Venezuela The ALADI framework is a preferential trade arrangement consisting of about 40 partial scope agreements involving two or more countries. Most were signed in the 1990s.

Sources: Compiled by CRS using information from IDB *Beyond Borders*; and WTO, *Discussion Paper No. 8*, “The Changing Landscape of Regional Trade Agreements,” 2005.

Table 2. Economic Indicators for Selected Regional Trade Blocs (2003)

Country	People (Million)	Nominal GDP ($Billion)	Exports		Imports	
			Amount ($Bill)	% World Total	Amount ($Bill)	% World Total
United States	293	10,971	725	9.46%	1,303	17.4%
Canada	32	870	286	3.73%	244	3.3%
Mexico	105	639	165	2.15%	171	2.3%
Total NAFTA	**430**	**12,480**	**1,176**	**15.4%**	**1,718**	**23.0%**
Central America & Dominican Republic	44	85	21	0.3%	32	0.4%
United States	293	10,971	725	9.5%	1,303	17.4%
Total CAFTA-DR	**337**	**11,056**	**746**	**9.7%**	**1,335**	**17.9%**
Argentina	39	153	30	0.4%	13	0.2%
Brazil	179	605	73	1.0%	51	0.7%
Paraguay	6	7	1	0.0%*	2	0.0%*
Uruguay	3	13	2	0.0%*	2	0.0%*
Total Mercosur	**227**	**778**	**107**	**1.4%**	**68**	**0.9%**
Bolivia	9	9	2	0.0%*	2	0.0%*
Colombia	45	97	14	0.2%	13	0.2%
Ecuador	13	30	6	0.1%	6	0.1%
Peru	28	69	9	0.1%	8	0.1%
Venezuela	26	109	27	0.4%	11	0.1%
Total Andean Community	**121**	**314**	**58**	**0.8%**	**40**	**0.5%**
CARICOM**	**15**	**54**	**12**	**0.2%**	**16**	**0.2%**
WORLD TOTAL	**5,920**	**55,821**	**7,661**	**—**	**7,477**	**—**

Source: Compiled by CRS using data from *International Financial Statistics,* International Monetary Fund (IMF), August 2005; the *Economist Intelligence Unit,* and the *CIA World Factbook.*
* Less than 0.1%.
** Data for CARICOM region are estimates from 2003, 2004, and July 2005.

World Trade Organization and RTAs

A basic principle of the General Agreement on Tariffs and Trade (GATT) that is administered by the WTO is the most-favored nation (MFN) principle. In general, the MFN principle requires that trade concessions granted to one WTO member are to be applied to the trade of all other signatories. RTAs, by definition, run counter to the MFN principle because products of RTA member countries are given preferential treatment over nonmember products.[11] However, the WTO allows member countries to form regional trade agreements under strict rules. The WTO position is that regional trade agreements can often support the WTO's multilateral trading system by allowing groups of countries to negotiate rules and commitments that go beyond what was possible at the time under the WTO. The WTO has a committee on regional trade agreements that examines regional groups and assesses whether they are consistent with WTO rules.[12]

WTO members are permitted to enter into RTAs under specific conditions.[13] Paragraphs 4 to 10 of GATT Article XXIV as clarified in the *Understanding on the Interpretation of Article XXIV of the GATT 1994*, provide for the formation and operation of customs unions and free-trade areas covering trade in goods. Article V of the General Agreement on Trade in Services (GATS), governs the conclusion of RTAs in the area of trade in services, for both developed and developing countries. Three of the key elements in these rules state that countries participating in an RTA must provide detailed notification of the agreement to the WTO; that the agreement applies to "substantially all" trade between partner countries; and that the agreement does not raise barriers to third-country trade.[14]

Another set of rules refers to the so-called "Enabling Clause", the 1979 Decision on Differential and More Favorable Treatment, Reciprocity and Fuller Participation of Developing Countries. These rules apply to preferential trade arrangements in trade in goods between developing country members and allows developing countries to form preferential trading arrangements without the conditions under Article XXIV.[15]

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[11] For more information on the WTO, regional trade agreements, and U.S. trade policy, see CRS Report RL31356, *Free Trade Agreements: Impact on U.S. Trade and Implications for U.S. Trade Policy,* by William H. Cooper.

[12] See World Trade Organization, "Understanding the WTO: Cross-Cutting and New Issues, Regionalism: Friends or Rivals?," [http://www.wto.org].

[13] For more information on the specific sets of rules for regional trade agreements among WTO members, see *Regional Trade Agreements: Rules* on the WTO website [http://www.wto.org]

[14] See Schott, Jeffrey J., *More Free Trade Areas?*, Institute for International Economics, Policy Analyses in International Economics 27, May 1989.

[15] For more detailed information on the Enabling Clause rules, see WTO, *Differential and More Favourable Treatment Reciprocity and Fuller Participation of Developing Countries* on the WTO website [http://www.wto.org].

For non-reciprocal preferential trade arrangements, such as the US-Caribbean Basin Economic Recovery Act, members must seek a waiver from WTO rules. These waivers require the approval of three-fourths of WTO members.

Economic Effects of Trade Integration

Supporters of trade integration in the Americas view hemispheric free trade as supporting U.S. economic and political interests in several ways. They argue that the movement towards trade integration is beneficial for U.S. economic prosperity and will serve to strengthen democratic regimes and support U.S. values and security interests. Forming closer economic relations with countries in the region is seen by some as a means to improve cooperation on other issues such as the environment and anti-drug efforts. U.S. opponents to regional integration in the Americas are concerned that hemispheric free trade would lead to a loss of jobs in the United States. They argue that trade agreements would result in U.S. companies shifting production to lower-wage countries with weak labor and environmental standards.

Economists are in general agreement that RTAs can provide economic benefits, but not that there are also associated costs. In general, they see RTAs as beneficial for an economy to the extent that they provide trade creation over trade diversion. When a trade agreement lowers trade barriers on a good, production may shift from domestic producers to lower cost foreign producers and result in substituting an imported good for the domestic good. This process is called trade creation. Trade creation provides economic benefits as consumers have a wider choice of goods and services available at lower costs. Trade creation also results in adjustment costs, however, usually in the form of domestic job losses as production shifts to another country.

The drawback to RTAs is that they may result in trade diversion because they are not fully inclusive of all regional trading partners. Trade diversion results when a country forms an RTA and then shifts the purchase of goods or services (imports) from a country that is not an RTA partner to a country that is an RTA partner. For example, if the United States was purchasing an item from Asia prior to NAFTA and then began to purchase this item from Mexico after NAFTA was enforced, solely as a result of the trade agreement, even though the Asian country was the lower-cost producer, then NAFTA would be associated with trade diversion. Mexico would now be the producer of that item, not because it produced the good more efficiently, but because it was receiving preferential access to the U.S. market.

The effects of trade creation versus trade diversion are complex and difficult to measure. Much depends on the market structure and costs in which an RTA intervenes and the long-term dynamic effects of the RTA. A report by the Inter-American Development Bank (IADB) states that most studies have found that "trade creation greatly dominates trade diversion" in most regional integration trade arrangements. The study indicates that in the case of NAFTA, all members stand to gain, particularly Mexico. In the case of Mercosur, the study indicates that Argentina, Brazil, and Uruguay have the potential of increasing their GDP.[16]

While an increase in RTAs throughout the Western Hemisphere may have benefits, they can also result in complex networks of preferential trade arrangements. There are an increasing number of overlapping trade agreements, each with its own tariff schedule and rules of origin regime. Some economists believe that these arrangements may pose challenges for developing countries and put them in a "weaker position than under the multilateral framework."[17] Developing countries may have difficulties in navigating the maze of rules that accompany RTAs, and they may not be able to fully benefit from the new trade rules. Another disadvantage for developing countries is that RTAs may result in a decreasing reliance on nonreciprocal trade preferences such as the duty-free treatment that Andean countries receive from the U.S. ATPDEA. According to the WTO study on RTAs, the replacement of preferential trade arrangements with RTAs could present developing countries with challenges as they transition from non-reciprocal trade preferences to mutual trade liberalization.[18] These disadvantages have the possibility of perpetuating poverty in the region.

U.S. Trade Policy in Latin America and the Caribbean

Since the passage of NAFTA, the United States, Canada, and Mexico have pursued trade liberalization through bilateral, regional, and multilateral negotiations. All have participated in the multilateral talks for an FTAA but have also formed other bilateral agreements to help achieve their overall trade integration objectives. Many of the negotiations that have produced trade agreements have been completed relatively quickly and have achieved broader trade liberalization than multilateral trade negotiations. One of the advantages in forming agreements on a bilateral or regional basis is that these agreements can achieve more liberalization in tariff and non-tariff barriers as opposed to the multilateral approach that usually achieves partial reductions on a limited number of goods.

NAFTA has served as a precedent for other U.S. trade agreements. The United States has advanced its trade policy agenda in the Western Hemisphere through bilateral trade initiatives with Chile, Central America and the Dominican Republic, Panama and selected Andean countries (see Table 3). The U.S.-Chile FTA was signed in June 2003 and entered into force in January 2004. CAFTA-DR was signed into U.S. law on August 2, 2005 and is expected to enter into force in January 2006. In May 2004, the United States began negotiations with Colombia, Peru, Ecuador, and Bolivia on the U.S.-Andean free trade agreement. Those negotiations continue and are expected to be concluded by the end of 2005. In April 2004, the United

[16] *Beyond Borders,* p. 41.

[17] Crawford and Fiorentino.

[18] Ibid.

States began negotiations with Panama on the U.S.-Panama free trade agreement and those negotiations have not been concluded.

Role of Trade Promotion Authority

Trade promotion authority (TPA) is an arrangement involving the executive and legislative branches that recognizes the distinct constitutional responsibilities of those branches regarding trade negotiations and trade policy. By virtue of the constitutional power to conduct foreign affairs, the President has authority to negotiate and enter into agreements with foreign countries, including those agreements dealing with trade and tariff policy. At the same time, the Constitution gives Congress the primary power over trade policy under Article I, and the Congress decides whether or not to approve statutory changes that are called for under trade agreements that the President has negotiated.[19]

The basic provisions of TPA were established in the Trade Act of 1974 (P.L. 93-618) for a limited period of time. Those provisions have been renewed periodically, most recently under the Trade Act of 2002. Under TPA, Congress provides that, if a trade agreement is reached by a given deadline, it will consider legislation to implement the trade agreement under expedited procedures that prohibit amendments, limit debate, and set deadlines on congressional action. Under the 2002 Act as amended, Congress approved TPA for trade agreements entered into before July 1, 2005, but also approved an automatic two-year extension of TPA to cover trade agreements entered into before July 1, 2007. With TPA, the President is assured that agreements such as the U.S.-Andean the U.S.-Panama FTAs would receive a timely, up-or-down vote in Congress as long as certain requirements, such as consultations with Congress, are met. Without TPA, bills would be considered under normal legislative procedures and would be amendable.

TPA expires in June 2007 and renewal of the trade act is uncertain. All trade agreements currently under negotiation by the United States must be concluded before this deadline in order to receive the expedited procedures under TPS.

North American Free Trade Agreement (NAFTA)

NAFTA, signed by President George H.W. Bush on December 17, 1992, has been in effect since January 1994. It is the largest preferential trade agreement in the world. The agreement eliminated tariffs and other trade and investment barriers among Canada, Mexico, and the United States with a phase-in period of 15 years. The phase-in period will end in 2008. The three countries form the largest market in the Western Hemisphere, encompassing 430 million people and with a gross domestic product (GDP) of $13.4 trillion. Total exports from the three countries total over one trillion dollars, or 15.4% of the world total. Imports totaled $1.7 trillion in 2003, or 23% of the world total.

[19] For more information on Trade Promotion Authority (TPA), see CRS Report RS22102, *Trade Promotion Authority: Possible Vote on Two-Year Extension*, by Lenore Sek.

Table 3. United States' Trade Agreements

Agreement	Status
Multilateral Agreements	
GATT	Contracting Party - January 1, 1948
WTO	Member - January 1, 1995
FTAA	Negotiations began in 1994 but are currently stalled
Free Trade Agreements in the Western Hemisphere	
NAFTA	Entry into force - 1994
United States - Chile	Entry into force - 2004
CAFTA-DR	Date of signature - August 5, 2004. Expected to enter into force in January 2006*
U.S.-Andean FTA	Negotiations began in May 2004 but have not been concluded
U.S.-Panama FTA	Negotiations began in April 2004 but have not been concluded
Other Agreements	
United States - Israel FTA	Entry into force - 1985
United States - Jordan FTA	Entry into force - 2001
United States - Singapore FTA	Entry into force - 2004
United States - Morocco FTA	Signed, not yet in force
United States - Australia FTA	Date of signature - May 18, 2004, not yet in force
United States - Bahrain FTA	Date of signature - September 14, 2004, not yet in force

Sources: Organization of American States (OAS), Foreign Trade Information System (SICE); Inter-American Development Bank, *Beyond Borders,* p. 26.

* CAFTA-DR has been ratified by Dominican Republic, El Salvador, Honduras, Guatemala, and United States. Costa Rica has not yet ratified the agreement.

The goals of the NAFTA are to eliminate trade barriers, facilitate cross-border movement of goods and services among the countries, promote fair competition in the free trade area, increase investment opportunities, and provide effective protection and enforcement of intellectual property rights. NAFTA is supplemented by two additional side agreements on environmental and labor standards. The trade liberalization program has been implemented according to schedule, or earlier. Over 90 percent of goods are currently duty-free.[20]

Total U.S. trade with NAFTA partners increased significantly over the past 11 years. Trade volume with NAFTA partners increased from $293 billion in 1993 to $710 billion in 2004. Canada and Mexico accounted for 31% of total U.S. trade of $2.29 trillion in 2004, up from $292.7 billion or 28% of U.S. total trade in 1993. The U.S. trade deficit with NAFTA partners has also grown, rising from $12 billion (9% of the total) in 1993 to $113 billion in 2004 (17% of the total). Over the past three years, the share of U.S. trade with NAFTA partners, with respect to the rest of the

[20] *Beyond Borders*, p. 29.

world, has fallen. In 2001, Canada and Mexico accounted for 33% of total U.S. trade. In 2004, this percentage fell to 31%. Canada and Mexico also account for a smaller share of the U.S. trade deficit since 2001, down from 27% of the total in 2001 to 17% of the total in 2004.[21]

Mexico and Canada have increased as a site for U.S. direct investment abroad (USDIA), though their share of total USDIA has fallen slightly since the 1990s.[22] Between 1993 and 2003, USDIA in Canada and Mexico increased from $84 billion (15% of total USDIA) to $254 billion (14% of total). In Canada, USDIA went from $70.4 billion (12.8% of total) to $192 billion (10.8% of total), while in Mexico it went from $15.4 billion (1.8% of total) to $62 billion (2.8% of total) during the same time period. Canada was the second largest recipient of USDIA in 2003 (behind the United Kingdom, which ranked first), while Mexico was the ninth largest recipient.[23]

U.S.-Chile FTA

On June 6, 2003, the United States and Chile signed the U.S.-Chile FTA in Miami, Florida. On September 3, 2003, President George W. Bush signed the bill into law (P.L. 108-77) and the agreement entered into force on January 1, 2004. The FTA with Chile is the first U.S. agreement with a South American country and, at the time it was passed, there were expectations that it would prove to be a step forward in completing the FTAA.[24]

The United States is Chile's largest single-country trading partner, accounting for 20% of Chilean exports and 15% of imports. In contrast, Chile ranks 29th among U.S. trading partners in total trade. When the agreement entered into force in January 2004, 87% of bilateral trade in consumer and industrial products became duty-free immediately, with the remaining tariffs to be reduced over time. Within four years of the agreement, about 75% of U.S. farm exports were to enter Chile duty-free. The agreement also increased market access for the United States in a broad range of services. For Chile, 95% of its export products gained immediate duty-free status and only 1.2% of its products fell into the longest 12-year phase-out period. In addition to the market access provisions, the agreement includes environment and labor provisions, more open government procurement rules, increased access for services trade, greater protection of U.S. investment and intellectual property, and creation of a new e-commerce chapter.

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[21] Based on trade data from the U.S. International Trade Commission.

[22] U.S. Direct Investment Abroad (ISDIA) is the book value of U.S. direct investors' equity in, and net outstanding loans to, their foreign affiliates.

[23] Based on data from the U.S. Bureau of Economic Analysis, *Survey of Current Business,* July 2004.

[24] For more information, see CRS Report RL31144, *The U.S.-Chile Free Trade Agreement: Economic and Trade Policy Issues,* by J.F. Hornbeck.

Central America - Dominican Republic Free Trade Agreement

On August 5, 2004, the United States, Costa Rica, El Salvador, Guatemala, Honduras, Nicaragua, and the Dominican Republic signed the CAFTA-DR. The agreement has been ratified by six countries and is expected to enter into force in January 2006. Costa Rica has not ratified.[25]

CAFTA-DR is a regional agreement with all parties subject to "the same set of obligations and commitments," but with each country defining its own market access schedule. The agreement replaces U.S. preferential trade treatment extended to these countries under the Caribbean Basin Economic Recovery Act (CBERA), the Caribbean Basin Trade Partnership Act (CBTPA), and the Generalized System of Preferences (GSP). It liberalizes trade in goods, services, government procurement, intellectual property, and investment, and addresses labor and environment issues. Most commercial and farm goods attain duty-free status immediately. Remaining trade will have tariffs phased out incrementally over five to twenty years. Duty-free treatment will be delayed longest for the most sensitive agricultural products. The CAFTA-DR specifies rules for transitional safeguards, tariff rate quotas, and trade capacity building.[26]

The Dominican Republic and Central America partners are smaller countries with a combined population of 44 million and a total GDP of $86 billion. Exports from and imports to the region account for less than one percent of the world total. All of the countries have had democratically elected presidents for some time, and several of the countries have experienced recent electoral transitions. For each of the countries the United States is the dominant market as well as the major source of investment and foreign assistance, including trade preferences under the Caribbean Basin Initiative (CBI) and assistance following devastating hurricanes.[27]

CAFTA-DR is not expected to have a large effect on the U.S. economy as a whole, but it could impose adjustment costs on some sectors. As with other trade agreements, supporters see it as part of a policy to support improved intra-regional trade, as well as political, and economic development in an area of strategic importance to the United States. Opponents to the agreement were seeking improved trade adjustment and capacity building policies for Central American countries and the Dominican Republic. They also argued that these countries had inadequate labor laws and that the labor provisions in the CAFTA-DR needed strengthening.

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[25] For more information, see CRS Report RL31870, *The Dominican Republic-Central America-United States Free Trade Agreement (CAFTA-DR),* by J.F. Hornbeck.

[26] Ibid.

[27] For more information on CAFTA-DR countries, See CRS Report RL32322, *Central America and the Dominican Republic in the Context of the Free Trade Agreement (CAFTA-DR) with the United States,* coordinated by K. Larry Storrs.

U.S.-Andean FTA

In November 2003, the Administration notified Congress that it intended to begin negotiations on an FTA with Colombia, Peru, Ecuador, and Bolivia. The notification said that an FTA would reduce and eliminate barriers to trade and investment and would support democracy and fight drug activity in the Andean region. The Andean governments want to ensure access to the U.S. market, especially since their current trade preferences will terminate at the end of 2006. The Andean governments also want to attract investment and see an FTA with the United States as a way to establish a more secure economic environment and increase foreign investment.[28]

The first round of trade negotiations was held with Colombia, Peru, and Ecuador (with Bolivia participating as an observer) in Cartagena, Colombia, in May 2004. Thirteen rounds have been held thus far and trade negotiators have stated that they expect to conclude the agreement by the end of 2005. Within the Andean countries there is broad grass-roots opposition to an FTA. The talks have drawn thousands of protestors in Colombia, Ecuador, and Peru. Opponents argue that any economic benefits from increased trade under an FTA will be realized by only a small segment of the economy, worsening the separation of the classes. They also argue that a large part of the Andean population is poor farmers, who are especially vulnerable and cannot compete against increased agricultural imports from the United States, which some Andean officials assert are heavily subsidized.

Presently, Andean countries have preferential trade access under unilateral U.S. programs, but that access is scheduled to expire at the end of December 2006. The program began under the Andean Trade Preference Act (ATPA; title II of P.L. 102-182), enacted on December 4, 1991. ATPA authorized the President to grant duty-free treatment to certain products from the four Andean countries that met domestic content and other requirements. It was intended to promote economic growth in the Andean region and to encourage a shift away from dependence on illegal drugs by supporting legitimate economic activities. ATPA was originally authorized for 10 years and lapsed on December 4, 2001.

After ATPA had lapsed for months, the ATPDEA (Title XXXI of P.L. 107-210), was enacted on August 6, 2002. ATPDEA reauthorized the ATPA preference program and expanded trade preferences to include additional products that were excluded under ATPA. ATPDEA also authorized the President to grant duty-free treatment to U.S. imports of certain apparel articles, if the articles met domestic content rules. The ATPDEA accounted for about half of all U.S. imports from the four countries in 2003. Duty-free benefits under ATPDEA end on December 31, 2006. While there is always some possibility that the trade preferences with Andean countries might not be renewed, an FTA with the United States would lock-in those preferences and additional duty-free treatment.

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[28] See CRS Report RL32770, *Andean-U.S. Free-Trade Negotiations*, by M. Angeles Villarreal.

U.S.-Panama FTA

On November 16, 2003, President George W. Bush formally notified Congress of his intention to negotiate an FTA with Panama. Negotiations began in April 2004, with eight rounds of negotiations held thus far. The last round was held in February 2005. Panama approached the United States for a stand-alone FTA, avoiding a link to CAFTA-DR because of the historical and strategic nature of the U.S.-Panamanian relationship. Panama's limited integration with the Central American economies also bolstered the case for separate negotiations.[29]

The United States is Panama's most important trading partner, accounting for approximately 50% of Panama's exports and 34% of its imports. U.S.-Panama merchandise trade is small. In 2004, U.S. exports to Panama totaled $1.8 billion and U.S. imports totaled $316 million, producing a U.S. trade surplus of $1.5 billion. Panama ranked 48th as an export market for U.S. goods and 99th for U.S. imports.

Supporters of the U.S.-Panama FTA believe that it would support foreign policy and economic interests of the United States and that is expected to lend stability to Panama's increasingly open economy. Those in the United States who oppose the FTA have raised concerns about labor and environmental standards in Panama. In Panama, protesters have held demonstrations against the agreement over various policy issues.[30]

U.S. and Panamanian negotiators have used the CAFTA-DR framework to advance an agreement. The negotiation process moved fairly fast in the early stages, but no significant progress has been made since February 2005. There is a possibility that talks will resume in the fall of 2005. President Bush visited Panama on November 7, 2005 and met with Panamanian President Martin Torrijos. The two leaders held a joint news conference in which they cited progress in reaching a free trade agreement but acknowledge the political challenges related to the trade talks.[31]

Free Trade Area of the Americas (FTAA)

The 1994 vision of hemispheric free trade has been embraced by President George W. Bush and promoted by the formal negotiations in the FTAA process but also by the expansion of bilateral free trade agreements. An FTAA could have 34 members and nearly 800 million people. This population would be nearly twice the population of the European Union. The FTAA trade talks were launched in April 1998 and, after seven years, the original deadline for concluding the agreement has passed and negotiators have failed to conclude an agreement, mostly over differences due to agriculture.

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[29] See CRS Report RL32540, *The Proposed U.S.-Panama Free Trade Agreement,* by J.F. Hornbeck.

[30] Ibid.

[31] Bumiller, Elisabeth, "Bush, Meeting Panama's Leader, Endorses Widening of the Canal," *The New York Times,* November 8, 2005.

Under the Declaration of Miami from the first Summit of the Americas, the 34 countries committed to make concrete progress toward an FTAA before 2000 and complete negotiations no later than 2005. The Declaration called for building on existing subregional and bilateral agreements to broaden and deepen integration. The Ministers elected to establish nine initial negotiating groups, which covered all the tariff and non-tariff barrier issue areas identified by the leaders at the Miami Summit. The overall process is directed by the Trade Negotiation Committee (TNC), co-chaired by the United States and Brazil for the remainder of the negotiations.[32]

Under the General Principles and Objectives for the negotiations, trade ministers agreed to provide transparency during the negotiations and also agreed that the FTAA should improve upon WTO rules and disciplines wherever possible and appropriate. The ministers agreed that the negotiations would be a single undertaking in that the signatories to the final FTAA Agreement would have to accept all parts of it (i.e. cannot pick and choose among the obligations.)[33] They also agreed that only democracies would be able to participate in an FTAA and to make public the preliminary negotiated texts.

At the November 2003 FTAA ministerial meeting in Miami, participating countries made a compromise on the scope and ambition of an FTAA. As worked out by the United States and Brazil, the compromise would create a two-tier FTAA structure by January 1, 2005. The first tier would be comprised of a common set of rights and obligations on the nine negotiating groups for all 34 FTAA countries. The second tier would consist of a series of plurilateral agreements in which countries would voluntarily undertake to achieve deeper disciplines and further liberalization in the nine groups. Although no negotiating area would be left out of the agreement, because countries could take on varying obligations within the FTAA structure, it was a very different notion from the broad "single undertaking" principle that had initially been envisioned.

The 2003 Miami declaration also instructed the deputy trade ministers to define the common set of obligations. However, the United States and Brazil were unable to agree on what areas would be obligatory for all participants and the FTAA negotiations were suspended. Brazil's position called for all industrial and agricultural goods to be in the market access provisions and pressed for elimination of export subsidies and action on domestic price supports for agricultural goods. The United States agreed to the elimination of export subsidies, but not domestic support for agriculture. The United States wants these provisions to be discussed in the WTO negotiations.

According to a recent report analyzing the possible future of the FTAA talks, the negotiations have produced a "heavily bracketed draft text and little else."[34] One

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[32] See CRS Report RS20864, *Free Trade Area of the Americas: Major Policy Issues and Status of Negotiations,* by J.F. Hornbeck.

[33] See FTAA website, [http://www.ftaa-alca.org].

[34] Schott, Jeffrey J., Senior Fellow, Institute for International Economics, *Does the FTAA*
(continued...)

positive development cited by the report is the trade capacity building initiatives advanced by the Inter-American Development Bank and national development agencies that have addressed critical infrastructure and administrative problems in smaller economies.[35]

The most recent Summit of the Americas, held in November 2005 in Mar del Plata, Argentina, failed to reach a consensus on the FTAA. One group, comprising the majority of the 34 participating countries, were in support of reviving the FTAA talks, while the other group, comprised of five countries including Brazil, Argentina, and Venezuela, refused to sign up for the talks. The disagreements mostly concern agriculture and intellectual property standards. The President of Brazil's top foreign policy aide, Marco Aurelio Garcia, commented after the meeting that it is necessary for "rich countries to reduce agricultural subsidies and barriers to trade" before talking about any launch dates for the talks.[36] There is also disagreement on the U.S. commitment to implementing continent-wide intellectual property standards, which would reduce the prevalence of unauthorized medicines. Brazil's government believes that this provision would reduce the availability of lower-priced medicines for low-income populations in Brazil.[37]

Regional Integration Initiatives in the Americas

Countries in the Western Hemisphere have been forming regional trade agreements since 1961 when the Central American Common Market was formed. Latin American countries view regional trade agreements as a tool to help promote economic and social development but also as a way of gaining leverage in the negotiations of larger scale agreements such as the FTAA. In general, Latin American countries have economic interests, but also recognize that trade agreements alone are not sufficient to combat poverty and the larger social problems caused by poverty.

Mexico

Since the early 1990s, Mexico has had a growing commitment to trade liberalization and its trade policy is among the most open in the world. Mexico has been actively pursing free trade agreements with other countries as a way to bring benefits to the economy, but mostly to reduce its economic dependence on the United States. The United States is, by far, Mexico's most significant trading partner. Approximately 90% of Mexico's exports go to the United States and about 60% of Mexico's imports come from the United States. Mexico's second largest trading

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[34] (...continued)
have a Future?, November 2005, p. 4.

[35] Ibid, pp. 4-5.

[36] *EFE News Service,* "Brazil criticizes Mexico's Stance on Regional Trade Pact," November 8, 2005.

[37] *Washington Business Information, Inc.,* "Intellectual Property Remains a Problem for Proposed FTAA," November 8, 2005.

partner is Canada, which accounts for approximately 2% of Mexico's exports and imports.[38] In an effort to increase trade with other countries, Mexico has negotiated a total of 12 trade agreements involving over 40 countries (see Table 4). These include bilateral or multilateral trade agreements with most countries in the Western Hemisphere including the United States and Canada, Chile, Bolivia, Costa Rica, Nicaragua, Uruguay, Colombia, Venezuela, Guatemala, El Salvador, and Honduras. Mexico has also been an active participant in the FTAA negotiations.

Mexico has also negotiated free trade agreements outside of the Western Hemisphere and, in July 2000, entered into agreements with Israel and the European Union. Mexico became the first Latin American country to have preferred access to these two markets. Mexico has completed a trade agreement with the European Free Trade Association (EFTA) of Iceland, Liechtenstein, Norway, and Switzerland. The Mexican government expanded its outreach to Asia in 2000 by entering into negotiations with Singapore, Korea, and Japan. In 2004, Japan and Mexico signed an Economic Partnership Agreement. It was the first comprehensive trade agreement that Japan signed with any country.[39] The large number of trade agreements has not yet been successful in decreasing Mexico's dependence on trade with the United States.

Canada

Canada has been active in the FTAA negotiating process, but has not pursued bilateral trade agreements to the degree of Mexico or the United States. Canada's dominating trading partner is the United States and most of its trade policy focus is centered on its trade relationship with the United States. Canada has achieved considerable economic integration with the United States in a number of sectors and considered options to further its relationship. However, after the terrorist attack of September 11, there has been a wide-ranging debate in Canada over its relationship with the United States and the question of whether deeper North American integration would be beneficial to the Canadian economy.[40] Canada has entered into three bilateral trade agreements since NAFTA. These include agreements with Israel (1997), Chile (1997), and Costa Rica (2001). It is also considering trade agreements with Singapore and the EFTA.

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[38] Based on statistics from the International Monetary Fund, *Direction of Trade Statistics*, 2005.

[39] *The Asahi Shimbun*, "Japan: Free Trade with Mexico," March 12, 2004.

[40] See CRS Report RL33087, *United States-Canada Trade and Economic Relationship: Prospects and Challenges*, by Ian F. Fergusson.

Table 4. Mexico's Trade Integration Agreements

Agreement	Status
Multilateral Agreements	
GATT	Contracting Party - August 24, 1986
WTO	Member - January 1, 1995
FTAA	Negotiations began in 1994 but are currently stalled
Regional Scope Agreements	
ALADI	Member - August 12, 1980
Free Trade Agreements in the Western Hemisphere	
NAFTA	Entry into force - 1994
Mexico-Bolivia	Entry into force - 1995
Group of Three (Mexico-Colombia-Venezuela)	Entry into force - 1995
Mexico-Costa Rica	Entry into force - 1995
Mexico-Nicaragua	Entry into force - 1998
Mexico-Chile	Entry into force - 1999
Mexico-Northern Triangle of Central America	Entry into force - 2001
Mexico-Uruguay	Entry into force - 2003
Mexico-Argentina	Under consideration
Mexico-Peru	Under consideration
Mexico-Ecuador	Under consideration
Mexico-Trinidad and Tobago	Under consideration
Partial Scope Agreements	
Mexico-Colombia-Venezuela	Date of signature: 2004
Mexico-Mercosur (2)	Date of signatures: 2002
Mexico-Brazil	Date of signature: 2002
Mexico-Panama	Entry into force: 1986
Mexico-Uruguay	Entry into force: 2001
Other Agreements	
Mexico-EU	Entry into force - 2000
Mexico-EFTA	Entry into force - 2001
Mexico-Israel	Entry into force - 2000
Mexico-Japan	Entry into force - 2005
Mexico-Singapore	Under consideration

Sources: Organization of American States (OAS), Foreign Trade Information System (SICE); Inter-American Development Bank, *Beyond Borders*, p. 26.

Southern Common Market (Mercosur)

Mercosur was created in March 1991 by Argentina, Brazil, Paraguay, and Uruguay through the signing of the Treaty of Asunción. The goals of the treaty included the formation of a common market with free movement of goods, services, and factors of production; the adoption of a common external tariff and a common trade policy; the coordination of macroeconomic and sectoral policies; and legislative harmonization in areas conducive to stronger integration.

Mercosur is the largest preferential trade group in South America, with a combined gross domestic product of $778 billion (representing 40% of Latin America's GDP) and a population of 227 million in 2004.[41] U.S. exports to Mercosur totaled $18.2 billion in 2004, while U.S. imports totaled $25.5 billion. The United States had a trade deficit of $7.3 billion with Mercosur in 2004, an increase of $2.7 billion over the $4.6 billion deficit in 2002. Prior to 2002, the United States had a trade surplus with these countries. The surplus went from a high of $11.1 billion in 1997 to $2.9 billion in 2001. The U.S. direct investment position in Mercosur totaled approximately $45 billion in 2004, down from $55.4 billion in 2000. Brazil accounts for over 70% of USDIA in Mercosur countries.

Mercosur countries have progressively lifted trade barriers and established a free trade area since 1991, but continue to have barriers in some sectors. In 1994, the Treaty of Asuncion was amended and updated by the Treaty of Ouro Preto. The 1994 treaty helped improve the institutional structure of Mercosur and initiated a new phase in the trade relationship of member countries as they furthered their goal of realizing a common market. Bolivia, Chile, Colombia, Ecuador, Peru, and Venezuela have associate member status in Mercosur. Associate members do not take part in Mercosur's major trade negotiations and may choose not to abide by its trade rules.

Mercosur countries began the transition to a common market in 1994 with the goal of completing internal free trade by 2000 and a common market by 2006. The free trade goal was delayed due to economic difficulties in the member countries. The 2002 crisis in which Argentina faced its most serious economic downturn in its independent history has been one of the more serious setbacks. Mercosur has a common external tariff (CET) organized in 11 tiers with tariff rates ranging from 0 to 20 percent with an average level of 13.5 percent that entered into force in 1995. The CET has some exceptions with special customs regimes applying to the sugar and automotive sectors. Member countries have approved common regional provisions covering trade in services, safeguards, anti-dumping and dispute settlement, but these have been only partially implemented. The executive body of Mercosur, the Common Market Council (CM), has agreed on a working program focused on the lifting of the remaining market access barriers.[42]

Throughout much of the 1990s, Mercosur was the most dynamic economic subgroup in the Western Hemisphere in terms of trade growth among its members. Things changed at the end of the decade when Brazil was faced with a financial crisis and the devaluation of the Brazilian *real* in 1999. The economic situation affected Argentina as well, causing a severe and political financial crisis that ended the presidency of Fernando de la Rua. The downturn in the economies of both countries caused the momentum towards deeper integration to decrease. Some have

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[41] Figures are based on data from the Economist Intelligence Unit.

[42] Inter-American Development Bank (IDB), *Economic and Social Progress in Latin America,* "Beyond Borders: The New Regionalism in Latin America," 2002 Report, p. 29.

questioned whether trade liberalization was partly at fault for the economic crises and whether further liberalization is feasible or beneficial for the economy.[43]

In recent years, Mercosur countries have been working on several trade initiatives. Mercosur and the Andean Community of Nations (CAN) signed a statement of intent in December 2004 to form an economic union similar to the European Union by 2019 (see section on South American Community of Nations of this report). Mercosur has also pursued trade liberalization with the EU. The 1995 EU-Mercosur Interregional Framework Cooperation Agreement began the preparation of negotiations for an interregional agreement which would a include a liberalization of trade in goods and services, in conformity with WTO rules, as well as enhanced cooperation and a strengthening of political dialogue. In June 1999, negotiations on the agreement formally began. The latest round of negotiations to strengthen political, economic, and trade ties between Mercosur and the EU took place in October 2004 and the next round is scheduled to take place before the end of 2005.[44]

Mercosur countries held preliminary talks with Mexico on May 20, 2005 toward making Mexico an associate member of the trade bloc. Associate members receive preferential duty treatment for their products but are not required to adopt Mercosur's common external tariffs.[45]

Andean Community of Nations (CAN)

The CAN is one of the oldest sub-regional groupings in the hemisphere. It was originally formed in 1969 as the Andean Pact (later called the Andean Group and later the Andean Community of Nations). The Andean Community presently consists of Bolivia, Colombia, Ecuador, Peru, and Venezuela. The Cartagena Agreement creating the Andean Pact was signed by Bolivia, Chile, Colombia, Ecuador, and Peru in May 1969. Venezuela acceded in February 1973 and Chile withdrew in October 1976.

In 2004, Andean Community countries had a combined GDP of $314 billion and a population of 121 million. Exports from these countries totaled $76 billion or 0.8% of the world total, while imports totaled $52 billion or 0.6% of the world total. The country with the highest amount of exports is Venezuela, with $36 billion in exports, and the country with the highest amount of imports is Colombia with $17 billion in imports. About ten percent of Andean Community trade is intra-bloc trade. The United States is the principal trading partner, accounting for approximately 50 percent of CAN exports, while the EU is second. U.S. imports from the region

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[43] Estevadeordal, Antoni, Dani Rodrik, Alan M. Taylor, and Andres Velasco, *Integrating the Americas: FTAA and Beyond,* "The Political Economy of Economic Integration in the Americas," 2004, pp. 430-431.

[44] For more information see Mercosur in the external relations section of the European Commission's website [http://europa.eu.int/comm/external_relations/Mercosur/intro].

[45] "Mexico, Mercosur Hold Initial Talks on Negotiating Free Trade Deal," *International Trade Reporter,* Volume 22, Number 22, June 2, 2005.

totaled $40 billion, while U.S. exports totaled $13 billion. The United States had a trade deficit of $27 billion with the Andean Community in 2004.[46]

The Cartagena Agreement was the initial step toward economic integration among the parties with a broader vision towards forming a common market over time. The process lost momentum in the 1970s but then revived in the 1990s. The group established a four-country free trade area in 1993 (Bolivia, Colombia, Ecuador, and Venezuela) and agreed on the implementation of a common external tariff. In 1996, the presidents of the Andean countries pledged to transform the group into a common market and created the Andean Community (it had been called the Andean Group prior to that) based on a new institutional structure. The parties agreed on a timetable to reincorporate Peru into the free trade area (Peru had been suspended since 1992), committed to creating a common market by the end of 2005 in which goods, services, capital, and labor would move freely. The leaders also started the negotiation of a four-tier common external tariff expected to be in place by the end of 2003.[47] Political and economic setbacks have prevented the formation of a more integrated Andean union.

The trade in goods between Bolivia, Colombia, Ecuador, and Venezuela is fully deregulated, which means that goods originating in any one of those countries can enter the territory of the others duty-free. As a result, these four countries have a free trade area that Peru is becoming a part of through a liberalization program. The efforts of the Andean countries continue to focus on integration and implementing measures for preventing and correcting practices that distort free competition[48]

The Andean Community is considered one of the most institutionalized regional agreements among developing countries. Its institutional structure is patterned along the lines of the European Community. The institutions include a formal Andean Presidential Council that meets regularly, a Court of Justice with supranational powers, and an Andean Integration System that incorporates all the Andean integration agencies.[49]

The Andean Community is pursuing trade integration agreements with Mercosur, as previously mentioned, and also with the EU. Free trade talks between the CAN and the EU were scheduled to start in 2006, but that is no longer a certainty. During a meeting in Peru in June 2005, members of the European Parliament said a lack of agreement on trade issues among CAN members may derail the start of talks. One of the major problems they mentioned has to do with the lack of agreement on

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[46] Andean trade data are based on data from the Economist Intelligence Unit (EIU). U.S.-Andean trade data are based on data from the United States International Trade Commission (USITC) trade database.

[47] *Beyond Borders,* p. 28.

[48] See Andean Community website [http://www.comunidadandina.org].

[49] CRS Report 96-541, *Western Hemisphere Trade Developments,* by Raymond Ahearn.

how to implement a common tariff structure. The CAN's target date for implementing a common external tariff has not been met.[50]

Central American Common Market (CACM)

The Central American Common Market (CACM) was established in December 1960 by Costa Rica, El Salvador, Guatemala, Honduras, and Nicaragua upon the signing of the General Treaty on Central American Economic Integration. Costa Rica acceded to the integration agreement in July 1962. The 1960 treaty envisioned the creation of a common market which would come into effect after the treaty came into force. Although integration looked very promising in the first decade, political and economic challenges in the region prevented the region from establishing the common market that was earlier envisioned. The process was renewed in 1993 with the Guatemala Protocol which provided a new foundation for Central America's economic integration. Member countries hoped to implement a customs union by the end of 2003 but that process has been delayed as well. With the signing of CAFTA-DR, it is uncertain whether or when the Central American region will establish a customs union. Currently, most intra-regional trade is tariff-free, but some exceptions remain including coffee and sugar. Member countries have agreed to a four-tier common external tariff schedule. About 80% of the common external tariff schedule has been implemented.[51]

Caribbean Community (CARICOM)

Members of the Caribbean Community include Antigua and Barbuda, the Bahamas, Barbados, Belize, Dominica, Grenada, Guyana, Haiti, Jamaica, Montserrat, St. Kitts and Nevis, St. Lucia, St. Vincent and the Grenadines, Suriname, and Trinidad and Tobago. The Dominican Republic has observer status.

In 1989, CARICOM members agreed to create a CARICOM Single Market and Economy (CSME) that would entail removing obstacles to trade in goods and services; allowing the free movement of skilled persons; ending the restrictions on capital movements; adopting a common external tariff (CET) and common trade policy; and having greater coordination in other areas of economic policy. The founding treaty has nine modifying protocols to facilitate completion of the single market. These include the Institutional Framework (Protocol I); Establishment, Provision of Services and Movement of Capital (Protocol II); Industrial Policy (Protocol III), Trade Policy (Protocol IV), Agricultural Policy (Protocol V), Transport Policy (Protocol VI), Disadvantaged Countries, Regions and Sectors (Protocol VII), Competition Policy (Protocol VIII), and Dispute Settlement (Protocol IX). Some of the protocols have entered into force while others are being applied provisionally by

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[50] "Prospects for Holding Free Trade Talks in 2006 between EU, Andean Nations Darken," *International Trade Reporter*, Volume 22 Number 25, June 23, 2005.

[51] *Beyond Borders*, p. 28.

some member countries. Protocols that have entered into force include I, II, IV, and VII.[52]

CARICOM has moved ahead with its regional integration since the founding treaty. Intra-regional trade is virtually free. All tariffs and most trade restrictions have been removed, although some exceptions do remain. Efforts have been made to harmonize national customs laws, but corresponding legislation has not been fully implemented. The trade group has instituted a regime governing common standards for trade in goods, and is establishing a Caribbean Regional Organization for Standards and Quality (CROSQ). The CET is fully implemented in most countries although member states have the right to negotiate bilateral trade agreements with third countries. Progress has been made in the free movement of capital, but some restrictions remain. In regard to the free movement of people, this is limited to certain professional categories. Member countries are also making progress in harmonizing regulatory frameworks, but much depends on their ability to devote the necessary technical and financial resources. The countries indicate that they need financing to establish a fund to assist the less developed countries and to establish the envisaged legal bodies.[53]

In 2004, CARICOM made advancements in its integration process, including implementation of the CSME, foreign policy coordination, and functional cooperation. CARICOM made progress on removing restrictions on services provisions and the movement of capital and skilled labor. In the area of functional cooperation, member countries have cooperated in the fight against HIV/AIDS and natural disaster management plans.[54] In mid-April 2005, CARICOM members established the Caribbean Court of Justice, headquartered in Port-of-Spain in Trinidad and Tobago, that will serve as region's final court of appeal and replace the Privy Council based in London. The Court will play an important role in the region's economic integration by ruling on trade disputes in the forthcoming CARICOM CSME. Barbados, Jamaica, and Trinidad are leading the way in moving ahead with the implementation of the CSME, and other Caribbean states are expected to become compliant by the end of 2005.[55]

CARICOM countries have been taking steps to form trade agreements with other countries and regional trade blocs. In March 2004, CARICOM (with the exception of the Bahamas and Haiti) signed a free trade agreement with Costa Rica. It is also in the process of negotiating an agreement to improve trade with Canada by focusing on four areas: market access, investment, services, and institutional arrangements and dispute settlement.[56] CARICOM countries are also negotiating

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[52] Ibid.

[53] Ibid.

[54] Inter-American Development Bank, *Annual Report 2004*, "Latin America and the Caribbean in 2004: Trade and Integration," July 7, 2005. See [http://www.iadb.org].

[55] See CRS Report RL32160, *Caribbean Region: Issues in U.S. Relations*, by Mark P. Sullivan.

[56] *Caribbean Media Corporation (CMC), BBC Monitoring Americas*, "Caribbean-Canada

(continued...)

agreements with the EU and Mercosur. CARICOM countries and the Dominican Republic are in the third stage of negotiations toward an economic partnership agreement that will contain a reciprocal free trade agreement with the EU. Officials from the Caribbean and Mercosur countries held talks in February 2005 about establishing a free trade agreement between the two regions.

South American Community of Nations (CSN)

After the Third South America Summit on December 8, 2004, the two major trade blocs in South America, Mercosur and the CAN, signed the *Cuzco Declaration,* a statement of intent to form the South American Community of Nations (CSN). The CSN is planned as a continent-wide free trade zone uniting the two trade blocs and has a plan to eliminate tariffs for non-sensitive products by 2014 and sensitive products by 2019. The declaration was signed by representatives from twelve South American nations. Panama attended the signing ceremony as an observer. One of the goals was to have a constitution drafted in 2005, but it is uncertain if that goal will be met because the first meeting of heads of state held in September 30, 2005 in Brasilia ended without a plan of action.

The group of twelve South American nations would eventually become the world's fifth largest trade block according to Didier Opertti, the Secretary-General of the Latin American Integration Association (ALADI). Tariffs are to be phased out in stages and through bilateral meetings between countries, without the need for parliamentary ratification in most cases.[57] Political leaders in South America view this agreement as a significant step towards economic integration in South America and the possible creation of a South American union. The accord includes all the countries in South America with the exception of the smaller economies of Suriname, Guyana and French Guiana. The two trade blocs have a combined GDP of $800 billion. Total trade among the countries totals around $30 billion a year.

Some South American leaders have mentioned the possibility of political union as well, saying that it would be "the most important political development of the decade." Brazilian Foreign Minister Celso Amorim underlined the importance of creating institutions that are needed to bring about South American economic integration and of doing the same in the future for social and political integration of the "South American Community".[58] Leaders expect that the integration of South America would put South American countries in a stronger position in negotiations with the rest of the world, including a possible free trade agreement with the EU and the Free Trade Area of the Americas (FTAA). Interest in strengthening integration with Latin America has been supported by foreign ministers of the 12 ALADI countries (Argentina, Bolivia, Brazil, Chile, Colombia, Cuba, Ecuador, Mexico, Paraguay, Peru, Uruguay, and Venezuela.)

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[56] (...continued)
Trade Talks Described as Successful," March 3, 2005.

[57] Raul Pierri, "Mercosur and Andean Community Sign Free Trade Pact," Bilaterals Org, October 19, 2004.

[58] Ibid.

The first summit of the South American Community of Nations was held in Brasilia on September 30, 2005. The summit was attended by the majority of heads of state of South American countries. Despite efforts by Venezuelan President Hugo Chavez to replace the proposed structure of the CSN by his own proposal, the representatives at the summit decided to press ahead with what already been developed by their foreign ministers in preparatory meetings. They endorsed the idea of a merger of Mercosur and CAN to make the whole of South America a free-trade area. One of the results of the summit was a request to the secretariats of all existing mechanisms of integration to prepare studies on the convergence of trade agreements between South American countries by mid-2006 at the latest.[59]

Policy Issues and Implications

Continuation of Bilaterals and Regional Trade Agreements

In the absence of an FTAA, it is highly possible that the number of bilateral RTAs in the Western Hemisphere may continue to increase. Some analysts note that as the number of RTAs increase, there is a possibility of consolidating existing agreements into larger trading arrangements in regions of the world, as in the case of the EU which went through five consecutive enlargements, bringing the membership of the Union from six to 25 members.[60] Another example of consolidation or expansion is the bilateral agreement between the United States and Canada in the 1980s, which helped to bring focus on the Uruguay Round of multilateral negotiations and the formation of NAFTA. However, some believe that this strategy is not the best course of action for the United States. One of the reasons given is that the focus on bilaterals is distracting the United States from its leadership role in energizing the FTAA negotiations. Another reason given is that the bilateral agreements are doing little to resolve problems such as the trade issues related to agriculture, or strengthening the trade relationship between the United States and Brazil.[61]

Completion of an FTAA

All the countries of the Western Hemisphere, with the exception of Cuba, have been active participants in the establishment of an FTAA. In August 2005, senior representatives from all FTAA countries met in Mexico. Caribbean trade officials urged countries to hold an administrative meeting prior to the November 2005 Summit of the Americas to restart the stalled FTAA negotiations. They suggested that negotiators look at the technical and political obstacles that are holding back the talks and restart the negotiations with a new "road map" that would guide negotiators

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[59] *Latin American Weekly Report,* "Chavez Comes Close to Derailing South American Community's First Summit*"*, October 5, 2005.

[60] Crawford and Fiorentino, p. 15.

[61] Masi, Fernando and Carol Wise, "Negotiating the FTAA Between the Main Players," *Mercosur and the Creation of the Free Trade Area of the Americas,"* Woodrow Wilson International Center for Scholars, 2005.

toward a conclusion of the negotiations.[62] However, the recent Summit of the Americas, held in Mar del Plata, Argentina, was not successful in reactivating the trade talks. The majority of the 34 participating countries were in support of the talks, while five countries, including Brazil, Argentina, and Venezuela, were opposed to signing up for the talks, mostly due to disagreements over agriculture and intellectual property rights.

Some observers are pessimistic about the near-term possibility of restarting the talks, but there are many analysts who believe that pursuing multilateral talks would be advantageous for the region. Some have expressed hope that progress on agriculture at the WTO and that the November 2005 Summit of the Americas could help move the negotiations forward. According to a study by the Government Accountability Office (GAO), there are three factors that have been impeding progress in the FTAA negotiations: 1) The United States and Brazil have made little progress in resolving basic differences on key negotiation issues; (2) member governments have shifted energy and engagement from the FTAA to bilateral and other multilateral trade agreements; and 3) two mechanisms intended to facilitate progress, a new negotiating structure and the co-chairmanship by the U.S. and Brazil, have failed to do so.[63] The GAO study found that officials from many nations and regional groups in the Western Hemisphere have indicated a continued commitment to establishing a mutually beneficial FTAA.[64]

If the FTAA talks move forward and an agreement is signed, it would provide considerable new trade and investment opportunities for the 34 participating countries. For the United States, an FTAA would support the U.S. interest in gaining deeper access to markets in South America. The United States might also benefit in that an FTAA could reinforce economic and political reforms that have occurred in Latin America and could help build support for other important U.S. goals such as drug interdiction, improving environmental and labor conditions, supporting educational reforms, and reinforcing democracy.[65] In terms of trade, the U.S. position has been that the FTAA would be significant if it achieves trade liberalization beyond that which has been accomplished under the WTO, especially in the areas of liberalization of trade in services and investment; liberalization in government procurement; enforcement of intellectual property rights; and the inclusion of labor and environmental issues.[66]

For countries in Latin America and the Caribbean, the FTAA may help national income levels in the region, but not all economic sectors would benefit. Some

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[62] Bussey, Jane, "Negotiators Call for Free Trade Area of the Americas Talks," *Miami Herald,* August 24, 2005.

[63] United States Government Accountability Office, *Free Trade Area of the Americas: Missed Deadline Prompts Efforts to Restart Stalled Hemispheric Trade Negotiations,* GAO Report Number GAO-05-166, March 2005.

[64] Ibid.

[65] Schott, Jeffrey, *Prospects for Free Trade in the Americas,* Institute for international Economics, August 2001, p. 109.

[66] Masi and Wise, pp. 309-310.

economists believe that trade liberalization is needed to improve economic development in the region. An International Monetary Fund (IMF) report found that trade openness in Latin America remained low and cited "abundant empirical evidence" that the more open a country is to trade, the higher its growth performance. Among the report's recommendations is that countries in Latin America need "to liberalize trade and strengthen their financial systems" to help sustain economic growth.[67] However, Latin American countries would have to take additional measures to benefit from trade liberalization and improve economic conditions. One study on the effects of an FTAA on Latin America reports that any significant effect on incomes and inequality would take a very long time to show up. It states that the long-term economic health of Latin America would require much improvement in education.[68]

Trade Integration and U.S. Interests

Trade integration in the Americas has gained momentum since the 1990s. The possibility of forming an FTAA or trade agreements with Andean countries and Panama is of interest to policymakers because of the economic and political implications for the United States. As the effects of NAFTA on the U.S., Mexican, and Canadian economies become clearer, policymakers are faced with the issue of whether trade agreements are beneficial to the United States and how the United States should proceed in its trade policy in the Western Hemisphere.

An underlying question is whether the United States should continue to deepen trade integration in the Americas and, if so, whether negotiating bilateral trade agreements is the most appropriate trade policy. As pointed out earlier, some analysts do not believe that bilateral trade agreements are the best course of action because they take away the focus from energizing the FTAA negotiations and are slowing down the process. Others believe that RTAs have led to the consolidation of trade agreements into larger free trade areas in other parts of the world and that the same thing could occur in the Western Hemisphere over time.

Another issue is whether the United States should deepen integration with its NAFTA trading partners. A recent study by senior fellows at the Institute for International Economics on the achievements and challenges of NAFTA finds that, while NAFTA has been successful in promoting regional trade and investment, it also has limitations. The authors propose that NAFTA be "upgraded" and that the United States, Canada, and Mexico should convert their free trade agreement into a customs union and adopt a common external tariff. They believe that this would promote commerce among the three trading partners; reduce distortions generated by

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[67] Gregg, Diana I., *International Trade Reporter*, "IMF Says Control of Inflation Big Plus, But Worries Latin America Growth Lags," February 9, 2005.

[68] Blum, Bernardo S., and Edward E. Leamer, "Can an FTAA Suspend the Law of Gravity and Give the Americas Higher Growth and Better Income Distributions?," *Integrating the Americas: FTAA and Beyond*, 2004.

NAFTA rules of origin; and help resolve some of the trade disputes that are affecting trade relationships in North America.[69]

Regional integration also has political implications for the United States. Some observers see the impetus for trade liberalization as political as well as economic. There are several questions that policymakers could consider. To what extent do trade integration agreements foster political stability in a country? Are they a useful tool for building a more democratic, secure, and prosperous region?

[69] Hufbauer, Gary Clyde, and Jeffrey J. Schott, *NAFTA Revisited: Achievements and Challenges*, Institute for International Economics, October 2005.