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LAFTA's Successes and Failures

By Dr Hermann Sautter, Göttingen*

The Latin American Free Trade Association (LAFTA), established by the Treaty of Montevideo in 1960, was an attempt by the participating countries to seek a way out of the dilemma of declining demand for their exports, on the one hand, and the inadequacy of a solely inward-looking strategy in development policy, on the other.

It was the immediate aim of LAFTA to remove import tariffs and other obstacles to trade so as to expand and diversify the commerce among member countries and thereby bring about a progressive integration of the economies of the partner countries. It was envisaged that intrazonal tariffs would be lowered each year by 8 p.c. of those levelled on imports from third countries, so that by 1973 goods would move throughout the free trade area without any liability to import duties. This was to be the basis of more far-reaching cooperation in a Latin American Common Market. The dynamic quality of LAFTA spread in the first few years of the association to other countries of Latin America. Between 1961 and 1967 Colombia, Ecuador, Venezuela and Bolivia announced their accession to LAFTA, assuming the same obligations as the seven founder states. If it is asked today how far LAFTA has progressed towards the ambitious aims of the early years, several undeniable successes can certainly be pointed out.

Expansion of Intrazonal Trade

One of the most striking features of the development of the foreign trade of Latin American countries is the absolute and relative increase of intrazonal exports since 1961, the year in which the first round of negotiations on tariff reductions was conducted by LAFTA.¹ (Table)

In 1969 the value of intrazonal exports was more than twice the 1961 total, and their share in total exports from LAFTA countries rose between these two years from 7.9 p.c. to 11.0 p.c. The structure of these exports is worth notice. The two most important LAFTA members, Argentina and Brazil, accounted for about 50 p.c. In all member countries non-traditional export goods

are playing a much bigger role in intrazonal commerce than in the trade with third countries. The Argentine exports to other LAFTA countries, for instance, consist as to about 21 p.c. of selected manufactures; these contribute no more than 5 p.c. to the country's exports to third countries.²

The multifarious activities of LAFTA acted undoubtedly as the major impulse for enlarging intrazonal trade. In the first ten years of LAFTA the member countries negotiated tariff concessions for about 11,000 different products on the so-called "National Lists". A first "Common List", which unlike the "National Lists" contains irrevocable concessions, has been agreed for 25 p.c. of the most important items of merchandise. Many other forms of collaboration likewise helped to stimulate foreign trade.

Table: Intrazonal Exports in the LAFTA Area

| Year | Intrazonal Exports US \$ mn | Index 1961 = 100 | p.c. of total exports |
|------|-----------------------------|------------------|-----------------------|
| 1962 | 546.9 | 110 | 7.9 |
| 1963 | 583.6 | 120 | 8.5 |
| 1964 | 716.3 | 145 | 10.1 |
| 1965 | 842.0 | 170 | 10.8 |
| 1966 | 875.6 | 173 | 10.2 |
| 1967 | 851.7 | 171 | 9.9 |
| 1968 | 992.2 | 193 | 10.4 |
| 1969 | 1,130.3 | 223 | 11.0 |

Source: INTAL, Boletín de la Integración (Integration Report), May 1971, Vol. VI, No. 65, p. 259.

It became very soon manifest that the tariff cuts needed supplementing by monetary measures. In 1966 the partner countries therefore agreed on the creation of a multinational settlement system

² Included were the so-called "productos manufacturados seleccionados" with the exception of the 4 most important processed agricultural products. Cf.: H. Sautter, *Strukturveränderungen im argentinischen Außenhandel unter dem Einfluß der europäischen Handelspolitik* (Structural changes in Argentina's foreign trade under the influence of the European trade policy), published at the end of 1971 in the series of publications by the Institut für Iberoamerika-Kunde, Hamburg.

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¹ ALALC-BID-INTAL: Siete años de acción de la ALALC (Seven years of LAFTA action), Buenos Aires, 1968, p. 16.

("sistema de créditos recíprocos y de compensación multilateral de pagos"). Although this clearing system is not a constituent part of the Treaty of Montevideo, it is to be regarded as an immediate outcome of the trade liberalisation initiated under that agreement and a demonstration of the will to resolve jointly any new problems which it might entail.

The nucleus of this system consists of the credit lines in convertible currency which the central banks of the member countries accord each other for bilaterally arranged sums. A multinational settlement of the balances as reported by the participating central banks is effected at quarterly intervals by the Banco Central de Reserva del Peru. The system has the merit of economy in the use of foreign currencies because a minor part of all transactions only need be settled in convertible currencies. In 1970 this had to be done in only 18 p.c. of all operations.³ About 48 p.c. of all intrazonal imports in 1969 were cleared by this system which now comprises 31 bilateral agreements. The clearing system has proved its effectiveness in the past years and represents a success in monetary cooperation between the LAFTA countries.

The Supplementary Industrial Agreements

The supplementary industrial agreements ("acuerdos de complementación") are another instrument of economic cooperation and have been gaining in importance since 1964. Articles 16 and 17 of the Treaty of Montevideo provided for such agreements. They have the aim of gradually coordinating the industrialisation policies of the signatory states and are for this purpose to bring about an understanding between representatives of the interested economic sectors. The initiative for the conclusion of such treaties lies clearly with the industrialists to whom LAFTA provides a regular opportunity for negotiations in their sectorial reunions. Negotiations on tariff cuts at the governmental level have been shown to have a much better chance of succeeding when preceded by such negotiations on the private level.⁴

In contrast to the concessions on the "National Lists" the tariff reductions negotiated in the framework of the supplementary agreements benefit only the contracting parties. A LAFTA member country which wants to accede to a supplementary agreement concluded by other partner states can under the present provisions do so only by offering an appropriate concession to the original signatories. It is thus crucial in

these agreements that the offers should be of equal value. To that extent they are chiefly an instrument for more intensive cooperation between countries at the same level of development. The 16 agreements concluded to date concern modern industrial sectors such as, e.g., the production of electronic data processing plant, electronic tubes, petrochemicals, office machines, air conditioning equipment, chemical-pharmaceutical products, etc. The tariffs of about 1,600 products were lowered in this way.⁵ It is due to the supplementary agreements that a big expansion was recorded in the intrazonal trade in highly labour-intensive industrial products in recent years, even though their share in total exports is still very small.

That LAFTA has facilitated many forms of political and economic cooperation as a permanent institution may be regarded as another positive aspect. It was on the basis of LAFTA that treaties were concluded to simplify international transport between Argentina, Brazil and Uruguay, to facilitate passenger traffic, to pursue a common policy in regard to shipping, to develop border regions of neighbouring states conjointly, etc. The regular meeting of entrepreneurs in the sectorial reunions offered opportunities for short-term arrangements on the handling of temporary production surpluses and deficits. Collaboration between LAFTA and the Inter-American Development Bank (IDB) has resulted in many investments of multinational importance which have accelerated the physical integration of the continent.

All these successes in peripheral fields cannot however hide the fact that LAFTA has so far failed in its main tasks and that it is at present still quite uncertain whether it will ever achieve its objectives. Which failures of LAFTA are responsible for this pessimistic forecast?

The Failure of Trade Liberalisation

The arrangements for the bulk of the tariff concessions were made in the first four years of LAFTA. Of 11,049 concessions on the "National Lists" in force now, 8,248 had been arranged by 1964. Since 1965 the programme of trade liberalisation has been stagnating. In that year no more than 226 concessions were negotiated; for 1970 the member countries reached agreement on tariff cuts on 149 items, and in 1971 the tariffs for 31 products only were reduced.⁶ The original plan of annual tariff cuts by 8 p.c. has thus failed. In the past two years it has not even been possible

³ INTAL: Boletín de la Integración (Integration Report), year VI, No. 65, May 1971, p. 260.

⁴ ALALC-BID-INTAL: Siete años de acción de la ALALC (Seven years of LAFTA action), *ibid.*, p. 109.

⁵ Cf. Deutsche Oberseische Bank, Wirtschaftsbericht über die lateinamerikanischen Länder sowie Spanien und Portugal (Economic Report on Latin America, Spain and Portugal), October 1971, p. 7.

⁶ Deutsche Oberseische Bank, *ibid.*, p. 6.

to carry out the minimum programme agreed upon under the Protocol of Caracas of 1969 which provided for annual tariff reductions of 2.9 p.c. The second "Common List" which would have been due in 1967 also failed to materialise because some smaller member countries did not feel able to agree to irrevocable tariff cuts for wheat and petroleum.

This development did not come as a surprise. The initial successes in trade liberalisation were achieved for goods presenting no problems because they had been exchanged between the member countries before LAFTA was set up. The willingness to make concessions grew progressively smaller as the removal of trade barriers impinged upon the member states' national development policies. For agricultural produce the contracting parties had reserved the possibility of resorting to far-reaching protective clauses in the foundation treaty of LAFTA already.⁷ Not one of them was willing to do without a self-sufficiency policy for agriculture.

Differences in Development States

Farther-reaching concessions for industrial products were foiled by LAFTA's main problem — the differences in the state of development reached by the member countries. The three big members Argentina, Brazil and Mexico were not willing to offer one-sided concessions to benefit their relatively less advanced partners. They gave priority to their own national development, and increased intrazonal trade was in their view to result from a speed-up of industrialisation. The small and relatively underdeveloped partner countries, on the other hand, were hardly in a position to offer concessions and, besides, were afraid of the "backwash" of trade liberalisation. They looked on LAFTA primarily as a means of promoting industrialisation by enlargement of their markets. These divergent expectations had been manifest already when the Treaty of Montevideo was signed and at that time led to a compromise in the form of a cumbersome procedure of product-by-product negotiations for the annual tariff reductions. These discrepancies between the individual countries, which had prevented the adoption of a more automatic integration process when LAFTA was founded, made themselves felt increasingly in subsequent years and in the end resulted in a complete obstruction of the annual rounds of negotiations. That the only, albeit slight, advances still being made at present flow from the negotiations on supplementary industrial agreements is further evidence of the fact that

differences in the levels of development are the unsolved cardinal problem of LAFTA. Equilibration of concessions is, as has been mentioned, an essential prerequisite for the conclusion of such agreements.

The problem of development differentials could be solved only through concerted development planning by all LAFTA member countries. Undesirable polarisation effects could thereby be avoided and the resistance of the smaller countries to unimpeded intrazonal trade be overcome. Attempts towards such a policy were made at various times. In its Resolution 100 in 1964 the Fourth Ordinary Conference postulated increased activities for the coordination of industrialisation policies, agrarian policy and measures in the monetary and fiscal fields. The American Presidents at their meeting at Punta del Este in 1967 likewise reaffirmed the need for complementing the tariff reductions by a common development policy so as to facilitate the transition of LAFTA to a Common Market. None of these beginnings however were pursued much farther. The task of developing the partner countries economically and integrating them at the same time in one unit — which is LAFTA's specific problem — remained unresolved.

The Lack of a Concerted Development Policy

Through their foreign trade the LAFTA countries have, up to the present time, been more strongly integrated with third countries than amongst themselves. Single-commodity productions for export to industrial countries occupy a strong structural position in their economies, and the bulk of imports, consisting of primary products, semi-manufactures and finished goods, also comes from third countries. The structure of foreign trade is reflected by the transport and communications network which owing to its one-sided orientation towards third countries promotes fragmentation rather than integration. The prevailing capital stringency and underemployment raise political problems which mitigate against any reallocation of resources such as would be inevitably involved in integration. Lack of coordination in monetary and currency policy almost nullifies the benefit of any tariff reduction programme. In contrast to the European countries where variations in development are less important and trade relations were intimate already before the trade obstacles were tackled, removal of trade obstacles as an isolated measure cannot be expected in LAFTA to set off an integration process. From this conclusions have been drawn on a sub-regional level which raise new issues for the future of LAFTA.

⁷ Cf. Article 27 seq. of the Treaty, in: ALALC, Tratado de Montevideo (Treaty of Montevideo), Montevideo, 1967.

Impatience with the dilatory progress of the integration process in LAFTA prompted the Andean countries — Colombia, Bolivia, Chile, Ecuador and Peru — to seek closer association by the Cartagena Agreement of May 25, 1969. The member countries of this so-called "Andean Group" are aiming on a subregional level at the objectives which have hitherto eluded Latin America on a continental scale — acceleration of trade liberalisation by an automatic programme of tariff cuts, a common industrialisation policy, coordination of national development plans and harmonisation over large areas of economic policy.

Compatibility with the Treaty of Montevideo was essential for the conclusion of the Agreement of Cartagena as all members of the Andean group are also members of LAFTA. The countries of the Andean group expressly stated that their subregional integration was intended to create more favourable conditions for further progress in LAFTA. Nevertheless there is no denying that through the Andean group an alternative to LAFTA has come into being which may erode the latter even more, especially if others emulate this example of a subregional integration unit.

Latin America and the European Communities

By Dr Jürgen Westphalen, Hamburg *

The Latin American reaction to the Common Market of European industrial countries was from the outset marked by scepticism and criticism. It was only recently that new tendencies have been discerned which can perhaps lead to a partial improvement in the relations between EEC and Latin America.

Various measures in European trade policy, especially on tariffs, have had a positive influence on the Latin American attitude to the EEC. New constructive proposals for the development of the mutual relations in the future have come from both sides — in the "Declaration of Buenos Aires" on July 29, 1970,¹ and the EEC Commission's report to the Community Council on "Relations with the Latin American Countries" of July 29, 1969.² A new approach to international cooperation has been indicated by the Bilateral Trade Agreement between the EEC and Argentina which was signed on November 8, 1971, and this may well be followed by similar agreements with other Latin American states.

The EEC has hitherto failed in giving the Latin American public an accurate picture of itself.³ As seen from Latin America, the European Common Market, on the one hand, sets an example worth emulating in its own integration efforts in the framework of the Central American Common Mar-

ket and the "Andean Group" and, on the other, constitutes a "selfish protective alliance" which handicaps third countries — and the developing countries of Latin America in particular — through its common external tariff, the protection given to local farmers and the policy of association.

Fears for Latin American Exports

The common agricultural policy — so runs the argument in temperate-zone countries of Latin America and in Argentina and Uruguay in particular — impairs Europe's imports of meat, cereals and other agricultural produce and aims at "self-sufficiency at a higher cost level . . . and possibly even export surpluses based on subsidies".⁴ The association policy — it is said in tropical countries of Latin America — with its tariff preferences gives aid and encouragement to the associated African countries competing with Latin America. A glance at the EEC's foreign trade statistics shows indeed that the fears of Argentina and Uruguay for the exports of their principal traditional products are not entirely unfounded. It must certainly be borne in mind that the common agricultural policy is not the only determinant of EEC imports of such agricultural produce from Latin America. Others, such as the trend of production

* Deutsch-Südamerikanische Bank.

¹ Cf. *Lateinamerika und die Europäischen Gemeinschaften* (Latin America and the European Communities). In: *Kurzbericht über Lateinamerika*. No. 4/70. Issued by Deutsch-Südamerikanische Bank A. G., Hamburg. P. 12 seq.

² Cf. *Die Beziehungen der EWG zu Lateinamerika* (The Relations of the EEC with Latin America). In: *Kurzbericht über Lateinamerika*. No. 1/70. Issued by Deutsch-Südamerikanische Bank A. G., Hamburg. P. 11 seq.

³ Cf. W. Renner, *Zusammenhalt der Gemeinschaft nach außen* (The External Cohesion of the Community). In: *La Notion d'un Marché Commun dans un Processus d'Intégration*. Bruges 1969. P. 117 seq.

⁴ *Hacia la Coordinación de la Política Comercial de América Latina*. Las Relaciones con la Comunidad Económica Europea. Análisis y recomendaciones del grupo de consultadores convocado por la Secretaría. Issued by CEPAL. Santiago de Chile 1962.