

It Takes Two to Tango: Can Brazil and the U.S.
Dance to the Same Regional Beat?

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Abstract

It Takes Two to Tango: Can Brazil and the U.S.
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The proposed Free Trade Area of the Americas has come to a standstill. Reasons for this reside in three aspects in which the FTAA differs from other regional integration schemes. First, it would combine existing preferential trading arrangements of which NAFTA and MERCOSUR are the two most significant ones. Second, each of the schemes has an undisputed regional leader: the U.S. and Brazil. However, two hegemon do not agree on a common vision for the hemispheric project. Third, the small membership of the two schemes is to be elevated to an area encompassing 34 states, i.e. to a situation of large n .

The literature maintains that the provision of a collective good becomes more difficult the larger the number of members party to the scheme. The solution offered for this problem of large n is the existence of either a hegemon or a group of likeminded states to overcome collective action problems. In the case of the Americas, the solution offered by the literature is the very problem for efforts to integrate the hemisphere. The FTAA negotiations are stalled because the attempt to forge collective action among 34 member states is sought by two countries simultaneously.

This thesis suggests that the large n problem of hemispheric integration will be resolved by the hegemon more successful in subdividing the group size and imposing its vision. The research of this study therefore compares the procedural strategies of the U.S. and Brazil in their quest to shape the substance of the regional scheme.

Acronyms

ALADI	Asociación Latinoamericana de Integración (Latin-American Integration Association)
APEC	Asia-Pacific Economic Cooperation
CAN	Comunidad Andina (Andean Community)
CARICOM	Caribbean Community and Common Market
CET	Common External Tariff
CU	Customs Union
CUSFTA	Canada-U.S. Free Trade Agreement
EAI	Enterprise of the Americas Initiative
ECLAC	Economic Commission for Latin America and the Caribbean
EU	European Union
FDI	Foreign Direct Investment
FTA	Free Trade Area
FTAA	Free Trade Area of the Americas
GDP	Gross Domestic Product
ISI	Import Substitute Industrialization
LEM	Large Emerging-Market Economy
MERCOSUR	Mercado Común del Sur The Common Market of the South

NAFTA	North American Free Trade Agreement
NTB	Non Tariff Barrier
PTA	Preferential Trading Arrangement
SACN	South American Community of Nations
SELA	Latin American Economic System
TNC	Transnational Corporation
TPA	Trade Promotion Authority
TRQ	Tariff Rate Quota
USTR	United States Trade Representative
WTO	World Trade Organization

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CHAPTER ONE: INTRODUCTION

1.1 What Project for the Western Hemisphere?

The idea to unite the states of the Americas into a single economic regional scheme area was born of two diplomatic initiatives, President George Bush's 1990 Enterprise for the Americas initiative (EAI), and the Summit of the Americas in Miami, U.S., December 1994. In Miami, Western hemispheric heads of state agreed to integrate their 34 countries into a Free Trade Area of the Americas (FTAA), seeing it as

a key to prosperity in trade without barriers, without subsidies, without unfair practices, and with an increasing stream of productive investments. Eliminating impediments to market access for goods and services among our countries will foster our economic growth. [...] Free trade and increased economic integration are key factors for raising standards of living, improving the working conditions of people in the Americas and better protecting the environment (Free Trade of the Americas 1994).

However, it is clear that hemispheric negotiations have not yet produced anything substantive. This is in spite of renewed commitment made by the heads of state at the Third Summit in Quebec City in April 2001 "to ensure that negotiations of the FTAA Agreement are concluded no later than January 2005" (Free Trade of the Americas 2001). Talks between the main actors have slowed and the two co-chairs of the process, the U.S. and Brazil, appear more interested in parallel integration projects in the region than in the common hemispheric one.

Leaders at the Fourth Summit of the Americas, which took place in Mar del Plata, Argentina on November 4-5, 2005, were hoping to produce a summit declaration that could call for relaunching talks on the FTAA. However, the Summit ended without a clear agreement on when to resume talks on the trade agreement, or even if talks could be

resumed. As it presently stands, the FTAA is a half-baked project with a very uncertain future.

The standstill in the FTAA process is the subject of this study. Many regional schemes have been conceived without coming to fruition; in that, the FTAA needs not be an exceptional case. However, the FTAA is an interesting case because the reason of the standstill points to a previously unobserved situation of integration schemes. There are three aspects in which the proposed FTAA differs from European integration as the traditional benchmark for preferential trading arrangements (PTAs) elsewhere.¹

First, it would combine several existent preferential trading arrangements (PTAs) – most notably the North American Free Trade Agreement (NAFTA) and the Common Market of the South (MERCOSUR).² These are the two most economically and politically significant PTAs of the Americas. Second, this importance results from the dominance of the United States and Brazil in either scheme. The U.S. and Brazil as the dominant countries in the respective PTAs have different views about the substantive and institutional shape of hemispheric integration.³ This is compounded by the economic disparities between the prospective future members along the North/South axis. Third, the small permanent membership of three (NAFTA) and four (MERCOSUR), respectively, is to be elevated to an agreement encompassing 34 states, i.e. to a situation of large membership (large n).

1.2 Not Accounted for by the Literature

Literature argues that the existence of an undisputed regional leader is a key condition for the successful integration of a regional scheme.⁴ Scholarship has

demonstrated that collective action problems are inherent in group behavior. Even if members of a group have similar interests, they may not be able to act collectively, as individual and social incentives may conflict. Two principal collective action problems occur in integration schemes. The first is free-riding, when countries defect from the obligation of contributing to the cost of building of an integrated economy while enjoying the benefits of the joint effort by others. The second is the problem of vision, when countries are unable to decide on a course of action in order to obtain a specific goal in a situation in which states have opposing interests.

Literature maintains that collective action becomes exponentially more difficult the larger the number of countries is that are part of a supranational organization. Such is the case of the Americas; the scheme aims to encompass 34 countries into a unique trading bloc, creating a situation of large n . Literature offers two solutions for the problem of large n membership: the presence of a hegemon (like the U.S. within NAFTA), or a group of likeminded states (such as Germany and France for European integration).

Scholarship therefore explains that a way out of collective problems encountered in a large n scheme can be mitigated through the presence of an undisputed leader. This undisputed regional leader, recognized by other members of the region to be more important to the group than that of any other state, facilitates the integration process by coordinating rules, regulations, and policies. As well, the leader eases distributional tensions that arise through side payments to countries benefiting unequally from the trade agreement. However, in the case of the Americas, *both* Brazil and U.S. act as regional powers in the South and North America respectively.

The solution offered by the theoretical scholarship, therefore, is the very problem for efforts to economically integrate the Western hemisphere. Although the large n concern can typically be addressed through the presence of a regional economic power, the FTAA negotiations are stalled because the attempt to forge collective action among 34 member states is sought by *two* countries. Albeit being the co-chairs of the FTAA talks, the U.S. and Brazil pursue opposing strategies of *sub*-regional integration rather than jointly advancing a hemispheric scheme. The U.S. seeks to negotiate bilateral free trade agreements with individual Latin American countries to isolate Brazil; conversely, Brazil reinvigorated MERCOSUR, extended its associate membership, and was instrumental in establishing the South American Community of Nations (SACN) in order to increase its bargaining power vis-à-vis the United States through a South American bloc.

Apart from collective action problems, the difficulties of large sized groups are likely to be further compounded when the integration project integrates countries at very different levels of economic and social development. Of the 34 countries involved in the negotiating process, only the U.S. and Canada are recognized as being industrialized nations, the other 32 being considered to be lesser-developed countries (LDCs) located in Latin America.⁵ Both the countries of the Southern Cone and those of the Northern continent are keenly preoccupied with the difference in levels of development between the 34 future members. Where the larger country is also more industrialized, this will accentuate the fears of smaller members that it is the larger country which will benefit most from the arrangement. For the industrialized countries, there is a concern of job loss as business moves to where labor is cheaper.

Within the context of the Americas, this fact has a bearing on the substance of the final agreement. As recognized regional co-leader of the integration process, Brazil is committed to assuring that issues relating to development are a key feature of the accord.⁶ For the United States, the president is concerned with getting trade agreements approved in Congress where sectoral and group interests lobby in their favor. Attempting to further their respective causes, both countries are subdividing the large n problem differently (Hülsemeyer and Cobbett, under review).

The regional integration of the Americas therefore presents a double-sided puzzle. Instead of spearheading the process, the presence of two leaders among the group of countries seeking closer ties has created further problems and has slowed down the negotiations. The stall in the process is therefore a symptom of lack of coordination between these two key countries.

Does this mean the death of the FTAA? Not necessarily, but it does mean that, given the unprecedented situation of a regional scheme composed of two leaders who do not share the same vision, we do not know what to expect in this case. Relevant literature does not tell us how this scenario will unfold, what the factors are that will determine the outcome.

Empirically and theoretically, therefore, the case of the Americas brings us onto virgin terrain; both in terms of the large n and in terms of North/South development divide. These two aspects of the America's project bring us to new development in regional integration schemes. What remains undone theoretically and empirically is the explanation of how integration will take place in the Americas. To do this, the theoretical

focus of my thesis will be on large n , the implications of the North/South being treated in Chapter 3 within the framework of the political empirical research.

1.3 Research Question

Within this context, the main research question addressed by this study is what form the finished agreement will take. While this thesis should logically deal with two questions - firstly, what is the likelihood of an American hemispheric regional scheme coming about and, secondly, what form will the future agreement take, it will concern itself with the second question, situating the possibility of there being no FTAA as one of three plausible outcomes. This organization of the thesis in this manner permits an exploration of the Americas as a case where two regional leaders are involved in a common process of regional integration.

This thesis suggests that the large n problem of supranational organization is *substantively* “solved” by the regional economic hegemon that is *procedurally* more successful in subdividing the group size (Huelsemeyer, and Cobbett, under review). The paper compares the strategies of the United States and Brazil in their quests to shape the content of the hemispheric integration project. The research question of the thesis looks at whether the institutional framework of the agreement will resemble that of a free trade area along the NAFTA template, as wished for by the United States, or will it resemble that of a customs union along the MERCOSUR template, as is the pattern in South America and as is championed by Brazil.

Therefore, in spite of the limitation of existing literature to indicate the possible outcomes of this impasse, in principle three scenarios can be expected in this case. First,

that the negotiating process will come to a dead end and that there will be no FTAA as the U.S. and Brazil remain deadlocked. Second, that the hemispheric agreement is negotiated in America's favor and is an agreement along the lines of NAFTA with no concession for Brazil's interests. Third, that the hemispheric agreement be signed as an agreement that goes beyond the NAFTA model. Any agreement that includes agriculture, such as a NAFTA +, or that is a complete customs union or a customs union within certain sectors of the economy will be signed in Brazil's favor.

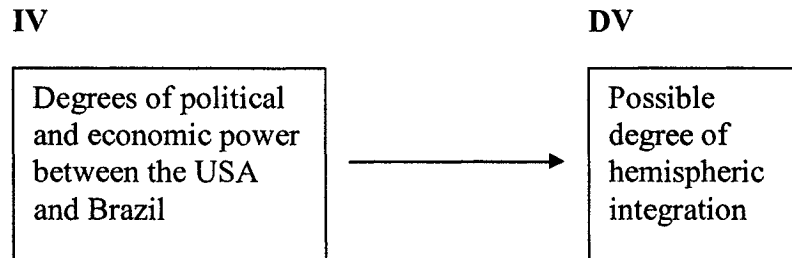
1.4 Analytical Framework

The analytical framework used to answer this question identifies the economic and political means at the disposal of the two regional powers to shape the integration process. I analytically separate political (decision-making process; domestic interests represented in negotiations) and economic (importance and direction of foreign trade and FDI) indicators to determine their relative bargaining power to ultimately capture all prospective 34 members. Figure 1 illustrates the argument. In a causal argument, the dependent variable (DV) is determined by the independent variable (IV). More specifically, the values of the IV have direct bearing on the outcome, the DV. In this case, the IV measures the degrees and use of both political and economic powers between the two countries in shaping an outcome of the negotiations in their favor. The DV is the possible outcome of the negotiating process between the two regional powers, the U.S. and Brazil.

This study is therefore an attempt to offer a specific explanation of the integration process in the Americas, an integration case with no empirical comparison, and to

examine the possible degrees of regional integration as likely outcomes of the negotiating process between the two regional powers, the U.S. and Brazil.

Figure 1: Causality of Argument



Note: IV- independent variable; DV-dependent variable

1.5 Organization of Thesis

The structure of the thesis will proceed as follows. The following chapter presents the theoretical framework within which this study will be conducted. It offers an overview of relevant literature beginning with Mancur Olson's (1971) *The Logic of Collective Action: Public Goods and the Theory of Groups*. This work's principal thesis is that rational self-interested individuals, coming together in a group, will not necessarily be able to achieve a common group interest. This is so even if there is unanimous agreement in a group about the common good and the methods of achieving it. Moreover, larger groups are less likely to achieve their goals than smaller groups.

Building on Olson's framework, Kindleberger elaborated a theory of group action through the presence of a hegemon. The hegemonic stability theory argues that the country with an outstanding economic and political power articulates and enforces the

rules of interaction among states, providing them with an international structure where smooth and beneficial international exchange can take place. In other words, the hegemon provides the international community with a public good, a more stable and secure environment.

This principle was taken up in more recent work where Mattli (1999) argued that the presence of a regional power was a key condition to successful regional integration. Mattli also expounded in *Logic of Regional Integration*, that regional integration was the result of a response by the political community to pressures of the business community to integrate into an economic bloc. Mansfield and Milner (1999) however, in a comprehensive review of regional integration schemes *The New Wave of Regionalism*, argue against Mattli's conclusion, explaining that the initiative for regional integration can arise within the political community.

The third chapter is the first of two chapters of empirical research. This research focuses on the U.S.-Brazil standoff within the framework of relational power. Within this concept, two dimensions are identified which will become the basis of the empirical research of this study, namely economic and political powers. Economic power within this context can be understood as the power relationship between the trading nations. Political power will be articulated around the different political cultures of the United States and Brazil, as well as on the different strategies used by both countries to rally support. Political and economic empirical research forms the basis of the third and fourth chapters respectively.

The last chapter evaluates, on the strength of the empirical research, whether the institutional framework of the agreement will resemble that of a free trade area like

NAFTA, as wished for by the U.S., or will it resemble that of a customs union, as is the pattern in South America and as is championed by Brazil. The conclusion also addresses the theoretical implications of this investigation.

CHAPTER TWO: LITERATURE, RESEARCH DESIGN, AND METHODOLOGY

Collective goods are the characteristic organizational goods, for ordinary non-collective goods can always be provided by individual action, and only where common purposes or collective goods are concerned is organization or group action ever indispensable (Olson 1971: 16).

2.1 Literature Review

The future hemispheric agreement of the Americas is a process involving 34 countries whose common goal is to agree upon a common set of rules and regulations that will frame their mutual economic relationships. This highly ambitious project necessitates the acceptance of all members of a single common legal framework. The framework will reflect the level of economic and political integration agreed upon, as well as the modalities of implementation. Decisions relating to the rate at which tariffs must be phased out, which goods and services can be excluded from the agreement and what side payments must be made to compensate asymmetric benefits must be agreed upon. How is such a framework agreed upon? How do 34 countries agree on the nature of their collective good?

The following literature review covers the theoretical contributions in answer these questions. The concept of *public goods* is not new to the field of international political economy. However, the proliferation of regional schemes in the last twenty years has brought to the fore an interest on issues relating to regional public goods. Furthermore, recent large n regional schemes have added another dimension to this study, how do projects with large membership overcome collective action problems.

2.1.1 *Collective Action Problems – Olson (1971)*

The work of Mancur Olson, *The Logic of Collective Action* (1971), was critical in explaining how groups worked together in spite of conflicting interests and varying levels of capabilities. Olson pointed out that voluntary rational self-interested individuals, coming together in a group, would not necessarily be able to achieve a common group interest. This is so even if there is unanimous agreement in a group about the common good and the methods of achieving it. Moreover, Olson claims that the larger the group, the less likelihood there is of the group furthering its common interest. Olson therefore frames his argument of collective action in terms of small vs. small groups.

As well as facing problems in the achievement of the common goal, Olson pointed out that the provision of the public or collective good is further characterized by a singular trait, that of the difficulty of excluding others from benefiting from it (1971: 14-16). Public goods are those where consumption by one person does not reduce the amount available to others. The impossibility of exclusion inherent in these goods has implications for its provision; members know that once the collective good is established, all will benefit equally even if all have not contribute equally to its provision. This impossibility of exclusion has an important impact on the incentive of certain members to pay for the good (Hasenclever et al. 2002: 88) and therefore creates problems of collective action. This is ever more the case the larger the group. Consequently, all collective action problems share the characteristic that excluding non-contributors to a collective benefit is an important cost. Collective action problems differ depending on how difficult it is to exclude others.

Situating the FTAA within this theoretical framework, it is clear that the large n of 34 countries has bearing on their capacity to provide themselves with a collective good. There is the question of choice among the varying possibilities of the future agreement's framework as well as the question of who will bear the responsibility of providing the good. Olson identifies three key factors that keep large n groups from furthering their common interest. The FTAA, as a large group, is consequently touched by these elements.

First, due to large n , members expect to receive smaller fractions of collective benefits. As the portion each member obtains of the collective good decreases with group size, individual reward for group-oriented action is further reduced. The individual member therefore discontinues participating fully before the optimal amount for the group as a whole has been obtained (Olson 1971: 35). This leads to a suboptimal supply of the common good because of the problem of dispersed benefits.

Second, suboptimal supply of the common good can be offset by small subsets. A small number of members that stand to gain enough from the collective good in order to provide it could offset suboptimal supply. However, the larger the group, the less likelihood there is that a small number of members optimize the supply of the collective good through concerted action.

Third, in larger groups there are higher organizational costs to be overcome before any of the collective good can be obtained. As the numbers of members increase, so do the related costs of organization of those members, decreasing the incentive for individual members to shoulder the burden. Thus, the higher the hurdle to jump before

anyone can benefit from the collective good, the less individual members feel like jumping it (Olson 1971: 48).

For these reasons, the larger the group, the harder it is to it to provide itself with an optimal supply of the desired collective good. Without coercion or outside incentives, large groups will not obtain even minimal amounts of the collective good. In this respect, the 34 countries of the Western hemisphere form what Olson would call a *latent* group. The group has the potential of providing itself with a common trade agreement but is unable to realize that potential power (1971: 49-51).

The group's inability can in principle be overcome by three types of organizations (Olson 1971:49-51). Firstly, latent groups with a large n can have the collective good obtained through the aide of "selective incentives." These selective incentives persuade group members to act in a group-minded way. This can be through positive reward or through coercion such as compulsory membership. The incentives are used in such a way as to affect only members, and not other individuals or groups outside of this organization. A latent group that acts in the group interest as a result of positive or negative incentives is called a "mobilized group."

Next, there are intermediate groups, small subsets of like-minded members who offer a way out of collective inaction by organizing the larger group. In such a group, no single member gets a share of the collective good that is sufficient to give him the incentive to provide it himself. Yet, the group is small enough that all members will be aware when another member does not contribute to the provision of the good. Coordination of the group is conducted through decision-making at the micro level. Large n groups with small subsets of likeminded members can therefore be moved from

latency to action through decision made by the small group. The Franco-German leadership within the European context is an example of a small subset within a larger group. Their partnership facilitated collective action when the European Community was a group composed of 12 and later 15 members; their leadership moved European integration forward and through the different stages of integration.⁷

Finally, groups can be mobilized through the action of at least one member who has sufficient incentive to bear the full burden of providing the collective good himself. Groups that have at least one of these types of members are called privileged groups. In these groups, there is an assumption that the collective good will be provided, without any group organization or coordination, solely because one powerful member wants and provides it.

Two features are attributed to this special case. Firstly, since no member of a group can be prevented from benefiting from the collective good, smaller actors will “free ride” on the largest member’s decision to bear a disproportionate part of the burden of providing the good (Olson 1971: 29-35). Therefore, and secondly, in privileged groups there is a tendency for the exploitation of the great by the small. The distribution of capabilities and incentives within these groups produces a situation of internal asymmetry. This asymmetry, however, works to the group’s advantage in that the smaller members receive the benefits of the collective good provided by the powerful member. In return, this leader determines the nature of the collective good provided.

Can any of these three solutions apply to the FTAA case? The first response of selective incentives cannot be applied to the regional scheme because the project is voluntary, ruling out the possibility of coercion to the group through compulsory

membership. Apart from coercion, there is also no evidence of positive inducements in the form of side payments. In fact, there is no evidence of other additional inducements besides the potential benefit of the collective good inciting the countries of the Western hemisphere to produce the good. The next possibility is the subset of likeminded members who move the group through its inaction. However, this option is not viable for the FTAA as Brazil and the United States (the only meaningful subgroup) are not likeminded and do not have the same vision of the collective good; otherwise, the FTAA talks would not be stalled in the first place. While the U.S. could theoretically find another partner and form another small group, this option is restricted by the fact that only Brazil is formally recognized as America's co-chair for the integration process and there is not another regional power to match Brazil's in the Southern Cone. What is left, then, is the option of a privileged group where a member must be willing to provide the collective good without the cooperation of other countries.

2.1.2 Hegemonic Stability Theory – Kindleberger (1973)

In the realm of international politics, Kindleberger (1973) developed the so-called Hegemonic Stability Theory (HST) as a special case within Olson's theory of collective action. Kindleberger adapted Olson's analytical framework to explain group action, that of states, in the international system. Analyzed within the Realist's paradigm, the international system is understood as being in a state of anarchy, there being no central authority. This anarchic system creates a security dilemma where states are fearful of each other. All countries try to gain security, obtain military superiority, and improve one's own security status. However, absolute security is impossible because states will

always have different capabilities of securing this end, creating insecurity among those less well equipped. States become trapped in the “Security Dilemma” as they attempt to increase their relative strength. For this reason, states are concerned with relative gains, that is to say, the amount of economic and political gains a state has in comparison to others.

Within such a context, cooperation for mutual benefit is unlikely. The security dilemma creates a situation where member states are unable to provide themselves with a collective good. Kindleberger’s contribution to understanding cooperation within such a system was to identify the presence of an outstanding economic and political power, a hegemon, as necessary to the provision of a collective good. Kindleberger argued that a single economic and political power, a hegemon, is necessary to provide and enforce a liberal trading order, which he considers an international public good. This single dominant state articulates and enforces the rules of interaction among states, providing them with an international structure where smooth and beneficial international exchange can take place. The hegemon has both the means and the willingness to do so. Other states recognize this asymmetric power and accept this dominance, recognizing that it provides them with the collective good.

The Hegemonic Stability Theory therefore argues that the presence of a hegemon creates a privileged group of the type described by Olson. The superpower facilitates collective action of large n groups by supplying and supporting the rules and regulations of the international system. While the hegemon bears the costs and responsibilities related to this role, it determines what the collective good will look like and the prevailing rules of conduct. Even though providing these public goods is costly, the

hegemon gains, even if it disproportionately bears the expense alone. If the international system prospers, the hegemon necessarily prospers as well, and it may secure or even extend the hegemon's leadership role.

The theory of hegemonic stability is therefore based on the Olsonian principle that large n groups are unable to engage in collective action unless the group is privileged by the presence of a hegemon. The powerful member provides the collective good through independent action (Hasenclever et al. 2002: 93), enabling collective action by supplying and supporting economic rules and regulations for the (at the time Western) international system, i.e. the largest n conceivable.

Since the elaboration of this theory to explain state interaction at the macro level, these theoretical underpinnings are being explored in literature at the mezzo level of regional integration. Mattli (1999) elaborates a conceptual model of regional integration where the role of an undisputed leader is identified as a prerequisite for successful integration.

2.1.3 The Logic of Regional Integration – Mattli (1999)

Whereby Kindleberger studied the role of a hegemon within the international arena, the role of a hegemon in regional schemes is a new element to have emerged in scholarship. Investigating the conditions under which a PTA is likely to be “successful”, conceptualized as the actual implementation of the stated goals of any regional integration treaty (i.e. irrespective of its *degree*), he asserts the existence of a general logic of regional integration.

Mattli identifies one demand and two supply conditions for successful PTAs; the former arises when businesses perceive advantages to be gained from wider markets with the *same* regulations, as this would create a more predictable environment (1999: 48-9). The more pronounced the market density already is (as in Europe and North America), the larger are the potential economies of scale, and hence the stronger is the pressure by the business community for common regulations.

Political leaders are more willing to accommodate the demand for functional integration (Mattli 1999: 50), the higher they judge the possible economic and political payoff of a regional scheme. Assumed to value both political autonomy and reelection, a prosperous domestic economy decreases, and an ailing one increases, their propensity to negotiate a PTA. Yet, their ability to do so, mirroring Olson's analytical framework, depends upon the resolution of a collective action and a coordination problem; they constitute Mattli's two supply conditions for successful integration. First, "commitment institutions" ensure compliance with the agreed upon collective rules and regulations. Without them, integration becomes more elusive but is nonetheless possible (Mattli 1999: 54). Therefore, they only constitute a weak supply condition, since apart from the European Commission no other successful PTA has a supranational commitment institution.

Mattli stipulates that the strong and absolutely necessary supply condition is the presence of an undisputed regional leader among the countries seeking closer ties. This requirement matches the privileged group model elaborated by Olson and adapted by Kindlberger into the hegemonic presence. Mattli sets out what exactly the tasks of the regional economic and political leader have to be in order to overcome large n group

latency. The regional leader serves as the focal point for joint rules, regulations, and policies in the integration scheme. Second, the leader eases the distributional tensions inherent in any regional scheme by acting as regional “paymaster” (Mattli 1999: 56).

The strong supply condition is the underpinning of successful integration. Mattli stipulates that the presence of an undisputed regional leader among the countries seeking closer ties is a prerequisite for *all* regional schemes. A large n group will remain latent, unable to provide itself with a collective good, if there is not a political and economic superpower willing to assume the role of providing the good for the group.

As in Olson’s privileged group, the regional leader has much to gain from the provision of this collective good. It is therefore willing to shoulder a disproportionate amount of the costs and responsibility related to the provision of the good. Regional benefits in the form of freer trade and agreements on issues such as intellectual property and government procurement, as in the case of a future FTAA, are public goods from which the hegemon will directly benefit. The hegemon also stands to benefit from having increased influence in the region, thus furthering its dominant position and further influencing the shape of integration.

In reference to the Western hemisphere, Mattli considers both NAFTA and MERCOSUR as successful integration schemes, with the United States and Brazil as their respective regional economic powers. However, he concedes that the presence of *two* such powers within the same integration project will *create*, rather than resolve, coordination problems within the group (1999: 57). Mattli’s analysis of the FTAA process is that Latin America would need to accept the U.S.’s terms as set out in the NAFTA model (1999: 163). As is clearly the case, this is not what is taking place.

The contribution made to scholarship by Mattli was to identify both the economic and political conditions inherent in regional integration schemes. In contrast to Mattli's causality, Mansfield and Milner (1999) hold that PTAs are effective ways for *governments* to institutionalize contested domestic economic reforms and some businesses may benefit as a *consequence*.⁸

2.1.4 *The New Wave of Regionalism – Mansfield and Milner (1999)*

Mansfield and Milner's overview of relevant literature points out that much of the existing research on regionalism focuses on the economic implications of preferential trading arrangements, neglecting the study of how political conditions shape regionalism (1999: 589). They note that recent burgeoning studies, of which Mattli's can be included, shed new light on how political factors affect and guide the regional integration process. Formerly a rather neglected approach, Mansfield and Milner argue that political conditions, such as domestic and international politics, are central to explaining why trade blocs occur. Moreover, their argument also includes the observation that the political underpinnings of regionalism explain variations within regional schemes.

While recent research has begun to broach the role played by political actors at the domestic and international levels, Mansfield and Milner claim that various key theoretical and empirical issues remain unresolved, including which political factors bear most heavily on regionalism and the nature of their effects. While it is frequently acknowledged that political factors shape regionalism, surprisingly few systematic attempts have been made to address exactly which ones most heavily influence why states choose to pursue regional trade strategies and the precise nature of their effects.

Mansfield and Milner (1999: 600) thus set up the framework for further study in the field, that of distinguishing between politically-induced regionalism and regionalism stemming primarily from economic forces. While Mattli considers both the economic and political forces in regional integration processes, his argument is that it is first and foremost the demand of the business community that stimulates a response from the political community. What Mansfield and Milner argue is that regional integration schemes can also be the outcome of political decisions.

These authors identify various elements of regional trade strategies that hold some appeal for public officials who need to, for example, attract the support of both import-competing and export-oriented sectors or to liberalize trade when faced with domestic obstacles to reducing trade barriers on a unilateral or multilateral basis (1999: 603). Indeed, using group membership within a regional scheme to stimulate economic and political reform is a key feature of recent regionalism.

Mansfield and Milner underline the fact that in the final analysis, it is politicians that make the decision to enter a PTA (1999: 604). Business communities can reclaim regional institutions to help externalize trade costs, but it is the preference of policy makers and the nature of domestic institutions that condition the economic integration process and directly affect whether states elect to embark on such initiatives.

2.2 Limits of the Relevant Literature

Scholarship has put forward that collective action in groups is problematic and that it is exponentially so the larger the group is. Large n groups can be helped towards action when there is a privileged group or hegemon ready to assume the role of providing

the collective good through rules and regulation and acting as paymaster. However, this solution offered by the literature is the very problem for efforts to economically integrate the Western hemisphere. In other words, the solution of a regional economic power to spear the integration process becomes a problem in and of itself when there are two powers within the same large n scheme. The FTAA negotiations are stalled because the attempt to forge collective action among 34 member states is sought by two regional economic hegemonies simultaneously, the United States and Brazil.

In sum, theoretical literature recognizes that coordination problems would arise if two competing regional economic leaders belonged to the same group; consequently, the only solution it imagines to this conundrum is that one country is forced to cede to the other's foreign economic policy strategy. Beyond this, the presence of two hegemonies creates a practical problem for which scholarship does not account. We are not told what to expect in the case of the FTAA. Two templates for the expansion of integration in the Americas are presented: the U.S.-inspired NAFTA template and the MERCOSUR model favored by Brazil.⁹ As both regional economic powers have the willingness to realize their respective visions for the Western hemisphere, the question that arises is who can better substantiate it depends upon their relative political and economic *ability*.

2.3 Research Design

As has been explained, the focus of this thesis is to identify likely degrees of regional integration emerging out of the negotiating process between the United States and Brazil.¹⁰ Will the institutional framework of the agreement resemble that of a free

trade area based on the North American NAFTA model or will it resemble that of a customs union such as MERCOSUR, as is the pattern in South American?

The U.S.-Brazil standoff can best be understood within the framework of relational power, that is the power of A getting B to do something it would not otherwise have done. In the case of the Western hemisphere integration it is the capabilities of the regional power vis-à-vis other the other regional leader and other countries, and its ability to get them to do what they would not otherwise do. Within the concept of relational power, two dimensions are identified which will become the basis of the empirical research of this study, namely economic and political powers.

Economic power within this context can be understood as the power relationship between the trading nations. More specifically, it involves the volume and value of trade transiting between the countries as well as the nature of the goods traded, that is, whether the goods are agricultural or industrialized. As well as trade, flow of investment will be studied. This economic data will indicate levels of economic dependency directly between the two hegemon and between each hegemon and other major economic partners such as the rest of South American and Europe.

Political power will first be articulated around the different political cultures in the North and South America. It is the assumption of this study that the different political cultures affect the strength of the position that the two hegemon bring to the negotiating table. Two dimensions of this culture will be studied. Firstly, whether regional integration arises as an initiative of the political community or whether regionalism stems primarily from economic forces. Secondly, decision-making process will be studied, looking in particular at the key role of presidents in both domestic and foreign policy making.

This political procedure, it is argued, has an impact on the substance of the future PTA in that presidents in the Southern Cone come to the negotiating table with more unified position than do their Northern counterparts. As it is presidents who initiate and control the integration process, rather than it being driven by the private sector, Brazil has arguably a more united front than does the United States, whose position is compromised by competing sectoral interests, such as divided interests across agriculture and industry.

Secondly, the analytical framework of structural power will be used within the political context. Strange (Lawton et al, 2000) explains that structural power is the power to decide the rules of the game and the power to shape frameworks within which states relate to each other, to people and to corporate businesses. In the hemispheric negotiating process, the U.S. is using this power to negotiate bilateral free trade agreements with individual South American countries so as to isolate Brazil. Brazil, meanwhile, attempts to unite the Southern Cone through reinvigorating and expanding MERCOSUR and through the new South American bloc, the South American Community of Nations, in order to increase its bargaining power vis-à-vis the United States.

Brazil's goal is to negotiate a hemispheric agreement that will widen market access while securing measures that permit it to pursue developmental policies. The ability to do this hinges on Brazil's ability to rally the Southern Cone behind a united front at the negotiating table; a role facilitated by the hierarchical presidential political decision-making culture in South America (Phillips 2004). However, the U.S. might be able to divide the South by signing bilateral FTAs with individual countries, undermining Brazil's ability to rally its neighbors behind a unified front.

If Brazil manages to unite the South there will be important theoretical and practical ramifications for the free trade agreement of the Americas. Firstly, it will demonstrate that integration can be instigated by the political actors, more precisely presidential policy, and not by the domestic private sector as argued by Mattli (1999) – thereby questioning current literature on regional integration. Secondly, it will potentially change the power relations between the two hegemonies, giving Brazil political leverage vis-à-vis the United States.

2.4 Methodology

In order to get a handle on the question of what will be the degree of regional integration of the Americas, three dimensions need to be studied and assessed. These following three dimensions will be run through both political (qualitative measures) and economic (quantitative measures) frameworks.

1. The first information necessary to the analysis is establishing the relative economic and political roles of both hegemonies within their own PTAs. This verification serves to confirm that each hegemon is in fact the undisputed economic and political regional leaders of North and South America respectively. More specifically, establishing these respective roles will permit the equal treatment of Brazil and U.S. as regional leaders, therefore on a level playing field.
2. Next, the relationship between the two powers needs to be studied. An analysis of the political and economic relationships between the US and Brazil will serve to clarify lines of dependency and power. Their relationship will be scrutinized in

order to identify possible asymmetrical relationships that could possibly give either one political and/or leverage in the negotiations of the FTAA.

3. Finally, NAFTA and MERCOSUR must be situated in a larger regional and global context in order to identify other factors bearing on the political and economic leverage of either regional leader. Of importance to this study is the strengthening association between MERCOSUR and the European Union (EU), the proposition for a South American Community of Nations, and the bilateral agreements drawn up between the U.S. and South American countries such as Chile who signed a FTA agreement in 2002.

Measures

1. Qualitative Measures

- a) Firstly, the interests presented and defended by both Brazil and the U.S. respectively will be analyzed. Study of the negotiating groups within the FTAA forum as well as presidential statements and other relevant literature, will permit me to identify the goals put forward by the two regional powers.
- b) The decision-making process in South America will be examined. It is believed that South American international macroeconomic policy is heavily influenced by the decision-making culture of the Southern Cone states. Therefore, close attention will be given to the role of presidents and to national executives in the identification and elaboration of key foreign policies. Consequently, it will also be necessary to look at how stable are Brazilian and American positions domestically. Lastly, a brief survey of the

business sector-government nexus in both countries will allow me to discern leadership roles that have an impact on the regional integration process.

c) Next, decision-making between the two hegemonies will be scrutinized. Of interest here is the reinforcement of a bloc-based approach to negotiations in the South. More specifically, the relaunching of MERCOSUR and the latest project for a South American Common Market are believed to be part of Brazilian strategies vis-à-vis the United States. Conversely, U.S. strategies to divide the South by signing bilateral FTAs with individual countries, thus undermining Brazil's ability to rally its neighbors behind a unified front will also be studied and analyzed.

2. Quantitative Measures

A quantitative measure is used to determine economic integration and lines of dependency between the various actors identified in this study. The measurement is the ratio between foreign trade (exports plus imports) and gross domestic product (GDP). This indicator is useful in gaining a broad sense of trends in integration over time and reflecting the proportions of domestic output that compete in different foreign markets. A breakdown of trade relations between the different actors using this ratio will therefore serve as grounds to understanding political and economic power relations and how this influences FTAA negotiations.

Of interest to this research is the nature of goods that are being traded between the different actors. The types of goods have a bearing on long-term dependencies between countries arising through their terms of trade.

Recognizing the central development role played by investment in capitalist economies, foreign investment flows (FDI) will be measured. Once again, this will be done by looking at it as a ratio to GDP. It is equally important to identify the principal sources of investment in the different countries in order to see the lines of dependency between the key actors.

Trade and investment flows will be examined according to the three aforementioned aspects. That is:

a) Relations between the hegemon and their respective PTAs.

Brazil: Imports/GDP – Exports/GDP (overall) – within MERCOSUR – within SACN (MERCOSUR and Andean Community)

b) Relations the two regional hegemon themselves

Brazil: Imports/US – Exports/US – within NAFTA

US: Imports/Brazil – Exports/Brazil – within MERCOSUR – with SACN

c) Relations outside the PTA, between each hegemon and other relevant trading partners.

Brazil: Imports/EU – Exports/EU – with others

US: Imports/EU – Exports/EU – with others

This information will be gathered using data from the World Trade Organization (WTO), the International Monetary Fund (IMF), the United Nations Conference on Trade and development (UNCTAD) and the Economic Commission for Latin America (ECLAC).

For a more complete economic portrait, the population size will be taken into account, a per capita GDP being given. As well, information on the two hegemon's current accounts will be presented.

Process Tracing

Process tracing will be used for the economic data in order to permit the establishment of the chain of events that influenced the FTAA process. The cause-effect link between the IV and DV of this research paper will be divided into smaller steps, permitting the identification of observable evidence of each step (Van Evera 1997: 64). The time line for the analytical study of measurements will be from 1985 to 2005. This twenty-year period of data collection was chosen in order to trace trade flows prior to the creation of MERCOSUR in 1991 and NAFTA in 1994 so as to be able to ascertain the effects of regionalism on the export and import patterns in the Americas.

CHAPTER THREE: TRADE IS ALWAYS POLITICAL

3.1 The Regional Economic Integration Process

The U.S.'s and Brazil's preferences of the nature of the final hemispheric trade agreement are articulated, amongst other things, in terms of the level of integration desired among primarily two options, those of the first two degrees of integration between member countries of a trade agreement. In order to situate these two visions as put forward by the two hegemons, a brief overview of the integration process is presented.

The U.S.'s preferred option is to secure a regional trade agreement along the lines of NAFTA. This agreement is organized according to free trade area (FTA) principles, which corresponds to the lowest level of regional integration within a preferential trading arrangement (PTA). A FTA is a preferred option for countries wishing to engage in free trade while retaining high degrees of control at the national level. The FTA can also be limited to certain sectors. In FTAs, tariffs and other trade barriers are abolished while various customs duties imposed on third countries are preserved (Huelsemeyer 2004: 4). Rules of origin are an intrinsic element of FTAs. Rules of origin (ROO) are the criteria used to define where a product was made. ROO are an essential part of trade rules because a number of policies discriminate between exporting countries: quotas, preferential tariffs, anti-dumping actions, countervailing duty (charged to counter export subsidies), and specify the necessary requirements for each traded product to be treated as an FTA good. Rules of origin can also serve as a protectionist measure by allowing certain goods to avoid competition from imports.

The FTA template offers the U.S. a means to securing export markets while maintaining a high level of political sovereignty vis-à-vis the other PTA members.

Brazil's preferred option is a customs union (CU) that would follow similar structure to that of MERCOSUR. A CU eliminates rules of origin found in an FTA by establishing a common external tariff and joint quotas vis-à-vis third countries. As imports into the customs union area face the same tariff in each of the member countries, there is no incentive for importers to enter by the lowest external tariff, as is the case in an FTA; a common external tariff thus creates "destination neutrality" for imports into the area. The format of customs union is the preferred model of economic integration for developing nations as it protects manufacturing facilities that are being rescaled for larger markets and greater competition.

The other two levels are common markets and economic union. While not of direct relevance to this study, it is interesting to note that the Andean Community made a commitment to move to a common market by 2005. This represents the first step of deep economic integration by enabling the free flow of goods, services, financial capital and workers. Further regional integration offers the possibility of moving toward an economic union, of which the European Union is the only empirical case. The recently launched South American Community of Nations pronounced integration along the lines of the European Union. This would entail bringing harmonized fiscal, monetary, and labor market policies to the common market with the possibility of adopting a single currency, thus rendering the economic union more effective, removing uncertainty about exchange rates and reducing transactions costs.

This sequence of regional integration steps does not imply a deterministic process through all stages. However, this delineation does indicate a political and economic logic behind the sequence (Huelsemeyer 2004: 3). As well as representing different levels of integration, NAFTA and MERCOSUR, as the respective PTAs of the United States and Brazil, are two distinct models for integration. NAFTA represents a contractual approach based on legal dynamics, whereas MERCOSUR is a participatory approach based on political dynamics (Bernier and Roy 1999: 87). Further differences can be noted between the two models in their relation to their respective regions. The architecture of the NAFTA reflects a 'hub-spoke' arrangement, with the U.S. as the hub and Canada and Mexico as its spokes. MERCOSUR, on the other hand, reflects a 'spoke-spoke' regionalism common in South-South integration projects (Grugel in Phillips 2004: 87). While Brazil is considered the regional hegemon, it is itself a developing economy, thus aligning it on the same grounds as its principal economic partner in the trading bloc, Argentina, also a developing nation.

Each country has also different orders of priority for the issues to be negotiated. Whereas the USA has prioritized market access for goods and services, intellectual property and government procurement, Brazil/MERCOSUR's primary issues concern agricultural subsidies, dispute settlement and technical norms (Lima 1999: 140). The Brazilian government's position is that it is unacceptable to concede preferential access to its markets without receiving concessions for its competitive export sectors such as agriculture.

Negotiations to date suggest that there is little chance that such concessions would be made within the hemispheric agreement. Data from the NAFTA show that although

eliminating tariff barriers was a key component of the agreement, nontariff barriers (NTBs, such as restrictions based on claims of pest infection) and tariff-rate quotas (TRQ, which impose higher tariffs on products that have attained a certain threshold) are commonly applied by the USA to Mexican agricultural products (Clement et al. 1999: 264).

3.2 Rules Matter: Different Decision-making Cultures

As this chapter will demonstrate, a core problem of free trade is overcoming protectionist domestic interests. The ability to do so effectively depends on the national political culture of decision-making. Negotiators need mechanisms to overcome or override the tendency of concentrated interests. While both the United States and Brazil are presidential systems, there are important differences that impact significantly on their respective abilities to conclude free trade agreements.

The one institutional element omnipresent in the Southern Cone is the high profile of national presidents and the role of national executives in forming a minimum and flexible regional institutionalization (Malamud 2003: 63). Without wanting to over-generalize on the “hyperpresidentialism” of Southern Cone heads of states, presidents are indeed the major actors of regional policy and are the key instigators of regional integration schemes (Phillips 2004: 93). The promotion of Brazil’s vision of the FTAA is therefore facilitated through presidential diplomacy, i.e. the political summit diplomacy understood as being at the heart of decision-making in the South and the locomotive for regional integration.

The U.S. president does not have the same domestic leverage. Unlike in Brazil, Congress regulates foreign trade. The separation of the powers of the executive from the legislative and judicial functions undermines the president's negotiating position. While Congress grants the president special negotiating powers, these are frequently circumvented by powerful lobby groups.

This chapter therefore presents the United States and Brazil's strategies in light of their respective political cultures.

3.3 Stitching FTAs –The U.S.'s Path to Hemispheric Integration

From the beginning, NAFTA was not only seen as an end in itself but also as a stepping-stone to a Western Hemisphere Free Trade Area (Smith 2001:42).

U.S. Strategy

The United State's objective is the extension of its NAFTA base into a vast Free Trade Area of the Americas, incorporating all thirty-four countries from Canada in the far north to the tip of Chile in the south. In face of Brazilian resistance to this vision of hemispheric integration, Washington has adopted a strategy of divide and conquer, that is an incremental inclusion of the entire hemisphere into its trade model by targeting key countries, such as Chile, and smaller countries through sub-regional free trade agreements such as the Central American Free Trade Area (CAFTA). The U.S. is similarly targeting the nearby regional grouping of Caribbean islands, the Caribbean Community (CARICOM), which has long been one of Europe's own historic spheres of influence.

The motivations linked to such a free trade zone have undergone revision by Washington since the declaration of the Enterprise of the Americas Initiative by Bush senior in 1990. American economic foreign policy has moved progressively away from Washington's traditional support for the multilateral trade system towards bilateralism, reciprocity and regional arrangements as alternative frameworks (Clement et al. 1999; Mace and Bélanger 1999). Signing of free trade agreements, such as with Canada (Canada-US Free Trade Agreement CUSFTA) and with Israel, led to the establishment of the North American Free Trade Area (NAFTA) and paved the way for the idea of a free trade agreement of all of the Americas. President Bush reiterated at the 2004 Special Summit of the Americas in Monterrey that America is committed to free and fair trade in the hemisphere through the free trade area of the Americas and through the growing number of bilateral free trade agreements (U.S. Department of State 2004).

When the Bush Jr. Administration took office in 2001, "America was falling behind the rest of the world in pursuing trade agreements" (Allgeier, April 2005). Instead of sitting on the sidelines and ceding foreign markets to competitors, the Administration concluded bilateral free trade agreements with ten different countries, each one opening markets to United States exports. The latest, CAFTA-DR, is a free trade agreement with five Central American nations (Costa Rica, El Salvador, Guatemala, Honduras, and Nicaragua) and the Dominican Republic. As the US Trade Representative Portman stated after the passage of CAFTA-DR through Congress, "the drive to open markets for U.S. exports continues" (Portman 2005). Signing bilateral agreements based on the NAFTA model has become the preferred American strategy to obtaining an integration scheme of the Americas. After NAFTA's inception in 1994, the U.S. first signed an FTA with Chile

in 2002; the Office of the United States Trade Representative hopes to also negotiate agreements with the Andean and Caribbean Communities.

As the Deputy U.S. Trade Representative Allgeier explained at the 2004 Brazil Summit,¹¹ bilateral agreements with Central and South American countries are not just paths for bilateral trade liberalization with the United States, but are stepping-stones toward hemispheric integration. Allgeier (2004) relayed that this strategy came about because several countries, notably within MERCOSUR, were not in a position at this time to agree to such an ambitious and comprehensive package as the original FTAA project.

From the beginning, NAFTA was seen as a potential stepping-stone to a Western Hemisphere Free Trade Area (WHFTA) (Smith 2001: 42). Central to this strategy was Mexico's acceptance of NAFTA terms and conditions. Mexico's integration into the accord demonstrated the feasibility and desirability of developing nations to adhere to the NAFTA model and to all the regulations it implies (Clement et al. 1999: 259). Mexico became a concrete example of regional integration with the USA for other developing countries, particularly those in Latin America. Correspondingly, Chile, Argentina and Costa Rica rapidly expressed interest in joining NAFTA. While these countries did not join NAFTA per se, the vision of the FTAA as presented by the USA is one along the same lines as the North American agreement, offering a free trade zone stretching from Alaska to Tierra del Fuego.

Although the United States hopes to gain access to the large consumer markets and resources in a hemispheric agreement, geopolitical concerns have assumed greater importance since the adoption of the "Enlargement Doctrine" under President Clinton

(Smith in Mace and Bélanger 1999: 108). This doctrine aims at strengthening and fostering liberal democracies and market economies wherever possible (Lake in Mace and Bélanger 1999: 102). Within Latin America, the FTAA is seen as a way for the United States to apply its trade policy as a geopolitical tool.

Trade policy as a central policy lever has led the Administration to revise the wisdom of achieving the FTAA in a multilateral negotiation encompassing 34 countries. The U.S. views hemispheric negotiations in the large group as giving free rein to countries who would benefit from the outcome – the collective good, without having to comply to the economic and political reforms demanded by the United States with its bilateral trade partners (Bélanger 1999: 104). The expansion of MERCOSUR and the consolidation of Southern Cone through agreements between blocs and countries, along with the European Union's steady and powerful presence in the region, are elements increasingly considered to be undermining U.S. presence and interests in the region (Lima 1999: 143).

The U.S. project for the Americas is treated therefore as more than a hemispheric trading block, it is seen as the means to establish political and economic conditions in the region consistent and supportive of American policies and interests.

Through the integration of the Americas, the U.S. aims at establishing regional hegemony by linking key issues, trade and security, within an ideological framework. This framework encompasses values such as building “a prosperous, free and democratic hemisphere whose future prosperity hemisphere depends on shared commitment and drive to build democracy, security and market-based development” (Allgeier 2002). Recent remarks by U.S. Ambassador Noriega (2005), Assistant Secretary of State for the

Western Hemisphere, reinforce this position, “these trade agreements are about more than commerce: they are about breaking down entrenched interests, stigmatizing corruption, rewarding reforms that bolster competitiveness, and ensuring that particularly the very poor have the tools they need to claim their fair share of economic opportunity.”

According to the U.S. Administration, NAFTA’s success owes as much to the economic reforms and disciplines required by the agreement and enacted by the signing members as it does to the market access. This is one of the most important lessons of NAFTA that the United States aims at conserving within the proposed FTAA (Allgeier 2004). Signatories to a free trade agreement under this format will be required to adapt their domestic economic policies to a supranational model within a tight legal framework.

Treating Brazil as the leader of the “won’t do” countries after the breakdown of negotiations at the fifth World Trade Organization ministerial conference held in Cancún, Mexico in 2003, the United States Trade Representative, Robert B. Zoellick, warned that America could opt to strike bilateral deals with “can do” nations (*New York Times* 2003). This statement illustrates America’s decision to sub-divide the large n by signing bilateral FTAs with individual countries, or sub-regional blocs in Latin America.

Deputy U.S. Trade Representative Allgeier stated at the 2004 Brazil Summit in New York that, “it should not be too complex to stitch together bilateral accords signed independently and expand bilateral undertakings into plurilateral ones.” This strategy has the double goal of achieving integration through bilateral accords and of isolating Brazil who has developed its own strategy of subdividing the large n . It equally ensures that trade expansion through the implementation of a trade agreement will respect the NAFTA framework as the United State’s preferred integration model.

President and Congress: Not Always Seeing Eye to Eye

The president's ability to negotiate trade agreements is intimately linked to congressional approval via the so-called fast-track authority, now labeled Trade Promotion Authority (TPA). It was instituted in the early 1970s and enables the president to negotiate trade agreements that can only be approved or rejected as a whole, but not amended, by Congress. Yet, since trade agreements are comprised of a multitude of items, representing many vested interests defended by various lobby groups, fast-track authority is not easily forthcoming and is granted only for specified time periods. For instance, in 1997 Congress denied fast-track authority to President Clinton for his attempt to incorporate Chile into NAFTA.

Although it is in principle possible to pursue trade negotiations without TPA, this becomes very intractable if there is a need to change existing U.S. laws or levels of trade protection in any significant manner. In an ambitious scheme such as the integration of the Americas, where the negotiation of preferential market access is one of the controversial issues, a lack of presidential fast-track authority would immediately question any accord reached at the negotiating table (FOCAL 2002).

President Bush's fast-track authority was renewed in July 2005, but even then there can be considerable difficulty in getting trade agreements through Congress as the recent Central American-Dominican Republic Free Trade Agreement (CAFTA-DR) shows. In the U.S. Senate, legislators broadly focus their voting patterns on the concerns of constituents statewide. A Senate Finance Committee hearing on CAFTA demonstrated that the U.S. sugar lobby's influence made the vote in the Senate closer than expected (FOCAL 2005). In Congress, legislators kept specific constituent concerns in mind

making the vote on CAFTA in the House very close; it was passed on 28 July 2005 by a very narrow 217-215 vote.¹² The Administration needed to forge a cross-party alliance of supporters for the agreement, since the president could not rely on the majority of his own party. The passage of CAFTA-DR was seen as a minimal condition for the pursuit of further hemispheric negotiations; had Congress not approved this small trade agreement, there would have been little hope that it would be ready to pass a hemispheric trade treaty.

The growing ambivalence within the United States on issues affecting American relations with other countries and regional blocs, as evident with the CAFTA-DR, is being played out through a tug of war between the Administration and the influence of organized groups on their representatives in Congress (Tussie 1998: 90). Concerns of job loss are voiced readily in Congress (Scott and Ratner 2005) and they color legislative deliberations on U.S. trade policy and negotiations (Schott 2005). This is nothing new. Trade agreements are a source of major debate in Congress. Free trade creates anxiety in the American public who perceive potential job loss as being linked to the signing of free trade agreements. In tune to their constituents and the general public opinion, legislators are equally wary of voting in favor of trade agreements (FOCAL 2005).

This opinion is supported by arguments, such as the one put forward by the Economic Policy Institute (Scott and Ratner 2005), that expansion of NAFTA-style agreements, such as the DR-CAFTA and the FTAA, will displace production that could support more American jobs. The article states that the growth of the United States trade deficit with Mexico and Canada within the NAFTA caused a net decline in U.S. production, sacrificing about 1 million American jobs.

These cleavages within the domestic political arena are given free rein in the absence of a regionalist policy that is sufficiently consistent and integrated into its overall foreign policy for it to generate necessary support to rally Congress (Bélanger 1999: 97). As Mayer (1998:106) put it, domestic politics matters; the nature of institutions and interests in the domestic arena explains the difficulties in getting trade agreements through the legislative process.

3.4 Southern Unity – Brazil’s Leverage for Shaping the Hemisphere

Various Latin American countries, for example, established PTA over the past decade to improve their leverage in negotiations with the U.S. and NAFTA (Mansfield and Milner, 1999).

Brazilian Strategy

The economic strength of the North American advanced industrialized nations creates a situation of asymmetric interdependence with the less advanced South. These differences are articulated along the Brazil/MERCOSUR negotiating axis that promotes integration into the global economy along different lines than those put forward by the United States. The integration of the Americas into the U.S.’s preferred model would prevent the Southern Cone from putting into place an alternative economic framework of integration, a model of development for less developed countries. However, in the wake of the demise of the Cold War, South American countries have adopted a broad menu of strategic options to connect their countries to the global economy: unilateral liberalization, alignment with the U.S., sub regional integration and partnerships with major powers outside of the hemisphere (Smith 2001: 62). Brazil, as regional economic hegemon, uses this context to rally the Southern Cone countries around a vision of the

Americas that combines the necessity of hemispheric integration along the lines of the special needs of developing nations.

Lula de Silva, President of Brazil, reiterated to the Brazilian legislature in 2003 that the main attraction in the signing of a hemispheric agreement is the desire of greater participation in world trade and more particularly the possibility of preferential access to the most dynamic market in the world, the United States (Lula da Silva 2003). In spite of many of the setbacks encountered by Mexico, NAFTA bolstered both trade and investment in this developing country and this success is an incentive for Latin America to engage in economic integration (Clement et al. 1999: 294).

Brazil, however, does not intend to pursue trade agreements along the same lines as Mexico. President Lula de Silva (2003) stated that, “political lucidity obliges us not to be impressed merely by export opportunities, at the cost of losing sight of the bigger picture.” This bigger picture is the promotion of an economic and political model infused with a social democratic agenda (Phillips 2004: 74). In Brazil this is possible due to the relative success of import substitution industrialization (ISI), permitting the permeation of priorities and structures associated with developmentalism and industrialization into a ‘Brazilian model’ of neo-liberalism. Phillips adds (2004: 71) that this model was facilitated by an abundance of financial direct investment into Brazil during the 1990s. Neoliberal restructuring in Brazil, under President Fernando Henrique Cardoso (President of Brazil from 1994 to 2002), did not overthrow welfare provisions of the 1988 Constitution and the political executive maintained the central developmental role of the state within the economy. Lula upholds and promotes this adapted vision of economic liberalization; he sets this out clearly: “basically, what we want is a balanced FTAA that

guarantees us genuine access to the other markets in the hemisphere, and which at the same time allows us space for development-orientated policies” (Lula da Silva 2003).

In order to facilitate development-oriented policies Brazil argues that, “a free trade agreement needs to take into account the differences between the economies represented at the negotiating table” (Lula da Silva 2003). It clarified that its principal position towards the FTAA negotiations is that it is not reasonable to want identical rules and obligations for 34 countries with such different characteristics and in such different situations (Lula da Silva 2003). The NAFTA model proposed by the United States does not take into account these differences, treating all members as co-equal partners. ‘Special and differential treatment’, such as Mexico received as a developing country under the World Trade Organization (WTO) was lost under NAFTA (Clement et al. 1999: 273), and can be expected to be lost for the Southern countries under an FTAA.

As Lula da Silva emphasized (2003), issues that come up against opposition in the FTAA negotiations can be perhaps more readily resolved in the World Trade Organization forum where debate could be more effective and more democratic, and have many more different interests involved. This is particularly the case with agriculture where, as a major agriculture exporter, Brazil believes that gains can be made in the WTO. In line with its regional role as regional hegemon Brazil, along with other key emerging economies - China, India and South Africa, is assuming a leadership role within the Group of 20’s caucus involved in the Doha Round of the current trade negotiations of the WTO. The objective is to represent and defend its domestic needs alongside assuming the role of speaker for the countries of the Southern Cone.

Of the nine FTAA negotiating groups (market access; agriculture; government procurement; investment; competition policy; intellectual property rights; services; dispute settlement; as well as subsidies, antidumping, and countervailing duties), agriculture and market access are the cornerstones of MERCOSUR's vision of, and position in, the hemispheric negotiations.¹³ There is a consensus in the South that any FTAA must open the U.S. agricultural sector, that is to say that it must be genuinely "WTO-plus."

The U.S. government's response to the developmental differences between economies in the integration scheme has been to initiate a comprehensive trade capacity building program - the Hemisphere Cooperation Program, to help small and developing countries in the region benefit fully from the FTAA. The angle of this aid is to increase the capacity of the region's smaller and less developed countries to take part in the FTAA negotiations through technical assistance and training for government officials on issues such as customs facilitation and intellectual property rights protection. The program would also help these smaller nations to comply with their trade commitments within a hemispheric free trade area. This program, however, does not address disparities between economies. From the point of view of developing countries in the Southern Cone, this program is a far call from the European Regional Policy whose objective is to reduce the development gaps among the various regions.

The convergence of sub regional arrangements under American leadership along the lines of bilateral agreements is therefore an outcome that Brazil wishes to avoid in order to secure its own goals within a development framework. Central to Brazil's position is the desire to retain an important level of autonomy vis-à-vis the United States,

something sacrificed by Mexico when it joined NAFTA. This autonomy gives Brazil free rein for the maintenance of independent dialogue and negotiations within its region and internationally (Lima 1999: 147).

In sum, Brazil's strategy on hemispheric regional integration has not changed in any important way since the announcement of the Enterprise for the Americas Initiative, guaranteeing a unified position among MERCOSUR members so as to enhance its bargaining position vis-à-vis the U.S. and to expand that unification to the other Southern Cone members behind a united front (Lima 1999: 138).

Reinforcing MERCOSUR and Creating the SACN

The creation of MERCOSUR was a state-elite led process. It was national executives rather than legislators, government rather than business and elites rather than the population that instigated and pursued the integration process (Borrás and Kluth 2003: 223). Regional integration was used as a political tool by presidents to converge political and economic interests between Argentina and Brazil (Kaltenthaler and Mora 2002). In this respect, integration through the MERCOSUR was not a neo-functionalist institutional response to greater economic integration and greater trade interdependency, rather elites created a condition of economic independence in order to reduce rivalry between Brazil and MERCOSUR (Kaltenthaler and Mora 2002: 83). Not only a means of implementing neo-liberal domestic policies at the domestic level, MERCOSUR was in and of itself a trading bloc that was committed to liberalizing trade in the mode of open regionalism (Hester and Beaulieu 2003). MERCOSUR facilitated reforms on two levels: domestically, as a means of implementing sensitive economic domestic reforms that may

not have been possible unilaterally and, regionally, as a move away from import substitute industrialization (ISI) to the creation of 'open' regional blocs along the lines of freer trade and liberalization.

This model of integration developed at the subregional level, that is one initiated by the political executives, serves as the basis for further hemispheric integration, both at the regional level with the creation of the SACN as well as the project of hemispheric integration for all the Americas. Brazil seeks to use MERCOSUR to lever its power and project itself as a regional leader. This position was first assumed under the presidency of Fernando Henrique Cardoso and is being reinforced under Lula de Silva.

Therefore, on the tails of creating closer ties with Argentina, cooperation with other countries of the Southern Cone became a priority in Brazilian foreign policy. Philips (2003: 120-125) maintains that a major reason for assuring the longevity of MERCOSUR by its members was precisely to secure its role as a negotiating bloc within the FTAA, and Brazil adopted the so-called "4+1 negotiations," i.e. between MERCOSUR and the U.S. (Lorenzo and Osmani 2003). Securing the 4+1 formula of negotiations (Brazil, Argentina, Paraguay, Uruguay and U.S.) was a significant gain for Brazil as it is a determining element for the definition of integration of the Americas (Lima 1999: 136). The reinvigoration of MERCOSUR in mid-2000 aimed both at strengthening the ties between the four permanent members of the trading bloc as well as at expanding its associate member base across the continent (Phillips 2003:14). This reinvigoration was an essential step for Brazil in its securing its regional influence through the trading bloc and in securing its strategic objective of co-chairing the FTAA process through the MERCOSUR

To further underline its foreign policy goals within the hemisphere, Brazil has therefore worked at expanding the membership of MERCOSUR and being instrumental in creating the South American Community of Nations, signed by the presidents and representatives of its twelve member states in Peru on December 9, 2004. This new regional bloc has been built by dovetailing the existing two major trading agreements in the Southern Cone, namely the MERCOSUR and the CAN (Andean Community) along with Chile, Guyana and Suriname. While this scheme sets out plans for economic integration, it is essentially a political project. Most decisive in this regional process is the political will that must take precedence, political and diplomatic coordination are the priority areas of action.

In contrast to MERCOSUR's geographical widening, the creation of the SACN aims at deepening the institutionalization of a South American bloc. Its promoters, Presidents Lula of Brazil, Nester of Argentina, and Toledo of Peru compare the SACN to the European Union. At the first meeting of heads of state of the SACN in Brasilia on 30 September 2005, the attendees stressed as its essence the social and economic integration of the peoples of South America (Marquez 2004; Andean Community General Secretariat 2005). The scheme has a long term view of establishing common government and currency along with the four fundamental freedoms associated with deep regional integration: free movement of goods, services, capital and people. It is supposed to culminate in the establishment of a joint central bank, currency, passport, and parliament by 2019. As such, the SACN is essentially a political project, intended to further strengthen the South's collective bargaining power vis-à-vis the United States (Weiss 2004).

This project is being achieved by building on shared 'state ideals' within the Southern Cone (Borrás and Kluth 2003). These ideals constitute the basis for the formation and articulation of 'regional ideals', which are the cognitive parameters decided by national elites (Borrás and Kluth 2003: 211). Shared regional ideals can be seen in the shared macro-economic co-operation in terms of exchange rate stability between the region's two largest nations, Brazil and Argentina, which is at the heart of the MERCOSUR (Borrás and Kluth 2003: 217).¹⁴ Along the lines presented by these authors, there are state ideals shared by Argentine and Brazilian elites which have become the cognitive outline for the new SACN. The first is economic; sound public finances, free trade and monetary stability. The second is political; that of democratic government which, according to the statement made by the Andean Community Secretary General Wagner (Andean Community 2005), will be enriched through the integration process which aims to be socially inclusive.

The reinforced MERCOSUR is articulated explicitly as the template for South American integration, the two projects contributing to the management of American hegemony (Phillips 2003: 126). As former Argentine president Eduardo Duhalde explained on the launching of the SACN, "our countries cannot face alone the challenges of the new economic and political world order" (BBC 2004a). The high profile of national presidents and the role of national executives in forming a minimum and flexible regional institutionalization is an important institutional element facilitating this process. Malamud (2003) explains that this outstanding characteristic kept MERCOSUR from stalling and has been decisive in these new developments of regional integration.

In order to facilitate this policy, Brazil has adopted a strategy of “pacing and hedging” that accommodates its preference for slower integration, thus ensuring its foreign policy goals (Guedes da Costa 2001). It not only provides time for Brazil to adjust to the economic levels of its key partners (Guedes da Costa 2001: 107; Lima 1999: 142), this strategy also gives it the necessary time to attempt to unify the Southern Cone into a single negotiating bloc.

At the national level, changes brought about within the government facilitated the president’s control on trade-policy negotiation. Lula da Silva centralized trade policy negotiations within the Ministry of External Relations (the *Itamaraty*), moving this ministry to the center of trade-policy making in Brazil and more directly under his supervision. By doing this, Lula assured that he would be able to circumvent power struggles occurring within the government. The *Itamaraty* created the *Secretariat Nacional da ALCA – SENALCA* (National FTAA Secretariat), which grouped representatives from other ministries and government agencies, as well as representatives from civil society (Maroconini 2005: 8). The FTAA thus gave an occasion to the Brazilian executive to overhaul its trade-policy-making culture, bringing it closer to presidential power.

The inclusion of members of civil society into the trade policy-making process, via their participation in SENALCA, was one of the factors that have led the diverse socioeconomic groups in Brazil to generally support the Brazilian government’s position on the prospective FTAA. The nineties witnessed a broadening of the participation by civil-society in trade matters. The Lula government ensured as well the presence of “social” ministries and agencies in the SENALCA and other national forums on trade

negotiations contributed to reducing public resistance to free trade agreements (Maroconini 2005: 9).

Moreover, this political-led integration process has been able to count on key support from the business community, which actively participated in shaping Brazil's negotiating position (Lima 1999:148). Institutional deficit, linked to a long tradition of power centralization during the years of authoritarian rule, created a dynamic whereby business addresses directly the core of decision-making power – the president, instead of passing through less reliable institutional channels (Malamud 2003: 64). The government set up the *Coalizao Empresarial Brasileira* (Brazilian Business Coalition, CEB), bringing together various sectors - agriculture, industrial and services, in order to facilitate a broader consensus on government positions (Maroconini 2005).

Consequently, the Brazilian government can count as well on the general support of the Brazilian political elite who accepts that the country is in a period of transformation at the global level, with a view to its major trading partners (Guedes da Costa 2001:94). Importantly, the private sector, including MERCOSUR businesses, supports the idea of a gradual pace for negotiations as it permits them to adjust more smoothly to a more competitive economic environment.

Brazil's Allies: Steadfastness Not Guaranteed

A possible cleavage in South American countries' vision is the question as to whether the various states would be better served within a free trade area or a customs union.¹⁵ After Chile had signed an FTA with the U.S. in 2002, some Argentine leaders made no secret of their preference for a bilateral trade pact with the United States

(*International Herald Tribune* 2002). While not a concern in the Southern Cone at present, negotiating bilateral agreements with the United States remains a trade option for Latin American countries whose dependence on the American market is substantial (cf. the CATFA-DR). While this does not seem to be the present tendency, it appears that drawing up bilateral agreements with the United States remains a feasible and interesting trade option for many Latin American countries. A significant increase in bilateral agreements and closer economic relations with the United States could possibly undermine the negotiating power of a South American bloc. Thus, the challenge for Brazil is reckoning its relative economic strength vis-à-vis America.

3.5 Relational Political Power

Political power has been articulated around the different political cultures in the United States and Brazil. The different political cultures of these two regional economic powers impact on their capacity to shape the integration of the Western hemisphere as they play an important role in supporting or undermining the positions that the two hegemons bring to the negotiating table.

This political procedure, it is argued, has an impact on the substance of the future scheme. The regional hegemon that is procedurally more successful in subdividing the group size will equally determine the nature of the regional scheme.

The empirical evidence in this section points to the necessity in evaluating the different political culture of members of an integration scheme. While the president of the United States plays a key leadership role, in collaboration with the USTR, in negotiating trade agreements, this chapter has demonstrated that this leadership is undermined by sectoral interests, such as divided interests across agriculture and industry, and interest

groups such as environmental and human rights groups. Analysis of job loss through trade agreements with less developed countries has further entrenched the polemic nature of the debates. The convergence of diverging interests, first in the USTR and later through representation in Congress, has therefore intensified polarization of politics in the United States. The House of Representatives has become an obstacle for free trade agreements and the U.S. president cannot be sure, in spite of TPA, of getting new agreements ratified by the legislation.

Review of the present chapter leads me to argue that presidents in the Southern Cone come to the hemispheric negotiating table with more unified national position than does their Northern counterpart. The hierarchical presidential political decision-making culture in South America, which is supported by the private sector through a history of working closely with the executive, affords Brazil a centralized negotiating agenda. The U.S. president has to contend with a national political culture that undermines his bargaining position. Contrary to Mattli's logic of regional integration and in support of Mansfield and Milner's argument that regional integration schemes can also be the outcome of political decisions, it appears that regional integration projects, such as the recently adopted SACN, can be politically induced.

CHAPTER FOUR: THE ECONOMIC MEANS FOR THE POLITICAL PROJECT

Trade patterns in the Americas over the last forty years reveal that there are two main axes to which countries in the North and South converge respectively (Mace and Bélanger 1999: 245). In the North, Canada, Mexico and Central America coalesce around the United States. Canada and Mexico are linked to U.S. trade under NAFTA and the recent adoption by the United States Congress of a free trade agreement with Central America will bring these countries further into the American economic orbit. In the South, there is an increasing concentration of trade around the Brazil/Argentina axis, notably since the creation of MERCOSUR.

This chapter looks at these economic dynamics, tracing trade and foreign direct investment flows. A breakdown of trade relations between the regional powers and other significant trading partners serve as grounds to understanding the economic power relations and how this affects the U.S. and Brazil's political project to sub-divide the large *n*.

4.1 The U.S.'s Relative Economic Strength

General Overview

The United States has an absolute economic advantage over all the other individual countries in the hemisphere. Mace and Bélanger (1999: 42) contend that this dominant position is accentuated by a thirty-year power gap between it and the other countries of the region.¹⁶ The IMF indicated in its World Economic Outlook of September 2004 that global growth continues to be driven by the United States

(International Monetary Fund 2004: 1). Its Gross Domestic Product (GDP) totaled US\$10.4 trillion in 2002 (see Table 1), an output three times that of Japan, almost five times that of Germany and more than six times that of the UK. Its GDP per capita of US\$39,900 is significantly higher in comparison to other developed countries as well. The American annual GDP growth rate was 4.2 percent in 2004 and fell to 3.5 percent in 2005. This drop reflected a downturn in inventory investment, a slowdown in consumer spending, and a curbing in federal government spending (Bureau of Economic Analysis 2006).

Table 1: Basic Economic Indicators for the U.S.

	GDP (billions US\$)	GDP per capita (US\$)	Exports (millions US\$)	Exports as % of GDP	Imports (millions US\$)	Imports as % of GDP	FDI inflows (millions US\$)	FDI inflow as % of GDP	Population (millions)
1985	4,220.250	17,701	218,815	5.1	352,463	8.3	16,918	0.60	237,924
1990	5,803.075	23,207	393,592	6.7	516,987	8.9	48,422	0.83	249,464
1995	7,397.650	27,762	584,743	7.9	770,852	10.4	58,772	0.79	262,803
2000	9,816.975	34,774	781,125	7.9	1,259,300	12.8	314,007	3.1	282,192
2002	10,446.250	36,208	693,860	6.6	1,202,430	11.5	71,331	0.68	287,941

- N.B.** * Indicators specify the absolute numbers as current prices.
 * Exports (Imports) as % of GDP: calculated on basis of the IMF's World Economic Outlook GDP data and the WTO's total exports (imports) data
 * FDI Inflows as % of GDP: calculated on basis of UNCTAD's FDI data and the IMF's World Economic Outlook GDP data

Sources:

- * WTO <<http://stat.wto.org/StatisticalProgram/WSDBViewData.aspx?Language=E>> (accessed September 9, 2005)
 * UNCTAD Foreign Investment Database <<http://www.unctad.org/Templates/Page.asp?intItemID=3198&lang=1>> (accessed September 14, 2005)
 * IMF World Economic Outlook <<http://www.imf.org/external/pubs/ft/weo/2003/02/data/dbginim.cfm>> (accessed September 14, 2005)
-

The US market is highly competitive except for some light manufactures textiles, clothing, and footwear, and some agricultural sectors with high border barriers. Being an industrialized nation, agriculture accounts for a marginal share in the total national income.

On the downside, the American current account deficit has continued to deteriorate over the past year. The United States' international deficit in goods and services increased to US\$59 billion in August from US\$58 billion in July 2005, as imports increased more than exports (U.S. Census Bureau 2005). The IMF regards the simultaneous current account deficit of US\$59 billion as a key risk (International Monetary Fund 2004:12), as it has continued to increase over recent years. The high level of the American deficit in relation to exports is of interest within the context of U.S. ambitions of increased export market share in the Southern Cone.

U.S. Economic Ties with Brazil

The United States' statement in the 2004 World Trade Organization Policy Review of Brazil declared that years of expanding trade, capital flows and cross-border investment have greatly expanded the political and commercial ties between the two nations. This same issue statement recognizes that Brazil is one of the world's top trading countries that have "been flexing its muscles - and influence - as an exporter." However, in spite of being the largest economies in North and South America, respectively, two-way trade flows between the two countries are small in relation to trade with other partners (see Table 2).

U.S. trade with Brazil has increased by 38 percent in absolute terms over the last 15 years but the ratio of trade with Brazil as a total of American foreign trade remains at 1.52 percent (see Table 2). In this sense, Brazil is distinguished in the Southern Cone by the significantly lesser importance of the North American Market in its trade profile as compared to other countries of the region (Phillips 2003). Unique is also the composition of the two-way trade: 70 percent of American exports to Brazil and almost 75 percent of Brazilian exports to the United States are manufactured goods (Schott 2005).

U.S. Economic Ties with the "South"

The major part of United States' economic exchange occurs within NAFTA (see Table 2). In 1990, trade within NAFTA was worth US\$230 million, having grown to US\$578.6 million in 2002, an increase of 151 percent (ECLAC Badecel Database 2005). With the exception of Mexico, the United States has not had a strong economic interest in closer relations with its neighbors to the South (Corrales and Feinberg 1999).¹⁷ From the Latin American point of view, the U.S. is seen as the most attractive market, but also the one most prone to closure.

U.S. exports to South America have not been significant, never reaching the import levels registered from this region to the U.S. market. At the beginning of the 1990s, U.S. exports to MERCOSUR and the Andean Community (CAN) were close to US\$13 million, representing only 3.4 percent of its total exports (see Table 2). By 2002, this had climbed to almost US\$23 million, a mere 3.8 percent of American total exports. On the other hand, imports from these two trading blocs amounted to US\$26.4 million in 1990, having increased to US\$46.8 million by 2002, a growth of 77 percent (ECLAC

Badecel Database 2005). The economies in the South are therefore significantly more dependent on the U.S. than vice versa. Of note, however, is that more than one-third of the nation's foreign oil purchases come from Latin America (Cardoso and Hills 2005).

Table 2: Foreign Trade Data for the U.S. to Selected Destinations (US\$ million, % of total trade and % of GDP)¹⁸

	Brazil	NAFTA	MERCOSUR (4)	ALADI	EU (15)
1985	10,665 (1.5%) (0.2%)	149,022 (21.2%) (3.5%)	14,831 (2.1%) (0.3%)	32,765 (4.6%) (0.7%)	116,816 (16.6%) (2.7%)
1990	13,461 (1.5%) (0.2%)	230,119 (25.7%) (3.9%)	16,918 (1.8%) (0.2%)	100,788 (11.2%) (1.7%)	201,148 (22.5%) (3.4%)
1995	20,184 (1.5%) (0.2%)	369,161 (28.0%) (4.9%)	27,585 (2.0%) (0.3%)	171,089 (12.9%) (2.31%)	253,139 (19.2%) (3.4%)
2000	28,635 (1.4%) (0.2%)	626,143 (31.7%) (6.3%)	37,523 (1.9%) (0.3%)	325,576 (16.5%) (3.31%)	379,564 (19.2%) (3.8%)
2002	27,928 (1.5%) (0.2%)	578,662 (31.%) (5.5%)	33,708 (1.8%) (0.3%)	299,612 (16.3%) (2.8%)	365,035 (19.9%) (3.4%)

N.B. * U.S. Export data with Bolivia (CAN and ALADI) as well as Cuba (ALADI) not available for 1985

Sources:

* 1985: U.S. Census Bureau Foreign Trade Statistics <<http://www.census.gov/foreign-trade/balance/c2010.html#1985>> (accessed October 6, 2005)

* 1990-2002 ECLAC: Base de Datos de Comercio Exterior BADECEL <<http://www.eclac.cl/badecel/default.asp>> (accessed September 14, 2005)

United States foreign direct investment in Latin American countries has been increasing in recent years in response to political and economic reforms. The value of U.S. investment in the three largest Southern Cone countries: Argentina, Brazil, and Chile, approaches the value of that in Spain, France, and Italy. U.S. foreign direct

investment in Latin America has averaged some US\$12 billion per year (Cardoso and Hills 2005) over the past decade.

The health of the American economy increasingly depends on foreign markets. The record current account deficit necessitates either reducing imports or increasing exports. In this context, Latin America has become a valuable target for U.S. exports. Firstly, the Southern Cone represents a potential market of over 350 million people. This figure is significant as the region is considered an important emerging locomotive for the world economy (Muñoz 2001: 80-1).

U.S. Economic Ties with the European Union

After NAFTA, the European Union is the United States' most important trading partner (see Table 2). In 1990, trade with the EU was worth US\$201 million, having grown to US\$365 million by 2002, an increase of 81 percent (ECLAC Badecel Database 2005).¹⁹ The EU and the United States both account for around one fifth of each other's bilateral trade. This substantial amount, along with the significant levels of mutual investment (worth about one quarter of the economic transactions), illustrates a high degree of interdependence between the two economies. For the period of 1982 to 2002, European countries accounted for an average of 40 percent of total annual FDI inflows into U.S., while conversely the U.S. made up an average of 48 percent of total annual FDI inflows into the European Union (United Nations Conference on Trade and Development 2005).

Despite such economic integration and collaboration, a number of disputes blight this portrait. These include trade issues such as the banana and steel conflicts. In addition,

the EU and the United States are not only partners, but also rivals in the global market place. They have similar economies and domestic market size. They are also competing to establish privileged economic relationships with nations in the Southern Cone, thus ensuring increased market access for their respective exports. In this respect, the other's strategy in the region is of primordial interest to both America and the EU, especially in light of South American states attempt to diversify their dependence on the U.S., looking primarily to Western Europe.

4.2 Brazil's Relative Economic Strength

Brazil is pursuing its economic development goals in three ways. Firstly, Brazil is involved directly in the hemispheric negotiations for integration, but is actively promoting agreement and integration in the Southern Cone, through the reinforcement of MERCOSUR and through the recent adoption of the SACN. Secondly, Brazil is pursuing negotiations, alongside other members of MERCOSUR, for a trade agreement with the European Union. Lastly, Brazil maintains an active presence in multilateral trade forums such as the WTO where larger membership prevents the adoption of more restrictive trade rules (Lima 1999: 145).

General Overview

Studying Brazil's current economy requires placing it in the context of its recent transition, as with other South American economies, from the inward-looking development model of import substitute industrialization (ISI) to adoption of outward-looking neoliberal economic policies. The crisis of the closed and state-led economic

model in the 1980s led South American countries to converge and adopt an open market-led economic model. Like other Southern Cone countries, Brazil has incorporated the priorities and structures associated with developmentalism and industrialization elaborated under the ISI model. These priorities coexist with the neoliberal model, creating a South American version of neoliberalism (Phillips 2004: 70).

In Brazil, this version has been possible due to the fact that it has received important external financing, thereby reducing the fiscal constraints imposed on the government and gave it a freer rein (Phillips 2004: 71). This is not to say that neoliberalism did not gain a firm footing in Brazil. Phillips (2004) explains that policies were slower to emerge and take root in Brazil than elsewhere in the region. This has permitted the Brazilian government to promote developmental goals as the basis for its participation in the hemispheric scheme.

Brazil's economy is showing signs that it is the strongest it has been for many years, having made a dramatic turnaround since the early 1990s (Dos Santos 2005). Macroeconomic policies conducted throughout the last ten years are resulting in a current account surplus, the seventh largest in the world in 2004 (ECLAC 2005). Brazil is reaping the benefits of macroeconomic consolidation, underpinned by a prudent policy stance and the strengthening of institutions for macroeconomic policymaking. The OECD 2005 Report remarks that the current account surplus is due to robust export growth rather than a compression of imports, indicating a vibrant economy instead of prudent protectionist policies.

Brazil is South America's leading foreign direct investment recipient and it is one of the leading recipients of foreign direct investment (FDI) among all developing

economies (ECLAC 2005: 74). Brazil's annual average FDI inflow for 1999-2002 was US\$25 billion as compared to, for the same period, Argentina's US\$9 billion, Chile's US\$4.5 billion, and Venezuela's US\$3 billion (UNCTAD 2005).

Table 3: Basic Economic Indicators for Brazil

	GDP (billions US\$)	GDP per capita (US\$)	Exports (millions US\$)	Exports as % of GDP	Imports (millions US\$)	Imports as % of GDP	FDI inflows (millions US\$)	FDI inflow as % of GDP	Population (millions)
1985	231.757	1,709	25,639	11.0	14,332	6.1	1,441	0.62	132,999
1990	465.004	3,091	31,414	6.7	22,524	4.8	989	0.21	146,592
1995	703.961	4,290	46,506	6.6	53,783	7.6	4,405	0.62	158,874
2000	599.811	3,604	55,086	9.1	58,631	9.7	32,779	5.4	171,279
2002	460.533	2,589	60,362	13.1	49,603	10.7	16,590	3.6	176,391

N.B. * Indicators specify the absolute numbers as current prices.
 * Exports (Imports) as % of GDP: calculated on basis of the IMF's World Economic Outlook GDP data and the WTO's total exports (imports) data
 * FDI Inflows as % of GDP: calculated on basis of UNCTAD's FDI data and the IMF's World Economic Outlook GDP data

Sources:

* WTO <<http://stat.wto.org/StatisticalProgram/WSDBViewData.aspx?Language=E>> (accessed September 9, 2005)

* UNCTAD Foreign Investment Database
 <<http://www.unctad.org/Templates/Page.asp?intItemID=3198&lang=1>> (accessed September 14, 2005)

* IMF World Economic Outlook
 <<http://www.imf.org/external/pubs/ft/weo/2003/02/data/dbginim.cfm>> (accessed September 14, 2005)

The increase in inflows from annual averages of US\$1 billion between 1985 and 1990 to an average of US\$15.7 billion for the second half of the 1990s, culminating in an all time high of FDI inflows with US\$32 billion in 2000, demonstrates the effectiveness of macroeconomic policies and the attraction of Brazil for investors (see Table 3).

Although having decreased somewhat at the beginning of this decade, FDI inflows were on the rise once again in 2004 with an intake of US\$18.2 billion (ECLAC 2005).

Brazil's exports in the last two years have outpaced the growth of world exports (ECLAC 2005: 37); they have been increasing steadily from 6.7 percent of GDP in 1990 to 13.1 percent in 2002 (see Table 3). Foreign trade for 2005 reached new records. Total exports were valued at US\$118,309 billion, while overall imports were worth US\$73,545 billion, resulting in a trade surplus of US\$44,764 billion (Brazilian Ministry of Development, Industry, and International Trade 2006).

Signs of a strong domestic economy match this favorable trading profile. Growth of 5.2 percent in 2004, the highest for over a decade, created more than 1.5 million jobs in the formal sector. Its GDP of US\$789.3 billion for 2005 puts Brazil ahead of Mexico that has been the region's top economy since 2001 and which has a GDP of US\$758.1 billion (Latin Business Chronicle 2006a). It also demonstrates the gap between Brazil's economy and those of other leading Southern Cone economies: The 2005 GDP figures are for Argentina US\$177.3 billion, for Chile US\$100.7 billion, and for Venezuela US\$131.0 billion. In spite of a robust GDP, Brazil's 2005 GDP per capita ranked eighth after Chile US\$6,224, Venezuela US\$4,956, and Argentina US\$4,512 with a per capita of US\$4,297; Mexico ranked first with a GDP per capita of US\$7,183 (Latin Business Chronicle 2006b).

With respect to its sectors, Brazil ranks fourth worldwide in agro industry and agriculture, and this is one of the most dynamic sectors of its economy. Agriculture accounts for 10.2 percent of Brazil's GDP and employs 23 percent of the labor force (Agriculture and Agri-Food Canada 2005). Brazil is also the world's leading producer of

orange juice products and is the world's third largest producer of corn. One of the main recipients of FDI in Brazil is the food and beverage industry (Phillips 2004: 36). The country is itself one of the leading investors in agricultural research and development in South America. The ECLAC report (2005: 80) explains that the role played by foreign investors is changing the export potential of the Brazilian economy, even in more traditional resource sectors such as paper and pulp. These changes are shifting the export structure toward faster-growing non resource-based manufacture, an increase from 35.8 percent to 44.5 percent of total exports in 2004.

In spite of these new trends, Brazil remains vulnerable as a commodity exporter, a factor accentuated by the fact that one of the main recipient of foreign direct investment at the sectoral level in Brazil was in the food and beverage industry (ECLAC 2005: 36). While natural resources prices for certain goods remain high, those chiefly linked to mining and oil extraction, prices for agriculture have dropped in real terms.²⁰ For Brazil, this reality is aggravated by protectionist measures and subsidies of agricultural products within developed countries, creating barriers to their domestic markets.

This concentration in natural resources and more particularly in agricultural products influences Brazil's position at the hemispheric negotiating table where reduction to agricultural subsidies in North America, as well as an end to anti-dumping legislation, has become the locus of Brazilian interests.

Overall, the countries of the Western hemisphere play a leading role in Brazil's foreign trade. Approximately 40 percent of imports and exports result from commercial transactions with these countries. Among them, Brazil's commercial transactions are

highly concentrated in just a few countries, namely Argentina, Chile, Mexico, and especially the United States. These relations will now be examined.

Brazilian Economic Ties within MERCOSUR and the Southern Cone

The economic strength registered by MERCOSUR in the last years is an asset for Brazil in the context of hemispheric negotiations (Lima 1999: 148). Where in the 1980s Brazilian exports to the rest of South America averaged at under 10 percent of all exports, most trade being with the United States and the EU, this pattern changed in the mid-1990s. Trade between Brazil and the other MERCOSUR countries has been growing since 1990; in 1985, trade with MERCOSUR represented 4.2 percent of Brazil total trade and 0.7 percent of its GDP. This flow peaked in 2000 when trading with MERCOSUR was valued at over US\$15.9 billion (see Table 4).²¹ The exported goods were quite diversified, with an important share for middle and high intensive technology. Imports were composed primarily of agricultural products and middle intensive technological manufactured goods such as textiles and chemical products.

This economic trading bloc has been the model on which Brazil seeks to expand its economic influence to the rest of the Southern Cone.

While in 1985 Brazilian trade with rest of South America averaged at 9.8 percent of its overall trade and 1.7 percent of its GDP (commercial exchange was overwhelmingly with the United States and the European Union – see Table 4), this pattern changed in the mid-1990s after the founding of MERCOSUR in 1991. By the turn of the century, Brazil had substantially increased its trade with members of the Latin American Integration Association (ALADI).²² By 2002, trade represented 19.5 percent of

Brazil's international exchange, some 4.6 percent of its GDP. This translates into a growth of 98 percent of Brazil's trade within the region (ECLAC Badecel Database 2005). As the largest recipient of imports from the other countries within the region Brazil has substantial surpluses with several of its neighbors, among them Bolivia, Colombia, and Paraguay.

These data reveal two interrelated points. First, they demonstrate a significantly increased Brazilian presence within the region and, second, we see that while Brazilian trade with ALADI doubled since the 1980s and grew with the EU by 21 percent, trade with the United States actually decreased by 2 percent (see Table 4).²³ These trade flows and economic ties with the Southern Cone support Brazil's political projects of expanding the associated membership of MERCOSUR and of promoting the SACN.²⁴

Brazil's increased trade flows in the region are one dimension of Brazil's increased trade presence in the region; the other is the high percentage of Brazilian ownership in a new kind of company termed "trans-Latins." The 2004 ECLAC report (2005: 42) explains that these are Latin American companies that have acquired assets in other Latin American and Caribbean countries. Among them, 49 percent of the sales were made by Brazilian firms. Of the top ten firms in the region, six are Mexican, four are Brazilian; of the top twenty-five firms, nine are Brazilian. Brazil also hosts 400 of the 500 TNCs in the region because it is an attractive location for headquarters. Its size and proximity to other countries in the region make Brazil an excellent choice for setting up headquarters in South America, contributing to a perception of Brazil as being the major economic center for the region. This portrait demonstrates Brazil's economic regional

power, both as a trading center for the Southern Cone and as a source of FDI within the region.

The strategy of regional integration presented under Brazil's leadership is a more feasible option of integration into the global economy for Southern Cone countries for two reasons. First, only MERCOSUR, Chile and Mexico have attracted interest from the European Union to initiate trade agreements and only Chile, Mexico and Peru have gained membership in the Asia-Pacific Economic Cooperation (APEC) (Smith 2001: 63). Brazil's vision regional integration offers potential economic gains to all participating nations through increased free trade. Second, as opportunities are not evenly distributed across the region by key structural factors – geographic location, natural resources, demographic size, level of development, political structure and ability, Brazil's project offers benefits of a integration scheme without being confronted by the impacts of full blown global economic integration.

Brazil's Economic Ties with the U.S.

Brazil's trade pattern is echoed somewhat in international finance where the United States is by far the single most important country of origin for FDI in Brazil; the EU as a bloc is of equal importance as the United States.

Brazil's exports to U.S. have increased substantially in the last years: from US\$8.6 billion in 1995 to US\$13 billion in 2000, and to US\$15.3 billion in 2004; this reflects an increase from 2.9 percent of GDP to 3.3 percent in 2002. This growth in volume is not, however, an increase in the ratio of total exports to the United States; in fact, there has been a decrease from 26.7 percent of Brazil's total exports to 25.4 percent

in 2002. Imports reflect a similar profile, indicating however a relatively small increase in imports from the United States. In 1985, they represented 1.2 percent of Brazil's GDP, and 19.5 percent of its total imports. By 2002, imports rose to 21.5 of Brazilian total imports, some 2.3 percent of its GDP. This portrait shows a rather stable trading partnership, not demonstrating any of the significant Brazilian trade increases within the Southern Cone.

Brazil exports resource-based commodities such as orange-juice products, sugar and soy, manufactured articles such as shoes, textiles, steel, furniture and aeronautic production and automobile parts and software—product lines responsible for 75 percent of the nation's exports to the United States. While Brazil has a diversified industrial base, it is dependant on its exports of agricultural and mineral products. Brazil claims that American subsidies to its domestic producers put Brazilian exports at an unfair disadvantage.

Brazil's position within the hemispheric negotiations therefore is that taken into account that it has already opened its market considerably over the last decade; it is not in Brazil's interest to make further concessions with the USA without removal of key barriers in USA economy. The Brazilian authorities have expressed concern that an FTAA will not actually improve its access to the U.S. market as its competitive exports, agriculture, steel, and shoes, will likely to be continued to be penalized. The removal of these barriers is a necessary requirement preceding further opening of the Brazilian market to American exports (Lima 1999:148). These fears are based on American government policies that support domestic producers in certain domains. For example, in March 2005 the WTO ruled that U.S. support for cotton farmers was unfair. Brazil is

seeking permission from the WTO to increase duties on some American goods, should attempts at negotiating a solution fail (*BBC News* 2005). Recently, the United States administration announced safeguards to protect its domestic steel industry. While officials reserved 52 percent of the 5.4 million ton import quota on unfinished steel for Brazil, this is seen as a concession to Brazil in order to keep the FTAA discussions moving forward (Flynn 2002). Brazilian diplomats, on the other hand, contemplate invoking WTO rules and ask for compensatory duties on other Brazilian exports to the United States.

Table 4: Foreign Trade Data for Brazil to Selected Destinations (US\$ million, % of total trade and % of GDP)²⁵

	USA	MERCOSUR (4)	ALADI	EU (15)	China and Japan
1985	9,642 (24.1%) (4.1%)	1,701 (4.2%) (0.7%)	3,942 (9.8%) (1.7%)	9,529 (23.8%) (4.1%)	3,327 (8.3%) (1.4%)
1990	12,041 (22.3%) (2.5%)	3,762 (6.9%) (0.8%)	6,978 (12.9%) (1.5%)	15,046 (27.9%) (3.2%)	4,543 (8.4%) (0.9%)
1995	21,283 (21.2%) (3.0%)	13,432 (13.3%) (1.9%)	20,579 (20.5%) (2.9%)	27,892 (27.8%) (3.9%)	7,447 (7.4%) (1.0%)
2000	26,686 (23.4%) (4.4%)	15,912 (13.9%) (2.6%)	25,111 (22.0%) (4.1%)	29,475 (25.8%) (4.9%)	8,020 (7.0%) (1.3%)
2002	26,078 (23.6%) (5.6%)	9,218 (8.3%) (2.0%)	21,570 (19.5%) (4.6%)	31,770 (28.8%) (6.8%)	8,765 (7.9%) (1.9%)

Source:

* ECLAC: Base de Datos de Comercio Exterior BADECEL

<<http://www.eclac.cl/badecel/default.asp>> (accessed on 14 September 2005)

Although the United States is the single most important trading partner for and investor in Brazil, this predominance is qualified by Brazil's economic interaction with the EU and ALADI.

Brazilian Economic Ties with the European Union

The EU as a *region* (as opposed to the United States as a single country) is Brazil's main trading partner, receiving over a quarter of Brazil's external trade.²⁶ In September 2005, the European Commission met with MERCOSUR ministers to affirm the importance of their strategic relationship and renew their commitment to pursue negotiations for an Association Agreement aimed at establishing a comprehensive political and economic partnership between the two regions. The ambitious inter-regional Association Agreement is seen as an instrument to reinforce political, economic, and trade relations between the EU and MERCOSUR (European Union 2005a). It is intended to cover trade in goods, services, investment, intellectual property rights, government procurement, technical barriers to trade, and business facilitation. The last negotiating round took place in Brussels in July 2004 and talks are set to resume in early 2006. The following statement by Austria's former foreign minister in Sao Paulo is indicative of the EU's interest in staking out a privileged relationship with Brazil: "...an agreement (with MERCOSUR) would enhance the competitiveness of our economies, increase growth and thereby contribute to economic and social cohesion. It would also send a strong signal to the rest of the world about the strategic nature of our partnership" (Ferrero-Waldner 2005).²⁷

The relative importance of Brazilian foreign trade with the EU will increase with the expansion of this bloc's membership from 15 to 25. This latest development considerably increases the consumer base of the trading bloc, the population being at 456 million in 2003, making Brazil's trading relationship with the EU a central component of its foreign trade policy. Conversely, Brazil is the EU's main trading partner in Latin America and its 11th-ranked trading partner worldwide (Ferrero-Waldner 2005). Brazil is also an important destination for European investments in such diverse areas as telecom, energy, financial services, the automotive industry, the agro-industry, and the retail sector. Equally, Brazilian exports to the European Union comprise of a variety of product groups: inedible crude materials, except fuel (29 percent), food and live animals (28.9 percent), machinery and transport equipment (14.2 percent), manufactured goods (13.4 percent), and chemical products (4.3 percent) (European Union 2005b).

As well as important ties with the EU, Brazil's commercial ties with Japan and China are noteworthy. A 2004 visit by Japanese Prime Minister Junichiro Koizumi aimed at reinforcing these ties. Japan's Economy Ministry official stated that it was Japan's ambition to close an accord with Brazil in the next year "We don't want to miss out on Brazil, a country that already signed accords with the European Union and Free Trade Area of the Americas" (Washington Times 2004). Two years ago, China and Brazil entered into a bilateral trade partnership. While there have been certain difficulties encountered within this commercial relationship, for example when the world quota for textiles expired, China's booming market has been an important new destination for Brazilian exports of raw materials such as soybeans and iron ore. Total trade between the

two nations grew five-fold between 2000 and 2003 to a value of US\$8 billion (BBC News 2004b).

4.3 Analysis of Relational Economic Power

This chapter traced economic data between the regional powers and other key partners and trading blocs. These flows indicate, at first sight, clear levels of economic dependency between the U.S. and the South. The countries of the Southern Cone are dependant on the U.S. as both a market destination as a source of foreign direct investment. The economic relationship between Brazil and the United States clearly tilts power in favor of the U.S. This relationship, however, is offset by the European Union's presence in the Southern Cone. As well as fostering a close trading and investment relationship with Brazil, the EU's strategy is to undermine America's hegemony in the South.

As well as being offset by Europe's economic presence, U.S. hegemony is dampened through the increasing important economic relations between the countries themselves. The Brazil/Argentina axis, through the relaunching and reinforcing of MERCOSUR, has stimulated interregional trade and investment in the region. The Southern Cone, and MERCOSUR in particular, is very successful in attracting FDI into the region. The size of the domestic markets and the potential growth perspective in the consumer base is seen as an interesting investment market for other OECD countries than the U.S., particularly European countries. China and Japan, both key international economic actors, have shown recent interest in strengthening their economic relations with Brazil.

For these reasons, and in spite of a clear economic advantage held by the U.S., the dependency level of Brazil vis-à-vis the U.S. is mitigated by other countries' trade, investment and economic interest in the Southern Cone.

CHAPTER FIVE: CONCLUSION

At the first Summit of the Americas, in Miami in 1994, the region's 34 governments signed up to a common vision of free trade. That consensus started to erode by the third summit, Quebec 2001. At Mar del Plata 2005, the fourth summit, consensus has unraveled. While the plan for a Free Trade Area of the Americas has obviously stalled, new routes to hemispheric integration have started to emerge.

5.1 More than One Route to Integration

A review of relevant literature demonstrates that the FTAA presents a puzzle not accounted for by existing theories. The necessity of a hegemon as a response to large n group collective action problems is creating coordination problems in the case of an American hemispheric project. It is not clear whether the final collective good should be a NAFTA+ type of agreement, as wished for by the US, or a customs union along the lines of MERCOSUR, Brazil's desired option.

In spite of the limitation of existing literature to indicate the possible outcomes of this impasse there are, in principle, three scenarios that can be expected in this case.

1. That the negotiating process will come to a dead end and that there will be no FTAA. The United States and Brazil remain deadlocked. This might arise because the U.S. is unwilling to concede on key issues such as agriculture and Brazil is unable to rally the Southern Cone behind its negotiating position. Both parties find alternative trade agreements that, while less than optimal, offer viable alternatives.

2. That the hemispheric agreement is negotiated in the US's favor and is an agreement along the lines of NAFTA with no concession for Brazil's special interest such as agriculture. Brazil shows itself incapable, both politically and economically, of uniting the South behind its leadership. America manages to mold the hemispheric agreement by stitching up bilateral FTAs with Southern Cone nations. This is conventional wisdom.²⁸
3. Finally, hemispheric integration could be "deeper" than NAFTA, the united South behind Brazil managing, for example, to gain important concessions in the American agricultural market and/or EU-type structural funds to help address the North/South development gap. Brazil is able to rally the South behind a common political economic project, and reduce its dependence on the U.S. by reinforcing its alliances with the EU. The U.S. strategy, on the other hand, is seriously hampered by its domestic political culture, considerably reducing the president's ability to sign a FTAA.

There is, therefore, more than one route to Western hemispheric integration. The NAFTA model can be expanded by signing bilateral agreements with the United States, leaving the hegemon to 'stitch' together the different accords at the end, or the South American countries can accelerate their own processes of sub-regional integration, under Brazilian leadership, the groupings of which could then negotiate a trade agreement with the U.S. (Smith 2001: 44).

5.2 Evaluation of the U.S. Strategy

Power distribution in the Americas indicates that the United States enjoys clear economic advantage over the other members of the hemisphere. U.S. power has essentially remained unchanged over the past thirty years. The United States is the main commercial partner of the majority of countries in the Americas and within such circumstances it can be expected that future hemispheric integration reflects the interests and expectations of this country.

The American strategy permits it to pursue integration along lines of its own interest, establishing trade regulations that comply with a NAFTA-type model. It equally attempts to undermine Brazil's plan of rallying the Southern Cone around the alternative MERCOSUR model. Yet, while the United States would have the economic capacity to carry out a hemispheric project unilaterally and to mold the integration process, its domestic clout is less certain, for it depends upon getting trade agreements with lesser developed countries through Congress. Like the NAFTA debate (Huelsemeyer 2004) and the recent Central American-Dominican Republic Free Trade Agreement demonstrated, the legislative and political conditions for the pursuit of further hemispheric agreements would not necessarily be forthcoming.

The U.S. strategy is therefore hindered by its political culture of decision-making. In key initial years following the Miami Summit, President Clinton did not obtain fast-track authority and so had to water down the U.S.'s commitment to the process. This reduced America's hegemony in the integration process, watering down its preferred scenario of progressive and selective enlargement of NAFTA. The FTAA principles now

form a much heavier and more multilateral institutionalized format than the one initially foreseen by Washington (Bélanger 1999: 96).

The principal obstacle, therefore, is getting trade agreements, in particular with lesser-developed countries, through Congress. Polemic debates on the advantages of free trade agreements are likely to continue to be a hot topic for both the general American public and, consequently, in the U.S. Senate and Congress.

As well, American leadership and vision is contested in the Southern Cone where important political and economic differences exist with the developed North (Mace and Bélanger 1999: 243). In parallel, U.S. ambitions of integrating the Americas have reinforced Brazil's commitment to MERCOSUR and a greater emphasis on cooperative strategies within the region (Lima 1999: 137). A reinforced MERCOSUR, the consolidation of Southern Cone countries into a common bloc and the European Union's steady and powerful presence in the region further undermine American presence and interests in the region (Lima 1999: 143). Consequently, the United States is unable to act as sole hemispheric hegemon.

Lastly, even if the United States manages to implement its strategy, the widening of NAFTA template will eventually have to come across the challenge of its articulation with the MERCOSUR Zone. The problem of political connection between Brazil and the U.S. might be delayed by their actual two diverging strategies of hemispheric integration, but the problem of political connection will need to be resolved if the United States continues to enlarge its presence in the Southern Cone (Bélanger 1999: 108). In this sense, the "problem" of a powerful Brazil and a contesting hegemonic presence in the South, is unlikely to disappear. Brazil can significantly affect the capacity of the U.S.

government to advance its regional policy agenda. It is pursuing an independent and forceful foreign policy that does not mind clashing with Washington.

5.3 Evaluation of Brazil's Strategy

Conversely, Brazil's strategy to increase its bargaining power vis-à-vis the United States by dividing the large n through the creation of a united Southern Cone bloc depends upon its strong economic and political performance. This strategy appears supported by data that shows increased trade and economic ties with countries in the region. This economic portrait confirms Brazil's role as regional economic powerhouse, reinforcing its political leadership within the Southern Cone and its opposition vis-à-vis the United States. As well, the economic importance of the EU for both trade and FDI allows Brazil to mitigate the importance of the American market.

Brazil's political project of a united South depends on its capacity to continue to rally its neighbors around its foreign policy. The potential weaknesses of this strategy lie in the individual political economic strategies of neighboring countries. Brazil's strategy depends on careful timing in uniting the South while assuring economic liberalization in answer the developmental needs of other SACN member. Only if the SACN project comes through in real terms will Brazil be able hold the interest of the other members. The relaunching of MERCOSUR, the reinforcement of Brazil's relationship with Argentina, and the significant new ties with other key countries point to a strong political partnership that can possibly steer and implement this project. There is the danger, however, that countries will defect and sign an FTA with the United States who is able to deliver the economic advantages.

The continuing expansion of MERCOSUR, with the critical inclusion of Mexico in this project, further undermines the United States' influence in Latin America. The launching of the new geopolitical bloc, the SACN, has further cemented the commitment of the Southern Cone heads of state to unite in face of American hegemony. The political ambitions of this scheme mark a new stage in unification and cooperation between these countries. The success that Brazil has shown in uniting the region is aided by the European Union's presence in the region that seems to have as much interest in curbing the American role in the hemisphere as does Brazil itself.

5.4 What Future for the Western Hemisphere?

The research conducted in this study leads me to conclude that the first scenario is unlikely. Brazil's geographical diversification does not make the U.S. market irrelevant, and much less so for other Cone countries; Brazil's leadership role in the South hinges upon taking this into account. The U.S. cannot ignore the potential benefits of the emerging Southern Cone economies. The second scenario has become unrealistic because of American decision-making culture. Instead, this paper submits that the evidence makes the third scenario the primary candidate for the manner (both procedurally and substantively) in which hemispheric integration will tend to proceed. The likely ensuing substantial extension of the initial timeline works to advantage Brazil's effort to first break the FTAA group size into a Southern bloc.

The latest developments by Brazil and the Southern Cone are significant in light of the United States president's difficulty to pass the latest FTA agreement with Central America. Furthermore, the open timeline for hemispheric negotiations plays into the

hands of Brazil to pursue the unification and strengthening of the new South American negotiating bloc.

It appears plausible to envisage a reinforced South negotiating a free trade agreement with the U.S that goes beyond the NAFTA template. Another factor in the balance is the current Doha round of the WTO on issues relating to agriculture. If concessions by developed countries are made on agriculture and non-agricultural market access in the final agreement of the Doha Development Agenda, there is reason to believe that the U.S. will embark upon a renewed round of hemispheric negotiations on terms favorable to Brazil.

In this sense, the third scenario seems the most probable. Hemispheric integration will be “deeper” than NAFTA, the united South behind Brazil managing to gain important concessions in the U.S., amongst which that of access to the agricultural sector. In this vein, the United States has recently demonstrated new flexibility on issues important to Brazil, such as farm trade. In a speech to Brazilian leaders, Mr. Bush recently reiterated in the strongest terms an offer to make substantial cuts in agricultural tariffs (The Economist 2005).

5.5 Theoretical Implications of this Research

The project of regional integration of the Americas is relevant over and beyond its own future. This regional integration scheme raises two important theoretical issues.

Firstly, empirical evidence shown in this research demonstrates that integration can be instigated by political actors, more precisely presidential policy, and not solely by the domestic private sector as argued by Mattli (1999). The Southern Cone offers,

therefore, matter for expansion of theory on regional integration. This case points to the necessity to conduct further research on integration, particularly on the role of political actors as initiators of the process.

Second, in more general terms, the paper suggests that the large n problem of supranational organization is substantively “solved” by the regional hegemon that is procedurally more successful in subdividing the group size. Thus, beyond the hemisphere, this may imply lessons for other integration schemes where the large n problem recently emerged as a hindrance, namely the European Union after the addition of ten new countries in 2004 and the 53-member strong African Union.

This paper’s general proposition has been that, contrary to the literature, the larger the number of member states is, the more likely it is that this leads to more than one regional economic hegemon.

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Endnotes

¹ Its central feature is that the geographical “widening” and institutional “deepening” have both taken place simultaneously within the *same* PTA – slight name changes from EEC to EC to EU notwithstanding.

² Several other organizations exist in the Western hemisphere, among them the Organization of American States (OAS), the Latin American Integration Association (LAIA), and the Caribbean Community and Common Market (CARICOM). Yet, the former two do not qualify for definition as a PTA (see Mansfield and Milner 1999), while the political and economic importance of the latter is negligible.

³ This study is concerned with *regional economic* power and not global military power, where the USA stands alone as the international superpower. Thus, American hegemony in the latter is immaterial for our purposes.

⁴ Literature explains that success of integration is achieved through the implementation of a treaty, not just the signing of it, entailing establishing common rules, regulations and policies.

⁵ As an indication of the difference in economic development, it is interesting to note that the United States has a GDP equal to 75 percent of the total goods and services produced in the hemisphere.

⁶ In spite of extensive literature on regional schemes, the specific challenges arising within integration schemes between Northern developed nations and less developed or emerging nations from the South have not been systematically addressed.

⁷ The importance of this intermediate group within the new European context has diminished because of the new members. The European Union is confronted, along with the FTAA, now with the same issue of collective action problems within a large n group.

⁸ As we will see below, this appears to be the pattern in the Southern Cone, while Mattli’s regional logic corresponds more to the integration process seen within NAFTA.

⁹ Perales (2003:95) explains the choice of a customs union as the preferable institutional form of the MERCOSUR, for it offers stronger policy coordination leading to greater stability, i.e. allowing for stable predictions about trade policy behavior.

¹⁰ While this thesis starts with two questions - firstly, what is the likelihood of an American hemispheric regional scheme coming about and, secondly, what will the collective good look like-the research design logically concerns itself only with the second, taking the first as given.

¹¹ The Brazilian-American Chamber of Commerce event organized every year to coincide with spring meetings of the International Monetary Fund (IMF) and the World Bank.

¹² The CAFTA proponents had emphasized that about 80% of goods from these countries already enter the U.S. market duty-free, whereas the opening of their financial sectors would mean large opportunities for U.S. investors. By contrast, the opponents stressed the low labor standards in the Central American nations, thus worrying about American employment.

¹³ In addition to these negotiating groups, the FTAA talks contain four special committees of which the Technical Committee on Institutional Issues necessarily is the most important one, since it would reflect the substantive agreement, if it were to occur. (The other special committees are the consultative group on smaller economies; the committee of government representatives on the participation of civil society; as well as the joint government-private sector committee of experts on electronic commerce.)

¹⁴ Borrás and Kluth's argument is that inspite of the Brazilian and Argentine monetary crises within the last 10 years, both countries have adhered to shared ideals which has permitted the continuation of the Mercosur.

¹⁵ A free trade area removes barriers to the exchange of goods among the member states of the PTA, but all retain separate external tariffs toward third countries. To avoid that non-members seek the cheapest way of entry into the FTA and then transship goods within it, a free trade area requires elaborate rules of origin (ROOs); they determine the conditions under which a good qualifies as a good produced within the FTA. Third party merchandise is thus still subject to duties *between* the FTA members. However, ROOs are costly both for companies to prove and for the bureaucracy to administer. In a customs union, the members establish a common external tariff (even if only for specific sectors). The incentive for transshipment is thus nil, and ROOs can be eliminated. The crux for a CU is the agreement on the precise level of the joint customs regime (see Huelsemeyer 2004).

¹⁶ As an indication of the difference in economic development, the United States has a GDP equal to 75 percent of the total goods and services produced in the hemisphere.

¹⁷ One of the USA's principal interests in regional integration with Mexico is production sharing wherein Mexico serves as a link in manufacturing processes with USA firms, offering lower production costs (Fraser 2003).

¹⁸ Table 2 methodology. Percentage of total trade: foreign trade (exports plus imports) with selected destinations as a ratio of U.S.'s total world trade. Percentage of GDP: foreign trade (exports plus imports) with selected destinations as a ratio of U.S.'s annual GDP

¹⁹ The data are calculated for all years as EU (15), i.e. for the 15 member states that the Community had from 1995 to 2004, to make them comparable across time.

²⁰ According to UNCTAD (Least Developed Countries Report 2004: 126) comparisons of the prices of agricultural, raw materials, and food and beverages in 2003 with 1980 prices show a drop of 60 percent and 73 percent respectively.

²¹ While Brazil is the focus of this study, it is worth mentioning that there has been a general expansion of intra-Latin American trade which increased over 135 percent between 1986 and 1992 (Niam 1994 in Corrales and Feinberg 1999).

²² The ALADI is the largest Latin-American group of integration. It has 12 member countries: Argentina, Bolivia, Brazil, Chile, Colombia, Cuba, Ecuador, Mexico, Paraguay, Peru, Uruguay and Venezuela. This data was used for this study as it is the most comprehensive data for Brazilian trade in South America offered by ECLAC's database. It is clear that the ALADI grouping includes Cuba and Mexico, two countries that are not of direct interest to this study. The data does however give a clear indication of trade flows between Brazil and South America.

²³ While Brazil is the focus of this study, it is worth mentioning that there has been a general expansion of intra-Latin American trade that increased over 135 percent between 1986 and 1992 (Niam 1994 in Corrales and Feinberg 1999).

²⁴ While these data reflect Brazil's relationship within ALADI, the only major difference between the SACN and ALADI is that Mexico is not a member of the SACN. However, if the negotiations for full Mexican membership status within MERCOSUR come to fruition, there will effectively be common membership of the two blocs.

²⁵ Table 2 methodology. Percentage of total trade: foreign trade (exports plus imports) with selected destinations as a ratio of Brazil's total world trade. Percentage of GDP: foreign trade (exports plus imports) with selected destinations as a ratio of Brazil's annual GDP

²⁶ The relative importance of Brazilian foreign trade with the EU is likely to increase with the expansion of the bloc's membership from 15 to 25 as of May 2005, i.e. an expanded consumer base with a population of roughly 465 million.

²⁷ Apart from the EU, Brazil has geographically diversified its commercial ties further to include Japan and China. A 2004 visit by Japanese Prime Minister Junichiro Koizumi aimed at reinforcing these ties (*Washington Times* 2004). China has become an important new destination for Brazilian exports of raw materials such as soybeans and iron ore. Total trade between the two nations grew five-fold between 2000 and 2003 to a value of US\$8 billion (*BBC News* 2004).

²⁸ However, the failure of President Bush to convince his counterparts at the summit meeting of hemispheric leaders in the Argentinean resort Mar del Plata of a NAFTA-type FTAA underscores the doubtfulness of this scenario (Rohter and Bumiller 2005).