

# CEPAL

## Review

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# CEPAL

## Review

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## Introduction

# Latin America and integration: options in the crisis

*Guillermo Maldonado L. \**

While it is true that some of the causes of the present situation in Latin America are of external origin and that there is little possibility that Latin America will be able to change them, it is no less true that, if the region is to grow it must determine what action its members are ready to take together in order to increase their independence. This article's main argument is that Latin America must strengthen its arrangements for regional co-operation and integration and make better use of its own resources; ideas, projects and processes have been set in motion for this purpose and must be given real political support.

In addition, as an external reflection of what is being done within the region, negotiating power will have to be generated and wielded in the international arena in order to enable the region—and each of its countries—to participate on a more equitable basis in world trade and international negotiations, with a view to defending its legitimate interests.

Within this frame of reference, certain questions arise in the light of the present crisis: in what way and at what cost will Latin America come through this crucial decade of the 1980s? What should be the strategies of its future development in a world in which the comparative and absolute advantages of international trade will undergo profound change? What is the role and what are the prospects of regional co-operation in this difficult transition?

If correct answers are to be found for these and other questions, it will be necessary to monitor systematically the development of the international situation, to study the new technological trends which may emerge in the future development of the centres and their possible impact on the Latin American economy, to devise programmes to reduce the region's external vulnerability, to foster the processes of co-operation and integration among the Latin American countries, and to secure a unified Latin American position which will increase the region's negotiating power.

•Director of the Division of International Trade and Development of ECLAC. This article is a summary of documents prepared in the Division by the author and by Armando di Filippo, Eduardo Gana, Carlos Pérez del Castillo and Marianne Schaper.

The author of this article is convinced that a new international division of labour is becoming established as a result of the big technological changes taking place in the main industrialized countries, changes which are reflected in their production structure, in their relations with each other and in the consolidation of a system of international economic relations based once again on the exercise of power rather than on co-operation. The uncertainty, state of crisis and instability of the international financial, monetary and trade systems are also manifestations of the transition towards this division of labour and towards a system of international relations to sustain it. Just as it is high-technology services and activities which provide the driving force for the changes within the centres, it is the unilateral exercise of power and bilateralism which is increasingly replacing international co-operation and multilateralism in the relations among States.

The most serious problem is without a doubt the region's indebtedness. In order to service its debt, Latin America has become locked into a continuous process of adjustment to new circumstances which has not only prevented any growth in the majority of the economies of the region, but has also produced a per capita decline to the levels of 10 or 20 years ago.

In the 1980s Latin America has become a net exporter of capital to the developed world. A historical trend has thus been reversed, essentially as a result of the exorbitant rates of interest payable on the foreign debt. The larger part of the surpluses of foreign currencies have been obtained by cutting back imports and not expanding exports. This development has also been affected by the protectionist policies and practices of the industrialized countries and by the rapid deterioration in the terms of trade.

At the same time, at the end of the 1970s and the beginning of the 1980s, there was a vigorous return to democracy as a form of government and social order. This process has been hindered by the need to adopt austerity policies to service the foreign debt. The reduction of public expenditure, the freezing of wages and the runaway inflation have made the process of democratic consolidation more difficult, especially after the painful experience of life under au-

thoritarian régimes. These facts show how vulnerable the region is and how limited each country's room for manoeuvre in devising and applying economic policies to re-established the former rate of economic and social growth and distribute its fruits equitably. Nevertheless, and despite the continuing state of crisis, the democratic process has shown enormous vigour and has received great popular and institutional support.

Examination of the economic realities of Latin America and of political pronouncements and acts indicate that the situations confronting the countries of the region are difficult to bear. The countries are reaching the limits of social and political tolerance and a situation is emerging in which there could easily be an upsurge of violence, intolerance and polarization of positions. This atmosphere works against the application of policies designed to achieve economic growth on the basis of democratic consensus.

If Latin American is to resume its economic

and social development, it must secure, at least, a steady increase in exports; this means that the protectionist policies and practices of the industrialized countries which are affecting the region must be halted or moderated: the industrialized countries must accept a deficit in their trade with the Latin American nations. However, it is important to move away from the present ridiculous situation in which the region exports capital, and return to the situation in which Latin America receives a net inflow of financing. If this objective is to be attained, there will have to be more order in the macroeconomic policies of the industrialized countries responsible for the high interest rates and growth of protectionism.

The democratic process will also have to be consolidated: democracy must not be limited to the electoral process but must provide the legal, institutional and social framework within which the inequities which remain a feature of Latin American development can be eliminated.

## I

### The crisis in the international economic orders and its implications for Latin America

Five main arguments are analysed in this first section. First, that the system of international co-operation which emerged after the Second World War was a powerful factor in promoting and channeling the economic development of the capitalist world in the next twenty years. Second, that the activities of the economic co-operation institutions controlled by the big developed capitalist nations —such as IMF, the World Bank and GAIT— helped to consolidate an international division of labour based on the relationship between the centre and the periphery. Third, that this arrangement has been in a state of profound crisis since the 1970s when the long-term forces which imparted this dynamism became exhausted and the world economy grew increasingly sluggish and unbalanced. Fourth, that the present interregnum necessarily entails a deterioration in the institutional superstructure

of international co-operation and negotiation. And fifth, that a technological revolution has begun to grow and spread in the centres which will fundamentally change the international division of labour and, consequently, the structure of the centre-periphery system.

#### 1. *The organization of the international economic order and its effect on the periphery*

The system of international relations which emerged from the Second World War produced a wide network of political and economic institutions of a multilateral nature designed to direct and control the understanding among States. Never before in history had it been possible to construct such a universal and complex system of international bodies.

In this system some bodies play vital roles in

the Financial, monetary and trade operations of the developed world; for example, the World Bank, the International Monetary Fund and the General Agreement on Tariffs and Trade. The economic power of the big industrial centres is expressed through these institutions, and their functioning is affected both by the struggle among those Powers and by the way in which they exert their influence on the developing regions of the world.

In the promotion of development the assistance furnished by the World Bank usually took the form of tied loans, which helped the periphery to acquire basic infrastructure, but which were used for the purchase of goods and services supplied by the private companies of the central countries. Something like this happened in the case of several institutions, such as the Inter-American Development Bank and the International Development Agency, to name two institutions of special importance for the Latin American economies. The failure to establish preferential treatment for the Latin American suppliers of capital goods encouraged the massive acquisition of equipment from the centres. Development assistance was thus an ambivalent factor. On the one hand, it limited the independent technological development of the peripheral regions, thus impeding the proper expansion of their capital goods industries. On the other hand, it provided the essential infrastructure for Latin American development.

In the trade sphere, the General Agreement on Tariffs and Trade worked to establish uniform and equal treatment in tariff matters on the part of every country in its relations with all other countries. Its rules were based on manufactures where the comparative advantages were on the side of the centres, and they did not deal with primary commodities, where the comparative advantages were with the periphery.

Under the influence of the GATT rules the tariffs on trade in manufactures grew more liberal, but the centres granted high subsidies and strong protection to their domestic agriculture. In the 1960s—owing to the influence of the UNCTAD generalized system of preferences—part iv was added to GATT, providing for the possibility of preferential treatment for the developing countries.

From the end of the Second World War up to

the present time, as several EGLAC studies anticipated, the elasticity (prices and incomes) of the demand for manufactures in relation to the corresponding elasticity in the demand for primary commodities led to a systematic increase in the share of manufactures in the value of world trade. As the developing countries were exporters of primary commodities and importers of manufactured goods, their trade balances showed chronic deficits, with consequent indebtedness.

As a result of these basic imbalances, the world economic system and trade in particular—based on the principle of liberalization—did not bring about balanced and stable development but instead encouraged tendencies towards structural imbalance and inequitable distribution of the fruits of trade. Thus the need for co-operation proclaimed by UNCTAD on the basis of the ECLAC ideas.

In the monetary and financial sphere, these imbalances were controlled cyclically by the application of restrictive measures suggested to the deficit and debtor countries by the International Monetary Fund as a means of adjusting their external balances. Accordingly, the restriction of imports as part of the adjustments made necessary by the external imbalance had a negative influence on levels of activity and development prospects in the countries which depended on manufactures acquired from the centres. The strategy of industrialization by import substitution attempted by the majority of the large and medium-sized countries of Latin America was designed to produce self-centred development<sup>1</sup> which would reduce the vulnerability of the regional production structure to the fluctuations of international trade. This policy could not always be reconciled with the trade and financial openness advocated by GATT and the Bretton Woods institutions.

<sup>1</sup>Development tending to strengthen and diversify domestic production on the basis of national and regional demand. However, the Latin American production of capital goods was not included in the application of protectionist measures. In order to reduce the costs of industrial investments, imports of production equipment were freed from **all** restrictions and subsidized in many different ways. These policies did not foster the independence of regional development.

The liberalization of trade between the centres —after the reconstruction of Europe and Japan with United States help— was an efficient tool which boosted their economies and strengthened their mutual interdependence. It left the periphery in an unfavourable competitive position.

The economic events of the 1970s brought out more clearly the bias and shortcomings in the functioning of some of the institutions established in the postwar period. The official development assistance furnished by the World Bank, IDB and other intergovernmental organs declined in relative importance as financial privatization and transnationalization increased in the 1970s. The GATT rules and regulations are increasingly broken by the new forms of trade controls stemming from the need of the centres to protect their domestic levels of activity and employment. Similarly, the financial and trade difficulties of a more sluggish and less balanced world economy have changed the liquidity and balance-of-payments situations, lessening the usefulness and effectiveness of IMF, particularly in the management of the foreign debt. These problems damage international relations between centre and periphery.

## *2. The North-South negotiations in the framework of international co-operation*

The structural imbalances in the North-South relationship call for a new international economic order and reform of the institutional superstructure. Today more than ever before this new order advocated by the United Nations since the early 1970s is an essential condition for restoring harmonious development in the world economy and mitigating to some extent the dangerous consequences of world economic restructuring brought about by technological change.

However, the adoption by the United Nations General Assembly (on 1 May 1974) of the Declaration and Programme of Action on the Establishment of a New International Economic Order has been followed by more than 10 years of debate, consultations and negotiations among developed and developing countries in a multitude of forums both within and outside the United Nations system, with very discouraging results.

The objective of the developing countries, which became the central topic of the so-called North-South dialogue, was the establishment of a new and more equitable international framework of relations which would give them a greater say and more decision-making power in three closely interrelated areas: primary commodities, trade and monetary and financial matters.

The main aim for primary commodities is to achieve better conditions of access to the markets of the developed countries, greater participation by producers in marketing, distribution and transport systems, and an increase in the industrial processing of raw materials in the producer countries themselves. All these topics are still under study and no concrete measures have yet been adopted.

In the trade sector the developing countries wish to check and reverse the protectionist trends and make progress towards the liberalization of international trade. They are seeking to establish a set of rules and principles which will bring about a juster and more equitable trade system.

In the financial and monetary area the intention of the developing countries is to devise a new international monetary system which will meet their needs and give them a greater say in decisions affecting their interests. Faced with the increasing and serious shortage of financial flows, they are seeking an expansion of the resources available to the developing countries. These resources would come from international financial institutions by means of additional allocations of special drawing rights, an increase in IMF quotas and expansion of the compensatory financing service. None of these proposals has so far been accepted nor has any progress been made on the initiatives for reform of the international monetary system.

Although the developed countries approved the resolution on the establishment of a new international economic order, out of a desire to reach agreements which would bring some order to the energy products markets through price adjustments in the mid-1970s, they fell back in defense of the prevailing system, which they found a useful means of protecting their more immediate interests. Throughout the negotiating progress they maintained a sceptical attitude as to the competence of the United Nations

forums, advocating the full validity of the specialized forums such as GATT and IMF, in which they held advantages in relative power or voting rights. This helped to weaken the general framework of negotiation and no major agreements were reached for the transformation of the system of international economic relations.

### *3. The dynamics of the international economic system and its consequences for Latin America*

The accelerated growth of the world economy in the first decades after the war was due to the great dynamism of the industrial centres. This dynamism began to fade in the 1970s, yielding to the pressures of stagnation and deflation which became more acute at the end of the decade. Throughout this process the non-convertibility of the dollar, which came into effect in 1971, was an important innovation which highlighted the preponderance of a single country in the world monetary system.

The effects of this slowdown were not felt immediately in Latin America, partly because the financial freedom of the 1970s allowed the Latin American economies to continue to grow beyond the limits imposed by the purchasing power of their exports. In other words, the weaker locomotive power of the centres was offset to a large extent by abundant private financing of a transnational nature. The open trade policy of the United States from about 1975 also seems to have been a factor which stimulated imports to a level higher than the corresponding level of domestic economic activity.

The decline in the economic dynamism of the centres has profound structural causes—associated in part with the exhaustion of the postwar technological cycle—which have slowed down the rate of accumulation. The imbalance in the composition of global demand—excessive consumption and insufficient investment—together with energy and ecological restrictions on the supply side, helped to create the troubling conditions of "stagflation" which was a feature of the 1970s. It is a familiar story that, in order to overcome this situation, the United States applied a combination of monetarist and supply-side policies using the reduction of the money supply as its tool; it also went to the private financial market to fund its fiscal def-

icit and reduce the tax burden on the private sector in order to stimulate investment and consumption.

This policy resulted in a great reduction in inflationary pressures and a sharp domestic recession which increased the levels of unemployment and idle capacity. Although economic activity in the United States made a vigorous recovery, investment—a fundamental long-term factor—has not grown at the expected rate, especially with respect to its more productive components.

The monetarist and supply-side strategy reduced the share of wage earners in the global product—a consequence of the higher rate of unemployment and the loss of negotiating power by wage earners—and the return on financial capital increased considerably. Producer businesses experienced a reduction of their wage costs but a relative increase in their financial costs; this impeded accumulation for productive purposes by private business.

The high real interest rates in the United States spread—although at lower levels—to the rest of the developed central economies. In order to avoid domestic inflation or uncontrollable fluctuations in their exchange rates, Europe and Japan had to bear the recessionary effects of the monetarist and supply-side strategy of the United States. Thus, the "stagflation" which emerged in the 1970s is being combatted with policies which have not yet proved their medium and long-term effectiveness as means of restoring the economic growth rates of the centres.

The recession in the centres has had a devastating impact on the Latin American economy. The decline in living standards and increase in idle capacity, sometimes with the abandonment of production by failed businesses, and in unemployment, with all its social and political effects, are some of the most important results.

During the 10 years immediately preceding the crisis the patterns of Latin America's involvement in the world economy had undergone a profound transformation. The processes of internationalization and establishment of financial links with the industrialized market-economy countries had grown stronger, accentuating the vulnerability of the region to external fluctuations (ECLAC, 1983 and 1984).

The large external debt and the burden of servicing it are one of the serious problems reflecting the external stranglehold on the region's economy. Study of this situation illustrates the limited capacity of the region, internally and externally, to take independent decisions on more suitable policies.

The net amount of external investments and loans has been lower than net remittances of interest and profits. For this reason, in 1984—for the third consecutive year—Latin America had to make a sizeable net transfer of resources to the rest of the world. This transfer was in the order of US\$ 26 700 million which, although lower than the US\$ 30 000 million for 1983, signified, for the region's import capacity, a reduction of approximately 24% in the value of exports of goods and services.

The structural aspects and the inadequate domestic economic strategies and policies were important, but it was the external factors which lay at the root of the Latin American crisis and determined its scale. In the majority of the countries of Latin America these factors evolved in similar conditions and with common features.

#### *4. Prospects for the world economy and the consequences for Latin America*

The phenomenon of "stagflation" in the 1970s has been interpreted as an excess of effective demand accompanied by an inadequate rate of productive accumulation rather than as a lack of effective demand in the strictly Keynesian sense (Prebisch, 1984). The increasing share of government expenditure and wages—public and private—in the national income reduced the amount of the private reinvestable surplus and gave rise to a distribution struggle in the consumption sphere which affected investment in two ways: firstly, in consumerist attitudes in the use of the surplus which slowed the investment rate; and secondly, in the internal composition of this investment, both public (defence, space programme) and private (designed to improve the forms of consumption rather than to increase labour productivity and employment). Of course, the monetary and energy crises of the 1970s also played a part in creating problems of inflation and slowing down investment.

As has already been pointed out, the mone-

tarist and supply-side policy applied in the United States from the 1980s succeeded in controlling "stagflation" and after the initial recession (1981-1982) produced a recovery (1983-1984). But this strategy is based on macroeconomic imbalances which are difficult to sustain over the medium and long term: fiscal deficit, trade deficit, and rates of open unemployment above the historic postwar rates. Future modification of this policy depends to a large degree on the decisions taken by the economic authorities of the industrialized world and the international co-operation institutes under the control of the central countries. This circumstance invests any assessment of the short and medium-term prospects for Latin America with a considerable degree of uncertainty. The international situation has become so fluid that the terms of the problem are changing from one day to the next.

In these circumstances the Latin American countries must adopt a regional strategy based on increased co-operation and harmonization in the international promotion of their common interests rather than on bilateral arrangements and vertical relationships.

Perhaps any future concession by the industrialized centres of trade and financial terms more favourable to the region will result not so much from the representations of each individual Latin American economy or greater bilateral co-operation, as from a common, firm and united attitude in defence of shared interests. This proposal is all the more valid in the present financial international situation.

After the period of transition, which will perhaps take what remains of the 1980s, the centres will step up their development on the basis of the new technologies and energy sources which they are now preparing at top speed. The technological revolution in microelectronics, biotechnology and the use of more diversified sources of energy will generate economic structures which will transform not only the societies of the centres but also the international character and distribution of the world's productive capacity. It is difficult to foresee what impact this process will have on the place of Latin America in the world order, but there is no doubt that it will have profound social and economic effects.



### 5. *Some possible action for Latin America*

The present crisis might bring about a reaction on the part of Latin America which would have certain features which must be described. The external restrictions and the shortage of foreign currency is forcing governments to impose tighter regulation of the region's import capacity and compelling the State to take a more active part in the control and administration of foreign trade. With a view to solving the problem of unemployment and correcting the shortcomings in the region's production capacity, attention might be given to strengthening those forms, institutions and mechanisms of planning which are compatible with the operation of the market. The reduced import capacity will perhaps stimulate industrial activity to replace from Latin American sources an influx of imports which is now no longer available. The need to replace with domestic savings the interrupted flows of external financing might encourage tax reforms to penalize luxury consumption and reward the accumulation of capital. Perhaps a more austere and equitable attitude in the areas of consumption will be balanced by a more dynamic and responsible attitude to accumulation. National capital might possibly be repatriated, while the various forms of speculation and corruption—especially in the financial sector—could be combatted with greater vigour.

If these hypotheses as to the Latin American response to the crisis are found to make sense, a strategy would be established for greater recourse to State intervention<sup>2</sup> and planning in economic life; the national market would be protected and productive domestic activities promoted; regional trade would be set up on new bases which are already being explored; and more equitable trends would be encouraged in the distribution of income and consumption, with a view to promoting accumulation based on domestic savings. This picture would be compatible with the con-

tinuation of the democratic régimes which have recently come to power in the region.

Self-centred development, the search for efficient and democratic planning, diversification of production and industrialization, regional co-operation and integration, as well as the promotion of more dynamic and equitable growth, constitute a turnaround in ECLAC'S thinking. But the region is not the same as it was in the early postwar years. Today the societies and the economies of Latin America are much more developed and interdependent; they have a degree of real and formal integration which did not exist before; their average level of education is much higher, and they have highly trained teams of scientists, technicians and professionals. Lastly, they also have an increasing potential for joint defence of their common interest in the international, political and economic spheres.

The urgent need to reactivate the national and regional production of Latin America and to retool its industry with a view to long-term expansion means that there will have to be a pragmatic review of foreign policy and of international negotiations. In view of the emergency situation caused by the present shortage of foreign exchange, it is legitimate to use measures of protection and barter trade to maintain levels of activity and employment, facilitate the retooling of production units and, in general, promote the accumulation of capital.

The counterpart of these tactics and strategies of negotiation with the governments and businesses of the centres is to be found in the process of Latin American co-operation and integration. The unity of the countries of Latin America has an external expression in the strengthening of their power to negotiate with the centres and an internal expression in the greater integration of their economies.

The search for self-centred development which will help to solve the basic problems of Latin American societies would seem to require, in the long term, a new ethics of development which will neutralize divisive outside intervention and harness the enormous possibilities of technical progress which are at hand. The new technology must be sifted and adapted for use in accordance with the objectives of self-centred development.

<sup>2</sup>This should not be confused with an inflated bureaucracy or excessive growth in an inefficient public sector.

## II

# Latin America's foreign trade: diagnosis, prospects and policies

### 1. *Characteristics of Latin American trade and impact of the crisis*

The restrictions imposed on regional development by the international environment manifested themselves, where trade was concerned, in the spectacular fall in the prices of primary commodities,<sup>3</sup> a fall which was all the more serious as these commodities accounted for 80% of all Latin American exports. On the other hand, there was no change in the traditional dependence on imports of manufactures, mainly intermediate and capital goods, which at the beginning of the 1980s still made up 60% of the region's total imports. It is thus easy to appreciate the great importance of external purchasing power for this essential supply and the persistent structural imbalance in the relationship of the Latin American countries with the exterior.

In the trade sphere the recovery of the central economy would not necessarily lead to an increase in the real export earnings of the developing countries, particularly the countries of Latin America. The present protectionist trends—features of the trade controls which are on the increase in the centres—might have a harmful effect both on the volumes and on the prices of the goods exported by Latin America.

Although the region has benefitted from the United States recovery in 1983-1984 and from the overvaluation of the dollar, which have facilitated a great expansion of their exports to the United States, for reasons which have already been mentioned it remains to be seen whether the recovery of the centres will continue.

On the other hand, when the dollar returns to a more reasonable value competition from the United States economy will be felt in the markets

of Europe and Japan, regions in which production is also undergoing changes with the introduction of new forms of technology. It must therefore be assumed that in this stage of technological transition, with the consequent restructuring of comparative advantages in the international order, all the central economies will proceed to protect their national markets. This action might extend to control of the levels of activity and the employment situation, and continue until the new structure of comparative advantages in the developed world become clearer.

### 2. *The protectionism of the centres*

In recent years protectionism has been a dominant feature of the trade policy of the industrial nations. In putting protectionism into practice they have made use of a whole series of tariff and non-tariff barriers in their markets which are damaging Latin American production and exports.

One of the negative aspects of tariff barriers is the graduation of tariffs which, by taking into account the degree of processing of the products concerned, has become a powerful obstacle to the region's industrialization. The non-tariff barriers include import quotas, variable surcharges, safeguard clauses, "voluntary" export restrictions, discriminatory practices, compensatory rights, technical trade barriers and production and export subsidies. Protectionism has also grown in other forms. One example is the sharing agreements which the countries of the region have had to accept as the only means of exporting to a developed nation, as happened in the case of the GATT Multifibre Agreement. To appreciate the importance of these measures, it is sufficient to recall that in recent years approximately one half of the region's exports—excluding oil—to the United States, the European Community and Japan were affected by them. In practical terms, these protectionist measures are producing a

<sup>3</sup>The composite index for the 24 main export commodities of Latin America (excluding oil) fell by 25% between 1980 and the beginning of 1985.

situation in which the industrialized countries have the capacity to "administer" their trade with the developing countries.

This new protectionism has developed at the margin of the rules and obligations of the international trade system based on the GATT regulations. As protectionism for the most part involves bilateral arrangements, it represents a steady retreat from multilateralism as a means of solving the increasing economic and trade problems. In turn—as a result of the threat of protectionism—investment in export-oriented activities has declined in many countries of the region, especially with respect to manufactured goods<sup>4</sup>.

Although it is difficult to assess the full extent of the effect of this increased protectionism, it might prove to be one of the main problems affecting international economic relations and hindering the recovery of the world economy.

### 3. Latin American trade prospects

The prospects for a sustained expansion of Latin American trade up to the end of this decade depends on a number of factors, including the following:

i) *The world economic recovery.* This will be determined by the macroeconomic policies of the industrialized countries, especially the United States, owing to the controlling role of their economies in the international financial and monetary system.

ii) *The behaviour of primary commodities.* Owing to the dependence of Latin America on exports of primary commodities—and the close relationship between price movements and developments in world economic activity—there can be no great hope of a recovery of the economies of the region based on exports of raw materials. Some forecasts suggest that the average annual increase in the real value of world exports of primary commodities will be in the

order of 2 to 3% in the period 1985-1995 (ECLAC, 1985). Over the same period the real rate of growth in manufactures is estimated at 12%. If this proves to be the case, the region's terms of trade will suffer yet another major setback.

iii) *The protectionist trends.* There is little prospect of preventing an upswing of protectionism in the industrialized countries, despite the numerous undertakings which these countries have given in recent years. Owing to a number of factors of a structural nature, it is not thought that the protected industries of the developed countries will regain their international competitiveness; this might lead to the adoption of additional restrictive measures for those sectors. If that happens, the region's capacity to service its debt and finance higher levels of imports by means of increased export earnings would be even more seriously affected.

iv) *Adjustment policies.* If the present recessionary processes remain unchanged, some countries of the region will find themselves in situations difficult to control from the social as well as the economic standpoint. The possibility of expansion in the future will depend to a large extent on the external conditions which determine Latin America's trade expansion, such as: the world economic recovery, the international prices for the main Latin American exports, the net amount of external financing and the level of international interest rates.

v) *International negotiations.* Broadly speaking, the prospects for and results of future international negotiations will depend on the negotiating capacity of the developing countries, something which rests to a large extent in their own hands. The first step is to strengthen cooperation and solidarity among these countries. Moreover, there is an obvious need to review the objectives, procedures and strategies of future negotiations with the industrialized countries, so that the dialogue will be more effective and not cause the same frustrations as in the past.

### 4. Negotiating policies and options in the area of trade

The first lesson of the North-South dialogue is that trade, financial and monetary matters have been discussed and negotiated by each country in isolation and in different forums. In the case of

<sup>4</sup> A concrete example of this trend is the law approved on 31 July 1985 by the Congress and President of the United States under which the United States, to protect its own industry, will vote in the international financing institutions against any loan for projects for the mining, smelting and refining of copper.

primary commodities the focus has always been on individual product negotiations. In the GATT multilateral talks the negotiation has been broken down into groups and subgroups either of specific products or of specific barriers. Thus, there has never been a comprehensive or integrated focus for negotiations on the trade problem. The cost of this defect has been very high for the developing countries, for it impedes the process of co-ordination and joint action, makes it easier for the industrialized countries to create division and disagreement and neutralizes the negotiating power of the developing countries.

Latin America should conduct the negotiations with the industrialized countries in a much broader forum which would include primary commodities, manufactures, capital goods, services, technology, investments, and monetary and financial matters, as well as the region's purchasing power, which has never been given any importance at a negotiating table. The struggle to increase the negotiating power of the region will not be based on a desire for confrontation but rather on the intention to safeguard the region's legitimate interests.

If there is to be a new, more equitable and dynamic international trade system, the following objectives will have to be taken into consideration:

- i) Structural adjustment policies must be viewed as a new dimension of the future trade system. The theory that such adjustment would be produced spontaneously through the free play of market forces has proved incorrect.
- ii) A satisfactory system of safeguards will have to be established in order to solve, in a clear, consistent, equitable and non-discriminatory manner, the problems and difficulties which will inevitably arise.
- Hi) Attention should be given to the method of handling the processes which fall outside the GATT regulations and obligations or which are not dealt with adequately by the present trade system.
- iv) It will be necessary to secure the active participation of all countries and interaction among the various subsystems.
- v) A strong link must be established between trade and development and this link must

be incorporated in the generalized system of preferences without introducing new concepts such as graduation and reciprocity.

- vi) The trade system must begin to function again on a stable basis. This requires new initiatives in the areas of employment, monetary stability and the transfer of resources to the developing countries.

These objectives will be achieved only by the united will of the various groups of countries. One fact which must be stressed in future negotiations is that the present order has not only ceased to function for the developing countries but has also ceased to suit the developed countries themselves.

It must also be stressed that widespread protectionism has been one of the decisive causes of the erosion of the fundamental principles of the international trade system. Given this situation, two kinds of measure might be agreed at a regional level: preventive measures to prevent the opening of any debate detrimental to the region's exports; and the possible adoption of new measures. This will require a detailed knowledge of the legislation and regulations in force in the industrialized countries and of the pressure groups which might act for or against Latin American exports; it will also require retaliation against protectionism, with the application of similar measures against exports of the developed countries to the region. Such action might also have a preventive effect, since industrialized countries considering the adoption of protectionist measures would study the implications of retaliation very carefully. Furthermore, this kind of equal treatment would elevate the negotiations to a more political level where the regional mechanisms for agreement and co-ordination would have to be strengthened.

The most important contribution that Latin America could make to the world recovery would be to continue to fight for greater recognition of the increasing importance of the developing countries in the functioning of the world economy and of the need for an integrated approach—covering monetary, trade and financial matters—in international action to correct the shortcomings of the present world trade system.

Analysis of the debt situation illustrates the

interdependence between developing and developed countries. It also confirms the close relationships between the monetary, Financial and trade systems. In any common formula for debt service, agreements on the extension of time-limits and reduction of interest rates must take

second place to the main goal of facilitating Latin American growth. At the same time, the conclusion of agreements for this purpose would enable the region to increase the volume of its imports from the industrialized countries, which would assist the recovery of the world economy.

## III

### Regional integration and co-operation

#### 1. *General background*

Faced with a pressing need to increase and diversify intraregional trade and step up industrialization, the Latin American countries devised systems of integration. Starting from very low levels, trade within the region has grown very rapidly as a result of the liberalization of trade, export promotion programmes and the introduction of other instruments of integration, including payment systems. In addition to growing, trade has changed its composition. The advance of industrialization has made it increasingly possible to incorporate intermediate goods and certain capital goods.

Nevertheless, the participants did not all benefit equally from this process. Some countries accumulated deficits in their trade with the region on top of their deficits in international trade; others saw their national industries threatened by the tariff reductions inherent in the process of integration.

For these and other reasons some Latin American countries became increasingly reluctant to continue to reduce tariffs and derestrict their imports from the region, and although the time-limits for compliance with the agreements were extended and increasing numbers of exceptions were permitted, the integration systems could not attain all their goals. In the 1970s the negotiations not only marked time but even gave clear signs of moving backwards. When the economic crisis burst on Latin America, several countries began to apply a number of non-tariff restrictions which further eroded the agreed preferences.

All this seems to indicate that general, multi-

lateral and automatic removal of tariffs is not of itself a sufficient response to the needs of the countries and the genuine diversity of the region. Owing to the different levels of development of productive structures and the different degrees of openness to the exterior, the costs of integration are perceived more clearly than the benefits. The latter seem more uncertain and distant.

This means that in the present economic circumstances the Latin American countries are willing to grant each other tariff preferences only at reduced levels, or for specific items, or for some members and not for others. These concessions are often granted only for limited periods or are made subject to quotas.

Furthermore, the results of industrial integration have so far been meagre, although this does not invalidate the considerable power of this tool as a means of avoiding costly duplication of certain investments, exploiting the advantages of specialization and distributing the benefits equitably.

Lastly, it must be stressed that the systems of payment and reciprocal credit were the instruments which functioned most effectively in the past. They produced a considerable saving of foreign exchange, since it was necessary to use convertible currency only to settle the trade balances. The systems were easy to administer and the costs were very small in comparison with the great benefits obtained.

The economic crisis in the region also caused the payment systems to collapse. Convertible currency became scarce, since almost all the countries had to bear the heavy burden of servicing

their external debt at a time when external borrowing as a source of financing had disappeared. Some Latin American countries could not pay off the balances of their debt, while others began to exclude certain exports from the payment systems. The countries of the region are now seeking possible ways of reactivating these mechanisms which have proved to be a valuable means of increasing intraregional trade.

### *2. The need to upgrade the integration systems*

It is essential to re-establish the direction and reconstitute the elements of the integration systems of Latin America. The region's external structural dependence and vulnerability authenticate the need to lay the foundations for more dynamic, solid, equitable and independent economic and social development.

Despite the obstacles to integration and the errors which may have been committed in using some of the instruments, these methods still offer the region an opportunity to set in motion economic growth based on their own potential and strengthen the links among the countries to enable the nations of Latin America and the Caribbean, acting together, to solve the problems of their inequitable role in the international economy and strengthen their negotiating power with the rest of the world.

Within this framework one of the specific tasks which the integration systems will have to tackle is the re-establishment of the levels of intraregional trade, which have declined as a result of the crisis. This will require utilization of idle resources and an increase of the imports which the region needs in order to resume its development. This purpose will be served by improving the mechanism of compensatory payments and reciprocal credit, as this will produce an increase in trade with a minimum expenditure of convertible currency.

Another task will be to adapt the productive apparatus of Latin America to the changes taking place in the industrialized centres. If the region wishes to improve the integration of its productive sectors, fill the gaps in its industrial structure and involve itself in world technological progress, all the countries will have to join in a common effort.

The Quito Plan of Action defines sufficiently

clearly some of the tasks which have to be tackled in the immediate future. A large part of this responsibility was assumed by the Latin American Integrations Association at its second Council of Foreign Ministers. The Latin American economic system covers a large part of the region and, given co-operation, can contribute to unity and a greater Latin American presence in international negotiations. The Andean Group, which has played a pioneering role in defining the concept of integration —by adding the political and programme dimension— is a rich source of experience in this area, as are the Central American Common Market and the Caribbean Community with their achievements in the derestriction of trade and development of co-operation in many different sectors.

The integration systems have been under serious pressure as a result of the slowdown in the industrialization process and the Latin American crisis. Nevertheless, their institutions have remained largely intact and ready to operate in the new stage which the region is entering.

### *3. Co-operation and integration*

Economic and technical co-operation has always existed in Latin America and it has grown considerably stronger in recent decades. This process has been facilitated by the integration movements which broke down the isolation in which each country lived. Co-operation differs from integration in its instruments and legal framework, but this difference amounts to little in practice. The integration systems include areas of co-operation which go beyond the limits of mutual open markets. The results of this co-operation tend to foster the subsequent integration of economies, although many of these measures operate at the margin of the integration systems. Both sets of measures should be strengthened on a mutual basis.

Many of the areas of co-operation included in the integration systems have maintained a degree of coherence and dynamism even in difficult times. Mention must be made of the electric power link-up in the Central American Common Market, which continues to advance despite the considerable tensions in the area. In the Andean Group the Hipólito Unanue, Simón Rodríguez and Andrés Bello agreements continue to

function and, working together with the Andean Parliament and the Andean Tribunal of Justice, they are surmounting the economic dimension and aiming at the establishment of a genuine community of countries.

A number of moves have also been made in the Caribbean Community (CARICOM) to give this group greater cohesion. The Organization of Eastern Caribbean States was recently established among the less-developed countries and it already has joint bodies such as a Central Bank and a Supreme Court of Justice as well as joint diplomatic representation. Because of its particular geographical configuration, CARICOM committed itself from the outset to establishing regional maritime and air transport companies.

The Latin American Free Trade Association/Latin American Integration Association has organized special programmes of support for the relatively less-developed countries in which it has called for the co-operation of the other member countries. Unfortunately, these programmes proved of little use to the recipient countries, not only because they were furnished with few resources but also because they were not organically incorporated in the main areas of action of these institutions.

With the establishment of SELA in 1975 the countries attempted to open up a new channel for their aspirations for regional co-operation and to meet the need for co-ordination of policies towards the rest of the world. The system proved fairly effective with regard to the second objective, but less effective with respect to Latin American co-operation. The action committees—the mechanism chosen as a means of securing this co-operation—were rarely able to perform their functions, mainly for lack of commitment on part of the member countries. The most important committees are the ones for assistance in the reconstruction of Guatemala, which has already ceased to operate, for marine products and for drinking water; mention must also be made of the Latin American Technical Information Network and the Regional Food Security System. Other important areas of the work of SELA are the co-ordination of the Latin American position in the international negotiations in UNCTAD, GATT and the North-South dialogue, as well as on the Malvinas conflict (ECLAC, 1985).

At the present time, the renegotiation of the

foreign debt is monopolizing the efforts of the Latin American countries to reach agreement among themselves, though they have not even been able to achieve the desired unity of approach.

This incomplete list gives some idea of the large areas in which regional co-operation could strengthen a productive capacity and trade which, in the narrow national environment, could prove uneconomic. In the light of the variety of options available, provision must be made for an equally broad range of modalities, forums and mechanism of co-operation.

#### 4. *Geopolitical aspects of integration*

There are centripetal forces operating in favour of Latin American development and centrifugal forces pushing the region towards disunity in its policy towards the industrialized centres. The natural reluctance of governments to surrender any measure of freedom in determining economic policy is being aggravated by the crisis and by the need to correct, in whatever way possible, the external imbalance caused by debt servicing. The external restrictions occupy the attention of governments, so that discussion of development is increasingly limited to matters connected with the solution of the external problems.

In addition to the disunity caused by the crisis, there are other factors operating against integration: the region's great size and difficult geographical features, which create problems of communications and in intraregional trade, and the economic diversity, hostile attitudes, and tendency towards bilateralism.

Geopolitical tensions and the diversity of political régimes have also slowed integration and co-operation in Latin America and the Caribbean. The geopolitical tensions not only weaken the links between countries but also jeopardize the very basis of the national development of each nation.

Of the 21 countries for which information on the functional distribution of expenditure by the central government is available, eight spend more on defence than on health, three spend more on defence than on education, and two spend more on defence than on health and education combined (IMF, 1983).

In other words, in some countries military

expenditure is in open competition with economic and social development, for government expenditure tends to be fixed in the short term. Furthermore, a large proportion of military expenditures are on purchases of weapons from the big powers and further reduce import capacities, aggravating the problem of foreign debt and creating new links of dependence on the central countries.

From another angle, this preoccupation with weaponry impairs the effectiveness of the action taken to strengthen the political and economic links within the region. The tensions and conflicts, usually bilateral, not only affect the relations between pairs of countries but also tend to paralyze the initiatives for regional integration and co-operation.

If integration is conceived as a process in which all social agents take an active part, then the existence of democratic systems of government is a necessary condition for its attainment. Similarly, integration can only be said to be taking place when its benefits are perceived by a large part of the population of each member country. One of the benefits most easy to appreciate is the freedom of movement of persons among the countries of an integrated system, a situation difficult to bring about in an atmosphere of restriction imposed by non-democratic governments.<sup>5</sup>

How can regional integration and co-operation contribute to solving these problems? A first step would be to extend the concept of integration to the political level, for up to now the

<sup>5</sup>The European Economic Community, for example, grants associate status only to countries with democratic governments.

predominant view has been "commercialise". It will also be necessary to stimulate awareness of the need to achieve regional unity in order to deal with the present situation and future international relations, since regional unity achieved through integration is the only kind of unity which can guarantee the countries genuine security while preserving the attributes of true sovereignty.

In addition to devising mechanisms for the fair distribution of the benefits of integration, it will be necessary to secure active participation in this process for all social, political and economic groups and thereby increase their democratization.

One means of creating a political environment favourable to the solution of border disputes by peaceful means might be the conclusion of a Latin American treaty which would include: a guarantee of the territorial integrity of every country in the region and a commitment to non-aggression; the peaceful solution of disputes; express rejection of the use of force in the solution of conflicts or disputes of any kind; a gradual reduction of military expenditures and allocation of these funds to economic and social development; and reaffirmation of democracy and ideological pluralism as forms of coexistence and government.

Latin America's integration and co-operation organs must be given a role in these political tasks. For unless the secretariats of the subregional integration systems and SELA play a part in removing the obstacles to integration, the process will not be able to break free of the narrow and incomplete framework of "commercialism". The difficulties confronting this undertaking are enormous.

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