Part IV Country Reports

CHAPTER 65

ARGENTINA

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* Consultant and Professor, School of Government, Universidad Di Tella, Buenos Aires, Argentina. I appreciate financial support from the World Bank as well as the suggestions made by Mr. Patrick Macrory on a preliminary version of this paper. This paper was drafted before the devaluation of the peso implemented in early 2002 and in the final version I have added some clarifications and references to the current crisis. Nevertheless the essential messages of the paper, such as the fact that weak negotiating countries can end up paying a very high price, are not affected by recent events.

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I. Introduction

After decades of being marginal players in the multilateral trade negotiations, developing countries, including Argentina, decided to participate actively in the Uruguay Round. The main purpose of this chapter is to measure the imbalance between the concessions given and those received by Argentina in these negotiations. I conclude that the value of the concessions given has been far greater than the value of the concessions that Argentina received. Other subjects discussed in this chapter include an analysis of the economic consequences of this imbalance and the prospects for Argentina in a new multilateral round.

The first message I want to convey is that although there are several factors explaining the unbalanced outcome, Argentina's weak negotiating strategy was an important element. The evidence from Doha indicates that the leadership has not yet understood this point, and the economic analysis presented in this chapter indicates that the costs of a weak negotiating strategy are very high.

The second lesson is that protectionism increases the degree of incoherence between the multilateral trading system and the international financial system in ways that have so far not been studied in depth. The analysis presented here indicates that by reducing the exports of efficient producers, agricultural protectionism worsens their solvency indicators. This in turn, increases the level of country risk and the structure of domestic interest rates, therefore slowing growth and the capacity to service debt.

The chapter is organized as follows. Part II presents a brief description of Argentina's long-run trade performance as well as its role in the multilateral system prior to the Uruguay Round. Part III provides a quantitative measurement of the value of the concessions given and concessions received in the Uruguay Round negotiations, while Part IV analyses the economic effects of this imbalance. Part V offers a preliminary discussion of the interests of Argentina in ongoing regional trade negotiations, particularly between MERCOSUR and the EU. Part VI includes a discussion of the prospects for Argentina in a new round. Finally, I present brief concluding remarks.

II. The Role of Argentina in International Trade and in the GATT

At the start of the twentieth century Argentina was an active participant in the globalization process that was taking place at the time. The economic crisis of the 1930s put an end to this process. The crisis was deepened by the infamous U.S. Smoot-Hawley Tariff Act of 1930, and world trade is estimated to have fallen by around sixty percent between 1929 and 1933.[1]

Argentina suffered the consequences of this crisis, and like other countries, erected high barriers to imports. Unlike many other countries, however, it continued to remain inward-oriented for many decades after the Second World War.[2] Domestically, this ideology and its associated policies were fueled by economic theory and by rent-seeking groups, including the expanding military-industrial complex. With respect to economics, the trade policies of Argentina and most Latin American economies were influenced for decades by Raoul Prebisch's famous theories of import-substitution and the secular decline of the terms of trade of primary commodity exporting countries. After World War II, their own domestic policies, coupled with the increasing agricultural protectionism of

[1] Jagdish Bhagwati, Protectionism 21 (1990).
[2] *See* for example the excellent work by Carlos Diaz Alejandro, Essays on the Economic History of the Argentine Republic (1970).

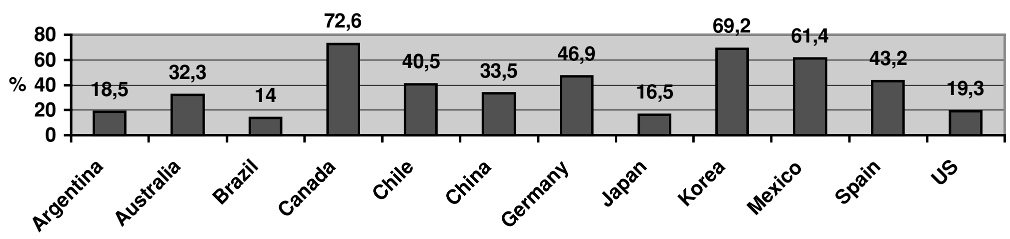

Figure 1: Trade Output Rations in a Sample of Countries, 1999
Source: Author's elaboration based on World Bank data.

the richer countries, meant that Latin American countries remained quite marginalized from international trade flows. This is one of the most important factors explaining the relatively poor growth performance of the region during the last thirty years.

Argentina's trade-output ratio (ratio of exports plus imports of goods to GDP) declined dramatically as a result of the drastic shift in its trade policies. Thus, while the ratio fluctuated between 35 percent and 45 percent during the 1920s, by the late 1940s it had declined to fifteen percent. From then until the end of the 1980s (in which decade the Government implemented the most protectionist policies for years), the trade-output ratio fluctuated around ten percent.

Inward-looking policies isolated Argentina from the growth of international trade that began in the late 1940s when the GATT was created.[3] Argentina was admitted to the GATT in 1967, but it was not an active participant in the Tokyo Round of multilateral trade negotiations that took place in the 1970s. For example, Argentina had bound only seventeen percent of its tariff lines prior to the Uruguay Round.[4]

As a consequence of its inward-looking policies and accompanying trade-distorting measures, such as the nationalization of public service companies and increasing fiscal deficits, Argentina lost competitiveness and its long-run potential growth rate declined. For example, while the per capita income gap between Argentina and the the richest country at that time (the United Kingdom) in 1900 was forty percent, the difference, this time with the United States, had widened to seventy percent by 1999.

Argentina remains a marginal player in international trade despite the fact that several years ago it completed an important reduction of trade barriers initiated in the late 1980s. Figure 1 shows that the trade-output ratios of Argentina and Brazil are the lowest in a sample of countries. This occurred in spite of the fact that Argentina's reform policies led to a doubling of the value of its exports during the 1990s.[5]

III. The Uruguay Round Negotiations

Both the preamble to the GATT and Article XXVIII bis of the Agreement state that multilateral trade negotiations should be conducted "... on a reciprocal and mutually advantageous basis ... ". I show in this part shows that the results of the Uruguay Round

[3] For a discussion of the early years of the GATT and the trade liberalization it led to, *see* Bhagwati, *supra*, note 1.
[4] Michael J. Finger, Merlinda Ingco and Ulrich Reincke, The Uruguay Round: Statistics on Tariff Concessions Given and Received 24 (1996).
[5] It should be said that after the 2002 devaluation, Argentina's dollar-based GDP has fallen, which in turn implies an increase of the trade-output ratio. Eight months after the devaluation, the country is still adjusting to the crisis; in this period exports have declined by eight percent and imports by a staggering sixty percent. Therefore it is still risky to say where the new equilibrium will lie after the adjustment has been completed.

("UR") for Argentina are clearly unbalanced in that the concessions it gave to its trading partners, particularly OECD countries, far outweigh those it received from them. I do this by quantifying the economic value of concessions in intellectual property, in services, and in trade in goods.

Argentina is not alone. For many developing countries the UR did not result in a balanced exchange of concessions.[6] Why did this occur and what are the consequences? I believe that one of the underlying reasons for this outcome in the case of Argentina and other countries was that their political leaders used the UR not as an instrument to open foreign markets, but mainly as a means to lock in unilateral economic liberalization policies. There were other factors, including, as I will argue, powerful rent-seeking groups from industrial countries that have undermined the multilateral trading system and forced developing countries to bind concessions against their will. These forces also explain part of the unbalanced outcome.

In quantifying the balance, I start by looking at the concessions given by developing countries with respect to intellectual property rights and trade in services, and then discuss the concessions given and received with respect to trade in goods.

A. Intellectual Property Rights: The Case of Patents for Pharmaceutical Drugs

Despite the resistance of some developing countries, the industrialized countries had sufficient negotiating power to include intellectual property rights in the UR, a new subject which resulted in the Agreement on Trade-Related Intellectual Property Rights ("TRIPS"). As a result, there is now under way a policy reform process that is increasing the strength of intellectual property rights ("IPRs") in many developing countries to a level that is closer to the standards of the industrialized countries. This has occurred despite the lack of any theoretical or empirical analysis to show that policy reforms induced by the TRIPS will increase world welfare, or the welfare of developing countries.[7] Why did this occur? What will be the impact on Argentina?

1. Rent-Seeking by Pharmaceutical Drug Companies

One of the main reasons why the patent section of the TRIPS takes the form that it does can be traced to the power of rent-seeking groups associated with certain forms of innovation and their intellectual protection, including pharmaceutical drugs.[8] Given the size of the pharmaceutical market and the economic interests at stake, I concentrate my remarks on the impact of TRIPS on this sector.[9] Also, for other forms of IPRs such as trademarks and copyrights, the differences in views between industrialized and developing countries on what should be the length and strength of protection are not as significant as they are in the case of pharmaceutical drugs. What was the strategy of the international pharmaceutical drug companies that enabled them to impose their patent policies on developing countries?

[6] Michael J. Finger and Julio J. Nogués, *The Unbalanced Uruguay Outcome: The New Areas in Future WTO Negotiations*, 25(3) THE WORLD ECONOMY 321 (2002).
[7] ***See,* in this respect, Chapter _ of this book **(Correa).**
[8] As I show below, pharmaceutical drug markets in several developing countries generate significant rents.
[9] The pharmaceutical industry is one of the few industries for which patent protection is critical as an incentive for investing in R&D. Pharmaceutical drug companies have one of the highest ratios of R&D to sales and most drug products can be easily copied. Patents are less significant in many other industries in which the incentives to innovate are essentially market-based, such as being the first to market. Richard Levin, Richard, Alvin Klevorick, Richard Nelson and Sidney Winter, *Appropriating the Returns from Industrial Research and Development*, Brookings Papers on Economic Activity**,** No. 3 (1987).

In March, 1987, only a few months after the UR had been launched, Gerald Mossinghoff, then President of the US Pharmaceutical Manufacturers Association ("PMA"), declared that the Association was working with the U.S. Congress to get it to enact "...the intellectual property revisions of the Omnibus Trade Bill that would strengthen the hand of the U.S. Government in urging all our trading partners to respect our rights in inventions and trademarks ...."[10] Soon afterwards, the U.S. Congress enacted the Omnibus Trade Act of 1988, which among other things amended Section 301 of the 1974 Trade Act so as to make it easier to impose retaliatory trade measures with respect to practices of foreign governments that are "unjustifiable ... unreasonable or discriminatory" and which burden or restrict US commerce.[11]

The law provides that failure to provide fair and equitable IPR protection is a form of "unreasonable" practice.[12] At the request of the PMA, supported now by the newly strengthened hand of the U.S. Government, the U.S. Trade Representative ("USTR") initiated a series of actions against developing countries that did not provide patent protection for pharmaceutical drugs, including Argentina, Brazil, Korea, and India. At the time, according to the World Intellectual Property Organization, forty-eight countries, most of them developing, did not provide patent protection for pharmaceutical drugs.[13] The PMA and the USTR therefore had fertile ground on which to deploy the strengthened Section 301, and they worked enthusiastically to force developing countries to enact patent protection for pharmaceutical drugs.[14]

Even in the United States, the degree of support for the patent system has fluctuated over time.[15] During the 1980s the U.S. Government favored strong IPR protection. The pharmaceutical industry took advantage of this, first by obtaining reform of domestic patent law, and then by moving aggressively towards forcing developing countries to introduce patent legislation or to reform their existing laws.[16] Clearly, the industry would not had been able to push as successfully at other points in time as it did in the 1980s, and

[10] Gerald Mossinghoff, *Public Policy Challenges to the Pharmaceutical Industry,* PHARMACEUTICAL MANUFACTURERS ASSOCIATION REVIEW (1987).

[11] Section 301(a) and (b) of the Trade Act of 1974, as amended, 19 U.S.C. §2411(a) and (b).

[12] *Id.,*Section 301(d)(3)(B)(i)(II), 19 U.S.C. §301(d)(3)(B)(i)(II).

[13] World Intellectual Property Organization, *Existence, Scope, and Form of Generally Internationally Accepted and Applied Standards/Norms for the Protection of Intellectual Property*, WO/Inf 129, (1988).

[14] For a discussion of these policies and their consequences, *see* AGGRESSIVE UNILATERALISM: AMERICA'S 301 TRADE POLICY AND THE WORLD TRADING SYSTEM (Jagdish Bhagwati and Hugh Patrick eds.1990).

[15] Professor Fritz Machlup, who undertook an evaluation of the patent system for the US Congress in 1958, concluded:

> "... if one does not know whether a system as a whole (in contrast to certain features of it) is good or bad, the safest policy conclusion is to muddle through either with it, if one has long lived with it, or without it, if one has lived without it. If we did not have a patent system, it would be irresponsible on the basis of our present knowledge of its economic consequences, to recommend instituting one. But since we have had a patent system for a long time, it would be irresponsible on the basis of our present knowledge, to recommend abolishing it ... "

Fritz Machlup, *An Economic Review of the Patent System,* U.S. Congress, Senate Subcommittee on Patents, Trademarks and Copyright, Study No. 15, at 80 (1958). Patent protection for pharmaceuticals has been a controversial subject from time to time in the United States, but those that have confronted the PMA, such as the American Association of Retired Persons, have had limited success in protecting their interests.

[16] Note that the introduction of patents in developing countries provides rents immediately after the policy comes into effect, while extending the patent life in industrial countries, as was done in the U.S. Drug Price Competition and Patent Term Restoration Act of 1984, only provides a higher level of income many years down the road and is therefore, more uncertain.

today some voices are beginning to argue that patent protection may now be too strong, as witnessed by the Doha Declaration on Public Health.[17]

The TRIPS Agreement was drafted at about the same time as these developments, and the patent section (Section 5) was influenced by the PMA. The proposed reforms had the support of the EC and Japan. They were opposed by a number of developing countries, including Brazil and India, but Argentina did not take a position. In the event, all contracting parties to the GATT/WTO signed the WTO Agreement as a single undertaking. It of course included the TRIPS Agreement which stipulated that patents should be available for inventions in all fields of technology, and should last at least twenty years from the date of filing.[18] Previously, the coverage and duration of patents in developing countries varied, and was usually less than twenty years. Countries structured their IPR policies in ways that they determined to be in their national interest. Now the policy is one of stronger and more uniform patent protection; a policy for whose welfare consequences there is no theoretical or empirical evidence.

I want to end these brief comments on rent-seeking with one reflection from history. In the area of pharmaceutical drugs, the available evidence suggests that retaliatory threats and retaliatory actions gained prominence in the late 1980s with the passage of the amendments to Section 301. It is of interest to recall that before then, several industrial countries still did not provide patent protection for pharmaceuticals. For example, France only introduced patent protection for pharmaceutical drugs in 1960, Germany in 1968, Japan in 1976, Switzerland in 1977, and Sweden and Italy in 1978. It would appear that patents were introduced in these countries when the size of their pharmaceutical industry was such as to make the likelihood of drug innovation from investments in R&D high. In other words, patents were introduced somewhere along the path of a market-based growth process. Pharmaceutical companies in developing countries will not have the same opportunity for innovation simply because they have not reached a size where it becomes profitable to invest in R&D in new drugs. The term applied to them is "pirates". Clearly, the development process of this industry in many developing countries has been dramatically changed by the obligation to introduce levels of intellectual property that are not adequate to their stage of development.

2. Estimating the Value of Concessions in Patents

In order to provide a rough estimate of the value of concessions in patents, the following discussion will address the issues of rents, foreign direct investment and trade.

(a) Transfer of Rents. As already discussed, the issue of patent protection for pharmaceutical drugs has to do more with the question of appropriation of the rents generated in developing countries than with concerns regarding innovation and growth potential in these countries. Table 1 shows some economic characteristics of the pharmaceutical drug market in several developing countries in 1988. I used these aggregate sales figures in a 1993 paper to estimate the income gains and rents that would accrue to multinational drug companies upon introduction of patent protection.[19] The estimated income gains

[17] World Trade Organization, *Declaration on the TRIPS Agreement and Public Health*, WT/MIN (01)/DEC/2, (2001). The text of the Declaration appears in the Appendix 10 this book.

[18] TRIPS Agreement, Articles 27 and 33.

[19] Julio J.Nogués, *Social Costs and Benefits of Introducing Patent Protection for Pharmaceutical Drugs in Developing Countries*, THE DEVELOPING ECONOMIES, at XXXI-1 (March 1993). *See also,* Arvind Subramianan, *Putting Some Numbers on the TRIPS Pharmaceutical Debate*, 10 (2/3) INTERNATIONAL JOURNAL OF TECHNOLOGY MANAGEMENT 252–268 (1995), for additional estimations of rent transfers.

Table 1: Sales of Patented Pharmaceutical Products in Some Developing Countries, 1988[69]

	(U.S.$ million)				
Variables	Argentina	Brazil	India	Mexico	Korea
1. Pharmaceutical Market Size	1,200.0	2,000.0	4,200.0	1,000.0	1,000.0
2. Patented Pharmaceutical Market	771.6	1,750.4	2,546.0	852.5	308.0
2.1 Sales by domestic firms	231.0	93.8	920.0	136.5	188.0
2.2 Sales by patent holders	540.0	1,656.6	1,626.0	716.0	120.0
3. Ratio of $(2)/(1) \times 100$	64.3	87.3	60.6	85.3	30.8

[69] *Source:* Julio J.Nogués, *Social Costs and Benefits of Introducing Patent Protection for Pharmaceutical Drugs in Developing Countries*, THE DEVELOPING ECONOMIES, at XXXI-1 (March 1993).

come from two sources. The first is the assumed transfer to multinational companies of all sales of patented drugs by domestic firms (Line 2.1 in Table 1). The second source of income is derived from greater exploitation of the monopolistic power protected by patents. Since there is no strong evidence on the extent to which firms in the pre-patent situation are behaving competitively, the estimates had to rely on different assumptions of price increases upon introduction of patents.

Additional assumptions on price-cost margins are necessary in order to go from estimated income gains to an estimate of pure rents. For example, it has been reported that for many years Pfizer sold the antibiotic Tetracycline at $30.60 per bottle of 100 capsules.[20] When Pfizer's patent was challenged, competing firms sold the generic product at $2.50 per bottle of 100 units. Scherer also asserts that "... many similar cases of price-cost margins in the order of 90 percent or more for patented drugs have been identified .... "

The market for pharmaceutical products in Argentina has grown since 1988, and sales reached $3.4 billion dollars in 1999. Assuming that: (i) the breakdown between patented products and the participation of foreign and domestic firms is similar to that presented in Table 1; (ii) patents will allow greater exploitation of monopoly power resulting in a thirty percent increase in gross sales; and (iii) the average price-cost margin of patented drugs is fifty percent, then the estimate of rents transferred from domestic to international pharmaceutical companies would be equivalent to $425 million per year.[21]

These are sizable rents, though they will not all be transferred at once. One reason is that there will be a phase-in period during which the number of patented drugs will increase until reaching international levels. Another potential cushioning factor will be the issuance of compulsory licenses in instances where a patent goes unworked for a number of years or where there is abuse of market position. On the other hand, the "strengthened arm" of the U.S. Government will be used to extract the maximum monopoly profits. For example in its 2000 *Special 301 Report,* the USTR states that ensuring "... that developing countries are in full compliance with the [TRIPS] agreement now that the

[20] FREDERICK M. SCHERER, INDUSTRIAL MARKET STRUCTURE AND ECONOMIC PERFORMANCE (1980).
[21] For details, *see* J. Michael Finger and Julio J. Nogués, *supra* note 6.

transition period has come to an end is one of the Administration's highest priorities . . . ."[22] The Report stated that there are " . . . 59 trading partners that deny adequate and effective protection of intellectual property or deny fair and equitable market access to United States artists and industries that rely upon intellectual property protection", and sixteen of them, including Argentina, were included in the Priority Watch List.[23]

(b) Impact on Foreign Direct Investment and Trade. After patent legislation has been implemented in the developing countries, international drug companies can choose to source from plants in those countries or from their major production sites. In the latter case, domestic production would cease, imports would increase, and employment in the industry would decline. Evidence that reverse foreign direct investment ("FDI") is likely to occur comes from developing countries that have recently introduced and/or strengthened patent protection for pharmaceutical drugs. One example is Chile, which implemented new patent legislation in 1991, since when most foreign subsidiaries have opted to leave the country and source from abroad.[24] This is a sensitive subject on which more research is needed.[25]

This evidence is in line with the view that FDI inflows to this industry in developing countries were not inhibited by the lack of patent protection.[26] It contradicts the opinions of those who argue that strengthening patent protection in developing countries would attract FDI, particularly in the chemical and pharmaceutical industries.[27]

To sum up, unlike the negotiations on trade in goods, the UR negotiations on patents, particularly patents for pharmaceutical drugs, were conducted with practically no empirical and theoretical analysis to support the different proposals. In this situation, it is not surprising that many of the justifications for promoting a worldwide uniform patent system are either non-existent, or tend to work in the opposite direction to that argued by its supporters. In the case of pharmaceutical drugs, this includes the arguments that patents in this industry in developing countries will: (i) induce a faster transfer of technology, (ii) increase inflows of FDI and, (iii) induce local innovation. It seems clear that the worldwide extension of patent protection to pharmaceutical drugs will result in a

[22] U.S. Trade Representative, *2000 Special 301 Report*, available at http://www.ustr.gov/html/special.html.

[23] *Id.* The Priority Watch List includes those countries that are being closely monitored for eventual retaliation. The 2001 Special 301 Report, available at http://www.ustr.gov/enforcement/special.pdf, identifies 51 countries that deny adequate and effective protection of intellectual property or deny fair and equitable market access to United States artists and industries that rely upon intellectual property protection. Sixteen countries, including Argentina, were again on the Priority Watch List.

[24] According to a personal communication to the author from the Asociación Industrial de Laboratorios Farmaceúticos Chilenos, many foreign companies stopped production in Chile after passage of the patent law.

[25] In conjunction with the World Health Organization ("WHO") and other multilateral organizations including the United Nations Industrial Development Corporation, the WTO could monitor carefully the effects of patents for pharmaceutical drugs as they are introduced in developing countries. The introduction of patents on pharmaceuticals has potentially important public health and industrial effects. Countries might need to apply competition policies to soften potential abuses from patent monopoly but have little or no experience in doing so.

[26] *See* Claudio Frischtak, *Harmonization versus Differentiation in International Property Rights Regime*, 10 (2/3) International Journal of Technology Management 200 (1995) (Brazil); A.S. Kirim, *Reconsidering Patents and Economic Development: A Case Study of the Turkish Pharmaceutical Industry* 13 (2) World Development 219(1985); and Julio J. Nogués, *Patents and Pharmaceutical Drugs: Understanding the Pressures on Developing Countries*, 24(6) Journal of World Trade 81(1990).

[27] **S*ee* Chapter _ of this book **(Correa),** Part I, note 3.

massive transfer of rents from pharmaceutical drug companies in developing countries to international ones.[28]

B. Services

1. Privatization of Argentina's Service Industries

During the 1990s, Argentina significantly liberalized its service industries. The purpose of this liberalization was to modernize the country after years during which inefficient government-owned companies held a monopoly of public services. As the quality of the services they provided deteriorated at an alarming rate, these companies were subject to increasing public criticism. When a new Government took over in mid-1989, the efficiency of these enterprises had reached such low levels that the proposal to privatize them faced no significant opposition.

A sweeping privatization program was implemented over the next few years. Today, ten years after this program was launched, the National Government has practically no stake apart from minority shares in the numerous and economically significant enterprises producing goods and services that used to be publicly owned.[29] Power generation and distribution, communications and telecommunications, gas production and distribution, wholesale and retail trade, banking and insurance, and numerous companies producing tradable goods, such as petroleum, chemicals, and iron and steel, have been privatized. Long-term private concessions have even been granted with respect to water companies, port facilities, railroads, and roads.[30]

While a complete assessment of this privatization program is not available, it has had positive and negative aspects. The performance of the privatized companies has generally been very good in terms of growth and quality of services. During the period 1993 to 1998, the increase in GDP of the services producing sectors was 24 percent against 18 percent in the goods-producing industries. But in the communications industry, where FDI is significant, the increase in value added during the same period was 46 percent. There is no doubt that the liberalization of services explains the growing inflows of FDI which, as a proportion of GDP, have fluctuated between 1.2 percent in 1993 to 3.0 percent in 1997.

Most of the misgivings with the privatization process have to do with the prices at which some of the privatized services are being offered. Some of these excessive prices come from flawed privatizations, including in some instances, the granting of monopoly positions and in others, inadequate formulae for rate adjustments. Basic telecommunications is an example of an initial grant of monopoly rights,[31] while in many other

[28] More recently the outcry from many developing countries led WTO Members to issue the Doha Declaration on Public Health. Furthermore, a number of studies are questioning whether the TRIPS should not be made more flexible. One of these studies, entitled *Integrating Intellectual Property Rights and Development Policy,* was published in 2002 by the Commission on Intellectual Property Rights established by Clare Short, U.K. Minister of Development. This study is available at www.iprcommission.org.

[29] The major exception is Banco Nación which remains the largest single bank in terms of deposits.

[30] The Provinces implemented important privatization programs, but some still own important companies. FDI inflows have also been attracted by the sale of privately-owned enterprises. While this form of investment has been prominent in the manufacturing sector, in some services where private ownership by nationals used to be important, such as banking, FDI inflows have generally not been associated with the privatization process.

[31] The telecommunications industry has been opened to competition only recently, and new companies have already started to contest the monopoly rights that were granted during the initial years to the privatized basic telecommunications enterprises.

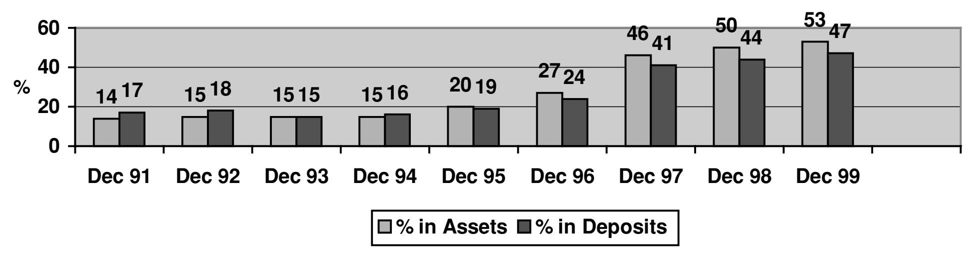

Figure 2: Participation of Foreign Banks in Argentina's Financial System
Source: Based on information provided to the author by the Central Bank.

service sectors the discontent arises from indexation formulas that have resulted in service prices that in some cases are well above international standards. Finally, criticism has also been raised against weak regulators. These regulatory deficiencies can also be attributed to the Government's lack of experience in exercising its new regulatory functions and in managing new competition legislation. Certainly more research has to be undertaken before definite conclusions can be drawn on these sensitive topics, but for the last two or three years as social problems have grown in intensity (high unemployment and increasing income inequality), public support for the privatized companies weakened and, following the devaluation in early 2002, they are suffering massive losses.

2. Estimating the Value of Concessions in Services

Argentina's UR concessions in services were quite significant and the discussion that follows intends to provide an estimate of its economic importance. I first note that for the sectors and subsectors where concessions were bound, there are no limitations on commercial presence or exceptions to the national treatment principle. This is the case with respect to: (a) business services; (b) communication services; (c) construction services; (d) distribution services; and, (e) tourism and travel services. Furthermore, in banking and related services, while trans-border trade was not bound, commercial presence was bound. As shown in Figure 2, foreign banks came to hold almost half of total deposits.[32]

Argentina's concessions with respect to telecommunications have also been important. For example, in the 1997 WTO agreement, Argentina bound commercial presence for the most important forms of telecommunications services and its concessions have been assessed as significant.[33] More recently, in June 2000, a Presidential Decree introduced further deregulation measures. Argentina did not participate in the post-UR financial services negotiations, the reason being that its earlier concessions had been significant.[34]

In sum, Argentina made significant concessions in services sectors in the UR as well as in more recent multilateral negotiations,. As a consequence, after decades of inward-looking policies, during the 1990s trade in services and services-related FDI inflows

[32] Following the devaluation of the peso in early 2002, this picture has changed.

[33] Peter Cowhey and Mikhail Klimenko, *The WTO Agreement and Telecommunications Policy Reforms*, Policy Research Working Paper 2601, World Bank (2001).

[34] Several studies show that in the banking industry, Argentina was one of the few developing countries that bound significant concessions in the Uruguay Round. For example, it has been shown that the liberalization index of Argentina for this industry is of a similar order of magnitude to those of the most liberal industrial countries. *See* Aaditya Mattoo, *Financial Services and the World Trade Organization: Liberalization Commitments of the Developing and Transition Economies*, Policy Research Working Paper 2184, The World Bank (1999).

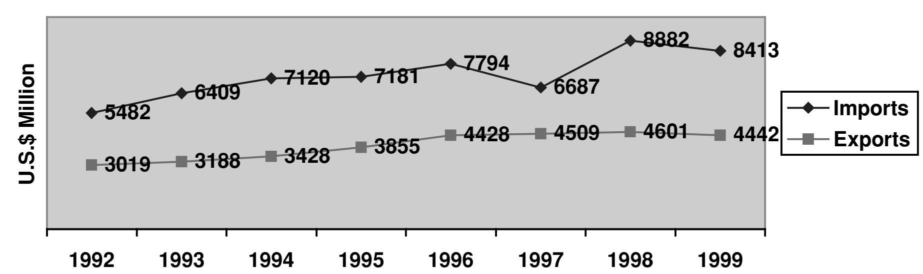

Figure 3: Trade in Services
Source: Ministry of Economy of Argentina.

blossomed. In what follows, we discuss trade effects and inward FDI flows into the services sector that were subject to the liberalization and privatization programs initiated in the early 1990s.

3. Trade in Services

In its successive Balance of Payments Manuals, of which the latest is the Fifth Edition ("BPM5"). the International Monetary Fund ("IMF") has recommended disaggregation of statistics on trade in services. In 1999, the Government of Argentina, which may be one of the few developing countries with complete and revised statistics on services trade,[35] published revised balance of payments accounts following the methodological guidelines indicated in BMP5. The new series start in 1992 and therefore provide valuable information on some of the trade effects following the liberalization of the services industries. What do these figures show?

Figure 3 shows exports, imports and trade balances for the services categories listed in BMP5. The figure shows a trade deficit increasing from $2.5 billion in 1992 to $4.3 billion in 1998.[36] This is in line with other Latin American countries, and contrasts with some Asian economies where trade in services, and exports in particular, is growing faster than trade in goods.

A second aspect worth noting is that this growing deficit is not the result of one or two services showing some unusual trade behavior, but the outcome of a number of categories that deteriorated during the 1990s. The sharpest declines occurred in the following accounts: (i) insurance and reinsurance (where the deficit increased by ten times), (ii) entrepreneurial services, (iii) financial services and, (iv) royalties. These statistics appear to show quite clearly that at the level of aggregation of the accounts indicated in BMP5, Argentina does not have comparative advantage in services. As we shall see, the picture is even worse if we add commercial presence as a mode of supply, as FDI inflows have grown rapidly.

One final comment. The work program leading to the publication of revised balance of payments accounts in 1999 also uncovered serious errors of measurement. There is no single services account that was being measured with reasonable accuracy and the largest errors appeared on the import side. For example, the previous figures underestimated services imports by $893 million in 1992 and by $2.3 billion in 1998. Clearly Argentina's participation in the UR services negotiations was based on rather poor statistics, and it

[35] Few developing countries, but most industrial countries, show entries on exports and imports for all the service categories listed in BMP5. *See* Obie Whichard, *Measurement, Classification, and Reporting of Services Activities: An International Perspective*, World Bank (1999).

[36] Because of the recession that started in 1999, the deficit in services trade also declined somewhat in that year.

is likely that the accuracy of official statistics is also a serious problem for many other developing countries.

4. Services-Related Inflows of FDI

Trade statistics say nothing about delivery of services under Mode Three (commercial presence) but in Argentina and other developing countries this appears to be the most significant source of supply. At most, balance of payments statistics represent a rough proxy of some of the trade flows under Mode One (cross-border). Again, the work leading to the publication of Argentina's revised balance of payments accounts in 1999 included a major effort to collect data on FDI. These statistics show the growth of inward FDI by economic sector and by country of origin for both stocks and profits/dividends.[37] What do these statistics show?

Following the liberalization of Argentina's trade and capital accounts in the early 1990s, inflows of FDI grew rapidly. In addition to the concessions given in the UR, the incentives for FDI were enhanced by Argentina's very open capital system and the very liberal treatment given to foreign capital. Most FDI inflows come under the umbrella of bilateral investment treaties that generally impose no restrictions in terms of sectors, percentage ownership, capital and profit remittances, or employment conditions.[38]

Between 1992 and 1998, the stock of FDI increased from $15.8 billion to $46.9 billions.[39] Table 2 provides a breakdown of this stock and the associated profits and dividends by economic sector. We see here that profits accruing to FDI enterprises in the services sectors jumped from $243 million in 1992, to $1.6 billion in 1998.

Over this period, the service category that has generated the most important flow of FDI profits has been electricity, gas and water, followed by distribution services. Figure 4 shows the accumulated flows of FDI for the period 1992 to 1998 by country of origin. As expected, Europe (mainly the Netherlands, Spain, France, and the United Kingdom), and the United States are the main sources of FDI inflows. Investors from these regions accounted for 72 percent of the accumulated FDI at the end of this period.

How much of this inflow of FDI can be explained by Argentina's concessions in the UR services negotiations is a difficult question to answer. Let us assume, for the sake of offering a rough estimate of the significance of these concessions, that commercial presence was a significant factor attracting FDI. In the UR Argentina bound commercial presence in all of the subcategories of the following services headings of the UR list where concessions were given: (i) business services, (ii) communication and telecommunications services, (iii) construction and engineering services, (iv) distribution services, (iv) financial services except insurance and reinsurance and, (v) tourism and travel.[40] Table 3 shows the inflows of FDI and associated profits classified according to Argentina's list

[37] Ministry of Economy of Argentina, La Inversión Extranjera Directa en Argentina: 1992–1998. Dirección de Nacional de Cuentas Internacionales, Ministry of Economy of Argentina: 1999.

[38] These treaties generally provide that investment-related disputes would be submitted to the International Center for the Settlement of Investment Disputes.

[39] Because of the sale of the remaining government shares in YPF (Yacimientos Petroliferos Fiscales), the largest petroleum company in Argentina, FDI inflows in 1999 reached the record level of $23.2 billion dollars. This raised the accumulated stock of FDI at the end of that year to $70.1 billion, more than twelve times higher than in 1992. Because of the unusual size of the YPF transaction, the comments in this part are focused on FDI inflows during the period 1992 to 1998.

[40] I am grateful to the Dirección Nacional de Cuentas Internacionales of the Ministry of Economy for providing the data for Table 3.

Table 2: Stock and Profits of FDI by Economic Sector Argentina 1992–1998

	(U.S.$million)						
Sector	1992	1993	1994	1995	1996	1997	1998
I- Stock		**17,392**	**22,319**	**27,828**	**32,609**	**40,929**	**46,858**
A-Goods	8,654	9,354	11,334	13,933	17,159	20,939	22,620
Petroleum	2,634	2,654	3,072	3,504	4,312	4,650	5,159
Mining	83	60	80	113	388	644	912
Manufacturing	5,937	6,640	8,182	10,316	12,459	15,645	16,549
B-Services	7,168	8,578	10,985	13,895	15,450	19,990	24,238
Elec., Gas, Water	2,291	3,229	3,691	4,876	5,286	6,567	7,526
Distribution	576	624	984	1,307	1,850	1,985	2,500
Communications	1,947	1,997	2,397	2,703	3,109	3,771	3,997
Banks	1,393	1,748	1,955	2,528	3,001	4,507	5,671
Others	961	980	1,957	2,481	2,205	3,161	4,544
II-Profits	**1,133**	**1,678**	**1,820**	**1,893**	**1,762**	**2,331**	**2,465**
A-Goods	890	873	1,279	882	909	1,203	908
Petroleum	349	290	430	409	451	363	209
Mining	−1	−10	−3	−4	−12	−4	−4
Manufacturing	452	593	852	477	470	844	703
B-Services	243	805	541	1,011	853	1,128	1.557
Elec., Gas, Water	−13	196	297	422	377	504	563
Distribution	133	163	294	213	189	150	204
Communications	91	92	34	178	113	217	291
Banks	71	204	−151	164	52	122	229
Others	51	149	68	34	122	135	270

Source: National Account Statements.

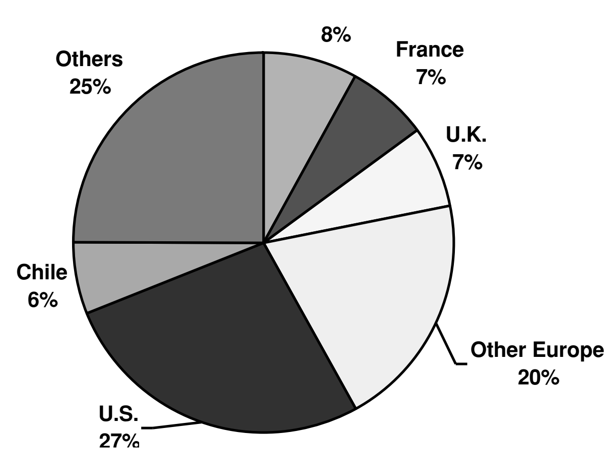

Figure 4: Stock of FDI by Country of Origin, Argentina 1998.
Source: Ministry of Economy of Argentina. (1999).

of concessions in the UR[41] for the categories where commercial presence was bound. According to these figures, the annual value of concessions given by Argentina to its trading partners was equivalent to $917 million of profits in 1998.

[41] Julio J. Nogués, *La Institucionalización de la Globalización*, in La Globalización y la Argentina, Consejo Empresario Argentino (Juan De Pablo, Rudiger Dornbusch and Julio J. Nogués eds. 2001) at 103.

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Table 3: Stocks and Profits of FDI by Economic Sector, Argentina 1992, 1995 and 1998

				(U.S.$ thousand)		
	STOCK			PROFITS		
Type of Service	1992	1995	1998	1992	1995	1998
Entrepreneurial	4,694	6,000	16,347	818	480	1,120
Post Office Mail	0	0	310,035	0	0	22,695
Telecommunications	1,947,284	2,618,745	2,553,150	180,482	261,746	342,692
T,V, and Cable	0	50,040	1,474,643	0	5,022	47,788
Construction	171,171	159,043	233,503	14,073	23,637	39,367
Wholesale Trade	292,160	349,782	85,985	79,940	50,168	−31,999
Retail Trade	146,053	485,349	1,689,820	34,675	90,226	146,165
Banks	1,393,000	2,528,000	5,670,939	71,000	163,000	229,000
Other Finance	91,510	156,157	460,482	34,473	11,703	90,918
Hotel and Restaurants	53,519	93,118	96,141	6,921	5,340	11,620
Other Transport	517	34,213	82,998	111	0	17,195
Total	4,099,908	6,480,447	12,674,043	422,493	611,322	916,561
Note Services where commercial presence was not bound:						
Electricity, Gas and Water	2,304,057	4,787,536	8,230,872	−11,916	422,666	568,319
Community Services	9,196	12,381	21,350	4958	1,685	6,818
Health	0	35,000	209,054	0	2,800	5,110
Transport	45,980	166,041	213,936	−71,662	−46,438	−42,130
Total	2,359,233	5,000,958	8,675,212	−78,620	380,713	538,117

Source: Dirección de Nacional de Cuentas Internacionales, Ministry of Economy of Argentina.
Note: Some of the figures in this table do not exactly match those in Table 2 because they come from a different source.

C. Trade in Goods

1. Manufacturing

In the area of trade in goods, probably the most significant concession given by Argentina in the UR was the binding of the maximum tariff rate at 35 percent for all goods. Previously, only seventeen percent of Argentina's tariff lines were bound.[42] In 1985/86, imports were controlled by very high tariffs and surcharges that put the simple average *ad valorem* rate at 39 percent. In contrast, the average MERCOSUR common external tariff ("CET") now stands at around thirteen percent.[43] Likewise, while in 1986, Argentina required advance import licenses for 47 percent of its tariff lines, this requirement no longer existed, at least until 2002.[44] However, other important non-tariff barriers still exist, such as those protecting the automobile sector as well as several antidumping measures.[45]

As a consequence of this trade liberalization program and other structural reforms, Argentina's trade grew quite significantly during the 1990s. In particular, the value of imports, that had stood at $4.3 billion in 1989, increased to $25.5 billion in 1999. Most

[42] Finger, Ingco, and Reincke, *supra* note 4, at 24.
[43] Julio Berlinski, El Sistema de Incentivos en Argentina (1998).
[44] Following the devaluation of early 2002, foreign exchange controls have been reinstituted.
[45] During 2001 increasing macroeconomic divergence from Argentina's attempt to sustain convertibility in the presence of a rapidly depreciating Brazilian "real" led to the implementation of an important number of departures from the CET, particularly by Argentina, Paraguay and Uruguay.

of these imports come from industrialized countries. Of particular interest is the fact that imports of capital goods from OECD countries increased from $745 million in 1989 to $4.2 billion in 1999.

2. Agriculture

Although one of the original objectives of the Uruguay Round was the "... reduction of import barriers..." to agricultural trade,[46] this goal was not met. The inefficient agricultural producers did not bind concessions of significant economic value in any of the major negotiating areas.

It is true that one of the advances achieved in the UR agricultural negotiations was the tariffication of non-tariff barriers, but even this process has been criticized as "dirty" in the sense that the base tariffs declared to the WTO were much higher than they were supposed to be. For example, the following *ad valorem* tariffs were notified by the EU as its UR base rates: rice 361 percent, wheat 156 percent, sugar 297 percent, meat 125 percent and dairy products 288 percent.[47] The sheer magnitude of these numbers is a clear indication of how strong some anti-globalization forces are in industrial countries. Even after reduction of many of these tariffs by 36 percent, which was the obligation undertaken by developed countries in the UR, many agricultural products were protected at a higher level than before the UR.[48]

Three policies were supposed to reduce agricultural protection by the OECD countries: (i) the reduction of tariffs, (ii) the binding of tariffs at the end of the implementation period, and (iii) minimum access commitments. In spite of these important opportunities for liberalization, the conclusion of the assessment of the UR results is that there is "... markedly little liberalization for most products in most countries ...."[49] The Agreement on Agriculture appears to be somewhat stronger with respect to the reduction of export subsidies, but overall there has been little progress and in some instances, the results have been retrogressive.[50]

Since the completion of the UR, OECD governmental assistance to agriculture has continued to rise. This assistance reached $336 billion in 1997 and $362 billion in 1998. This increase is partially explained by the reduction of international commodity prices, many of which continued to decline in 1999.[51]

The disappointing results of the agricultural negotiations helps to explain some trade developments. Traditionally, Argentina maintained an overall trade surplus with countries in the EU but during the 1990s this surplus shifted to systematic deficits. The size of these deficits has been influenced by Argentina's liberalization steps as well as by the continued resistance by the EU to liberalize its agricultural policies.

D. Summing-up

For Argentina, the UR resulted in an important imbalance between the concessions that it made and those that it received from OECD countries. First, at the end of the transition

[46] GATT Secretariat, *The Uruguay Round Ministerial Declaration* (1986).
[47] Dale Hathaway and Merlinda Ingco, *Agricultural Liberalization and the Uruguay Round*, in THE URUGUAY ROUND AND THE DEVELOPING COUNTRIESPAGES 30–58 (Will Martin and L. Alan Winters eds. 1995).
[48] *Id.*
[49] *Id.*
[50] Nogués, *supra*note 41, at 136.
[51] OECD, AGRICULTURAL POLICIES IN OECD COUNTRIES: MONITORING AND EVALUATION (This is a yearly report and the reader should consult the volumes for 2001 and 2002).

period, rents of $425 million per year may have been transferred from domestic to international pharmaceutical companies in developed countries. Second, liberalization of trans-border flows was accompanied by a doubling of the services trade deficit as imports, mostly from industrial countries, increased by 62 percent between 1992 and 1998. Third, in the service sectors where Argentina bound commercial presence in the UR, the profits of FDI firms, the majority of which are of OECD origin, reached $917 million in 1998. During these years, the stock of FDI in these sectors tripled. Fourth, Argentina's trade liberalization also resulted in a more than tenfold increase in the annual import bill of capital goods from OECD countries. In short, the concessions given by Argentina in the UR have provided important benefits to foreign companies from the industrialized countries.

On the receiving side, Argentina benefited from tariff reductions in manufactured goods, but as we have seen, it also gave important concessions in these products. As to the negotiations in agriculture, the outcome is certainly not "liberalization".

Summing up, according to the mercantilist equation by which the results of multilateral trade negotiations are assessed, Argentina was a big loser in the UR. This as I argue in the next part, particularly the results of the agricultural negotiations, has had serious negative economic consequences for the country.

IV. Costs of Agricultural Protectionism for Argentina

Argentina's agricultural and agro-industrial exports represent around fifty percent of its total exports of goods. It is not surprising, therefore, that the damage that agricultural protectionism inflicts on Argentina is in the billions of dollars. The social impact is also significant because, while some OECD agricultural producers receive as much as $35,000 dollars of subsidy per year,[52] poverty levels in the countryside of Argentina, as well as migration from rural to urban areas, have continued to rise. In a significant way, rural poverty in Argentina is the mirror image of the riches in the OECD countries.

A. Agricultural Protectionism and Financial Costs

The macroeconomic impact of agricultural protection is also significant. Had the UR Agreement on Agriculture resulted in an increase in Argentina's agriculture exports of say $5 billion, the country's debt service ratio would be lower. This, as I argue below, would reduce the level of country risk and the structure of domestic interest rates.

For example, between 1990 and 1998 Argentina's total exports to the EU increased by only 21 percent. This contrasts with the country's performance of total exports and exports of primary products plus foodstuffs that during the same period increased by 112 percent and 92 percent respectively.[53] As discussed earlier, with this performance, the traditional trade surplus that Argentina used to have with these countries shifted to a systematic deficit.

The imbalance is important; and is likely to have negative macroeconomic effects that go well beyond the direct trade and production effects. To understand this, recall that Argentina is a country with an open capital account and with free capital movements up to the end of 2001. Therefore, since the early 1990s its structure of interest rates has been determined by international risk-free rates plus a domestic risk factor. Since

[52] *Id.*, 2001.
[53] Nogués, *supra* note 41, at 185.

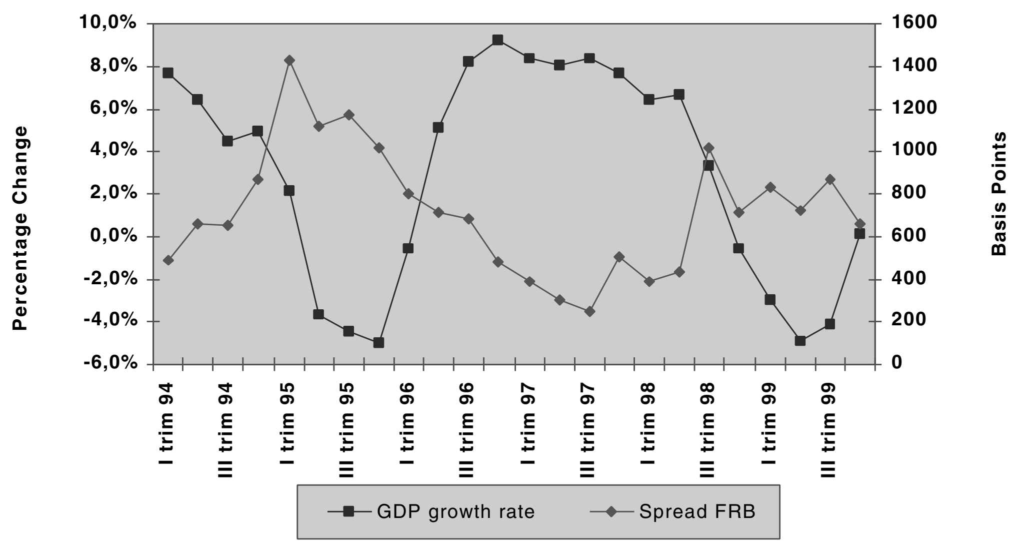

Figure 5: Country Risk and Interannual GDP growth rate
Source: Julio J. Nogués and Martin Grandes, *Country Risk: Contagion, Deficits or Political Noise,* IV(1) JOURNAL OF AAPPLIED ECONOMICS 125 (2001).

the national Government is by far the major borrower in international markets, the risk implicit in its bonds is a major determinant of domestic interest rates. When foreign investors conclude that the economic outlook of the country is likely to improve, they bring capital into the country, for example by increasing their demand for Government bonds. When this happens, the increase in bond prices result in a reduction in the level of country risk as measured by the interest spreads between domestic and risk-free bonds. In fact, as Figure 5 shows, the level of country risk is inversely correlated with short term economic cycles.

This figure shows year-on-year variation in quarterly GDP and the spread between the returns of Argentina's sovereign bonds and the comparable US Treasury bond. What determines this spread, usually known as the country risk factor? In recent empirical research, this risk has been found to be a function of a number of economic and political variables, including contagion effects from Mexico's financial markets, growth expectations, fiscal deficits, political noise effects, and solvency indicators such as debt service to exports.[54] This last variable helps to understand how the level of exports may have macroeconomic effects through financial variables. Our findings show that a one percent permanent increase in this variable increases country risk by 0.63 percent. With these results we can simulate what would be the level of country risk for different levels of additional exports.

This exercise is based on recent findings based on a computable general equilibrium model which suggests that the dismantling of OECD agricultural protectionism could have increased Argentina's exports by between 25 percent and 100 percent.[55] Based on these simulations and on the elasticity of country risk with respect to debt service to export ratio, we can conclude that had the level of exports in 2000 been 25 percent higher, the country risk would had been ten percent lower. If lower agricultural protectionism

[54] Julio J. Nogués and Martin Grandes, *Country Risk: Contagion, Deficits or Political Noise,* IV(1) JOURNAL OF APPLIED ECONOMICS 125 (2001).
[55] CARLOS SÁNCHEZ AND GABRIEL CASABURI, LAS DISTORSIONES DE LOS MERCADOS MUNDIALES DE ALIMENTOS Y SU IMPACTO EN LA ARGENTINA (2001).

had enabled Argentina to increase its total exports by fifty percent, the level of country risk would had been 33 percent lower.

Summing-up, in addition to the traditional static welfare losses from agricultural protectionism, the analysis of this part indicates that because agricultural protectionism also increases interest rates in efficient producer countries like Argentina, the cost of this protectionism is higher than what has been traditionally assumed. For example for 2000, the average country risk faced by Argentina' domestic residents was 672 basis points.[56] Had Argentina faced open international agricultural markets, its country risk would had been much lower, saving domestic debtors billions of dollars in interest costs.

B. Other Costs of Agricultural Protectionism

I have argued elsewhere that the higher structure of interest rates caused by higher country risk implies lower growth.[57] In addition, not only the level but also the policies used to implement this protectionism create additional costs for a country like Argentina. This occurs because international price fluctuations are accentuated by the policies of industrialized countries that shelter their domestic farmers from these fluctuations. By increasing the instability of Argentina's terms of trade, the slower growth resulting from higher country risk occurs along a path of widened business cycles.

On a related matter, I hope that this discussion has illustrated the importance of the Marrakesh mandate for the achievement of greater coherence between international financial organizations like the IMF and the World Bank, on the one hand, and the WTO on the other.[58] As long as agricultural protectionism in industrialized countries continues to remain at the very high level of the last decade, there will remain clear opportunities for increasing the "coherence" between international financial markets and the multilateral trading system. A significant decline of agricultural protectionism would facilitate repayment of foreign debt and strengthen the international financial system.

C. Summing-up with a Proposal

This discussion has shown that the increased financial costs faced by countries that are efficient producers as a consequence of protectionism on the part of industrial countries is higher and sometimes much higher than usually thought. Additional dynamic costs of these policies are caused by slower growth rates and magnified business cycles. Both the static and dynamic economic costs faced by Argentina and other efficient developing country producers that can be attributed to agricultural protectionism by industrialized countries are shamefully high.

Unfortunately, there is every indication that this protectionism is becoming more entrenched.[59] My proposal is for the existing Working Group on Trade, Debt and Finance in the WTO to be transformed into a negotiating Body. It is quite incredible that issues

[56] Data provided by Dirección de Cuentas Internacionales of the Ministry of Economy.

[57] Nogués and Grandes, *supra* note 54.

[58] *Declaration on the Contribution of the World Trade Organization to Achieving Greater Coherence in Global Economic Policy making*, in The Legal Texts: The Results of the Uruguay Round of Multilateral Trade Negotiations (1999) at 386.

[59] The passage of the US Farm Bill of 2002 and the 2002 proposal by the EC to reform the Common Agricultural Policy support this view. A preliminary analysis of these proposals appears in the recent report issued by the World Bank and the International Monetary Fund entitled *Market Access and Developing Country Exports-Selected Issues*, available at www.worldbank.org.

like trade and environment have become negotiating topics and yet the strong link between trade and debt still remains on the sidelines of the multilateral trade negotiations. Including trade and debt as a negotiating topic would change the structure of incentives as it would make more visible the costs of agricultural protectionism and would trigger a debate on who should pay for it.

V. Regional Trade Negotiations between MERCOSUR and the EU

As a member of MERCOSUR, Argentina is participating in several regional trade negotiations, including those with the Andean Group, with the United States (in the Free Trade Agreement of the Americas ("FTAA"), and with the EU. At the time of drafting this chapter (the end of 2001), only the negotiations with the EU had advanced to a stage where some relevant comments on trade negotiating strategies can be offered. The negotiations with the United States had not yet started, and the agenda of the FTAA indicated that these would start in late 2002. Only a preliminary exchange of documents had taken place with the Andean Group, where the goal is a free trade agreement in goods.

A. Background

In December, 1995, MERCOSUR and the EU signed an interregional cooperation agreement that seeks to create a free trade zone. Since then, both regions have held a number of meetings, and in 1999 the Bi-Regional Negotiating EU/MERCOSUR Committee ("BNC") initiated the negotiations. By the end of 2001 the BNC had already met six times, most recently in early July 2001 in Montevideo and in Brussels in late October 2001.

The first three meetings dealt essentially with the exchange of information. The fourth meeting of the BNC ("BNC IV") held in Brussels, was more substantive in character. Here MERCOSUR indicated that it was seeking a free trade agreement. Essentially, the MERCOSUR was expressing its aim that the Common Agricultural Policy ("CAP") should not be an obstacle to the establishment of a free trade agreement. In turn, the EU expressed that it was planning to present to MERCOSUR a concrete offer and demand for market access in the next BNC meeting. This proposal would later prove to be far from a free trade agreement.

B. Differing Negotiating Goals and Strategies

The MERCOSUR document, entitled "Modalities for the Tariff Negotiations", demanded, in line with its goal of establishing a free trade area, that "... it is necessary to establish a reference tariff on the basis of which liberalization would be negotiated ...". It further stated that "... specific tariffs, mixed tariffs and any other type of tariffs should be transformed into an *ad valorem* equivalent that for negotiation purposes would be the maximum reference tariff .... " MERCOSUR offered to reduce its common external tariff ("CET"), which is defined on an *ad valorem* basis, plus any modifications introduced after its establishment in 1994 to zero over a ten year period, the same period proposed by the EU. Of course, there would be a list of exceptions for sensitive products.

Obviously, the goal of MERCOSUR's demand for *ad valorem* tariffication was to ensure that the many trade measures protecting EU agricultural and agro-industrial products should not be an impediment to the negotiations. In essence, by proposing to base market access negotiations on transparent equivalent *ad valorem* tariffs and to negotiate their elimination over a ten year period, MERCOSUR was offering full reciprocity. In fact as we shall see, it was in effect offering more as it was not refusing to negotiate other issues put on the table by the EU, some of which appear to be of doubtful economic interest to the region.

In contrast, the EU never agreed to negotiate on the basis of equivalent *ad valorem* tariffs. It argued that this would undercut the CAP, with respect to which it is only prepared to negotiate in a multilateral round (which, as I argue below when discussing the Doha Declaration, is unlikely to occur in a significant way). In response, MERCOSUR argued that its goal was to put the regional negotiations on an equal footing for both sides, and not to challenge the CAP. In fact, so far the EU strategy appears to have been to negotiate specific elements of the CAP on a product-by-product basis. The differences between the MERCOSUR proposal and that of the EU are significant.

C. The EU Proposal

The EU presented its proposal at the July 2001 BNC meeting,. In contrast to MERCOSUR's offer for a free trade agreement, it is difficult to see how the EU offer could have been more mercantilist. While the EU proposed that both sides should eliminate *ad valorem* tariffs over a period of ten years, this proposal hides an important imbalance in market access concessions, as now explained:

- The EU proposal would ensure free access to the MERCOSUR market for EU manufactured products, the most protected sector of the economies of the region, in exchange for access to what is already a very open market in the EU.
- The picture is very different with respect to agricultural and agro-industrial products. Except for a few countervailing measures, agricultural protection in MERCOSUR is also based on *ad valorem* tariffs. The EU proposal to dismantle *ad valorem* tariffs would also provide a high degree of access to the MERCOSUR market for EU agricultural products. It would not however provide much access for MERCOSUR agricultural and agro-industrial products to the EU. In addition to *ad valorem* tariffs, the EU imposes seasonal tariffs, specific-rate tariffs, and mixed tariffs, and it also employs export subsidies, budget support, tariff escalation, special agricultural safeguards and quotas.[60] The EU has offered to dismantle only the *ad valorem* tariffs, which would leave a very high degree of protection in place, particularly for products where MERCOSUR has comparative advantage.
- To compound the problem, the EU agricultural and agro-industry policies provide a high degree of protection administered in a very non-transparent way. It could take the MERCOSUR negotiators several months to gain detailed knowledge of this protection and then they will be faced with the difficulty of deciding how much MERCOSUR should "pay" the EU to eliminate the *ad valorem* tariff or other components of its agricultural protection? The complexity of this problem increases when approached on a product-by-product basis. Different products are protected by different measures in the EU, but in general *ad valorem* tariffs do not provide the bulk of protection to agricultural products.[61]

[60] Some products of significant export value for MERCOSUR, such as beef, also face sanitary and phytosanitary barriers, some of which appear to be supported by weak scientific evidence.

[61] The nature of the complexity of EU agricultural protectionism can be illustrated by two examples. The first is fruits such as pears, apples, and oranges. For specific periods of the year classified by month or

- Furthermore, in contrast to the initial MERCOSUR proposal that covered all products, the EU proposal excludes around one thousand tariff lines of which 781 are products of great export interest for Argentina. Estimates of the *ad valorem* equivalent by the Secretariat of Trade with respect to a sample of the excluded products show a high average level of protection of these products of 36 percent, with a maximum of 463 percent. Exclusion of these products significantly reduces the MERCOSUR export potential of a trade agreement with the EU.
- In addition to full access to the MERCOSUR markets for goods, the EU is demanding: (i) full reciprocity in textiles and footwear, (ii) standstill and rollback, (iii) for fisheries products, liberalization would take into account "access to water resources", (iv) duties on wine would be abolished in the framework of a separate agreement including "protection of geographical indications and traditional expressions." In Argentina textiles and footwear are two "sensitive" labor-intensive sectors. Standstill (no new measures to be introduced) and rollback (of import measures to some specified date) have not been discussed in detail but given the nature of the CAP, there is no way that a realistic rollback by the EU could offer gains in market access that would match a similar reform by MERCOSUR. Details of the proposal on access to water resources and geographical indications have not been specified, but Argentina's national fishing fleet is not significant and, although Argentina has good wines, it has not developed significant geographical indications, so that in these areas too, it may be the loser. In sum, reciprocal concessions in these areas of the expanded negotiating agenda appear to have greater commercial value for the EU.
- The EU has also demanded negotiations on government procurement and services. In both areas, the EU seeks a high degree of access to the MERCOSUR markets. In services, for example, it seeks access to all markets except audiovisual services, national maritime cabotage and air transport services. The proposal clarifies that the "right of commercial presence" does "... not extend to seeking or taking employment in the labor market or confer a right of access to the labor market of another party." [62] Regarding government procurement, the presumption is that EU multinationals are better positioned to sell to MERCOSUR governments than vice versa.

D. Summary

With the available information it is risky to forecast where the regional negotiations between MERCOSUR and the EU will end. One general comment is that the outcome will not be the broad free trade agreement that MERCOSUR countries initially sought. A second general comment is that in agriculture, the outcome will most likely be one of very limited liberalization by the EU. If so, the economic results of these negotiations

consecutive months, fruits are protected by *ad valorem* and specific tariffs. Given the objective of protecting farm incomes, the EU specific tariffs vary inversely with the level of import prices. The result of this is that for pears for example, there are ten rates varying between zero and ten percent. In addition, specific tariffs also vary by time of the year so that the number of possible combinations protecting pears is very high. In simulations performed by Argentina's Secretariat of Trade, the EU *ad valorem* tariff equivalent, including the effects of specific tariffs, protecting pears varies between zero and 77 percent.

[62] *European Union Working Text: Trade in Services,* EU draft, July 2, 2001.

will be of limited value for Argentina. Further discussions will have to take place before a comprehensive assessment can be made of the net benefits that Argentina might derive from a MERCOSUR-EU trade agreement.

VI. Argentina's Prospects in a New Multilateral Trade Round

Argentina failed to defend its interests effectively at the WTO Ministerial Meeting held in Doha in November, 2001. Having been taken in by the UR Agreement on Agriculture, including the dirty tariffication practiced by industrial countries, Argentina should had gone to Doha prepared to say no to a new multilateral round. The prospect of still another negotiation where little agricultural trade liberalization is expected to take place worsens the development prospects of the country. In contrast to the weakness shown by Argentina, the EU hinted at Doha that unless specific language on agriculture was included in the Ministerial Declaration, it was ready to say no to a new round. In particular, the EU went to Doha prepared to stand firm on its objective not to allow specific quantitative targets for agricultural liberalization. For example, the EU strongly objected to the language that suggested an agreement to dismantle export subsidies, and in the end its threats prevailed.

There is little in the Doha Ministerial Declaration to suggest that significant liberalization of the agricultural protectionism practiced by industrial countries will be achieved. The statement in the Declaration that the negotiations should aim to achieve "... substantial improvements in market access; reductions of, with the view to phasing out, all forms of export subsidies; and substantial reductions in trade distorting domestic support ..."[63] is not substantially different from the language of the UR Ministerial Declaration that promised significant reductions in import protection. As noted above, OECD agricultural protectionism today is about the same if not higher than what it was before the conclusion of the UR.

The outcome of the new WTO negotiations will depend on the ability of different countries to obtain their goals. Unfortunately, the available evidence suggests that the EU and Japan will most likely prevail. These countries not only convinced other Members to exclude quantitative targets for agricultural trade liberalization from the Ministerial Declaration, but also succeeded in including the statement that "... non-trade concerns will be taken into account in the negotiations ...."[64] Another statement included at the behest of the developed countries was that "... under WTO rules, no country should be prevented from taking measures for the protection of human, animal or plant life or health, or of the environment at the levels it considers appropriate ..."[65] This statement refer to sanitary and phytosanitary standards. Emerging evidence suggests that these standards are being used with protectionist intent.[66]

Argentina went to Doha without having prepared a negotiating strategy. Neither the Minister of Foreign Affairs, the country's chief negotiator, nor any other minister attended the meeting. Its deputy chief negotiator arrived late. In contrast to the lack of political

[63] World Trade Organization, *Doha Ministerial Declaration,* WT/MIN(01)/DEC/1, ¶13. The text of the Declaration is provided in the Appendix _ to this book.
[64] *Id.*
[65] *Id.,* ¶*6.*
[66] *See,*e.g., John Wilson, *Standards, Trade, and Development: What is Known and What do We Need to Know,* presented at the World Bank Seminar on Informing the Doha Process: New Research for Developing Countries, Cairo, Egypt, May 20–21, 2002.

importance given to this meeting by Argentina, other developing countries like Brazil and India attended with clear objectives and a strategy that apparently included saying no to a new round if they did not achieve minimum goals. Thus, for example, Brazil played a key role in the Declaration on the TRIPS Agreement and Public Health. Likewise, in his opening statements, India's Minister of Commerce and Industry, its chief trade negotiator, stated that the "... draft Ministerial Declaration is neither fair nor just to the viewpoint of many developing countries ... It is a negation of all that was said by a significant number of developing countries and least developing countries ...."[67] It is therefore not surprising that India played a key role with respect to the Doha Ministerial Declaration on Implementation-Related Issues and Concerns.[68]

In my view, Argentina should had prepared a negotiating strategy that at a minimum included the threat of not supporting a new round if specific agricultural commitments were not included in the Ministerial Declaration. If it had done so, the WTO Members would have witnessed a confrontation between rich protectionist countries and poor but efficient developing countries. I believe this would have benefited Argentina in much the same way as standing firm proved to be a successful strategy for other industrialized and developing countries. As things stand, Argentina is headed towards another multilateral negotiation that will most likely result in an unbalanced outcome and additional net costs to the country. Obviously this can still be corrected during the negotiations but for this to happen, Argentina must develop an aggressive strategy.

VII. Concluding Remarks

At the time of the UR, Argentina and many other developing countries that implemented inward-looking policies for decades, had to show to the globalizing world that they were doing their homework. For many reforming countries, the UR was an instrument to lock-in unilateral liberalization policies while for industrial countries, it was an agreement to sell and export increased quantities. In part because of this but also to a significant extent because Argentina lacked a negotiating strategy, it came out of the round with a clear imbalance between the concessions it gave and those that it received.

The imbalance for Argentina is significant and probably one of the most important of the UR, and I have shown that this outcome entailed very high costs to the country. In spite of this, Argentina has apparently not learned the lesson that in order to increase the likelihood of success in international trade negotiations, it is crucial to draft a strategy and to have the capacity and strength to implement it. My argument in support of this statement comes from Doha. I have presented evidence supporting the argument that in contrast to other industrial and developing countries, Argentina participated in the Doha Ministerial Meeting ready to agree to any language for the agricultural negotiations or, for that matter, on any other topic. Its general stance has been and continues to be that any negotiation, irrespective of its outcome, is better than no negotiation. As long as the Government fails to develop a strategy, the country will continue to sign unbalanced negotiating outcomes and as a consequence, will sacrifice development opportunities.

Finally, the fact that agricultural protectionism in OECD countries remains irresponsibly high is a clear sign of the lack of coherence between the international trading system

[67] World Trade Organization, *Statement by India*, WT/MIN(01)/ST/10, (2001).
[68] WT/MIN(01)/17.

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and the international financial markets. This link has to be studied more carefully with the expectation that more precise and complete awareness of the financial costs of agricultural protectionism will add to the pressures for liberalizing OECD markets during the Doha Development Round. My concrete suggestion is to transform the Working Group on Trade, Finance and Debt into a negotiating group before the conclusion of this round.