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Global Trade Policy:

Made in Latin America?

Atlantic Council Policy Brief

Peter S. Rashish

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Foreword

This year is a pivotal moment for global trade policy. Two huge deals—namely the Trans-Pacific Partnership (TPP) and the Transatlantic Trade and Investment Partnership (TTIP)—have the potential to dramatically redefine the nature of the global economy. With the Doha Development Round stuck, these regional agreements offer the opportunity to greatly encourage inter-regional trade and investment and set high labor, environmental, and product safety standards. The United States, Europe, and Asia are major focal points for these ongoing negotiations, but Latin America is at the center of their convergence.

Progress toward integrating the trans-Pacific and transatlantic marketplaces has major implications for the trade, investment, and regulatory policies for all countries involved. However, in the absence of a concerted effort to ensure compatibility, there is a serious risk of setting up divergent trade regimes through TPP and TTIP. It is vital that governments and business leaders have an open dialogue to make sure that all four regions benefit.

This policy brief sets out a new framework for considering the Americas' position in global trade and makes the case that Latin America is at the heart of both the transatlantic and trans-Pacific negotiations. Most importantly, it puts forward specific policy recommendations that would ensure future cooperation to secure the best outcomes for all countries involved.

Over the course of the past year, the Atlantic Council has led a concerted effort to promote the economic and geostrategic benefits of an ambitious TTIP agreement for the United States and European Union. With this policy brief, we are launching a new effort looking at the interplay between TTIP and TPP, and the role of the Americas in either helping set new global rules or being forced to react and adapt to a changed environment.

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TPP and TTIP offer the opportunity to greatly encourage inter-regional trade and investment and set high labor, environmental, and product safety standards.

While the United States, Asia, and the European Union dominate the trade headlines, Latin America is where many of the most significant future moves on the global economic chessboard are likely to play out. This is especially true given select countries' relatively high integration into the world economy [See Figure 1].

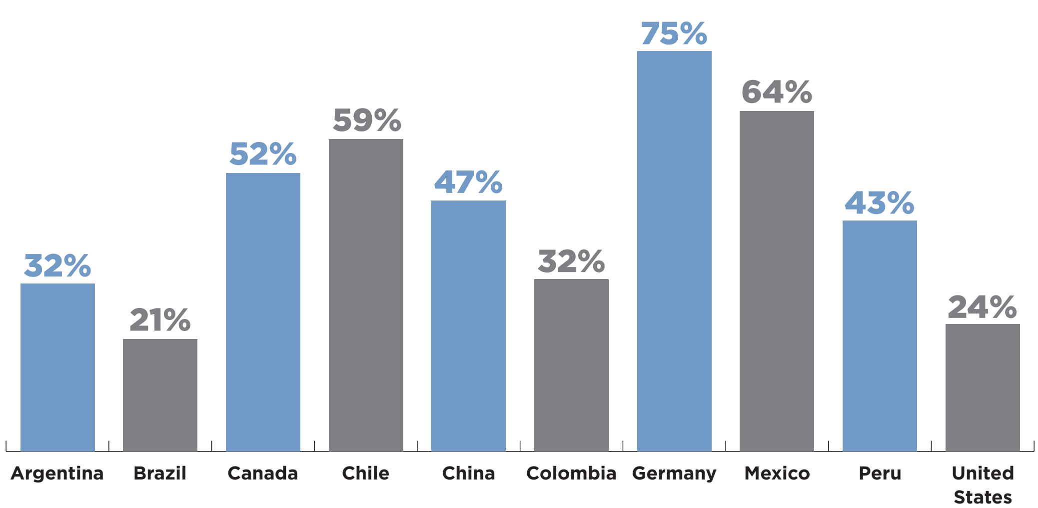
The choices that major economies within and beyond the region make in the coming years will be crucial factors in determining how Latin America will be integrated into the next wave of globalization. These changes will also help determine whether the high-standard, open, market-based approaches to trade promulgated by the United States and the European Union set standards that will one day become global in reach.

In the nearly ten years since the failure of the Free Trade Area of the Americas (FTAA), trade policy activism has undergone a shift in focus. While the Doha Round of talks in the World Trade Organization, launched in 2001, is grasping for achievements, two "mega-regional" deals that cover more than 60 percent of global GDP—the Trans-Pacific Partnership (TPP) and the Transatlantic Trade and Investment Partnership (TTIP)—stand a reasonably good chance of success.

If TPP and TTIP constitute grounds for optimism that trade policy is entering a new period of dynamism, how can Latin America leverage this evolution to greatest effect? And what is the role for the United States, the European Union, and Latin America—three regions that share strong political, historical, cultural, and economic ties—to forge a common trade policy agenda?

FIGURE 1. Select Latin American Countries Are Highly Integrated into the Global Economy

GLOBAL COMPARISON OF TRADE IN GOODS AS A PERCENTAGE OF GDP



Data Source: http://data.worldbank.org/indicator/TG.VAL.TOTL.GD.ZS

Mega-Regional Trade and the New Commerce Paradigm

Both TPP and TTIP are comprehensive, high-ambition projects that aim to go beyond simply improving market access for exports of goods and services. Often referred to as "twenty-first century" agreements, they dig deeper into domestic policies than previous deals. In addition to removing tariffs, each seeks to implement new levels of regulatory efficiencies, strong intellectual property rights, protections for international investors, and high labor and environmental protections.

Twelve countries from the Pacific Rim are taking part in the TPP talks, including three from Latin America.[1] TTIP is a bilateral negotiation between the United States and the European Union. Given the size and scope of these trade deals, and the absence of progress in the World Trade Organization (WTO), these two large trading blocs in the making are likely to create rules that will be adopted globally, as well as new supply and value chains that will spur higher levels of productivity and economic growth. As a result, outward-looking Latin American countries—both those participating in TPP negotiations and those who would be affected by the deal as non-signatory countries—are realizing their economic interests depend on embracing this global trade momentum.

Although no Latin American countries (or any other third-party countries) will participate in TTIP during the negotiation phase, ten countries (Chile, Colombia, Peru, Mexico, Guatemala, El Salvador, Honduras, Nicaragua, Costa Rica, and Panama) have free-trade agreements (FTAs) with both the United States and the European Union [SEE FIGURES 2 AND 3]. If the two TTIP partners

1 TPP negotiating countries include: Australia, Brunei, Chile, Canada, Japan, Malaysia, Mexico, New Zealand, Peru, Singapore, the United States, and Vietnam.

FIGURE 2.
US Free-Trade Agreements with Latin America

COUNTRY	DATE SIGNED	DATE ENTERED INTO FORCE
Chile	2003	2004
Colombia	2011	2012
Costa Rica	2004	2009
Dominican Republic	2004	2007
El Salvador	2004	2006
Guatemala	2004	2006
Honduras	2004	2006
Mexico	1992	1994
Nicaragua	2004	2006
Panama	2007	2012
Peru	2006	2009

FIGURE 3.
EU Free-Trade Agreements with Latin America

COUNTRY	DATE SIGNED	DATE ENTERED INTO FORCE
Chile	2002	2003
Colombia	2011	2013
Costa Rica	2012	2013
El Salvador	2012	2013
Guatemala	2012	2013
Honduras	2012	2013
Mexico	1997	2000–2001
Nicaragua	2012	2013
Panama	2012	2013
Peru	2011	2013

decide to open up the deal to other trading partners after its conclusion, several of these countries can be expected to attempt entering TTIP to preserve their privileged access to the transatlantic marketplace. But the next generation of provisions embedded within TTIP will be more ambitious than those already in place through existing FTAs. This is a challenge that can be overcome by introducing phase-in periods for obligations and benefits that take into account countries' different levels of institutional capacity.

Beyond TPP and TTIP, a third factor is leading to a rethink on trade: the region's declining terms of trade. From 2005 to 2011, with the exception of the low point of the financial crisis in 2009, Latin America recorded positive terms of trade. But the region's value of exports compared to its imports has declined in the last few years. The reasons are two-fold: slowing growth in key emerging markets and a fall in commodity prices.

Both of these trends are likely to continue over the medium term, forcing countries to shift from a reliance on mineral and raw materials exports to higher value-added products. This is influencing trade policy decision-making in countries with strong trading relationships in the Pacific basin (i.e., Chile and Peru), as well as those more oriented toward Europe (such as Brazil). China is the main concern. Almost 90 percent of Latin America's exports to China are in mining and agriculture, including 80 percent of Chile's copper exports. China is also the destination for 40 percent of Brazil's soybean exports. For both geographical and product diversification, Latin America is looking to vary its exports to China and to open up new export markets elsewhere. This new trade paradigm puts added pressure on select countries to ensure that they are positioned to capture the potential benefits of new mega-regional trade agreements.

Rule Maker or Rule Taker?

Latin America is at a crossroads as the two mega-regionals take over (at least temporarily) from the WTO as the main locus of trade policy innovation.

Will it be a rule maker or a rule taker? Will the region find a way to have a seat at the TPP and TTIP tables—either literally or through influence derived from parallel trade deals of its own inspiration? Or will it sit back and watch as new trade deals are negotiated?

Latin America may lack the geopolitical weight of the United States, the unity of purpose and political integration levels of the EU, and the tradition of pragmatic intra-regional trade experimentation of Asia. But the region is largely comprised of fast-growing democracies that will be sought-after partners for the next phase of trade policy activism.

Mexico, for example, is already assuming a leading role on the world trade stage. The region's second-largest economy is an early adopter of FTAs and well integrated into the North American value chain through the North American Free Trade Agreement (NAFTA) that it joined in 1994. Forty percent of US imports from Mexico consist of content originally made in the United States.

In addition to NAFTA, Mexico has signed numerous FTAs over the last twenty-five years: the EU (1997), Japan (2004), ten countries in Latin America, and several others. Today, 90 percent of Mexico's trade is covered by its FTAs. Merchandise trade

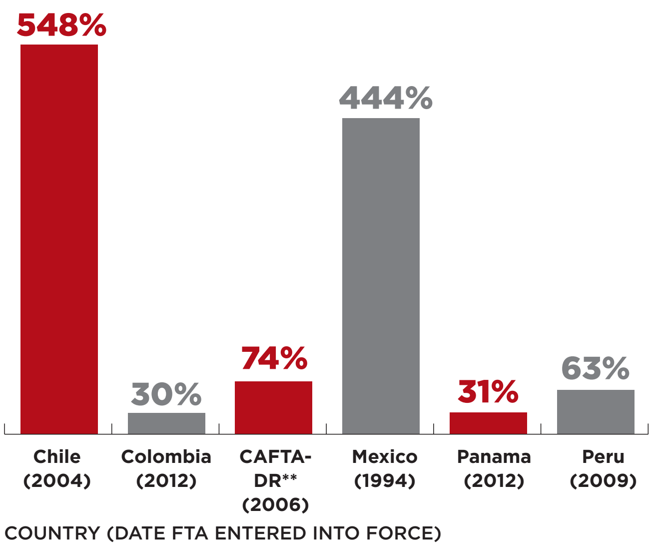
Latin America is largely comprised of democracies that will be sought-after partners for the next phase of trade policy activism.

accounts for 68 percent of Mexico's GDP—much larger than that of China and one of the highest shares in the world among large economies. At the same time, in Mexico, as with other free-trade partners throughout Latin America, US exports have increased significantly since FTA implementation [SEE FIGURE 4].

As a member of TPP, with existing trade deals with the United States, Canada, and the EU, Mexico is a powerful example of global commerce potential when a government is determined to be at the forefront of trade policy engagement.

FIGURE 4. Latin American FTAs Yield Increased US Exports

INCREASE IN US GOODS EXPORTS TO FTA PARTNERS SINCE AGREEMENT IMPLEMENTATION*



*The percentage increase was calculated using data from one year prior to the agreement being implemented.

**CAFTA-DR includes: Costa Rica, El Salvador, Guatemala, Honduras, Nicaragua, and the Dominican Republic. The agreement entered into force for the United States, El Salvador, Guatemala, Honduras, and Nicaragua in 2006, for the Dominican Republic in 2007, and for Costa Rica in 2009.

Data Sources: http://www.census.gov/foreign-trade/balance and http://export.gov/FTA/index.asp

The Pacific Alliance: Trade Policy Leadership "Made in Latin America"

Beyond Mexico's success, the Pacific Alliance is reason to be optimistic that select Latin American countries can play a leadership role in the newly emerging constellation of trade policy. Founded in 2012 by Chile, Colombia, Mexico, and Peru, the Alliance is a trade bloc in which members are also taking incremental steps toward greater economic and diplomatic integration. The fast-growing members of the Alliance have a combined GDP of $3 trillion and account for more than half of all Latin American trade. The Alliance is also globally integrated; members have FTAs with countries representing almost 75 percent of the world economy.

Several aspects of the Pacific Alliance make it poised to play a significant role in regional and global trade. Alliance countries are outward-looking in their trade policy and are strong democracies with market-oriented economies. These attributes make them obvious partners in plurilateral and multilateral trade fora for the United States and the European Union. For example, the four Alliance members are among the fifty countries participating in the Trade in Services Agreement (TiSA) talks launched in March 2013 in Geneva.

The Pacific Alliance is also open to expansion—Costa Rica and Panama are poised to join soon, and an additional thirty countries have observer status, including the United States, China, India, Japan, and Turkey. This power of attraction is a political currency that the Alliance countries can stock and spend to influence the direction of global trade policy in talks such as the TPP.

The EU is Mercosur's single-largest trading partner, accounting for 20 percent of its exports and imports. Thirty-five percent of its EU-bound exports are in higher value-added products.

Brazil: An Awakening Trade Policy Giant?

Until now, Latin America's largest economy, Brazil, has not been able—or has not wanted—to translate its status as a regional superpower into trade policy leadership. Although it is normal for large countries with domestic economies of scale to be less globally integrated than smaller economies, Brazil (at 21 percent) has the lowest amount of merchandise trade in overall GDP of any economy globally. It is also absent from key global value chains: only 3 percent of Brazilian exports to the United States include US content, less than one-tenth of the Mexican level.

Brazil has around the same number of FTAs in force as Mexico. However, only one of Brazil's FTAs is with a country outside Latin America (Israel), while Mexico has entered into non-Latin American agreements with Canada, the EU, Israel, Japan, and the United States. This means Brazil has no trade or integration agreement in force with North America, the EU, or Asia—the world's three largest economic regions and the most important in terms of trade policy innovation. As a member of Mercosur, Brazil has signed FTAs with Egypt, the Palestinian Authority, and the Southern African Customs Union, though each are pending ratification.[2]

Brazil also lacks trade policy autonomy. All trade agreements must be negotiated and concluded together with its Mercosur partners (Argentina, Paraguay, Uruguay, and Venezuela).

Politically, Brazil has traditionally defined its global role through leadership within the multilateral trading system represented by the WTO and through the BRICS (Brazil, Russia, India, China, and South Africa)—the informal grouping of large emerging economies that, like Brazil, lacks FTAs with key trading partners.

There are signs, however, that Brazil is reassessing its position within global trade politics. Most telling is the energy Brazil has put into reviving the trade pillar of the negotiations toward an EU-Mercosur Association Agreement. The talks have moved forward fitfully for fifteen years. But technical meetings were held between the two sides in March 2014, and the parties are likely to exchange tariff proposals by mid-2014. In April 2014, Brazil confirmed that the joint tariff-reduction proposal to the EU will cover 90 percent of bilateral trade. This comes after Argentina's decision to be more flexible in a number of product areas.

The EU is Mercosur's single-largest trading partner, accounting for 20 percent of its exports and imports. Compared to Asia, where Mercosur's trade is largely commodity-based, 35 percent of its EU-bound exports are in higher value-added products. The sophistication of the EU-Mercosur economic relationship is shown by the relative weight that investment plays into its commerce: Mercosur and the EU exchanged $182 billion in goods and services in 2011, the last year for which comprehensive figures are available. The stock of FDI that year stood at over $500 billion, with $400 billion going from the EU to Mercosur, and more than $115 billion from Mercosur to the EU.

2 Brazil, through Mercosur, also has a preferential trade agreement in force with India that represents an important step toward a full-fledged free-trade area.

The United States and the European Union will drive forward their own vision of trade liberalization by pursuing more effective global economic governance with like-minded Latin American allies.

Bridging the Atlantic—North and South

Latin America is already participating to a certain degree in the new global trade dynamics that are privileging FTAs over the WTO as the framework for liberalization and integration. Mexico is a founding member of NAFTA. Chile, Mexico, and Peru are members of the TPP negotiations. The four Pacific Alliance countries are creating their own momentum in the region, establishing a free market that accounts for 35 percent of Latin America's GDP. Brazil is laboring to get its Mercosur partners to conclude talks with the EU. Even Ecuador, a member of the Hugo Chávez-inspired Bolivarian Alliance for the Peoples of Our America bloc, has begun exploring an FTA with the EU.

Can Latin America bring to bear enough policy muscle to forge its trade destiny alone? Or would finding common ground with the United States and the European Union—with which it shares a strong cultural, historical, political, and economic heritage—provide a faster track to achieving its objectives? Latin American economies' participation in TPP, while necessary, will not be sufficient to propel the region into trade policy's leading ranks. Given the nature of its trade and investment flows, and its political interests, Latin America also needs to play a part in the North American and European economic and trade spheres. At the same time, the United States and the European Union will drive forward their own vision of trade liberalization by setting high regulatory standards and pursuing more effective global economic governance with like-minded Latin American allies.

The countries with the deepest economic integration levels with the United States and the EU—Canada, Mexico, Switzerland, Iceland, Liechtenstein, Norway, and Turkey—are watching and in some cases advocating for their interests in TTIP. A number of Latin American economies that have FTAs with the United States and the EU may begin to do the same. They will have a particular interest, for instance, in the outcome of TTIP negotiations on regulatory convergence. The United States and EU are likely to recognize mutual safety certifications and testing procedures for sectors like automobiles and pharmaceuticals to create a one-stop shop for regulatory approvals. How will they treat third-party countries? Will they also find regulatory mechanisms to facilitate the movements of products from non-TTIP trading partners within the US-EU economic space?

Policy Recommendations

This policy brief has shown that the United States and Europe would each reap significant gains through enhanced economic cooperation with Latin America. Here are nine concrete steps that policymakers can take to ensure that TPP and TTIP help contribute to a broader level of international economic cooperation.

1 If the United States and the EU decide to allow other countries to dock onto TTIP once concluded, they should include their largest Americas FTA partners—Canada and the four Pacific Alliance countries—among the priority candidates.

2 Forward movement in the EU-Mercosur free-trade negotiations, especially Mercosur's decision to propose new tariff reductions, should reignite the long-delayed discussions with the United States for a US-Mercosur FTA.

3 A formal NAFTA review process should be launched that is focused on the potential benefits of enlarging its membership to include the Pacific Alliance.

4 Once TTIP is concluded, the United States, EU, Canada, and the four Pacific Alliance countries will all have FTAs with each other and should consider adopting common approaches to rules of origin as well as so-called "diagonal" cumulation in order to facilitate trade.

5 The like-minded countries of the EU, NAFTA, and the Pacific Alliance should coordinate their positions within the Doha Round, the Trade in Services Agreement, and any future plurilateral or multilateral trade talks.

6 Given that 56 percent of merchandise trade is in intermediate products, seven countries/blocs including the United States, EU, Canada, and the four Pacific Alliance countries should create a new "Global Value Chain (GVC) 7." The GVC7 would promote the inclusion in future trade negotiations of ideas to enable efficient global value chain operations.

7 The United States and the EU should explore making mutual recognition agreements in TTIP open to Latin American countries who can comply with either the US or the EU standard, whichever is least onerous to their existing regulatory regimes.

8 As investment increasingly drives trade, the United States, the EU, and the Pacific Alliance should create a common benchmark for investor protection by aligning and modernizing the investor-state and state-to-state dispute settlement procedures in their FTAs with one another.

9 TPP should be concluded by 2015. If not, the United States, Canada, and the Pacific Alliance should explore options for regional agreements with individual countries or smaller groups in the Asia-Pacific region, such as Japan, Australia, New Zealand, and ASEAN. Such agreements could be concluded quickly among like-minded partners.

If most of these steps are taken, Latin America has the potential to become a lynchpin of a new multipolar global trade constellation. This is true on an East-West axis considering Latin America's role within the Asia-Pacific sphere, and on a North-South axis with deeper hemispheric integration and stronger EU-Latin America trade links on the horizon. Latin America's leading economies will have cemented their Pacific vocation through TPP and the Pacific Alliance, found a role in the new transatlantic marketplace of TTIP, and even crafted a partial, more flexible, less politically charged successor to the Free Trade Area of the Americas via NAFTA and future FTAs with the United States.

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