FTAA in Perspective: North-South and South-South Agreements in the Western Hemispheric Countries

Inter-American Development Bank

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Evolution of Regionalism in the Western Hemisphere

The second wave of regionalism has gained momentum in the Western Hemisphere

- **Renewal of LAC’s Old Regional Initiatives**
  - LAFTA → LAIA
  - Andean Community
  - Central American Common Market (CACM)
  - Caribbean Community and Common Market (CARICOM)

- **Creation of New Trade Blocs**
  - NAFTA
  - MERCOSUR
  - FTAA
  - MERCOSUR-EU
Policy Questions/Objectives of the Study

• What is the potential impact of the respective integration options for hemispheric members?

• What pattern of structural transformation does each country or regional bloc undergo?

• How different is the North-South approach in comparison with the South-South arrangement?

• What is the role of Latin America in the FTAA for the respective LAC’s members?
Main Features of the CGE Model (I)

**Model:** Multi-region, multi-sector, comparative static

**Production Sectors:** Constant Elasticity of Substitution (CES)

**Demand:**
- Final Demand: Utility Maximization by Household
- Intermediates: Fixed Input-Output Coefficients

**Trade:** Imperfect substitution
- Exports: Constant Elasticity of Transformation (CET)
- Imports: Constant Elasticity of Substitution (CES)

**Factors:**
- Land
- Capital
- Labor

**Base Year:** 1997
Main Features of the CGE Model (II)

• **Trade-linked Externalities:** Melo and Robinson (1992)
  * Sectoral Export Externality
    \[ SAD_i^k = \left( \frac{EK_i^k}{EK_{0i}^k} \right)^{\eta_k^k} \]
  * Import Externality of Capital and Intermediate Goods
    \[ SAD2_i^k = n_i \cdot \left( \frac{MTOT_i^k}{MTOT_{0i}^k} \right)^{\eta_{m_k^k}} + (1 - n_i) \]
  * Aggregate Export Externality
    \[ SAC^k = \left( \frac{ETOT_i^k}{ETOT_{0i}^k} \right)^{\eta_{k^k}} \]

• **Scale Economies:** Melo and Tarr (1992)
  * Contestable Markets for Manufacturing Industries
### Sectors in the CGE Model

<table>
<thead>
<tr>
<th>Primary Sectors</th>
<th>Heavy Manufactures</th>
</tr>
</thead>
<tbody>
<tr>
<td>Grains</td>
<td>Petroleum and Chemicals</td>
</tr>
<tr>
<td>Vegetables, Oilseeds &amp; Soybeans</td>
<td>Iron and Steel</td>
</tr>
<tr>
<td>Sugarcane &amp; Other Crops</td>
<td>Automobiles and Parts</td>
</tr>
<tr>
<td>Livestock</td>
<td>Machinery and Equipment</td>
</tr>
<tr>
<td>Mining</td>
<td></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Light Manufactures</th>
<th>Services</th>
</tr>
</thead>
<tbody>
<tr>
<td>Meat Products</td>
<td>Utilities and Construction</td>
</tr>
<tr>
<td>Processed Foods</td>
<td>Trade and Services</td>
</tr>
<tr>
<td>Textiles and Apparel</td>
<td></td>
</tr>
<tr>
<td>Other Light Manufactures</td>
<td></td>
</tr>
</tbody>
</table>
Regions in the CGE Model

- Canada
- United States
- Mexico
- Central America and the Caribbean
- Colombia
- Venezuela
- Rest of the Andean Community
- Argentina
- Brazil
- Chile
- European Union
- Rest of the World (ROW)
Exports by Major Partner

Source: FTAA Hemispheric Database, IDB.
Imports by Major Partner

Source: FTAA Hemispheric Database, IDB.
MFN Ad Valorem Tariffs by Major Partner

Source: FTAA Hemispheric Database, IDB.
Notes: 1997.
Allocation of Domestic Support

Source: OECD PSE.
Notes: 1997.
Allocation of Export Subsidies

Source: WTO Notifications.
Notes: 1997.
Regional Agreements in the Model

- **Regional Agreements**
  - NAFTA
  - CACM and CARICOM
  - Andean Community
  - MERCOSUR
  - G-3 (Mexico, Colombia & Venezuela)
  - EU

- ** Preferential Agreements**
  - Caribbean Basin Initiative (CBI)
  - Andean Trade Preferential Act (ATPA)
  - MERCOSUR-Chile
  - Chile-Canada
  - Mexico-Chile

Source: FTAA Hemispheric Database, IDB.
**Alternative Scenarios for Latin America**

<table>
<thead>
<tr>
<th>Scenarios</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. South American Free Trade Area (SAFTA)</td>
</tr>
<tr>
<td>2. AC-US FTA</td>
</tr>
<tr>
<td>3. MERCOSUR-US FTA</td>
</tr>
<tr>
<td>4. AC-EU FTA</td>
</tr>
<tr>
<td>5. MERCOSUR-EU FTA</td>
</tr>
<tr>
<td>6. FTAA</td>
</tr>
</tbody>
</table>
## Impact on GDP by Scenario

<table>
<thead>
<tr>
<th></th>
<th>1</th>
<th>2</th>
<th>3</th>
<th>4</th>
<th>5</th>
<th>6</th>
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</thead>
<tbody>
<tr>
<td>Country</td>
<td>SAFTA</td>
<td>AC-US</td>
<td>MERC.</td>
<td>AC-EU</td>
<td>MERC.</td>
<td>FTAA</td>
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<tr>
<td>Canada</td>
<td>0.00</td>
<td>-0.01</td>
<td>0.02</td>
<td>0.02</td>
<td>0.04</td>
<td>0.57</td>
</tr>
<tr>
<td>United States</td>
<td>0.00</td>
<td>0.15</td>
<td>0.20</td>
<td>0.02</td>
<td>0.03</td>
<td>0.35</td>
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<tr>
<td>Mexico</td>
<td>0.00</td>
<td>-0.05</td>
<td>-0.02</td>
<td>0.01</td>
<td>0.03</td>
<td>1.02</td>
</tr>
<tr>
<td>Central America</td>
<td>-0.01</td>
<td>-0.07</td>
<td>0.00</td>
<td>0.01</td>
<td>0.04</td>
<td>2.22</td>
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<tr>
<td>Colombia</td>
<td>0.28</td>
<td>0.92</td>
<td>0.02</td>
<td>0.95</td>
<td>0.05</td>
<td>1.32</td>
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<tr>
<td>Venezuela</td>
<td>0.37</td>
<td>1.40</td>
<td>0.03</td>
<td>0.59</td>
<td>0.10</td>
<td>2.08</td>
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<tr>
<td>Rest of AC</td>
<td>1.21</td>
<td>1.78</td>
<td>0.07</td>
<td>1.84</td>
<td>0.21</td>
<td>2.98</td>
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<tr>
<td>Argentina</td>
<td>0.61</td>
<td>0.00</td>
<td>1.59</td>
<td>0.46</td>
<td>4.20</td>
<td>2.49</td>
</tr>
<tr>
<td>Brazil</td>
<td>0.46</td>
<td>-0.01</td>
<td>2.59</td>
<td>0.37</td>
<td>4.94</td>
<td>3.39</td>
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<tr>
<td>Chile</td>
<td>1.14</td>
<td>-0.01</td>
<td>0.00</td>
<td>0.04</td>
<td>0.11</td>
<td>2.84</td>
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<tr>
<td>Latin America</td>
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<td>0.17</td>
<td>1.34</td>
<td>0.39</td>
<td>2.78</td>
<td>2.52</td>
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<tr>
<td>European Union</td>
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<td>0.00</td>
<td>0.00</td>
<td>0.51</td>
<td>0.61</td>
<td>-0.01</td>
</tr>
</tbody>
</table>
Impact on Exports by Sector:
Andean Community

Scenario 2:
AC_US FTA

Scenario 4:
AC-EU FTA

% Change
Primary
Light Manufactures
Heavy Manufactures
Total
Impact on Exports by Sector: MERCOSUR

Scenario 3: MERCOSUR-US FTA
Scenario 5: MERCOSUR-EU FTA

% Change

Primary
Light Manufactures
Heavy Manufactures
Total
Impact of FTAA on Exports of Latin American Countries

% Change

- Primary
- Light Manufactures
- Heavy Manufactures
- Total

Mexico, Central America, Colombia, Venezuela, Rest of AC, Argentina, Brazil, Chile
Increased Exports to Hemispheric Market by Sector: FTAA

The chart above illustrates the share of exports by sector for various countries in the context of the FTA Agreement (FTAA). The sectors are categorized into Primary, Light Manufactures, and Heavy Manufactures. The chart compares the export shares for countries such as Mexico, Central America, Colombia, Venezuela, Rest of AC, Argentina, Brazil, and Chile.
Share of Latin America in Exports to the Hemispheric Market: FTAA

- **Primary**
- **Light Manufactures**
- **Heavy Manufactures**
Summary and Conclusions

* SAFTA generates modest gains, but can be superior to the North-South arrangement in terms of specialization of high value-added exports.

* The North-South integration has sectorally differentiated impact on Latin America, depending on partners.

* FTAA is the best option for hemispheric partners except MERCOSUR, for which integration with the EU is more preferable.

* In the FTAA scenario, Latin America absorbs some 50 percent of the increased exports to the FTAA market. The presence of LAC contributes to increase exports of non-resource-based exports.