

Latin America in the global economy

Advancing market access



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Editors:

Division of Economic Studies.
Vice-presidency of Development Strategies of the
Corporación Andina de Fomento (CAF).
desarrollo@caf.com

Coordination and editorial production:

Secretary and Corporate Communications Direction.
Publications Unit of CAF.
Phone: (58 212) 209.2249 - Fax: 209.2211
publicaciones@caf.com

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Foreword

Enrique García

Executive President and CEO - Corporación Andina de Fomento

Deepening the participation of Latin American economies in international trade is a key component of a development agenda for resuming quality, sustainable and inclusive economic growth. Most countries of the region are currently undertaking efforts to foster closer trade links with the rest of the world, mitigate the risks inherent to trade liberalization, and include all segments of society in the benefits of broader trade openness.

Although during the last two decades Latin America has significantly opened its markets to international trade, its relative share has fallen systematically and now represents less than half of what it was 40 years ago. In contrast, the weight of other economies in world trade has grown dramatically, especially that of China and East Asia.

The declining regional presence in world trade is partly due to the low productivity that characterizes the countries of the region, a factor that limits the competitiveness of the Latin American export basket. In this respect, there is a clear need to link the trade agenda with the adoption of a set of policies and domestic reforms aimed at raising the quality of participation in global markets through improvements in productivity.

It is also essential to reduce - and eventually eliminate - trade and physical barriers that still hinder the access of Latin America to export markets. In this regard, it is critical to make coherent use of the various trade agreements that suit the specificities of the economies of the region, their comparative advantages and the balance of their individual interests.

Although there are important complementarities between the different forms of international trade participation - whether multilateral, bilateral or regional - for each country there will be a specific correspondence between the need for increased trade liberalization and the different alternatives available. The best use of the various aspects of trade negotiations also require that they constantly adapt to the changing conditions of international trade, and that they stay in tune with the progress made in specific areas.

Given its commitment to the design and execution of a renewed development agenda for Latin America, CAF supports the region in its objective of achieving increased and more equitable access to world markets. This publication offers a contribution to the public policy debate on this issue by examining relevant aspects of the international trade agenda.

The complex web of spheres of international trade participation that countries have available is illustrated throughout this book, identifying the trade barriers that limit the free flow of goods and services, and evidencing the impact that trade agreements may have on economic and social variables. The book also analyses how the region can exploit more effectively the increased participation of China in international trade, and emphasizes the critical aspects of the trade negotiations on particularly sensitive issues, such as a liberalization of the agriculture and service sectors, intellectual property right protection and trade facilitation.

Our hope is that this book will contribute to stimulating the debate and guide the implementation of public policies in the effort to achieve greater access to international markets and promote economic growth, with the ultimate purpose of improving the quality of life of all Latin Americans.

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Academic advisors of this project were Miguel Rodríguez Mendoza and Pablo Sanguinetti.

The main authors are:

Chapter 1	<i>Luis Miguel Castilla</i>
Chapter 2	<i>Miguel Rodríguez Mendoza</i>
Chapter 3	<i>Stefania Scandizzo</i>
Chapter 4	<i>José Pineda</i>
Chapter 5	<i>José Pineda</i>
Chapter 6	<i>Luis Miguel Castilla and Federico Ortega</i>
Chapter 7	<i>José Pineda</i>
Chapter 8	<i>Cristina Fernández</i>
Chapter 9	<i>Stefania Scandizzo</i>
Chapter 10	<i>José Pineda</i>

Osmel Manzano provided contributions to chapter 1.
Maritza Hidalgo was in charge of the book's final edition.

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Research assistants were Jennifer Arencibia, José Herrera, Ricardo Isea, María Caridad Ortiz, Federico Ortega, Andrea Otero, Mariana Penzini and Javier Pérez.

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Toward a coherent strategy for increasing participation in global markets

Introduction

Increasing participation of Latin American economies in world trade constitutes, without doubt, a key component of a development agenda that seeks to achieve quality economic growth, that is both sustainable and inclusive. Toward this end, the 2004 edition of the Report on Economics and Development presented a set of proposals that emphasized the potential of greater participation in the global economy, that would mitigate the inherent risks of such participation and that would provide, at the same time, the inclusion of all segments of society. As a fundamental element of this thinking, a more efficient access to international markets was proposed, via a change in productive patterns aimed at raising the economies' total productivity.

Such a change, however, should be promoted together with the strategic enlargement of access to global markets and an increase in the process of trade openness with which the region is committed since the 1980s, following the world-trend toward trade liberalization. Within the GATT¹ framework, industrialized countries have significantly reduced their tariffs and have eliminated a large part of their non-tariff barriers. Developing countries, including Latin America, have undertaken important reforms

in this area, abandoning protectionist policies in favor of export promotion in an environment of unambiguous openness to trade.

In general, the world-wide process toward trade liberalization has resulted in stronger economic links among countries, which are every day closer to each other thanks to the flows of goods and services, of capital and even of immigrants. World exports, as a percent of world GDP, have doubled in the past 40 years and almost half of this growth has occurred in the last decade. In the specific case of Latin America results have also been clear, and the region's international trade has grown in a significant and accelerated manner after the reforms undertaken in the 1980s.

In spite of this, and of country efforts to consolidate trade openness, regional participation in world trade has diminished, a fact that should be a red flag for policy-makers. In fact, as shown in Figure 1.2, while the relative participation of China and East Asia has grown, that of Latin America has decreased and is today smaller than that of these two regions, representing less than half of its participation forty years ago. Even though some Latin

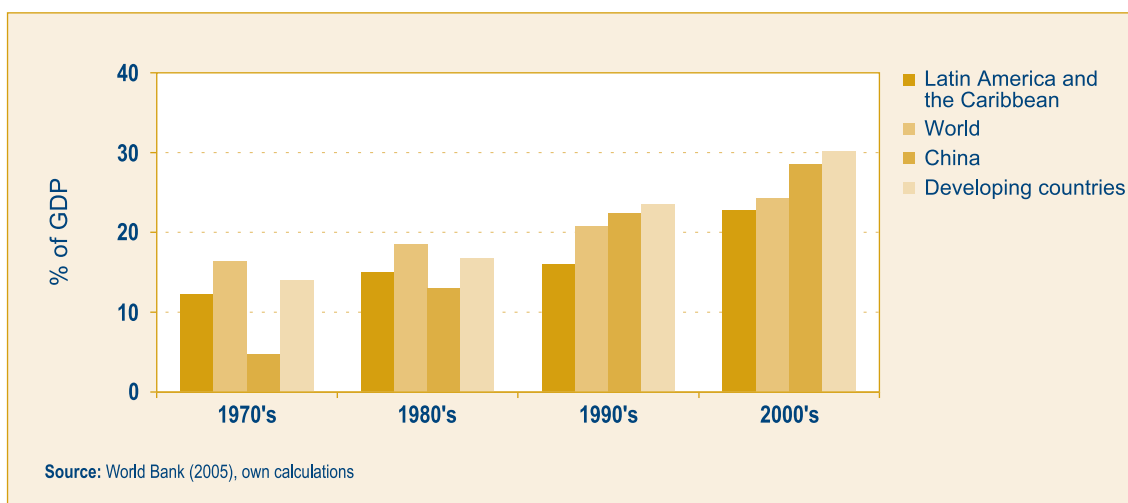


Figure 1.1
Exports performance

¹ GATT: Global Agreement on Tariffs and Trade.

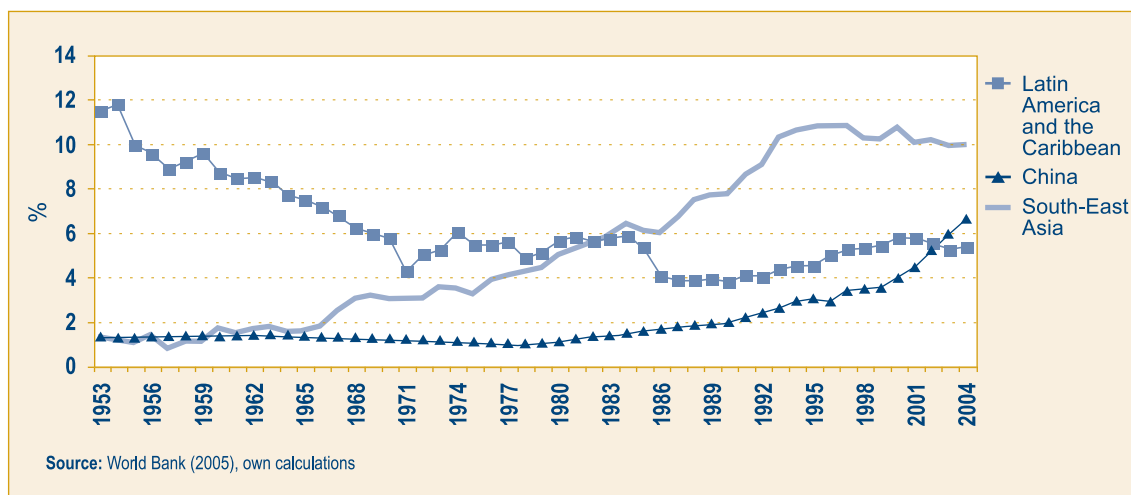
American countries –such as Mexico, Chile and the Dominican Republic– have successfully managed to increase their participation in world trade, the region as a whole shows an important gap with respect to the rest of the world. Latin America therefore faces the challenge of reversing this trend and of beginning to pursue wider and more secure markets for its exports, with the objective of resuming a leading role in the international arena and, finally, of promoting the growth of its countries and the welfare of its people. This objective requires, of course, a carefully designed trade strategy, whose fundamental elements constitute the core of this book, as will be seen in the coming chapters.

It is important to underscore, however, that increased market access is neither the only nor the most important challenge faced by the countries of the region. Equally urgent and possibly even more important, is the attention and commitment of sizeable efforts to improve internal productivity, whose benefits translate, without doubt, into greater exporting potential for these countries, providing competitiveness and opening new opportunities. It therefore appears necessary to link the trade agenda of Latin American countries with the introduction of economic policies and reforms aimed at improving internal productive efficiency and the quality of participation in global markets. This must be complemented, of course, with a policy agenda to strengthen infrastructure and logistic platforms, to attract foreign direct investment and that includes export promotion measures.

The evolution of Latin American foreign trade, as discussed above, has occurred in a context of radical change in the geography of global trade, due largely to the emergence of China and India as powerhouses in the trade of goods and services, respectively. In the first case, with China's entry to the World Trade Organization (WTO) in 2001, manufactured products from this country began an aggressive penetration of main industrialized markets, competing with the supply of other developing countries with similar comparative advantages. This is a reflection of the significant degree of trade openness achieved by the Chinese economy, whose international trade has grown seventeen-fold in the same period, capturing an important percentage of world trade (4.8% of world trade in average, for the period of 2001-2003).

In the case of India, exports of services grew, during the nineties, at an annual rate of 15% in dollar terms, compared with 9% during the eighties. Cumulative exports of services increased four-fold in the nineties. According to Salgado (2003), in 2001 India was responsible for close to 1.3% of world service exports, a considerably dynamic sector, basically due to the growth of telecommunications, financial, business and community services². Even though the high elasticity of the demand for services, and the increased use of these as intermediate inputs, were important factors in propelling the growth of services in the nineties, several supply-side elements such as reforms, technological

Figure 1.2
Share on
world exports



² Gordon and Gupta (2003).

advances and labor skill upgrades also played a fundamental role³.

The region's performance is clearly far from that registered by emerging economies such as those mentioned above, and has exhibited a sustained loss of relative weight in world trade, as has been already stated. However, to understand this drop it is necessary to closely examine the patterns that have characterized the region's trade in recent times, in the context of the dynamics of world trade flows. By doing this, one will obtain a perspective of Latin America's decrease in importance in world trade, and acquire a vision of why economies such as China, which will be considered in Chapter 6, have flourished in the international arena, generating important impacts on the region.

Trade patterns in goods

In a study commissioned for this book, Zignago (2005) reviews factors that explain the relative performance of the region in light of the dynamics of world trade. According to this study, the region's trade flows have essentially been affected by demand factors in the region's export markets –i.e., by the general demand conditions of export markets– and by demand factors of export products –i.e. the dynamics of world demand for specific products exported by the region. The study also argues that in the face of, for example, reduced global export demand, countries could adopt measures such as greater diversification of trade partners (geographical adaptation), as well as of the types of products exported (sectoral adaptation). Accordingly, changes in country (or regional) participation in world exports, not explained by demand or adaptation variations, are assumed to reflect changes in countries' competitive positions⁴.

Table 1.1 shows evidence of the fall in Latin American participation in world trade, as already discussed, and shows the aforementioned decomposition of export changes in demand changes associated respectively with markets and products. In this table one observes how, while Latin America

experienced a slight loss in its participation between 1995 and 2002, other developing countries, such as those of Eastern Europe or Asia, increased it by 31.4% and 22.3%, respectively. From the point of view of demand factors, Latin America and the Eastern European countries benefited moderately, during this period, from demand growth in their trading partners.

At the same time, however, all regions considered in this study (with the exception of some specific countries) faced significant contractions in international demand for their products, especially in the case of Latin America and Africa. In the specific case of Latin America, the table shows how, notwithstanding important gains in competitiveness during the period under consideration (1995-2002), these were lower than those observed in Eastern Europe and Asia, and were not capable of compensating the losses generated by demand effects. This has resulted in the observed reduction in the relative weight of Latin American exports and the unequivocal conclusion for the need, not only of widening markets, but also of decisively promoting reforms to improve countries' productivity.

The review of specific cases highlights interesting differences between countries. Even though most countries have obtained competitiveness gains, diluted in part by negative demand effects, there are success stories of countries that undertook important reforms of their productive systems; others sought trade agreements to improve access to trade partners' markets, as was the case of Mexico with the North American Free Trade Agreement (NAFTA). In this case, experience seems to show that it is not possible to indefinitely sustain greater trade participation with strategies based exclusively on trade agreements to increase market access. In fact countries that were early reformers, such as Chile, South Korea and Taiwan, consolidated larger gains through adaptation, by diversifying markets or products.

Regarding the sectoral composition of trade in goods, one observes that manufactured products are the

³ According to a management survey undertaken by A.T. Kearney (2004), the two main characteristics that attract international investment to India are labor qualification and management skills.

⁴ In other words, according to Zignago's (2005) methodology, the changes in a country's competitive position are calculated as residuals.

Table 1.1 Decomposition of global exports market share growth (1995-2002)

	Growth in market share	Demand effects		Total	Adaptation		Competitiveness
		Geographical	Sectoral		Geographical	Sectoral	
	1	2	3	4 = 1-2-3	5	6	7 = 4-5-6
Developed countries	-5.2	-0.6	-1.4	-3.2	-1.6	-0.1	-1.5
CEEC-Turkey	31.4	0.9	-11.2	41.7	-4.1	1.0	44.8
Africa and Middle East	-21.5	-1.2	-22.7	2.4	-4.1	-3.4	9.9
Developing Asia	22.3	-6.7	-12.4	41.4	-0.4	1.2	40.6
China	59.0	-10.9	-6.2	76.1	0.1	1.8	74.2
South Korea	8.6	-3.2	-0.6	12.4	2.7	1.8	7.9
India	13.4	-4.7	-12.0	30.1	-0.2	0.4	29.9
Taiwan	-6.4	-1.4	-0.1	-4.9	4.2	0.7	-9.8
Latin America	-0.9	1.3	-20.1	17.9	-1.3	0.7	18.5
Argentina	-11.0	-8.6	-11.8	9.4	0.8	0.4	8.2
Bolivia	-6.9	-9.1	-14.0	16.2	-1.4	2.0	15.6
Brazil	-2.4	-6.1	-13.1	16.8	3.8	1.4	11.6
Chile	-3.2	-5.2	-14.7	16.7	6.1	1.5	9.1
Colombia	-16.1	3.8	-10.0	-9.9	-0.5	1.3	-10.7
Costa Rica	20.9	6.7	-15.9	30.1	-0.9	-10.3	41.3
Ecuador	-21.9	1.3	-7.8	-15.4	-5.6	-0.2	-9.6
Mexico	70.8	5.3	4.5	61.0	-2.7	0.5	63.2
Peru	11.9	2.7	-16.3	25.5	-3.0	-3.7	32.2
Venezuela	-18.0	3.5	7.5	-29.0	-0.5	-2.6	-25.9

Source: Zignago (2005)

most dynamic. In fact, trade in manufactured goods has been gaining ground in total world trade and, from representing close to half of the total goods' trade at the beginning of the 1960s, now represents close to 80%. On their part, the more dynamic emerging economies have been gaining ground in the world market for manufactured goods, at the expense of other developing economies. For example, countries such as China and the economies of South East Asia have exhibited important growth in the participation of manufacturing products in their exports. Latin America, on its part, shows a more modest growth, led mainly by Mexican exports.

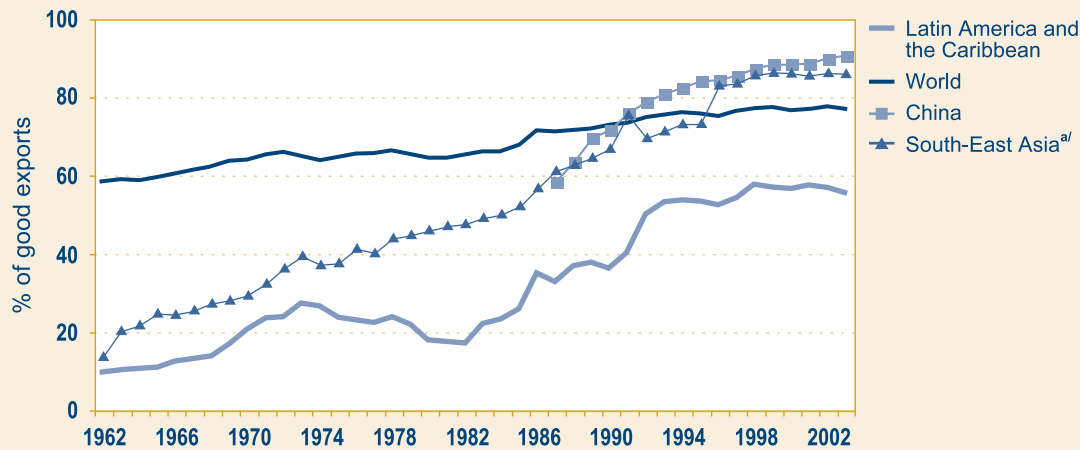
These trade patterns reflect countries' comparative advantages. Figure 1.4 shows an estimation of

these, using the Balassa⁵ index. Comparing today's comparative advantages with those of thirty years ago, one can appreciate how these have not changed. The fact that Latin America has lost market participation in manufactured goods reflects the region's resource endowment, i.e. its relative abundance in natural resources, and its failure, with some exceptions, to use such resources to significantly move up the value added chain. In this sense, one should point out that successful cases such as those of Chile and the Dominican Republic⁶ show that the region is capable of successfully penetrating the most dynamic markets through value aggregation strategies and the diversification of production based on resources that exhibit relevant comparative advantages.

⁵ This index is obtained according to the trade pattern of the region with respect to the rest of the world. If the index is greater than one, it indicates that the region has a comparative advantage in the category of goods. On the other hand, if the index is less than one, the region does not have a comparative advantage.

⁶ Chile, for example continues to present the same comparative advantages of 30 years ago. In fact, it still presents a very low proportion of intra-industry trade. According to Fundación Chile (2005), the Chilean strategy has consisted in adding value to said advantages through quality improvements and the international promotion of its products (wines, new varieties of fruit, salmon), reorganizing sectors (based on its forestry wealth, Chile began specializing in paper and other wood products) and the introduction of technology (the development of sectors that provide services to traditional Chilean primary sectors). The Dominican Republic is a similar example, where what has pushed forward the growth of service exports has been the development of tourism. That is another case of exploitation of a comparative advantage.

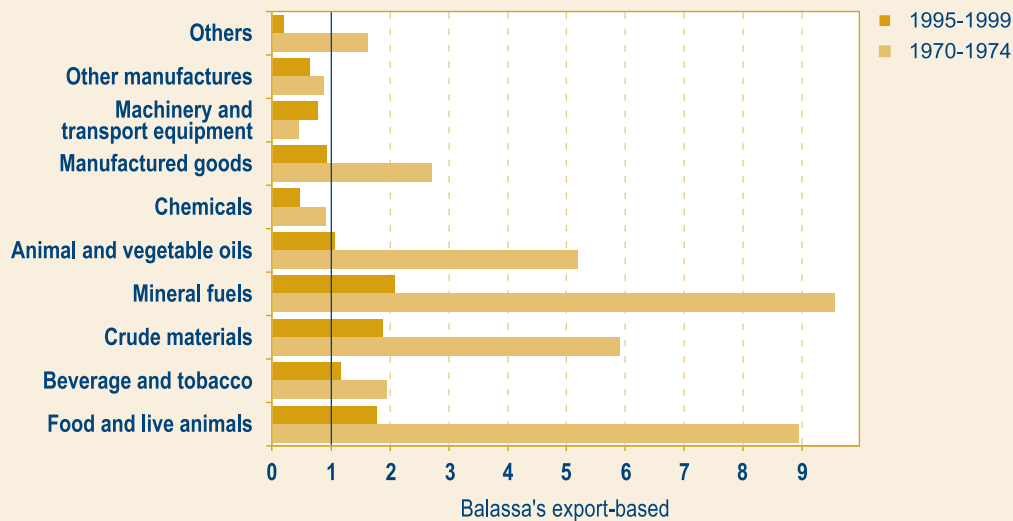
Figure 1.3
Performance of
manufacturing exports



a/ The South-East countries are Korea, Singapore, Philippines y Thailand.

Source: World Bank (2005), own construction

Figure 1.4
Comparative
advantage



Source: UN (2005), own construction

On the other hand, trade patterns also respond to the degree of fragmentation of productive activity⁷. Currently, about 40% of world trade is intra-industry, i.e. the exchange of similar goods between

countries. This type of trade has exhibited, moreover, an increasing trend⁸. In developing countries, intra-industry trade is mainly vertical, that is, countries trade goods within the same productive chain

⁷ Fragmentation is defined as the division of the productive chain between several countries, in which the localization of production and the subsequent stages of value aggregation are determined according to the particular comparative advantages of each country.

⁸ According to the results of an OECD (2002a) study, the participation of this type of trade within the total trade of manufactured goods between its member countries grew more than 10% for 25 of its 29 members. For the case of East Asia, Ng and Yeats (2003) find a similar trend, and greater increases. In general, within the trade of manufactures in this region, intra-industry trade went from 26% in 1985 to 38% in 2001. Finally, in the European Union it increased from 31% to 47%, and in the North American Free Trade Area (NAFTA) from 28% to 34% during the same period.

—one country, for example, imports automobile parts, assembles them and then exports the automobiles back to the country that sent the parts. If, on the other hand, both countries trade the same good—for example, vehicles—one would say that intra-industry trade is horizontal.

Table 1.2 illustrates this trade pattern by region in the particular case of intra-regional trade, given that intra-industry trade tends to be more present within regions than between different regions of the world⁹. In the case of Europe, 35% of intra-industry trade is vertical, while in North America this type of trade represents 29% of total intra industry trade, and in East Asia about 24%. This reflects the aforementioned fragmentation effect of the productive chain, whose different phases are located in different countries of the same geographical regions. This segmentation or fragmentation of the productive chain has

been possible thanks to a reduction in transportation costs, to technological development and to the capacity to disseminate and absorb the latter. By contrast, one sees how the share of intra-industry vertical trade in Latin American regional blocks (exception made of Mexico) is comparatively low.

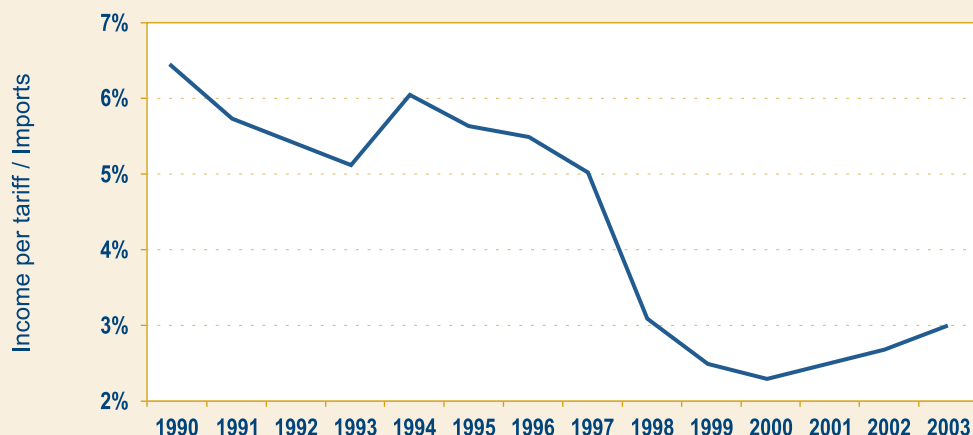
The greater growth of world trade in manufactured goods, as compared to other goods, is also due in part to the world-wide liberalization of this type of trade. For example, Anderson *et al* (2000) consider that in high income countries, tariffs on industrial products decreased from more than 40% in 1947, to 1.5% in the year 2000. Tariff reduction, clearly, is not limited to manufactured goods but, as already mentioned above, is part of a sustained process of world trade liberalization. An example in point is the important decrease observed in tariff revenues as a fraction of total imports.

Table 1.2 Typology of intra-regional trade by trading blocs

Regions	Inter-industrial	Others not classified	Horizontal intra-industrial	Vertical intra-industrial
EU 25	38.31	1.53	24.66	35.51
NAFTA	27.97	19.44	23.58	29.01
Mexico	36.33	10.93	10.07	42.67
Mercosur	67.63	0.52	15.97	15.87
Andean community	80.79	0.47	8.16	10.59
East Asia	62.93	4.96	7.95	24.15

Source: Zignano (2005)

Figure 1.5
Tariff performance



Source: World Bank (2005), own construction

⁹ We focus on intra-regional trade, where most intra-industry trade is concentrated. By contrast, in the extra-regional trade, the participation of the intra-industry trade is low for most of the regions considered.

On the contrary, however, for some products in which the region has comparative advantages, in particular agricultural goods, there still exist important trade barriers that discourage the aggregation of value. As will be shown below, developed countries, in spite of low average tariffs and various systems of preferential treatment, still present considerable obstacles in the form of tariff peaks and tariff escalation. In the case of intra-regional trade, barriers have diminished notably thanks to the proliferation of regional trade agreements, even though significant non-tariff barriers persist and the use of contingent protectionist measures has increased. On the other hand, the penetration of other developing markets has proven quite difficult, in so far as they impose, in general, high barriers to Latin American exports, especially linked to the lack of trade agreements between the region and other developing countries.

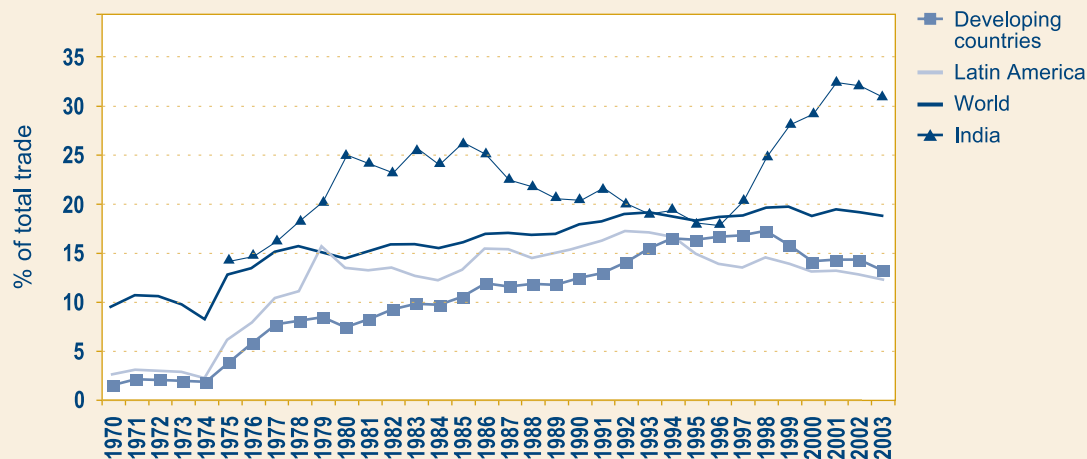
Summarizing, the comparatively modest performance of Latin American exports (with the exception of Mexico) has occurred in a context of expanding world trade, in particular in the case of South East Asia and China. Examining in detail the evolution of the latter, one appreciates how their export growth has been fundamentally determined by the high dynamism of manufacturing exports, while Latin America continues to export mainly primary products. In large measure, these patterns reflect the comparative advantages of each region; furthermore, China and the countries of South East Asia

have achieved productivity improvements, allowing them to build productive chains that have vigorously propelled intra-industry trade. Finally, in the case of Latin America, an important factor –even when not the only one– that has limited larger world penetration of their exports, has been the persistence of trade barriers in spite of the global process of trade liberalization. The reduction (and eventual elimination) of such barriers therefore becomes an indispensable component in the region's strategy of increasing access to external markets.

Trade patterns in services

In parallel to the expansion of international trade in goods, an important phenomenon that has occurred in the past few years has been the growth of international trade flows in the service sector. International trade in this sector has grown twelve fold in the last 30 years, with the participation of services in world trade practically doubling during this period. In the future this trend is expected to continue, not only thanks to the greater ease of transporting services, but also because the demand and supply of services tend to grow with country income levels.

Traditionally, services were considered non-tradables, but thanks to technological developments, many of them are today traded internationally. Commercial services can be of intermediate charac-



Source: World Bank (2005), own construction

Figure 1.6
Trade in services

ter, such as communications, transport and financial operations; or final, such as tourism and recreation, health and education. Figure 1.7 reflects the evolution of trade in services by area. As can be seen, traditional services –travel (tourism) and transportation– represented 72% of global service trade in the 1970s. Although still representing the largest proportion of service trade, such participation has dropped to 53% in 2003. In fact other services that have benefited more from technological developments have grown much faster, as is the case of financial, technological and consulting services, among others.

In the service sector, the story is relatively similar to the case of trade in goods. Latin America, as is the case in many developing regions, has comparative advantages due to relatively low labor costs (ILO, 2005). However, after an apparent boom in this sector in the seventies, the region's participation in the market for services has steadily been diminishing during the past decades¹⁰. India stands out for its growing participation, for reasons discussed in the previous section.

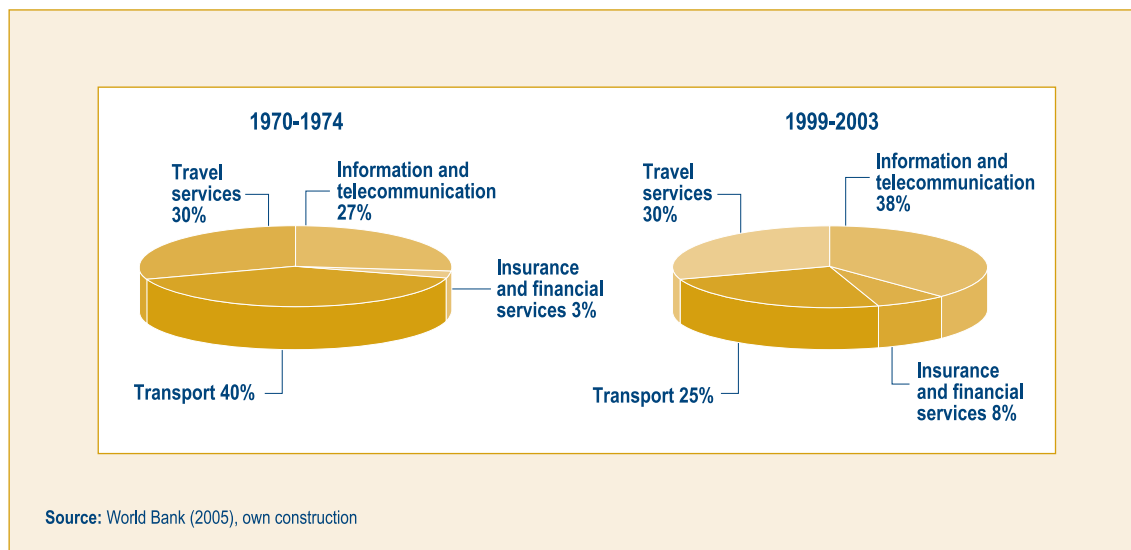
In a way similar to that of trade in goods, the evolution of the service trade in Latin America is explained in good measure by the pattern of specialization according to comparative advantages.

The region has more or less kept stable and even increased its participation in the travel (or tourism) sector, which reflects its advantages in natural resources. Service trade in the region has increased in spite of the large number of barriers that hinder it, such as quotas, tariffs, taxes, licensing requirements, among others (McGuire, 2002). Frequently such restrictions discriminate against foreigners and, in this sense, if one observes the differences that exist in the treatment of nationals and foreigners with respect to services, one concludes that there are important restrictions imposed to trade in services in the region¹¹.

There also exist obstacles to cross-border movement of labor, such as entry barriers, residency restrictions, special taxes, and many other regulations that vary from country to country (Martinez and Villa, 2005). The reduction of such obstacles, therefore, must be part of a trade negotiations agenda oriented toward promoting greater trade in services in the region's countries.

Summarizing, the world has experienced important growth in the trade of services, thanks to the liberalization of the sector in several countries and to recent technological developments. Also, developing countries could benefit more from this growth if they would eliminate some important restrictions

Figure 1.7
Structure of
trade in services



¹⁰ After the participation of Latin America in world service exports increased from 1.2% to almost 5% between 1974 and 1979, this indicator has diminished systematically. In 2003 this proportion was less than 3% (World Bank, 2005).

¹¹ McGuire *et al* (2000).

and barriers still present in their service markets, as was the case in India. In this sense, they should allow, for example, the entry of direct foreign investment in the same terms that exist for local enterprises, reduce specific restrictions that limit the flow of services and provide greater investment in infrastructure and human capital, as a platform for a better utilization of the region's comparative advantages and to benefit increased trade in the service sectors.

Strategies for deepening market access

In the previous section it was shown how the participation of Latin America in world trade has fallen during the last five decades, in spite of the region's efforts to increase trade openness. On the one hand, this decline, as already mentioned, is due to the existence of important barriers, not all strictly trade-related, that limit the region's real access to external markets. On the other hand, productivity problems that afflict Latin American economies represent another fundamental factor.

In this sense, it should be mentioned that, even though productivity problems are of vital importance in a national agenda oriented toward increasing participation in global markets, the theme is complex and requires a special and dedicated analysis. This topic will not be examined directly at this time, but left to the following edition of the Report on Economics and Development for detailed consideration. At this time, the book will deal exclusively with specific market access topics. In this sense, we will try to put into perspective the concrete limitations to market access faced by Latin America that have contributed to its declining world trade participation. We will also highlight the elements that could form the essence of a strategy to gain and consolidate greater access to world markets, within the framework of the different options of trade liberalization currently available to the region.

As will be shown below, the decline in the relative weight of the region in international trade is due, on one hand, to the persistence of important trade barriers, especially in the case of products of great interest to Latin America (such as agriculture). These barriers frequently take the form of tariffs, but non-tariff barriers have also proved especially important. On the other hand, one must consider the existence

of an inefficient logistic platform, especially at the port and customs level, which add expenses to trade, and thus raise additional obstacles.

From the point of view of the obstacles still faced by Latin America, the book includes revised estimates of the concrete impact of trade liberalization agreements. As will be seen, the evidence provided by such exercises weakens the generalized belief that liberalization, especially of strategic sectors such as agriculture, necessarily causes unemployment and increased poverty.

In addition, the need for the region to build a coherent negotiation strategy with regard to the multiplicity of trade options available, oriented toward the ultimate objective of advancing the multilateral liberalization, is clearly shown throughout the book. The greater integration of Latin America in world trade requires the creation of a strategy that utilizes the different options available in a way that best fit the specifications of the region's economies, its comparative advantages and the balance of their particular interests. As will be demonstrated in this book, there exist many complementarities between the different options: multilateral, bilateral or regional. For each country there will exist a specific correspondence between the need for greater trade liberalization and the integration alternatives at its disposal.

The selection of an adequate integration route (or group of routes) is complex and there is no unique solution. The decision requires an understanding of the costs and benefits of the different international integration alternatives, for which it is necessary to evaluate, on one side, the aggregate and sectoral impacts of these trade options and, on the other, their social and territorial impacts. The latter reflects the growing interest among policy makers in identifying the real effects of international liberalization on key variables such as employment, income distribution and poverty indices. In general, the evidence presented in this book shows how, subject to the characteristics of each trade agreement, trade liberalization has a positive impact, both in economic as well as in social terms, for countries participating in these agreements.

With respect to the potential complementarities between different spheres of negotiation, aggressive trade liberalization carried out within the frame-

work of bilateral agreements between the region's countries and its principal industrialized partners could break the inertia that characterizes certain regional integration schemes. In fact, many of the compromises acquired in these bilateral agreements could be used by sub-regional blocks to advance their internal processes of political integration and harmonization, for example. On the other hand, even if the multilateral option of the WTO would seem to generate greater benefits, the implementation of regional agreements can provide greater negotiating power to small economies and prepare them to face more stringent and more relevant multilateral obligations.

It is also important for the region's countries to take advantage of multilateral negotiations to enlarge their markets and achieve greater and more secure access to them. In this sense, clear and definitive advances in agriculture negotiations, for example, can only be achieved within the WTO, insofar as its commitments affect all countries. The agricultural sector, because of its contribution to GDP, and its potential effects on other productive activities, is very important to Latin American economies. However, as will be shown in this book, this is one of the most widely protected sectors in the world, and constitutes a critical negotiation topic that should be carefully addressed in the multilateral context, even when this does not exclude partial advances in the framework of other negotiation spheres.

Another central issue in trade negotiations is, as already mentioned, the protection of intellectual property rights. This is a topic of particular complexity and that often becomes one of the most difficult at the negotiation table. In this sense, and in spite of the limited room for maneuver that the region appears to have in this matter, the book shows how achieving ample coverage of intellectual property rights, defined to include traditional knowledge, biodiversity, geographical indications, among others, may be in the interest of developing countries that seek to protect exports associated with their particular comparative advantages.

Of course, trade liberalization cannot be the only element of an integration project of global scope. It should be accompanied by action in other areas associated, either directly or indirectly, with trade, such as air and maritime customs, customs transit

and technical norms, as well as increased coordination and harmonization of policies, among others. In this sense, greater advances in trade facilitation can increase the real access of the region's countries to world markets. Although these measures may seem obvious, one of the great obstacles faced is that such improvements in the logistic platform often imply investment that these countries are not in a position to undertake in the short term. Successful experiences, however, show how the medium and long term benefits outweigh the initial implementation costs.

This book, explicitly oriented toward the issues that must be contemplated by a strategic agenda aimed at greater market access, is organized in nine chapters (excluding this one). These nine chapters form—although not formally—three large areas within the theme of market access. An initial diagnostic (chapters 2 and 3) illustrates the complex scheme of international integration options that countries have at their disposal, and identifies the trade barriers that limit the free flow of goods and services.

The second thematic area (chapters 4, 5 and 6) examines empirical evidence related to concrete impacts that different trade agreements can have on economic (growth, sectoral activities, employment, trade flows), social (employment, income distribution, poverty) and geographical-territorial (inequality and convergence within trade blocks) variables of participating countries. As a special case, we also analyze how Latin America can benefit more effectively from the greater participation of China in global trade.

Finally (chapters 7 to 10), critical topics of negotiations are analyzed associated with the liberalization of agriculture and services, with the protection of intellectual property rights and with trade facilitation. In the following section the principal conclusions and central messages of each chapter are summarized.

Negotiation strategies and trade agreements

Chapter 2 presents a discussion of the multiple spheres of international integration, and analyzes different trade scenarios, their interrelations and complementarities. These spheres are articulated around three principal axes: regional integration agreements,

trade agreements with developed and developing countries outside the region, and multilateral negotiations within the framework of the WTO.

Such a multiplicity of trade negotiation routes imposes challenges for Latin American countries and requires the mobilization of important human and material resources, such as increasingly sophisticated technical analyses. The need to insure complementarity among the different initiatives adds complexity to this task. In this sense, although up to now the coexistence of regional and extra-regional agreements has not caused relevant problems in the handling of trade policy, warning signs regarding the superposition of norms and commitments indicate that this situation may be changing.

For example, the future of the Central American Common Market (CACM) after the free trade agreement (FTA) between the US and Central America (CAFTA), or that of the Andean Community (AC) once an FTA is signed between some of its member countries and the US, cannot be assured if its member countries do not take the necessary measures to avoid that their integration schemes become obsolete. The same can be said about Mercosur countries with respect to their negotiations with the European Union. The task is urgent because the commitments assumed in the framework of bilateral agreements have, in some cases, greater scope than those assumed at the sub-regional level.

In this sense, the chapter states that regional integration should be reinforced with the objective of maintaining the goal of facilitating a more effective integration of Latin American countries in the world economy. Although an integration project of regional scope has not existed since the beginning of the 1990s, it would seem that the conditions exist to resume these initiatives¹². In the first place, countries have already advanced in the process of tariff reduction¹³. Secondly, many countries in the region have shown themselves ready to liberalize their traditionally sensitive sectors, in agreements with the US and other industrialized countries. This leads to the proposal of a Latin American regional agreement that would promote the rapid development of

a regional free trade area. Although implying great challenges, such an initiative would add new impulse to integration in the region.

In addition, it is shown how trade negotiations within the WTO framework offer the opportunity of achieving goals that cannot be completely accomplished in regional agreements. Such is the case of agricultural negotiations, a topic of the greatest importance for numerous Latin American countries. Even when regional agreements consider reciprocal liberalization measures in agricultural trade, these are often insufficient for eliminating the distortions that affect trade in this sector. To eliminate such distortions, the policies of industrialized countries regarding export and production subsidies must be substantially modified. This will only be possible within multilateral negotiations in which the concessions negotiated are sufficiently attractive for these countries to introduce changes in their current agricultural policies.

The chapter concludes that multilateral negotiations could also help to widen the scope of trade agreements subscribed by the majority of Latin American countries, if these can be translated into an effective decrease in the protection of highly protected sectors. More importantly, multilateral negotiations offer the opportunity to open markets in other developing countries, especially those with greater trade potential for the region, an opportunity that has not yet been well explored.

Trade barriers faced by the region

Chapter 3 identifies the trade barriers that limit, both at present and potentially in the future, the access of regional exports to global markets. In spite of advances in trade liberalization, the region still faces important tariff and non-tariff barriers that, together with other factors, continue to negatively affect Latin America's participation in world trade.

In developed countries, in spite of low average tariffs and various systems of preferential treatment, considerable barriers remain, in the form of tariff peaks (tariffs over 15%), and tariff escalation (tar-

¹² FTAA is more a North-South initiative than to a regional integration scheme.

¹³ According to the ALADI Secretariat, trade agreements between its members should result in the liberalization of approximately 90% of regional trade by the year 2007.

iffs that increase with the degree of processing). In addition, the use of non-tariff barriers persists, with significant effect on the region's exports. Barriers are often high in sectors of greatest importance for the region's exports, as is the case of agricultural and textile exports.

In the case of intra-regional trade, the chapter highlights how barriers have diminished notably, thanks especially to the proliferation of regional trade agreements. However, the persistence of significant non-tariff barriers and the increase in the use of contingent protectionist measures such as antidumping and safeguards should be of concern to policy makers.

Other developing countries have proven difficult markets to penetrate, in spite of greater liberalization within the WTO framework. In fact these countries present the highest barriers to Latin American exports, due in particular to the shortage of trade agreements between Latin America and other developing countries.

In addition, given the particular nature of services, barriers to such trade differ from those that affect trade in goods. Given that service imports often do not imply the crossing of borders, it is much more difficult to apply tariffs or border taxes, making the utilization of quotas and other qualitative restrictions much more common in controlling import flows. In addition, one must consider that service trade, much more than trade in goods, is affected by local policies that discriminate in favor of domestic products¹⁴. In general, restrictions on trade in services have smaller effects on costs and prices in industrialized countries than in developing countries. In addition, Latin American and Asian countries often present high barriers and discriminate against foreign producers.

Based on these considerations, it seems clear that from the point of view of trade barriers, the strategy of the region's countries to achieve greater access to global markets must center on the precise identification of these barriers, especially of non-tariff barriers, and on their reduction and eventual elimination, through negotiations and the signing of trade

agreements. In the case of services, the removal of trade barriers implies the adoption of domestic policies that level the playing field for domestic and foreign agents, and the elimination of quantitative restrictions to the flow of imports.

Aggregate and sectoral impacts of trade agreements

Chapter 4 offers a contribution to the measurement of the aggregate and sectoral impacts of the different spheres of negotiation. This contribution consists in the discussion of empirical exercises oriented toward understanding how trade liberalization –considered in its different concrete representations– can affect the structure of production, modify productive conditions, and impact employment and, consequently, welfare. Such exercises are based on 12 concrete scenarios of trade options that countries of the region have already negotiated or are currently negotiating.

In general, the results of these exercises show that, both in the short and in the long run, all trade agreements considered have a positive impact on production and welfare in each of the countries involved. The benefits are greatest in the long run, when the impacts of trade liberalization on total country productivity are felt and there exists the possibility for capital accumulation. An important point to highlight, from the evidence presented, is that developing countries obtain greater gains than developed ones in the processes of trade liberalization in which they participate. This is to be expected, insofar as developing countries present greater relative trade distortions and, therefore, can derive greater potential benefits from liberalization.

On the other hand, we find that trade agreements have less positive results on the production and welfare of non participating countries, mainly associated with possible trade diversion generated by the agreements in such countries. However, taking into consideration the global effect of the trade agreements analyzed, one concludes that the level of trade creation produced between participating countries is greater than that of trade diversion

¹⁴ These policies include for example, measures that provide a direct advantage to domestic producers, as in the case of subsidies, or that create a competitive disadvantage for foreign producers via, for example, direct or indirect taxes. Domestic measures that affect the movement of productive factors (labor and capital) can also constitute barriers to the trade of services.

between non participating countries. Therefore, in global terms one observes that the trade agreements analyzed are net trade creators.

Furthermore, it is important to point out that comparing the simulated scenarios and their respective results one finds that free world trade –i.e., the WTO multilateral option– is the route that generates greater benefits for all countries, both in Latin America and the rest of the world. This is particularly true in the agricultural sector. The results for liberalization in service trade show effects similar to those of trade liberalization in agricultural and manufactured goods.

Analogously, more limited trade agreements, such as those between Latin American countries or with developed countries, also have positive effects on trade, production and employment levels. In short, there does not exist an absolute criterion for determining with precision the optimal strategy or route for international integration. In this sense, it would seem that countries still prefer to start their integration processes through diverse and more limited routes, from which they also benefit, and which serve as preparation for more demanding negotiation scenarios.

Results at a more disaggregated sectoral level indicate the existence of a large degree of compatibility between multilateral negotiations and bilateral agreements of the region's countries with industrialized economies. Nonetheless, such complementarity should not be taken as given, and its analysis is of the utmost importance in the design and selection of a trade strategy aimed at achieving greater access to international markets for the region's countries. A careful selection and a coherent management of the different trade scenarios is therefore essential to avoid possible obstacles created by incompatibilities between agreements, that would undermine the benefits of greater participation in the world economy.

Social and territorial impacts of international integration

The analyses of trade liberalization processes should also consider their impact on social variables such as employment and income distribution, and on the geographical-territorial dynamics of such processes, aspects that are dealt with in chap-

ter 5. This analysis is necessary, given the common belief that trade liberalization generates undesirable effects on social variables in smaller and less developed economies. Evidence rejecting this perception may provide governments with room to maneuver, allowing them to advance their trade negotiation agendas with renewed vigor, and to assure larger popular acceptance for signed agreements.

Specifically, this chapter examines the potential impacts of the free trade agreements that Colombia and Peru are currently negotiating with the United States on employment and distribution, taking into account productive sectors, income distribution and levels of worker qualifications. The evidence obtained for these Andean countries rejects the belief that trade agreements between small and large economies always constitute a threat to labor stability and increase poverty levels. Although the effect is limited, the empirical exercise indicates that, in Colombia as well as in Peru, trade liberalization with the US would generate an expansion of production and employment in sectors intensive in low skilled labor.

On the other hand, the signing of such agreements not only benefits workers from the poorest segments of both countries, but such benefits would be comparatively higher than the ones received by higher income workers. Consequently income distribution tends to improve, particularly in the case of Peru. The analysis performed for these countries therefore reveals that, although trade liberalization agreements do not constitute a solution to poverty problems, there is no evidence that they necessarily worsen conditions.

In a second section of this chapter, the topic of geographical-territorial impacts in the Andean Community (AC) is approached, via an analysis of the dynamics of income convergence, at the national level and with respect to regions and territories both within the Andean block and within the single member countries.

Evidence indicates that, in effect, the Andean integration process has generated income convergence between member countries. Furthermore, this convergence shows a positive trend. At the regional and territorial level of the AC as a whole, however, results indicate the presence of important inequalities and

disparities that reflect, in turn, the territorial inequalities within member countries. This means that the integration process may have generated the displacement of productive activities (and of employment), benefiting some regions and territories within each country, and deepening income inequalities.

According to the literature in this area, how integration affects the dynamics of geographical and territorial inequality will depend on the impact of integration on firms' decisions on location, and by extension, on the geographical distribution of employment. This, in turn, will depend on the relative importance of external markets with respect to local ones in response to the integration process, and on the degree of trade with other member countries.

The chapter concludes that such results clearly impose important challenges for these sub-regional economies, with respect to the need for strategies and policies that compensate for potential regional and territorial inequalities. In this sense, the evidence presented indicates that these inequalities are mainly due to income disparities between regions, for which policies should concentrate in particular on strengthening growth in the more affected regions, and in compensatory income redistribution measures.

China: opportunities and challenges for Latin America

Chapter 6 analyzes what could be called “the China effect” on Latin American economies. This effect is of particular relevance for the region, in view of the growing Chinese presence in international markets, especially in the case of primary goods, where Latin America exhibits important comparative advantages. However China's presence has been also increasing in the market for manufactured goods, where the region's countries have been directing important efforts.

This chapter shows how China's trade liberalization has generated, on balance, a favorable impact on the region, by considerably increasing its trade flows. This has been especially true for the exports of primary products that, in addition, could be significantly increased with greater foreign direct investment, from China as well as from third countries. With respect to these investments, it is important that they not be limited to extractive activities,

but that they also produce positive spillover effects on other economic sectors, generating greater productivity and employment.

Chinese liberalization, however is disadvantageous for those countries that are making important efforts to obtain a better position in the export of manufactured goods. The largest competition from China has been observed, as expected, in the U.S. market –in the garment industry, in the case of some Andean countries, and in mid and high technology products, in the case of Mexico. In both cases, evidence shows that increasing value added and technology, which in turn promote product differentiation, could help these economies successfully overcome such strong competition.

Greater economic complementarity between China and Latin America will also depend on the reduction of trade barriers, especially non-tariff ones, that still limit the access of Latin American products, in particular agricultural products, to the Chinese market. The effective benefits of market enlargement that China represents for the region will therefore depend, in good measure, on the ability of our countries in obtaining the reduction of such barriers within the WTO framework.

It is also essential to obtain decisive advances in direct bilateral agreements with China. At present, there have been few effective efforts in this area, and only Chile has completed negotiations with this country. Greater advances in this sense will not only bring about concrete gains for each country or regional block that takes part in the agreements, but will also imply important advantages for China. In fact the latter has been facing contingent protectionist measures such as antidumping and safeguards by countries of the region, which could be avoided if this nation were to achieve trade agreements with Latin American countries.

The challenge of agricultural liberalization

Chapter 7 focuses on the analysis of international trade liberalization in agriculture, a sector where Latin America exhibits important comparative advantages. Furthermore, in the presence of a solid agro-industrial sector, liberalization in this area could potentially generate wider positive effects with respect to production and employment. The

discussion of the different forms of trade protection and of the impacts of trade liberalization under different negotiation scenarios yields the conclusion that multilateral negotiations would generate the largest gains to the region's countries.

Nonetheless, countries should try to negotiate agreements according to their productive structure and specific socioeconomic conditions. In addition, the diversity of agricultural policy instruments among an agreement's member countries may obstruct free trade in the framework of regional and bilateral trade negotiations. Therefore, the achievement of free trade in these agreements requires a consensus regarding a common agricultural policy among member countries.

On the other hand, agricultural subsidies and protection levels will continue to represent a controversial issue in negotiations between developing and industrialized countries. A crucial aspect that individual countries should consider when negotiating is the precise identification of the most important distortions affecting their trade flows, with the objective of dedicating efforts and of developing abilities to successfully negotiate their elimination. In this sense, some evidence supports the relative importance of the elimination of tariffs vis-à-vis the elimination of subsidies, given that, in principle, all developing countries benefit from tariff reduction, which is not the case of the reduction of subsidies, given price effects in agriculture importing countries. Complete agriculture liberalization (including subsidies), however, would also increase salaries in the sector, which could compensate the increase in price of the consumer basket.

Analogously, it is crucial that countries identify which sectors lose and which gain from free trade agreements, with the objective of adopting internal policies that optimize the distribution of the gains from liberalization. In particular, they should recognize the labor market adjustment mechanisms and the possible effects on employment and salaries, which may be relevant in determining the final impact of agricultural liberalization on the most vulnerable sectors of the economy.

In this sense, it is worth mentioning that the most significant impacts of agricultural liberalization will be felt in a multilateral liberalization scenario. In this case the sectoral interests of the region's countries are best represented, given that, in this context, decisions must be respected by all countries.

Liberalization of services: a world to explore

Chapter 8 presents another sector of importance in the exporting dynamics of industrialized countries and of certain emerging economies: services. Developing countries can approach the challenges implied by the greater dynamism of the service market from two different points of view. The first takes into account that greater participation of suppliers of external services in the national market may raise efficiency and increase the variety of available technologies. The second refers to market access, and takes into consideration the export potential of developing countries in service markets. In fact some niche markets, such as the case of business services¹⁵, present interesting opportunities for countries, as in the case of India, characterized by salary differentials with respect to developed economies, highly trained labor and an adequate infrastructure for the transport of services.

Although up to now Latin America's position has not been homogeneous with respect to services as productive sector inputs, one sees the importance of modernizing existing regulations, and of persevering in the deregulation of foreign investment, which seems to be part of the agenda of the region's countries. As for the case of market access, it is very important to insist in the need to advance in areas of the movement of persons, government procurement, state level legislation and subsidies.

Latin America's position should be to opt for the combination of integration routes that best fits the interests of each country, as suggested in earlier chapters. Issues such as subsidies and government procurement appear more appropriately dealt with at the level of multilateral negotiations, whereas at a bilateral level advances may be possible with respect to state legislation and cooperation for the modern-

¹⁵ Matoo and Wunsch (2004) define business services as total services minus transportation, tourism and government services, or alternatively as the sum of Communications, Construction, Insurance, Financial, Computing and Information Services, Personal Services, Cultural and Recreational and fees for licenses and patents.

ization of regulations. As for the movement of persons, which has suffered a setback due to prevailing security conditions, particularly in the case of developing countries, it would appear possible to deal with this multilaterally and, in parallel, to seek specific advances in bilateral treaties under negotiation.

Lastly, the chapter concludes that, independently of the region's interests, the service sector is difficult to protect, especially with the growth of e-commerce. Therefore, the region must follow a pragmatic approach and concentrate on obtaining the greatest possible gains from trade agreements, and not to try to limit its growth. This effort should not be limited to the field of negotiations, but instead should include the establishment of a better infrastructure for the supply of services and, in particular, labor market improvements with respect to wages and training.

Toward a balanced protection of intellectual property rights

Chapter 9 discusses elements regarding intellectual property rights protection, in view of its increasing importance in the world trade debate. In fact trade flows are increasingly affected by issues of intellectual property, and differences in protection between countries are becoming elements of growing tension in international trade relations.

At present, developing countries find themselves under rising pressure to increase their protection levels, generally considered insufficient. On the one hand, multilateral organizations propose the world-wide harmonization of intellectual property rights protection. On the other, the topic has become particularly urgent for developing countries negotiating free trade agreements with the US. These agreements in fact include commitments with respect to the protection of intellectual property that, in many cases, are stricter than those contemplated in the WTO.

For developing countries, and for Latin America in particular, the chapter underlines two key implications of intellectual property rights protection. On the one hand, international pressure toward greater protection imposes costs on these countries, with respect to both its implementation and in terms of social welfare. On the other hand, intellectual property rights protection could help safeguard some

exports of interest to Latin America, based on their comparative advantages. This is particularly relevant, for example, in the case of exports that involve geographical indications, genetic resources, biodiversity, traditional knowledge and folklore, among others. Given the importance of these matters for the region, a common regional position is desirable, in spite of the different degree of interest of each country with respect to single issues.

Even within the limits established by various international, regional and bilateral agreements, the region's countries still have some room to negotiate. This includes, for example, the use of compulsory licenses in the case of public interest concerns, or as a mechanism for the control of abusive practices; the establishment of patenting criteria that conform with countries' level of development; and the administration of the intellectual property rights system to improve patent quality, promote local innovation and favor its use by small and medium size enterprises.

Within this context, Latin American countries should identify policy priorities. At the national level, the debate should be enriched through wider participation of civil society, whereas at the regional level it should include topics of cooperation, with the objective of stimulating scientific and technological development, given the role played by intellectual property. At the level of international and regional negotiations, it is necessary to precisely identify "offensive" and "defensive" interests, both national and regional, and to strengthen the capacity of negotiating teams. It could also be appropriate to favor multilateralism in the design of international standards for intellectual property.

An agenda for trade facilitation

Lastly, beyond the reduction of tariff and non-tariff barriers that prevent greater market access, chapter 10 presents the need for measures that are not strictly trade-related but that serve to facilitate the international flow of goods. It shows how countries' trade flows are affected by regulations, practices, and internal procedures that, even when not explicitly designed to restrict trade, in practice serve as important obstacles. These constitute, therefore, a limitation to greater access to global markets, and their reform should be considered within the set of international integration strategies.

In this chapter, an overview of the different issues associated with the regional trade facilitation agenda is presented. The evidence illustrates that trade facilitation reforms in fact represent significant savings (in time and resources) for trade operators. Improvements oriented towards reducing transportation costs, as well as those directed towards port infrastructure, customs procedures and border crossings, are especially relevant for the Andean Community, given the importance of maritime and terrestrial trade in the sub-region.

Efforts to facilitate trade are not new, and many are part of the domestic agenda of countries seeking to increase competitiveness. What is new is the beginning of negotiations on trade facilitation within the framework of the Doha Round. Nonetheless, one cannot expect results in the short run, given that for the moment discussions are still at the stage of technical aspects and the sharing of country experiences. The WTO negotiations, in addition to specific agreements that may be achieved, offer a chance to learn from different countries' experiences in the adoption of trade facilitation measures, to evaluate their costs and benefits and, in the case of developing countries, to mobilize resources to carry them out.

The adjustment costs inherent to a trade facilitation program have generated some concerns in developing countries. Among these concerns, administrative

costs and difficulties arising from the implementation of obligations resulting from trade agreements are singled out. In addition, many trade facilitation reforms require investments in new technologies for the management of customs and ports, which in general are very costly.

These costs, however, may not represent an important obstacle. Technical assistance and capacity building in developing countries are part of the negotiation mandate, and it is very likely that considerable resources be mobilized toward this end. There are no guarantees however, that such resources would benefit the region's countries, for according to current trends in international cooperation, the poorest countries will be those to benefit the most. In this sense, Latin America should count on its own efforts and resources.

In summary, this book offers various explanations regarding Latin America's decreased participation in world trade, a stable pattern of the last four decades. Its smaller relative weight stems in part from the low productivity that characterizes the region's countries and in part from the existence of trade and physical barriers that continue to limit access to the region's export markets. A better utilization of the different spheres of trade negotiation, and thus a reduction of existing barriers, is proposed as a key element of a development agenda for the region's economies.

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