When You Come to a Fork in the Road, Take it Reflections on North American Integration: Regional and Multilateral

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INTRODUCTION

The title of this article was coined by the great American philosopher Yogi Berra. There are many roads that lead to greater economic integration or ever-tighter linkages among countries. Globalization is, indeed, an ongoing process of deepening integration fed by trade, financial flows, direct investment, production networks and increasingly by the technological revolution in information and communication. So it is not necessary to choose one route in, for example, trade policy. In the Western Hemisphere bilateral, regional and multilateral policies are all being pursued. Moreover, there are many facets of integration that go beyond economic linkage but we tend to think mainly of trade and investment as primary and pay far less attention to other avenues.

In this article I shall begin with a brief tour d'horizon of the multilateral landscape. This is, of course, a vast and complex subject and I intend to be selective and to highlight the main issues related to hemispheric integration. In doing so it is important to deal with the American strategy of 'competitive liberalization' past and present,[1] as well as the 'new geography' of global trade. I will then seek to explore a different idea or concept of integration and to propose some possible options for extending and deepening the linkages among countries and peoples in this hemisphere.

I DOHA, CANCUN, AND THE NEW GEOGRAPHY

The Uruguay Round marked a fundamental transformation of the multilateral trading system from the shallow integration of the General Agreement on Tariffs and Trade (GATT), with its focus on border barriers and its rules to buffer or interface between international and domestic policy, to a system of deepening integration with a primary focus inside the border on domestic regulatory and legal institutional

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1 The term is used for a policy strategy that employs bilateral or regional agreements to encourage broader or multilateral liberalization. See Sylvia Ostry 'Regional Dominoes and the WTO: Building Blocks or Boomerang?' (Fraser Institute Conference, Toronto, November 1999), online: <http://www.utoronto.ca/cis/ostry.html>. For a recent version see C. Fred Bergsten & Institute for International Economics, *The United States and the World Economy: Foreign Economic Policy for the Next Decade* (Washington, DC: Institute for International Economics, 2005) at 35.

infrastructure

The implicit Grand Bargain that concluded the negotiations—the North to open their markets for agriculture and labour intensive products, especially textiles and clothing to the South, and the South to accept the so-called new issues of trade in services, trade-related intellectual property (TRIPS), and trade-related investment measures (TRIMs)—turned out to be a Bum Deal. Also, as virtually a last minute piece of the deal, the creation of a new institution, the World Trade Organization (WTO), with the strongest dispute settlement mechanism in the history of international law and virtually no executive or legislative authority. Since the WTO consisted of a 'single undertaking' the deal was pretty much take it or leave it for the Southern countries. So they took it but, it's safe to say, without a full comprehension of the profoundly transformative implication of the new system (an incomprehension shared by the Northern negotiators as well, I might add).

There were a number of significant unintended consequences of the Round. The most important was a serious North-South divide in the WTO. While the South is hardly homogenous there is a broad consensus that the system is asymmetric and must be rebalanced. The debacle of Seattle in 1999 ended in a walkout of virtually all developing countries. It's more than symbolic that the outcome of the Doha Ministerial Meeting in 2001 was termed a 'development agenda' and not a round. The main objective of the Doha meeting was to avoid another Seattle. Thus its great success was that it didn't fail. Both the United States and the European Union visited Africa and the Declaration repeatedly refers to technical assistance and capacity-building. Pushed by the successful non-governmental organization campaign about AIDS in Africa the Americans even seemed willing to antagonize Big Pharma. So Doha was unique in its focus on the South and on development.

But Doha included many other agenda items, especially, of course, agriculture. And, at the insistence of the European Union, the so-called Singapore issues of competition policy, investment, government procurement and trade facilitation. The Doha negotiations went nowhere. All deadlines were missed and there was no progress on key issues, especially agriculture. The ambiguous drafting was too clever by half. And that brings us to Cancun in September 2003.

I was at Cancun and when the meeting ended so abruptly I was swept by a strong sense of *déjà vu* all over again. Cancun was a mid-term Ministerial meeting as was Montreal in the Uruguay Round in 1988. On the last morning of the Montreal meeting around six a.m. the bleary-eyed negotiators were waiting for the United States and European Union warriors who had been up all night dealing with agriculture. When they arrived they announced that it was too bad but they hadn't reached an agreement so we should tidy up the agenda items and finish the *communiqué*. A group of Latin Americans headed by Brazil said 'no': no agriculture, no agreement on anything. It was a moment of shock but was handled with great finesse by announcing that the meeting was adjourned and would be reconvened shortly in Geneva. No big headlines ensued.

In any case my *déjà vu* feeling soon dissipated. The North-South divide had taken a different shape. There appeared to be an axial shift in the political economy of policy-making that would require a fundamental reorientation of the players and the game. Two new coalitions of Southern countries were formed at Cancun. One, termed the G20, led by Brazil and India as well as China (the Big Three) and South Africa included a number of Latin American countries. Its main focus at Cancun was agriculture, catalyzed by an unacceptable draft proposal from the United States and European Union. The G20 seemed an unlikely coalition since it included countries with varying views on economic policy and, indeed, on agriculture. But it didn't collapse under pressure at Cancun and, despite losing members because of American bilateral pressure, it has survived thus far. It appears to be reaching out to the least developed countries (LDCs) to coordinate positions on agriculture and perhaps other issues.[2] And it or its leader, Brazil, has succeeded in challenging the Free Trade Agreement of the Americas to the chagrin of the United States. And India and China are now exploring a free trade agreement as well as a number of other preferential arrangements.

The G20 was very active at the UNCTAD XI meeting at Sao Paulo in June 2004 and, indeed, at that meeting a South-South Round of negotiations was launched under special provisions of the original GATT in which developing countries provide trade preferences for products from other developing countries. This was underlined as another example of the 'new geography' of the trading system by UNCTAD head Rubens Ricupero and the Brazilian president Luiz Inacio Lula da Silva.

Indeed the new geography was evident at Cancun in the formation of another coalition—the G90. This included the poorest developing countries, mainly from Africa. After failing to convince the United States to eliminate cotton subsidies to help the poverty-stricken African exporters and to persuade the European Union to remove the

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2 G20 Ministerial Meeting, Delhi, 18–19 March 2005. The meeting was attended by the coordinators of the Africa Group, ACP countries, CARICOM, and Least Developed Countries (LDCs). See 'G20 Ministerial Meeting Ends with Declaration' TWN Info Service on WTO and Trade Issues (21 March 2005), online: Third World Network <http://www.twnside.org.sg/title2/ twninfo190.htm>.

Singapore issues from the agenda, the G90 terminated the negotiations. It's important to note that at Cancun non-governmental organizations played a prominent role with respect to the G90. African non-governmental organizations were included in many official delegations and they provided ongoing information as well as research and policy analysis. They had regular briefing sessions from officials and Ministers.[3] As noted earlier, they (plus some Northern non-governmental organizations) could be described as a virtual secretariat launched by the internet. But unfortunately there's not enough information to explore this important development in more depth.[4]

The formation of Southern coalitions will undoubtedly change the dynamics of the Doha negotiations, especially but not only on agriculture. The G20 was actively engaged in the bargaining over a 'framework' agreement (a broad outline with minimal detail), which was agreed by all-night bargaining at the end of July before the 2004 summer break. This allowed the negotiations to start again after the United States election and perhaps be concluded, one hopes, just a year later than the target date set at Doha. But there won't be another Blair House deal by the Big Two that sealed the Uruguay Round without the Big Three and perhaps the G90 as well. Indeed splits between the G90 and other developing countries are being encouraged by the rich countries. The geography certainly makes trade policy more complex! Both the United States and the European Union are using bilateralism and other policy instruments to weaken the G20 and provoke conflict with the G90. And of course the new geography is not confined to trade. A shift in the 'balance of power' is underway and, as was the case in the nineteenth century, the response will spur changes in both domestic and external efforts. But that's another story.[5] Back to trade!

The story of the new geography has just begun and its evolution is fraught with uncertainty. Yet clearly the nice, neat concept of regional integration is getting more messy and more complex. Added to the already existing coalitions in the negotiation of the 'framework' agreement was FIPS or Five Interested Parties of the European Union, the United States, Brazil, India, and Australia (representing the Cairns group). Someone has called this the G5, or Gestalt Group. Is it simply a

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3 Falou Samb, Agency for International Trade Information and Cooperation Senegal, correspondence with the author (February 2004).

4 The author has launched a project with a group of African graduate students to track the role of non-governmental organizations in the trade policy-making process in Africa at both the country and regional level.

5 But one that needs exploring because there is, of course, considerable overlap between high and low policy today. See, for example, 'Charlemagne: The Reds in the West' *The Economist* (15 January 2005) 40, on the 'emerging axis' between China and Europe.

wily means of co-opting the G20 or will it continue to play a significant role in the negotiations? We'll have to wait and see. But whatever else, it's certainly inter-regional. As are the growing partnerships or other relationships between the European Union and LAC (Latin American and the Caribbean), which have been expanding and strengthening since the 1990s. The EU-LAC summit process is described as 'a distinct form of North-South integration,' 'an exercise in political alliance-building,' and an effort to 'encourage the LAC countries to adopt policies that increase social cohesion by reducing poverty and inequality.'[6] So South-South is new but so is a quite new North-South. The point to be made is that the ongoing changes in the political economy of trade policy-making are too complex and uncertain to rely on one paradigm such as the linkage between regional and global trade and investment integration. The concept of competitive liberalization touted by the USTR will likely result in fragmentation not integration. There is an enormous economic and political disparity between the United States and the other Western Hemisphere countries, so bilateral and regional agreements (often including 'WTO plus' versions of, for example, TRIPS and investments) are creating a new and ever-mutating spaghetti bowl. To add to the mass both Mexico and Chile are pursuing a large number of bilateral agreements. The transaction costs for business of the rules of origin included in the agreements are so large that many corporations are choosing to pay non-preferential or MFN tariffs. These ever-proliferating preferential agreements have been strongly criticized in the Report by the Consultative Board to the WTO Director General.[7]

Competitive liberalization is not a new idea by any means. But the form it is taking now differs significantly from that of its earlier phase in the 1980s, which I have called domino policy. The main architect of regional domino policy was the US, which initiated a multi-track policy with the Canada-US Trade Agreement (CUSTA) because the Uruguay Round was stalled by the European Union over agriculture and Brazil and India over the new issues. A major objective for the Americans was to demonstrate to the Europeans that bilateralism was a feasible alternative that would be actively pursued if the foot-dragging at the GATT continued. For Brazil and India and their followers, the implied threat was strongly reinforced by a new 'tough policy' announced by President Reagan in September of 1985 that included support for the little-used section 301 of the 1974 *Trade Act*. CUSTA was

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6 Inter-American Development Bank, *Integration and Trade in the Americas: III EU-LAC Summit: Special Issue on Latin American and Caribbean Economic Relations with the European Union* (Washington, DC: Inter-American Development Bank, May 2004) at 1-3.

7 Peter Sutherland *et al.*, *The Future of the WTO: Addressing Institutional Challenges in the New Millennium* (Geneva: WTO, January 2005).

the first trade agreement to include trade in services. While it can't be proved it may well have helped add to the internal pressure in Europe to agree to launch the Round. NAFTA, the next domino, built on CUSTA and the Uruguay Round GATS (General Agreement on Trade in Services) and included TRIPS and a very impressive investment regime—the two new issues not achieved in CUSTA. But the next domino—a multilateral agreement on investment to be concluded at the OECD then transferred to the WTO—failed and indeed proved to be a boomerang since investment issues have been kept out of the WTO ever since.

The earlier version of competitive liberalization was primarily directed to extending multilateralism. Since that was the ultimate American target, the European Union had to be part of the end game. But now the entire game involves the European Union. And it's being played by others, especially China in Asia. Fear of an Asian Union led by China and excluding the United States may be exaggerated.[8] Or maybe not. ASEAN plus three (China, Korea, Japan) has been announced.[9] But the main issue is that a *global approach* seems the best strategy no matter how difficult it will be. A global rules-based system is the best alternative when one considers all of the others. It would be very dangerous to eschew the multilateral approach and will be very challenging to devise policy options to facilitate deeper integration not just in the hemisphere but in the global system. That takes us to the other road in the fork.

II Integration: Process by Project

The only example of 'deep integration' that exists today is the European Union. The objective was political, driven by the need to forever preclude a repeat of the wars of the twentieth century. The means were economic, such as the creation of a single market and free flow of factors of production. But of course, a great deal more was involved, especially the creation of a range of institutions. And the story has not ended. The deepening and widening process is ongoing. As is the search for a shared concept of community.

In the Western Hemisphere the integration process has been mainly a product of the private sector. Policy has played a minimal role. There are some regional institutions but they also are minimal. It's not clear what the objective is but it is not to build a 'community'. One of

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8 Claude Barfield, 'China, the United States and the Rise of Asian Regionalism' (Paper presented to the Western Economic Association International 79th Annual Conference, Vancouver, 29 June-3 July 2004) [unpublished].

9 See 'Baucus proposes FTAs in Asia to offset Chinese influence' *Inside U.S. Trade* 22:50 (10 December 2004) 15.

the abiding characteristics of the Latin American region is the extremely high inequality in income and health. In a recent Latinobarametro survey *The Economist* reports that seventy-one per cent of respondents think that their country 'is governed for the benefit of a few powerful interests.'[10] The hopes that trade liberalization would ameliorate this were dashed and, in any case, misplaced. Yet most experts agree that inequality and poverty, as well as widespread crime and corruption in many countries, pose a serious threat to the sustainability of democracy. And create serious impediments to domestic and international policy effectiveness. Deep integration requires increased convergence of per capita income to promote social cohesion: catch-up is the aim. Thus while the focus of the Washington Consensus was efficiency—a worthy and necessary objective—the 'second generation' reform has also underlined the importance of dealing with poverty and equity and a growing number of suggest that the serious inequality in Latin America contributes to lower growth.[11] But dealing with these issues is not like macro-economic stabilization. Second generation reform has landed development economics squarely into neo-institutional economics. And the truth must be faced: this is largely *terra incognita*. As a recent book on the subject states: 'Second-generation reforms are a motley crew, encompassing broad reforms of the state, the civil service, and the delivery of public services; of the institutions that create and maintain human capital (e.g., schools and the health care system); and of the environment in which private firms operate (more competition, better regulation, stronger property rights).'[12] That's part of the list. And as the authors note: 'Any economist can tell you that curtailing inflation requires lower money growth' but most are silent on how to reform legal, regulatory and political institutions.[13]

Nonetheless the research on institutions and the link with economic performance in the region has begun. Neo-institutional economics is the vogue. One hopes that it can be encouraged and that the minimalist mathematical model can be resisted. As one expert or innovation has noted 'case studies are data' and the need to pursue a wide range of these will be essential. Benchmarking best practices is

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10 'Democracy's low-level equilibrium' *The Economist* (August 14 2004) 41.

11 See Nancy Birdsall, Augusto de la Torre & Rachel Menezes, *Washington Contentious: Economic Policies for Social Equity in Latin America* (Washington, DC: Carnegie Endowment for International Peace and Inter-Americas Dialogue, 2001), and Pedro-Pablo Kuczynski & John Williamson, eds., *After the Washington Consensus: Restarting Growth and reform in Latin America* (Washington, DC: Institute for International Economics, 2003).

12 Patricio Navia & Andrés Velasco, 'The Politics of Second-Generation Reforms in Latin America' in Kuczynski, *ibid*. at 266.

13 *Ibid*.

usual in the private sector so why not the public sector?

Granted the second generation reform agenda is formidable but it's also necessary for deepening integration. So why not launch the process with some projects? That has already started, as is apparent in the Inter-American Development Bank's *Beyond Borders*.[14] Noting that infrastructure projects have significant network and scale economics, regional infrastructure projects should have had a high priority but did not. That changed when IIRSA (Integration of Regional Infrastructure in South America) was launched in 2002, as was the Puebla-Panama Plan (both with IDB support). Both are complex multinational, multisectoral, and multidisciplinary. Careful monitoring and analysis will yield extremely important insight not only into best practices but the vital link between infrastructure and growth. In rural areas infrastructure is essential if farm productivity is to improve: trade policy is pointless if you can't get your product to the market. As Robert Pastor points out NAFTA made no provision for infrastructure and the resulting delays because of increased traffic 'have raised the transactions costs of regional trade more than the elimination of tariffs has lowered them.'[15]

Regional infrastructure is a project of high priority. But there are many others that could be listed. Thus, for example, the financial crisis of the 1990s underlined the need to reform the capital markets and the banks. And the requirement to develop regional standards for fiscal discipline.[16] The list could be long and experts will have many important proposals. What is needed is an institution for selecting, launching, and evaluating the proposed projects. And a funding mechanism that includes contributions from all the countries in the hemisphere, allocated by an appropriate and mutually agreed formula. And a shared objective of deepening integration. The creation of the 'Convergence Club' in the OECD countries after the Second World War was certainly due to economic factors such as trade, investment, and technology transfer but also depended on what Moses Abramovitz called in his 1986 seminal article 'social capabilities' or what would be called institutions today.[17]

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14 Inter-American Development Bank, *Beyond Borders: The New Regionalism in Latin America*, (Washington, DC: Inter-American Development Bank, 2002) at 126-44.

15 Robert A. Pastor, 'North America's Second Decade' *Foreign Affairs* 83:1 (January/February 2004) 127.

16 John Williamson, 'Summing Up' in Kuczynski, *supra* note 11 at 311-12.

17 Moses Abramovitz, 'Catching Up, Forging Ahead, and Falling Behind' (1986) 46 Journal of Economic History 385.

CONCLUSION

The issue of deepening integration is complex and multi-faceted. In the Western Hemisphere the main approach has been preferential trade and investment policies. But today's world of ever-changing geography and balance of power requires a global approach. And a policy that recognizes that institutions matter.