

CEPAL

REVIEW

NUMBER 51
DECEMBER 1993
SANTIAGO, CHILE

ANIBAL PINTO
Director of the Review

EUGENIO LAHERA
Technical Secretary



UNITED NATIONS

CONTENTS

Inauguration of the "Fernando Fajnzylber" Conference Room and presentation of CEPAL Review No. 50	7
<i>Gert Rosenthal and Alejandro Foxley</i>	
Flying geese or sitting ducks? Transnationals and industry in developing countries	15
<i>Michael Mortimore</i>	
Industrial policy: where do we stand?	35
<i>Wilson Peres Nuñez</i>	
The challenge of industrial competitiveness	49
<i>Rudolf M. Buitelaar and Leonard Mertens</i>	
Rural society: its integration and disintegration	69
<i>Martine Dirven</i>	
Indigenous peoples and modernity	89
<i>John Durston</i>	
Women: productivity and labour in the United States	103
<i>Inés Bustillo and Nancy S. Barrett</i>	
Capital flows and their effect on the monetary base	113
<i>Helmut Reisen</i>	
Old and new trade policies	123
<i>Daniel Lederman</i>	
Integration and trade diversion	133
<i>Renato Baumann</i>	
European integration and Latin American trade	149
<i>Miguel Izam</i>	
Natural resources: the current debate	163
<i>Fernando Sánchez Albavera</i>	
Guidelines for contributors to CEPAL Review	179
Recent ECLAC publications	180

European integration *and Latin American trade*

Miguel Izam

*Economist, ECLAC Division
of International Trade,
Transport and Financing.*

Difficult as it is to forecast the magnitude of the impact of the Single European Market (SEM) on the rest of the world and on the European Community (EC) itself, the predominant feeling is one of concern, especially in the developing countries. This article seeks to determine how the completion of the SEM may affect Latin America's exports to the Community, using basically a short- and medium-term analytical approach. This is because a series of elements make it possible to predict with some confidence that the deepening of Community integration will take more time than originally foreseen. Especially noteworthy among these elements is the need for the EC to carry out an economic adjustment, for which purpose it will be necessary to coordinate the macroeconomic policies of its member countries more effectively and to resolve various important political problems, starting with the ratification of the Maastricht Treaty. In any event, it is reasonable to assume that, in the long run, the economic implications of the SEM for the rest of the world, including Latin America, will be positive. Section I of the article discusses the most probable effects of the deepening of European integration on the EC itself and on the rest of the world in the short and medium term. Section II examines the structural weakening of trade links between Latin America and the Twelve in recent decades and identifies the key reasons for this phenomenon, while Section III summarizes the effects that the SEM may have on Latin America's trade in the foreseeable future, which, unlike the Single Market's positive impact in the long term, may not be beneficial for Latin America.

I

The economic impact of the Single European Market on the European Community and on the rest of the world

1. Potential economic benefits for the EC

The basis of the SEM is the dismantling of physical, technical and fiscal borders, allowing people, goods, services and capital to circulate freely throughout the Community's territory. Theoretically, this deregulation will lead to greater competitiveness, forcing entrepreneurs to reduce prices and production costs. In turn, the drop in prices will stimulate demand and therefore raise output, and the resulting economies of scale will cut costs even further. Gains may also be expected from the use of new marketing strategies, the greater efficiency that business enterprises can achieve through the adoption of technological and management innovations, and the introduction of new production processes, all of which will be driven forward by the dynamics of the internal market itself.

The Cecchini report (Cecchini, 1988), which was prepared at the request of the Commission of the European Communities (CEC), quantifies the effects of streamlining customs formalities, government procurement procedures and financial services. It estimates that the greatest gains would result from the removal of barriers in financial services markets, in the expectation that the reduced costs of these services would be transferred to the economy as a whole. This would lower prices and increase demand and output, in turn bringing down the cost of credit and boosting investment.

All the foregoing would generate a 4.5% increase in the Community's gross domestic product (GDP), create 1.8 million new jobs, deflate consumer

prices by 6.1%, improve the balance of public finances by the equivalent of 2.2% of GDP and strengthen the current account of the Community's balance of payments by around 1% of GDP. The biggest growth in the Community's GDP would be obtained, however, if EC Governments adopted more expansionary fiscal policies and spent the entire increase achieved in the public sector balance; under these circumstances, the GDP growth rate would rise to 7.5%, 5.7 million new jobs would be created, retail prices would be reduced by 4.3%, but the current account would show a deficit equivalent to 0.5% of GDP. Both scenarios would result in a one-time gain in the medium term, four or five years after the culmination of the Single Market.¹

2. Some qualifications regarding the Cecchini report

It is important to note that the benefits projected in the Cecchini report are based on a methodology which takes into account only the static economic effects of the completion of the SEM. Consequently, it does not quantify the dynamic growth effects. In that regard, a study by Baldwin (1989) finds that the latter would be similar in magnitude to the static benefits projected by Cecchini. However, Baldwin's estimates have been seriously questioned, not only because of the methodology he used but also because, even if we accept that these effects would indeed manifest themselves, they would do so only in the long term.²

¹ It should be noted that the methodology used and the projections made in the Cecchini report served as the basis for a study directed by Emerson and others (1988), which was also published officially by the Commission of the European Communities (CEC) (1988).

² See the comments by Pierre-André Chiappori and Anthony Venables at the end of Baldwin's article (1989).

□ The author wishes to thank Héctor Assael, Armando Di Filippo, Robert Devlin and Jan Heirman for their valuable comments and Jaime Contador for his assistance in preparing the statistics used in this article.

The Cecchini report has also been severely criticized because the benefits it predicts, even in the case of its most pessimistic estimates, are based solely on the most favourable scenarios. An important argument in this connection is that the report does not delve deeply enough into the economic adjustment that would necessarily take place in the nations of the Community, nor does it examine in sufficient detail the intensity and duration of this adjustment or its possible adverse effects in terms of unemployment. In principle, taking full advantage of the economies of scale would involve restructuring production in a way that would inevitably lead to the disappearance of a significant number of the Community's enterprises.

Thus, a study by Smith and Venables (1988) notes that the number of EC enterprises would be likely to decline in all but two industries, namely cement and office machinery. The most extreme case is footwear, in which 207 of the existing 739 firms in the Community would disappear. A significant part of these losses would be concentrated in a few countries; for example, the United Kingdom would lose 46 of its 65 footwear firms, 31 of its 52 carpet factories and 1 of its 3 motor vehicle companies. This means that the unemployment problem could become more critical in the short or medium term, which might in turn bring social and political pressures to bear and thus lead to an increase in EC protectionism. Otherwise, the costs of unemployment would have to be absorbed by the governments through the payment of benefits or through a more expansionary fiscal policy, whose financing would have to come from the private sector and would thus tend to push up the interest rate.

Another line of criticism regarding the benefits projected by the Cecchini Report is that the report was written before certain historic events of momentous importance to the world, and especially to the EC, had taken place. These include, in particular, German reunification, the events that are reshaping central and eastern Europe, the Gulf War and the Enterprise for the Americas Initiative. It is also argued that a considerable portion of the anticipated benefits of the Single Market have already been reaped through intra-EC mergers, acquisitions, joint ventures and investments on the part of a number of Community enterprises.

All this explains why most economic analysts who have studied the topic agree that the Cecchini Report overestimates the economic gains that the EC

would obtain as a result of the establishment of the SEM. From this standpoint, the Institute for European-Latin American Relations (IRELA, 1991, p. 19) states that "various unofficial studies have estimated the acceleration of growth at no more than 1.5% - 2.5%". By way of illustration, it is worth noting Peck's estimate (1989, p. 289) that the economic gains would only be about 2% of the Community's GDP.

3. Likely prospects for the rest of the world

From a systemic viewpoint, the SEM can only be understood within its global historical context. On the one hand, this programmatic advance further deepens the most highly evolved regional integration model currently in existence. On the other, it is imperative that the EC enhance its technological capacity in order to improve its international competitiveness, especially compared with the United States, Japan and the newly industrializing countries (ECLAC, 1990a). Thus, looking beyond all the rhetoric and well-meaning statements, we see that the Community's motives for bringing the Single Market into operation clearly have to do with internal needs associated with its own development. The economic impact of the SEM on the rest of the world is thus a factor that will be determined primarily by the way in which Community dynamics unfold.

There can be little doubt that the SEM will have negative economic implications for the rest of the world, at least in the short and medium term. The basis for this assumption is that the elimination of internal barriers is clearly intended to increase Community demand for goods and services produced within its own territory, whose prices will be lower in comparison both with those existing before the Single Market and with those of non-Community imports. Indeed, the whole methodological formulation of the Cecchini Report is based on this argument. The Commission of the European Communities (CEC, 1989) has explicitly stated, moreover, that it expects the SEM to further stimulate the rising trend in the ratio of intra-Community imports to total EC imports.³

³ In 1963, intra-Community merchandise trade represented 48% of total EC trade (CEC, 1989), but by the beginning of the 1980s this coefficient had risen to over 50%, and by 1991 it stood at nearly 62% (CEC, 1992, p. III).

It is therefore evident that there will be diversion of trade in respect of imports from the rest of the world, and the scope of this diversion, other things being equal, will depend mainly on the price elasticity of EC demand. The Commission of the European Communities (1988) estimates that non-EC imports will drop by between 7.9% and 10.3%. It should be noted that this effect cannot possibly be offset by any increase in trade flows that might be created by additional EC growth, because under the assumption of linear behaviour, even if the generous estimate of a 4% rise in the Community's GDP proves to be correct, this would bring about an increase of only 0.4% in non-EC imports, since they are equivalent to rather less than 10% of Community GDP.

Ultimately, then, even in an optimistic scenario where the Community grows by an additional 4% and the reduction in its imports from outside the EC does not exceed 7.9%, exports from the rest of the world to the EC will still drop by 7.5%. Therefore, the net trade effect on non-EC economies will be generally negative. Moreover, a series of other factors would appear to indicate that the trade-related costs to the rest of the world would be much higher than this estimate.

Another element to bear in mind is that EC exports to third markets would be relatively more competitive, thereby crowding out exports from the other countries of the world and diverting a portion of their trade, to an extent which remains to be estimated. Another argument along the same lines has to do with the Community's order of preferences: a topic which, because of its importance to Latin America, will be discussed below. Nevertheless, it is worth noting here that some other regions of the world may also have to face considerable –although differentiated– economic costs, especially because the creation of the European Economic Space will promote trade between the Twelve and the members of the European Free Trade Association (EFTA), a group which is already the main trading partner of the EC.⁴

Another area where there may be negative implications for the rest of the world is that of economies of scale. If the EC can achieve minimally efficient operations of scale on its own, then restrictions on

imports from outside the Community would seem to be a natural counterpart (Dornbusch, 1989). Among other factors, this explains why a good many transnational corporations are reallocating resources to Community territory as a way of helping to forestall the negative impact which the SEM is likely to have on them. Between 1981 and 1983, 15% of United States foreign direct investment went to the EC, but between 1984 and 1987 the figure rose to 55%, while during the same years the corresponding indicator for Japan climbed from 10% to 17% (CTC, 1989).

Thus, there is every reason to assert that the Single Market will, implicitly and inherently, have adverse economic effects on the rest of the world.⁵ The real question, then, is not whether the Single Market will have negative implications for the rest of the world, but how strong the impact will be. Similarly, there is little point in asking whether the internal barriers to be eliminated will be transferred to the borders of the EC; as noted earlier, there is no need to do so in order to build a "European castle", i.e., a scenario which would have negative economic implications for the rest of the world even if the EC did not consciously and deliberately apply an economic policy expressly aimed in that direction, as it would in the case of a "Fortress Europe".

In any case, as we have already seen, everything seems to indicate that the Community will inevitably have to face up to the need to adjust its economy in the process of constructing the Single Market, at least in the short and medium term. Accordingly, higher unemployment can be expected to result from the enhanced competitiveness which will be made possible by the free circulation of goods and services throughout the Community's territory, and this could trigger the adoption of an expansionary fiscal policy (which would be perfectly consistent with the "social dimension" of the agenda being pursued by the Twelve), thereby pushing interest rates up and hence imposing a further burden on the developing countries, especially those with high levels of external indebtedness.

⁴ EFTA accounts for more than 20% of the Community's non-EC trade.

⁵ In addition to all the reasons mentioned earlier, it is common knowledge that when the Single Market is in operation the EC will apply certain technical standards to its imports which will make it even more difficult for exports from the rest of the world to gain access to this market. This point will be discussed in section III below.

Nor can the application of a complementary trade policy which would tend to exacerbate EC protectionism be ruled out.⁶ In this scenario, "Fortress Europe" would indeed be the appropriate term, in the sense that the "castle of the Twelve" would be explicitly and consciously defending itself against the rest of the world, launching "missiles" in the area of economic policy—especially trade policy—of a calibre which cannot be gauged at present but which would affect above all the developing countries,⁷ especially since the Community's capacity to negotiate and retaliate would undoubtedly be even stronger if all its trade regulations were centralized. It should also be noted that the developing countries' share of EC trade has been declining steadily in the past few years. In the 1980s alone, the share of the latter nations fell from 20% to 13% of Community

trade, whereas the share of the developed countries in EC trade rose from 76% to 84% during the same period.⁸

Nevertheless, the EC is making a big effort to show that the Single Market will have beneficial consequences both for the Community itself and for the rest of the world because, it claims, it will represent a big step towards deregulation and economic liberalization which will in turn give rise to a more competitive international economic environment. Even admitting that this might be true in the long run, however, it is difficult to reconcile this statement with the fact that the EC has been one of the main obstacles to the timely and fruitful completion of the Uruguay Round of GATT, which would indeed bring about a considerable improvement in the operation of the multilateral trading system.

II

Weakening of trade relations between Latin America and the EC⁹

The European Community is the biggest trading bloc in the world, not only in terms of its total trade but also of its merchandise transactions with the rest of the world.¹⁰ Since 1975, however, it has ceased to be the principal market for Latin American merchandise exports. In 1970 the EC received over 33% of all Latin America's exports, surpassing even the United States, which accounted for only 28%, but this order was reversed in the mid-1970s when the United States became the number one recipient of exports from the region, and the trend later became even more marked. Thus, in 1990 the EC bought only 24% of Latin America's exports, whereas the United

States received 36% of the total.¹¹ The Community has also become less important as a supplier of Latin American imports. In 1970, over a quarter of the region's purchases from abroad were from the EC, but in 1990 the figure stood at only 19%.

This situation becomes even clearer when the trends in Latin America's share in EC trade are taken into consideration. In 1965, the region received 6.1% of the Community's exports to the rest of the world, while it supplied 9% of the Twelve's imports from abroad. By 1990, however, these shares had fallen to 3.4% and 5.2%, respectively. There has thus been a structural weakening of trade relations between the

⁶ Such protectionism might even be backed up by discriminatory, non-transparent application of new technical standards in EC trade: an issue which will be analysed in the last section of this paper.

⁷ This view coincides with that of Emmerij (1990, pp. 248-249), who says: "To sum up on the question of trade diversion versus trade creation, my understanding is that the dangers for the developing countries are greater than the opportunities".

⁸ The remaining share corresponds to trade with Central and Eastern Europe, according to data from the *United Nations Monthly Bulletin of Statistics*, New York, various issues.

⁹ The statistical data on trade between Latin America and the EC whose source is not explicitly stated were prepared by the author on the basis of figures provided by ECLAC.

¹⁰ In 1990, the EC accounted for almost 38% of all world trade in goods, and even if only its merchandise transactions with countries outside the Community are taken into account, its share still came to 20% (ECLAC, 1992a).

¹¹ It is worth noting that whenever Latin America is taken as a whole, this obscures the big differences between the individual countries of the region. Thus, for example, Ecuador is the Latin American country for which the EC market is the least important (10%), but the opposite is true of Chile (37%), where the weight of EC trade is greater than that of the United States (17%).

two regions, reflected in Latin America's virtual marginalization from the circuit of European merchandise transactions.

It is important to note that trade is not the only area in which economic relations between the EC and Latin America have lost ground in the past few decades. A similar process has taken place in the financial sphere, especially in foreign direct investment. At the same time, the amounts of official development assistance which Latin America receives are not very significant as a proportion of total EC contributions to the developing world (Izam, 1991). All this stands in curious contrast with the notable tightening of political ties between Latin America and the EC (ECLAC, 1990b).

The responsibility for the structural economic distancing being witnessed between Latin America and the EC cannot be solely attributed to either of the two trading partners. In fact, over the past 20 years Latin America has been going through a process of virtual marginalization from world trade flows as a whole in terms of both exports and imports of goods.¹² This phenomenon is largely due to the fact that the region's export structure has not evolved in line with the dynamic changes that have taken place in international demand.¹³

Thus, even though the share of manufactures in Latin American exports stands at 34% (a notably high coefficient in comparison with the 9% recorded in 1970), the region's economies are still preponderantly primary-commodity exporters, although appreciable differences exist among them.¹⁴ The countries of Latin America need to confront this reality and gear their economies to a change in production patterns based on the deliberate and systematic absorption of technological progress in order to gain a greater competitive edge in the international market (ECLAC, 1990c and 1992c).

As a reflection of this situation, the structure of Latin American exports to the EC has been highly concentrated in commodities. In 1970, 61% of this trade flow was composed of agricultural commodities

and foodstuffs, and exports of non-manufactured goods as a whole represented 95% of the total. By 1990, the share of the latter had dropped to 77%, while the proportion of agricultural products had fallen to 42%. Even so, however, this means that over two-fifths of Latin American merchandise exports to the EC still face problems in gaining access to this market as a result primarily, but not exclusively, of the Community's Common Agricultural Policy (CAP).

In the past 20 years manufactures have increased from 5% to 23% of Latin American merchandise exports to the EC. This figure must be qualified, however. In 1980, the share of manufactures in Latin American exports to the Community was similar to that of manufactures exported to the United States, i.e., about 12%. In 1990, however, while manufactures represented 35% of Latin American exports to the United States,¹⁵ in the case of Europe they barely amounted to 23%, which was a good deal less than the share of manufactures in total Latin American exports to the rest of the world (34%) in that same year. Hence, the EC has lost importance as a market for Latin American exports of manufactures, with its share falling from 17% to 14% between 1970 and 1990.

The size of this decline cannot be explained merely by stating that the export performance of Latin American manufactures is lagging behind that of the newly industrializing countries of Asia, or by pointing out that the manufactures which Latin America exports to the EC are suffering waning demand in that market. The fact is that a significant proportion of these exports are subject to various protectionist measures that make it difficult for them to enter the Community. In short, as will be analysed below, Latin America's commodity exports and its sales of manufactures are both confronted with tariff and non-tariff barriers that hinder their access to the EC market.

1. Tariff barriers to EC imports

The average tariff rate applied by the EC to imports from GATT member countries is only about 5%. However, this apparently low figure masks the tariff barriers which the EC applies to production activities

¹² Its export coefficient has fallen from 4% to 3.2%, while that of imports has dropped from 3.8% to 2.7%.

¹³ Another very important reason has to do with the difficulties experienced by the region in gaining access to international markets for its exports.

¹⁴ For example, manufactures represent over 50% of Brazil's total exports, whereas in Ecuador they account for less than 2%.

¹⁵ Note also that the figures for exports from Latin America to the United States do not include transactions related to in-bond assembly industries.

that have a higher value-added component. This practice penalizes certain Latin American exports, especially manufactures, by impeding their access to the EC market through the application of duties that rise in direct proportion to the product's degree of processing. One illustration of the Community's escalating tariffs is the case of Chilean tomato exports to the EC market: fresh tomatoes are subject to a 3% tariff, but the rate for tomato paste is 18% (Sáez, 1992).

It should be noted that the EC applies tariff escalation schemes to a very substantial proportion of its imports of manufactures. What is more, in a number of economic sectors, this type of protectionism is more restrictive in the EC market than in the United States and Japan. It applies, *inter alia*, to the production chains for beef, vegetables, vegetable oils, paper, lead, zinc and petroleum, all of which are vitally important categories in Latin America's exports to the Twelve (Butelmann and Campero, 1992). The EC tariff structure thus distorts the competitiveness of the more highly processed Latin American products exported to this market, not only hampering their access to it but also, in many cases, actually preventing it.

2. Non-tariff barriers to EC imports¹⁶

In the agricultural sector, most non-tariff barriers (NTBs) are applied through the CAP, affecting temperate-zone crops—including sugar—which make up nearly three-quarters of the value of the Community's agricultural imports.¹⁷ These measures are applied not only to unprocessed agricultural commodities such as fruits, vegetables, seeds, fish and beef, but also to certain more highly processed goods such as wine. Besides the CAP limits, quantitative restrictions are also applied to exports of some tropical products such as bananas, as a means of reserving preferential access for exports from Caribbean and African countries. In the final analysis, over a quarter (in terms of value) of the foodstuffs exported by Latin America to the EC is subject to NTBs.

¹⁶ Statistical data on non-tariff barriers were taken from ECLAC, 1992b. Note that the coverage coefficients cited in the text mean that at least one non-tariff barrier is applied to Latin American exports in their target market.

¹⁷ The most frequently used measures are variable duties, reference prices and voluntary export restraints.

Manufactures are also liable to various types of non-tariff barriers to access to the EC market.¹⁸ Excluding chemicals, 26% of the total value of Latin American manufactures exported to the EC is subject to NTBs. Textiles, clothing and footwear—which face barriers equivalent to 90%, 55% and 99% of their respective values—are among the most seriously affected goods.

Apart from the above-mentioned sectors, NTBs have a strong impact on two other categories of Latin American exports to the Twelve, namely, fuels and iron and steel, whose exposure to protectionist measures amounts to 44% and 92%, respectively. In sum, 22% of the total value of Latin America's merchandise exports to the Community is liable to non-tariff barriers, which have a relatively greater effect on manufactures than on foodstuffs and agricultural products.

In its use of non-tariff barriers, Europe is a much more protectionist market with regard to Latin American exports than are the United States and Japanese markets, since NTBs are applied to only 13% of Latin American merchandise exports to each of the latter markets. The Community's non-tariff protectionism is also systematically higher than that of both the United States and Japan for Latin American exports of fuels, iron and steel, and manufactures other than chemicals. In foodstuffs, Japan's non-tariff barriers exceed those of the Community, which in turn are higher than those imposed by the United States.

Because of the great heterogeneity of the Latin American countries, the implications of the Community's non-tariff barriers are very different, in terms of magnitude, for each individual country. These effects depend on the composition and total value of the various products which the countries export to the EC¹⁹ and on the sectoral distribution of NTBs in that market. Thus, in terms of the proportion of total exports from each of the countries to

¹⁸ The most frequently used instruments are quantitative limits, supervision measures, licenses, quotas, voluntary export restraints, anti-dumping measures, countervailing duties and safeguard clauses.

¹⁹ Nearly 80% of Latin American exports to the EC come from just four countries, namely Brazil (38%), Argentina (14%), Mexico (13%) and Chile (12%). The concentration as regards exports of manufactures is even greater, with three countries—Brazil, Argentina and Mexico—accounting for almost 85% of total Latin American exports of such goods to the EC.

the EC that is subject to non-tariff barriers, those which suffer most are Mexico (52%), Uruguay (47%), Ecuador (29%), Argentina (28%), Costa Rica (20%) and Honduras (20%).²⁰ In contrast, the consequences are practically nil for Nicaragua (2.4%), Bolivia (0.1%) and El Salvador (0.1%). These figures indicate that the effects on Latin America of the completion of the Single European Market are likely to be highly differentiated in the various countries that make up the region.

In conclusion, EC protectionism is responsible, on the one hand, for much of the gradual weakening of the Community's trade with Latin America in both commodities and industrial goods and, on the other, for the fact that the share of manufactures in Latin American exports to the EC market is still very small and, in fact, is even well below the share of these products in Latin America's total exports. All this seems to suggest that the Community assigns relatively low priority to its trade with Latin America.

3. The European Community's scale of preferences

The Community's first aim is to strengthen its ties with the member countries of EFTA (Delors, 1991). At the same time, as a result of the political and economic reforms being undertaken in Central and Eastern Europe, the EC is having to redefine its relations with these countries, both for economic and social reasons and from a geo-political standpoint. In fact, there is currently a spate of trade negotiations between the Community and practically all these nations, a number of which already enjoy trade preferences under association agreements or under the Generalized System of Preferences (GSP).

As for the Community's position regarding the developing world, the countries with the highest priority are those of Africa, the Caribbean and the Pacific (ACP) which are signatories to the Lomé Convention. They are former colonies of European countries to which the EC offers trade preferences, institutional advantages and development assistance.

²⁰ The sectors affected in the various countries are as follows: Mexico, mainly petroleum; Uruguay, foodstuffs and textiles; Ecuador, foodstuffs and clothing; Brazil, foodstuffs, iron and steel, and footwear; and Argentina and Chile, foodstuffs. Tropical products, particularly bananas, are seriously affected in such Central American countries as Costa Rica, Honduras and Guatemala, as well as in Colombia and Ecuador.

The trade preferences include free access for industrial goods and most tropical agricultural commodities, even though some of them compete with the Community's own products, as in the case of sugar.

The second line of Community preferences is extended to the Mediterranean countries which have signed agreements with the EC on trade cooperation and development aid. These agreements provide for duty-free entry of industrial goods other than textiles. Agricultural products that compete with Community products protected by the CAP are subject to quotas, in connection with which they receive partial exemption from customs duties. It should be noted that a number of these countries have applied for membership in the EC.²¹

The EC has also shown considerable interest in the Arab countries of the Persian Gulf region, essentially because of the Community's energy dependency on that part of the world. Specifically, the EC has sought to expand existing trade agreements to include matters concerning trade cooperation, technology transfer, investment incentives, agricultural development and other areas related to development assistance.

The Asian and Latin American countries come last in terms of priority, since they only enjoy the advantages to which they are entitled under the GSP.²² Moreover, it is important to note that, in the case of Latin America, the GSP has not afforded the anticipated benefits, even though the advantages it does provide have increased considerably during the past decade. In 1980, 10% of Latin American exports to the EC entered under the GSP, and by 1988, this coverage had risen to 20% (IRELA, 1992). Because of certain features of the Generalized System, the Latin American countries with the most highly diversified structures of production and well-established trade networks are the ones that have gained the most from it (e.g., Brazil, and to a lesser extent, Argentina and Chile).

²¹ Namely Cyprus, Malta, Morocco and Turkey.

²² Apart from the GSP which the EC grants to the entire Latin American region on an equal basis, some nations are accorded special treatment whereby they receive greater benefits than those afforded by the common system. However, these preferences are temporary in nature, and the advantages they provide are not comparable with those received by the ACP countries. For example, the Andean countries are granted such benefits as a way of encouraging them to produce crops other than coca.

There are a number of reasons for Latin America's limited benefits from the Community's GSP. First, the great majority of agricultural products are excluded from the System, because since their entry would affect the economy of the Twelve, they are therefore considered "sensitive" products. In effect, this means that a large proportion of Latin American exports to the EC are simply denied the advantages of the Community's system of preferences. Second, in Latin American trade circles the GSP is accused of suffering from a notable lack of transparency and coherence, which severely hinders its effective use and leads to difficulties in its application; in particular, countries must apply for concessions in order to receive them, and the System thus tends to favour countries that possess more export experience and dynamism, such as certain Asian nations.

It is hoped that in the future the EC will reformulate the GSP by giving it greater stability and easing

the rules of origin, as well as opening up the possibility of granting a cumulative form of treatment at the regional or subregional level, which would facilitate access to the EC for Latin American exports and also provide a further incentive for the economic integration of Latin America (SELA, 1992). However, "the possibilities are remote that the GSP will have a significant impact on the current situation in the coming years" (IRELA, 1992, p. 28).

The foregoing lends weight to the view expressed by a President of the European Parliament, who said: "to put it bluntly, Europe has never set its sights on Latin America" (Barón, 1991, p. 95). It is therefore probable that the EC will continue to show little economic interest in Latin America, although some advances may still be made through the various forums that exist for dialogue between the Twelve and Latin America.²³

III

Effects of the Single European Market on Latin America's trade

1. General effects

As we have seen from the foregoing, all in all the impact of the Single Market on Latin American trade will be more negative than for the rest of the world. This is mainly a consequence of the historical process of weakening economic relations between Latin America and the EC—a phenomenon for which both sides are responsible, although not necessarily to the same degree—and of the fact that the Twelve have shown little interest in this region of the developing world. The trade costs to Latin America cannot be precisely measured, for they will basically depend, first, on these developing countries' capacity to react in a way that will increase their exports' access to the EC market and, second, on the economic dynamics generated by the Single Market within the EC and the possible further heightening of Community protectionism.

In institutional terms, EC protectionism is scheduled to undergo a fundamental change in 1993. The Single Market presupposes a common trade policy,

and the countries will therefore not be able, on an individual basis, to impose national restrictions on certain direct imports from third countries or on products which have passed in transit through other Community countries.²⁴ In the past, these national barriers have been utilized, in particular, to protect "sensitive" sectors such as textiles, clothing, footwear, agriculture and steel, all of which, as noted earlier, are a vital part of Latin America's export trade with the EC. It is not clear, however, whether the benefits afforded by the establishment of homogeneous Community measures to take the place of national restrictions will outweigh the potential costs.

²³ One example would be consideration of the feasibility of expanding the operations of the European Investment Bank to include the financing of Latin American projects.

²⁴ Consequently, article 115 of the Treaty of Rome (the Treaty establishing the European Economic Community) will no longer be valid.

The types of restrictions most frequently applied to these sectors are quotas, the use of "basic import prices", which can be used to impose anti-dumping measures, and voluntary export restraints. The EC may be tempted to utilize these types of protection more intensively after the establishment of the Single Market (Koopmann and Scharrer, 1989).

These measures are on the very borderline of legality under GATT, since they contravene the spirit if not the letter of the General Agreement. They are therefore known as "grey-area measures" and are the subject of negotiation in the Uruguay Round under the heading of safeguards. Other instruments of major concern are local-content rules, reciprocity agreements and the possible abuse of what is known as the "new trade policy instrument".²⁵ Should the Uruguay Round fail, this would encourage the build-up of trade mega-blocs. In this scenario, the EC (but not only the EC) might close its borders by erecting extraordinarily high protectionist barriers.

Community protectionism could also increase under the Single Market even if the Uruguay Round reaches a successful conclusion, however. As already noted, the number of firms in the Community as a whole would decline in practically all production sectors (Smith and Venables, 1988). Moreover, it is a fact that the less developed countries within the Community will, as a result of the Single Market, face a very critical situation in certain economic sectors which are in direct competition with Latin American exports. Thus, a recent EC study found that the hardest-hit categories of exports from Greece and Portugal will be textiles and knitwear, the food industry and metal products (Instituto de Estudios Económicos, 1991). All these are traditional labour-intensive sectors, and their importance is illustrated by the fact that the textile industry, which provides 9% of all jobs in the manufacturing sector at the Community level, accounts for over 23% of such jobs in Greece and Portugal (ECLAC, 1992a). It would be no surprise, then, if these nations try to secure protection against third countries when the Single Market comes into effect.

It is important to add that an increase in protectionism is to be expected not only in "sensitive"

²⁵ This instrument allows private EC entrepreneurs to apply directly to the Commission for protective measures against imports that allegedly use "unfair trading practices".

traditional sectors, but also in others that may emerge in the event of an economic adjustment, which, as stated earlier, is quite likely. This raises serious doubts about the accuracy of estimates regarding the benefits that would accrue to Latin America and the rest of the developing countries as a result of the Single Market, when those estimates are based on methodologies which assume that the degree of EC protection will remain stable.²⁶

Another cause of concern is the new common provisions which will enter into effect following the elimination of the national technical borders that have prevented the free circulation of goods within the Community. These provisions mainly deal with production, labeling and packaging standards; brand-name registration and quality certification procedures; safety and consumer protection standards; and environmental and plant and animal health regulations.²⁷ According to the United Nations Conference on Trade and Development (UNCTAD), most of these measures are considered to be tantamount to non-tariff barriers to trade.

There is no question but that it will be easier and less costly and uncertain to deal with each of the EC countries on the basis of a single system of standards and of commercial and economic requirements, instead of negotiating individually with each of the twelve nations that make up this integration scheme. However, it is more than likely that these provisions will be harmonized on the basis of the strictest national laws, and this will make it more difficult, in the short term, for some Latin American products to gain access to the market. The EC would do well, therefore, to give the Latin American countries enough time to adapt to the new standards, with the actual amount of time depending on their level of development. This extension could also be complemented with meaningful, integrated support in the form of dissemination of the relevant information among the economic agents.²⁸

²⁶ For an example of this type of estimate, see Page, 1990.

²⁷ As of 1993 the EC countries were to be required to recognize as equivalent the standards of the other countries, with the temporary exception of regulations concerning public health and safety.

²⁸ This support could be provided through the joint programme currently being designed by the Permanent Secretariat of SELA and the Commission of the European Communities for evaluating the impact of the harmonization of EC technical standards on Latin American exports.

It is a fact that European consumers are leaning more and more towards higher-quality products, since their standard of living, basically reflected in a high and ever-increasing level of disposable income, is such as to allow them to turn their attention to health-related and environmental matters. One expression of this phenomenon is the tightening of Community environmental regulations, which is expected to cause some EC smokestack industries, especially mineral-processing plants that pollute the environment, to relocate to Latin America (Grandi, 1991).²⁹ As IRELA put it, "Latin America will thus be in a position to benefit not only from an increase in its exports of minerals to the EC but also from sales having a higher value-added component" (IRELA, 1991, p. 38).

This point of view, which appraises only the short-term benefits for Latin America, takes into account neither the need for ecologically sustainable development in the countries of the region nor the fact that environmental protection is the whole world's responsibility. Moreover, the supposed gains for Latin America of serving as a "garbage dump" might not even be realized, since the EC plans to maintain its tariff escalation system, and Community ecological standards will also be extended to imports, as for example in the case of Latin American tropical timber (Grabendorff, 1992, p. 230).

In any event, Latin America will have to meet the challenge of responding to these new international demand requirements by diversifying its export structure with the help of more aggressive commercial policies and by making the necessary investments to increase the competitiveness and quality of its products through the application of socially and environmentally sustainable economic models. It is vital, however, that these standards should operate transparently and on a non-protectionist basis. Unfortunately, there is no guarantee that the EC will apply these measures in an unbiased manner. This concern has led one United States Assistant Secretary of State for Economic and Business Affairs to affirm that his country's "bottom line" in this critical area is transparency" (McAllister, 1989, p. 20).

²⁹ However, the relocation of polluting enterprises from developed to developing countries is a phenomenon which is not yet borne out by sufficient empirical evidence (Dean, 1992).

All the above factors indicate that the EC's non-tariff protectionism will probably increase as the Single Market enters into operation. Against this backdrop, the cost of a "Fortress Europe" –whether partly or fully realized– would be higher for Latin America than for the rest of the world. However, as discussed in Section I of this article, the impact on both areas would be less under the "European castle" hypothesis, i.e., in a scenario in which protectionism does not get worse. Even in this case, however, for the same reasons mentioned earlier, the cost for the Latin American countries would still be comparatively greater than for the rest of the world.

2. Effects on specific sectors

The demand for most agricultural products shows little price or income elasticity, so that neither the lower prices nor higher incomes which are anticipated outcomes of the SEM will lead to significant increases in the Community's demand for imports. Such increases are even less likely if an appreciable proportion of Latin American merchandise exports to this market must compete directly with European products or with the output of the African, Caribbean and Pacific countries, which are protected by the CAP and by the Lomé Convention, respectively.

The products that could be affected the most severely include bananas, tropical woods, sugar, cocoa and temperate-zone agricultural products such as grains, soya and products thereof. This would hurt practically all the Latin American countries in varying degrees. On the other hand, one product on which the impact may be positive is coffee, but even so this would benefit the Central American countries more than, say, Brazil or Colombia, since Community consumer preferences will probably be for the higher-quality coffee blends from Central America (Grabendorff, 1992, p. 229).

The demand for minerals and metals is also quite inelastic with respect to price and income, and Community imports of these goods are therefore unlikely to increase significantly. Moreover, as one of the main purposes of the Single Market is to enable European firms to absorb technological innovations and thus reach higher levels of efficiency, the introduction of new production processes may be expected to lead to a decline in the Community's consumption of minerals and metals.

Indeed, the Community's technology policy points in this direction, since its objectives include

promoting the replacement of traditional materials by less costly ones (e.g., fibre optics) and the recycling of waste. Thus, "products that may run up against problems or sustain negative impacts include iron ore and concentrates and undressed ores of such non-ferrous metals as copper and bauxite" (Grandi, 1991, p. 100). At the same time, since the EC is expected to maintain its tariff escalation system, the prospects for more highly processed goods are not very bright either. The Latin American countries whose mineral and metal exports to the EC may be the most severely affected are Bolivia, Brazil, Chile, Peru and Venezuela.

The outlook for oil exports is even bleaker. IRELA reports that representatives of the Member States of the Conference on Security and Cooperation in Europe, of the Republics of the former Soviet Union and of Australia met on 17 December 1991 in the context of the Hague Conference on the European Energy Charter, "whose ultimate purpose is to create an energy market in Europe based on the rich petroleum and gas reserves of the former USSR. The combination of supplies from the East and investments from the West could eventually lead to European self-sufficiency in the energy sector, which would cause Latin American fuel exports to lose a large portion of their European market" (IRELA, 1991, pp. 36-37). Moreover, the EC's energy policy involves using energy-saving technologies or petroleum substitutes. Thus, the impact on Ecuador, Mexico and Venezuela would be significant.

In contrast, the demand for manufactures is highly income- and price-elastic. Consumption of manufactured goods may therefore be expected to rise, but this will not necessarily increase imports of such products from non-EC countries, since the Single Market will make the Community's own production more competitive, especially in this sector. Hence, even if Community protectionism does not increase, the outlook is bleak for Latin America. The tariff escalation system and the existing non-tariff barriers are quite enough, just as they have been in the past, to form a tough barrier to Latin American manufactures seeking access to the EC.

As a matter of fact, just three categories of manufactured products—footwear, textiles and leather goods—account for over 5% of Latin America's total exports of tangible goods to the EC, and in all three, Latin America has gradually been losing ground in terms of its share of Community imports, while stronger East European competition may

further accentuate this decline in coming years (Grabendorff, 1992).

Latin America's trade in services will not readily benefit from European liberalization either, since it is not yet sufficiently competitive in international markets in this sector. One of the few exceptions to this rule is tourism: an activity that could eventually bring some benefits to Latin America owing to the higher incomes of EC citizens.

In conclusion, all the indications are that the repercussions of the Single Market on Latin America's trade will, at least in the short and medium term, be negative. This applies not only to the Community's own territory but to the rest of the world as well, since the EC will also improve its own competitive position in international markets, including that of Latin America.³⁰ Thus, the Latin American region has no choice but to face the challenge of making the necessary structural transformations in order to become more fully integrated into the world economy while also broadening its trade options so as to diversify its export products and markets as much as possible. Even so, the need to build stronger economic ties with the EC should not be neglected. To this end, Latin America will have to strengthen its bargaining power both by making a greater effort to work towards regional integration and by making better use of existing forums for political and economic dialogue with the EC.

3. Other considerations

It should be borne in mind that the above conclusions are based on an approach that focuses on the Single Market's short- and medium-term effects. In the long run, a more optimistic scenario could be envisioned, for three reasons. The first would be the EC market's eventual success in dealing with the vicissitudes of economic adjustment within the framework of more coherent macroeconomic policies. It is quite probable

³⁰ A drop in the prices of Latin American imports coming from the EC is therefore likely. However, this benefit may be offset, first, by the costs associated with a decline in the competitiveness of Latin American exports *vis-à-vis* Community exports in external markets and, second, by the possible deterioration of the terms of trade for Latin America's principal exports as a consequence of the greater international supply resulting from the exportation of European products that compete with those of Latin America (especially temperate-zone farm products).

that the Single Market, as it matures, will move towards a dynamic restructuring of comparative advantages among its member countries and will attain high enough levels of productive efficiency to make its products more competitive in the international market.³¹ Under such conditions, EC protectionism on a scale comparable to present levels or those foreseeable over the medium term would no longer be justified. Furthermore, in the long run the dynamic benefits of deepening the European integration process should manifest themselves, with the resulting external economies for the rest of the world.

The second reason would be the assumption that the multilateral trading system will evolve in

the direction of greater openness and competitiveness, with international trade regulations being geared to the achievement of greater transparency in international trade, not only in goods but also in services and financial flows. An obvious precondition for this outcome is the satisfactory conclusion of the Uruguay Round within a reasonable space of time.

Finally, with regard to the possible benefits for Latin America, it will be crucial for the countries of the region to continue making headway in their efforts to restructure production within the framework of an open economy and political and economic stability so that they may develop the dynamic comparative advantages they need to fill the available niches in international markets. This means that the Latin American export structure will have to evolve in a dynamic manner in line with the changing conditions of world demand, which will require the application of a technically, economically, socially and environmentally sustainable long-term development model.

(Original: Spanish)

³¹ All this would be in a context of European political and economic reorganization involving not only the successful resolution of certain political conflicts within the EC and the strengthening of its free trade agreement with EFTA, but also the attainment of a more integrated and virtually continental-scale European economic scheme.

Bibliography

- Baldwin, R. (1989): The growth effects of 1992, *Economic Policy*, No. 9, Cambridge, England, Cambridge University Press, October.
- Barón, E. (1991): Una atracción no correspondida, *Pensamiento Iberoamericano. La nueva Europa y el futuro de América Latina*, special issue, Madrid, Ibero-American Cooperation Institute (ICI)/State Agency for the Fifth Centenary.
- Butelmann, A. and M. P. Campero (1992): Medición del escalonamiento arancelario de las exportaciones chilenas a los EE.UU., *Estrategia comercial chilena para la década del 90. Elementos para el debate*, A. Butelmann and P. Meller (eds.), Santiago, Chile, Economic Research Corporation for Latin America (CIEPLAN).
- Cecchini, P. (1988): *The European Challenge 1992: the Benefits of a Single Market*, Aldershot, Gower Publishing Company Limited.
- CEC (Commission of the European Communities) (1988): The economics of 1992. An assessment of the potential economic effects of completing the internal market of the European Community, *European Economy*, No. 35, Brussels, March.
- (1989): *European Economy*, No. 39, Brussels, March.
- (1992): *Suplemento-objetivo 92*, No. 9, Brussels, November.
- CTC (United Nations Centre on Transnational Corporations) (1989): *The CTC Reporter*, No. 27, New York, United Nations, Spring.
- Dean, J. (1992): Trade and environment: a survey of the literature, Patrick Low (ed.), *International Trade and the Environment*, World Bank Discussion Papers, No. 159, Washington D.C.
- Delors, J. (1991): Primero reforzar, después ampliar, *Pensamiento Iberoamericano. La nueva Europa y el futuro de América Latina*, special issue, Madrid, Ibero-American Cooperation Institute (ICI)/State Agency for the Fifth Centenary.
- Dornbusch, R. (1989): Europe 1992: macroeconomic implications, *Brookings Papers on Economic Activity*, No. 2, Washington, D.C., The Brookings Institution.
- ECLAC (Economic Commission for Latin America and the Caribbean) (1990a): *Europa 1992 y sus consecuencias económicas sobre América Latina* (LC/R.918 (Sem.59/3)), Santiago, Chile, September.
- (1990b): *¿Cooperación o divergencia? Hacia una nueva agenda en las relaciones euro-latinoamericanas* (LC/R.929 (Sem.59/5)), Santiago, Chile, October.
- (1990c): *Changing Production Patterns with Social Equity* (LC/G.1601-P), Santiago, Chile, March. United Nations publication, Sales No. E.90.II.G.6.
- (1992a): *La política comercial de la Comunidad Económica Europea después de 1992: implicaciones*

- para América Latina (LC/R.1139), Santiago, Chile, April.
- (1992b): *Las barreras no arancelarias a las exportaciones latinoamericanas en la Comunidad Económica Europea, los Estados Unidos de América y el Japón* (LC/R.1201), Santiago, Chile, October.
- (1992c): *Social Equity and Changing Production Patterns: an Integrated Approach* (LC/G.1701 (SES.24/3)), Santiago, Chile. United Nations publication, Sales No. E.92.II.G.5.
- Emerson, M. and others (1988): *The Economics of 1992: the EC Commission's Assessment of the Economic Effects of Completing the Internal Market*, Oxford, Oxford University Press.
- Emmerij, L. (1990): Europe 1992 and the developing countries: conclusions, *Journal of Common Market Studies*, vol. XXIX, No. 2, special issue, Oxford, Basil Blackwell, December.
- Grabendorff, W. (1992): European integration: implications for Latin America, Colin I. Bradford (ed.), *Strategic Options for Latin America in the 1990s*, Paris, OECD Development Centre.
- Grandi, J. (1991): El impacto del mercado único europeo para América Latina: obstáculos y oportunidades, *Integración Latinoamericana*, No. 167, Buenos Aires, Institute for Latin American Integration (INTAL), May.
- Instituto de Estudios Económicos (1991): El impacto del mercado único en el sur de Europa, *Revista del Instituto de Estudios Económicos*, No. 3, Madrid.
- IRELA (Institute for European-Latin American Relations) (1991): *El mercado único europeo y América Latina*, Dossier No. 34, Madrid, September.
- (1992): *América Latina y Europa: hacia el año 2000*, Dossier No. 40, Madrid, September.
- Izam, M. (1991): Europe 92 and the Latin American economy, *CEPAL Review*, No. 43 (LC/G.1654-P), Santiago, Chile, April.
- Koopmann, G. and H. Scharrer (1989): EC trade policy beyond 1992, *Intereconomics*, vol. 24, No. 5, Hamburg, Verlag Weltarchiv GmbH, September-October.
- McAllister, E. (1989): A U.S. perspective on EC-92, *Economic Impact*, No. 69, Washington, D.C., United States Information Agency (USIA).
- Page, S. (1990): *Some Implications of Europe 1992 for Developing Countries*, London, Overseas Development Council (ODC), December.
- Peck, M. J. (1989): Industrial organization and the gains from Europe 1992, *Brookings Papers on Economic Activity*, No. 2, Washington, D.C., The Brookings Institution.
- Sáez, S. (1992): Chile y la Comunidad Económica Europea, in A. Butelmann and P. Meller (eds.), *Estrategia comercial chilena para la década del 90. Elementos para el debate*, Santiago, Chile, Economic Research Corporation for Latin America (CIEPLAN).
- SELA (Latin American Economic System) (1992): *Reunión sobre comercio entre el Grupo de Río y la Comunidad Europea. Nota de la Secretaría Permanente*, Caracas, October.
- Smith, A. and A. Venables (1988): An assessment based on a formal model of imperfect competition and economies of scale, *Research on the Cost of Non-Europe. Basic Findings*, vol. 2, Luxembourg, Commission of the European Communities, Office for Official Publications of the European Communities.