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Current Challenges and Prospects

The FTAA process has had a star-crossed history. Each summit meeting has been followed by serious financial crises in the region. The Miami Summit was followed almost immediately by the collapse of the Mexican peso; the optimism from the Santiago Summit faded several months later in the wake of the Brazilian financial crisis. In both cases, national problems were contagious and infected seemingly prosperous neighbors and trading partners in the hemisphere. Indeed, Argentina's slow recovery from the Brazilian shock has raised concerns that history could repeat itself after the Quebec Summit.

Each crisis tested national resolve to sustain domestic reforms and to pursue regional integration initiatives. But, interestingly, in each case the national responses—particularly the reform of exchange rate regimes and financial sector regulations—strengthened the ability of Latin American countries to continue restructuring and opening their economies.

The leaders of the 34 countries in the Western Hemisphere who convened at the Third Summit of the Americas therefore looked with some satisfaction at the progress achieved during the first three years of FTAA negotiations. Despite the recurring financial crises, the FTAA process survived and continued to advance, albeit with foot-dragging by countries suffering from the effects of the tequila and samba shocks.

As shown by the readiness indicators in chapter 2, most Latin American countries are now better prepared to deal with new economic maladies and to adapt more quickly to rapidly changing developments in global markets than they were at the time of the Miami Summit more than six years ago. The chances that such problems will derail the hemispheric initiatives have been significantly reduced.

But complacency is not in order. Latin American and Caribbean (LAC) countries remain vulnerable to economic and political shocks that could complicate their efforts to undertake FTAA obligations. US leadership of the FTAA process is still hampered by the lack of fast track negotiating authority and continuing concerns about globalization initially raised in the debate over the NAFTA. Combined, these factors have been a drag on the FTAA negotiations, as other countries in the hemisphere cite the ambivalent US policy as an excuse to not move forward with their own reforms.

Overall, Western Hemisphere countries face five broad challenges that need to be addressed during the next stages of substantive negotiations. Summit leaders will have great difficulty in fulfilling the ambitious vision of free trade and investment in the hemisphere without immediate attention to these issues.

Current Challenges

The first challenge is economic: Will economic growth be strong enough over the near to medium term to allow the LAC countries to implement and sustain the reforms so vital to their development and so critical to their acceptance and enforcement of free trade obligations under the FTAA?

Economic growth has recovered from the weak commodity prices and financial shocks of the late 1990s, but prospects that seemed bright at the Santiago Summit in April 1998 are now much more muted. In early 2001, the World Bank (2001) projected real GDP growth of just over 4 percent for Latin America and the Caribbean for the period 2000–02, with per capita GDP rising by 2.6 percent—an improvement over the negative per capita GDP results in 1999–2000. However, these estimates already have been scaled back substantially due to the weakening US economy and energy problems in Brazil. In any event, such modest growth prospects are not enough to provide resources to meet growing social needs and ensure continued domestic political support for economic reforms, including the liberalization required by the FTAA.

In addition, despite good overall economic performance over the past decade, many LAC countries face growing problems due to increasing inequality between the haves and the have-nots in their societies. Perhaps most critically, unemployment remains high in many countries; it averaged 9 percent across the region in late 2000 (ILO 2000). In some countries, the problem is nearing the crisis stage; jobless claimants represent 15 to 20 percent of the workforce in Colombia, Jamaica, and Argentina. Moreover, the ILO (2000) reports that labor conditions—measured by changes in the number and quality of jobs, real wages, and productivity—actually deteriorated during the 1990s in Argentina, Colombia, Ecuador, Paraguay, and

Venezuela. Rising unemployment (when coupled with highly overvalued exchange rates) often leads to rising protectionist demands. The correlation is already evident in Argentina, where layoffs in the auto sector have provoked opposition to free trade in those products within the Mercosur.[1]

On top of their current economic woes, Latin American countries are now burdened by their earlier successes. The Washington Consensus set out guidelines for macroeconomic stabilization but did little to address the problems that arise when those domestic macroeconomic reforms succeed. After a decade or more of reform, countries still confront problems regarding how to share the wealth so as to promote higher living standards for the whole population, how to regulate economic activity in a more open and competitive environment, and how to strengthen the rule of law in societies long dominated by administrative fiat or military command. The success of the FTAA will depend importantly on the ability of countries to undertake so-called "second generation" reforms that enable them to address these pressing democratic, economic, and social problems.

The second challenge derives from the tepid political backing government officials and business leaders have given to the talks to date. Despite strong rhetoric and the noble declarations of the summit meetings, the FTAA has not been a front-burner issue for most countries in the hemisphere. To be sure, this low profile has had some salutary effects: the technical-level talks have proceeded in deliberate fashion without substantial attacks from the antiglobalization groups that protested, sometimes violently, against ministerial meetings of the WTO (December 1999 in Seattle) and the IMF (April 2000 in Washington and September 2000 in Prague). As summit leaders discovered in Quebec City, however, this was but a momentary reprieve.

There are several reasons for the restrained support for the FTAA talks so far. For one thing, the 2005 deadline for ending the negotiations is just too far beyond the time horizon of elected officials. Political leaders live in the near term. They face continuing distractions from pressing domestic problems and international initiatives. Moreover, government officials have not been pushed hard by their business leaders, who have specific lobbying interests in ongoing national reforms and see little prospect for the FTAA talks to produce concrete benefits for them over the next few years. Bluntly put, one should not expect business leaders to actively support and lobby their elected leaders to conclude and implement a hemisphere-wide free trade pact until after market access negotiations move into their final stages and the likely results begin to take shape in 2003–04.

Tepid political support for the FTAA is particularly troublesome in the hemisphere's two largest economies. Brazil, the largest country in South America, has focused on recovery from its own domestic economic crisis

1. For an analysis of the relationship between exchange rate overvaluation and pressures for import protection, see Bergsten (1998).

and the related challenge of consolidating its customs union with its Mercosur partners. This has led some Brazilian manufacturers to lobby strongly against the FTAA. In North America, the United States has been plagued by a fracturing of the traditional bipartisan consensus on trade policy, which has made negotiators very cautious about new commitments that require reform of US trade barriers. Indeed, US trade politics pose such a fundamental challenge to the future of the FTAA that I discuss it separately below as the last and most important obstacle to the talks. More generally, however, the level of engagement by both government and business leaders will have to increase if negotiators are to receive the political support they need to reform longstanding trade barriers and achieve free trade in the hemisphere.

The third challenge is the continuing political and economic strife in the Andean Community, where political corruption is endemic. Colombia, formerly a bastion of peace, democracy, and prosperity, is beset with a debilitating insurrection by both left- and right-wing paramilitary forces. Governments have collapsed in Ecuador and Peru, exposing the shallow roots of democracy in those countries. In Venezuela, President Hugo Chávez has force-fed constitutional changes that strengthen his hold on power and raise concerns about his autocratic intentions.[2]

Furthermore, economic growth in the Andean region has been buffeted since 1998 by the samba shock, weak commodity prices, and political mismanagement. The Brazilian crisis hit the Andean countries hard, contributing to a deep recession in Ecuador, Venezuela, and Colombia in 1999. The region recovered somewhat in 2000 but is still clinging to the fragile lifeline of high oil prices.[3] Moreover, as noted above, unemployment has increased substantially throughout the region, reaching 20 percent in Colombia and about 15 percent in Ecuador and Venezuela in late 2000. Peru and Bolivia also suffered large jumps in unemployment from 1995 levels (ILO 2000).

These regional problems already have infected neighbors and threaten political harmony among FTAA partner countries. Colombia's response to its armed insurrection (financed by drug trafficking and kidnapping) and its related antidrug campaign risk expanding the conflict into Ecuador, Venezuela, and Brazil, and pushing drug distribution networks deeper into Central America and the Caribbean. At the same time, divisive border disputes have flared up across the northern tier of South

2. Reinforcing these concerns, Chávez reserved Venezuela's position on key provisions—including the democracy clause—of the Quebec Summit Declaration.

3. Even before the sharp price increases at the end of the 1990s, Venezuela's oil exports accounted for about 80 percent of export earnings and 40 percent of government revenues. Colombia and Ecuador derived about one-quarter of export revenues and one-third of government revenues from petroleum products.

America. Venezuela has renewed claims to almost half the territory of Guyana, which also is engaged in a testy border conflict with Suriname (*The Economist*, 19 August 2000, 32). Disputed claims to territorial waters also mar relations between Venezuela and Colombia.

In sum, economic malaise and civil strife are compounding deep-rooted problems of governance in the Andean region, complicating the reform efforts needed to prepare those countries for free trade in the hemisphere. Related to these problems, the revival of petty nationalism threatens to undercut the political comity required to maintain the cohesion of their integration initiatives and to work together to conclude the FTAA pact.

The fourth challenge comes from other trade negotiations that threaten to distract attention and energies away from the Western Hemisphere talks. In particular, the FTAA process faces competition from the prospective launch of new multilateral trade negotiations in the WTO perhaps as soon as the next ministerial meeting in Doha, Qatar in November 2001; from existing regional pacts pursuing deeper integration policies; and from other superregional initiatives such as talks with the European Union and the free trade initiatives in the Asia–Pacific Economic Cooperation forum, in which five Western Hemisphere countries participate.

Concurrent negotiations pose both substantive and resource problems for many of the FTAA countries. Multiple negotiations place significant demands on governments in terms of representation at the meetings and technical expertise to deal with the host of new regulatory practices and other behind-the-border measures that increasingly take center stage in trade negotiations. Many countries, especially small economies, face clear resource constraints in preparing for and participating in new trade talks even though the agendas of the regional and multilateral talks are quite similar.

To be sure, there is a big difference between committing to free trade (in regional pacts) or to reduced levels of protection (in a WTO accord), especially when trade with regional partners accounts for a substantial share of a country's total trade. Given current economic problems and the likelihood of continuing adjustment pressures in national economies due to globalization, domestic lobbies may tend to push for smaller doses of liberalization in order to maintain some trade policy tools to protect domestic industries under duress—and this would favor WTO over FTAA negotiations. Such concerns already have been raised in Brazil and, to a lesser extent, in Mexico. The challenge for FTAA countries will be to demonstrate to their domestic constituencies that the regional and multilateral initiatives are mutually reinforcing, and not mutually exclusive.

For example, achieving comprehensive reform in agriculture may be difficult in the FTAA talks without parallel progress by other major producing nations, especially the European Union. The new WTO round could be an important complement to the FTAA talks, since Latin American countries could join other WTO members in pressing the transatlantic powers to lower their farm trade barriers.

The fifth challenge for the FTAA process resides in North America. It results from the seven-year impasse over reauthorization of US fast-track negotiating authority. While US officials do not need fast-track authority to enter into new trade negotiations, it is critical for their successful negotiation. In the past, US officials have entered trade negotiations without fast track but with the explicit understanding that it would be in place well before the final stages of the talks. Today, however, there is no such assurance; fast-track legislation has been defeated several times in Congress and the issue has caused deep divisions between and within both major political parties.

The impasse has two important implications for the FTAA talks:

1. It raises questions about the depth of the US political commitment to the hemispheric initiative and its willingness to reform its own trade barriers. While the US market is generally open, the few remaining US barriers must be on the table if the FTAA talks are to succeed.

2. It impedes US leadership in the process because it constrains US negotiators from making offers that would require changes in existing US trade practices, policies, and laws.

US caution elicits a reciprocal response from US trading partners, making them reluctant to put their best offers on the table. Latin American negotiators will not risk provoking domestic opposition from groups facing increased competition unless they can secure countervailing support from exporters who would benefit from improved access to the US market. Some countries cite the lack of US fast-track authority as an excuse for not moving forward in the talks. Over time, this could cause the entire negotiation to unravel.

President George W. Bush has committed to work for reauthorization of fast-track procedures (which he has renamed "trade promotion authority"). He will have to garner support from some Democrats in Congress to offset several dozen members of his own party who do not support free trade pacts in order to create a bipartisan majority in support of new trade initiatives.

The task is delicate but doable. Democrats will demand that attention be given to labor and environmental objectives in trade accords. Republicans will insist, in turn, that the trade pacts do not intrude on domestic regulatory authorities or promote re-regulation of economic activity. The new administration will face an early test on these sensitive issues in ratifying the recently concluded US–Jordan FTA (which includes provisions on labor and the environment) and in the ongoing FTA negotiations with Chile and Singapore.

FTAA Scenarios

Given these challenges, what are the prospects for the FTAA negotiations over the next few years? No simple forecast is possible; the problems are too complex. Rather, let me offer two possible scenarios.

The more pessimistic scenario, which could be characterized as "braking for globalization," projects a continuation of current political and economic problems that moderate the pace of integration at both regional and hemisphere-wide levels. It takes into account the vulnerabilities of many of the emerging markets in the region to volatile global trade and capital flows and the backlash against globalization that has been manifested by opposition to new trade pacts (especially in the United States). As a result, progress on new trade initiatives is delayed, if not derailed.

The more optimistic scenario, by contrast, projects the continuing consolidation of regional integration arrangements, the fulfillment of the Santiago Summit process, and the completion of FTAA negotiations by 2005, if not sooner. It clearly is *not* a status quo scenario. Meeting these objectives will require new dynamism and leadership, above all by the United States, to overcome the rash of economic and political challenges that beset countries in the Western Hemisphere at the end of the twentieth century. Let me describe these alternative scenarios in somewhat greater detail.

"Braking for Globalization" Scenario

This scenario projects a minimalist outcome for the FTAA process because the challenges cited above are not adequately addressed. The United States fails to overcome its domestic policy stalemate. Political commitment to negotiating FTAA liberalization remains weak, the fragility of democratic coalitions in nascent democracies in Central and South America precludes substantive reform, and economies in the region remain vulnerable to external economic shocks and domestic protectionist demands.

In this scenario, economic growth in Latin America recovers from the 1999 slump but expands only moderately as foreign investors react to the uncertain policy climate. High unemployment impedes reform initiatives or, even worse, sparks protectionist responses. Though domestic economic problems spur restructuring in the financial sector (with international assistance), political, labor, and judicial reforms proceed slowly due to bickering among political parties. Domestic adjustment problems dominate the political debate in both North and South America, tempering support for a broad trade deal.

In the United States, trade remains a focal point for partisan battles. The backlash against globalization increases the political costs of the liberalization needed to secure agreement on an FTAA. Fast-track legislation either remains in limbo or is burdened with onerous conditions limiting US liberalization and US obligations in new areas.

Under these conditions, Western Hemisphere countries concentrate their commercial energies on new multilateral trade negotiations (albeit with a modest agenda) and on their own regional integration initiatives. However, deepening of these relationships is impeded by national economic problems that create frictions among partner countries; in particular, internecine disputes between Argentina and Brazil slow the integration process in the Mercosur. At best, the FTAA talks are distracted for a few years; at worst, frictions within NAFTA and Mercosur, coupled with distractions from the WTO talks, lead the FTAA process to stall. In that event, the more comprehensive political, economic, and social initiatives undertaken at the Santiago Summit are not fulfilled as well.

"Building on Globalization" Scenario

This scenario projects the successful completion of the FTAA negotiations by 2005 based on more active US leadership in the talks and on the willingness and ability of Latin American countries to sustain and augment their national economic reforms. Those reforms encourage the consolidation of ongoing regional integration arrangements, creating more open and competitive economies that are better positioned to adopt and implement hemisphere-wide free trade commitments. This optimistic forecast is based on several factors.

First, despite the current rash of economic problems, the pace of policy reform continues to advance (albeit with minor detours), despite two major financial crises that have inflicted significant costs on national welfare. Domestic regulatory reforms and privatization programs, reinforced by regional integration pacts, continue to encourage important new regional infrastructure projects and thus strengthen economic linkages between partner countries. Illustrative of such projects are the extensive networks of gas pipelines linking the Mercosur region with Chile, Bolivia, and other South American markets, and the Puebla–Panama Plan (launched in March 2001), which aims to link power grids and expand road and rail transport networks between Mexico and the Central American countries.[4] These projects demonstrate that the physical integration of the region proceeds apace and promotes the deepening of economic relations among FTA partners. Moreover, these investments in steel and concrete increase pressure to accelerate the pace of trade talks throughout Latin America.

Second, the globalization imperative will continue to catalyze integration in the region, even as it complicates the task of building political sup-

4. For an overview of regional infrastructure in the LAC region, see IDB (2000).

port for the process. Changing conditions in world markets, particularly rapid advances in communications, transport, and information technologies, now almost compel countries to adapt quickly or fall sharply behind their trading partners in the global competition for market share and investment resources. Countries can no longer build regional economic fortresses to protect their industries from foreign competition; instead, they must use regional integration arrangements to help prepare themselves to compete more effectively at home and abroad.

To be sure, countries must adequately manage globalization pressures and ensure that the prospective FTAA is an integral part of their policy response. This point is particularly relevant for smaller economies, which are generally more open and susceptible to trade and capital shocks but will also gain the most from FTAA reforms. These countries need to formulate development strategies that deal with the globalization pressures and use their integration arrangements to help resolve their most pressing problems—fiscal reform, human resource constraints, and telecommunications and transportation networks that are inefficient either because they lack economies of scale or because of state-sanctioned monopolies (for a fuller discussion, see IGE 1997).

Third, cementing closer political relations will continue to be a strong rationale for deepening regional economic cooperation. The obvious example of this was the formation of Mercosur, which has sought (so far successfully) to mitigate the long history of political confrontation and military competition between Argentina and Brazil. More broadly, the same can be said of the Miami and Santiago Summits, which used the FTAA initiative as the linchpin for joint efforts on a broad array of political, social, and environmental programs in the Western Hemisphere. The FTAA contributes to a new spirit of cooperation and consultation between the United States and its Latin American neighbors that sharply contrasts with the North–South antagonism that marred relations over the past century.

Fourth, the United States realizes the large opportunity cost to its broad economic and political interests of not moving forward with the FTAA and the Santiago Summit process. The United States benefits when its neighbors prosper and democratic processes take root; the FTAA clearly reinforces the economic and political reforms that have been achieved throughout Latin America. Propelled by the renewal of fast-track authority, US negotiators assert stronger leadership on the broad array of hemispheric initiatives undertaken at the Miami and Santiago Summits. The success of the FTAA then helps build support throughout the region for other important US political and foreign policy goals, including drug interdiction, improving environmental and labor conditions, supporting educational reforms, and reinforcing democracy.

In sum, the challenge for Western Hemisphere leaders is to overcome the economic and political problems that confront their countries and put obstacles in the path of hemispheric integration. "Braking for globalization" will not resolve those problems. The leaders must meet head-on the challenge of global competition through a combination of domestic reform and hemispheric cooperation.

The Quebec Summit and Beyond

The Miami Summit established the vision of free trade in the Americas. The Santiago Summit started the negotiating process that has produced in early 2001 an initial though incomplete bracketed text of the FTAA. Like its predecessors the Quebec Summit focused more on procedure than substance; it reconfirmed the political commitment to dismantle barriers to hemispheric trade and set a specific timetable for doing so. The leaders agreed to start the crucial market access negotiations by 15 May 2002, to sign the pact no later than January 2005, and to expedite domestic ratification procedures so that the FTAA could enter into force by 1 January 2006.

While the summiteers provided political impetus for the hard bargaining ahead, they did little to settle substantive differences over the scope and coverage of the FTAA. To some extent, the timing of the meeting dictated this result. The summit took place just three months after the inauguration of US President George W. Bush. While the summit provided an immediate opportunity for him to galvanize domestic support for the FTAA process, it came too early in the new term for President Bush to do more than begin the delicate task of reconstructing the bipartisan coalition needed in Congress to pass trade promotion (also known as fast-track) legislation. At the same time, the largest FTAA participant from South America, Brazil, came to the summit distracted by the ongoing challenge of consolidating Mercosur in the aftermath of the sharp devaluation of the Brazilian real in early 1999 and by its already hotly contested presidential campaign. As a result, Brazilian officials were reluctant to discuss new reforms in advance of the elections in October 2002—and thus supported the delay in FTAA market access negotiations.

However, the Quebec Summit did commit to several initiatives that should strengthen political and economic relations among the hemispheric partners and contribute to advancing the trade talks to a successful conclusion. Three decisions merit particular attention.

First, the summit leaders recognized that "maintenance and strengthening of the rule of law and strict respect for the democratic system" are critical to the success of the FTAA and other summit initiatives. To that end they advanced a "democracy clause" that establishes a strong presumption that only democratic nations will be welcome to participate in summit initiatives such as the FTAA. The leaders warned that "any unconstitutional alteration or interruption of the democratic order . . . constitutes an insurmountable obstacle to the participation of that state's government in the Summit of the Americas process," (Declaration of Quebec City, 22 April 2001). However, they did not agree to automatically disqualify such a country from participating in the FTAA or other hemispheric programs. Recognizing the utility of neighborly advice and political coercion—which had worked successfully to forestall coups in both Central and South America during the 1990s—the leaders merely committed to consult each other on possible responses.

Second, the summit leaders committed to closer cooperation "to prevent, mitigate, and respond to the consequences of natural disasters." Since the Miami Summit, Hurricanes Mitch and Georges have pounded Honduras and Nicaragua and several Caribbean islands, massive mudslides have buried coastal towns in Venezuela, and devastating earthquakes have hit El Salvador. These disasters have caused tremendous human suffering and damage to the economic infrastructure of these countries, further complicating the task of preparing for hemispheric free trade. Unfortunately, all too often humanitarian relief has been disorganized and insufficient to address the long-term damage to local communities and national economies (*The Economist*, 19 January 2001, 31). To address this problem, the leaders pledged to help countries better prepare for the inevitable recurrence of natural disasters and improve efforts to provide more effective and timely responses to such events.[5]

Third, the summit leaders committed to the transparency of the FTAA talks and "to increasing and sustained communication with civil society." In that regard they cited the decision by trade ministers in Buenos Aires to release the draft FTAA negotiating text as evidence of their desire to work constructively "with all sectors of civil society." The restricted distribution had raised concerns, particularly among nongovernmental organizations, that prospective trade obligations would infringe on important regulatory policies and require governments to subordinate consumer, labor, and environmental goals to trade policy objectives. Trade officials wanted to avoid the mistakes that contributed to the demise of the Multilateral Agreement on Investment, whose drafts had been closely held by OECD negotiators and contained flawed provisions (for example, regarding regulatory takings) that provoked strong opposition from nongovernmental organizations (Graham 2000).

5. What is really needed is a regional agency akin to the US Federal Emergency Management Agency. This body could be charged by summit leaders to coordinate disaster relief plans, stockpile supplies, and establish a fund (based on financial commitments from FTAA countries) to dispense emergency aid to help rebuild economic infrastructure in countries with limited resources.

The Quebec Summit initiatives should help keep the FTAA negotiations on track. However, the successful conclusion of the FTAA ultimately requires the United States, as the predominant market in the hemisphere, to take the lead in addressing the challenges at home and abroad that threaten to stall the trade talks. Two complementary initiatives need to be advanced.

First, President Bush needs to reconfirm through concrete actions his commitment to securing trade promotion authority that is as comprehensive in scope and coverage as that accorded his predecessors. Having trade promotion authority will not resolve differences among FTAA participants on the key issues affecting hemispheric trade. But it will assure other countries that the United States intends to put its trade barriers on the table (just as it did in NAFTA) to promote the successful conclusion of the free trade talks.

As noted earlier, passage of such legislation will require building a bipartisan coalition of pro-trade members in both houses of Congress. To do so, administration and congressional leaders must bridge the gap between Democrats and Republicans over key US trade negotiating objectives on labor and the environmental issues. The president and Congress will have to craft a pragmatic compromise—one that recognizes the narrow but legitimate role for such provisions in trade pacts—in order to attract enough support from Democrats to advance legislation in the second half of 2001.

At the same time, however, US objectives on labor and the environment must not be so ambitious that they provoke a veto from countries that currently are reluctant to include these issues in a trade pact. At the Buenos Aires ministerial, most countries opposed including trade-related labor provisions in the FTAA that could be enforced via trade sanctions. For that reason, the US compromise should also include commitments to pursue international initiatives on labor and the environment in forums other than the FTAA and the WTO, which have primary responsibility for those issues (CEIP 2001).

The results of these domestic consultations could hopefully yield new approaches for dealing with labor and environment issues in trade agreements that could be advanced in both the current hemispheric negotiations and the prospective new WTO round. It would make sense to try out the new ideas first in the Chile–US FTA talks. Those talks could draft model provisions on labor and the environment that might be acceptable to both developed and developing countries in the broader FTAA pact. The Chilean negotiators have indicated that they would consider obligations in those areas in a bilateral accord, as long as enforcement is not linked to imposition of trade sanctions (as in the US–Jordan FTA signed in October 2000). In fact, a side agreement to the Chile–Canada FTA already includes some labor obligations, whose violation could trigger the imposition of fines against a country in which there is a persistent pattern of lax enforcement of national labor laws.[6] In sum, if Congress and the Bush administration can agree on narrowly focused objectives regarding labor and the environment, then summit leaders may well accept provisions on these issues in the FTAA and/or summit accords.

Second, the United States needs to take the lead in promoting collaborative solutions to economic problems abroad that threaten to block participation by many developing countries in the FTAA and other hemispheric initiatives. The United States has already extended trade preferences for access to its market in the Trade and Development Act of 2000, which granted NAFTA-like benefits to countries in the Caribbean Basin, and the Andean Trade Preferences Act.[7] These programs provide a way station to the broader, reciprocal free trade obligations that will be undertaken in the FTAA.

But trade preferences in the US market provide only short-term and fleeting benefits. More important, the United States also needs to help its partners overcome obstacles that impede their development and thus hamper their ability to participate fully in hemispheric initiatives. In particular, the United States needs to support so-called "capacity building" efforts by the private sector and regional development agencies in areas such as transportation, telecommunications, and power generation. Financial support and technical assistance, particularly training of administrative and regulatory officials in the financial services and telecommunications sectors, would strongly complement efforts to boost productivity in FTAA countries and thus enhance their ability to implement and sustain free trade reforms.

Completing the FTAA

The Quebec Summit filled some of the potholes in the path of the FTAA but much roadwork remains. Over the near-term (i.e., 2001–02), negotiators need to pursue two tasks. First, they need to formulate rules and modalities for conducting the crucial final phase of the negotiations in which politically sensitive trade barriers will have to be addressed and decisions taken on the appropriate transition period to hemispheric free

6. That agreement does not specify whether the fine would be levied on offending firms or government agencies, nor how the funds would be disbursed (Elliott 2001). To help promote better working conditions in the partner country, however, it would make sense to dedicate revenues generated by fines to labor training and worker adjustment programs, as well as improved enforcement procedures.

7. The ATPA, which expires in December 2001, should be extended to encourage recipient countries to augment their domestic economic reforms so that their firms can better compete under the prospective FTAA.

trade. Second, they need to sharpen their red pencils and reduce the "brackets" in their draft agreement.

The ultimate test of the FTAA process, however, will come only after November 2002, when the United States and Brazil become co-chairs of the final stages of the negotiations. At that point, the willingness of the trading powers of North and South America to engage in broad-based liberalization of their own trade barriers will determine the fate of the entire venture.

Bridging the gap between the US and Brazilian positions thus will be key to the successful end game of the negotiations. To date, their bilateral trade and investment relationship is small relative to the size of their markets. Two-way trade totaled almost $30 billion in 2000, far less than the $248 billion in US–Mexico trade. The United States accounts for about 20 percent of Brazil's trade, Brazil for about 1.5 percent of total US trade. However, US FDI in Brazil reached $35 billion on a historical cost basis in 1999—about the same as in Mexico and more than in any other developing country.

For the United States, a prosperous Mercosur is essential to the hemispheric free trade zone. In turn, increased access to the growing Brazilian market via direct exports and sales by their Brazilian subsidiaries is the real prize of the FTAA for American firms. Eliminating the high Mercosur common external tariff along with liberalization of investment and government procurement regulations would open substantial new opportunities for US producers and service providers.

Similarly, for Brazil the main attraction of the FTAA is its promise of increased access to the US market. Although US trade barriers are generally very low, many of the notable exceptions affect Brazilian exports. In the FTAA talks, Brazil will probably target high US tariffs on orange juice, shoes, and apparel; tariff quotas on sugar; and antidumping regulations that block steel shipments.[8] Without progress in reducing or eliminating US barriers to its exports, Brazil will be reluctant to open its market fully to competition from the industrial powers of North America, and may settle instead for incremental reforms via WTO negotiations. Brazilian President Cardoso bluntly warned his colleagues at the Quebec Summit that an FTAA would be "welcome if its creation is a step toward providing access to move dynamic markets . . . otherwise it would be irrelevant or, worse, undesirable."[9]

Brazil's strategy, however, is complicated by its need to attract continuing substantial flows of US and European FDI, which is why it, and its

8. Brazil's Ambassador to the United States, Rubens Barbosa, claims that, absent these barriers, along with those on tobacco, gasoline, shrimp, ethyl alcohol, and crude soybean oil, Brazilian exports would increase by $831 million (report dated November 2000, http://www.brasilemb.org/trade/trade_barriers.htm).

9. Statement presented at the summit working sessions, cited at http://usinfo.state.gov/regional/ar/summit.

Mercosur partners, are also negotiating a possible free trade pact with the European Union (see Schott and Oegg 2001). To a certain extent, the FTAA gives Brazil leverage in its parallel talks with Europe. But Brazil faces a tough task in dismantling agricultural barriers to its exports in both the United States and the European Union; both will likely seek to exempt specific farm products from the free trade obligations. Brazilian negotiators thus will likely pursue a two-track strategy: work with other agricultural exporting nations in the WTO to push both regional trading powers to *reduce* their farm trade barriers in new multilateral negotiations, and negotiate bilateral FTAs that *eliminate* key US and EU farm restrictions.

Bridging the gap between the US and Brazilian positions is doable but will require careful negotiation of phase-in periods for some reforms and possibly carve-outs from reform commitments for some products. Eliminating all tariffs is likely to be the basis of the deal, with some balance struck between US farm trade reforms and enhanced access to the Brazilian procurement and services markets. Antidumping reforms probably will be too narrow to resolve US–Brazil problems; this could present the biggest obstacle to agreement on the FTAA unless steel trade problems can be resolved through broader multilateral accords.

Of course, such a negotiation depends critically on the reauthorization of US trade promotion authority. If US legislation is enacted by early 2002, there should be ample time to conclude the entire FTAA negotiation well before the January 2005 deadline.

FTAA participants would have 26 months between the Brazilian election in October 2002 and the negotiating deadline to conclude the talks. That should be plenty of time to set up schedules for implementing market access reforms in a way that allows for orderly adjustment to free trade for the most import-sensitive products or sectors. Indeed, if sufficient progress is made in the market access talks in 2002, countries could consider anew accelerating the FTAA target completion date by 6 to 12 months—and thereby afford additional time for ratification before entry into force of the FTAA by year-end 2005. By advancing the deadline, negotiators would also avoid complications that could arise if the final stages of the FTAA talks coincided with the US presidential election in November 2004.

The major drawback would be the added burden of this accelerated process on negotiators from smaller economies. As noted earlier, these countries face substantial obstacles in preparing their domestic firms and government agencies to meet the demands of an FTAA. Trade officials will need help from their friends in the finance and development assistance agencies to ensure that these countries can be full and active partners and faithfully implement the reforms mandated by the hemispheric trade accord. In particular, FTAA partners should extend longer phase-in periods for FTAA reforms and commit additional financial and technical assistance, perhaps via earmarked programs of the World Bank and the

Inter-American Development Bank, to ensure that the smaller countries in the region have the capacity to fully implement their obligations.

In sum, concluding the FTAA talks is feasible by the January 2005 deadline, if not sooner. However, the successful outcome to the trade talks depends importantly on key legislative initiatives in both North and South America. US officials need new trade promotion authority to provide the requisite support and negotiating flexibility to craft the best deal. The LAC countries need to deepen then domestic economic reforms to promote development and facilitate the adjustment over time to the new trade regime. Working together, both can achieve a result that fulfills the vision of the summit leaders to "create greater prosperity and expand economic opportunities while fostering social justice and the realization of human potential" (Declaration of Quebec City, 22 April 2001).