

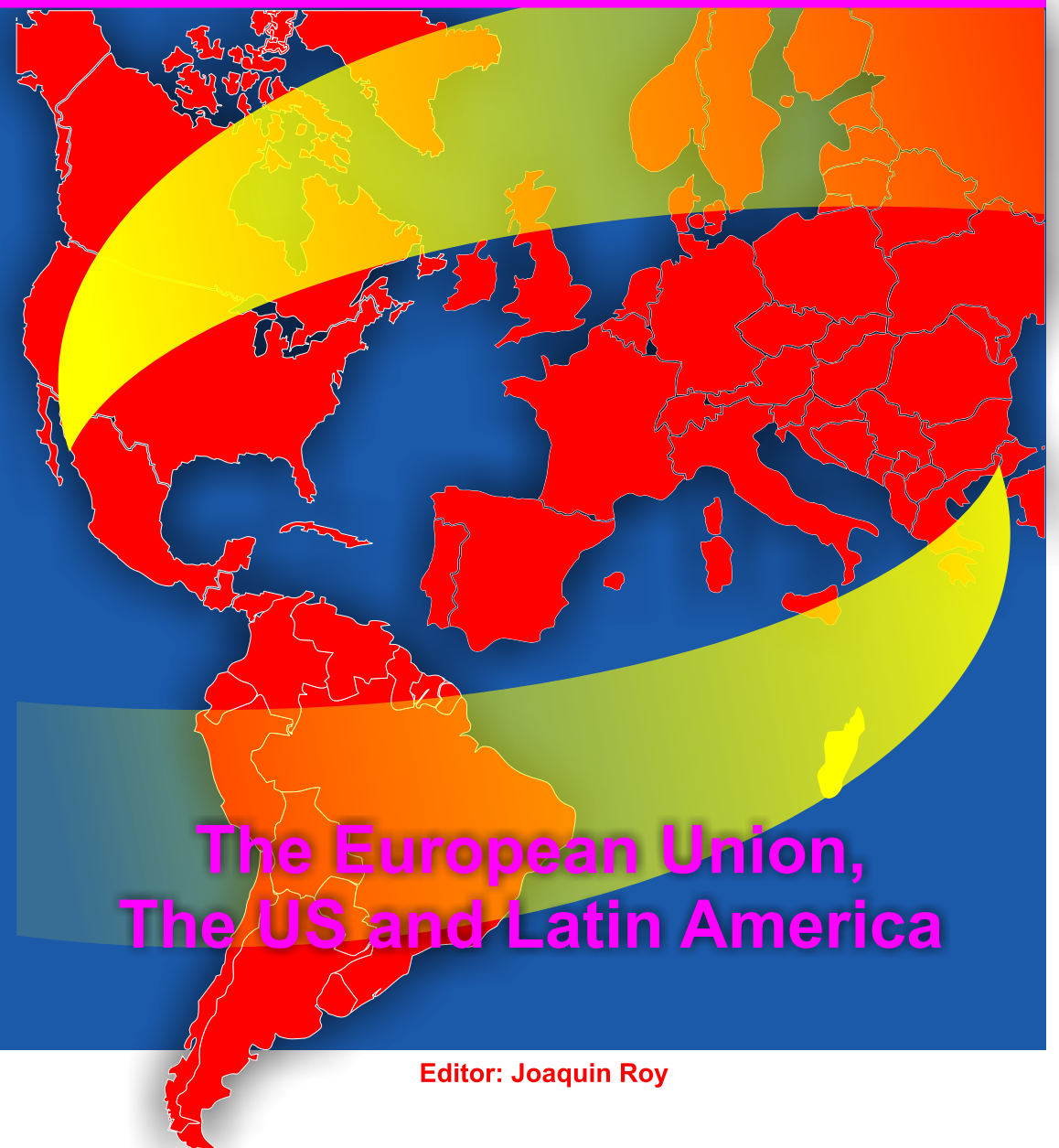
# A New Atlantic Community

The year 2015 is destined to be remembered for a series of events that deal directly with the background, the current state and future shape of what can be called a New Atlantic Community. Several important gatherings and processes involving the European Union, the United States and the Latin America-Caribbean region take place this year. On April 10 and 11, 2015, the Seventh Summit of the Americas, with a focus on "Prosperity with Equity: The Challenge of Cooperation in the Americas", will be held in Panama City, Panama. It will be attended by the leadership of the Western Hemisphere. Later in the year, on June 4-5, 2015, the highest representatives of 61 European, Latin American and Caribbean countries are scheduled to meet in Brussels in the biannual summit of the EU and the CELAC organization. They comprise one third of the United Nations membership. Throughout all this year, the economic and political scene will reveal the evolution of a trend-setting project announced in 2003: the planned Trade and Investment Partnership (TTIP) between the United States and the European Union. In consequence, the main topics and themes of this monograph are the TTIP itself, its impact on Latin America, the overall relations between the EU and Latin America, and the general issues of regional integration and economic cooperation in the Western Hemisphere.

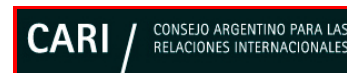
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A New Atlantic Community - Editor: Joaquín Roy



Editor: Joaquín Roy



**A New Atlantic Community:  
The European Union, the US and Latin America**

**Joaquín Roy (editor)**

Miami-Florida European Union Center/Jean Monnet Chair, 2015



# **A New Atlantic Community: The European Union, the US and Latin America**

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Jean Monnet Chair, 2015

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## **Preface**





# **A New Atlantic Community: The Background**

Joaquín Roy

University of Miami

## **The European Union and Latin America**

Several important gatherings and remembrances involving the European Union, the United States and the Latin America-Caribbean region will take place this year. On April 10 and 11, 2015, the Seventh Summit of the Americas, with a focus on “Prosperity with Equity: The Challenge of Cooperation in the Americas”, will be held in Panama City, Panama. It will be attended by the leadership of the Western Hemisphere. Participants and observers will still remember the failure of the agreement for the establishment of the Free Trade Area of the Americas envisioned in Miami two decades ago in 1994, the same year of the foundation of the North-American Free Trade Agreement formed by the United States, Canada and Mexico.

On June 11-12, 2015, the highest representatives of 61 European, Latin American and Caribbean countries are scheduled to meet in Brussels. They comprise one third of the United Nations membership, with a total population of over 1.1 billion and a combined GDP of approximately US\$20 trillion. For almost two decades the two regions have regulated their diverse links through the EU “Strategic Partnership”. This setting complies with the mandate of organizing a biannual summit that customarily has been held since 1990, alternating European and Latin American capitals. The timing and the choice of the place of the 2015 event is extremely significant, because it is the first time that this conclave takes place in the capital of the major institutions of the European Union, the organization that is considered the most ambitious entity in regional integration and cooperation among states. This event is also the second time that the Latin American/Caribbean side is represented collectively by the Community of Latin American and Caribbean States (CELAC). The preceding meetings were held in Rio de Janeiro (1999), Madrid (2002), Guadalajara (2004), Vienna (2006), Lima (2008), Madrid (2010) and Santiago de Chile (2013).

The European Union and the Latin American-Caribbean areas are two regions that in fact are the most “natural allies” of the planet (along the links of the United States/Canada with Europe itself), bonded by solid cultural, historical, economic, and legal ties. Politics is a dimension that remains under study, taking into account different interpretations of democracy and political approaches. In the political realm, both regions co-operate very closely at different international

levels, maintaining an intensive “political dialogue”. They also interchange in many nuances across a wide regional level, evident also at sub-regional scenarios. For Brussels, Latin America is subdivided along bureaucratic parameters, respecting the sub-regions as self-defined by Latin Americans. From this perspective, the EU (as a whole) deals with the entities known as Central America, the Andean Community, and MERCOSUR, as well as with the Caribbean. The economic relationship between the European Union and Latin America can be inspected in three sectors: trade, investment and development aid. Each one shows interesting aspects confirming perceptions and offering backing evidence for the preferences of each part. The EU is the largest donor of development aid and the first investor, and the second trade partner after the US.

### **A Wider Global Picture**

This summit of 2015 takes place in the middle of a crucial year in the economic and political evolution of both continents. 2015 is also the setting of the full development of a trend-setting project announced in 2003: the planned Transatlantic Trade and Investment Partnership (TTIP) between the United States and the European Union, scheduled by both parties to be finalized at the end of 2015, but many predict it will take longer to be approved. This ambitious operation could ultimately form the largest economic bloc in the planet, the result of an apparent world-wide frenzy for the establishment of trade agreements as a sign of effective globalization. Since its announcement, influential governments of Europe have expressed satisfaction with the project and have entrusted the European Commission (holder of the exclusive competence of EU foreign trade) the mission of drafting an agreement that by law would receive the nod of the deciding EU institutions (the Council and the Parliament). Scholars and media have already paid considerable attention to the project.

Together, both projects (TTIP and EU-CELAC) could then in turn form a much larger economic (with political consequences) bloc of formidable world reach, in what could be termed as an Atlantic Community. The facts and prospects of this triangular scenario are truly impressive in comprehensive terms and in comparative dimensions. The combined population is over 1.4 billion, 19.8% of the world. By itself, the EU is the world’s largest trading bloc (almost one-fifth of global trade and one-quarter of the global economy). The EU and US together, with a combined population of over 800 million, generate almost half of global GDP, handle nearly 30 percent of global merchandise trade, about 40 percent of world trade in services, and well over half of foreign direct investment. The United States directs half of its total foreign direct investment (FDI) toward the EU, and the EU’s FDI in the U.S. accounts for almost two-thirds of America’s total incoming investment. Approximately 15 million jobs are linked to the transatlantic economy. Globally, either the EU or the US is the largest trade and investment partner for almost all other countries in the world. The EU and the

United States are each other's leading partners by trade volume (imports plus exports). Every day, the EU and the U.S. trade goods and services worth \$2.7 billion. TTIP could benefit the rest of the world by more than €100 billion.

### **Issues to Consider**

Any analytical and research plan is pressed to consider several fundamental issues of both processes. The most important one is the evaluation of the European Union itself as a model or reference for effective regional integration. Is the EU accepted as a cohesive partner by the United States, with full autonomy to negotiate such a formidable deal? Is the EU the irreplaceable model for effective regional integration in Latin America? Are there any other models in other parts of the world? What are the domestic obstacles for a deeper integration dimension in Latin America and the Caribbean? What is the negative role of strict national sovereignty, presidentialism, lack of national social integration, poverty and inequality? How does populism present opposition to what may be perceived as loss of sovereignty? How is European investment in Latin America perceived and received—as a positive, unconditional contribution, or as a reborn example of “imperialism”? How is the EU democratic conditionality in development aid programs perceived in Latin America when considering bi-regional pacts with Latin America/Caribbean? What is the role of the preferred strategy of the United States in international trade schemes? Is this influence an irresistible force in Latin America?

When considering the role of the United States in negotiating with the EU, what are the domestic constraints in the US for deeper commitments in international trade and cooperation? What are the “red lines” in Congress and the White House? How are European regulatory conditions perceived in negotiations with the US? What is the impact of European basic conditions of the welfare state regulations on the development of a trade pact with the EU? Will the sensitive fields of health, labor law, and immigration affect the negotiations of the TTIP? What influence does the calendar of elections in Europe (national and EU-wide) and in the United States (mid-term and presidential) have in the development of a trade pact (now and in the future)? Will the US President obtain the “fast track authority” to sign trade deals? How autonomous is the authority of the European Commission in negotiating external trade for the whole EU membership?

In sum, when dealing with the multiple aspects of this triangular scenario, observers and researchers must be prepared for long and complex negotiations on both sides of the Atlantic and be ready to witness disappointments and failures, as well as to certify successes.

In fact, this expanded interpretation of the concept of “transatlantic” relations including Latin America and the Caribbean has been a key factor for the recognition of our European Union Center and the award of the Jean Monnet

Chair at the University of Miami, with over US \$1.8 million in grants. Our staff and partners at Florida International University have entrenched themselves in the study of both bi-continental processes. We have followed them with research, teaching and publications. This volume is dedicated to the analysis of such diverse developments.

### **A Seminar and a Monograph**

The present monograph reflects the proceedings (with a few additions) of a seminar under the comprehensive title of “A New Atlantic Community: The European Union, the US and Latin America”. It was organized by Jean Monnet Chair of the University of Miami, under the sponsorship of the Miami-Florida European Union Center of Excellence (a partnership with Florida International University) and the EU Commission. It was held on Friday, February 27, 2015, at the School of Business Administration of the University of Miami. The main topics and themes were the Transatlantic Trade and Investment Partnership (TTIP) to be agreed between the European Union and the United States and its impact on Latin America, the relations between the EU and Latin America, and the overall issues of regional integration and economic cooperation in the Western Hemisphere. This volume, available for free access in the web of the Center, will also take the form of co-edition published by the Argentine Council of Foreign Relations (CARI) to be distributed in Latin America, and available on their web.

Welcome and introductory words were provided by **Douglas Fuller** (Associate Dean, College of Arts and Sciences, University of Miami), **Rebecca Friedman** (Co-Director, EU Center, Florida International University), and **Richard Weisskoff** (Chair, Department of International Studies). British Consul General **Dave Prodger**, Spanish Deputy Consul General **Javier Pagalday**, and French Consul General **Philippe Letrilliart** offered comments. Sessions were chaired by **Markus Thiel** (Florida International University), **Aimee Kanner** (Florida Atlantic University), **Eduardo Elena** (Director, Latin American Studies, University of Miami), and **Ambler Moss** (University of Miami).

A selection of the themes and issues were grouped in four fundamental parts responding to general approaches. Part I (“**Background and setting**”) describes the overall presence of the TTIP. **Joseph A. McKinney** (Baylor University, Waco, Texas), in “Regional Economic Integration in the European Union and North America: A Theoretical Perspective” provides a comprehensive analysis of the major aspects of the bi-continental project crafted by the two partners.

**Tamás Novák** (Budapest Business School; MTA KRTK Institute for World Economics), in “Global Political and Economic Restructuring through Free Trade Agreements (FTAs),” points out the motivations and consequences of today’s FTAs as a result of the changes in the international political power. **Beverly Barrett** (University of Houston), in “Trade in Higher Education Services in the TTIP Negotiations and Beyond”, examines the role of higher education services in

trade negotiations, due to their dual purposes for employability and to enhance civil society, as nations cooperate across national boundaries. **María Lorca**, University of Miami, in “The Price of Energy and its Impact in the Economies of the US and Eurozone: Implications for the TTIP,” deals with a crucial sector that has an extraordinary impact on the overall picture of the plan crafted by these formidable world powers. **Sarah Beringer**, University of Nuremberg, Germany, in “The TTIP Partnership from a German Perspective: Economic Interests and Political Discourse,” tackles the perception of the TTIP from the point of view of the most powerful economic and political leadership in Europe, destined to dominate the rest of the negotiations.

Part II is dedicated to topics that spillover beyond the basic scope of the bi-continental partnership (“**Beyond Economics**”). **Maxime H. A. Larivé** (University of Miami), in “TTIP: Creating an Economic NATO or Fermenting European Fears?”, ventures into the sector that would be better treated in a study of strategic issues, reflecting on two dimensions: the projected benefits of the TTIP for the EU and the debate and perceptions within the EU about the TTIP. **Vicente Palacio** (Fundación Alternativas, Madrid), in “Revisiting the TTIP: the Revenge of Politics”, remind us that, as the original essence of the EU is based on more issues than simple trade of goods and financial investments. **Javier Bonilla and Pedro Isern** (ORT University, Montevideo, Uruguay), in “Symmetries and Asymmetries in Integration Processes”, deal with an array of dimensions in a variety of integration and economic cooperation experiments, with the warning that with certain actors in certain contexts, integration does not always translate into optimum results. **Willem Maas** (York University, Canada), “Trade, Regional Integration, and Free Movement of People,” offers an analysis in which the issue of transnational citizenship becomes central, dealing with concrete examples of accomplishments in Latin America under the influence of the European precedent.

Part III covers topics dealing with the link between **Europe and Latin America**. **Ángel María Casas Gragea** (Metropolitan Autonomous University, Mexico, D.F., Mexico) and **Pedro Caldentey del Pozo** (Loyola University Andalusia, Cordoba, Spain), in “The Crisis of the European Integration Model, and its Implications for Latin American Integration” venture in the area where doubts of the adaptation or adoption of the EU model become evident. **Ana Paula Tostes** (Rio de Janeiro State University), in “The Effect of the TTIP on the BRICS Countries: The Case of Brazil,” deals with one of the most important consequences of the TTIP on the emerging powers that are presenting a challenge both to the United States and to Europe, choosing Brazil as the central focus of analysis. **Liliana Lizarazo, Lurong Chen, and Philippe De Lombaerde** (UNU-CRIS, Bruges, Belgium), in “Health-Related IPR Provisions in FTAs in the Atlantic Community,” ponder why health-related Intellectual Property Rights (IPR) provisions are seen as so controversial in trade negotiations and how the court system is facing the problem of balancing this issue with the right to health.

**Alejandro Chanona**, of the National Autonomous University of Mexico, in “The European Union and Latin America: Facing the Drug-Trafficking Challenge”, offers an analysis of the EU-LAC cooperation to fight drug trafficking combined with dealing with the underlying causes of the problem through drug-use prevention and rehabilitation of addicts.

Finally, in Part IV, labeled as “**Inside Latin America**” but spilling over the geographical limitations, authors concentrate on several dimensions that pertain to Latin American countries. **Rita Giacalone** (University of Los Andes, Venezuela), in “Latin American Answers to Mega-Regional Projects: Options and Limits,” inquires about the response of Latin America absorbing the impact of projects like TTIP with the result of generating other alliances inside the area (convergence of and expanded MERCOSUR with the Pacific Alliance and the combination of ECO-ALBA-Petrocaribe Zone). **Félix Peña** (Universidad Nacional de Tres de Febrero, Argentina) in “Regional integration in Latin America: the strategy of ‘convergence in diversity’ and the relations between Mercosur and the Pacific Alliance,” proposes the encouragement of an agenda of cooperation provided by all Latin American countries, with the result that its effects would then transcend the strict regional scope. But, as in most other cases, this scope will require perseverance, technical imagination and political will. **Carlos Malamud** (Real Instituto Elcano, Madrid), in “Regional Integration in Latin America: a Diagnosis of the Crisis,” presents an analysis of the general integration process, outlining the short- and long-term options for interregional cooperation, as a useful option until a reasonable solution is found to the current issues the Andean Community (CAN), Mercosur, Unasur, and the Alliance of the Pacific.

Academic and logistical assistance was provided by **Diana Soller** (Editor and Research Assistant, University of Miami) and **Nilda García** (Editor and Research Assistant, University of Miami). Technical assistance was given by **Luis Vidal**, **James Aggrey** and **Benjamin De Tullio** (Computer Support, College of Arts and Sciences), and financial control was coordinated by **Miguel Ramírez** and **Alexis Fernández** (Department of International Studies) and **Tracy Ehrlich** (College of Arts and Sciences). Program co-sponsors and contributing institutions were the **European Commission**, the **Delegation of the European Union in the United States**, the **European Union Studies Association** (EUSA, EU-LA Interest section), the **Latin American Studies Association** (LASA, Europe-Latin America Section), the **Argentine Council of International Relations (CARI)**, the **Center for International Business Education and Research** (CIBER U. Miami) and **Center for Latin American Studies** (CLAS, University of Miami). Support for participation was also provided by **the National University of Tres de Febrero** (Buenos Aires), the **University ORT** (Montevideo, Uruguay), the **Real Instituto Elcano** (Madrid), and the **Fundación Alternativas** (Madrid). Special gratitude is due to **Pedro A. Gonzalez** (President of the Florida Association of Hispanic Journalists).

## **I. Background and Setting**





# **Regional Economic Integration in the European Union and North America: a Theoretical Perspective**

Joseph A. McKinney

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## **Abstract**

Regional economic integration is occurring in Europe and in North America, driven partly by market forces, but also by policy measures. The process has been much more formal and policy-driven in the European Union than in North America. A number of comparative regionalism theories have sought to explain how economic integration develops differently in different regions. This paper compares and contrasts the progression of regional economic integration in the European Union with that in North America, assessing the degree to which various theories can reasonably explain the differences.

## **Introduction**

Regional economic integration occurs naturally when economic agents are free to engage in trade and investment. But it is also affected by policy measures and by the establishment of regional institutions. Economic interdependence increases the need for cooperation in order to provide public goods that are beyond the scope of one country, and to internalize positive and negative externalities (Keohane 1984). In the case of heterogeneous populations, preferences for policies and institutions differ across groups, necessitating a weighing of the costs and benefits of particular integration policies (Alesina and La Ferrara 2005). Through participation in regional institutions, countries develop a more accurate picture of what is important to the partner countries, learn what they can expect from each other, and can develop a higher level of mutual trust (Axelrod 1983).

Transactions costs among nations can also be reduced as countries agree beforehand on what types of bargains are desirable, and build mechanisms for challenging forbidden types (Martin and Simmons 1998). Establishment of rules at the regional level, and monitoring of compliance with them, can provide for a more favorable business climate by reducing uncertainty (Keohane 1984). However, compliance is costly, and formulation of rules can beyond a point become counterproductive.

Institutional arrangements can also help to alleviate time inconsistency problems by allowing politicians to shift to the regional level actions that have

short-term costs but long-term benefits, and can also perform a valuable signaling function that policies are stable (Martin and Simmons 1998). This paper assesses the degree to which the economic integration and institutional development that have occurred in the European Union (EU) and the North American Free Trade Area (NAFTA) can be reasonably explained in each case by existing theories of regional economic integration.

## **Formation of European Union Institutions**

The institutional arrangements that eventually evolved into the European Union had their roots in the desire of the world, and particularly the countries of Europe, to have more peaceful political and economic relations. While European history is replete with military and economic conflicts, the first half of the twentieth century was particularly devastating. Europe had been at the center of two world wars, with the period between characterized by economic and financial turbulence. During the interwar period there was little cooperation in economic matters.

Some European intellectuals, such as Altiero Spinelli and Jean Monnet, envisioned a European federation that, by eliminating national borders, would put an end to international conflict within Europe (Sporaloro 2013). The founding document of European integration, however, was more modest. The Shuman Declaration of 9 May 1950 proposed placing the coal and steel industries of France and West Germany (and other countries that wished to join) under the control of a supranational High Authority. According to the declaration, “The solidarity in production thus established will make it plain that any war between France and Germany becomes not merely unthinkable, but materially impossible” (Shuman Declaration 1950). The European Coal and Steel Community (ECSC) was formed in 1951 by the Treaty of Paris, and in addition to France and West Germany included Italy, Belgium, the Netherlands and Luxembourg as member countries.

In 1957, the Treaty of Rome established a European Common Market and the European Atomic Energy Community. This treaty provided for the removal of tariffs among the member countries, for establishment of a common external tariff, and for eventual unrestricted movement of factors of production. These market liberalization measures triggered a strong inflow of capital into the member countries that stimulated economic activity and led to a series of enlargements. Membership in the group expanded to include the United Kingdom, Ireland and Denmark in 1971; Greece in 1981; Spain and Portugal in 1985; Austria, Finland and Sweden in 1995; ten additional countries mainly from Eastern Europe in 2004; Romania and Bulgaria in 2007; and Croatia in 2013, for a total membership of 28 countries.

While the institutions of the European Union have taken shape gradually over time, most of the present-day institutions had their origin in the European

Coal and Steel Community. The executive body of the ECSC was a High Authority consisting of nine members. Since the High Authority was truly a decision-making body, some member countries were uncomfortable with its supranational character. Therefore, an Assembly composed of 78 deputies representing national parliaments was created and given supervisory power. A Council composed of a representative from each of the member governments was formed, the purpose of which was “to harmonize the activities of the High Authority and the general economic policy of the governments” (ECSC Treaty 1951). Finally, a Court of Justice composed of seven members was constituted to ensure proper interpretation and implementation of the founding treaty.

In 1957, when the European Economic Community and the European Atomic Energy Community were formed, their institutions were similar to those of the ECSC but with more powers residing in the Council as direct representative of the national governments. The name of the Common Assembly was changed to European Parliament in 1962. In 1967 the institutions of the three communities were merged by implementation of a Merger Treaty, with the executive functions of the High Authority being transferred to the Commission of the European Communities. In 2002 the Treaty of Paris expired and the High Authority ceased to exist as a legal entity (Europa 2007).

Preliminary moves toward monetary unification among the EC countries had been made in 1979 through the establishment of the Exchange Rate Mechanism. In 1992 the Treaty on European Union (Maastricht Treaty) was signed and expanded the role of the supranational institutions (in particular by giving the European Parliament some co-legislative powers), and set forth a plan for monetary unification and a common currency. The European Central Bank came into existence in 1998, the euro was established as a unit of account in 1999, and it became a circulating currency and the official currency of the twelve participating countries (now 19) in 2002. The Treaty on European Union changed the name of the European Communities to the European Union and established the concept of European Union citizenship.

An attempt was made through a Convention on the Future of Europe in 2002 to develop a European Union Constitution that would have given additional supranational powers to the EU institutions. A draft constitution was signed in 2004, but was subsequently rejected in referenda in France and the Netherlands. Consequently, a less ambitious plan called the Lisbon Treaty was approved. This treaty, among other things, established a President of the European Council and a High Representative for Foreign Affairs. It also strengthened the supranational functions of some of the EU institutions by, for example, giving the European Commission exclusive competence in the negotiation of trade and investment treaties, and giving the European Parliament the right to approve or disapprove trade agreements.

In general, the European Commission serves as the executive body of the EU and initiates EU legislation. The legislative body of the EU was originally the

Council of Ministers, with ministers in the appropriate subject area from each member country voting on the legislation. The European Parliament had only an advisory role with regard to legislation. However, in the Maastricht Treaty the Parliament was given co-decision authority over some issues, and in the Lisbon Treaty was made co-legislator with the Council on most issues. The Court of Justice interprets, and oversees the implantation of EU legislation.

The EU has gone farther than any other regional economic integration scheme toward a federal economic system. Significant sovereignty has been ceded to EU institutions concerning matters of regional economic integration. However, the EU remains a long way from a true federal system in this regard. Only recently, are steps being taken toward a banking union. The lack of a fiscal union has created strains for the monetary union, in that no automatic stabilizers exist to make transfers from more prosperous countries to those experiencing recession. Even with its federalist economic elements, nations in the EU continue to exercise considerable sovereignty with regard to economic issues.

### **Formation of NAFTA-Related Institutions**

The countries of North America, in entering into the North American Free Trade Agreement (NAFTA), had much more limited aims than those of the EU countries. Its major focus was to remove impediments to trade in goods and services. In the 1980's the United States had become frustrated at not being able to get trade issues such as services trade, agricultural trade, investment measures, and intellectual property issues onto the agenda for multilateral trade talks. A decision was made to pursue bilateral and regional free trade agreements, both as a way to put pressure on trading partners to enter into a new round of multilateral negotiations and as a way to demonstrate that progress on the new issues was possible. The US-Israel free trade agreement went into effect in 1984, and the implementing legislation for the agreement stated that the US would consider requests for such agreements from other countries.

Canada requested a free trade agreement in 1985, negotiations began in 1987, and the US-Canada free trade agreement went into effect in 1989. This agreement was quite comprehensive and demonstrated that progress was possible in bilateral negotiations on the issues that the US was pushing for inclusion at the multilateral level. Mexico requested a free trade agreement with the US in 1990. Canada soon joined the negotiations, and the North American free trade agreement was signed in 1992, entering into force in 1994.

NAFTA built upon the template of the US-Canada free trade agreement, but also contained provisions concerning protection of intellectual property and a controversial chapter on investor-state protections. In side agreements to the main agreement, environmental and labor issues were for the first time connected to a free trade agreement. The agreement established several institutions that

were, in distinct contrast to those of the EU, minimalist institutions (McKinney 2000).<sup>1</sup>

A Free Trade Commission oversees the implementation of the agreement and helps resolve disputes that may arise from application of the agreement. It consists of the trade ministers of the three countries who meet once a year to discuss the agreement and to deal with any problems. The Free Trade Commission oversees working groups that look into specific trade issues, and basically focuses on trade facilitation issues arising from the NAFTA.

Besides the general dispute settlement mechanism of NAFTA, there are specific dispute settlement mechanisms for addressing financial issues, investor-state disputes, and trade remedies. Chapter 11 of NAFTA provides that companies from one of the countries investing in another can sue the federal government of the host country for damages arising from violation of the terms of the agreement, with the dispute settled through binding arbitration. Chapter 19 of the agreement provides for binding arbitration of disputes arising from the application of antidumping or countervailing duty laws.

The North American Agreement on Labor Cooperation established a North American Commission on Labor Cooperation (CLC) with a secretariat located in Washington, D.C. A council comprised of the labor ministers of the three countries oversaw the work of the commission. The commission encouraged cooperation and consultation regarding labor issues in North America, and conducted some studies of North American labor markets. The CLC is, unfortunately, no longer functioning due to lack of funding. National Administrative Offices in each of the NAFTA countries were established to hear complaints that member countries are not enforcing their labor laws.<sup>2</sup> They may issue a report on the matter under investigation, and if the issue remains unresolved they may seek an evaluation from a committee of experts. Should the matter still remain unresolved, theoretically the matter could go to binding arbitration with monetary enforcement assessment.

The North American Agreement on Environmental Cooperation likewise established a North American Commission on Environmental Cooperation (CEC) that is overseen by the environment ministers of the three countries. The CEC secretariat is located in Montreal, Canada. The CEC has continued to receive funding, but its budget has recently been reduced. The CEC has conducted some useful studies on the environment of North America, the first studies looking at the region as a whole. The CEC is able to self-initiate studies of perceived environmental problems, or respond to requests of private parties to investigate such problems. The CEC can receive submissions from persons or organizations in

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<sup>1</sup> The next six paragraphs draw upon information presented in (McKinney 2000).

<sup>2</sup> In recognition of the fact that the US was negotiating a number of bilateral and regional free trade agreements, in December 2004 the name of the US NAO was changed to Division of Trade Agreement and Technical Cooperation (in the US Department of Labor) to implement the labor provisions of all of the free trade agreements.

either of the member countries alleging that a member country is not enforcing its environmental laws. It studies the issue and may publish a factual record describing the situation. If one country considers that another is engaging in a persistent pattern of failing to enforce its environmental laws, the case can be taken to binding arbitration with possible monetary enforcement assessment. Both the NAAEC and the NAALC have a supranationalist element in that some decisions can be taken by a two-thirds vote of the respective national representatives rather than through consensus.

Two other NAFTA-related institutions are bilateral rather than trilateral and deal with environmental issues along the US-Mexico border. A Border Environment Cooperation Commission assesses proposals for the funding of environmental projects in the border region and makes recommendations to the North American Development Bank (NADBank), which makes loans to fund the approved projects. While some much-needed projects have received NADBank funding, the institution is grossly underfunded to address environmental needs along the border.

### **Theoretical Explanations for Divergent Developments**

As described above, regional economic integration has proceeded very differently in Europe and North America, and the resulting institutional arrangements diverge widely. Can these differences be explained by theories of comparative regional integration? To some degree they can.

Economic integration arrangements began in Europe primarily from a desire to try to ensure peaceful relations. But once the process was underway, it seems to be explained reasonably well by neofunctionalist political theory initially articulated by Ernst Haas (1968). According to this theory, as countries become economically interdependent with each other, demand increases for rules and procedures to simplify their interactions. The higher degree of interdependence creates a need for institutions to facilitate cooperation among the participating countries, so as to realize the potential for mutually beneficial gains and to address negative externalities (Keohane 1984). Institutions can also provide “voice opportunities” for weaker countries in the relationship to make their views known and have them acted upon (Grieco 1994). However, certain conditions are important in determining whether the institutions demanded will be supplied. The supply of institutions depends upon a high degree of social and political pluralism in the participating countries, a reasonable degree of symmetry among the countries with regard to this pluralism so that interest groups in the different countries can unite across national boundaries in pursuit of common goals, and highly bureaucratized decision-making in the member countries that makes policy-coordination by national civil services more efficient (Mattli and Sweet 2012).

Economic interdependence of the EU countries greatly increased as a result of the common market arrangement, and conditions sufficient for suprana-

tional institutions to develop existed. The completion of the internal market under terms of the 1985 Single European Act further increased economic interdependence, and in 1992 the Treaty on European Union laid the groundwork for monetary union and expanded the role of the supranational institutions. The common currency and monetary union among the participating countries further increased their economic interdependence, and the strains arising from the Eurozone crisis have caused moves toward a banking union and some steps toward fiscal union. The independence and supranational character of the European Central Bank have also been strengthened during this time.

In general, there has been a progressive move toward greater supranationalism of the institutions of the European Union as greater economic interdependence has created a demand for stronger regional institutions, and the necessary conditions for calling forth supply of these institutions have generally been present.

The conditions in North America have been very different than in Europe, and regional economic integration in North America has a distinctly different character. The theory that has considerable explanatory power for North America is externality theory. According to this theory the demand for regional institutions depends on both the frequency and the perceived riskiness of transactions among the member countries. Externalities that affect cross-border economic transactions "...arise from economic and political uncertainty as well as financial hazards that market actors may face when dealing with multiple polities and markets in a region" (Mattli and Sweet 2012: 6). As new opportunities for exchange arise, the demand increases for regional institutions to alleviate these costs. However, political leaders must be convinced that supplying these institutions is worth the costs in terms of national sovereignty conceded (Mattli and Sweet 2012).

In contrast to the European Union where positive integration measures (regional regulations and policies) have been employed, in North America mainly negative integration measures (removal of impediments to trade and investment) have been used. Because the United States has been stable and for the most part liberal in its trade policies, and therefore has acted as "benevolent hegemon" in North America, there has not been as much demand for regional institutions as in Europe. And because each of the three countries of North America has jealously guarded its sovereignty, there has not been a willingness on the part of politicians to develop strong regional institutions.

A third theory that has some explanatory power for both the European Union and NAFTA is contracting theory. According to this theory, the institutional development of a regional economic integration arrangement will depend heavily on the original contract agreed (Cooley and Spruyt 2009). In the European Union, the basic documents such as the Treaty of Rome were incomplete agreements in that they set forth general priorities and objectives, but were not very specific about how these priorities and objectives were to be achieved. The



intention was that the terms of the agreement would subsequently be defined and perhaps revised according to the wishes of the parties involved, and in view of changing circumstances. Supranational institutions such as the European Commission and the European Court of Justice were given authority to make decisions that could only be reversed by unanimously agreed treaty revision. Such a treaty allows for the evolution of institutions and for increases over time in their supranational authority (Mattli and Sweet 2012).

In contrast, the NAFTA is a more complete treaty spelling out its terms in great detail. Its purpose was much more limited than that of the Treaty of Rome in that it aimed only at establishing a free trade area, although it did deal with much more than tariff elimination in that it addressed nontariff barriers to trade, investment regulations, and intellectual property protection. Its provisions are quite specific, however, and there are no supranational institutions that have the authority to elaborate on or modify them. It has an intergovernmental mode of governance (Mattli and Sweet 2012).

According to contracting theory, the type of contract upon which a regional integration scheme is founded will be influenced by how asymmetric in power the contracting parties are, and how willing the parties are to cede national sovereignty to regional institutions (Cooley and Spruyt 2009). The European Union countries had more power symmetry and were more willing to make concessions of national sovereignty than were the countries of North America. In North America, the United States dominates the region in terms of economic and political power, so Canada and Mexico insisted on a complete contract with terms spelled out specifically, with any possible future changes requiring the consent of each of the countries. Furthermore, the United States had made it clear that it would cede no national sovereignty to supranational institutions, and therefore a complete contract was considered necessary by Canada and Mexico to protect their interests (Mattli and Sweet 2012).

## **Conclusion**

The regional economic integration arrangements of the European Union and NAFTA have developed in very different ways and have distinctly different institutional structures. The countries of the European Union have chosen to deal with collective action problems through setting up robust supranational institutions and delegating to them the authority to make binding decisions. On the other hand, the countries of North America have chosen to deal with collective action problems through regional cooperation, jointly exercising authority through minimalist intergovernmental institutions. The different paths chosen on opposite sides of the Atlantic can be understood through the lenses of neofunctionalist, externality and contracting theories of comparative regional integration.

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# Global Political and Economic Restructuring through Free Trade Agreements (FTAs)

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## Abstract

Research on deeper economic cooperation by preferential trade agreements (PTAs) has mostly centered on the economic implications of the PTAs for decades. A number of alternative analyses emphasize the role international power relations and multilateral institutions play in the formation of regional economic initiatives either positively or negatively. The new generation of FTAs differs from earlier waves of similar agreements of the nineteenth and twentieth centuries. They are probably much less about economic benefits than geostrategic objectives and global political concerns. It is, however, almost inevitable that in a period of uncertain economic growth "...the ultimate success of the negotiations and the long-term viability of the arrangements turn more on economic and commercial considerations" (World Economic Forum 2014: 18).

## Introduction

For decades, mainstream research focused almost exclusively on the economic implications of preferential trade agreements. In most cases *ex ante* theoretical studies and impact assessments have emphasized mostly the positive impacts experienced by the countries participating in such arrangements, while possible negative outcomes were considered unlikely scenarios.<sup>1</sup> Recent international trade discourse has been dominated by mega-regional trade agreements.<sup>2</sup> These trade agreements can produce widespread and often unforeseen effects on domestic economies, international relations and politics. These impacts are very diffi-

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<sup>1</sup> According to the literature, there seems to be a consensus that earlier arrangements in the nineteenth century were more positive in terms of trade creation while those between the world wars were mostly trade diverting. But regarding the implications of preferential trade agreements concluded after World War II there is no consent at all (Mansfield 1999: 593).

<sup>2</sup> In this paper the term "mega-regional" FTA is used to mean agreements that involve three or more countries; cover at least 25 percent of global trade flows; and include regulatory commitments rather than trade liberalization (Draper, Lacey, Ramkolowan 2014: 8). From another perspective, these deals can be classified as deep arrangements which cover several measures beyond tariffs. These agreements also change tariffs but the most important implications relate to nontariff barriers, regulations and standards, or other similar measures (Lawrence 1996).

cult to forecast or fully understand given the uncertainties regarding the content of the final agreements and lack of consent about the impacts of such large-scale arrangements. Mutually advantageous implications of ambitious free trade agreements under negotiation, however, cannot be taken for granted.

In the past decade the multilateral system administered by the WTO came under challenge. A number of rapidly developing countries do not share the core principles that have underpinned open rules-based commerce or more precisely, they do not accept the rules of Western dominated institutions without having their say properly heard. Several states consider that traditional institutions of international economic relations and regulation do not take into account the changing global power relations. Large emerging countries including China, India or Brazil are becoming increasingly important economic and political players globally (or regionally – Russia); but, their weight is not fully reflected in the international power relations.<sup>3</sup> Most advanced countries consider this development to be a major challenge to the international economic and political system – the very system they once used to have almost exclusive influence over the world. These different interests led to either the paralyzation of some international organizations or to their reforms (the IMF is a good example) or to the deadlock of their operations (e.g. the WTO) or to increasing political and security challenges (Russia).

Given these significant changes, it seems that the declining global hegemony of the US – mostly in terms of economic indicators – and the very poor economic performance of the European Union, have contributed to the current wave of regionalism through deep trade deals. It is also most certainly true that we have entered into a new phase of international power relations.<sup>4</sup> The new mega-deal proposals constitute a new-generation of negotiations aimed at repositioning economies in a more intensified global competition. Other opinions go further by emphasizing that the new generation of FTAs may be an appropriate means in managing the challenges of emerging countries. On the other hand, however, these agreements are feared to undermine the social model of Europe. The basic question for many analysts and policy makers in Europe is how the economic problems can be managed in a sustainable way while preserving the values of the social market economic systems that Europe is justifiably so proud

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<sup>3</sup> For example, the organizational reform of IMF has been stalled since 2010 by the obstructions imposed by the US Senate. The reform would grant increasing voting powers to developing countries. See, for example, the latest coverage: Statement by IMF Managing Director Christine Lagarde on IMF Quota and Governance Reforms. For more information see Press Release No.14/568, December 12, 2014 accessible at <http://www.imf.org/external/np/sec/pr/2014/pr14568.htm>

<sup>4</sup> As Pascal Lamy, Director-General of WTO in 2012 put it: “The old theories and hypotheses which governed the way we looked at trade in the twentieth century will require better calibration with the new reality of trade in the twenty-first century.” Article available at: [http://www.wto.org/english/news\\_e/sppl\\_e/sppl258\\_e.htm](http://www.wto.org/english/news_e/sppl_e/sppl258_e.htm)

of (e.g. labor regulations, environmental protection, health care and pension systems etc.).

Today mega-trade deals seem to be used more extensively to influence future economic, political and interstate power relations on a global scale. The uncertainties, however, regarding the impacts of these agreements are significant and no one can predict the future with much confidence. The economic arguments in support of TTIP (Transatlantic Trade and Investment Partnership) and TPP (Trans-Pacific Partnership) seem to be based on wishful thinking – an approach that several times has biased the fair *ex ante* evaluations of PTAs or deeper economic cooperation (Barbee 2014: 208).

### **Waves of Free Trade Agreements**

The underlying reasons behind the establishment of Free Trade Agreements have been numerous since the second half of the nineteenth century when the very first wave of such arrangements was initiated. In addition to the bilateral free trade agreement between Great Britain and France in 1860, which involved the MFN clause, several customs unions were also established at the time (Austria-Hungary, Germany, Italy etc.) which had led to a remarkable trade liberalization, an almost complete single market in Europe by the turn of the century, covering a very large share of the global trade flows. Between the two World Wars a completely different international economic system emerged in which the new regional arrangements had caused trade to divert and eventually separated trade blocks from each other and, as such, pursued inward looking, trade protectionist policies. All such initiatives were highly preferential in the time of the Great Depression.

Although expected, economic benefits have always been one of the most important driving forces behind the waves of regional economic integration, from time to time, additional interests and objectives would surface. There have been times when economic benefits were subdued to international political interests. We witnessed an especially complex set of motives after World War II. Some of the most important perspectives are as follows: (1) FTAs were often utilized by larger states to intensify their economic and political influence on smaller countries. A prime example for this type of motivation is the establishment of COM-ECOM (Council for Mutual Economic Assistance) in order to coordinate the economic development in Eastern Europe, but it goes without saying that control over this geographically vast economic integration was in the hands of the Soviet Union. (2) An additional motivating force behind the birth of FTAs was the desire to reduce the collective dependence of groups of states on third parties. Typical examples include the regional initiatives between developing countries during the fifties and the sixties in order to mitigate their vulnerability in international economic relations against more developed regions. (3) The establishment of the European Communities after World War II seems to be the most successful at-

tempt at managing the security policy challenges posed by the Soviet Union. (4) In other cases regional arrangements promoted and consolidated domestic economic reforms and democratic transformation. This was the case of the EU integration of Greece, Portugal, and Spain. The waves of enlargement in the European Union have demonstrated that economic integration can usefully serve as the driving force for political cooperation and as a means of “stability export” both in economic and political understanding.

While stronger economic ties or broader economic opportunities worked well in developed Western European countries, economic integration and cooperation between less developed countries were less successful. By the end of the eighties, several earlier assumptions had changed. Reforms and political transformation had taken place in many parts of the world which created a new framework for trade agreements. In less developed countries the earlier autarchy-oriented, inward-looking policies had changed. Import substitution strategies and integrations have always faced the same burden: lack of capital, the inability to obtain the latest technologies, and the scarcity of qualified labor force. These countries started to become more open towards international economic (trade and FDI) cooperation. The collapse of the Soviet Union and the economic and political changes in the Soviet space prompted a number of countries to stabilize their internal transformation by entering the European Union. In addition, in the Post-Soviet region we also witnessed several attempts by Russia to create a sort of economic integration. In this period, the objective of small countries became increasingly centered on the need to align and integrate with a large “center” – it was expected that several benefits may be associated with this adjustment, including the inflow of FDI, improving export performance and the stabilization of political systems after transitioning from an autocratic regime to a democratic one.

### **Changing Interstate Power Relations and the Role of FTAs**

After World War II, the GATT liberalization and the establishment of preferential trade arrangements went hand in hand for several decades and they seemed to be complementing each other. But, because of the significant changes in the global business environment and interstate power relations recently, the two processes started to move in completely different directions. These changes had contributed to the emergence of a new wave of regional integration efforts completed now with several novel features.

(1) In contrast to previous decades, trade liberalization in the manufacturing of goods in the multilateral framework had deepened. As a result, the potential benefits of free trade agreements stemming from the elimination of tariffs would only make a limited impact in most cases. In other words, the Vinerian balance of losses and benefits in terms of trade diversion and trade creation – even in theory – should be small without additional efforts to extend the scope of

the arrangements. (2) Foreign direct investments of recent years resulted in the emergence of global value chains that strengthened multiple economic ties not only between neighboring countries, but across regions and continents. FDI links and relations became much more convoluted compared to previous decades (centuries) due to the new strategies of large transnational firms. (3) Some of the arrangements made since the nineties started to become deeper and deeper as they were no longer just about tariff cuts. Non-tariff barriers were also being eliminated or other fields of economic policies were being harmonized. (4) The discrepancy between global liberalization and regional cooperation became even more evident. Multilateral trade negotiations stalled and very little or no advancement was made in this regard. (5) Once hailed as the most successful integration effort, the European Union and most importantly the Eurozone were facing a series of crises ranging from economic growth problems to income inequalities and social hardships. (6) The shift in the global economic balance of power intensified after the turn of the millennium and was coupled with the consequences of the economic crisis unfolding after 2008. It was against this backdrop that negotiations of mega-regional trade agreements were started with the objective of establishing deep integration with countries that possess overwhelming shares in global trade and FDI and place central role in the emerging global value chains – a development that has attracted great attention in recent years from among scholars and large international economic institutions.<sup>5</sup>

Due to these changes, the twenty and twenty first century regional trade agreements or regional arrangements should be fundamentally different from each other. As Richard Baldwin puts it: “[t]wentieth-century RTAs concern ‘made-here-sold-there’ goods, while 21<sup>st</sup> century regionalism concern ‘made-everywhere-sold-there’ goods. The difference means that 21<sup>st</sup> century RTAs include rules on *making* goods as well as *selling* them” (Baldwin 2014: 5). The mega-regional deals are increasingly thought to be motivated not simply by economic objectives, but more importantly by geopolitical considerations (or simply by international political objectives) which is not in contradiction with the previously mentioned diverse set of motivations behind earlier trade arrangements.

Referring to more details, the following motives can be identified behind the large objective of “geopolitics.” (1) In recent years, economic growth in the world has been uneven. Large emerging countries have experienced rapid economic convergence led by China’s catching up in the past decade, but other states also have shown growing influence on global economic developments and trade. China has overtaken the US in term of its share in global GDP (it is measured at PPP, but it is still an important development).<sup>6</sup> As a result, the soft power of

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<sup>5</sup> See inter alia for example: Interconnected Economies. Benefiting from Global Value Chains. OECD Publishing. <http://dx.doi.org/10.1787/9789264189560-en>; or IMF 2013. etc.

<sup>6</sup> For most recent data see the World Economic Outlook of the IMF see <http://www.imf.org/external/pubs/ft/weo/2014/02>.



emerging countries and especially that of China may challenge the soft power of the US and the EU (Stiglitz 2015). (2) The European economy has been struggling since 2008. Lack of economic growth and emerging social problems in a number of member states are threatening the very foundations of the EU. It seems that we are not only dealing with temporary economic stagnation affecting a few countries, but with a rudimentary, systemic problem, the crisis of the Eurozone. As a result, dissatisfaction among the population is increasing, domestic political challenges are growing and future prospects are unclear.

The emergence of contemporary large deals is explained by the need to set standards to which emerging nations should adjust if they wanted to benefit from international economic relations with large industrialized nations. These new trade arrangements may win some time for the current most developed countries: if these deals succeed, and emerging countries adjust, then they will follow western rules and comply with liberal market economic principles. Economic benefits of FTAs – and deeper cooperation – are not at all obvious today. *Ex ante* and *ex post* analyses of FTAs also differ from each other considerably and in recent decades it has been almost impossible to separate the economic impacts of institutionalization of cooperation (e.g. a free trade agreement) and the impacts of overall global liberalization (Vetter 2013: 3). While geopolitical motives may be important from the perspectives of the launching and negotiating mega-regional trade agreements, these considerations are insufficient to implement them in a long term sustainable way. In other words, “TTIP at its core is an economic negotiation that in the end will stand or fall on its economic merits” (Hamilton 2014: VII).<sup>7</sup>

Many decision makers and analysts view the emergence of these agreements as a tool to influence interstate power relations – an approach that seems to be similar to the race during the Cold War between the West and the East. According to this perspective, the changing economic realities may be influenced by building blocks that are unified by the unlimited liberalization of economic flows and regulation. This way the free trade agreements may serve as a means to strengthen political alliances with long term partners in the developed world. Building blocks also seem to follow the logic of the interwar period. An important difference from the interwar period is the existence of the WTO, a multilateral institution that may mitigate the risks associated with building blocks – provided it can function properly. If not, the future of international economic relations and the prospects depend on the reaction of large emerging countries currently not participating in the negotiations.

Here an interesting theoretical notion put forward by Paul Krugman is worth considering. According to Krugman, if a country with PTA tries to use its power to influence global trends; this may lead to disastrous consequences if oth-

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<sup>7</sup> A recent paper argues that official studies do not offer a solid basis for an informed decision on TTIP. See Capaldo 2014.

er similar agreements are in place because “the blocs may beggar each other. That is, the formation of blocs can, in effect, set off a beggar-all trade war that leaves everyone worse off” (Krugman 1991: 8). According to him, these negative impacts may only be minimized if trade blocks are few or if there is a very large number of such arrangements. If there is only one block, then it is global free trade. He argues that “world welfare is minimized for a world of three trading blocs” (Krugman 1991: 12). If we consider this, it is remarkable that the share of TTIP and TPP in terms of global GDP and global trade is over fifty percent (excluding the double counting of the US). From this perspective, the idea of RCEP (Regional Comprehensive Economic Partnership) may attract greater attention in the future.

## Options and Conclusions

If the US led mega-deals fail, it will hurt the image and leadership of advanced countries in international trade issues in favor of emerging nations, most importantly China. If the deals are successful, developed countries will get additional leadership by setting norms and regulations for large segments of international trade flows (Dube 2014: 17). Taking into account the above considerations, the most important question concerns the response of third countries, especially large emerging countries having a major role in formulating global shifts and changes. The basic strategies are the following.

1. *Wait and see.* There are a lot of uncertainties surrounding these deals especially the TTIP because of the widely different opinions within the European Union. Most critics are focusing on the ISDS (Investor State Dispute Settlement), environmental protections or GMO (Genetic Modified Organisms) products. For third countries, it is reasonable to wait and see what the final outcome of the agreements concerned will be. The external situation and the negotiation positions may change significantly. It cannot be ruled out that significant concessions and compromises will be the only solution for consolidating these diverging interests. Just to mention one issue: probably it would be reasonable to abandon the ISDS in its current form in TTIP negotiations given the very negative opinions and sentiments of a wide circle of stakeholders.<sup>8</sup>

2. *Disengagement from global trade liberalization.* If multilateral trade negotiations are blocked because of internal conflicts (between advanced and emerging states) then several countries may become even more disinterested in international trade liberalization. Mega-trade deals coupled with slow progress in multilateral trade negotiations could easily result in developing inward-looking or more protectionist policies in several countries.

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<sup>8</sup> Among many other proposals see for example: Congressional Financial Services Committee leaders: Exclude ISDS from US-EU deal <http://www.bilaterals.org/?congressional-financial-services&lang=en#sthash.Q9Kwk01h.dpuf>.

3. *Unilateral significant liberalization of excluded countries.* This would serve as a means to mitigate the trade diversion impacts due to mega-deals. Although it is not very likely, theoretically we can construct a framework where outside countries with large liberalization or adjustment efforts can simply eliminate most of the advantages of the participants in mega-trade deals while preserving some independence in their regulatory framework (World Economic Forum 2014: 28-29).

4. *Joining mega-deals.* This is the same strategy that was followed by mostly smaller countries in earlier decades when they considered it their interest to swiftly adjust to the rules defined by larger countries. This is a quite reasonable strategy for small states with insufficient domestic factors of production to boost growth. The situation may be different for large countries, but even in their case, bilateral negotiations of a certain kind with the EU or the US may be feasible. In fact, this would be the best scenario for advanced nations since this would mean that large emerging countries are willing to adjust to the rules set by the US and the EU. As a result the rule setter and rule taker position would not change much globally.

5. *Trade war by establishing new trading blocks.* Although trade between large outside countries is somehow limited mostly for geographical reasons, theoretically, the establishment of other trade deals with the participation of large countries and nations from the African continent, Far Eastern and South American countries cannot be ruled out. China, India, Indonesia, Russia, Brazil and Nigeria altogether make up almost 45 percent of the global population. If we accept that mega FTAs currently negotiated are more and more driven by political and strategic interests and not only by economic ones, the establishment of alternative competing arrangements may be a realistic option.

6. *Revitalization of the WTO.* As stated in the World Economic Forum (2014), “[i]f the RTAs and their power asymmetries take over, there is a risk that the GATT/WTO would go down in future history books as a 70-year experiment where world trade was rules based instead of power-based” (27). Something similar happened to the IMF before the economic crisis of 2008. Current perspectives for larger engagement of WTO in global trade talks are low. Hopes, however, are realistic given the small steps taken in the Bali ministerial meeting, which were celebrated loudly. In fact, for the time being, these small agreements saved the WTO from falling into oblivion. Its future existence is still not based on strong foundations. The role of IMF in global affairs was revalued due to the economic crisis. If mega-deals fall short of expectations, the WTO can still serve as an instrument of global cooperation in international trade.

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# **Trade in Higher Education Services in the TTIP Negotiations and Beyond**

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## **Abstract**

The unprecedented growth of trade in services over recent years reflects the composition of the contemporary knowledge economy, in which countries seek a balance between international cooperation and national competitiveness. Given the opportunity to further liberalize international trade this paper explains the negotiating parties' interests in higher education services within the context of the Transatlantic Trade and Investment Partnership (TTIP). This research analyzes how trade in higher education services may be addressed in ongoing negotiations, given the preexisting trade frameworks, and it draws conclusions comparing the interests of countries in Europe and the U.S. to participate in regional integration initiatives for higher education services.

## **Introduction**

The growth of trade in services reflects the composition of the contemporary knowledge economy, in which partner countries seek a balance between international cooperation and national competitiveness. The United States (U.S.) and the European Union (EU) are historical trading partners, and they enjoy the largest trade and investment relationship in the world. Given the opportunity to further liberalize international trade this paper explains the negotiating parties' interests in higher education services within the context of the Transatlantic Trade and Investment Partnership (TTIP). This research analyzes how trade in higher education services may or may not be addressed in ongoing negotiations, given the preexisting trade frameworks, particularly the General Agreement on Trade in Services (GATS) originally negotiated by the World Trade Organization (WTO) in 1995. This paper draws conclusions comparing the interest of countries in Europe and the U.S. to participate in regional integration initiatives for higher education services. The potential inclusion for private education in ongoing trade negotiations is still obscure, and the scarcity of public information may be a reason for reserved interest in this sector. Public education is not open for trade liberalization as stated in the GATS.

Given the importance of the services sector in trade agreements, international trade governance has the potential to intersect with higher education poli-

cies across countries. This research examines the place of trade in higher education services in Europe and the U.S. in reference to the formal negotiating trade frameworks. Specifically within the EU, there is uncertainty since the education sector is not explicitly excluded in the Services Directive, which was adopted in late 2006 to simplify the provision of business services in the Single Market. At this time, it is not clear whether higher education services will be part of the TTIP or related negotiations. An analysis of the foregoing treatment of trade in services in previously negotiated agreements serves as an important guidepost for future considerations. International market access for higher education services and mutual recognition of professional qualifications are two key areas in the negotiations that are considered in this research.

### **Recent and Ongoing Mega-Trade Negotiations**

Since 2001, the leading associations of higher education in the U.S., Canada, and Europe have taken the position that their member institutions were committed, “to reducing obstacles to international trade in higher education using conventions and agreements outside of a trade policy regime” (Joint Declaration 2001).<sup>1</sup> The TTIP was announced in the spring of 2013, with the first formal negotiations taking place from July 8 to 12 in Washington, D.C. Alongside these negotiations are important developments in multilateral trade. The Trade in Services Agreement (TiSA) is being negotiated with more than 23 members of the WTO, which comprise 70 percent of global trade in services (European Commission 2015). The TiSA negotiations, for which the EU countries are represented as one of the negotiating members, were launched in 2012. The Comprehensive Economic and Trade Agreement (CETA) was announced by the EU and Canada on October 28, 2013. The CETA may be considered as a prototype for an even larger potential agreement of the TTIP, and the CETA is expected to increase two-way trade by 23 percent or 26 billion euro (EUA 2014a:9). The Trans-Pacific Partnership (TPP) has also run ahead of the TTIP negotiations, and the TPP is among twelve countries in the Pacific Rim. Like CETA, the TPP serves as background to the TTIP and TiSA negotiations. The TPP negotiations formally began in November 2011, among the U.S. and countries in the Trans-Pacific Strategic Economic Partnership.

These transatlantic negotiations must be understood in the context of EU and U.S. trade policies, and in accordance with rules in the WTO. A final TTIP agreement would be composed of three parts: Market Access, Regulatory Cooperation, and Rules (European Commission 2015a). There are four Modes in negotiations for the supply of services in the GATS and the proposed TTIP, which

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<sup>1</sup> These leading higher education associations are the American Council on Education (ACE), Association of Universities and Colleges of Canada (AUCC), Council for Higher Education Accreditation (CHEA), and European University Association (EUA).

are: 1. Cross border supply, 2. Consumption abroad, 3. Commercial presence, and 4. Presence of natural persons. Higher education services and professionally mobility policies are considered as part of Mode 4. An electronic educational service may be considered as part of Mode 1, and the presence on an international campus as part of Mode 3. The EU Member States have already liberalized many services in the framework of the GATS. The schedules for service liberalization in the TTIP, TiSA, CETA and other recent free trade negotiations are informed by the criteria that negotiators refer to as "GATS-plus." Therefore the current negotiations of the TTIP and TiSA must build upon concessions already made in the GATS schedule. It is important to note that in the GATS public services are excluded, which means that public services from state higher education institutions are excluded from negotiations (EUA 2014 2:4).

Whether the TTIP negotiations lead to liberalization of market access in higher education services is a key question as the negotiations develop (EUA 2014a). Education is closely tied to national identity, and an identity is political (Checkel and Katzenstein 2009). In the EU, the balance between national and regional identity is a delicate equilibrium. Therefore, it is expected that the balance between the state role and a supranational role in higher education and research will be a sensitive public policy issue within the region and across the transatlantic. Policy diffusion throughout the region has gained momentum over recent decades (Börzel and Risse 2012). This regional diffusion has been replicated across continents. As Europe has led with regional integration since post-World War II, starting with economic integration, it is also leading with integration of the knowledge economy (European Commission 1997). The knowledge economy is composed of higher education services together with research and innovation policies. The European Union has policies in each area, though education has remained a national competency as delineated in the Maastricht Treaty, effective November 1, 1993.<sup>2</sup>

The Lisbon Treaty, effective December 1, 2009, specifies further how the EU may contribute to the quality of education by encouraging cooperation across member states.<sup>3</sup> While education remains a national competency support-

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<sup>2</sup> Treaty of Maastricht signed February 7, 1992 stated in Chapter 3, Article 126, "*The Community shall contribute to the development of quality education by encouraging cooperation between Member States and, if necessary, by supporting and supplementing their action, while fully respecting the responsibility of the Member States for the content of teaching and the organization of education systems and their cultural and linguistic diversity.*"

<sup>3</sup> The Lisbon Treaty signed December 13, 2007 stated in Article 165, Part 3, Title XII how the EU may support education,<sup>3</sup> as it "*shall contribute to the development of quality education by encouraging cooperation between Member States and, if necessary, by supporting and supplementing their action, while fully respecting the responsibility of the Member States for the content of teaching and the organization of education systems and their cultural and linguistic diversity.*"



ed by the EU, there has been an increased supranational effort in regional cooperation in higher education. Given the global competition in the knowledge society, the EU has taken an increasingly active role in higher education and research policies. Shared political, economic, and cultural values have resulted in the unprecedented higher education cooperation to create the European Higher Education Area (EHEA), the largest academic mobility initiative in the world. The Bologna Process was initiated in 1999 and established the objectives for the EHEA, in which the European Commission is a partner alongside 47 sovereign states. Recognition of the trends of economic globalization, together with internationalization of universities, drives the Bologna Process (Nokkola 2007:223). The European Commission plays a central role in higher education cooperation, supporting the advances in regional integration of this sector thus far. It represents the interests of the 28 EU member states, and it serves as a facilitating institution for higher education policy.

Comparatively in the U.S., higher education governance remains institution-centered rather than state-centered in its policy making, and in the U.S. institutions are accredited by regional peer review associations. In Europe this accreditation is given from national qualification agencies, in relationship with the European Association for Quality Assurance (ENQA) in Brussels, Belgium. While in the U.S. peer higher education institution associations accredit their fellow member institutions (U.S. Dept. of Ed. 2015). In the U.S. the public sector has an important role at the sub-national level among the fifty states to contribute substantively to financing public universities.

### **Europe and the United States: Trade in Services and Higher Education**

These trade liberalization efforts align with the negotiating parties' strategic interests. Expanding higher education access and quality, and improving the quality of the workforce are objectives across countries. The European Commission's Europe 2020 economic growth strategy has objectives for higher education alongside employment, innovation, social cohesion, and environmental sustainability. There have been eight negotiating round meetings since July 2013, with the most recent being in early February 2015 (USTR 2015). Trade in higher education services is not specifically excluded from the negotiations, according to US and EU negotiators (EUA 2014 2:4, 3:8). While the EU has the exclusive competency for the Single Market, and the related Services Directive, it supports the member states in their competency for higher education policy. There exists ambiguity on the relevance of the education sector within the Services Directive for the common market.

Seventy percent of employment in the U.S. is in the services sector (CRS 2014:14). Measured from the year 2000, there is an increasingly positive trend in trade in services between the U.S and the EU. Trade in services exports reached \$200 billion dollars in 2012, nearly double the level from 2000. Trade in services

imports demonstrated another double increase to nearly \$150 billion in 2012 (Akhtar and Jones 2014: 14). Except for a slight downturn during the global recession years from 2008 to 2009, trade in services continues on an upward trajectory.

The distinction between the public sector and the private sector in delivering higher educational services is necessary to delineate for the applicability of future negotiated agreements. As the GATS rules hold in the TTIP negotiations, in the GATS public services are excluded, which means public sector higher education institutions. Therefore current and future questions center on the place of private sector higher education and adult education institutions in trade agreements. Stakeholders have concern for how higher education would be treated as tradable service, if included in future trade agreements.

### **Market Access to Higher Education and Mutual Recognition of Professional Qualifications**

Taking into account how higher education is considered in various international trade forums, the GATS addresses twelve service areas, one of which is education. International market access for higher education services and mutual recognition of professional qualifications are two areas where ongoing policy developments are important for higher education services. Content analysis of recently negotiated agreements provides information about potential content within in the ongoing TTIP and TiSA negotiations. The CETA addresses mutual recognition of professional qualifications, and the TiSA is negotiating the short-term professional mobility of service providers (EUA 2014 3:18). In addition, “A Committee on Mutual Recognition of Professional Qualifications shall also be established under the Committee on Services and Investment and shall report to that Committee” (CETA 2014:448). The Committee may advise on a Mutual Recognition Agreement (MRA) or otherwise. In the CETA all professions may be considered to be part of a MRA. Comparably in the TTIP, only specified professions will be included in a potential MRA (EUA 2014 3:10). The European Services Forum (ESF) supports market access to the U.S. by European professional service providers, and the fields for which it advocates for mutual recognition are accounting, architecture, engineering, and legal services (EUA 2014 2:6). Potentially challenging in the future would be recognition in the U.S. where the fifty states have unique responsibility for accreditation across professional fields. The lead U.S. Trade Representative negotiator, Dan Mullaney, for his side, affirmed discussions regarding the professional mobility of architects and engineers (EUA 3 2014:10).

In market access, the exporting country has the responsibility for quality, and the importing country is not allowed to intervene, according to the Services Directive. This is contrary to the GATS, which allowed the importing states to establish quality assurance and accreditation systems that were non-

discriminatory (Amaral 2014:16). These inconsistencies between the EU Services Directive and the GATS, regarding exporting and importing countries' responsibilities in higher education are issues to be addressed in future trade legislation. The Services Directive supports the Single Market established with the Maastricht Treaty by simplifying business procedures for service providers, and it is an assertive action taken by the EU to extend the liberalization of services to education. The European Parliament and the European Council adopted the Services Directive on December 2006, and it was fully implemented by the member states within three years. The treatment of higher education is ambiguous because the Services Directive does not specifically exclude education broadly, even though national education systems are excluded. Some explicitly excluded sectors are environment, gambling, health, public health, and security. The Directive excludes the "Services of General Interest" (SGI), but includes the "Services of General Economic Interest" (SGEI), and it is difficult to define education in the appropriate category, particularly since there is no legal basis for their definition (Amaral 2014:14).

The TTIP considers how professional recognition may be actualized across participating countries. This makes an extension upon the objectives of the Bologna Process, for recognition of academic degrees across the 47 participating countries, to an even greater extent with the intention to ensure professional recognition intercontinentally (European Commission 2015c). The European countries and the United States are the largest markets for higher education as a destination. In Europe the educational exchange program of Erasmus, provided by the European Commission since 1986, has facilitated international trade in educational services. Various international education programs, partially supported and monitored by the Institute of International Education (IIE), in the U.S. are affiliated with the Bureau of Educational and Cultural Affairs (ECA) within the Department of State. The relationship of higher education to research and innovation is strong in the promotion of the mobility of students, scholars, and graduates for employability. The mobility of higher education for coursework and for research and development (R&D), and professional employment are complementary and together may be addressed comprehensively. The Congressional Research Service (CRS) has found that:

The treatment of services providers could be another area of focus in the TTIP negotiations. One issue that the TTIP could address is the licensing and certification of professional services providers. Appropriate credentials are required on both sides of the Atlantic in many fields such as medicine, insurance, education, and law. In the EU, such services are regulated by the member states, and, in the United States, at the state level. Thus, providing cross-border services could be challenging for services firms, because even if a services employee is qualified in one state or EU country, the certification may not be recognized elsewhere (Akhtar and Jones 2014:14).

The European Students Union (ESU) has taken the formal position that it does not welcome U.S. higher education institutions having open access to the European higher education market. Similar to the position of the higher education institutions in the Joint Declaration, this stakeholder would like to limit market access. Like the audiovisual sector has been taken off the negotiating table, with pressure from France in particular for cultural protection, the ESU advocates that higher education access not be a policy issue for negotiations (TTIP ‘threatens’ quality 2014). On market access issues there are stakeholders in higher education institutions that would like to protect national priority. On mutual recognition of professional qualifications there are fewer reservations, while national preferences continue to remain strong.

## **Conclusions**

The treatment of higher education services in the GATS has been limited. The ongoing negotiation of the TTIP and TiSA open possibilities for inclusion of provisions to liberalize higher education services in the private sector only (since the public sector services are protected from trade agreements). In the knowledge economy, higher education services and research innovation gain momentum from regional and global initiatives to support internationalization. The foregoing negotiations processes demonstrate the politically important issue areas for attention. The higher education services have not yet been comprehensively addressed in negotiations. The negotiated trade agreements must be approved by the legislature of each negotiating partner. In the case of the EU, each member state has an effective veto through the European Parliament. The Lisbon Treaty granted this institutional authority and veto power over trade agreements to the legislative body. The U.S. President has not received “fast-track” or Trade Promotion Authority (TPA) from the Congress, which expired in 2007 in the presidency of George W. Bush. Without the domestic political will these agreements will not come becomes finalized.

The higher education associations, such as the EUA and its US and Canadian counterparts, and some student stakeholders, concerned with educational quality represented by the ESU, have advocated to exclude private higher education providers from market access in the agreements. Higher education historically has been of high sensitivity politically. Therefore, stakeholder associations will pressure national governments to support measures to protect national higher education institutions from what may be viewed as unfair external competition. There is a distinction between higher education and adult education (or post-higher education) services in the GATS and in the TTIP, as legislation becomes crafted each may be treated separately. Looking to the future, the extent of TTIP provisions for education services in market access and mutual recognition of professional qualifications will be highly relevant to the sector.

The mega-regional trade and investment agreements strategically seek to balance a rising Asian presence, led by China, in international trade. They are a hybrid of regional arrangements and the WTO arrangement, except they do not include major emerging markets that will dominate world trade in the future, namely China, India, and Indonesia (Dadush 2015). As these trade agreements progress, there are risks that developing countries may be sidelined, given their challenges in matching the regulatory standards requirements (Dadush 2015). The higher education systems of developing countries are vulnerable to dominance from developed countries' negotiations (EUA 2014a:9). Negotiating common regulatory standards is more challenging than negotiating tariff reductions, given strong national prerogatives in traditionally sensitive areas such as agriculture, and in more recently considered areas such as education services.

This analysis has presented an overview of ongoing trade negotiations in services, specifically for the TTIP alongside the CETA and the TiSA. With an emphasis on market access and mutual recognition of professional qualifications in services, the ongoing negotiations will continue to face challenges from stakeholders in the higher education sector that seek to protect this sensitive area from market access. At this time it is not clear how the private sector providers of higher education, such as through private institutions abroad and through online degrees, may be treated in future trade agreements. The public sector service providers are protected from liberalization through the GATS rules. The dual purposes of education, to enhance social cohesion and to prepare for employability, are brought into the foreground as nations assess their willing to cooperate across national boundaries in formal trade agreements. Leading associations of higher education in the transatlantic community have said, "Higher education exists to serve the public interest and is not a 'commodity'," in affirming their members' interests not to pursue further liberalization of the higher education sector (Joint Declaration 2001). Therefore, any further concessions in the area of higher education policy are advised to proceed with caution. As has been noted, there are already avenues for higher education exchange independent of formal trade agreement frameworks. The place for higher education policy in the expanding economic integration through international trade agreements is still being determined. This analysis has addressed the historical challenges for higher education services considered as a component of international trade agreements.

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# The Price of Energy and its Impact on the Economies of the United States and Eurozone

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## Abstract

Economic history teaches that the price of oil matters because it has a severe and direct impact on the economic performance of countries. The data shows that every recession in the Organization for Economic Co-Operation and Development (OECD) countries in the last 50 years was preceded by a sharp rise in the price of oil. The world suffered an exorbitant increase in the price of oil (WTI Crude, real) during the summer of 2008, hitting US\$144.64 per barrel. Months later, a painful worldwide economic slowdown took place. Thus, the United States learned that it must work hard towards energy independence to break this correlation between high oil prices and economic recession. While the United States is working towards finding some energy independence, most countries in the Eurozone are oil and gas dependent. As the United States and the EU are about to finalize the Trans-Atlantic Trade and Investment Partnership, the economic performance of both blocks, particularly the Eurozone member states, will be largely determined by the price of crude oil and the price of the U.S. dollar.

## Introduction

Economic history teaches that the price of oil matters because it has a severe and direct impact on the economic performance of countries. Rising oil prices is equivalent to a tax increase which leads to a significant slowdown in economic activity.

The data shows that every recession in the Organization for Economic Co-Operation and Development (OECD) countries in the last 50 years was preceded by a sharp rise in the price of oil. Curiously, these increases in the price of oil were the result of armed conflicts. In fact, the four major armed conflicts of recent years can be linked directly or indirectly to the supply of oil and were immediately followed by economic slowdowns:<sup>1</sup> the First Oil Crisis of October of 1973, the Second Oil Crisis of January 1979, the First Gulf War in August 1990,

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<sup>1</sup> It is not the purpose of this article to elaborate on the nuts and bolts of the relationship between conflict, oil price and economic slowdown per se. That might be the topic of a future article.

and the Iraq War, or Second Gulf War, of March 2003. Furthermore, the world suffered an exorbitant increase in the price of oil (WTI Crude, real) during the summer of 2008, hitting US\$144.64 per barrel, and making many wonder if the world was facing another oil crisis. This episode was followed months later by a painful worldwide economic slowdown, inflation, increase of unemployment, and political instability with after-effects that will last for decades.

The U.S. economy is recovering from the Great Recession, but most countries in the Eurozone and the European Union (EU) are still seeking a way out. Furthermore, the United States has learned it must work hard towards energy independence to break this correlation between high oil prices and economic recession. For this reason, the U.S. has been looking for ways to be energy self-sufficient. Between 2005 and 2010 the country's shale-gas industry grew by 45percent per year.

Following the historic high of July 2008, the price of WTI-Crude real plunged to US\$43 in February 2009; reached a high of US\$115 in April 2011; and has been falling ever since. As a consequence, OPEC members are very nervous, and the drop of the price in oil had especially impacted the economies of countries such as Saudi Arabia and Venezuela.



Source: MacroTrends. <http://www.macrotrends.net/1369/crude-oil-price-history-chart>

While the United States is working towards finding some energy independence, most countries in the Eurozone are oil and gas dependent. The United States and the EU are about to finalize the Trans-Atlantic Trade and Investment Partnership and the economic performance of both blocks, particularly the Eurozone member states, will be largely determined by the price of crude oil and the price of the U.S. dollar.

## **The Price of Energy: Winners and Losers**

The price of oil surged from US\$16 per barrel in December 1998 to the all-time high of US\$144 in June of 2008. When the price of oil broke the all-time high of \$140 per barrel on Thursday, June 26, 2008, the Organization of the Petroleum Exporting Countries (OPEC) predicted that the price of oil would range between \$150 and \$170 per barrel in the years to come (Nasseri and Brown 2008). This extraordinarily high price had a detrimental impact on an already fragile world economy, forcing governments to work desperately to find ways of reducing the high energy bill for their economies and people. In fact, these efforts resulted in an important drop in the price of energy in the United States and a positive impact on the U.S. economy.

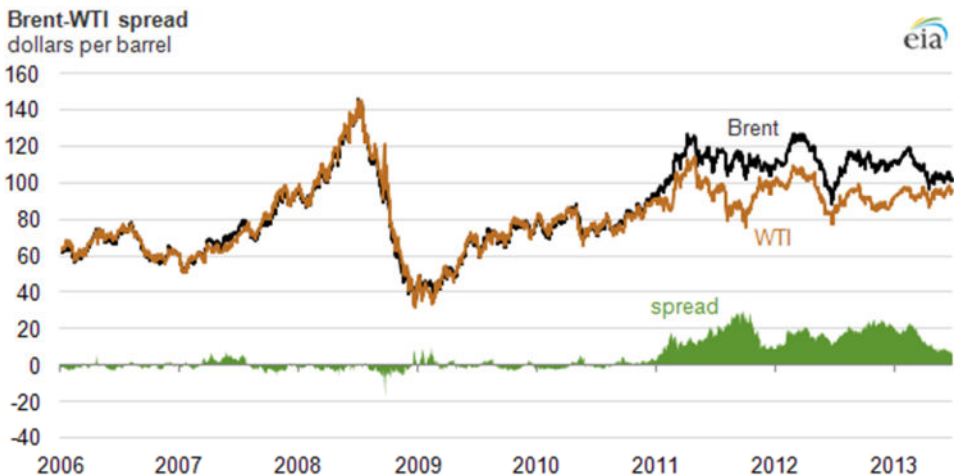
Since June 2014, crude oil prices have plunged 30 percent, causing alarm among the OPEC member states (Zhou 2014). The OPEC members met on Thanksgiving Day of 2014 to analyze the state of the oil market, which has been suffering from what some are calling a “global oil glut” due to soaring production in the United States and lackluster demand from struggling economies around the world. The announcement that followed the meeting stated that OPEC would maintain oil production at 30 million barrels per day (Hirst 2014) – despite the objections of desperate members such as Venezuela that wanted a production cut in order to increase prices. This automatically caused the price of oil to spiral into a terrific plunge. During that Thanksgiving Day meeting in Vienna, the oil ministers from OPEC members agreed to live with the effects of the U.S. “fracking” boom and let the markets sort it out (Cooke 2014). They believed that if the OPEC cuts output to raise the price of oil, it would lose market share. The way to win this energy war was to allow overproduction to depress prices to the point where cheap OPEC oil could destroy the profitability of North American producers and force the United States to cut production. Had OPEC maintained prices at \$40 or \$50 a barrel, “fracking” would not have become so widespread in the United States. This time, OPEC is changing this traditional “modus operandi” by trying to depress oil prices to fight a shale gas revolution that is threatening to make the OPEC irrelevant.

The case of the OPEC member Venezuela is particularly significant (Dielh 2014). The drop in the price of oil is having a dangerous impact on the economy of the country. On November 18, 2014 President Nicolas Maduro ordered \$4 billion in loan proceeds from China to be transferred from an off-budget fund to one counted in the country's international reserves. However, Venezuela had burned through one third of the Chinese money in one week (Kurmanaev 2014). If the prices do not rise in the short term, the country is heading for default.

## The Business Cycle and the Price of Crude Oil in the United States and Eurozone: FTAA Impact

In the international petroleum industry, crude oil products are traded on various oil bourses based on (1) established chemical profiles, (2) delivery locations, and (3) financial terms.<sup>2</sup> The three most quoted oil products are North America's West Texas Intermediate crude (WTI), North Sea Brent Crude, and the UAE Dubai Crude.

There are 46 oil exporting countries but the prices of these three oil products are used as a barometer for the entire petroleum industry. Historically, all three have traded closely but Brent Crude is typically priced at about \$2 over the WTI Spot price, which is typically priced \$5 to \$6 above the OPEC Basket prices as shown in the graph below.



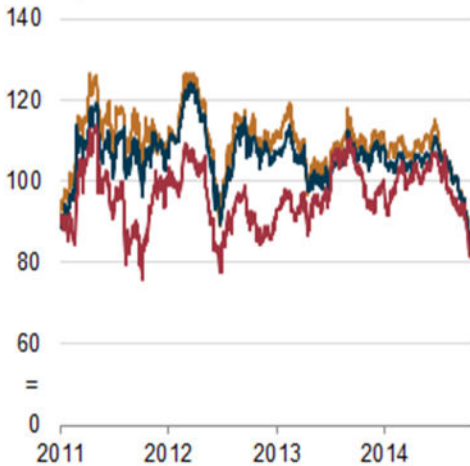
Source: U.S. Energy Information Administration, “Price difference between Brent and WTI crude oil narrowing,” June 28, 2013. <http://www.eia.gov/todayinenergy/detail.cfm?id=11891>

The following graph, with more details on the evolution of spot prices for WTI, Brent and Dubai/Oman, shows how the price of each company has dropped significantly while the spread has almost disappeared, both anomalies in this market.

<sup>2</sup> For a detailed guide on the many different types of crude oil visit [www.Oilprice.com](http://www.Oilprice.com), accessed at: <http://oilprice.com/Energy/Crude-Oil/A-Detailed-Guide-on-the-Many-Different-Types-of-Crude-Oil.html>

### Spot prices for select benchmark crude oils

dollars per barrel



West Texas Intermediate (WTI) Cushing  
Brent  
Dubai/Oman

Source: U.S. Energy Information Administration, “Benchmarks play an important role in pricing crude oil.” October 28, 2014 [.http://www.eia.gov/todayinenergy/de tail.cfm?id=18571](http://www.eia.gov/todayinenergy/detail.cfm?id=18571)

West Texas Intermediate (WTI) or Texas light sweet is a grade of crude oil used as a benchmark in oil pricing. Brent Crude is a major trading classification of sweet light crude oil that serves as a major benchmark price for purchases of oil worldwide. Brent Crude is extracted from the North Sea and comprises Brent Blend, Forties Blend, Oseberg and Ekofisk crudes.<sup>3</sup> Brent is the leading global price benchmark for Atlantic basin crude oils. It is used to price two thirds of the world's internationally traded crude oil supplies. The OPEC Reference Basket (ORB), also referred to as the OPEC Basket, is a weighted average of prices for petroleum blends produced by OPEC countries. It is used as an important benchmark for crude oil prices.<sup>4</sup> On 15 June 2005, the OPEC basket was changed to reflect the characteristics of the oil produced by OPEC members. The Reference Basket currently consists of a weighted average of the following blends of oil: Saharan Blend from Algeria, Ecuador, Iran Heavy from Islamic Republic of Iran, Basra Light from Iraq, Kuwait Export from Kuwait, Es Sider from Libya, Bonny Light from Nigeria, Qatar Marine from Qatar, Arab Light

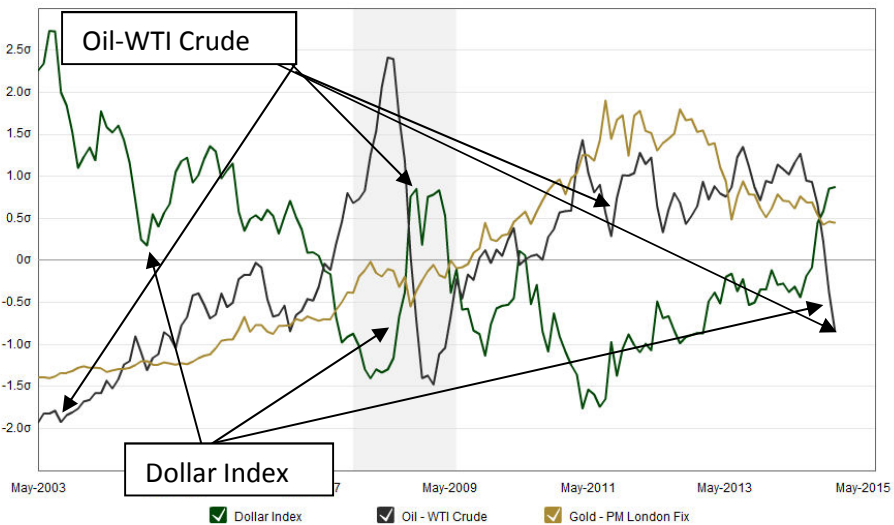
<sup>3</sup> Vantage Point. “Brent crude trading”, Trader Tech, accessed at <http://www.tradertech.com/trading/brent-crude>

<sup>4</sup> Organization of the Petroleum Exporting Countries. “OPEC basket price”, accessed at [http://www.opec.org/opec\\_web/en/data\\_graphs/40.htm](http://www.opec.org/opec_web/en/data_graphs/40.htm)

from Saudi Arabia, Murban from UAE, BCF 17 from Venezuela, Girassol from Angola.<sup>5</sup>

The barrel of oil is priced in U.S. dollars, which has a number of consequences. First, countries other than the United States have to engage in foreign exchange transactions to buy U.S. dollars to pay for oil. Second, oil producing countries receive billions of dollars every day, depending on the price per barrel and the value of the U.S. dollar. Thus, changes in the price of oil will be felt either on the producers' or on the buyers' side (Lorca-Susino 2008).

From 2001 to the summer of 2011, the price of oil was extraordinarily high, and the value of the U.S. dollar against major currencies was very low. More specifically, during this period of time, the U.S. dollar depreciated against the euro while the price of energy was on the rise. In summary, the U.S. dollar Index has been depreciating significantly while the price of oil has been increasing, as shown in the following graph.



Source: Macrotrends, “Dollar, Gold and Oil Chart - Last Ten Years,” accessed at <http://www.macrotrends.net/1335/dollar-gold-and-oil-chart-last-ten-years>

On the buyers' side, this depreciation of the U.S. dollar helped pay the oil bill in countries of the Eurozone, the United Kingdom and even China. On the oil producers' side, the effect of a cheap U.S. dollar and a high price of crude oil had a “bipolar” reading. First, oil producing countries have been receiving billions of dollars every day. Second, since the value of the dollars they have been receiving

<sup>5</sup> Organization of the Petroleum Exporting Countries. “Member countries”, accessed at [http://www.opec.org/opec\\_web/en/about\\_us/25.htm](http://www.opec.org/opec_web/en/about_us/25.htm)

had decreased against major currencies, those dollars could buy them fewer goods and services; that is, the purchasing power of oil producing and exporting countries decreased. Moreover, since most of the producing countries have their currencies pegged to the U.S. dollar, the weakness of the U.S. currency also drove down the value of their own currencies.

This depreciation of the U.S. dollar was at first regarded as a strategic move by the United States to gain export share and reactivate its economy (Lorca-Susino 2008). However, with respect to the price of oil, the low dollar was not an advantage because some oil producing and exporting countries were considering the possibility of pricing their barrels in currency other than U.S. dollars (Associated Press 2007). The sagging dollars also put special pressure on oil producing countries with dollar pegs such as Kuwait, which abandoned the dollar peg. The United Arab Emirates and Saudi Arabia considered substituting this fixed exchange rate policy for a basket of currencies with a heavy weight on the euro. As a result, the United States lost some of its economic and political influence in a very important area of the world.

### **Understanding the Price of Gas: A Quick Overview**

Understanding how the price of a barrel with 42 gallons of oil translates into the price of gasoline at the pump is not an easy task. On January 5, 2015 the price of the barrel of WTI oil fell below US\$50 and the price of gasoline at U.S. pumps hovered around US\$2.20 per gallon.<sup>6</sup>

In fact, nowadays, more and more scholars and politicians are trying to increase the transparency of the oil pricing mechanism, which previously was understood only by financiers. Unfortunately, governments — particularly in European countries — do not seem to realize the real impact of all the taxes on the prices paid at the pump and instead blame “speculators” and their contracts in oil futures markets as decisive factors in driving oil prices.

According to the Energy Information Administration, between 2000 and 2013 the average retail price for a gallon of gasoline in the United States was US\$2.45 and in 2013 the average price was US\$3.51<sup>7</sup>. The table below shows the different costs that contribute to the final price of gasoline at the pump. It is interesting to note how the increase in the price of oil is reflected in the percentage labeled “crude oil” with an increase of 12 percentages points from 56 percent to 68 percent. Furthermore, it seems that in order to balance out the increase in the

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<sup>6</sup> Buchele, Mose. 2015. “How crude oil prices drive the cost of gasoline”, State Impact, 26 January 2015, accessed at: <http://stateimpact.npr.org/texas/2015/01/26/oil-explained-what-is-brent-and-wti/>

<sup>7</sup> Energy Information Administration. “A primer on gasoline prices”, Energy Information Administration Prices, accessed at: [http://www.eia.gov/energyexplained/index.cfm?page=gasoline\\_factors\\_affecting\\_prices](http://www.eia.gov/energyexplained/index.cfm?page=gasoline_factors_affecting_prices)

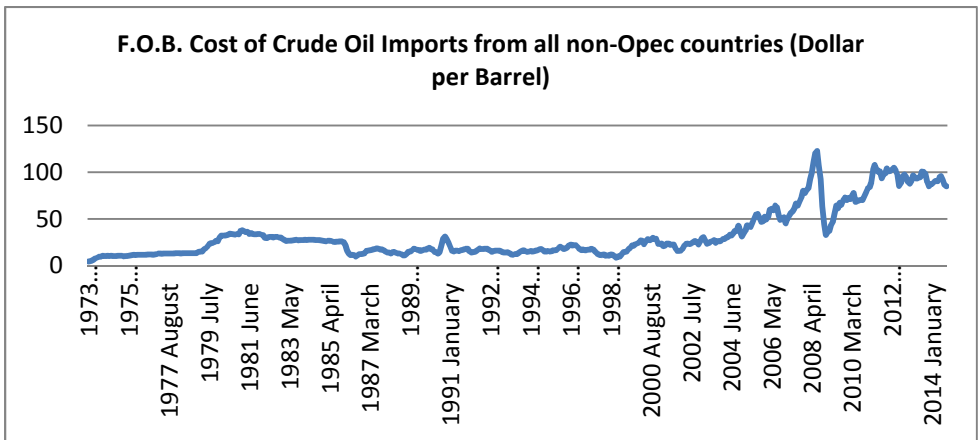


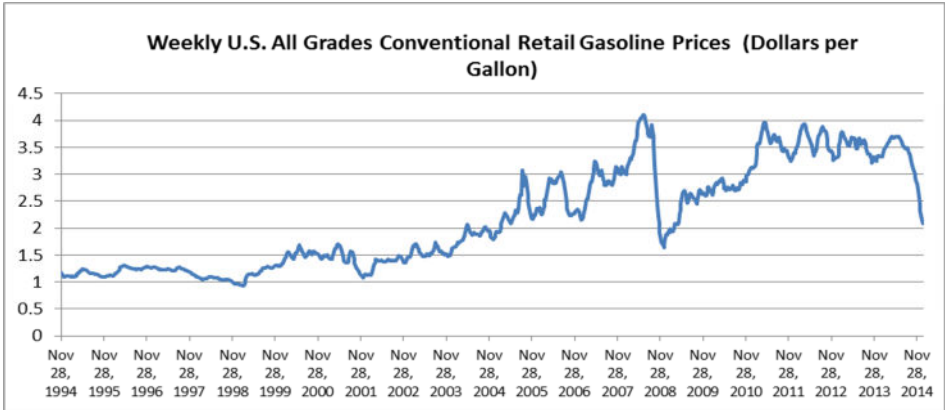
price of oil, federal and state taxes as well as the costs of distribution and marketing were reduced.

	2000 to 2012 Average Retail Price: \$2.45 Average barrel price:	2007 Average Retail Price: \$2.80 Average barrel price:
Distribution & Marketing	<b>11%</b>	<b>9%</b>
Refining Costs & Profits	<b>13%</b>	<b>11%</b>
Federal & State Taxes	<b>19%</b>	<b>12%</b>
Crude Oil	<b>56%</b>	<b>68%</b>

Source: Energy Information Administration. “A primer on Gasoline Prices.” Energy Information Administration Prices, access at: [http://www.eia.gov/energyexplained/index.cfm?page=gasoline\\_factors\\_affecting\\_prices](http://www.eia.gov/energyexplained/index.cfm?page=gasoline_factors_affecting_prices)

The two graphs that follow allow to compare and contrast the weekly evolution of the average price of all gasoline grades in the U.S. markets from November 28, 1994 until January 2015 — a period when the average price of gas was never below US\$1 per gallon — and the evolution of the average spot price for a barrel of crude oil from October 1973 until January 2015.





Source: The data was collected manually from the Energy Information Administration (<http://www.eia.doe.gov/>) and was recorded in excel to create the above graph.

In the European Union the price of oil is not only high but exorbitant. In the EU, the price of fuel at the pump is based on (1) government duty and tax, (2) the cost of petrol and diesel on the open market, and (3) the costs and profit of the wholesaler and retailer.<sup>8</sup>

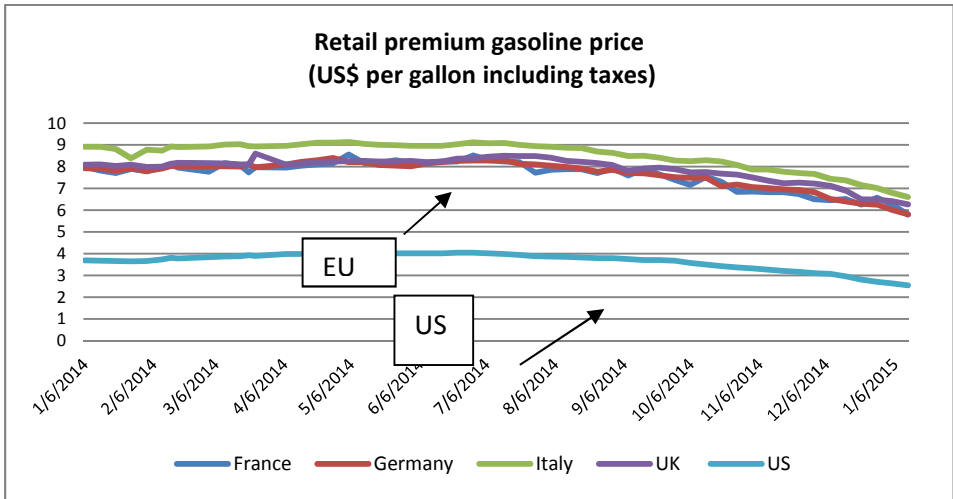
In March of 2014, the U.K.-based non-government organization *RAC Foundation* released a new report “European fuel prices,”<sup>9</sup> detailing the taxes and duties on the retail sale of petrol and diesel fuel in the countries of the EU. According to the report, the highest tax burdens on diesel fuel in the EU are found in Sweden, the UK, and the Netherlands. Motorists in those countries must face taxes and duties which make up 62 percent, 61 percent, and 61 percent of the retail price of fuel respectively. Correspondingly, the highest taxes on gasoline are found in the UK, Sweden and Italy, with respective rates of 59 percent, 56 percent, and 55 percent of the price at the pump. On the other hand, the lowest tax burdens on the retail sale of fuel are found in Luxembourg and Bulgaria. In these two countries taxes account for “only” 48 percent and 45 percent of petrol and 41 percent and 42 percent on diesel fuel – the lowest rates in Europe. Curiously, the price of fuels in the UK remains one of the highest in the EU despite the fact that the pre-sale cost of fuel in the UK is one of the lowest in the region.

The following graph compares the evolution of the price of gasoline in key EU countries and the United States. This graph shows that the price of gasoline is extremely high in the European continent and that Europeans pay much

<sup>8</sup> RAC Foundation. “Taxation as percentage of pump price”, accessed at: <http://www.racfoundation.org/data/taxation-as-percentage-of-pump-price-data-page>

<sup>9</sup> RAC Foundation. “European fuel prices”, accessed at: <http://www.racfoundation.org/media-centre/euro-fuel-prices>,

more than U.S. residents when it comes to domestic fuel prices. The reason for such pronounced difference is that there are massive taxes levied on fuel by the governments in Europe. In the United States, only 10 percent of what the end-user pays at the pump goes to the government, while in Europe, this rate is roughly 70 percent.



Source: U.S. Energy Information Administration, “Retail Premium Gasoline Prices, Selected Countries (US dollars per gallon, including taxes). <http://www.eia.gov/countries/>

### Price of Gasoline and its Impact on Economic Growth: What Can Be Expected?

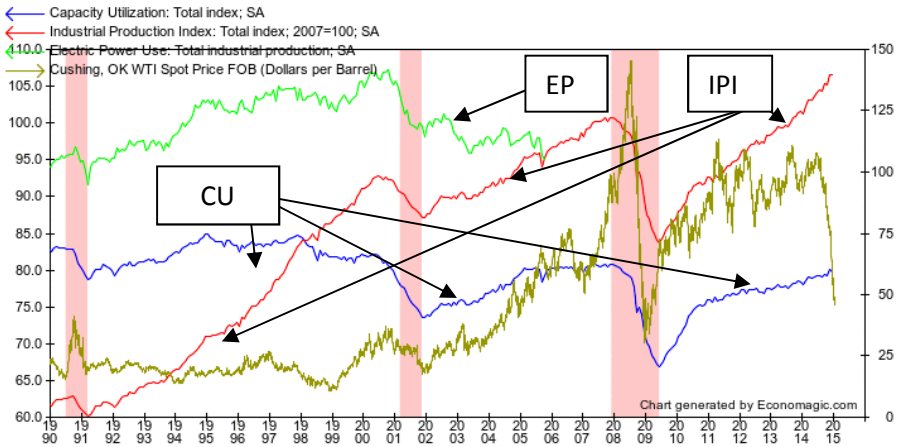
Energy prices can have powerful and deep impact on a country's economy. First, energy prices affect the final price of most goods and services due to transport, electricity, and fuel costs. Thus, if these rise faster than wages, consumers have less available income. This in turn will have a deep impact on consumer confidence and will result in less consumer spending and business hiring.

While the United States has recovered more strongly from the 2008 crisis than Europe that is still on a longer slump the U.S. economic recovery remains relatively weak. Even though stock prices have reached all-time highs, unemployment is still weak and capacity utilization is still below its 2008 level. The Federal Reserve Board constructs estimates of capacity utilization for industries in manufacturing, mining, electric and gas utilities.<sup>10</sup> For a given industry, the capacity utilization rate is equal to an output index (seasonally adjusted) divided

<sup>10</sup> Federal Reserve Board. “Industrial Capacity and Capacity Utilization”, accessed at: <http://www.federalreserve.gov/releases/g17/current/default.htm>

by a capacity index. This indicator is displayed as a percentage that points to the overall slack in the economy or a company at a given point in time. If a company is running at a 70 percent capacity utilization rate, it has room to increase production up to a 100 percent utilization rate without incurring the expensive costs of building a new plant or facility. Industrial production figures are based on the monthly raw volume of goods produced by industrial firms. The industrial production and related capacity utilization figures are considered coincident indicators because changes in the levels of these indicators usually reflect similar changes in overall economic activity that affect gross domestic product (GDP). The Federal Reserve watches industrial production very closely because it believes that inflation shows itself first at the industrial level, particularly when supplies of basic materials get tight and the increases in the cost of commodities and materials will be passed on down the line, ending up with individual consumers of higher-cost finished products.

It is particularly striking to see how during the recession, when the price of WTI reached an all-time high of close to US\$140 per barrel, both industrial production and capacity utilization suffered a significant drop. Since 2014, the price of WTI is suffering a significant drop and both indexes are reaching significant highs.

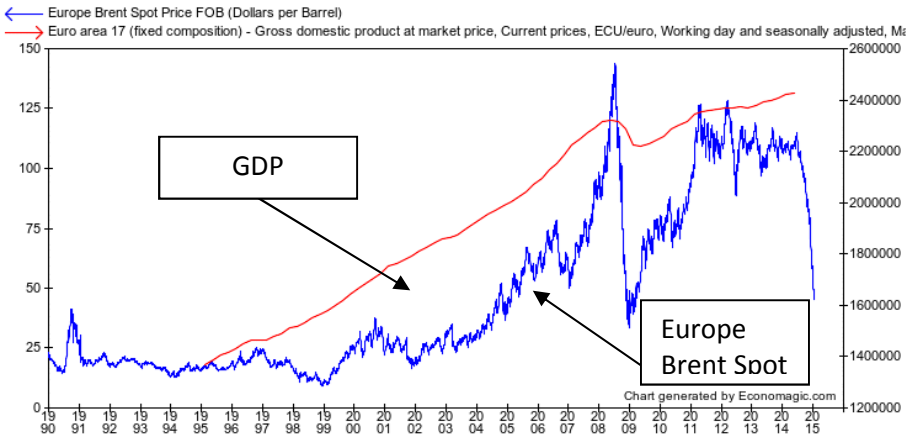
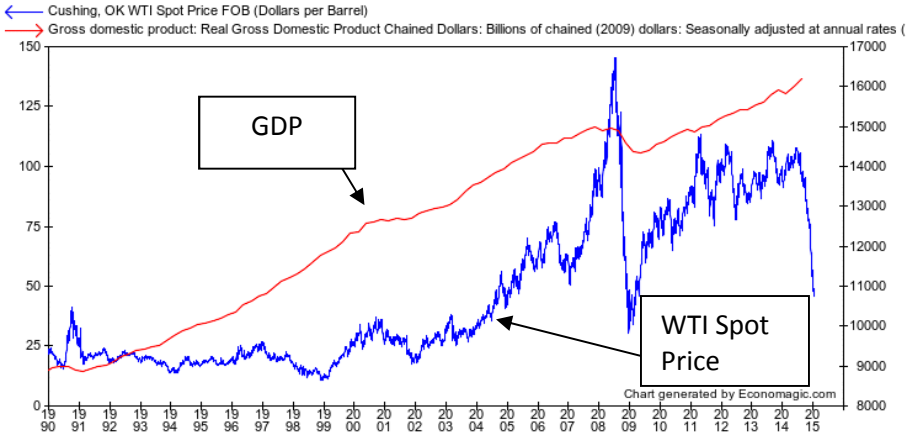


Source: Economagic, [www.economagic.com](http://www.economagic.com)

Falling gasoline prices are a favorable tailwind for the U.S. Economy. But the gasoline prices reduction has not been completely felt in the European Union where consumers have to pay higher prices than in the United States. Thus, this will be a headwind for the recovery of the block and it will create a comparative disadvantage for the EU.

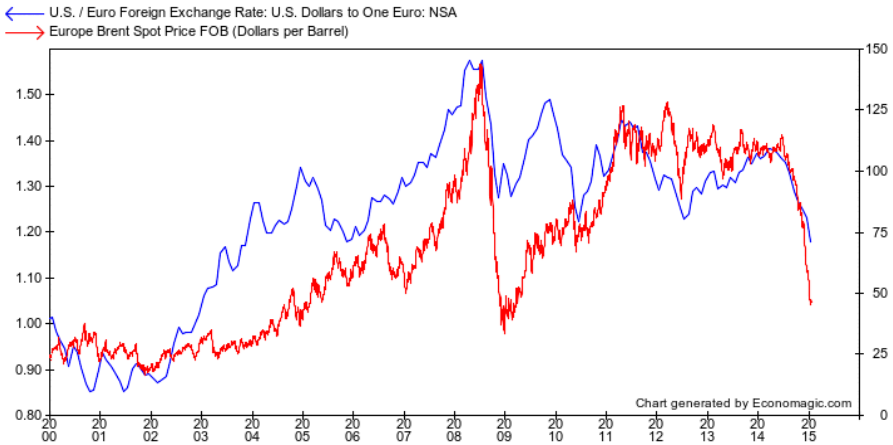
For instance, the following graph shows that in the United States the price of WTI and GDP are inversely correlated. In fact, since 2014, GDP in the

United States has been increasing significantly while the price of WTI has been suffering a major decrease. However, the graph does not reflect such a significant improvement in the Eurozone.



Source: Economagic. [www.economagic.com](http://www.economagic.com)

If the Eurozone cannot take advantage of oil and gasoline price drop, which is extremely important for the economic growth of the block, its economic future will be very dubious, particularly because the price of the euro is not going to make it easy to pay the bill. The following graph shows that the price of WTI is going down along with the price of the euro.



Source: Economagic. [www.economagic.com](http://www.economagic.com)

## Final Remarks

The U.S. increased sharply its oil production due to its desire to obtain energy independence. Back in 2005, the U.S. imported almost 60 percent of its oil needs from abroad while in 2014, it only needed 30 percent. This means that there is clearly an oversupply which is causing the prices to drop. Tumbling oil prices have led investors to lower its pricing assumptions for the two benchmark crude oils, European Brent and West Texas Intermediate (WTI). This will affect numerous industries around the world, and will have an effect on the business cycle on both sides of the Atlantic. Industries for which fuel is a direct and significant cost will see a positive effect from a decrease in the price of oil, as will consumer-dependent businesses in general because lower gasoline prices mean consumers will have more available income to spend on other goods and services. However, oil and gas exploration and production companies and their affiliates will be badly hurt by lower crude prices. The demand for oil is not very strong. There are two main reasons for that. On the one hand, a strong dollar is making a lot more expensive to pay the cost of oil. This is a challenge for countries that buy outside the U.S. since a weaker domestic currency to a strong dollar will weaken demand and put downward pressure on falling oil prices. Of particular interest is the case of the Eurozone for two reasons. First, most of the countries of the euro area are still facing the challenges of the economic recession. Second, the Eurozone is facing a significant drop in the price of the euro which makes oil prices more expensive. Therefore, the Transatlantic Trade and Investment Partnership will be heavily affected by the future changes in the price of this commodity.

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# The TTIP from a German Perspective: Economic Interests and Political Discourse

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## Abstract

As Europe's largest export nation, Germany has strong economic interests in the proposed Transatlantic Trade and Investment Partnership (TTIP), the free trade agreement currently being negotiated between the European Union and the United States. While its economic performance regarding foreign trade should make Germany one of the driving forces in the TTIP negotiations, the current political discourse has, however, been dominated by critics of the initiative, who fear that a trade contract with the United States would significantly lower German standards mainly in regards to food security, environmental protection and workers' rights. This paper aims to analyze these diverging influences on the German position in the TTIP negotiations and the overall effects on a potential agreement.

## The Context of Recent Efforts for Transatlantic Economic Integration

On February 13, 2013, the heads of the European Union, European Council President Herman Van Rompuy and European Commission President José Manuel Barroso, announced in a joint communiqué with U.S. President Barack Obama the launch of bilateral negotiations on a Transatlantic Trade and Investment Partnership (TTIP) (European Commission 2013b).

The TTIP is considered the most ambitious trade agreement in history for several reasons: it is being negotiated between the world's two biggest economies, which, at the same time, are each other's most important economic partners. If concluded, TTIP would represent the largest free trade area (FTA) in terms of GDP, FDI stock and also by population. Considering the scope of current negotiations, TTIP would go far beyond the reduction of conventional trade barriers and instead include regulatory issues, so-called *behind-the-border obstacles*, which go far beyond standards in current trade agreements (Akhtar and Jones 2013: 111ff.).

On the European side, due to its outstanding performance in international trade, Germany has long been a driving force in the pursuit of transatlantic economic integration. In the mid-1990s, Germany's then Foreign Minister Klaus Kinkel proposed a *Transatlantic Market Place*. Yet, the proposal failed to formalize in the context of post-NAFTA debates in the United States and a focus on the creation of a Monetary Union by major EU member countries, particularly France (Braml and Schmucker 2007: 100; Falke 2014: 435).

During 2006/2007, German Chancellor Angela Merkel made transatlantic trade a central issue of Germany's EU presidency and started pushing for a Transatlantic Free Trade Agreement (TAFTA). This time, however, France openly opposed such an agreement and the U.S. showed little interest in a "Merkel Initiative" since bilateral relations had cooled down over diplomatic differences on the war in Iraq (Bram and Schmucker 2007: 101; Schmucker and Mildner 2013).

Yet, some twenty years after Germany's first push for a transatlantic FTA, the economic crises in the United States and Europe and the stalemate of the WTO Doha Development Round have created a favorable political environment for reviving the project. Both, the U.S. government and the European Commission had been looking for growth measures beyond fiscal and monetary policy (Falke 2014: 436). At the same time, they needed to find an alternative way to the multilateral trade agenda, which is stalled due to unbridgeable differences between the positions of industrial nations and certain emerging market economies.

In this context, this paper will analyze the German stance in this new initiative. After an overview of the scope and content of TTIP, potential gains for the German economy will be highlighted. This is followed by an analysis of critical issues that have heated the public discussion on TTIP. Lastly, this paper will investigate how the diverging interests have been influencing the position of the German government.

## **The Content of TTIP Negotiations: Making Trade Rules for the 21<sup>st</sup> Century**

The content of current TTIP negotiations has been based on the recommendations of the so-called *High-Level Working Group (HLWG)*, a joint committee set up by the *Transatlantic Economic Council*. In its final statement in February 2013, the HLWG suggested that the U.S. and the EU should pursue a trade agreement which not only targets conventional trade barriers, but also tackles non-tariff barriers (NTBs) and sets new rules for global economic regulation (HLWG 2013).

The TTIP negotiations were officially launched on July 8, 2013 and are organized in three pillars: the first pillar covers issues connected to market access and therefore deals with conventional trade barriers as well as government procurement (HLWG 2013: 2). Since tariffs and tariff rate quotas (TRQs) are already very low in the EU and the U.S., negotiations in this area will mainly focus on tariff peaks<sup>1</sup> (Fretag et al. 2014: 9).

The second pillar, dubbed "Regulatory Issues and Non-Tariff-Barriers," targets primarily behind-the-border obstacles and aims at the alignment of na-

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<sup>1</sup> These are mainly recorded for agricultural products, beverages, textiles, and for cars (in the EU) and small trucks (in the U.S.).

tional regulation and standards (HLWG 2013: 3). This area is considered to deliver most of the economic gains. At the same time, it is controversial due to its impact on national laws and preferences (Schmucker 2014: 22).

The third pillar on “Rules” addresses topics which so far have not been covered under WTO regulation or need to be modernized. Among these issues are rules for subsidies, for privileges granted to state-owned enterprises, local content requirements, as well as provisions on labor and environmental standards (Falke 2014: 434; HLWG 2013: 5f.).

The transatlantic partners have here clear purpose of modernizing current international trade rules. Rather than maintaining the ones in former trade agreements which dealt with negotiating preferential market access for so-called “club goods.” The TTIP and the other Mega Regionals currently under negotiation are focusing on facilitating production processes for global value chains.

At the same time, the proposed negotiation structure shows that the TTIP is laid out to be far more than an economic project. Especially the third negotiation pillar on rules targets measures undertaken by the BIC countries (Brazil, India, China), which the EU and the U.S. have identified as trade distorting, but were not able to curb on the multilateral level due to opposition from these new central actors. In times where economic growth mainly occurs in the new mega markets, the TTIP offers a first mover advantage in setting global economic standards for the two traditional economic powerhouses and places them ahead of the new powers in the race for global economic supremacy (Novy 2014; Schmucker 2014: 20).

## **Potential Benefits for the German Economy**

While the geopolitical dimension adds a new standard for the negotiation of preferential trade agreements, the TTIP’s proposed economic effects alone are enough to define this initiative as exceptional. The transatlantic economy accounts for over 40 percent of global GDP (PPP) as well as for percent of global exports and 30 percent of global imports (Hamilton and Quinlan 2014: 20). In addition, the EU and the U.S. are among each other’s most important trading partners. While the U.S. received the biggest share of EU exports (17 percent) in 2011, the EU absorbed 19% of U.S. exports, which is a second rank after Canada (Francois et al. 2013: 8).

The interdependence of the world’s two biggest economies is further shown when looking at foreign direct investment (FDI). In terms of inward FDI, the transatlantic economy accounts for 55percent of global stock. For outward FDI the combined shares account for almost 70percent. Since 2010, the EU was able to attract 56 percent of total U.S. outward FDI. The U.S., conversely, received 71 percent of EU outward FDI in the year 2012 alone (Hamilton and Quinlan 2014: 9f., 20). FDI is particularly important in the context of global val-

ue chains, since foreign investment is the basis for the establishment of production networks (Felbermayr and Aichele 2014: 2).

Germany plays a central role in this relationship, not least because of the high degree of openness of the German economy.<sup>2</sup> In 2013, exports accounted for 50.6 percent of GDP (BMWi 2014). In 2012, 12 million jobs were supported by exports, which equaled almost one third of total employment (Felbermayr and Aichele 2014: 1). In 2013, the U.S. was ranked Germany's second largest export destination (8.1percent) just behind other EU member states (BMWi 2014). Reversely, Germany was the fifth largest export market for the U.S. (RGIT 2014: 1). What is striking is the fact that more than 50 percent of bilateral trade flows have inter-firm character (White House 2011).

On the investment side, Germany was the seventh largest foreign investor in the U.S. in 2013, supporting about 11percent of insourced jobs. The U.S. was the largest non-European investor in Germany in 2013 with U.S. majority-owned companies accounting for 632,000 German jobs (RGIT 2014: 1f.).

The importance of economic relations with the U.S. combined with Germany's high degree of export-orientation implies significant benefits that the TTIP could accrue to Europe's biggest economy. While experts agree that the TTIP will overall have positive effects, the exact amount of economic gains is at the moment hard to quantify since they depend on the models used for calculation, underlying assumptions as well as respective liberalization scenarios.

For Germany, Felbermayr and Aichele (2014: 15ff.) suggest that trade with the United States would significantly increase under an ambitious<sup>3</sup> TTIP agreement, particularly German gross exports to the American market. They expect the strongest gains for classic German strongholds such as the chemicals, transport equipment, and machinery sectors. Yet, foreign trade with European partners would decrease due to trade diversion. The highest gains should come from the reduction of NTBs and the harmonization of standards, which would particularly benefit German small and medium-sized enterprises (SMEs) (Felbermayr et al 2013a: 4).

Looking at overall GDP growth, however, available studies portray a more modest scenario. Felbermayr and Aichele (2014: 19) estimate German welfare gains in a range between 0.0 percent and 0.28 percent from potential tariff reductions under the TTIP. For the EU as a whole, the European Commission (2013a: 32-37) estimates the gains from an ambitious agreement with a GDP increase of 0.58 percent until 2027. Estimates for the U.S. are at 0.39 percent for the same timeframe.

The same is true when looking at job creation. Felbermayr et al. (2013b: 34-39) estimate that the unemployment rate in Germany would decrease by 0.47

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<sup>2</sup> With an overall degree of openness at 95 percent (2013), Germany is the most open economy among the G7 countries.

<sup>3</sup> This includes the reduction of tariffs and NTBs as well as the facilitation of FDI and better access to government procurement markets.

percent under an ambitious agreement. Real wages would increase by 2.19 percent. While this is within the European average, other countries, especially the U.S., Great Britain and the Scandinavian countries would benefit far more in this regard.

### **Sticking Points in the German TTIP Debate**

Due to the high level of export-orientation of the German economy, free trade initiatives have in the past created a broad pro-trade coalition consisting of not only politicians and business representatives, but also the general public. The TTIP, too, was initially greeted by German stakeholders and because of the country's central role in pushing for transatlantic economic integration, most observers expected Germany to lead the way in the negotiation process. While some controversies in regards to genetically modified organisms (GMO) and environmental issues were anticipated, many thought the German position would help to move along troubleshooters like France (Sparding 2014: 1f.).

These predictions were, however, proven wrong. While a survey conducted by the Pew Research Center in cooperation with the Bertelsmann Foundation in April 2014 showed that 55 percent of Germans consider the TTIP to be overall positive for their country (Pew and Bertelsmann 2014: 5). Thus, some sticking points have emerged that have the potential to become deal breakers. The debate centers mainly on the proposed alignment of standards, a potential investor state dispute settlement (ISDS) mechanism, as well as a suggested lack of transparency in the negotiation process. While societal groups are the major critics of these issues, the discussion goes far beyond the anti-globalization movement (Novy 2014; Sparding 2014: 1).

But why is this debate emerging at a time when the European Commission has just finished negotiating a trade agreement with Canada, the Comprehensive Economic and Trade Agreement (CETA), which already includes many of these controversial issues? For the majority of controversial topics, discussions are rooted deeply in different perceptions of the role of state, the functioning of the legal system, or the general conception of risk (Felbermayr and Aichele 2013: 22). Several studies<sup>4</sup> have laid out that the German public shows a high level of distrust in the American system and the United States per se. Particularly in what regards food security and quality, environmental safety, labor rights, consumer protection and even technical norms, Germans view American standards as inferior to not only German but European standards in general (Sparding 2014: 3).

Contrary to the U.S., where regulation is a consequence of scientifically proven risk, the German philosophy on regulation is based on the so called *Precautionary Principle*. For the agricultural negotiations of the TTIP, it was expected that this would give the European Commission almost no discretion on

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<sup>4</sup> E.g. the PEW/Bertelsmann study.

critical issues like hormone beef and chlorinated chicken. Yet, Germany's consumers seem to fear a downward spiral in other health and safety issues related to the regulation of toxic chemicals and medication (Falke and Felber 2014: 30). This is also true for technical and environmental standards. Only 10 percent consider American car safety standards as equal, only percent support an alignment of environmental standards (Pewa and Bertelsmann 2014: 14f.).

A similar picture is emerging when looking at social standards and workers' rights. The highly influential German Trade Union Federation (DGB 2014: 1ff.) for example, has indicated general support for the TTIP in case it was used to set new standards for a "fairer globalization." Yet, it expresses concerns that German labor standards could be lowered under the TTIP since the United States have only ratified two out of the eight core labor standards of the International Labor Organization (ILO). The debate is driven by several cases in which state governments in the U.S. have used political pressure to prevent the creation of workers' councils or unions in subsidiaries of German companies (Inside US Trade 2014b). The latter incidents have drawn a high degree of public attention in Germany and have also reinforced fears that German companies would increasingly transfer production jobs to the United States.

An issue that is seen just as critical as new trade regulation and the alignment of standards is the proposed ISDS mechanism. ISDS protects foreign investors' rights in granting them the option to bring claims against a host country before an independent arbitral tribunal.

While Germany has been one of the strongest advocates of bilateral investment treaties (BIT),<sup>5</sup> ISDS had never before emerged as a controversial topic. Yet, the two recent international claims of Swedish energy provider Vatenfall against German environmental legislation connected to the "Energiewende" have raised concerns that an ISDS chapter in the TTIP could lead to a flood of claims from American investors against similar legislation. For decades, the latter have earned a reputation as greedy "locusts" employing fleets of scrupulous lawyers, which are able to lever out democratic processes (Sparding 2014: 3, 7). The discussion on ISDS has reached such a degree that it has now spilled over on CETA.

Yet, it is not only the distrust in the U.S. and its system that is driving the opposition to the TTIP in Germany. In recent years, the country has shown an increasing degree of Euro-skepticism. A majority of Germans doubts that the European Commission is negotiating in Germany's best interest.<sup>6</sup> They consider the

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<sup>5</sup> Germany was the first country to sign a BIT (in 1959 with Pakistan) and has since negotiated over 130.

<sup>6</sup> Since the implementation of the *Lisbon Treaty* in 2009, trade policy making, including FDI and *intellectual property rights (IPR)*, is under exclusive EU competence (ToL Art. 207). Negotiations are conducted by the Commission, but the European Parliament enjoys far-reaching rights of co-determination since every trade deal needs parliamentary approval. While the Commission has to frequently coordinate with the national

Commission's negotiation style as in-transparent and undemocratic. Also, business lobbyists are perceived to receive preferential access over representatives of consumer, social and environmental interests (Sparding 2014: 7). Accordingly, 65 percent of Germans declare that negotiations should be conducted by the German government (Pew and Bertelsmann 2014: 17f.).

### **The German Government's Position on the TTIP Controversies: Sit out, Tackle or Retreat?**

The current German government, a coalition of Angela Merkel's Christian Democratic Party (CDU) and the Social Democratic Party (SPD), has manifested its support for the TTIP in the coalition agreement signed in November 2013. The agreement (Bundesregierung 2013: 15f.,168) outlines Germany's commitment to the principles of free and fair trade and its aim for a conclusion of the WTO Doha Development Round, TTIP, and other trade agreements. While acknowledging the need for the alignment of existing regulation through the TTIP, the agreement, however, also calls for maintaining the current European levels of health, environmental, social, consumer and data protection standards as well as an inclusion of all ILO core labor standards in EU-FTAs.

The text clearly shows the diverging political focuses of the coalition parties, with the CDU being considered the voice of Germany's industry and the SPD representing unions and civil society groups. But while the Christian Democrats are the senior partner in this so-called Grand Coalition, it has been the SPD that has dominated Berlin's position taking on the TTIP following the aforementioned public outcry. One of the loudest voices criticizing the TTIP has been Economics Minister Sigmar Gabriel. In line with demands from labor unions and trade critics within his party, he called for an exclusion of ISDS in both, TTIP and CETA, and even threatened to block the ratification of the latter otherwise (ICTSD 2014: 14f.).

The main proponents of the TTIP, the business wing of the CDU, on the other hand, remained silent since the revelations of the NSA spying scandal that further eroded public trust in the U.S. and, therefore, made supporting German-U.S. relations politically difficult. While Chancellor Angela Merkel and her CDU-ministers were rather careful to underscore the government's continued support for the TTIP, they have avoided dissenting from the position of their coalition partner. Moreover, the CDU has come under pressure from its own constituencies. In addition to the powerful but defensive farm lobby, representatives of German SMEs have spoken out against ISDS, claiming that the assessment of this mechanism is too costly for their businesses and therefore gives big corporations an advantage.

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governments of member states, national parliaments only get involved when mixed agreements are negotiated.



Yet, the German government seemingly has not given up on the initiative. In order to enhance the dialogue with civil society representatives, a TTIP council was created within the Economics Ministry (Sparding 2014: 6, 11). In addition, trade proponents within the Cabinet were able to change the position of Sigmar Gabriel and other critics who are now in favor of an inclusion of ISDS chapters in both the TTIP and the CETA, albeit only in the case of wide-ranging reforms to the current *modus operandi* (ICTSD 2014: 14).

In the wake of this political development, the European Commission, too, has reacted. In March 2014 the Commission temporarily suspended ISDS negotiations and initiated a public consultation process, which drew nearly 150,000 replies. The proposed reforms are currently under review. However, a final decision is not to be expected until late in the negotiation process. In addition, the negotiation instructions given to the European Commission by EU member governments were made public in October 2014 (ICTSD 2015: 4f.).

## **Conclusion**

Due to its general pro-trade standing and a history of pushing for transatlantic economic integration, Germany was expected to take a lead in the TTIP negotiations. While proponents of this mega regional agreement have been extolling the potential gains for the export-dependent German economy, public resentments, which are rooted in a deep distrust towards the United States and its economic system, have taken over the political discourse.

The outcry against the TTIP reached such a degree that Berlin was forced to slow down the negotiation process and to develop an alternative strategy, which included calls for a more transparent negotiation style on part of the European Commission and a drastic modification or even exclusion of the proposed ISDS mechanism.

Both trade supporters in the German government as well as the European Commission have recently taken steps to ease this debate. The creation of specific advisory groups on the national and EU level which are aiming at better involving public interests are steps in the right direction. The same is true for the European Commission's public consultation process on ISDS.

Yet, given Germany's weight in Europe, policymakers and negotiators should consider to go even further beyond conventional trade negotiation approaches in order to save the TTIP in the ambitious form it is currently being negotiated. Neither Germany, nor the EU or the U.S. could risk losing first-mover advantages in setting global trade standards to third countries and should, therefore, address key concerns more extensively.

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## **I. Beyond Economics**



# **TTIP: A Mega-Free Trade Agreement Lost in Translation?**

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## **Abstract**

The Transatlantic Trade and Investment Partnership (TTIP), initiated in July 2013, has become a sluggish and complex series of negotiation between the EU and the US. At first this massive bilateral trade agreement was expected to be quickly completed and agreed. The TTIP consists in removing trade barriers in a wide range of economic sectors as well as harmonizing some rules, technical regulation, standards, and approval procedures. According to the European Commission, the TTIP is projected to boost the EU's economy by €120 billion; the US economy by €90 billion; and the rest of the world by €100 billion. Almost two years in, the negotiations on the TTIP are facing serious criticisms inside Europe. The TTIP has provided the arguments to anti-globalization movements, fear of decline of democratic foundations, declining national sovereignty, as well as destruction of national/regional identities and cultures. Nevertheless, based on polls produced by Eurobarometer, a majority of European citizens are in favor of the TTIP at the exception of Austria clearly disapproving. The TTIP is seen as a way to re-launch the transatlantic economy, but mainly European economies stagnated since the financial crisis. The TTIP is as well a response to the other trade agreements, like the Trans-Pacific Partnership (TPP), and the rise of Asian economies. This paper seeks to reflect on two dimensions: the projected benefits of the TTIP for the EU and the debate and perceptions within the EU about the TTIP.

## **Introduction**

The European political elite, as well as the American President and a segment of the United States legislature seem committed to finalize the negotiations on the Transatlantic Trade and Investment Partnership (TTIP) in 2015. The transatlantic decision to launch negotiations for the implementation of the TTIP was initiated back in 2013. The Transatlantic Trade and Investment Partnership, currently under negotiations between the United States (U.S.) and the European Union (EU), is a massive Free Trade Agreement (FTA) with the purpose to create jobs and boost investments and trade on both sides of the pond.

The idea behind the TTIP falls under a global reading of power adjustment and shift in global influence of the Euro-Atlantic community. The 2008



financial crisis seriously affected the American and European economies and their overall global influence. The debate over the decline of the US as the hegemon and ultimately of the future of the liberal order (Ikenberry 2011, Kupchan 2012) raised important questions about the ability of the U.S. to shape global politics as it did during the Bretton Woods period and the 1990s (Culbert 1987, Ikenberry 1992, Ruggie 1982).

In the case of the EU and its 28 economies, its influence has certainly declined since then due to the internal economic crises affecting most of its Member States. For such reason, the TTIP was framed as a mega-FTA re-launching the transatlantic economic engine. The U.S. and the EU are each other's largest commercial partners especially in services, trade and investments.

The TTIP seeks to advance three core components between the two sides of the Atlantic: first, to increase market access through the elimination of barriers to trade and investment in goods, services, and agriculture as well as the further opening of government procurement markets; second, to enhance regulatory coherence and cooperation; and third, to develop new rules in areas such as foreign direct investment, intellectual property rights, labor, the environment, and emerging '21st century' areas of trade (e.g., regulating data flows, trade facilitation in a supply chain environment, and the role of state-owned enterprises) (Akhtar and Jones 2014). An important dimension of the TTIP is that it is more than establishing the base for a FTA considering the already deep trade relations between the EU and the US, but rather to implement regulatory alignment between the EU and the U.S.. "The TTIP negotiations involve two parties with their own sets of entrenched and advanced regulatory structures" (Aggarwal and Evenett 2013: 553).

The TTIP is not solely about economics, but it is deeply political as well. In order to understand the complexity behind the long-lasting agreement on the TTIP, this chapter seeks to explain the link between the desire/commitment by the members of the Euro-Atlantic Community (U.S., EU, EU-28) and the lack of popular support in Europe. Has the TTIP been lost in translation? In order to analyze this question, the chapter is structured around two parts: the first one consists in looking at the TTIP in its generality as well as its global constraints; the second section looks at the European perceptions on the TTIP and their effects on the ongoing negotiation process.

## **Mega FTA or Economic NATO? A Fragmented Global Economy**

The TTIP is an illustration of a fragmented global economy and a complex global trading system (Aggarwal and Evenett 2013). As per Aggarwal and Evenett, the global economy is facing three challenges since the financial crises: the rise of protectionism; a continued interest in Free Trade Agreements (FTA); and, the decline of the World Trade Organization (WTO) since facing the difficult negoti-

ations of the Doha round illustrating the tensions between the North and the South (2013).

Considering the shifting global balance of power, the continuous Eurozone crisis and the sluggish look of European economies several EU Member States, like the governments in the United Kingdom, the Netherlands, and Germany, were favorable and have been driving the negotiations process. These Member States want to find a way to rejuvenate the European economic engine with a long-term vision and a clear search for competitiveness and strengthening their global positions.

For decades the academic debate has been closely looking at the question of Regional Trade Agreements (RTAs) versus multilateral trading system (Baghwati 1992, Manfield and Milner 1997). In the case of the TTIP, the question of re-boosting the transatlantic economy falls under the broad question of stumbling blocks or building blocks. “With the United States increasingly looking east toward Asia, and the EU increasingly turning inward, the threat of the transatlantic community being pulled apart is real. But trade negotiations would reinvigorate the transatlantic alliance” (Barker 2013). Will the TTIP be a positive agreement, if implemented, for the world and the emerging power? Or will it contribute to the widening of inequality gaps between the Global North, the Euro-Atlantic community, versus the rest?<sup>1</sup>

## A Transatlantic Economy

Historically, the U.S. and the EU have been competitors and partners in the field of trade. But with the shifting global order and the lingering economic slowdown of the European economies, the U.S. and the EU are working on implementing the TTIP in order to form “a large Euro-Atlantic market and high transatlantic standards to open other markets and form the core of global standards” (Hamilton 2014a: 27). The TTIP could be a new dimension of the transatlantic partnership. But Hamilton argues that it is not an ‘economic NATO,’ but rather a second transatlantic anchor, rooted in deep and growing transatlantic economic integration” (2014a: 32).

The U.S. and the EU are the largest trading partners in the world. In 2013, the bilateral commerce accounted \$649billion. The transatlantic economy is the world largest accounting for three-quarters of global financial markets, over half of world trade, 50 percent of world gross domestic product, and 41 percent in terms of purchasing power (Hamilton 2014a: 32). The EU exports twice as many good to the U.S. than it does to China, and the U.S. exports three times as many goods to Europe as it does to China (Hamilton 2014a: 32).

The previsions for the impacts of the TTIP on American and European economies are a foreseen growth ranging from 0.5 to two percent of GDP and

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<sup>1</sup> For more information see Hamilton 2014b.

creating around two million jobs (Barker 2013). Barker underscores that “Today, a third of the tariffs paid by the United States go to Europe. “Zeroing out tariffs could add \$180 billion to both economies” (2013). As argued by Sapiro, Deputy U.S. Trade Representative from 2009 to 2014, the TTIP is “about establishing new rules of the road that reflect U.S. and EU core values and high standards. It also has the potential to cement an even stronger U.S.-EU partnership that could, over time, create a platform to embrace new TTIP members that qualify and thereby enhance broader Euro-Atlantic stability and prosperity” (Sapiro 2014).

The slow economic growth, limited job creation, and competition from emerging markets have contributed to launching transatlantic trade negotiations in order to eliminate tariff and non-tariff barriers. The argument for the TTIP is related to the creation of institutional rules in the transatlantic economy. The TTIP seeks to promote multilateral trade liberalization, establish new rules and standards at the global level, and respond to the rise of powerful emerging economies such as China and Brazil. The TTIP is framed as being the agreement allowing the creation of jobs on both sides of the Atlantic and boosting the sluggish European economic engine.

The TTIP is “much more than a free trade agreement,” it is the “next frontier” according to HR/VP Federica Mogherini (2015). The concept of next frontier underscores a clear strategic vision behind the largest free trade agreement in world. Trade is one instrument with several facets: on the one hand, it is a clear component of soft power, as through trade Western values, ideas and norms can be exported; and, on the other hand, it is about pure geopolitics as it would allow the Euro-Atlantic community to balance out thanks to an increase of trade relations and savings on removed trade barriers, and harmonization.

## **European Perceptions on the TTIP and the Negotiation Process**

Two years in the negotiation process of what should have been a technicality, European citizens are continuously skeptical about the TTIP. Since the collapse of the financial markets causing a snowball effect over the European economies, the economic situation of the European continent has been quite difficult. In most EU Member States, the rise of populist parties<sup>2</sup> – right and left combined – illustrates popular and domestic concerns over globalization, global markets, and the EU itself. In some ways, and in some countries like France, the TTIP has become a materialization of the global forces imposed on European citizens. This section is composed of two parts. The first one looks at the European concerns over the negotiations themselves and what is perceived as opaque-negotiations under the

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<sup>2</sup> The results of the 2014 European Parliament elections added to the recent elections of Syriza in Greece and the increasing popularity of extreme-right parties in France, the Netherlands, Austria, and the UK explain the shift of rhetoric over the TTIP.

helm of the European Commission, or Brussels. The second part seeks to look at the actual European ‘fears’ over the TTIP and its components.

## 1. The EU versus the Member States?

The negotiations process is already a cause of concerns for many European citizens. As written in the Treaties, the European Commission, or the executive body of the Union, is the lead negotiator representing the EU-28 in trade negotiations.<sup>3</sup> However, during the negotiations, the Commission maintains a strong relationship and discussions with the Member States through the Council of Ministers.<sup>4</sup> The European Parliament (EP) was historically kept informed, but with the implementation of the 2009 Treaty of Lisbon, its power in trade negotiations has increased.<sup>5</sup>

Until the Treaty of Lisbon, trade negotiations were mostly undertaken between the Commission and Council of Ministers. The EP was usually excluded. With the Treaty of Lisbon, the EP has grabbed some new powers in expressing its positions and recommendations on trade negotiations. “The explanation for the EP’s growing informal impact is as follows: as the EP now has to give its consent at the end of negotiations, the recommendations it issues in nonbinding resolutions before the negotiations have a similar political weight as the negotiating guidelines from the Council” (Van den Putte *et al.* 2014: 3). In the case of the TTIP, the EP has now increased its power as the Commission needs to inform the International Trade Committee (INTA) before and after each round of negotiations (Van den Putte *et al.* 2014: 3). Once the negotiations are completed the text ought to be approved by the Council of Ministers and the EP.

Despite a leading effort by an executive body, the Commission, the final agreement has to be approved by the Council of Ministers, representation of the EU-28, and the EP, in representation of European citizens. “Parliament must use its influence on framing TTIP rules,” argued Trade Committee Chair Bernd Lang, “to ensure that they serve all EU citizens, not just a few economic players and must therefore insist that the talks are more democratic and more transparent” (European Parliament 2015). In any case, the TTIP has to be ratified by the European Parliament through a yes or no vote in order to enter into force.

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<sup>3</sup> The EU external trade policy is one of the strongest elements in EU system of external relations. It is often defined as the European external ‘single voice.’ Based on the Treaties, the European Commission can negotiate preferential trade agreements (PTAs) with third states and international organization in the name of the EU and its Member States.

<sup>4</sup> Concerning the Council the general ruling and voting process on trade policy is based on the Qualified Majority Voting (QMV), except for cultural/audiovisual services (EU’s cultural and linguistic diversity) and social, education or health services, which have to be approved by unanimity.

<sup>5</sup> With the Treaty of Lisbon, the European Parliament is playing the role of co-legislator on trade matters.

Ultimately, the Commission may run the negotiations, but all the EU institutions are involved in the process. Additionally, the Commission, Council and the Parliament have tried to have a comprehensive strategy and be as transparent as possible as illustrated by the number of publications on European institutions' websites. The common market and international trade are central component of the EU, which fall under the capacity and authority of the Commission.

In the past, the Commission has negotiated a large number of trade agreements without taking into account concerns from European citizens. This one with the US, one of the possible largest trade agreements, seems to resonate differently among European heads of states and governments and citizens.

### Perceptions of the TTIP in Europe and the US

The success in the negotiations of the TTIP could lead to the largest trade agreement in history. The question of domestic politics is important to incorporate when studying trade agreements and policies (Alt *et al.* 1987, Milner 1987, Goldstein 1996). The public opinions on both sides of the Atlantic have had a say on their perceptions of the TTIP.

The TTIP is closely connected to the narrative of globalization (Bhagwati 2004, Stiglitz 2004). Overall European citizens are much divided on their understanding of globalization. They are neither in clear favor or full rejection. As illustrated in the table below (Table 1), at the EU level 40 percent of European citizens in 2012 saw globalization as an advantage for their national country, while 42 percent of them think that globalization represents a threat to national employment and companies. If one reflects on the perceptions of globalization on national EU Member States, few European citizens see a clear gain in globalization. Germans, with 53 percent, and Dutch, with 68 percent, are the principal citizens in favor of globalization, while the leader of anti-globalization is France with 65 percent against followed by Belgium with 57 percent. Only one quarter of the French citizens perceive globalization as a clear benefit for their country.

Table 1: Which one of the following two statements is closest to your opinion regarding globalization? (May 2012)

	Globalization represents a good opportunity for (NATIONALITY) companies thanks to the opening-up of markets	Globalization represents a threat to employment and companies in (OUR COUNTRY)	Do not know
Belgium	37%	57%	6%
France	25%	65%	10%

Germany	53%	36%	11%
Italy	29%	48%	23%
The Netherlands	68%	24%	8%
Poland	41%	32%	27%
Portugal	31%	44%	25%
Spain	35%	33%	32%
United Kingdom	45%	37%	18%
EU-27	40%	42%	18%

Source: European Commission. 2012. “Globalization.” *Eurobarometer Survey*. May [Accessed on January 28, 2015]

According to a recent study conducted in November 2014 by the European Commission about public opinion on the TTIP, a large majority of the EU-28 have responded favorably to the possibility of the TTIP (see chart 1 below). The most in favor are Poland (73 percent), the United Kingdom (65 percent), the Netherlands (74 percent), Malta (75 percent), and Lithuania (79 percent). The EU average in favor is at 58 percent. The EU Member States the least favorable to the TTIP are Austria (53 percent), Germany (41 percent), France (33 percent), and Luxemburg (43 percent). The EU average against the TTIP is at 25 percent. Overall the public concern remains high in two EU Member States, Austria and France, and, to a lesser degree, in Germany, the Netherlands, and the UK.

The French scepticism towards the TTIP reflects a cultural dimension and matches the numbers of Table 1, wherein French citizens are sceptical regarding the economic benefits of globalization. However, in the case of Germany, the lack of support vis-à-vis the TTIP does not connect with the perception on globalization. A recent study produced by the Pew Research Center in 2014 reports that 55 percent of Germans thought that the “TTIP will be a good thing for the country” and 25 percent did not (2014: 5). In the U.S., a majority thinks that the TTIP will be good at 53 percent and 20 percent are against it.<sup>6</sup>

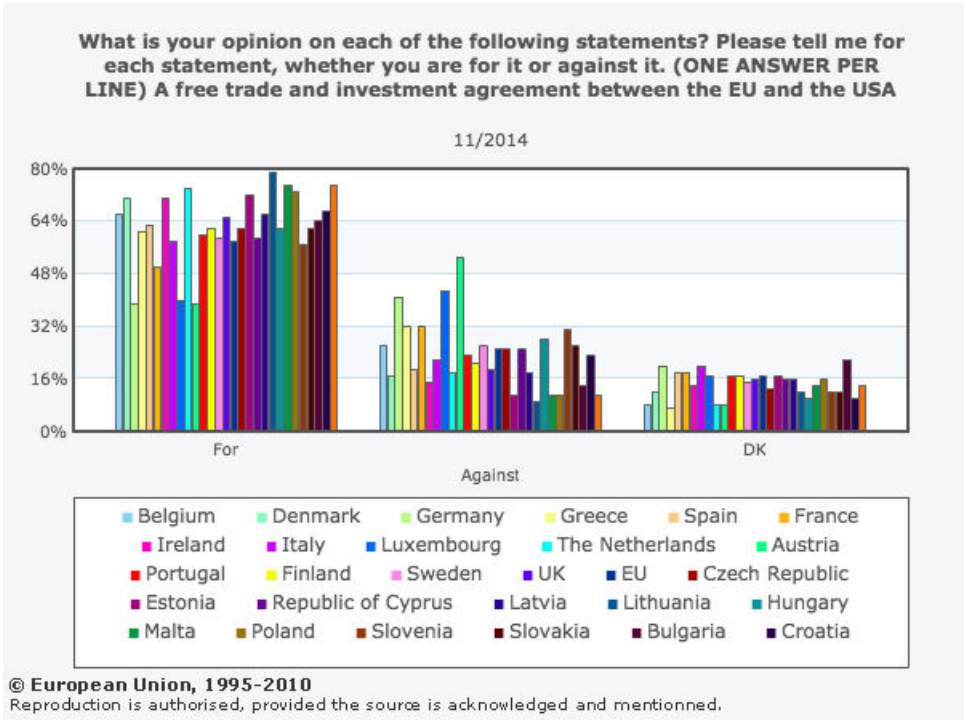
In fact all these numbers illustrate the complexity of the TTIP talks and multifaceted nature of the treaty. In theory, both sides of the Atlantic agree on the reduction and even elimination of tariffs barriers on all merchandise traded. The question of restriction on transatlantic investments is dividing the Atlantic. However the most contentious dimension of the TTIP talks is the question of technological and regulatory standards. Within the issue of standards, Europeans and especially Germans are very concerned about the protection over the regulation of data privacy. The U.S. and Germany tend to have similar positive perceptions of international trade. Both countries have economies closely connected to trade. In the case of Germany, the country has had trade surplus since 1952. For in-

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<sup>6</sup> For more information on the TTIP and European public opinion, see Dullien, *et al.* 2015.

stance as of November 2014, Germany trade surplus was of €17.9billion (Husna 2015).

Chart 1: European Perceptions on the TTIP



Source: European Commission. 2014. “Perceptions on the TTIP.” *Eurobarometer Survey*. November [Accessed on January 28, 2015].

Interestingly enough, the estimation of the overall potential wealth gains resulting from the TTIP would be made from cutting costs due to bureaucracy and regulations (Francois 2013). The contention is not about trade, but rather in the harmonization process. As illustrated by the data (Table 1 and Chart 1), the main concern is on the harmonization process. The main fear in Europe, for European citizens and other European groups, is that the “TTIP is nothing less than a new mechanism by which the ‘American system’ will eviscerate European standards and simply steamroll the European way of life” (Hamilton 2014a: 34). The main arguments raised by European policy-makers opposing the TTIP are entrenched in several narratives: concerns about lowering European standards on food (namely the question on Genetically Modified Food or even chlorine washed chicken); about the lack of transparency on the negotiation process; and, about the investor-state dispute settlement mechanism (ISDS) allowing corpora-

tions to sue governments if local laws threatened their investments (Barysch 2014).

Ultimately, Americans and Europeans are both agreeing on the fact that the elimination of trade barriers is a good thing. But the talks become very difficult once both sides lay down their approach on trying to harmonize the regulatory standards.

### **Concluding Remarks**

Part of the successful results of the TTIP negotiations may reside in the political leadership of the US, the EU-28 and the European institutions in framing the topics embedded in the TTIP and explaining its importance in re-launching the transatlantic economies. Domestically, several actors in Europe, such as agricultural lobbies, right and left populist parties, and anti-globalization parties, have had powerful voices and impact in the negotiations process. Some of the most contentious topics affecting the TTIP negotiations include “investor-state dispute settlement mechanisms (“ISDS”), cross-border data flows, regulatory cooperation, financial services, agriculture and government procurement, to name a few” (Sapiro 2014). These points of contentions are a reflection of national concerns and opposition to the TTIP.

Through the TTIP, the two transatlantic actors are working on boosting their share in the changing world order and establishing new global standards. “North Atlantic networks of interdependence have become so dense that they transcend foreign relations and reach deeply into each other’s societies” (Hamilton 2014a: 25). The TTIP is more than simple trade question. It is a very political file with domestic impacts and strategic ramifications.

The TTIP, if agreed and adopted, could offer to the US-EU the ability to maintaining the liberal world order created at the end of World War two. The rise of China and its dominance of global market are a reality affecting international norms and values. By combining their trading power, the US and the EU will be able to balance out rising powers and remain the leaders in global trade. Trade is more than simple commerce, values, norms and principles are embedded within this mega-free trade agreement.

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# Revisiting the TTIP: the Revenge of Politics

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## Abstract

Two years after their inception, the Transatlantic Trade and Investment Partnership (TTIP) negotiations have reached a critical point on a number of pending issues that will determine the future balance of power between the US and the EU. These issues can influence their relative international standing in areas as diverse as financial power, political influence, social, energy and environmental policies. The TTIP negotiations are part of a readjustment process from the United States and the European Union in response to a shifting geopolitical environment. A geopolitical landscape marked by a rapid economic and technological change, the precariousness of certain states' membership status within the EU, the declining of oil and commodity prices; in addition to the emergence of new energy sources, and the repositioning of emerging powers such as China, Russia, and Brazil in the global arena, calls for a close analysis of American and European responses to the new realities of the twenty-first century. This chapter addresses the convergent and divergent positions these transatlantic partners have variably taken at the TTIP negotiating table in response to the domestic challenges and geopolitical changes that both currently face.

## Introduction

The eighth round of TTIP negotiations of February 2015 should mark a critical point in an extended process as it will focus on a number of pending issues that will determine the relationship between the U.S. and the EU and their relative standing in areas as diverse as global financial power, political influence, and social, energy, and environmental policy. Both, the evolution of the two parties' bargaining positions and the reactions of China, Russia, and Brazil to the process over the two years (since talks were initiated in 2013), suggest that the TTIP agreement represents an integral step in the realignment of American and European geopolitics. A shift that is occurring at a moment when the U.S. is enjoying a post-crisis momentum that Europe has yet to achieve. As such, it could well provide a new road map for international environmental and financial governance.

As negotiations have progressed, each succeeding round has focused less and less on economic benefits and taken on a greater *political* dimension. Since it was first discussed in June 2013, the proposed agreement has increasingly become a means for the partners at the negotiating table to affirm themselves both

at home and abroad. However, further progress towards a final agreement is being hampered by three factors: geopolitical shifts, an economic slowdown in emerging markets, and domestic political and institutional constraints.

### **Geopolitical Shifts, Emerging Powers, and the TTIP Negotiations**

The first factor that should be considered is the fact that geopolitics are taking on new and unpredictable dimensions as emerging powers such as China, Russia, and Brazil jockey to improve their positions and forge coalitions (Mead 2014). Although each of these countries has pursued its own strategy vis-à-vis the U.S. and the EU, they have all in some way or another attempted to overturn the existing balance of power. On one front, China's territorial ambitions in Asia have triggered tensions with both the US and Japan. While on another, Putin's new Russia has been playing the geopolitical card for all it is worth in countries that once formed part of the Soviet Union, testing the resolve of the U.S. and the EU by seizing Crimea and stoking the flames of civil conflict in Ukraine (Stavridis 2014).

Much has been written regarding the TTIP's geopolitical importance and whether it was conceived to serve as a fulcrum with which to rebalance world power neatly between the US and Europe as a block and emerging powers. As we well know, trade has never been neutral; it has always been a highly sensitive matter in international relations. The reservations expressed at the July 2014 Fortaleza Summit by the leaders of BRICS nations (Brazil, Russia, China, India, and South Africa) regarding the implementation of the TTIP were accompanied by concrete measures intended to offset the impact of the U.S.-EU agreement: the establishment of a new global reserve currency and the creation of a new development bank with an initial capital worth US\$ 50 billion. Although these countries have not formally expressed their opposition to the TTIP agreement as a block, they are making it abundantly clear that the type of trade liberalization supposed by the TTIP agreement has ramifications that transcend the issue of global trade. The fact that it will not suppose a win-win game for all non-TTIP countries and there will inevitably be winners and losers, gives it a strong geopolitical dimension on par with other challenging issues such as nuclear nonproliferation, human rights, and climate change.

The TTIP agreement has therefore evolved from being a mere bi-regional regulatory framework with ramifications for global governance to constituting a political tool for defending the dominant role of the U.S., Europe (and by extension, NATO) in world affairs. Recent moves on the part of other major world powers will undoubtedly up the pressure on both TTIP negotiating teams. If the US and the EU want to save face and successfully assert their role as the joint institutors of the international rules of good governance, they must reach an agreement – which it to say practically any kind of agreement – soon. Failure to do so would result in an enormous loss of credibility and prestige for both. As a

result, it could weaken their bargaining positions with China and Russia and undermine the effectiveness of other free trade initiatives such the recently negotiated TPP and The Pacific Alliance and the more established MERCOSUR. Also, we should not forget that the initiation of negotiations toward a transatlantic partnership coincided with the first signs of a fall in the growth of Brazil's domestic market, the deceleration of the Chinese and Russian economies, and the slowdown of commodities prices. BRICS have good reasons to be wary of any regulatory framework devised by the Western countries.

### **The U.S., the EU, and the Economic Slowdown**

The effects of the emerging market slowdown forecast for 2015-16 will have an impact on the upcoming phase of TTIP negotiations. BRICS countries are now facing new economic challenges. The IMF lowered forecasts for global economic growth to 3.5 percent for 2015 and 3.7 percent for 2016, as indicated on its January 2015 World Economic Outlook. This projection stresses the flagging growth potential of emerging markets. Forecasted growth for China, whose economy is expected to suffer a gradual slowdown, has been lowered by -0.3 percent to 6.8 percent and growth in Brazil is expected to fall -1.1 percent to 0.3 percent. The outlook for Russia is even worse: a plunge of -3.5 percent, which, according to the IMF, will precipitate a deep recession. The IMF report also predicts lower oil prices and the further depreciation of both the euro and yen. In contrast, the US economy is expected to grow by 3.6 percent and growth in the Eurozone to slip slightly (-0.2 percent to 1.2 percent). Although Eurozone countries face the risk of permanent deflation, they are set to benefit strongly from lower oil prices, the lower exchange rate of the euro, and an easing of lending conditions. A tightening of the US monetary policy could trigger volatility in the financial markets of emerging countries (IMF 2015).

These forecasts cannot be expected to have a conclusive impact on the future of TTIP negotiations, especially in view of the fact that TTIP negotiations were launched as part of a liberalizing agenda largely conceived and justified (especially in Europe) as a means of overcoming the crisis and facilitating the recovery of world economy. However, two considerations should figure strongly in any long-term U.S.–EU strategy. The first is related to medium and long-term economic trends (Pascual-Ramsay and Imbernón Sáinz 2014). Over the past decade, BRICS have accounted for close to 50 percent of the world's growth. They currently account for 25 percent of world GDP, a proportion expected to peak at 40 percent by 2050. The economic output of China will surpass that of the U.S. (in nominal terms) by 2050 and the output of Brazil and India will outpace that of Germany, France, and the UK by 2060 (Wilson et al. 2011). Should the TTIP agreement collapse, and no other multilateral agreement is reached, and these forecasts prove to be accurate, it is natural to assume that emerging countries will forge their own trade agreements, which may not meet the TTIP governance

standards. It must also be remembered that the intertwined nature of export and foreign direct investment flows make it impossible to postulate that a slowdown of Russia or China would spark greater support for the TTIP agreement in the US and Europe. In other words, while geopolitics may be a zero-sum game, the world economy is not. The instrumentalization of world trade rules for geopolitical motives has its limits: as the relative success of the WTO Doha round meeting held in Bali in December 2013 has shown, the agenda for world governance also matters. Yet, both partners seem trapped between two conflicting political imperatives: attending to current geopolitical concerns and working responsibly toward good governance. In this context, it seems reasonable to conclude that the combination of two new factors (geopolitical challenges and economic slowdown) is not good news for the U.S., the EU, or the TTIP negotiations underway.

### **The Domestic Factors**

The above-mentioned geopolitics and emerging market dynamics aside, domestic political dynamics will also play a decisive role in TTIP negotiations to be conducted during 2015 and 2016.

U.S.'s backers of the TTIP agreement must overcome substantial domestic resistance, although it is still not clear whether or not it will become a hot issue during the 2016 Presidential election campaign. American congressmen on both sides of the aisle have repeatedly expressed their opposition to a "fast track" international trade agreement such as the TTIP or the TTP – without which it is very difficult to negotiate a meaningful deal. As many left-leaning American voters believe that free trade agreements endanger environmental protection, labor rights, and import safety standards, Democratic representatives naturally tend to shy away from political commitments on trade issues that could erode their electoral base of support. Although Republicans may support free trade at a philosophical level, they could be reluctant to support any agreement that would hand a political victory to President Obama. Furthermore, the call for a renewal of trade promotion authority (TPA) contained in President Obama's sixth State of the Union address delivered on January 20, 2015, was not warmly received. Obama's request was fiercely opposed by Democrats such as Harry Reid (majority leader of the Senate at that time) grounded on the argument that support for fast-track approval would hurt Democrats in the November 2014 midterm elections.

Since the Republicans have retaken control of the Senate, perspectives for a deal between the President and the Congress on the TPA have not improved, despite Republican pretensions to support free trade. Options for resolving the current gridlock include the possibility of circumventing the fast-track system provided for in the Trade Act of 1974 by creating specific ad hoc TPAs that covered only certain countries and specific topics such as the environment, labor rights, and health and giving a higher profile to congressmen directly in-

volved in the negotiations. Nonetheless, given the threat of severe recession now looming over the U.S.'s European allies, the political and security implications of the TTIP agreement may yet trigger U.S. bipartisan support for making a deal.

The EU, on the other hand, has never been a geopolitical player in the sense that the U.S., Russia, and China have assumed that role. It has no *grand strategy* of dominion over others and continues to maintain a postmodern perspective on world order; an attitude that will become even more deeply entrenched while the Eurozone struggles to recover and the current North-South gap within Europe remains unabridged. Therefore, no geopolitical sense of urgency to rush to a final agreement can be expected to arise in Europe in the short term.

Resistance in Europe to a liberalizing trade pact can be largely attributed to the effects of low growth rates, high unemployment (especially in states along the continent's southern periphery), a rise in protectionist sentiment, social unrest, and a general climate of political disaffection. Despite official efforts to sell the agreement as a mechanism for spurring growth and restoring the European economy, public awareness rests on the idea that the current economic hardships are largely the result of the economic and financial integration that left European economies exposed to the collateral effects of the American Great Recession. Such perception serves as a deal breaker on any attempt to implement a "liberal" approach.

The eighth round of talks took place from February 2<sup>nd</sup> to the 6<sup>th</sup>, 2015 in Brussels under the leadership of EU Trade Commissioner Cecilia Malmström and U.S. Trade Representative Michael Froman. However, lingering doubts about the feasibility of the € 315 billion Juncker plan have generated skepticism in Europe (especially in Southern European countries and France) regarding both: the much-trumpeted but fairly anemic European economic "recovery" and the real benefits of a trade deal with the US that may well imply high social costs. Europe's institutional framework could also slow down the negotiations to the point that they eventually derailed. Given the high sensitivity, of sector lobbies in member states and European citizens hit by the crisis, on issues involving banks and big corporations, the European Parliament – the only EU institution whose members are directly responsible to European voters - will undoubtedly play a decisive role in the process.

Although negotiators have made progress on points such as technical trade barriers, state-owned enterprises, customs and trade facilitation, and telecom services, they have yet to overcome differences regarding issues Europeans perceive as critical such as labor rights, consumer safety regulations, and environmental protection.

It is therefore no surprise that sensitive points will be negotiated at the highest political level. The first among them is the inclusion of an investor-state dispute settlement (ISDS) mechanism, by which foreign investors may bring cases against the countries in which they have invested before an arbitration tribunal



should they feel their financial interests have been harmed or discriminated against. The devil is in the details when it comes to democracy, transparency, environmental protection, labor rights, and consumer protection. Given the close integration of the U.S. and the EU financial markets, the financial sector regulation—especially when currently targeting unregulated derivatives and similar instruments—is bound to be a make-or-break issue from the European perspective (EU Commission 2014). The present opinion in Europe is that any deal failing to safeguard Europe's financial resilience from future crises, similar to the subprime crisis of 2008, would not be worth signing. Apart from the give and take of negotiations regarding the inclusion of an ISDS instrument or the agriculture, audiovisual, and financial sectors, there is also the economic climate to consider. While the European Parliament's International Trade Committee (INTA) is expected to present a resolution on TTIP at the May 2015 plenary session, any serious deterioration of economic conditions in the Eurozone could completely derail negotiations.

Paradoxically, the European Parliament, a frequently criticized and undervalued institution, will have the final word on the sensitive issues yet to be resolved during the last round of the TTIP process. Under pressure by European civil society organizations, INTA chairman Bernd Lange forced the public release of the European Council's mandate to negotiate, which had been kept under wraps until the fall of 2014. This was a first step forward in terms of closing a transparency gap that has loomed over the negotiations since the beginning (EU Commission 2015). However, no agreement will be possible without cross-party consensus within the EP. In principle, the TTIP agreement enjoys the support of majority groups in the European Parliament (the center-right European People's Party, the Progressive Alliance of Liberals and Democrats for Europe, and the European Conservatives and Reformists), which all regard the deal as a means of promoting employment and growth in Europe. However, groups that focus on highly sensitive environmental or social issues such as the Greens and the United Left have respectively distanced themselves from the process or outwardly rejected it (Pavón Losada 2014). As they remain very reluctant to accept many proposed tenets of TTIP and continue to strongly demand standards protecting the rights of workers and the environment and the inclusion of binding common regulation of transatlantic financial transactions, the Socialists could assume the role of bridge-builder between the two sides. Given that a comprehensive TTIP agreement would need to be ratified by all 28 member states of the European Union, approaching the Greens and left-leaning MEPs who currently reject the deal and attempt to build strong coalitions on this issue would appear to be a good strategy for easing the path to parliamentary ratification. In particular, in the light of the strong gains made by these forces at the national level during elections in Greece and the forecasted success of their Spanish counterparts in the upcoming Spanish general elections. In any case, it appears that consensus on the desirability of a transatlantic agreement will be more difficult to achieve in Europe, where

geopolitical positioning does not have the importance it could be expected to assume during ratification debates in the US Congress.

What can we learn from the domestic shortfalls of the countries and the barriers that have prevented them from reaching a consensus over the last two years? Put fairly simple, Americans and Europeans are moving in the same direction but playing on different chessboards. Their most irresolvable differences are related to labor rights, environmental protection, and the regulation of financial markets – issues at the very top of the global governance agenda. Trade is, and has always been, an element of national strategy, the ramifications of which extend beyond mere economics (Froman 2014); it is nothing less than “politics by other means.” Whereas the TTIP agreement may be perceived as a question of geopolitical leverage from an American perspective, it is viewed in the EU as an opportunity to further the implementation of good governance practices. Some voices in Europe have called for an accelerated, minimalist deal focusing mainly on the elimination of remaining non-tariff barriers (Dullen and Janning 2015). However, given that such a treaty would do little more than underline the differences between their socio-economic models, geopolitical concerns, and visions of global governance, it might not be the best option for either of the negotiating partners, especially in terms of their international leverage. If Europeans want to lead this process somewhere, it would be more advantageous for them to draw a few clear red lines on politically controversial issues such structural regulation than to sign a hurried, minimalist treaty that would offer only dubious, or at best, modest benefits.

## **Conclusion: Geopolitics and Beyond**

Since President Obama and the European Commission announced their intention to start the transatlantic trade negotiations in February 2013 strong political factors have had a continual impact on such process. Current differences between the two prospective partners stem largely from the divergent ways in which political factors are affecting them: the economic and social post-crisis circumstances that inform their respective positions are radically different.

The success of the TTIP agreement is imperiled by least three factors: marked geopolitical shifts, uncertainty generated by the slowdown of emerging markets, and political and institutional constraints imposed by the U.S. Congress, the European Parliament, the governments of various European states, and last but not least, civil society organizations on both sides of the Atlantic. Firstly, recent moves by the leaders of major emerging powers such as Russia, China, and Brazil within their spheres of influence and their critical positioning on TTIP exclusions, have added a sense of drama and urgency to transatlantic relations. From their perspective, the U.S. is using both the TTIP negotiations and the concept of transatlantic trade as geopolitical tools. For the Obama administration, free trade agreements such as the TTIP and the TPP are part of a broader strate-

gic campaign to secure American global dominance. A successfully negotiated TTIP agreement would mean replacing an antiquated trade system dating back to the end of World War II with a web of cutting-edge agreements that ensured the U.S. position as the linchpin of world trade. In contrast, for the EU—which lacks a “strategic culture”—the TTIP is generally perceived as an additional means of bringing an end to the economic crisis, defining new economic, social, and environmental models, and shaping global governance. Secondly, the emerging market slowdown forecasted for 2015-16 could have an impact on the upcoming phase of TTIP negotiations in that it will exacerbate the atmosphere of political uncertainty in which positions taken by the US, Europe, and other economic superpowers will be developed. The slowdown of the BRICS economies leaves the U.S. in particular with the dilemma as to whether it would be more advantageous to play the geopolitical card for all it is worth or to promote global governance and world economic recovery.

Thirdly, various forces within the U.S. Congress, the European Parliament and the governments of European states are mounting opposition to the agreement. It will not be easy to resolve the current impasse caused by differences over the possible inclusion of structural regulations that have become hot issues on both sides of the Atlantic such as an ISDS clause and strong guarantees for labor rights and environmental standards. Given the lingering effects of the economic crisis in Europe, the regulation of financial markets is crystallizing into a European requisite for any serious deal that may be eventually struck.

The final phase of negotiations will be extremely challenging. However, even if the upcoming trade negotiations fall short of delivering a speedy agreement in 2015 or expectations are lowered, the idea of forging a transatlantic partnership should not be abandoned. U.S. negotiators need to realize that given the current political and social situation in Europe, any deal that could further imperil a European economic and social “acquis” already sorely tested by the current crisis is out of the question. To ease the way for future negotiations and the eventual ratification of the treaty by the EU Parliament and the EU member states, any red lines drawn by EU negotiators should be pegged to clear regulatory pillars.

Once again, we are facing the revenge of politics. The consequences of abandoning efforts to reach a comprehensive agreement or signing a devaluated deal would likely be quite similar: either move would transmit a negative signal to emerging powers, harm the geopolitical leverage of both partners, and reduce the prospects for global governance on issues that go beyond trade. The problem negotiators face at this point is that the window of opportunity for pursuing a third option is rapidly narrowing.

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# Symmetries and Asymmetries in Integration Processes: The New Atlantic Community

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## Abstract

Integration processes are beneficial and necessary. However, we must stress the fact that for certain actors in certain contexts, integration does not always translate into optimum results. For example, we can reasonably think that there will be negative consequences for a small country with high-quality institutions (such as Uruguay) if it integrates with larger countries with low-quality institutions. Moreover, this problem is not solved by subsuming a complex and opaque area (such as MERCOSUR –Southern Common Market) under a larger and transparent agreement (such as a potential one between MERCOSUR and the European Union). Can countries with solid, transparent institutions successfully integrate with countries with weak, corrupt institutions? Can this hypothetical integration process really be so simple?

## Introduction

Both in the academic and business spheres, we almost systematically underline –without so much as a second thought– “the benefits” that integration processes “naturally” bring about.

This "optimistic" approach to integration most probably stems from a view held by international trade specialists - a view that is tinged with an understandable concern about encouraging free trade.

However, the integration of countries or regions (even only in terms of trade) is not something that can be *a priori* considered good or bad. To illustrate, the final outcome of an integration process like the one we are addressing here, taking into account the number of actors involved, depends on a myriad of complex variables. We could tentatively summarize these variables as follows: (a) the European Union (EU) internal policy; (b) the United States (US) internal policy; (c) variables that are truly intangible and that we could call Latin American Countries (LAC) “internal policies,” are yet to be determined. They mainly regard Brazil’s position, MERCOSUR (Southern Common Market), the Pacific players that still have to be fully identified, and special situations such as the Cuban question that has just gained prominence. Other variables to consider are, (d) the commercial, economic, political conditions under which the EU and the US

negotiations occur today; (e) the current state of negotiations between the US and LAC; and (f) the current state of negotiations between the EU and LAC.

Evidently, there are clear asymmetries among these points: a, b, and d, are presumably more important than the others. Moreover, we are aware that if we were to carry out an analysis of the variables that are, in turn, included in each point, the whole exercise would make little –if any– sense.

So, it seems pertinent to proceed in a more descriptive way and narrow the topic to questions about the traits that a satisfactory integration process should display. With more epistemological modesty, we will try to answer fundamental questions such as: With whom, how, and for what reasons, should integration take place?

The potential “New Atlantic Community” creates great possibilities that encourage exploring –at least partially– some conceptual aspects of these three questions. For this, we must revise various explicit and implicit concepts that will come into play if this initiative effectively moves forward.

### **Addressing Problematic Issues**

The first problematic element that we should question is the idea that *geography* (taken as the territorial “closeness” between countries) is the main factor in determining which will be the best placed actors in a successful integration process.

We are aware that history seems to contradict our position, but we believe that when the idea of “closeness” intervenes in an integration process that it is used to hide the fact that integration among countries rests in a form of proximity that is much more important than geography. Geographical “closeness” hide the importance of pre-existing historical or cultural dimensions (linguistic, religious, political, etc.), rather than strictly geographical proximity. Even though most cases of integration have taken place between countries “close” to each other, a careful examination of these cases shows that “geographical closeness” allows for more complex forms of “closeness” and that the latter ends up playing a greater role in successful integration processes.

Integration experiences such as Central America Free Trade (CAFTA) or the Nordic Council, which are seemingly based on adjacency and close territorial vicinity, are in fact based on pre-existing common political or cultural experiences. Everything indicates that the prior, long coexistence under the Captaincy General of Guatemala during colonial times is what upheld the cohesion of the Central American integration experience during the twentieth century.<sup>1</sup>

The integration of the Nordic countries is a slightly different case. These countries created a Nordic Council in 1952, which is an inter-parliamentary co-

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<sup>1</sup> Panama is not part of CAFTA because it came into being by separating from New Granada, an independent from the Captaincy of Guatemala.

operation and integration experience. In this case, geographical closeness may also be invoked.<sup>2</sup> But, its historical precedent comes from the existence, in the fifteenth century, of the Kalmar Union that joined the “Scandinavian” and “Nordic” people all together. And later, throughout the next three centuries, they were all grouped into two kingdoms: Denmark and Norway under one crown and Sweden under another. In sum, the “Nordic Council” is based on a common history more than on geographical closeness.

A second point we should stress is that we also intend to purposely leave out two arguments that are most often cited by economists and international trade specialists as the foundation of a “good integration process.” These bases are built on two overused ideas. On the one hand, is the idea that an integration process is essentially a process of “trade” (or at best, of “economies”) with successive and more encompassing stages? Political, institutional, and cultural issues are only relevant if they affect the integration of “trade.” In this sense, it is important to recall and link to our topic the impressive concept of development of William Easterly in *The Tyranny of Experts: Economists, Dictators, and the Forgotten Rights of the Poor* (2013).

As we will see, the European Union is an example that contradicts this vision because, from its outset, it contemplated horizons of integration that went far beyond trade. The European Coal and Steel Community, the backbone of European construction, goes beyond the production of coal and steel and addresses trade and political aspects linked with these industrial sectors.

In an opposite way, initiatives like NAFTA (North American Free Trade Agreement) only aimed for what would be a “second tier” trade arrangement among three markets: a simple free trade agreement that merely transcended the typical “preferential treatments” and never intended on going beyond that.<sup>3</sup>

On the other hand, so as to eventually have the conceptual tools that would allow us to identify what a “good integration process” looks like we must also question another integration “cliché.” We are all familiar with the claim about the need for economies that join an integration process to have “a reasonably high degree of complementarity.” This expression has a classic interpreta-

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<sup>2</sup> But in a much less obvious way than in the previous example. Here we have the peculiarity of Denmark being geographically contiguous to “continental” Europe, just like Estonia and Latvia were and who, only under Soviet pressure, cut ties with the Scandinavian world and became part of the Soviet world. There are also other territories that are relatively distant –like Greenland– who, being dependent, were always part of this peculiar Nordic “integration”.

<sup>3</sup> This is different from MERCOSUR, which was initially thought of as an integration process for a Customs Union but ended up being so imperfect that it boasts a lower degree of liberalization than a Free Trade Agreement. See a good paper written by Baldwin (1993).



tion.<sup>4</sup> But, it must be explained. We know this reasoning is antiquated and blatantly false: it is not true that, in order to integrate successfully, country A must be efficient in producing a good that country B lacks, and vice versa. This belief is set in the Ricardian thought mentioned in the footnote below.

The creation of the Latin American Integration Association (ALADI) was an integration process that was based on finding complements. We must note that here, “complement” is a euphemism. In fact, this idea of integration implies the absence of competition. That is, country “A” produces a good that country “B” does not have, and country “B” produces a good that country “A” does not have. Therefore, the producers of both goods find the size of their markets has grown – markets that are, in fact “protected.”

To sum up, we are trying to set aside some of the most overused bases of the integration discourse before we introduce the main thesis of this article. We only intend to analyse the importance and effects of two elements that are often overlooked and seldom put together when studying the terms and effects that integration processes can jumpstart. These are: (i) the *relative size* of the economies that will integrate (exclusively in relation to each other); and, (ii) the *degree of efficacy* of the existing rule of law and the *relative institutional quality* of the (formal) legal systems and (informal) regulatory systems that operate in the two societies in question.

### **Economic Scale and Institutional Quality: Symmetries and Asymmetries in the Integration Processes**

As mentioned above, in this section we are going to analyse the idea that the benefits and drawbacks for two hypothetical countries in an integration process depend on two main variables: (i) the *relative size* of the economies; and, (ii) the *quality* of each country’s *institutional and legal system*.

The relative size reflects the different economic weight of each country in relation to the other. The institutional quality reflects the efficacy of the legal system and the ability of laws, political-business leaders, and bureaucracies to carry out an efficient and reasonable integration agreement. This also includes the ability of different civil societies to control the dynamics of this agreement.

It is generically possible to claim (and it is almost obvious) that integration is a good thing when it involves two or more actors of high institutional quality; it is neutral or bad when it involves actors of high and low institutional quality; and it is bad or very bad when it involves actors of low institutional quality. At the same time, our approach considers that the size of the actors is as important as the institutional quality when it comes to judging the convenience of

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<sup>4</sup> The idea of trade “complementarity” between two countries comes from Ricardo’s theory of comparative advantage. To summarize, “complementarity” arises because England produces textiles efficiently and Portugal produces wine efficiently. Ricardo’s two economies would be, in current terms, two “complementary” economies.

integration. And at this point, a similar obvious claim can be repeated: countries whose economies are similar in size seem to foster more promising integration processes. However, things are hardly ever this simple.

Some illustrative examples will help clarify “an integration process” between two countries using their relative economic scales and institutional quality.<sup>5</sup>

### **Case 1: Can an Integration Process that Involves a Large Economy Lodged in a Country with High-Quality Institutions and one or More Small Countries with Low-Quality Rule of Law Be Promising?**

Here is an example: with CAFTA, a country with high institutional quality such as the United States has fostered an integration process with small economies lodged in countries of low and very low institutional quality (with the sole exception of Costa Rica).

We can rightly assume that the institutional shortcomings of Guatemala, Costa Rica, El Salvador, Honduras, and Nicaragua will neither harm nor enrich the institutional quality of the integration process, nor will they greatly affect the United States “civic life.”<sup>6</sup> At the same time, apart from the benefits brought about by trade relations, possible coordination of production, and other economic developments; obviously the larger economy’s greater respect for the law and its legal organization will become an incentive<sup>7</sup> for smaller economies with weaker institutions to improve and strengthen themselves.

But in general terms, and setting aside the concepts questioned at the beginning of this work, we can conclude that in this case we can foresee an integration process that will benefit all actors.

### **Case 2: Can Countries with Small Economies and Good Institutions Truly Benefit from Integrating with Large Countries with Bad Institutions?**

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<sup>5</sup> We are not taking into account cases in which the countries’ two traits (economic scale and institutional quality) coincide.

<sup>6</sup> We must note that even in countries with solid institutions do procedures and *modus operandi* manage to filter in and operate outside the law. For example, Mexico’s immigration, drug trafficking, and organized crime does affect the United States. However, this does not lead us to question the United States’ overall institutional quality and rule of law.

<sup>7</sup> Experience shows that the legal organization of countries and their institutional systems are complex historical products. Although the integration with economies and societies that have more organized legal systems and show more respect for the law should have a positive effect, we cannot be naïve and say that, for example, Central American countries’ institutional shortcomings will disappear.

In many ways, this second case is the “opposite” of the previous case. Uruguay’s complex situation is a historical example of this scenario. It is a very small economy that is lodged in a society where the rule of law and institutions are generally of relatively high quality. From 1991 to the present day, Uruguay has endured an integration process with two much larger economies (Argentina is 9.6 times larger than Uruguay and Brazil is 40 times larger than Uruguay) that are lodged in countries with permanent lack of legal guarantees, institutional weakness and general disregard for the law (including the laws that are directly related to and were agreed on in the integration process).

This scenario proves difficult for a small country with a relatively high institutional quality. The larger economies tend to impose conditions on the smaller economy. And this is aggravated because the larger economies disregard the rules they had agreed to and constantly behave in an arbitrary manner. Argentina’s trade policy (not to mention other policies) with Uruguay over the last five years is proof of this. The integration process may be interrupted or simply left to expire and be abandoned by the least favoured country. However, we must note that in this case, it is the weaker country. Then, it seems to be clear that the mainstream approach to the benefits of trade blocks lacks a better and careful understanding as North, Wallis and Weingast have argued (2009, 2013).

### **Case 3: What Prospects are there for an Integration Process Involving Two Large Economies of Different Institutional Quality, Where One Actor’s Institutional Organization Is Much Less Developed than the Others?**

This could be the case of a hypothetical integration between the United States and China or India. Taking into account that this example is farfetched –for now– we could imagine that disagreements stemming from differences in institutional quality and respect for the law would move into more political spheres. When “great powers” clash, the economic dimension and geopolitical strength tend to minimize the regulating role of laws. Even the recourse to international law and multilateral institutions is difficult due to the scale of the economies in question.

The current trade development between the aforementioned countries indicates that, even though they are far from any type of integration, the disregard of American laws, the use of falsification, the disrespect for patents, etc., especially by China, have become constant sources of conflict. Could they become an important problem of legal control for the United States?

Could the United States’ better laws have a greater influence over the institutional framework of integration than China’s feeble ones? In economies of this scale, we could expect political pressures to arise – far from the debate on integration. For example, China is the largest bondholder of the United States Treasury. This point is relevant because our intuition tells us that if there are two equal actors and one has good institutions and the other has weak institutions, the bad institutions would have more influence over a possible integration process.

That is, an obscure bureaucracy's ability to veto or boycott would be greater than a transparent bureaucracy's ability to influence. Integrating large economies is difficult, but we must hope that ultimately, political power would seemingly manage the conflicts created by the great economy of lower institutional quality.

#### **Case 4: What Would Happen in an Integration Process Involving Two Small Economies, One with High-Quality Institutions and the other with Low-Quality Ones?**

This case would once again show that when the economic scale of the countries is similar, the integration process tends to turn into a political struggle. In this struggle, the country with higher-quality institutions puts up a political fight so that the country with lower-quality institutions respects the established rules.

It is difficult to find a convincing historical example to illustrate this case.<sup>8</sup> Despite what is presented in the footnote, because we are dealing with relatively small economies, the country with higher-quality institutions may find it relatively easy to use in its favour the existing legal tools that are available in the supranational.

#### **Case 5: What Would Become of the Integration of Large Economies, both with Good Institutions?**

This scenario is particularly pertinent here. Setting aside difficulties related to trade issues, we could say that this case presupposes the existence of necessary but not sufficient conditions to create an institutional framework that brings both actors into a positive sum game. Given the complex nature of the EU and the United States, the final negotiations of the Transatlantic Trade and Investment Partnership (TTIP) will soon show to what extent a promising set of necessary conditions –that is, the high quality of US and EU's institutions– will prove to be a strong starting point for the arrangement to succeed.

#### **Other Cases**

It is possible to come up with more combinations of the two variables we are interested in. For example, a large country integrating with a small one, both with low-quality institutions; a large economy with high-quality institutions integrating with a small economy also with high-quality institutions, etc. But, given the narrow scope of this work, we cannot outline all the possible combinations and their peculiarities.

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<sup>8</sup> The example of Costa Rica and Nicaragua entails an institutional relationship between a small country with good institutions and a small country with bad institutions. When faced with a country of equal weight, it is difficult that the push for a transparent institutional framework be greater than the ability to hinder its creation.

## **An Exception: the European Union**

The European Union is the most sophisticated and relevant integration process to date. This agreement has developed different expressions (fiscal, trade, legal, monetary) and its comparative value makes it analytically relevant to us. Europe is composed by large, medium, and small countries, and countries with high-quality, some with medium-quality institutions and a few with low-quality institutions.

The European experience is also relevant for another reason. As mentioned above, integration processes are invariably carried out following rules that were set by their potential members' political leaders and bureaucracies. It may be true that the institutional quality of an integration process cannot be greater than the sum of the quality of its parts. That is, if countries A, B, and C are structurally corrupt and inefficient, the new agreement will most likely be corrupt and inefficient.

But, the opposite is not necessarily true: transparent and efficient countries can undertake an integration process that ends up having a lower institutional quality than those of its members. In some ways, the European Union is an example of this. Even though it has achieved a sophisticated and complex level of integration, disputes over certain issues remain unsolved. For example, the development of a European defence system has not been able to overcome the resistance posed by national military structures.

## **Facing the Possibility of the New Atlantic Community**

The possible EU / US / LAC integration will certainly translate into an opportunity to improve LAC institutions. We could say it is almost obvious that an integration process among these three actors will bring about positive consequences. As in the case of the incorporation of former Soviet-bloc countries to the EU, it is likely that the creation of regional institutions would –to a certain extent– strengthen laws and mechanisms of control, and inject some degree of transparency and efficiency into the unreliable legal framework of most Latin American countries.

If countries like Uruguay were to look for “exit options” from arrangements like MERCOSUR, these options would have to be moderate enough so as not to distress its larger members (Brazil and Argentina). With this in mind, is it true that a way out of MERCOSUR would be to blend it into an even greater trade and investment society, such as EU-MERCOSUR, where Argentina and Brazil would have main roles in negotiations? Would this “Atlantic Community” not generate the same problematic logic for small or relatively small countries with high-quality institutions, like Chile, Uruguay, or Costa Rica? In other words: in a negotiation with the United States or the EU, what is good for MERCOSUR, will be necessarily good for Uruguay as well?

The complexities of this initiative are obviously enormous. Maybe we should resort to new proposals. One proposal entails exploring the idea of creating “optimum institutional areas,” stemming from Robert Mundell’s concept of an “optimum currency area.” According to Mundell an optimum monetary area is:

“The geographic area in which a single currency would create the greatest economic benefit. While traditionally each country has maintained its own separate currency, work by Robert Mundell in the 1960s theorizes that this may not be the most efficient economic arrangement. In particular, countries which share strong economic ties may benefit from a common currency. This allows for closer integration of capital markets and facilitates trade. However, a common currency results in a loss of each country’s ability to direct fiscal and monetary policy interventions to stabilize their economies” (1961: 660).

Undoubtedly, this arrangement would not be simple. What would an “optimum institutional area” look like? How should we define it? It is an integration process involving two (or more) actors with at least one common “convergence” indicator: size or institutional quality – or lacking that, with asymmetries of size or institutional quality that do not harm one or more of the actors.

In short, what we dare to call an “optimum institutional area” would be nothing less than the joint determination from all the countries participating in the integration process of a minimum institutional quality of integration – an integration that is agreed on by all its members. In other words, we are referring to an institutional quality that, apart from being agreed on by every member, will inevitably end up being supranational.

What we are referring to – even though we refer to it as an “optimum institutional area” – is an institutional arrangement similar to what has emerged from Brussels for the European Union over the last decades. Whether or not this arrangement is possible or even imaginable for our New Atlantic Community – it is a different matter.

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# Trade, Regional Integration, and Free Movement of People

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## Abstract

A building block of regional integration in Europe has been the development of supranational rights, particularly the rights of citizens of member states to live elsewhere in the community. Since the first free movement rights in the early 1950s, the concept of a common EU citizenship has hardened into law, most famously in the Court of Justice's oft-repeated assertion that "Union citizenship is destined to be the fundamental status of nationals of the Member States." By contrast, efforts to foster the free movement of people in groupings such as CARICOM, the Andean Community, MERCOSUR, and UNASUR have so far been relatively modest. Nevertheless, actors within each of those organizations have or are considering supranational rights, thus it is useful to ask about the prospects of common free movement rights and perhaps eventually citizenship, focused foremost on the right of member state nationals to live and work elsewhere within the community. The paper's underlying argument is that successful and stable regional integration efforts must include free movement rights for people.

## Introduction

In a speech at Yale University about the Transatlantic Trade and Investment Partnership (TTIP) currently being negotiated between Europe and the United States, the European Commission Vice-President Viviane Reding argued that "a single market requires fundamental changes in which nation states cooperate. They must abolish their prerogative to establish border controls, excise customs duties, guarantee the free movement of people, goods, services and capital, etc. Overall, they must guarantee each of their own citizens and of every other member state of the European Union the same, Europe-wide enforceable rights." (Reding 2013) This idea that free movement of persons is central to the European project, and perhaps also other regional integration efforts, is something I find persuasive because I have been making similar arguments for a while (Maas 2005; 2007; 2009; 2013a; 2014a; 2014b).

The argument is that, alongside the economic logic of integration, European leaders share a political commitment to creating a common community of

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people, and that this commitment has gradually resulted in the creation of a common citizenship. The most important rights of the supranational citizenship involve free movement rights to live and work anywhere within the common territory, which is the foundation of a political community. Though always in tension with the desires of member state governments to maintain control over their borders and to decide who can live within their territory, the right of EU citizens to live anywhere within the EU is vigorously defended by central institutions such as the Commission and the Court. While it works in the European context, the relationship between trade agreements, regional integration, and free movement of people elsewhere is not always clear.

In this short paper I counterpoise the example of EU citizenship and nascent efforts in Latin America to develop forms of regional citizenship, to argue that successful and deeply rooted regional integration efforts must include free movement rights for people, and not simply the free movement of goods, capital, and services. The paper proceeds as follows: in the next section, I sketch the development of free movement rights in Europe. Then, I discuss some efforts to develop such rights in the Americas, emphasizing the distinct political dynamics at work in the two contexts. Then I raise some questions about the applicability of the European model in the Americas, before concluding with some brief thoughts about the role of national governments and supranational institutions in pursuing freer movement of people and a common citizenship in regional integration efforts.

## **Free Movement in Europe**

The postwar federalist determination to introduce a supranational European citizenship to supplement national citizenship was reflected in statements such as Winston Churchill's 1949 call for a "sense of enlarged patriotism and common citizenship" for Europeans. The previous year, at a conference bringing together hundreds of Europe's most important leaders and thinkers, Churchill had said: "We hope to reach again a Europe...in which men will be proud to say 'I am a European.' We hope to see a Europe where men of every country will think as much of being a European as of belonging to their native land. And wherever they go in this wide domain they will truly feel 'Here I am at home'." The 1950 Schuman Declaration spoke of "common foundations for economic development as a first step in the federation of Europe" a common market would create "a wider and deeper community" and "lead to the realization of the first concrete foundation of a European federation." The resulting 1951 Paris Treaty resolved "to establish, by creating an economic community, the foundation of a broad and independent community" – and alongside the treaty's free trade provisions also provided free movement for workers in the fields covered by the treaty – which were expanded significantly in the 1957 Treaty of Rome. Despite the gradual growth of European rights from the 1950s onward, EU citizenship's legal status

was confirmed only in the Maastricht Treaty, which entered into force in 1993. To some extent, this can be seen as a terminological delay. Indeed, Commissioner Davignon argued in 1979 that “the status of ‘Community citizen’ [was] officially recognized from the moment when the Treaties granted rights to individuals and the opportunity of enforcing them by recourse to a national or Community court” (Maas 2007).

The Treaties of Paris and Rome already prohibited any discrimination based on nationality among nationals of the member states, but the transformation of free movement rights from being defined and promoted in economic terms to being placed at the core of a new European citizenship was gradual. Free movement rights for workers were first justified in terms of enabling the free movement of labor and then as a measure to complete the single market. But they were extended and expanded even after the workers’ movement sufficient to support the common market had been achieved. This broadening of individual rights coincided with the growth of EU citizenship, which took decades to reach fruition—from postwar discussions to the Maastricht Treaty. Despite substantial support in the 1970’s for introducing European citizenship, the Community’s first enlargement (the UK, Ireland, and Denmark in 1973) stymied the process, but the two subsequent enlargements (Greece in 1981, Spain and Portugal in 1986) reinvigorated it. The eventual adoption of EU citizenship resulted not from Commission pressure but rather from bargaining among member states—including the three new Mediterranean members—and between member states and the European Parliament. With the Single European Act (SEA) in 1987, the Parliament had gained the power of co-decision, which helps explaining why the member states could afford to ignore the Parliament’s citizenship proposals before the SEA but accepted them in the discussions preceding Maastricht. Today approximately 14 million Europeans live in another EU member state, and intra-European migration increasingly resembles internal rather than international migration.

### **Free Movement in Latin America**

The introduction and expansion of free movement rights culminating in a common citizenship took decades to achieve in Europe. Analogous efforts in Latin America are nascent and will likely require many years, and similar political commitment. Currently the largest regional cross-border – not including internal migration, which can often be at least as important as international migration (Maas 2013b) – migrant communities are the Colombians in Venezuela and Ecuador, Nicaraguans in Costa Rica, Haitians in the Dominican Republic, and Paraguayans, Bolivians, and Chileans in Argentina, together accounting for over half (about 2.2 million) of the total 4.09 million intra-Latin American migrants (IOM 2012). This is, however, still less than the number of Latin American-born individuals residing in the European Union, around 4.29 million. Of these nearly 4.3

million Latin Americans in Europe, well over half reside in Spain (over 2.6 million people, chiefly from Ecuador, Colombia, Argentina, Bolivia, Peru, Venezuela, Brazil, the Dominican Republic, Uruguay, and Paraguay), with the next most important destinations the United Kingdom (424,000 individuals, chiefly from Jamaica and Brazil), Italy (358,000 individuals, chiefly from Ecuador and Peru), the Netherlands (335,000 individuals, chiefly from Suriname and the Netherlands Antilles), and France (156,000 individuals, chiefly from Haiti). Thus we can see both historical ‘brain drain’ to Europe (chiefly Spain) and North America (chiefly the United States) as well as more recent intra-regional migration.

There have been various efforts over the years to promote free movement of people within Latin America. The most advanced of these efforts are found in CARICOM and in UNASUR, which is in the process of consolidating the previous efforts of the Andean Community and of MERCOSUR:

## **CARICOM**

The Treaty of Chaguaramas established the Caribbean Community and Common Market in 1973, superseding the Caribbean Free Trade Association, which in turn had replaced the West Indies Federation. The Revised Treaty of Chaguaramas establishing the Caribbean Community, including the CARICOM Single Market and Economy (CSME), was signed in 2001. According to the article 45 of the revised treaty: “Member States commit themselves to the goal of the free movement of their nationals within the Community” (CARICOM 2001). Free movement of people is seen as “an essential factor in an ever closer union among the people of CARICOM Member States.” Article 45 on free movement “entails the right to seek employment in any Member State and the elimination of the need for work permits and permits of stay,” but its implementation has been subject to constant delays.<sup>2</sup> Of particular note is the CARICOM passport, which is a common format that has been gradually introduced since 2005 and, according to an official press release “is seen as a defining symbol of regionalism” (CARICOM 2009). Despite this rhetoric, however, the development of freedom of movement within CARICOM appears relatively limited.

## **Andean Community**

The Andean Pact was created by Bolivia, Chile, Colombia, Ecuador, and Peru by the Cartagena Agreement of 1969 and renamed the Andean Community (Spanish: Comunidad Andina) in 1996. Chile became an observer in 1976, while Venezuela joined in 1973 but left again in 2006 to join MERCOSUR. The Communi-

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<sup>2</sup> For more information see document at:  
[http://www.caricom.org/jsp/single\\_market/freemovementskills\\_socialsecurity.pdf](http://www.caricom.org/jsp/single_market/freemovementskills_socialsecurity.pdf) and  
 table, and  
[http://www.caricom.org/jsp/single\\_market/fulloperationalisationfreemovement.pdf](http://www.caricom.org/jsp/single_market/fulloperationalisationfreemovement.pdf).

ty's Decisión 504 of 2001 created a standard-format Andean passport for use in the member countries. Furthermore, in Decisión 545 the Community approved an Andean Labor Migration Instrument which provides for the relative free movement of workers between member states, as well as banning discrimination based on nationality against workers from other Community member states. In terms of its provisions, Decisión 545 resembles the early free movement provisions of the European Union.

## **MERCOSUR**

In 1991, Argentina, Brazil, Paraguay and Uruguay signed the Treaty of Asunción, creating the Southern Common Market, or MERCOSUR. The 1994 Protocol of Ouro Preto amended the Treaty of Asunción and transformed MERCOSUR from a Free Trade Area into a Customs Union. Free movement rights within MERCOSUR started in 2002 when the member states signed the Residence Agreement, which finally entered into force in 2009 after ratification by Paraguay's Senate. The Agreement is intended to resolve the situation of irregular migrants from within the region and "has transformed the migration regime for South Americans" because nationals of member or associate states "may reside and work for a period of two years in another member state if they have an identification document and a clean criminal record" (Acosta, Arcarazo and Geddes 2014).

Similar to the early years of European integration, the Agreement also provides "the right to work and equal treatment in working conditions, family reunion or access to education for children"; and it is even more generous than the early European free movement provisions because "sufficient resources do not represent a condition sine qua non" and the "permit may then be transformed into a permanent one after two years" if applicants can prove they have sufficient resources to sustain themselves in the territory of the host state. Bolivia (which is in the process of becoming a full member) along with Chile, Colombia, and Peru also observe the Residence Agreement. Venezuela became a full member in 2012 but (as of this writing) has not yet implemented the Agreement, nor have Associate members Ecuador, Guyana and Suriname.

Besides the Residence Agreement, of particular note within MERCOSUR is the Citizenship Statute, signed in 2010, which provides an action plan for full implementation on common citizenship on the thirtieth anniversary of the signing of the Treaty of Asunción, in 2021. The Citizenship Statute has three main objectives: free movement of people within the region; equal civil, social, cultural, and economic rights and freedoms for citizens of member states (comparable to non-discrimination on the basis of nationality); and equal conditions of access to work, health, and education (MERCOSUR 2010). Although the Statute sets some parameters for achieving these objectives, its decision-making procedures appear to be largely intergovernmental, based on bargaining between the

member states. Thus a prediction based on the European experience is that further institutionalization will be necessary for these objectives to be realized.

## **UNASUR**

The Union of South American Nations, usually known by its Spanish acronym UNASUR (Unión de Naciones Suramericanas; Portuguese: União de Nações Sul-Americanas, UNASUL; Dutch: Unie van Zuid-Amerikaanse Naties, UZAN), is a consolidation of MERCOSUR and the Andean Community – both discussed above – together with every other country on the South American continent except for the French Guiana, which is an overseas territory of France. In the area of migration, there is a policy of officially welcoming but covertly rejecting irregular migrants, which seems paradoxical when viewed from the lens of Europe or North America, where the official discourse emphasizes rejection while the reality is more liberal (Acosta Arcarazo and Freier forthcoming).

The UNASUR treaty lists one of the Union's objectives as "the consolidation of a South American identity through the progressive recognition of the rights of nationals of a Member State resident in any of the other Member States, in order to achieve a South American citizenship" (Art. 3i), and this idea is frequently repeated by government leaders. Most recently at the December 2014 summit, UNASUR general secretary Ernesto Samper emphasized that "We have approved the concept of South American citizenship. This should be the greatest register of what has happened". UNASUR citizenship includes creating a "single passport" and common educational rules to give South Americans the right to live, work, and study in any UNASUR country, similar to free movement within the EU (Robertson 2014). Together, the Andean Community, MERCOSUR, and UNASUR provide an exciting venue for the potential development of a continent-wide supranational citizenship.

## **Future Prospects**

A key reason for the success of European integration is the rise of individual free movement rights, which gives concrete rights and entitlements to citizens of all EU member states and prohibits discrimination based on nationality (Maas 2013c). Despite this success, however, the limits to European citizenship remain evident – such as the limited extent to which EU citizens have rights to access social assistance in a member state other than that of their nationality (Verschuere 2014). In any case, the "right of EU citizens to enjoy full social rights in their host state is closely related to their engagement in the performance of economic activities, as either workers, self-employed or service providers" (Mantu 2013: 463). Within North America, Canada's travel visas for citizens of Mexico are an affront to the idea of creating a common community and the egre-

gious misregulation of Mexican immigration to the United States also shows the limits of NAFTA free movement provisions. However, free movement efforts in Latin America show more promise.

One difficulty in comparing current developments in Latin America with the historical development of free movement rights and citizenship in the European Union is that concepts such as democracy appear to be understood differently in the two regions. For example, central governments in MERCOSUR appear “less committed to democratic consolidation based on citizenship and social inclusion than the EU assumes and, as a result, EU pro-democracy policies resonate less than expected. Local civil society actors, in contrast, do identify with EU understandings of democracy” (Grugel 2007). This matters because introducing a concept of ‘citizenship’ – as MERCOSUR and UNASUR do explicitly and the Andean Community and CARICOM do at least implicitly by focusing on free movement rights for workers – means negotiating not only intergovernmental agreements and photo opportunities for heads of state and government but also procedures and practices which will impact individuals throughout the region. Across Latin America, the construction of a citizenry has long been tied to the nation-building project yet, despite efforts to develop ‘modern’ citizenship, “the boundaries of citizenship in the region have been circumscribed by racial, spatial, class-based, and gendered hierarchies,” the development of civil and political rights is hampered by weak democratic institutions and rule of law, and social rights reflect persistent poverty, inequality, and lack of universal access to basic social services (Meltzer and Rojas 2014: 253).

The initial drafts for the TTIP negotiations pay passing mention of free movement for individuals, but focus mostly on mobility that is useful to business, such as intra-corporate transfers.<sup>3</sup> Similarly, despite promises in early drafts, the final treaty text of CETA, the agreement between the European Union and Canada, also does not mention a general free movement right for individuals but limits mobility provisions to temporary workers connected with business.<sup>4</sup> This relative absence of free movement provisions in the two trade agreements is regrettable, because inclusion would likely have strengthened the popular support for the agreements, as well as intensifying the benefits of freer trade. This is because the volume of trade increases greatly the more people know each other.

As John Helliwell has shown, the effect of a border is many times greater than that of geography or distance: one explanation for so-called “border effects” emphasizes that it is “cheaper and easier to operate within networks of shared norms and trust, and that the density of such networks declines with distance, especially as one crosses national borders” (Helliwell 2002). Networks and shared norms depend on two features: first, the movements of people, because

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<sup>3</sup> For more detailed information see <http://trade.ec.europa.eu/doclib/press/index.cfm?id=1230>.

<sup>4</sup> For more detailed information access [http://trade.ec.europa.eu/doclib/docs/2014/september/tradoc\\_152806.pdf](http://trade.ec.europa.eu/doclib/docs/2014/september/tradoc_152806.pdf).

personal contacts establish and maintain networks and trust; second, formal institutions to supplement informal personal networks.<sup>5</sup> So, too, we should expect that trade agreements will be more effective if they include provisions for the freer movement of people, not simply the freer movement of goods or capital. Furthermore, besides their anticipated positive effects on regional integration, free trade agreements might become more politically palatable if ordinary citizens can see the benefits not just for businesses and large corporations but also for themselves and others like them. This means that free movement should not simply be for goods or services or capital but also for people.

As the experience of NAFTA shows, alongside that of the emerging free movement regimes in Latin America, such a transition will not be easy to achieve. However, the counterexample of Europe provides some grounds for optimism, although in Europe the decades-long process of ever-expanding free movement rights culminating in European citizenship, though supported by national political leaders committed to creating a shared community, was guided and amplified by strong supranational executive (European Commission) and judicial (European Court) authorities, which for the moment are non-existent or embryonic in the Americas. The prediction, therefore, is that it will be difficult for free movement of persons in the Americas to quickly come to resemble internal rather than international migration, as has happened in Europe. Examples ranging from the denaturalization of Dominicans of Haitian origin to the continuing problematic status of Mexicans in the United States – contrast the hardening of the US-Mexico border with the softening and outright removal of border controls within Europe’s Schengen zone – support this thesis, although the rhetoric of free movement and shared citizenship in CARICOM, the Andean Community, MERCOSUR, and UNASUR may yet prove such pessimism unwarranted.

## Conclusion

A key element of regional integration in Europe has been the development of supranational rights and a common European citizenship. Since the first free movement rights for coal and steel workers in the early 1950’s, supranational rights for EU citizens have been extended to ever greater categories of people, reflected in the European Court’s oft-repeated assertion that “Union citizenship is destined to be the fundamental status of nationals of the Member States.” By contrast, efforts to foster individual free movement in CARICOM, the Andean Community, MERCOSUR, and UNASUR have so far been relatively modest. Nevertheless, each of those integration efforts are considering supranational rights, thus it is useful to ask about the prospects of common rights and perhaps

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<sup>5</sup> Under formal institutions, Helliwell includes “laws and the administration of justice, the design and implementation of standards, and the efficiency and quality of essential services, including (especially) health and education but also including the classic utilities – water, heat, light, power, and communications.”

eventually citizenship, focused foremost on the right of member state nationals to live and work elsewhere within the community.

This paper has argued that successful regional integration requires states to extend free movement rights to individuals, rather than simply promoting the free movement of goods, services, or capital. Against the backdrop of EU citizenship, the paper assessed current efforts underway in Latin America to create regional rights, including most notably free movement rights and citizenship analogous to those found in Europe. A tentative conclusion is that, while supranational rights are difficult to achieve, they help provide legitimacy for what would otherwise be simply free trade agreements with no benefits for ordinary citizens and therefore that the rise of common free movement rights perhaps coupled with a common citizenship is an important indicator for the success of regional integration beyond mere trade agreements.

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## **II. Europe and Latin America**



# **The Crisis of the European Integration Model and its Implications for Latin American Integration**

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## **Abstract**

The internal tensions and questions raised around the survival of the Economic and Monetary Union are among the main manifestations of the global crisis in the European Union (EU). The flaws in the Euro design are not the only problem that the EU is facing. There is an open debate surrounding common policies, budgetary mechanisms and institutional governance that are threatening the principles and method of the European integration model. This context suggests that the neo-functionalist theoretical indicators of regional integration have been losing analytical and explanatory power in what concerns understanding the strategic role of regional integration, especially in presence of the many questions that have arisen in recent years in Europe and in Latin America. The hypothesis of this article is that the crisis is directly affecting the theory of the European integration model, and indirectly affecting the method. In turn, this has an effect on the depth and continuity of the regional integration processes in Latin American countries that have taken European integration model as a reference for their own integration.

## **Introduction**

Since the establishment of the Euro in 1998, the European integration began to face an internal crisis regarding its own goals and challenges. This translated into at least fifteen years of crisis of the European Union (EU). The launch of this single currency seemed to be the culmination of an economic integration on its way to the next theoretical stage: political integration. European regional integration is compared to a bicycle that, in order to remain upright, must continue to move forward. Europe, therefore, must continue pedaling through a logical path traced by theory in order to gradually achieve its goals. After the Euro, what would seem to be the next stage in this cycling tour was the political integration of the EU members. However, the bicycle now seems to have interrupted its gradual march forward, and seems to have veered away from its integrationist course. In the current context, the European countries are weathering deep economic and social crises—and in more than one case, also political. It would seem that the European integration is partially at fault to be blamed for this prob-

lem, especially since it has shown little ability to find common solutions. Or at least, the proposed solutions *from Brussels* do not seem to suit the belief system that neo-functionalism has theoretically offered, inspired by the ideals set forth by Jean Monnet and the rest of the Founding Fathers. It would seem that national interests, especially German interests, weigh more heavily than the Community's welfare; that is, economic interests under a liberal approach.

The crisis calls into question the neo-functionalist theoretical perspective that could serve as a tool to interpret the evolution of European regional integration. It also situates the European countries at a series of crucial crossroads that could lead the European Union to a different destination, away from the logic of the integration model that not long ago it was heading towards. Some people would say that this is the end of a willful and solidary —Socratic and Christian— European integration; others would say that it is nothing more than a demonstration of Europe's pragmatism and individualism (Madariaga 1962: 50).

Undoubtedly, the European integration has raised interest and curiosity in Latin America. The process of European integration has been a benchmark for those in Latin America, like the Central American Integration System (SICA), the Andean Community (CAN) and the Southern Common Market (MERCOSUR). The EU founded an integration model heir to a historical momentum and ideas incited at the time by Monnet and subsequently by neo-functionalism. The European regional integration has accomplished many goals since its birth/conception, and it is because of this success that the regional process has earned the category of universal regional integration model. And, this is why the EU has served as an example that nourished the theoretical analysis, conceptual frameworks and methods on the regional integration literature. The EU displays a model, for many quasi sacrosanct, based on the transferring of sovereignty, the creation of supranational institutions, the development of mutual interests, and the search for prosperity and peace for all member states. The post-liberal regionalist processes —the Bolivarian Alliance for the Peoples of Our America (ALBA) and the Union of South American Nations (UNASUR), for instance, seem to move away from some of the principles of the aforementioned European construction. Therefore, the troubled European integration is also in crisis as a reference model for Latin American integration.

This context suggests that the neo-functionalist theoretical keys to Regional Integration have been losing analytical and explanatory power in understanding the strategic role of regional integration. Especially, in the presence of the many questions that have come up in recent years in Europe and in Latin America. The hypothesis of this article is that the crisis is directly affecting the theory of the European Integration model, and indirectly affecting the method.<sup>1</sup>

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<sup>1</sup> The analysis presented in this article is inspired by previous work by Romero and Caldentey regarding the keys to understanding the European regional integration process (Romero and Caldentey 2010).

In turn, this has an effect on the depth and continuity of the regional integration processes in Latin American countries that have taken European Integration as a reference for their own integration.

### **European Economic Integration and the Crisis: an Incomplete Task**

After the Second World War, prominent political leaders —Jean Monnet, Robert Schuman, Konrad Adenauer— had the vision and initiative to use regional integration to transform a devastated Europe into the EU it is today. Their fundamental objective was to create in Europe a land of prosperity, solidarity and peace. The Schuman Declaration of May 9, 1950 states: "Europe will not be made all at once, or according to a single plan. It will be built through concrete achievements which first create a *de facto* solidarity" (Schuman 1950).

The European integration project has gradually increased and grown until 2007, when the last of its most recent members joined —besides Croatia in 2013. What in 1952 began as a coal and steel common market has now become an imperfect economic and monetary union linked together by a common currency. Throughout this period, country membership has grown from six to 28. As Monnet once stated, "Within these vast country conglomerates, the common interest was too imprecise and the common disciplines were too relaxed. It was necessary to start with more pragmatic and, at the same time, more ambitious actions: an audacious and targeted attack on national sovereignties" (2010: 311).

This integration process, unlike others taking place in the rest of the world, did not only pursue commercial goals; it also had economic, social, and political aims. This was a trend intuitively defined from the early years by the Founding Fathers. Subsequently, and based on the European experience, the political and economic science scholars, close to the heat of the reality, conceptualized and created logical steps for the countries that wanted to walk the path of deep regional integration. They aimed at understanding the center of gravity that had pulled the European integration process into motion. But the question now is whether or not the regional integration method and model they proposed in order to achieve the economic, political and social goals for building an integrated community, are universal and mechanical truths for other regions such as Latin America.

Therefore, economically, the EU Single Market —under the 1987 Single European Act— had to be followed by an economic and then a monetary union; consequently, a single currency was introduced for most of the EU members. The existence of the Euro has brought changes in the European monetary institutions, as well as in the monetary policy of the member-states.

There are pending tasks that the 2008 crisis has fiercely forced onto the negotiations table. However, until now, there have been only timid attempts for resolution. There are still items on the To Do List, such as: the harmonization of tools and practices to ensure that monetary policy is truly unique, and the crea-



tion of a system that allows for the national central banks to implement a decentralized monetary policy and to make the most of national peculiarities. That is, a comprehensive common policy that should support the employment, growth, and stability of the community as a whole, while paying attention to the particularities of the member countries.

Although, it is known, the crisis has exposed the economic and monetary union in the EU as an incomplete regional integration stage. The telluric forces that triggered the crisis of 2008 have seriously damaged the European edifice, revealing its vulnerabilities. Now the cracks have allowed the architects to identify where the construction failures are. However, the countries are not arriving at a consensus on how to approach the building repairs. As a consequence, they are not taking actions that are aligned to the community logic (model and method) that is drawn by neo-functionalism and the *spillover effect* (Hurrell 1995: 59-61). Presently, a more effective policy would be to implement common financial tools and community fiscal integration. All these implications further reduce national sovereignty —*more Europe*; but, the political will has not come this far yet. It gives the impression that the structure is propped up by scaffolding while the next course of action is determined.

As the British leaders have proposed more than once, the best course of action would be to fortify the European building from different bases: a free trade zone and intergovernmental cooperation, nothing more. This was precisely the British position during the large EU expansion in 2004. The discussion among the members was either to follow the way of incrementalism or the way to deep integration stages and common policies. The *Anglo-European Dream* seems impossible, but who knows? In hindsight, it is possible to see that Germany and the other member-states interest in the markets of Eastern European countries look for the achievement of wider expansion, thus sacrificing depth.

But beyond the traditional British case, now other EU member-states are also showing interest in curbing the logic of the progress of integration through the strengthening of supranational institutions. Some examples are the discussion about the nationalization of some policies covered by the common budget; the unilateral announcements of the adjustment of internal policies adopted in the Schengen framework; the factual modification of decision-making outside the EU institutions; or the lack of progress towards a common fiscal policy.

### **European Integration and Political Crisis: an Increasingly Faraway Task**

In the 1950's, the European integration was forged by guaranteeing prosperity and peace through supranational institutions and decisions that were based on the common interests of member-states. And since its birth, the EU has aspired to achieve political integration to ultimately become a regional state, that is, a new political entity different from the traditional nation state. But, the problems and obstacles that the EU has been facing do not seem to augur a politically integrat-

ed Europe in the short term. As Monnet stated: “All my reflections and observations lead me to conclude what is already my profound conviction: the effort that the western European countries make to raise to the challenge of the circumstances, the danger that threatens us and the American effort, need to become a true European effort, only possible if a Western federation were to exist” (2010: 310).

As mentioned already in this work, the process of the European integration inspires neo-functionalism. The authors of this article are convinced that in order for regional integration to be successful and beneficial to each of its member-states, it is necessary to build supranational institutions to which in certain matters the states cede part of their sovereignty. Under this approach, the traditional nation-state, the main institution of modern political order, loses its strength.

The neo-functionalists believe in the spillover effect. When members of an integrationist group are creating greater interdependence among each other, the ensuing process of cooperation between these countries will inevitably lead to integration of a higher and deeper order; not only economic but also political. The mechanical process is to go from a customs union to an economic and monetary union and from a complete economic integration to political integration (Hurrell 1995).

Despite the fact that the EU is the inspiration for this neo-functionalist approach, starting from the Nice Summit in December 2000, the EU has faced serious difficulties to further the deepening of its integration process. Progress in the EU seems to have become increasingly intergovernmental because matters of high policy remain in the hands of the European Council and the Council of the EU. Autonomous and supranational institutional platforms, like the European Commission or the European Parliament, still lack decision-making capacity. Under the logic of neo-functionalism, it is difficult to explain the current dynamic of the EU next to its challenges, questions, and deepening integration. However, many scholars and politicians, despite understanding the current reality, still cling to the idea that the integration progress is irreversible. Now, more than ever before, the belief in the idea of irreversibility is being challenged by less dogmatic approaches.

On the way to political integration, and after its recent expansion—for historical reasons and to maintain the balance of power—the EU has kept supranational and intergovernmental institutions that limit Germany’s hegemonic action; but also, to timidly move towards more democratic forms of decision-making. The distribution of votes according to each country’s population gives greater democratic legitimacy to the European process. Naturally, however, it ends up favoring Germany, the country with the largest population among member-states, while at the same time eroding the previously accepted hegemonic balance of power in Europe. If it has not already, it could produce the Franco-German alliance that has historically been the backbone of the European integra-

tion process. In 1952, Michel Debré pointed out that "for the sake of Germany itself, Europe must not become a German Europe" (Monnet 2010: 411). A Europe, the German Europe, should be avoided because it will not bring anything good to Europe. In the context of the current crisis, this idea has often been repeated on Debré's same track. "In 1953 the novelist Thomas Mann appealed to an audience of students in Hamburg to strive for 'not a German Europe but a European Germany'. This stirring pledge was endlessly repeated at the time of German unification. Today we have a variation that few foresaw: a European Germany in a German Europe" (Beck 2013: vii-viii).

Existing institutions, beyond the lack of genuine democratic supranational institutions, do not limit Germany's hegemonic capacity. However, they keep it relatively under the control of other EU countries. The European project has been made viable since the end of World War II, therefore, because of the dominance of the non-democratic criteria in the European Council, in the Council of the EU, and also to a lesser extent, in the Parliament.

### **Latin America, the Model of European Integration and the Crisis**

The process and model of the European integration for many years has had a special echo in Latin America. Politicians have taken European integration as a buzzword to try and give credibility to the rhetoric on their own discourses on regional integration. And, it must be said, they have achieved little success on reaching the goals of their own regional integration process and in the impact on Latin American peoples' welfare. In most cases, the intellectual, political and economic elite in Latin American countries have adopted speeches, looks and aspirations from abroad. This created a foreign-focused view of integration — especially attentive to the European model— that is common in the region. Latin America holds this approach due to its Socratic-Christian heritage that hails from Europe, which rhetorically aligns the Latin American system of beliefs regarding integration with the Mediterranean and Continental European views of integration (Madariaga 1962: 50-65).

Because of the referential power of the European integration, neo-functionalism has been the theoretical base for many of the integration processes in Latin America. SICA, CAN, and MERCOSUR are clear examples of its influence on the Latin American regional processes of integration. Such European influence is notable in their original institutional design and in their group goals. However, in the praxis of these processes —when it is necessary to implement the method— visible outcomes have been just a few and those few results have slowly been fading since the nineties. Their regional integration agreements have not really grown out of the field of theoretical proposal and aspirations.

However, other regional groups around the world have often questioned the European integration model and method. In the work *A Grand Illusion? An Essay on Europe*, published in 1996, the historian Tony Judt values the achieve-

ments of the European integration but attributes them to a unique and unrepeatable fact in history that does not respond to a logic (a model) that can be projected indefinitely into the future. For Judt, the European integration as a model is an illusion. Although the author does not mention the European integration as a reference model for others, it is clear to us that he would consider it another illusion (Judt 2011: 3-44). As Tanja A. Börzel reminds us, the early studies of compared regionalism revealed that the integration effort of developing countries that took European integration as a model remained largely ineffective. Ernest B. Haas goes even further in his works published in the 1970's, declaring the invalidity of the model (Börzel 2011: 7).

Independently from what has been previously stated, the idea of regional integration is incredibly powerful in the Latin American imaginary from the nineteenth century onwards —*La Patria Grande* (the Great Homeland). This is why regional integration groups from the past have survived, and in the last decade, new ones have been created, as ALBA and UNASUR. These new South American integration processes are presented as a regional proposal with economic, political and social goals, but without a supranational institutional structure that allows for the fulfillment of these deep and wide integrationist aspirations. Malamud and Gardini even argue that regional integration is no longer an option for Latin America, and the space left available from the disappearance of a deep regional integration model is being occupied by the rhetoric of politicians. And this rhetoric is neither a model nor a method (2012: 131).

There is no true reproduction of the European method in any of these integration processes conceived to respond to the aspirations of the Latin American integrationist tradition. ALBA seeks to free itself from the European model and has created a different one. As such, the European integration model is still in the foreground in Latin America. In the cases of SICA, CAN and MERCOSUR, where the European model is still kept as a reference, the designed method has been approached ineffectively. Moreover, in the new aspirations like UNASUR, the European method benchmark disappears even in rhetoric. Surely this shows a referential loss of the European integration model considered as valid for Latin American countries.

## Conclusions

The European process launched by the Founding Fathers more than five decades ago conceived to end war in Europe once and for all, is in crisis. As a consequence, the theoretical model that stemmed intuitively from the process, and the method to make it work, are also in trouble. The search for peace has seemed to lose strength as a leitmotiv for the process. Also, the idea of reunification after the fall of the Berlin Wall, that could somehow be an updated version of the motivation for peace, is also weakened. The theoretical framework for regional integration no longer has the analytical and explanatory power to face the many

questions that have come up in recent years. At the end of the twentieth century, the duties of economic European integration seemed largely fulfilled, and it looked like the process had matured enough to enter into its next stage, political union. Therefore, it is paradoxical that European integration has entered into a crisis from which it still has not recovered, and which has only deepened since the 2008 crisis and aftermath.

Given the above, we can say that the crisis faced by the European integration model has become an almost incontestable fact, undoubtedly amplifying the economic and social crisis in its member-states since 2008. European integration has thus emerged as a process unable to consolidate through consensus its own progress, as measured by the goals set by the countries. And it is not able to respond—from the supranational space—to the problems faced by member countries.

This calls into question the neo-functionalists' ideas, Monnet himself, and of course any understanding that attempts to generalize and systematize the current progress of the European regional integration. When there is a crack in the belief system on which European integration has been built, instead of more integration, Europe has less integration. This leads us to wonder whether there could be a real regional integration with a theoretical framework and method different than the one proposed by neo-functionalism and Monnet. The sub-regional integration processes in Latin America are certainly suffering the effects of the theoretical and practical references to the European process, as well as the changes in the relations between the European Union and Latin America.

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# **The Effect of the TTIP on the BRICS Countries: The Case of Brazil**

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## **Abstract**

This paper seeks to evaluate the potential impact of the Transatlantic Trade and Investment Partnership (TTIP) on the BRICS countries. One of the responses to the economic international crisis was the European Union (EU) and the United States decision to create a High-Level Working Group (HLWG) in order to boost transatlantic trade and investment between super powers. The inter-regional initiative was to adopt a more creative, flexible, and "open-minded attitude" in order to find solutions for advancing negotiations between the trade partners. This initiative emerged at the 2011 EU-US Summit, where leaders instructed the Transatlantic Economic Council to establish the HLWG, whose mandate is to identify and assess options for strengthening transatlantic trade and investment. Then, the largest bilateral trade agreement in the world appeared as the "agreement of the century": the TTIP. This raises two important questions: What impact will the agreement have on the relations between BRICS countries? What alternative strategies do they have to face a new balance of power?

## **Introduction**

Two major events challenged the balance of power at the turn of the century: the rise of emerging markets such as the BRICS countries (Brazil, Russia, India, China and South Africa), and the unpredicted international economic crisis, which affected the two largest world economic powers: the European Union (EU) and the United States (U.S.). More specifically, China has emerged as a player that must be taken into consideration when talking about international politics nowadays. One can say that China has changed the International Division of Labor (IDL), as large economies, such as the U.S., and emerging markets, such as Brazil, depend on Chinese imports and exports.

It is no coincidence that there have been several initiatives on transatlantic cooperation between the EU and the U.S. – between their corporations and their governments – since 1995. The foundation of a New Transatlantic Agenda (NTA) and the Transatlantic Regulatory Cooperation (TRC) initiatives has contributed to the progress of reducing costs for businesses and consumers in a few sectors of the economy in both regions. Since then, a number of advances have



quietly been made.<sup>1</sup> The global crisis accelerated cooperation efforts and led European and American leaders to instruct the Transatlantic Economic Council to establish a new joint High-Level Working Group (HLWG) in 2011. The HLWG serves to identify and assess opportunities for strengthening transatlantic trade and investment, especially in areas that have the greatest potential to support jobs creation and growth. Its primary goal was to respond to the specific characteristics of transatlantic economic relations “by identifying policies and measures” to increase the EU-U.S. trade and investment and foster “mutually beneficial job creation,” economic growth, and international competitiveness. The leaders’ main concern was to minimize the impact of the U.S. crisis and the sovereign debt crisis in the Eurozone on inter-regional trade. The hidden goal however, is to join forces to face the new international scenario, in which China has become both a key partner and a potential threat at the same time.

### **The Very First Boost**

Together, the EU and the US have the largest bilateral trade and investment volumes in the world: roughly 31 percent of world trade and over 49 percent of the world GDP is concentrated in these two regions. Approximately one trillion dollars in goods and services are traded between the two each year and they invest nearly US\$ 4 trillion in each other’s economies. All of this supports around 13 million jobs on both sides of the Atlantic.

The EU-U.S. HLWG was founded to enhance transatlantic trade and investment between the EU and the U.S. by adopting a more “flexible” and “open-minded attitude” towards the development of solutions for negotiations on trade. The HLWG establishment, however, coincided with the emergence of several new outlooks on trade in the aftermath of the failed multilateral trade negotiations during the World Trade Organization (WTO) Doha Round. In this context, the 2012 report of the Transatlantic Task Force on trade focused on the need for a new understanding of several aspects of transatlantic relations. The acceleration of negotiations looked for a deeper bilateral transatlantic economic integration as an essential procedure to recover from the economic crisis. The report remarked that the EU and the U.S. could “exercise the leadership required to kick-start global trade liberalization, strengthening the multilateral trading system” (GMF 2012). However, the acceptance of common principles and standards has been perceived as a key initiative to boost trade and investment between Europe and the U.S.; the exact same method was used in the EU to consolidate its common market. Indeed, since the 1990s, both the US and European multinational companies have expressed divergent views on what is the best way to regulate goods

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<sup>1</sup> A comprehensive study on different activities and sectors that could be regulated is still in progress. Even so, it has been confirmed that the areas that will be affected include antitrust or competition procedures, consumer protection, environmental regulations, manufactured and industrial products, etc.

and service markets, as regulations are considered the main barrier to transatlantic trade. The main reason why these companies seek to achieve greater harmonization in standards and regulatory procedures is to reduce the costs arising from the need to comply with two different sets of regulations and standards. Regulatory cooperation is an umbrella concept that incorporates a broad range of activities.

As one of the most ambitious initiatives aimed at achieving strong convergences and aligning policies, the TTIP emerged as the largest inter-regional agreement, which earned the title of “*the agreement of the 21<sup>st</sup> century.*”

As other economic and political heavyweights look for new joint projects in the East, the EU and the U.S. have accelerated negotiations aimed at constructing a free avenue for trade and investment cooperation as a major goal in their own foreign policies. The Obama administration’s economic policy treats the creation of high-standard trade rules as a vital issue for the global economy. The TTIP is expected to reduce the costs companies incur while engaging in transoceanic trade, which will make products and services less expensive. Although it is still too early to assess the impact of this bilateral partnership on third countries, corporations and business groups from the BRICS countries are becoming concerned with the future preferences of the EU and the U.S. negotiators.

### **What are the Promises that Have Been Made?**

Contrary to what happened over the past two decades, progress in emerging markets is now slow. Currently, advanced economies are growing more and emerging economies are growing less. However, China is, as always, the exception among the BRICS. Its growth forecast pointed to acceleration over the course of the year, after achieving a growth rate of 7.7 percent in 2013 (est.).

The U.S. has also demonstrated its strength once again. It has obtained positive results in the housing industry, business investments, and employment. The housing industry grew at an annual rate of 12.9 percent in May 2013 (Thomas 2013), which represented the fourth consecutive quarter with a double-digit growth. The U.S. unemployment rate dropped to 7.3 percent on August 2013, which was the lowest it has been since December 2008. Furthermore, Europe soon started to join the U.S.’s recovery.

In addition to showing signs of recovery, the EU and the U.S. appear ready to deepen their economic partnership. Once the TTIP is in place, gains are expected to reach 86 billion euros per year for the EU and 65 billion euros for the U.S. European business executives say that 80 percent of the benefits of the agreement would result from the reduction of regulatory burdens and bureaucracy, as well as from the opening up of the services and public procurement markets. Once the deal is fully implemented, it is expected that every year, an average European household would earn an extra €545 and the European economy would be boosting its GDP approximately 0.5 percent a year.

It is estimated that EU corporations will sell an additional €187 billion of goods and services a year to the U.S. This is good news for jobs. Surveys commissioned by Bertelsmann Foundation revealed, however, that incomes in the U.S. would rise 13.4 percent per capita thanks to the TTIP, whereas those in Europe would only increase 5 percent. Even with this unequal distribution of the agreement's benefits, Europe will lose more if the TTIP does not go through, since it has fewer options compared to the United States. Around 43 percent of Americans believe that the TTIP will help the U.S. compete with China, and therefore, support its approval.

Overcoming its internal asymmetries will not be an easy task for the EU. Europe is experiencing serious problems of competitiveness due to the economic difficulties countries in the south of the continent, such as Greece, are having. Furthermore, there are major differences in the financial rules and exchange rate policies that will have to be revisited in order to comply with the TTIP. Finally, the EU's institutional procedures on treaties require all stages of negotiation to be approved, which takes time.

In this scenario, according to the Trade Regulator Cooperation report, it is important to take note of two policy options that can indeed bolster cooperation. The initiatives to reinforce these two policies have demonstrated their capacity to vitalize transatlantic cooperation: (1) attracting high-level political support, and (2) dramatically increasing the involvement of legislators (the U.S. Congress and the European Parliament).

The first policy is related to the creation of the Transatlantic Economic Council (TEC) in April 2007. The Council was designed, in part, to generate the kind of high-level political support that previous initiatives lacked. In other words, the institutionalization of cooperation can create conditions that are more conducive to defining the terms for the partnership's development, by clarifying what steps are needed to reach an agreement and identifying the limits of procedures that must be improved.

The second policy is quite important considering the predominance of the executive branches as a driving force for cooperation. The involvement of the legislative branch could facilitate the harmonization of regulations. Regulation of standards and measures are necessary in both domestic and international markets. In an increasingly integrated transatlantic market, Parliaments will be called upon to balance the often-competing demands of trade expansion and barrier reduction, on the one hand, and domestic health and safety concerns on the other.

The Obama administration clearly seeks to make this partnership a more popular and visible initiative. Thanks to the president Obama's efforts, the cooperation debate, which began quietly, is no longer a matter of importance only for the country's political elite. Indeed, the increased involvement of legislators can provide the democratic impulse needed to overcome the TTIP criticism in the U.S.

## **Brazil and China in the Context of the BRICS**

The BRICS countries joined to form a group of emerging economies that aimed to introduce changes to the liberal international order established after World War II. The group's creation has led to the reordering of international coalitions, the search for new opportunities to pool interests, and the optimization of efforts on development and economic growth in the existing liberal order. It is no coincidence that most of the BRICS countries have vast territories, large populations, and a varying number of neighbors with whom they need to accommodate their interests. Another important element is that the BRICS countries are natural regional leaders, which can be involved in regional integration efforts. They also face problems of poverty and inequality anchored in historical processes of social divisions left by the legacy of dictatorships and longstanding poverty. Their indexes on human development and inequality reflect the violent past and social unrest these countries experienced throughout their history, which differ significantly from the data of developed countries. This means that the BRICS group must have a dual purpose: in addition to improving their position in the international market, they need to solve parallel problems involving domestic policy reforms, social policy adjustments, decreasing violence, poverty and inequality.

The decision to create a common development bank was developed during the fourth BRICS Summit held in New Delhi in 2012, which was subsequently announced at the group's fifth Summit in Durban in 2013, and finally plans were put into motion at the sixth Summit in Brazil in 2014. The BRICS bank was created with the purpose of increasing the weight of the BRICS countries in the global governance of international finance institutions, which could represent an improvement of multilateral strategies of the emerging powers.

In regards to trade, the last two decades have been very lucrative for both Brazil and China. Thus, Brazil must address the asymmetries in its bilateral exchange with China through changes to its industrial and innovation policies, such as new legislation (tax reform, for example) and development agencies to increase the competitiveness of Brazilian firms and add value to its exports. Although domestic political battles and institutional imperfections are a major source of Brazil's lack of competitiveness, Brazil's trade policy has been lacking a more liberalizing agenda. Furthermore, to increase their absorptive capacity for foreign direct investments, both China and Brazil would benefit enormously from strengthening institutions capable of curbing corruption through checks and balances.

Brazil's geography is abundant in natural resources and has excellent environmental conditions which could be used to enhance the role of agriculture as a component of its "soft power" strategy. In addition, to the abundance of mineral resources and arable land, it has additional resources that can be used by Southern American countries. Like Brazil, China will continue to benefit from a strong

domestic market and a sophisticated industrial economy in the future. However, the agreements between China and Brazil are still limited, as both countries' maintain strong trade relations with the EU and the US.

According to a FitchRatings report from 2012 entitled "China's Economic Rise Provides Mixed Benefits for Latin America," overall, Latin America has benefited from its relationship with China, as it has brought higher commodity prices, increased growth and investment, and improved their governments' finances. However, as a result of Latin America's specialization in commodities and China's transition into a higher value-added manufacturing exporter, 92 percent of Latin American exports to China were commodities, according to the FitchRatings in 2010. Therefore, Latin America's long-term position in this partnership is weak, other sources for growth and trade, such as services, should be pursued.

China is Brazil's main trading partner; it was the destination of approximately 19 percent of Brazilian exports (followed by US, 10.2 percent and Argentina, 8.1 percent) in 2013. However, Brazil is not listed as one of China's top ten trading partners. Although the two countries are partners in the BRICS, they do not seem to be building a typical South-South relationship. As Pereira and Neves (2011) have remarked, "the two countries do not constitute a South-South exchange (a balanced exchange between developing countries), as official Brazilian rhetoric may suggest, but rather an increasingly North-South relationship — with Brazil as an exporter of commodities and an importer of manufactured goods from China." In 2013, the top three Brazilian products and their derivatives exported to China were soybean (50 percent), iron ore and concentrates (28 percent), and oil and derivatives (6.7 percent). Conversely, the top three imports from China were machinery and electrical appliances and parts (30 percent), machinery and mechanical appliances and parts (20 percent), and inorganic and organic chemicals (6 percent) (China-Brazil Update 2014). On the one hand, strong trade relations do exist between China and Brazil, which has led the Brazilian government to invest in strategic sectors, such as industry and technology. On the other hand, the goals and features characterizing South-South cooperation are not present in this relationship. This complex scenario demands a change in attitude or focus from Brazil in order to face this rising Asian giant, instead of expecting China not to pursue the optimization of its advantages in the global economy.

### **Brazil in the Context of the US-EU Partnership**

The TTIP follows the trend of focusing foreign policy on regionalism. The BRICS countries are clearly grounded in regional political alliances, while, at the same time, they seek to develop multilateral relationships. The goal of joining free trade zones is far from being just the privilege of the wealthier nations as before. On 2012, Colombia, Mexico, Chile and Peru signed the Pacific Alliance agreement, which established zero tariffs for 90 percent of goods traded between

them. Chile and Peru joined the group of countries involved in the Transpacific Trade Partnership (TPP) negotiations, which includes nine countries on both sides of the Pacific Ocean and promises to boost trade with Asia. Brazil, on the other hand, has been trying hard to play a leadership role in MERCOSUR and enhance the consolidation of the common market since 1990's.

Brazilian foreign policy is constrained by its involvement in MERCOSUR and its relations with Argentina. Argentina buys most of Brazil's semi-manufactured export products, but, is currently experiencing a domestic crisis that is affecting its imports from Brazil. As Argentina is Brazil's third largest trading partner, behind China and the US, every drop in Argentina's economic growth or retraction of its economy means a loss of several millions of dollars in foreign trade for Brazil. The slowdown of the Argentine economy in 2012 made Brazilian exports fall 20.7 percent, according to economic consultants in Buenos Aires. The most affected sectors by the decline were the auto parts industry, agricultural machinery and electronics, among others.

MERCOSUR has become less of a project of regional economic integration and trade, and more of a political forum in recent years. After the barring of Paraguay in 2012 and the admittance of Venezuela as a full member, MERCOSUR has been seen as a political platform rather than a framework for regional development. However, the worse may be yet to come. According to Peña (2014), the future of MERCOSUR can be directly associated to the development of both multilateral instruments, like the WTO, and interregional ones, including the TTIP and the TPP. Even considering that the impact of TTIP on Latin American countries will vary, members of MERCOSUR, such as Brazil, would suffer from the adoption of new standards and intellectual property rights rules. The success of the two major transoceanic treaties will affect other multilateral mechanisms for regulating trade, which means that the global multilateral trade system is about to be impacted to an extent that cannot be foreseen yet.

Brazil's situation is so complex that even if MERCOSUR accelerates talks with the EU, cooperation with Europe will still take years to materialize. When Brazil was classified as an upper middle-income country, it lost some of the advantages it had in its trade relations with the EU, which turns the acceleration of the MERCOSUR-EU negotiations into a matter of survival. The WTO Generalized System of Preferences (GSP) reduced import tariffs on a number of items sold by developing nations. The recent loss brought by Brazil's change in status still needs to be calculated and new strategies need to be found urgently. In 2012, Brazil was the third largest beneficiary, with sales of US\$ 2.3 billion, behind India and Thailand. In all, the U.S. concedes this advantage to 127 countries and territories under the GSP. As a result of the change, approximately 3,500 products used by the Brazilian auto parts, construction, chemical, steel, capital goods and food industries now have to contend with full tariffs.

Moreover, Brazilian exports of steel, machinery, fuel, beef and cotton now face greater competition when selling to Europe, as the US produces the

same products. For airplanes and cars, products manufactured in Brazil come up against strong competition in the US from European products, and from US products in the EU. Brazil's growing trade deficit increases the urgency for the country to make new deals. Indeed, there are two potential scenarios for Brazil: it can either bring new life into MERCOSUR, or it can look for a way out of it. There is no road in between. While Chile and Peru are signing free trade and bilateral agreements with the US, the EU and China, Brazil shyly continues to wait for MERCOSUR to make a move.

The EU is an important market for Brazilian commodities. In 2012, Brazil exports to Europe totaled US\$ 48.8 billion to Europe, of which US\$ 24.3 billion were commodities, namely agricultural products. Altogether, the European market was the destination of 20 percent of Brazilian exports. In the 1990's, that figure was more than 30 percent. However, during fifteen years of negotiation, both sides have missed deadlines and compromises. Even so, there are new expectations that talks will move faster in 2015, which could be decisive for Brazil. If they do not, there is a possibility that preference will be given to the U.S. as an exporter of agricultural commodities to the European market, which will directly affect the Brazilian economy. In this context, Brazil has just assumed the rotating presidency of MERCOSUR and thus, it is in a good position to make concrete advances on the free trade agenda. This could be a good opportunity for breathing new life into inter-regional cooperation.

## **Final Notes**

There is a disconnection today between the way business operates beyond borders and the methods governments use to pursue international trade. A comprehensive joint action to regulate international trade among big corporations, global economic groups, and governments is obviously at needed. The EU and the U.S. already control about half of the supply of services in the world and account for one third of the global trade of goods. Although the two economic superpowers are still recovering from the crisis, there are reasons to believe that the TTIP will accelerate and achieve new forms of cooperation between the regions, and generate millions of euros of savings for companies. While the full consequences of the TTIP are still unknown, it is clear that the two major powers are pushing ahead with transoceanic agreements in order to establish a new global commercial order in which the balance of power would be completely different from predictions on the rise of the East.

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# Health-Related IPR Provisions in FTAs in the Atlantic Community

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## Abstract

This chapter addresses Intellectual Propriety Rights (IPR) clauses in FTAs in the Atlantic Community that impact the right to health. The chapter also discusses why health-related IPR provisions are so controversial in trade negotiations and how national (and regional) courts are trying to solve the problem of balancing IPRs and the right to health.

## Introduction

Since the 1990s, Free Trade Agreements (FTAs) which seek to deepen bilateral, inter-regional and region-to-country economic relations have proliferated in the Atlantic Community. Some regional groupings such as the Andean Community of Nations (CAN) or MERCOSUR have lost some terrain and sometimes had to adapt their rules to allow the signature of FTAs by their member states. Simultaneously, trade agendas have been politicized and the social agendas are more prominent in new groupings such as UNASUR. Other new regional groupings such as the Pacific Alliance or the Transatlantic Trade and Investment Partnership (TTIP) projects continue to focus on trade, strengthen IPR, seek International Technology Transfer (ITT) and go beyond the standards of the World Trade Organization (WTO). In the area of health, the main issues at stake are global access to medicines and global IPR protection in order to stimulate R&D (Mercuro 2006:38-40; Sell 2011).

## IPR Clauses in FTAs and the Right to Health

The new generation of FTAs includes some conditionality related to the duty to respect human rights (HR) (Bartels 2008), but the EU and the U.S. HR conditionality in FTAs refers mostly to first generation rights, giving Economic, Social

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<sup>1</sup> The authors thank Yentl Clijmans and Jania Silva for their help with data collection.

and Cultural Rights (ESCR) only a marginal role except for some labor standards of the International Labor Organization (ILO) included in the US FTAs.

The ESCR Committee of the UN<sup>2</sup> and other organisms such as the World Health Organization (WHO) have identified potential negative effects of Trade-Related Aspects of Intellectual Property Rights (TRIPS+)<sup>3</sup> clauses in the EU and the US FTAs and expressed doubts on whether increased protection of IPRs effectively supports R&D in health for the general benefit (’t Hoen 2003; UN-ESCR Committee 2010: 10-1; Ely 2003). In fact, instead of recognizing the positive effects of TRIPS+ protection of IPR on innovation (Mercurio 2010), their possible detrimental effects on the access to medicines have been identified as follows: (i) *broadening patentability or the ever greening of pharmaceutical patents*, (i.e. the registration of new forms and new uses of known substances to extend the patent by modifying the molecules which “do not significantly improve the therapeutic effect of medicines”); (ii) *restricting patent oppositions*, seeking to avoid “*patent applications that do not fulfil the requirements in national legislation for granting the patents;*” (iii) *extension of patents beyond the TRIPS protection*; (iv) *introduction of Test Data Exclusivity and a Patent-Registration Linkage*; and (v) *IP enforcement requirements* (e.g. by seizing generics in transit) (UNDP-UNAIDS 2012; Nasu 2010).

The Doha Declaration on TRIPS and Public Health of 2001 (DD 2001) sought to enhance flexibility to the TRIPS enforcement in case of a public health crises in developing countries (Crook 2005: 545, 550; UNDP-UNAIDS 2012; Roffe and Spennemann 2006:85-6). Although in the Special 301 Report<sup>4</sup> of 2013 the U.S. recognized the scope DD 2001, it did it under the condition that “*market access barriers that U.S. pharmaceutical and medical device companies face in many countries*” had being reduced (USTR 2013:22-3).

Until 1994, when NAFTA and the European Economic Area were signed, no FTAs included binding IPR rules yet. The CAN was a pioneer in including IPR rules into its regulation but the scope of these rules is not clear (Kohl et al. 2013). Table 1 offers a panoramic view of the inclusion of IPR clauses in FTAs in the Atlantic Community and indicates whether they are binding or non-binding. These results should be carefully analyzed provided that in recent years, IPR-related investment rules are being included in FTAs as it is the case of Canadian FTAs. The table shows a clear trend over time: binding clauses on IPR are becoming a constant in FTAs. A more detailed analysis should confirm the idea

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<sup>2</sup> The right to health is recognized in the Universal Declaration of Human Rights (UDHR) (25) and in the International Covenant of ESCR (ICESCR) (12). General Comment 14 of the ICESCR Committee defined the content, implementation and enforcement of the international right to health.

<sup>3</sup> TRIPS+ clauses increase the protection of IPR beyond the parameters of the TRIPS (see Horn et al 2009).

<sup>4</sup> The annual global review of IPR protection and enforcement by the Office of the US Trade Representative (USTR).

that the EU and the U.S. include binding TRIPS+ clauses whereas south-south FTAs agreements include binding clauses while staying within the TRIPS framework.

TRIPS+ clauses in FTAs involving the EU and the US are strongly contested by some emerging economies but IPR protection through investment clauses has been a low profile mechanism. This new modality of TRIPS+ clauses by means of including IPR in the definition of investment in the Bilateral Investment Treaties (BITs) and in some investment clauses of FTAs represent a threat to the DD2001 because it opens new ways to protect IPR (investor-state dispute settlement mechanism for investments involving IPR, market value compensation for losses and prohibition of direct and indirect expropriation) at the cost of universal access to medicines (Benedict 2012; see also Ruse-Khan 2011b, 2014a).

Table 1: IPR provisions in FTAs in the Atlantic Community

FTAs entered into force in:	Number of FTAs in sample:	Of which FTAs,		
		without IPR clauses	with non-binding IPR clauses	with binding IPR clauses
1950s	1	1	0	0
1960s	1	1	0	0
1970s	6	6	0	0
1980s	2	1	1	0
1990s	16	10	0	6
2000s	25	9	3	13
2010s	13	2	0	11
<b>Total:</b>	<b>64</b>	<b>30</b>	<b>4</b>	<b>30</b>

Sources: Kohl et al. (2013) (FTAs until 2011), <http://rtais.wto.org/UI/PublicAllRTAList.aspx>, and texts of FTAs taken from government websites.

## The Economic Importance of Pharmaceutical Trade and Investment

Health-related IPR provisions matter from an economic perspective because of their effect on the cost of medicines (Andia 2011; as quoted in Lamprea 2013:28). Price controls of medicines have been proposed by governments, mostly designed by taking as a reference a basket of international prices to guarantee a good allocation of governmental resources. Another issue is the development of generic medicines once patents expire.

Recently, the development of bio-generics has led to even more complexity than with chemical generics; biological medicines represent almost 30 percent of the pharmaceutical market in some countries where they are mostly

financed by the public health systems (Minsalud 2014). In this market, the discussion on patent flexibility is less relevant than the technological capacity of developing countries to regulate these processes and to produce bio-similars. The U.S. and the EU and their biotechnological industries are expressing concerns about the enforcement of the DD 2001 in this respect and they are addressing these issues to the WTO as they concern not only IPR but also Technical Barriers to Trade (TBT).

In Latin-America, some countries are trying to regulate the market to allow the commercialization of bio-similars, but it remains a huge challenge and therefore, regional (and south-south) cooperation is being proposed to deepen market regulation and production without the intervention of U.S. and EU pharmaceuticals and strong emerging economies such as India and Brazil are leading the way (Feijó et al. 2012, 2014; Lage 2011).

One of the main foci of the TTIP is the regulation of the pharmaceutical sector, seeking to reach a better coordination between the European Medicines Agency (EMA) and the U.S. Food and Drug Administration (FDA), at the level of technical requirements for good manufacturing practices and quality (Goyens 2014). Although both parties have a strong IPR system and seek to keep health expenditures under control,<sup>5</sup> with the TTIP they aim at harmonizing regulations to improve access to complex medicines with special reference to generics (bio-similars).

It is not easy to quantify the economic relevance of the pharmaceutical sector in all its aspects, but when looking at trade of the two major players in the Atlantic Community, we see that exports of pharmaceuticals represent approx. 4 percent of total trade for the EU and 3 percent for the U.S. (figure 1). The trend is slightly upward in both cases, although these percentages are sensitive to price movements on raw materials and energy markets. Based on OECD figures, we calculate that the pharmaceutical sector represents approximately 5,6 percent of EU's outward FDI position, while the corresponding figure for the U.S. would be 1,1 percent. A relevant fact is that multinational pharmaceutical companies receive much of their revenues as service payments for their IPR.

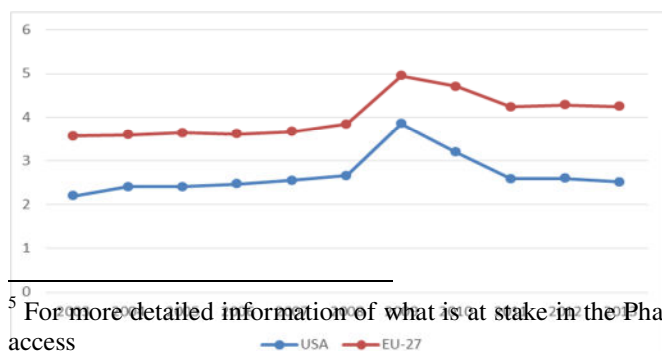


Figure 1: Share of pharmaceuticals in total exports of the EU and the US (%), 2003-2013

Sources: EUROSTAT, European Commission

<sup>5</sup> For more detailed information of what is at stake in the Pharmaceuticals in TTIP please access

and International Trade Administration, US Department of Commerce (HS30).

Looking at the structure of the Atlantic pharmaceutical trade (table 2), some observations arise: first, the relative importance of intra-regional trade for the EU, NAFTA and UNASUR seems to be slowly decreasing (i.e. the relative importance of extra-regional trade flows is increasing). Second, the U.S. has reduced its trade dependence on the EU. Third, MERCOSUR and the Pacific Alliance have been sourcing relatively more from the EU and relatively less from the U.S. over the last decade. Fourth, both MERCOSUR and the Pacific Alliance saw the share of intra-regional sourcing decrease in the 2000s, after which it has stabilized or even recovered slightly.

Table 2: Structure of pharmaceutical imports (SITC 54), by origin (2013-2000)

<b>2013</b>	<b>EU27</b>	<b>Mercosur</b>	<b>NAFTA</b>	<b>Pacific Alliance</b>	<b>UNASUR</b>	<b>USA</b>
EU27	66,73 %	0,22%	15,28 %	0,18%	0,22%	14,21 %
Mercosur	49,68 %	6,98%	20,39 %	4,66%	8,62%	16,15 %
NAFTA	55,30 %	0,65%	11,49 %	0,57%	0,73%	6,55%
Pacific Alliance	45,98 %	5,63%	27,16 %	3,56%	7,54%	22,85 %
UNASUR	46,72 %	8,01%	20,77 %	6,63%	11,25%	15,93 %
USA	57,95 %	0,29%	5,93%	0,53%	0,31%	
<b>2010</b>	<b>EU27</b>	<b>Mercosur</b>	<b>NAFTA</b>	<b>Pacific Alliance</b>	<b>UNASUR</b>	<b>USA</b>
EU27	68,85 %	0,31%	14,30 %	0,17%	0,31%	13,56 %
Mercosur	46,27 %	6,79%	23,40 %	4,43%	8,46%	17,70 %
NAFTA	59,01 %	0,45%	12,36 %	0,51%	0,51%	6,69%
Pacific Alliance	42,01 %	5,74%	30,52 %	3,45%	7,74%	26,42 %
UNASUR	43,13 %	8,04%	23,69 %	6,72%	11,46%	17,78 %
USA	61,65 %	0,27%	6,81%	0,46%	0,29%	
<b>2000</b>	<b>EU27</b>	<b>Mercosur</b>	<b>NAFTA</b>	<b>Pacific Alliance</b>	<b>UNASUR</b>	<b>USA</b>
EU27	69,79	0,11%	16,24	0,10%	0,11%	15,80

	%		%			%
Mercosur	45,69 %	9,37%	24,73 %	7,38%	12,23%	19,14 %
NAFTA	59,99 %	0,38%	18,02 %	0,60%	0,52%	13,32 %
Pacific Alliance	37,84 %	7,93%	30,92 %	7,23%	11,93%	25,88 %
UNASUR	41,89 %	11,02%	24,51 %	10,75%	16,13%	17,52 %
USA	68,93 %	0,21%	6,14%	0,56%	0,25%	

Note: Read horizontally, the table shows the relative importance of imports by origin (as % of total imports).

Source: UN COMTRADE.

### The Growing Role of National Courts in Balancing IPR and the Right to Health

The tensions between IPR and the right to health concern the trade partners of the US and the EU but also the WTO because national courts are often aligning with goals of the WHO and the UN (MDGs, SDGs) that seek universal coverage in health-care. This situation is challenging the international *status quo* where most of the IPR regulations are binding rules, whereas ESCR such as the right to health are not globally enforced due to lack of sanctions (Crook 2005:538; Van Hees 2004).

Certain courts in Latin America are worldwide recognized as very active in the defense of ESCR; in some cases also regional courts (i.e. Andean Tribunal of Justice (ATJ))<sup>6</sup> have protected ESCR over trade and investment. These courts are part of the globalization of HR phenomenon, understood as a growing judicial adjudication on HR matters (Tushnet 2008; Kennedy 2006; Stone and Matthews 2008; Bomhoff 2008), as a consequence of the emergence of constitutions where ESCR are included with more binding force than before following the guidelines of the UDHR and the ICESCR (ICJ 2008; Landau 2014).<sup>7</sup> TRIPS+ clauses are therefore facing a new challenge at the national (regional) level of emerging countries, mostly from Latin America where the judiciary privileges

<sup>6</sup> ATJ ruled that the patent registration of proof data for medicines would threaten free competition and the right to access to medicines by extending patents (Ruling 114-AI-2004; quoted by Uribe 2007: 115). CAN modified its decisions to allow the signature of the FTAs of Colombia and Peru with the US and with the EU (Saura 2013; Helfer and Alter 2014).

<sup>7</sup> Certain constitutional rules address health care and have been the basis of the judicial enforceability of the right to health (Bonilla 2014; Ely and Parra 2009; ICJ 2008; Rodríguez 2011).

constitutions, UDHR and ICESCR over WTO rules. Moreover, some national courts in emerging economies are pushing for a strict regulation of the market of medicines, seeking equality and efficient public resource allocation by avoiding paying exorbitant prices for medicines (see ruling C313/14 of the Colombian Constitutional Court (CCC)).

There is empirical evidence from Colombia, Brazil and Argentina, where rights-based judicial adjudication has been crucial in the enforcement of ESCR and in particular in the protection of the right to health (Byrne 2009; Narula 2011; Bonilla 2014; Lunes et al 2012; Mæstad et. al. 2011). Countries such as Brazil and Argentina have even delayed the signature of FTAs with the U.S. and the EU, among other reasons because of the TRIPS+ clauses of these agreements.<sup>8</sup> In Brazil, some landmark cases of annulling patents for constitutional reasons<sup>8</sup> are a concern as well as lawsuits “filed by Brazil’s National Industrial Property Institute (INPI) seeking to invalidate or shorten the term of certain “mailbox” patents for pharmaceutical and agrochemical products” (USTR 2014:49).

The U.S. has also been expressing concerns about Brazil (and Peru) because of the “proliferation of counterfeit pharmaceuticals manufactured, sold and distributed” (USTR 2014:20). Argentina (since 1996) and Chile remain on the priority watch list because of the existence of “unfair commercial use or unauthorized disclosure of test and other data generated to obtain marketing approval for pharmaceutical products.” Chile, despite the existence of the U.S. FTA, is also urged to implement a more expedite patent system for pharmaceutical products (USTR 2014:44).

In Colombia, the CCC held that FTAs should be enforced and interpreted in accordance with the protection of constitutional rights, especially the right to health (Lizarazo et al. 2014; Kingah et al. 2014). The negotiations of the COL-EU FTA were controversial because IPR clauses were closer to the parameters of EU legislation (TRIPS+) at the cost of the DD 2001 (Ifarma and FMS 2009; Seuba 2009: 65-8). The final version of the EU FTA conditioned its enforcement to the respect of the general interest and the DD 2001 is an interpretative parameter for public health issues (Seuba and García 2010). Colombia also remains on the watch list of the USTA because it is limiting the patentability of some pharmaceuticals and there are also some concerns about data protection (USTR 2014:50).

Another pending issue is the seizure of generic medicines in transit from India to Brazil by EU countries because they are seen as an obstruction to the enforcement of the right to health to the benefit of trade (Stelen et al 2012; Mercurio 2012). Conflicts about border seizures, IPR protection in cases of compul-

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<sup>8</sup> A lawsuit was presented eg against the patent of Abbott Laboratories for being granted under the ‘pipeline mechanism’ (i.e. revalidation of patents already granted elsewhere without following the Brazilian procedure) and despite the fact that the generic was validated by the WHO (<http://business-humanrights.org/en/abbott-laboratories-lawsuit-brazil-patent-law-access-to-medicines>).



sory licensing and potential TBT in bio-generic regulations are being presented before the WTO Dispute Settlement Mechanism (DSM) where the relevance of HR agreements and in particular of the DD 2001 remains unclear, in strong contrast with national courts where the ICESCR is gaining relevance vis-à-vis WTO law.

## Conclusions

In the Atlantic Community, the EU and the U.S. appear as the leading IPR holders, suppliers of regulations and producers of pharmaceuticals. The TTIP emerges as a new way to coordinate rules but faces opposition of Latin-American countries. The UNASUR in particular, under Brazil's leadership, is trying to support the development of a market for pharmaceuticals far from the TRIPS+ regulations. Although the Pacific Alliance emerges as a grouping which is more aligned with FTAs of the EU and the U.S., countries such as Chile and Colombia are also trying to develop the market of bio-generics in order to keep their public health expenditures under control. It remains unclear whether they have the institutional capacity to regulate and produce bio-generics. New TBT standards as promoted by the U.S. and the EU through the TTIP represent new challenges for these Latin America countries.

The consolidation of national activist courts supported by the UN, WHO and NGOs in the defense of ESCR and the rise of emerging economies, open new perspectives for the goal of balancing IPR and the right to health at the benefit of most vulnerable populations and without affecting innovation. Over-protection of IPR holders in combination with non-coordinated intervention of different judicial authorities at different levels are creating legal uncertainty and the costs of litigation may also affect social policy goals. In fact, the balancing of IPR with the right to health, as it was intended by DD 2001, is provoking contradictory rulings at different levels (international, national and regional) which is related to overlapping levels of regulation (national constitutional level, FTAs, regional integration groupings, WHO, WTO, EU etc.).

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# **The European Union and Latin America: Facing the Drug-Trafficking Challenge\***

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## **Abstract**

In recent decades, the fight against drug trafficking has been one of the most important issues in the relations between the European Union (EU) and Latin America and the Caribbean (LAC). The growing focus on this question is fed by the new challenges that drugs and their dynamic impose on both regions. EU-LAC cooperation to fight drug trafficking promotes a balanced, comprehensive vision that recognizes the importance of combatting drugs through policies designated to intercept narcotics and strengthen national institutions, but also to deal with the underlying causes of the problem through programs that include drug-use prevention, rehabilitation of addicts, and alternative development programs in producing countries. The EU-LAC relations in this area can contribute to the development and implementation of alternative policies in the framework of the world debate about the limits of the traditional paradigm for fighting drug trafficking. Despite this opportunity, an analysis of cooperation projects in this field reveals the gap between the discourse and implementation, not only in terms of resources, but also of approach. And this is because the logic of limiting the amount of drugs that leave Latin America for Europe continues to prevail.

## **Introduction**

Cooperation to fight drug trafficking and consumption has gradually been incorporated into the European Union (EU)-Latin America and the Caribbean (LAC) agenda since the mid-1990's. In contrast with traditional views like the so-called "war on drugs," which has focused on combatting production and emphasizing a prohibitionist approach banning drugs, EU-LAC

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\* This paper presents some preliminary results of an ongoing research project "Facing Transnational Organized Crime: Comparative Study of Regional Strategies", National Autonomous University of Mexico (UNAM).



cooperation conceives of illegal drugs as a social and security problem requiring a comprehensive policy response.

A first look at the EU-LAC counter-narcotics cooperation paradigm suggests that it should support the non-traditional efforts of many Latin American countries facing the drug problem. Moreover, in the framework of the debates about the failure of punitive responses, based on eradication, prohibition, and criminalization of consumption, the European “harm reduction” model prioritizing prevention, medical treatment, and partial decriminalization of drug use could be a point of reference for a renewed strategy against drugs.

Yet, bi-regional cooperation against narcotics faces different constraints: the different inter- and intra-regional perceptions of the drug problem and how to deal with it; the inexistence of a single voice and common strategy on drugs in LAC; the limited resources for bi-regional cooperation programs; and the pre-eminence of the focus on combatting cocaine production in the Andean countries.

### **The European Model: Harm Reduction**

According to the 2014 European Drug Report, drug consumption in the EU remains stable: around 14.1 million people are taking or have at some point used cocaine; 10.6 million, ecstasy; and 73.6 million, cannabis (EMCDDA 2014:13). Nevertheless, overdoses continue to be the main cause of death among young people, and concern exists about the growing use of synthetic drugs and the “new psychoactive substances.” It is also important to point out that the EU countries are no longer just drug consumers: they have become producers of cannabis and synthetic drugs, thus making the problem more complex.

According to the European Commission (2011), “illicit drugs are a major threat to the health and safety of individuals and societies in the EU.” Therefore, for EU members, drug trafficking and consumption are related to public security issues (health and well-being).

In the EU, member country governments continue to shoulder the responsibility for drug policy design and implementation. Over the last 20 years, they have developed frameworks for EU action to coordinate drug policies and create a common framework to make national strategies consistent and strengthen cooperation.

In 2003, the EU adopted “harm reduction” as a common principle for drafting EU drug strategy for 2005-2012; the approach was adopted in December 2004. Harm reduction is an alternative answer to drug prob-

lems that seeks to reduce the harm associated with illicit drug use and develop specific programs focused on the life-threatening conditions of drug users, as well as prevention, rehabilitation, and reintegration policies. Therefore, national strategies are increasingly oriented around this model. According to the 2014 EMCDDA report, a trend seems to be emerging toward countries focusing on penalizing supply rather than possession of these substances.

Hence, European drug policy aims to take a balanced, integrated approach to the drug problem combining demand reduction and supply reduction measures (European Commission 2011; Council of the European Union 2012). The European Council has specified two general aims regarding drugs: 1) complementing national actions in preventing and reducing drug use to contribute to attaining high levels of health protection and well-being; and 2) taking action against drug production, cross-border trafficking, and the diversion of precursors.

The 2013-2020 EU Drug Strategy is structured around these policy areas and three crosscutting themes:

- 1) Coordination: police cooperation and coordination within the EU, improving Europol capacities and border controls in the framework of the European Area of Freedom, Security and Justice;
- 2) International cooperation: identifying European Neighborhood countries as a priority as well as the need to address old and emerging trafficking routes such as those in West Africa.
- 3) Research, information, monitoring, and evaluation: through the European Monitoring Centre for Drugs and Drug Addiction (European Union 2012; EMCDDA 2013).

The European Union Action Plan on Drugs (2013-2016) states that two fundamental objectives exist within the EU legal framework: reducing both drug use and supply. Likewise, it seeks to effectively reduce the age at which users begin to consume these substances. In sum, the main approach in the region for reducing demand is the harm reduction model. Member states still have different opinions about drug policy and priorities, and gaps still exist in anti-narcotics actions, especially among nations like Italy, Spain, and some Eastern European countries, where criminal groups are more active. These differences make it difficult for the EU to adopt common positions in international bodies and in discussions with third parties, including Latin America (Gratius 2012).

### **Latin America's "War on Drugs"**

Latin America and the Caribbean have a long history of fighting drug trafficking. Prohibitionist policies centered on the head-on fight against the production and

transportation of illicit drugs became important after 1973, with Richard Nixon's "War on Drugs." This approach became more and more entrenched after the end of the Cold War, when the fight against drug trafficking became one of the most important items on the inter-American agenda.

However, an assessment of the "war on drugs" in Latin America shows its limits: between 1999 and 2010, coca leaf and cocaine production decreased by 50 percent in Colombia, but has increased in Peru and Bolivia (during the same period the land used for drug cultivation practically doubled in Peru) (Gratius 2012). There has been a worrying increase in cocaine consumption in South America, especially in Brazil. The number of past-year cocaine users in South America was estimated at almost 2 million in the period 2004-2005 and 3.35 million in 2012 (UNODC 2014: 36). Moreover, drug trafficking is one of the main factors behind increased criminal violence in the region, particularly in Central America, Mexico, Venezuela, Brazil, and Colombia. With a homicide rate of 26.5 per 100,000 people, Central America is the most insecure area in the world (UNODC 2013:33).

Drug trafficking challenges the national security of the Latin American countries in different ways. A state's response capabilities *vis-à-vis* this threat depend on its institutional strengths, its location on the map of criminal activity (producing, consuming, and transit countries), and the mechanisms it uses to deal with them.

The complex problem of drug trafficking in Latin America has generated a variety of responses at national, sub-regional, and hemispheric levels. It is important to note that, in all cases, the need to promote comprehensive policies to combat this threat is recognized, but, historically, governments prioritized the traditional model centered on the use of force.

For many countries in the region, drug trafficking is the main threat to national security, and the armed forces have been incorporated into a variety of activities in the war on drugs: border enforcement, prohibition activities, the arrest of criminal leaders, and public security. With their respective differences, Mexico, Guatemala, Honduras, Peru, Brazil, and Colombia are examples of these policies. But for other countries, like Chile or Uruguay, the drug problem remains on the public security agenda. The Uruguayan government has even gone as far as to decriminalize cannabis, regulating its production and commercialization.

At the hemispheric level, since the 1980s, Latin American countries have promoted regional cooperation against drug trafficking in the framework of the Organization of American States. The first initiatives were intended to create multilateral mechanisms opposed to U.S. unilateral policies. In particular, emphasis was on the principle of shared responsibility and regional counter-narcotics cooperation. The establishment

of the Inter-American Drug Abuse Control Commission (CICAD) in 1986, the approval of the first Anti-Drug Strategy in the hemisphere in 1996, and the creation of the Multilateral Evaluation Mechanism in 1998 were part of this dynamic (Chanona 2011).

The principle of shared responsibility, the promotion of multilateral cooperation, and the commitment to adopt comprehensive policies against drug trafficking are elements of the Hemispheric Plan of Action against Transnational Organized Crime (2006); the Hemispheric Drug Strategy (2010); and the Hemispheric Plan of Action on Drugs 2011-2015 (2011). Nevertheless, until now, hemispheric cooperation against drug trafficking and consumption has had limits. A coordinating mechanism is still lacking, and sub-regional initiatives have been playing a more important role in the fight against organized crime.

### **Bi-Regional Cooperation**

Latin America and the European Union share values and principles that are the core of their bi-regional partnership. In the area of security, both regions have adopted the broad concept of multidimensional security and share values like solidarity, cooperation, multilateralism, respect for human rights, and shared responsibility on drug issues.

Both regions agree that fighting drug trafficking and consumption requires international cooperation and an “integrated, multidisciplinary and balanced approach combining drug demand reduction and drug supply reduction measures” (EU-CELAC Quito Declaration 2013).

In response to the challenge of increased cocaine consumption in European countries, in 1995, the Specialized High-Level Political Dialogue on Drugs with the Andean Community was established. In the case of the Caribbean Community, a strategic area for moving drugs to Europe, the Barbados Action Plan was put into effect in 1996 with the participation of the United Nations Office on Drugs and Crime and the CICAD.

At the bi-regional level, the EU-LAC Coordination and Cooperation Mechanism on Drugs was formally launched in 1998,<sup>1</sup> with the aim of fostering institutional strengthening and the development of national and regional policies to allow the countries to deal with the drug problem. Its action plan, known also as the Panama Action Plan, was approved in 1999. Since that time, both regions have worked in key areas including:

- Demand reduction: exchange of information on drug policies, prevention and treatment activities;
- Supply reduction: joint actions to identify and dismantle organized crime

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<sup>1</sup> Since December 2011, with the creation of the Community of Latin American and Caribbean States (Comunidad de Estados Latinoamericanos y Caribeños, or CELAC), the term “LAC” has been replaced by “CELAC.”

- groups, strengthening judicial cooperation; promoting alternative development projects to coca plantations;
- Mutual technical assistance programs on capacity-building (police, customs, judicial action);
  - The establishment of drug observatories, with the aim of creating an integrated system of drug information, collecting comparable indicators on production, consumption, trafficking, chemical precursors, and money-laundering;
  - Strengthening maritime cooperation, particularly with the Caribbean through the Barbados Plan of Action;
  - Technical dialogue on precursor chemicals; and
  - Improved capacities against money laundering, with special attention to Andean and Caribbean countries (EEAS 2014).

The Cooperation Program between Latin America and the European Union of Drug Policies (COPOLAD) was established in 2009. Based on the idea of promoting an inclusive and balanced anti-drug strategy, the program has four components: 1) consolidation of the EU-LAC Coordination and Cooperation Mechanism on Drugs; 2) consolidation of the national drugs observatories; 3) capacity-building in demand reduction (prevention, treatment, rehabilitation, and harm reduction) and 4) capacity-building in supply reduction (law enforcement and alternative development). For 2010-2014, the EU had originally earmarked €6 million for the project. In March 2013, that budget increased by a little over half a million euros (Council of the European Union 2013; COPOLAD 2015).

In 2009, a program was also launched with the aim of fighting the criminal networks along the cocaine route, which includes 36 countries of Latin America, the Caribbean and East Africa, with a budget of €50 million, making it one of the EU's priority programs. Four of the seven components of the Cocaine Route Program are open for CELAC countries:<sup>2</sup> the Program on the Prevention of the Diversion of Drug Precursors in the Latin American and Caribbean Region (PRELAC); the Airport Communication Programme (AIRCOP) to intercept cocaine shipments; cooperation with the American Police Community (AMERIPOL)<sup>3</sup> to strengthen cooperation of law enforcement and judicial and prosecuting authorities; and cooperation with the Financial Action Task Force of South America

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<sup>2</sup> African countries participate in the other three programs: Anti-Money Laundering and Financial Crime Initiatives in West Africa (AML), the Seaport Cooperation Project (SEACOP), and the West African Police Information System (WAPIS).

<sup>3</sup> Members: Colombia, Bolivia, Brazil, Ecuador, Peru, Panama, Martinique, Barbados, and Trinidad and Tobago.

(GAFISUD), to deal with money laundering and financial crime (Council of the European Union 2013;European Union 2015).

The most recent meeting of the Coordination and Cooperation Mechanism on Drugs took place in 2012 in Brussels. In addition to reiterating its commitment to cooperation for reducing both demand and supply, the EU and the LAC emphasized the importance of facing down the new challenges linked to chemical precursors and the diversification of synthetic drugs.

Table 1. EU-LAC Cooperation Programs on Drugs (2004-2015)

Program	Objectives	Budget (Euros)
<b>Bi-Regional</b>		
COPOLAD 42 months from December 2010.	To strengthen capacities and encourage the process of elaborating drugs policies in LAC.	6,574,786.74 (EU)
PRELAC I March 2009- February 2012	To strengthen trans-regional capacities to prevent the diversion of chemical substances. Supporting international cross-border cooperation.	Total: 2.437.075 90% (EU) 10% (UNODC)
PRELAC II February 2012- February 2015	To strengthen the relationship between private sector and control authorities. Complement other EU initiatives.	Total: 3.061.300 98 % (EU) 2% (UNODC)
EU-LAC Intelligence Sharing Working Group 2006-2009	To increase the exchange of operational intelligence.	514.504 (EU)
EU-LAC Cities in Partnership 2007-2010	To improved policy decisions at the city level on the quality and coverage of drug treatment, rehabilitation and harm reduction.	1.400.000 (EU)
<b>Multi-regional: LAC and West Africa</b>		
COLACAO 2006-2010	Law enforcement and intelligence cooperation to reduce the amount of cocaine destined for or transiting Africa (interdiction capabilities)	800.000
Cocaine Route	Law enforcement to fight against international criminal networks.	50,000,000 (EU)

2009-today	36 countries	
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Source: Own elaboration based on Gratius, 2012; EEAS, 2014; EEAS 2014a; COPOLAD, 2015; CICAD, *Proyecto PRELAC*, Council of the European Union, 2013 and European Union, 2015.

Despite these links, bi-regional cooperation to fight drugs has different limits, among them:

- a) The impact and the perceptions of drug trafficking are so different in both regions: while in an important number of Latin American countries drug trafficking is a national security concern, for EU members the drug problem is seen as linked to public health and public security.
- b) There is no single voice or common strategy on drugs in Latin America and the Caribbean (Gratius 2012). The region's complexity makes it difficult for all the countries to participate in cooperation programs, and the tendency is to emphasize sub-regional and bilateral activities. The challenge for the Latin American and Caribbean countries continues to be how to reconcile the different strategies.
- c) The perception of EU members on drug trafficking from LAC. Europe accounted for 24 percent of all cocaine users worldwide (UNODC 2013). This explains why the EU has been prioritizing sub-regional and bilateral cooperation programs with Andean countries (Colombia, Peru, and Bolivia as cocaine producers).

When we analyze the EU-LAC cooperation programs on drugs during last decade, we note the preeminence of programs with the Andean and the Caribbean countries over the bi-regional ones. For example: 1) the special trade preferences to Andean and Central American countries under the "GSP-Drugs scheme;" 2) sub-regional programs with the Andean Community such as: Combating Illegal Drugs in the Andean Community (PRADICAN), funded with €3.25 million; and the Support for the Andean Community in the Area of Synthetic Drugs Project (DROSICAN), with €2.55 million to fight synthetic drugs; 3) sub-regional programs with the Caribbean Community, such as: CARICOM Regional Demand Reduction (€ 800.000), Support Capacity Building for Law-Enforcement Agencies (€ 400.000) and Institutional support to the CARICOM Implementation Agency for Crime and Security (IMPACS) in its role to inform policy development (€ 800.000); and 4) alternative development projects and programs to fight against drugs in Bolivia, with total funding of €119 million from 1999 to 2013; Peru with €32 million from 2014 to 2017 and Colombia, which has received around €165 million for peace laboratories and regional de-

velopment (CICAD 2007; Gratius 2012; EEAS 2014a; European Commission 2007; European Commission 2013).

Table 2. EU Bilateral Cooperation Programs on Drugs (1998-2015)

Program	Budget (Euros)
<b>Colombia</b>	
Peace Laboratory in Magdalena Medio I (2002) II (2003) and III (2006)	92,000,000
Regional Development for Peace and Stability I and II	34,600,000
Peace Laboratory Montes de María (2008)	8,000,000
New Peace Territories (2010)	30,400,000
<b>Bolivia</b>	
PRAEDAC: Alternative Development in Bolivia (1998-2006)	19,000,000 (77% of total)
APEMIN II (January 2004-July 2010)	7,000,000
Support for the Control of Coca Production in Bolivian Society (started in 2008)	10,000,000
Sector Budget Support to the National Integral Development with Coca (started in 2008)	26,000,000
Integral Study of the Coca Leaf (2008-2010)	1,000,000
PISCO: Institutional Strengthening to Combat drug Trafficking (Agreement 2011)	9,000,000
Alternative Development Programs 2014-2020	25,000,000
<b>Peru</b>	
Anti-drug Program (2014-2017)	32,000,000
<b>Venezuela</b>	
DROGASTOP 2011-2013	Total: 6,300,000 3,300,000 from the EU

Source: Own elaboration based on Gratius, 2012, EEAS 2014a; EEAS, 2014b; European Commission, 2007a, European Commission, 2010; European Commission, 2011a; European Commission, 2013; European Commission, 2014 and Europe Aid.



Thus, although in its discourse, the EU identifies LAC as “strategic partners” against drug trafficking and insists on the importance of strengthening bi-regional cooperation and promoting comprehensive policies against illicit drugs, the reality is that the Europeans prefer sub-regional and bilateral agreements and programs, centered in controlling cocaine and synthetic drug production and trafficking. In a study for the European Parliament, Susanne Gratius (2012) revealed that most of the EU projects in LAC are designed to reduce drug supply. According to her data, 102 out of 13 projects focus on reducing supply.

## **Conclusions**

EU interest in anti-narcotics cooperation arises out of different factors. Outstanding among them is the damage caused by drug consumption in terms of addiction and death, the increase of synthetic drug production in the EU, and concerns about violence levels in Latin America and the Caribbean linked to organized crime activities. For their part, the Latin American countries have found in the Europeans a key partner for fostering a comprehensive vision in the face of the organized crime challenge. Since the 1980s, the Latin Americans have emphasized shared responsibility among producing, transit, and consuming countries, as well as the importance of multilateral cooperation to deal with these challenges.

The evaluation of EU-LAC cooperation in the fight against drugs shows that, despite good intentions, the tendency has been to emphasize the fight against production and transportation of drugs from Latin America to the EU. What distinguishes this strategy is the use of instruments of greater scope, including issues linked to institutional strengthening, the rule of law, police institutions, the development of intelligence capabilities, and actions against money laundering, and boosting international cooperation.

In the first years of bi-regional cooperation on drug issues, the differences between the EU discourse on a balanced focus and that of the United States, which put greater emphasis on prohibition, were noteworthy. However, the United States has recognized shared responsibility and fosters programs that include the institutional strengthening of Latin American countries to face down this challenge. The EU, meanwhile, has broadened out its programs focusing on preventing drugs from arriving to its shores.

The EU and the United States share concerns about chemical precursors, the production of new synthetic drugs, and the importance of slowing the flow of drugs to their countries. At the same time, it is fundamental that Latin America and the Caribbean continue to emphasize with their partners

the need to develop cooperation directed at the structural roots of drug trafficking and the violence it engenders. In the current context, given the limits of the prohibitionist paradigm for fighting drug trafficking, alternatives are being debated and the comprehensive, balanced approach to LAC-EU cooperation may be a reference point. The challenge is making sure the comprehensive approach translates into specific public policies. For the time being, we must not lose sight of the fact that in many Latin American countries, the priority is immediate answers in the face of the insecurity crisis and violence. This leads to strengthening policies centered on the use of force. For this reason, in the short term, the European vision of reducing damages will continue to be used in a “complementary” way, through notions like citizens’ security or prevention and rehabilitation policies. For its part, given the concern about increased use of synthetic drugs and psychoactive substances, and in a context of limited resources, the EU is going to focus more attention on its close neighbors in Eastern Europe and will continue to bet on broader projects like the Cocaine Route Programme aimed at preventing drugs from crossing its borders.

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### **III. Inside Latin America**



# Latin American Answers to Mega-Regional Projects: Options and Limits

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## Abstract

European negotiations with the US leading to a mega transatlantic project and similar mega-trade deals in Asia-Pacific were answered with three Latin American projects – the MERCOSUR-Pacific Alliance convergence, supported by Chile-Brazil; the ECO-ALBA-Petrocaribe Zone promoted by Venezuela; and acceleration of MERCOSUR-enlargement with Venezuela, Bolivia, and Ecuador. This article analyses the agreements' geo-economic and geopolitical options and limits.

## Introduction

By 2000, the principle of reciprocity, upon which the General Agreement on Trade and Tariffs (GATT) had been built after World War II, was no longer in operation (Halperin 2004). Since the 1960s and 1970s, free trade zones and custom unions formed by developing nations, and generalized schemes of preferences adopted by developed nations had been exempted from no discriminating against trade by the rest. During the nineties, bilateral and regional trade agreements increased in number and generated the phenomenon of the “spaghetti bowl.” The start of the Doha Round (2001) opened the possibility of bringing order and coherence to the multilateral system, but trade in agriculture derailed negotiations, which have stagnated since 2005 (Giacalone 2007).

Multilateral negotiations have been surpassed by technological change that diminishes distance, accelerates communications, and allows big business to relocate productive activities in the most competitive environments. Fragmented production chains and intra-industry and intra-company trade have augmented together with associated services (Kotschwar 2014).

Besides the stagnation of multilateral negotiations and the increase in regional and bilateral trade agreements, in 2008 the global crisis reduced the price and volume of exports and reverted investment flux (ALADI 2012; CEPAL 2009), with negative consequences for all nations. Presently, the United States (US) and the European Union (EU), which together represent 46 percent of global GDP and 25 percent of world trade (Kotschwar 2014), are negotiating a mega-trade deal (the TransAtlantic Trade and Investment Partnership, TTIP) to revert those consequences.



Felbermayr et al. (2013) and Roy and Dominguez (2014) studied the impact of the TTIP on Latin America, while Gayá and Rozemberg (2014) analysed its consequences upon the Southern Common Market (MERCOSUR). In this article, we look at the geo-economic and geopolitical options and limits of the Latin American projects that emerged in response to mega-trade negotiations: the MERCOSUR-Pacific Alliance (PA) convergence, supported by Chile-Brazil; the ECO-ALBA-Petrocaribe Zone promoted by Venezuela; and the enlargement of MERCOSUR with Venezuela, Bolivia, and Ecuador, originally supported by Brazil, and now by Argentina and Venezuela. All these projects represent efforts to model the region's global insertion according to the interests of their respective proponents.

### **The MERCOSUR Enlargement**

This process effectively started with the approval of Venezuela's entry to the agreement (2006), which was not achieved until 2012. To this day, Venezuela is still going through a period of adapting tariffs and norms for MERCOSUR. For Venezuela, this was a geopolitical project to create a Regional Mega-State by enlarging MERCOSUR with Venezuela, Bolivia, Ecuador, and Cuba (Dieterich 2007: 30, quoted in González 2007: 12). MERCOSUR's enlargement was also a Brazilian economic project that began with the 1994 proposal to integrate tariffs and institutional structures of the Andean Community (CAN) (Bolivia, Colombia, Ecuador, Peru, and Venezuela) and MERCOSUR (Argentina, Brazil, Paraguay, and Uruguay) into a South American Trade Zone. By 2004, this goal was not achieved, but Brazil established the South American Community of Nations – later converted into the Southern Union of Nations -- and CAN members signed trade agreements with MERCOSUR and became associate members.

Venezuela's entry increased the population, natural resources, GDP, and intra- MERCOSUR trade (Coelho et al. 2006). Ghazalian (2013) estimated the effects upon trade of commodities of converting associates into full members, and found that enlargement would increase exports from previous members to associates but not in the opposite direction. This trend is confirmed by trade between Venezuela and MERCOSUR since 2006.

In spite of Venezuelan geopolitical interest in MERCOSUR, its impact has been bigger in the economic field and Brazil, whose trade balance with Venezuela in 2008 amounted to 5.7 billion dollars, with a 4.6 billion surplus (Aragao 2009). The Venezuelan entry also meant the possibility of Argentina balancing the power of Brazil in MERCOSUR, the agreement's projection toward the Caribbean (González Urrutia 2007: 15, 9), and gains in energy security. But, the contradictory political and ideological goals of Venezuela and the rest of the members weakened the group (Gantz 2013: 216).

Since 2012, MERCOSUR enlargement has accelerated in response to new regional and international contexts. At the MERCOSUR summit meeting in Bra-

silia, the protocol for Bolivian admission was signed (Geffner 2014: 7). This is hailed as a defensive measure against the EU and the US that strengthens the negotiating power of MERCOSUR (Parlamento del Sur2013), but is an overstatement because Bolivia continues individual negotiations with the EU (Los Tiempos 2013), and together with Ecuador it increases MERCOSUR's GDP only by 2 percent (Guillén 2013). The move looks like a political decision to shift the internal balance of MERCOSUR by reducing Brazil and Argentina's relative weight, because it will mean less percentage of GDP, territory, and population for them (Cimadamore and Rodriguez 2013: 124).

If originally Brazil promoted MERCOSUR enlargement due to economic reasons, now Brazil prefers convergence with the PA while Argentina and Venezuela push for association with the Alternativa Bolivariana para Nuestra América (ALBA)-Petrocaribe, and the Caribbean Community (CARICOM). During the 2014 MERCOSUR Summit, Brazil proposed to shorten the time for establishing a common South American market which will be reached in 2019 due to the trade agreements between MERCOSUR and associates. Brazil wants to accelerate the process with PA members to counter the effects of the global crisis. Argentina and Venezuela prefer instead negotiations with ALBA-Petrocaribe (Scharfenberg 2014; BID-INTAL 2015: 89-96) and an agreement with the Eurasian Union (Primicias24 2014), while Brazil, Paraguay, and Uruguay want one with the EU (Yakovleva 2014). Internal disagreements continue to limit the geopolitical weight of an enlarged MERCOSUR.

### **MERCOSUR-PA Convergence**

By mid- 2013, ECLAC data rendered a 5 percent combined growth index for the PA (established in 2012) against 2.9 percent for MERCOSUR, and while intra-regional trade in MERCOSUR fell 9.4 percent during 2012, in the PA it grew 1.3 percent (Oppenheimer 2013), though volume and value of MERCOSUR trade are bigger (Geffner 2014). A meeting between the foreign ministers of MERCOSUR and the PA (Cartagena 2014) ended with a declaration that echoed a previous document by former Chilean President Ricardo Lagos and former Brazilian President Lula (Da Silva and Lagos 2014; MERCOSUR ABC 2014). Both recommended a Latin American regional project with a pragmatic and economic orientation, based on the links established between MERCOSUR and PA by companies and economic groups.

Since 2009, ECLAC has recommended the convergence of trade agreements in Latin America. In 2014, it was considered urgent due to the global trend to establish mega-trade agreements (Rosales 2014: 8). MERCOSUR-PA convergence is expected to precipitate convergence among other agreements, increase the negotiating power of the region, strengthen productive activities and trade, and counter the fall of exports in extra-regional markets (Rosales 2014: 28-30).

The Brazilian-Chilean proposal can be linked to the fact that they followed similar development models under their military regimes – Brazil inspired by German neoliberalism with state intervention, and Chile by the Chicago School that favoured retraction of the state from the economy (Ramírez 2012: 77). Both changed from heterodox to orthodox policies when confronted with high inflation, fiscal and external imbalances, and failure of import substituting industrialization (Fosu 2013). As a result, Brazil occupies an intermediate position between governments with neoliberal and statist development models (Lima 2013).

Brazil, the largest South American economy in GDP and trade, the most industrialized and with the biggest business companies, prefers exclusive regional trade arrangements to sell goods and services among its asymmetrical regional partners. Chile, a medium economy with a smaller domestic market that limits scale economies and high technology industrialization, prefers open trade schemes. While Brazil became the axis of a MERCOSUR custom union, Chile signed a variety of North-South and South-South Free Trade Agreements (FTAs).

Under the government of Dilma Rousseff, Brazilian industry reduced its exports and lost part of the domestic market to Chinese imported goods. This is attributed to the overvaluation of the Brazilian currency and lack of industrial competitiveness. To protect its industry Brazil has distanced itself from the World Trade Organization – which in 1995 substituted GATT --, has not signed North-South FTA, and is isolated from global productive chains (Veiga et al. 2013: 37-38). EU-US negotiations and similar processes in the Pacific would mean reduction of MERCOSUR agribusiness exports, loss of FDI, trade diversion for MERCOSUR goods in Latin American Pacific nations participating in those negotiations, and less exports to China and India (Gayá and Rozenberg 2014). These facts are leading Brazil to look for alternatives.

The geo-economic options of MERCOSUR-PA derive from their weight – MERCOSUR with a population of 282 million, a GDP of 3.300 billion dollars and a total trade of 824.658 million, and the PA with a 3.000 billion GDP and 50 percent of total Latin American trade. Together they represent 85 percent of Latin American population, 91 percent of its GDP, and more than 80 percent of its trade (MERCOSUR ABC 2014). Their members cover an area from the Mexican Gulf to the Southern Atlantic and Pacific Oceans that facilitates relations with the US, the EU, and China.

In 2013 exports of goods from the PA to MERCOSUR were similar in value to exports from MERCOSUR to the PA, and included more value-added goods (Rosales 2014: 44, 56). Mexico, Colombia, Chile, Brazil, and Argentina were the nations with more potential for intra-industry trade and for inserting themselves in intraregional production chains (Rosales 2014: 53). Summarising, MERCOSUR sells to the PA goods with more value added and the PA does the same to MERCOSUR, creating the basis for intra-industry trade and productive chains between them (Carta Mensual 2013). Additionally, the economic success

of the PA may generate a larger market for MERCOSUR goods, or displace them by similar ones due to the external agreements signed by PA members (Peyrani and Geffner 2014: 24), and FDI from MERCOSUR to the PA and contrariwise, in 2013 reached 1,220 million dollars and 4,077 million, with Chile representing more than 50 percent of PA's FDI to MERCOSUR (Rosales 2014: 71-72).

MERCOSUR-PA convergence has limits in terms of intraregional trade, productive integration, and private sector confidence in economic institutions. Obstacles to intraregional trade are the diversity of bilateral trade preferences and norms of origin, and the lack of infrastructure in transport and communication (Ulloa and Marambio 2014). Though intraregional trade in manufactures is growing, it is of final goods. This shows little intraregional productive integration because productive integration increases trade in intermediate goods and associated services among interconnected enterprises (CEPAL 2014: 69). In extra-regional chains, Latin America has low participation in segments of global production of manufactured goods (Blyde 2014). Also it occupies a low position in global index of respect for private property rights that varies from Venezuela, with the lowest scoring in the region (Rosales 2014: 38), to the opposite situation in Chile and Peru. MERCOSUR-PA convergence will not mean convergence of countries images, so FDI will probably follow existing patterns of location.

MERCOSUR-PA represents all South America and it looks similar to the MERCOSUR-CAN proposal, but the PA is stronger than CAN and Mexico and creates a second economic axis besides Brazil. The geopolitical weight of the group depends on the congruence of Brazilian and Mexican objectives, so if they can assume concerted positions, the geopolitical consequences could be far reaching.

If the amount of population provides room for scale economies and growth in domestic consumption, its geopolitical impact varies with the number of nations included, which may increase because the PA has its own enlargement program as shown by ongoing negotiations with Central American nations. Members represent votes in regional and multilateral organizations, an important consideration for Brazil which wants a permanent seat in the United Nations Security Council.

### **ECO-ALBA-Petrocaribe**

Venezuela considered ALBA the hard core of regional integration based on ideological and political affinity of members (Alcalá 2011, in Giacalone 2013: 149-150), but now is making effective its entry to MERCOSUR and pushing for the incorporation of Bolivia and Ecuador (El Informador 2013). This is considered a pragmatic movement given the impact of the global crisis on oil prices, but it can be an ideological alternative to the PA too.

In March 2013, Bolivia, Cuba, Ecuador, Nicaragua, and Venezuela<sup>1</sup> signed an Economic Complementary Agreement (ACE 70) of ALADI (SELA 2013: 17). SELA (2013) links this decision with the Venezuelan need to convert its trade agreements into ACEs because after its adaptation period Venezuela will have to negotiate them through MERCOSUR. Venezuela declared its intention of linking ACE 70 to Petrocaribe, CARICOM and MERCOSUR (ALBA-TCP/Petrocaribe 2013). The ALBA's Summit Meeting (2014) stated the objective of designing strategies and actions to make viable an Economic Complementary Zone made up by ALBA/Petrocaribe/CARICOM/MERCOSUR (Periodico 26 2014), and MERCOSUR established a mechanism to promote the ECO-Zone (SELA 2014: 25). The Venezuelan proposal coincides with a Brazilian economic expansion project in the Caribbean (SELA 2015). Both clash with Mexico's economic and geopolitical intentions of deepening its trade agreements in the region.

ECO-ALBA is expected to combine natural resources in energy and land for agriculture. However, economic complementarity between ALBA and the rest is low, and should be established first within ALBA, which is a political and only secondarily economic cooperation organization (SELA 2013: 24; Giacalone 2013). Also Petrocaribe is an oil cooperation agreement with geopolitical objectives, whose trade component derives from the need of oil-importing nations to repay debts with Venezuela through barter-type agreements.

The geo-economic limits of the ECO-ALBA-Petrocaribe Zone are several. First, is the situation of Venezuela, affected by a severe economic downturn (Geffner 2014). The fall of international oil prices has cut down Venezuelan financial resources for cooperation and foreign investment and reduced the cost for client nations of importing oil from other sources. The zone allows Venezuela to import goods and services without employing dollars, and Nicaragua and Bolivia to replace political will for certainty in their exports to Venezuela. Secondly, member nations belong to different regional agreements namely Nicaragua is member of ALBA, the Central American Economic Integration System (SIECA), and two North-South FTAs (CAFTA-DR and CARIFORUM-UE). English-speaking nations of Petrocaribe belong to CARICOM and CARIFORUM-UE.

Petrocaribe has 19 members; ALBA, 8; CARICOM, 14; and an enlarged MERCOSUR, 7. As some are simultaneously members of ALBA and Petrocaribe, Petrocaribe and CARICOM, and ALBA and MERCOSUR, the final total is 25 nations, a significant voting bloc in regional and multilateral institutions, though it implies long and complex negotiations to establish an agreement. The fact that Venezuela considers ALBA a geopolitical instrument to displace US hegemony in the region limited its attraction for Central American and Caribbean governments -- only five became ALBA members (Altmann 2009) --, and this may also limit the attraction of members and FDI to ECO-ALBA.

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<sup>1</sup> ALBA members Antigua-Barbuda, St. Vincent, and St. Kitts-Nevis did not sign because they are not members of ALADI.

## Options and Limits

### Options and Limits of Latin American Regional Projects

	ENLARGED MERCOSUR	MERCOSUR-PA	ECO-ALBA-PETROCARIBE
GEO-ECONOMIC OPTIONS	To develop regional productive chains and attract FDI	To develop regional and global productive chains and attract FDI	To combine natural resources (energy, land, etc.)
GEO-ECONOMIC LIMITS	Little effect of Bolivia and Ecuador's entry on MERCOSUR's GDP  More gains by core economies than by new members may exacerbate asymmetry	Clashes between divergent economic models may weaken compliance	Internal diversity in participation in trade agreements Little economic complementarity Ideological and political orientation of Venezuela
GEOPOLITICAL OPTIONS	Fewer actors may accelerate its establishment	Increased importance if Brazil and Mexico agree in common positions	A large number of members means more voting power in regional and multilateral organizations
GEOPOLITICAL LIMITS	Internal disagreements weaken external projection	Opposition by ALBA members of MERCOSUR	Venezuelan economic problems may compromise viability and external projection

Summarising, ECO-ALBA-Petrocaribe is the most ambitious and most difficult project to negotiate. MERCOSUR-PA convergence has economic importance and may have geopolitical clout if it puts Brazil and Mexico side by side at negotiations. An enlarged MERCOSUR may be concluded faster but has less geopolitical and economic importance, due to internal disagreements and the ideological-political orientation of ALBA members. These are potential developments because so far we find: ALBA converted into ACE 70, and promoting a complementarity economic zone with Petrocaribe/CARICOM/MERCOSUR; a project of MERCOSUR-PA convergence, which has produced two joint meetings; and MERCOSUR enlargement with Venezuela and Bolivia.

Finally, the most important factor in determining options and limits is Brazil because MERCOSUR's choice will depend on the decision of its largest

economy. Brazilian promotion of South-South negotiations since the 2000s created marginal new trade in Africa and with BRICS/IBSA (Oliveira and Onuki 2013: 3). However, if South-South trade grew from 8 percent of total trade in 1990 to 28 percent in 2012, this was due to Asian-Pacific rather than Brazilian exports (Rosales 2014: 19-21). Thus, Brazilian external coalitions may be instruments of soft-balancing against developed nations and multilateral institutions, but add little in economic terms (Oliveira and Onuki 2013: 10).

Presently, Brazil has to choose between either making its industry more competitive (Oliveira and Onuki 2013) or to enlarging its political power in the international scene (Veiga et al. 2013). The former needs Brazilian participation in global production chains and the latter rests on a South-South orientation. Brazil may move either way but also sign as many regional agreements as possible, like Brazilian business have suggested (Giacaglia 2013: 109). Brazil may simultaneously negotiate convergence with PA, complementarity with ALBA-Petrocaribe/CARICOM, and proceed with MERCOSUR enlargement. These moves are possible because all projects strive to include MERCOSUR and Brazil could not opt for the *status quo* because of the potential negative effects of the mega-trade deals (Gayá and Rozemberg 2014).

In conclusion, all these Latin American projects have geo-economic potentialities. Geopolitically, their potentialities are fewer – they represent more votes but internal disagreements prevent an external united front. However, the decision to negotiate them is positive because it recognises the need for concerted actions and may help turn ideological extreme positions into more pragmatic regional interests.

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# **Regional Integration in Latin America: The Strategy of “Convergence in Diversity” and the Relations between MERCOSUR and the Pacific Alliance**

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## **Abstract**

Convergence and confrontation are two different strategic options that have been evoked with respect to the relation between MERCOSUR and the Pacific Alliance. Choosing one or the other transcends the level of the economic and the commercial, and deeply affects the political. Their impact is closely related with regional governance and the achievement of a climate of harmony functional to democracy and to the economic and social development of member countries.

The idea of convergence in diversity has been proposed as central to the development of a strategy to joint work among the member countries of both integration processes. The different agreements and measures eventually adopted by member countries of both schemes could contribute to the goal of achieving a reasonable degree of regional governance. Showing that this is possible might be a worthy goal to nourish the agenda of cooperation between all Latin American countries. Its effects would then transcend the regional scope.

## **From the Founding Moments to a Sustainable Integration Process**

Reconciling different and even conflicting interests and views among nations of the same geographic region has never been an easy task. However, it is a necessary condition to develop sustainable strategies and policies for regional economic integration, including joint trade negotiations with third nations, particularly if they are embodied in agreements and institutions intended to be permanent.

In a way, the foundation is the easy stage of an integration process among nations of the same region. For example, in the case of MERCOSUR –and this could eventually be the case of the Pacific Alliance– the hardest part was not necessarily signing the founding agreement in 1991. The initial moment requires, of course, strategic vision and political skill; but, it also requires luck. Many initiatives succumb or loose vitality in this first stage which, however, can last several years.

Calling the attention at the international level is a common occurrence in the founding moments of the integration processes between nations and, as a result, it generates great expectations. For example, it happened in 1969 with the signing of the Agreement of Cartagena, which was the result of a very strong involve-

ment of the then presidents of Chile and Colombia. In its initial stage and for some years, the so-called Andean Group managed to concentrate much international attention, especially when it adopted, in December 1970, its foreign investment regime known as Decision N° 24.

The high expectations that are normally generated by the launch of an international integration agreement between Latin American countries have usually led to frustrations, sometimes very difficult to overcome. Something like this happened over fifty years ago with the launch of the Latin American Free Trade Association (LAFTA), then replaced in 1980 by the Latin American Integration Association (LAIA). Different regional integration experiences –and not only in Latin America– have taught us the difficulty of sustaining in the long run the reciprocity of interests that support the associative pact. Sooner or later what could be called the ‘curve of disenchantment’ starts to show, often caused by the fact that not all participating countries continue to view the corresponding agreement as a generator of mutual gains. At this point is where the loss of effectiveness, efficiency, and legitimacy of the rules originating in the founding agreement begins, often through a trickle effect (Peña 2014a).

Particularly, changes in the realities at the regional level –sometimes as a result of changes at the global level or even at the national level of member countries– present a test for the effectiveness of the mechanisms implemented for the conciliation of national interests among the members of an integration process. This may also have an impact on the effectiveness of the common rules that have been agreed. An example of this can be portrayed in the evolution of the Andean Group and its main joint body – the Board of the Cartagena Agreement– which lost efficacy and even legitimacy after a founding period with a favorable external context and affinity of values and interests between the member countries. Then, the decline began with the withdrawal of Chile and after the transformation into the Andean Community of Nations (CAN); eventually, the original enthusiasm was gradually eroded.

The situation may be more complicated when a founding moment characterized by the affinity of values and interests –a situation of like-minded countries– is later followed by periods of significant differences between the partners, even if temporary. It also becomes more difficult when no effective mechanism for the conciliation of interests is established to help achieve a dynamic balance between the different national interests, when these do not necessarily converge. In this regard, the role of the ‘independent facilitator’ in the decision-making process is critical and provides a guarantee for those participating countries with a smaller endowment of relative power. The relatively short history of MERCOSUR shows, at different moments, interesting examples of this. It is even possible to formulate the hypothesis that the absence or weakness of effective mechanisms to facilitate the coordination of national interests has been one of the reasons that would explain the recurring difficulties that MERCOSUR had, and still has, to adapt to the effects of the internal and contextual changes dynamic that have

characterized the relations between its member countries –Argentina and Brazil in particular– since the integration process was launched.

### **Factors that Could Contribute to a Sustainable Integration Process**

Which are then some of the factors that could help sustain over time the political will of a group of sovereign nations to work together, within the scope of an integration process intended to be permanent? Without the concurrence of these factors it seems difficult for a voluntary process of integration –in the sense of systematic joint work between sovereign nations– to be sustainable in the long run.

From the different Latin American experiences it seems that three factors should be considered carefully.

The first one is the ability to adapt the original integration project to the frequent changes in the political and economic conditions of the member countries, including also the external environment, both regional and global.

The second aspect is the density and quality of the economic and, above all, production networks that are developed as a result of the commitments made in the framework of the integration process.

And a third factor, strongly linked to the previous one, is the quality of the ground rules as measured by their effectiveness (ability to penetrate reality), their efficacy (ability to produce the results) and their social legitimacy (the ability to take into account, through the process of rule-making, the social interests of all member countries, reflecting thus a dynamic picture of perception of mutual gains).

There are at least three relevant aspects that could be of importance to facilitate the practice of the difficult art of achieving sustainable equilibrium points in any institutional agreement among nations of a same geographic region. Especially if they aspire to develop a permanent multidimensional cooperation process with strong emphasis on trade and productive integration, such as is the case of MERCOSUR and now of the Pacific Alliance.

The first aspect is the articulation of the strategies for development and international integration of a country with the requirements of the corresponding regional or multilateral agreement. Among many others, an example in this regard are the trade policies needed to be applied in view of the combination of offensive and defensive interests of the firms and social sectors of a country along with the legal commitments relating, in particular, to the access to the respective domestic market and trade protection. In times of global economic crisis with a relative decline of international trade flows, the natural tendency of every country could be to protect the jobs of its population. Often, this is done covertly and with such legal subtlety that it becomes difficult for those eventually affected by the policy of one of the partners to prove that the agreed rules have been violated. Other times, violations are done overtly and this affects the international credibil-



ity of the country applying the measures contrary to the agreement, and could eventually have a negative impact on the effectiveness of the integration process.

The second relevant aspect is the articulation between the different preferential agreements in which countries can participate, including the commitments made at the global-multilateral level. In fact, it is increasingly common for a country to participate simultaneously, or to aspire to do so, in different regional and preferential trade agreements concluded, at least formally, within the multilateral framework of the WTO. This may eventually trigger the need to achieve equilibrium points between the commitments made in the different agreements and the respective national interests. Achieving such balance also depends on the concessions and the rules agreed upon in each of the agreements. In particular, it depends on the actual goals and the political and strategic scope of each concrete regional preferential agreement.

Finally, the third aspect is the articulation between the requirements of the short and the long term, both in the national strategies and in the international commitments taken on by a country. What can be observed on this respect, at least in recent years, is an effect of growing erosion of the distinction between short and long term interests resulting, among other factors, from the close link between trade and productive investment, which is reflected in the new forms of organizing production at a multinational level. In fact, the fragmentation of production in different modalities of transnational value chains is generating a great difficulty to distinguish between the short and long term effects when a country applies restrictive trade policies. Depending on how they are applied, even when theoretically, such measures would impact only short term trade flows. In addition, they may also have a strong effect on investment decisions in the corresponding country as a result of the appraisal that is made on the convenience of operating from its market within the context of a transnational value chain. The uncertainty regarding trade flows can then affect productive investment decisions that, while aimed for the long-term, also have a bearing on the short-term. In the automotive industry, for example, it can lead investors to prefer those countries within a region that, together with market size and level of industrial development, provide assurance of the fluidity of cross-border trade flows.

### **The Relationship between MERCOSUR and the Pacific Alliance**

An issue that is worth monitoring closely is the relationship that has developed between the two main Latin American preferential spaces: the Pacific Alliance and MERCOSUR (Foxley and Meller 2014). It is a matter of economic interest, but also of strong geopolitical connotations. It should be noted that the relations among several countries of the Pacific Alliance with MERCOSUR countries, and particularly with Argentina and Brazil, are very close at all levels and transcend trade.

Hence, the importance of raising the question of whether these two regional preferential spaces will complement each other or if, on the contrary, will challenge views still prevails. It is a question that could take time to find an answer that is based on solid arguments and not only on ideological or emotional ones. Among other reasons, time could be necessary in order to have a clearer picture of which are the effective commitments that are eventually manifested in the space of the Pacific Alliance and to appreciate the true scope of the present ‘metamorphosis’ of MERCOSUR. This is, the effects resulting especially from changes in its membership, the convenience of capitalizing on the experience gained since its creation, and its recommendable adaptation to national, regional and global realities different from those of the time of its creation (Boletín Techint 2014).

Until now, the Pacific Alliance could be the equivalent to the process of building a house. The willingness to do so exists and the plans are being approved. But, the actual construction will take time, which in turn may be impacted by the dynamics of change of the external environment. MERCOSUR is also the equivalent of a house under construction –the current experience of the EU shows that this is a constant reality of voluntary integration processes among sovereign nations (Friedmann 2015; Van Middelaar 2013) – but, it already needs to be expanded and adjusted to the new realities of its owners and the environment in which they live.

Both constructions are developed within the broader institutional frameworks that exist in the region. All of them aim to ensure regional governance, in terms of peace and political stability, and not just in the economic aspect. These are, in particular, the frameworks of the LAIA and the UNASUR –and to some extent also that of the CELAC–. Additionally, there are also regional institutions such as the ECLAC and the CAF-Development Bank of Latin America that can play a very useful role in facilitating the articulation between both integration processes (Peña 2014b).

How to get both processes to complement each other, generating a convergence of development and trade policies and also achieving a growing number of transnational production networks? This is perhaps the central question on which to base the future articulation between MERCOSUR and the Pacific Alliance from now on, while maximizing the installed capacity within the scope of the regional institutions mentioned above.

### **The Strategic Idea of Convergence in Diversity**

As stated earlier, one can reflect on the latest initiative that has been raised in terms of Latin American regional integration (Peña 2014b). It comes at a time when the multilateral trading system is still unable to offer interesting negotiating perspectives, beyond the efforts at the WTO Ministerial Conference in Bali and,

most recently, the launch of the negotiating process aimed at concluding a plurilateral agreement on environmental assets.

But even if the outlook of such perspectives became more optimistic, the initiative that has arisen within the scope of the Pacific Alliance is opportune, as it can lead to a renewal of the methods for the enhancement of the regional space in terms of the productive development of each country and of their insertion in global economic competition.

This initiative was proposed on June 20, 2014, in Punta Mita, Mexico, where the Ninth Summit of the Pacific Alliance (Chile, Colombia, Peru and Mexico) took place (Peña 2014c). Among other things, it was agreed "to hold an informative ministerial meeting on the Pacific Alliance with countries members of MERCOSUR." Moreover, "with the same informative spirit," the Presidents agreed to "conduct a seminar of academics, businessmen, entrepreneurs and senior officials of the Pacific Alliance, MERCOSUR and other countries of the region, including Central America and the Caribbean."

The initiative of Punta Mita opens a window of opportunity for the discussion of the strategic idea of "convergence in diversity," presented by the new government of Chile.

We must keep in mind that convergence and confrontation were, until Punta Mita, the two main alternatives evoked by the relation between MERCOSUR and the Pacific Alliance. It is clear that choosing one or the other transcends the economic and the commercial and deeply affects the political, as their impact is closely related with regional governance and the predominance of a climate of harmony functional to democracy and to the economic and social development of the member countries.

It is important to have accurate data on the reality of the relations between the countries of both regional spaces. Hence, the relevance of the publication of the ECLAC report entitled "*The Pacific Alliance and Mercosur. Towards convergence in diversity*" (only in Spanish) (CEPAL 2014), which provides the necessary information for an approach based on the reality of the relations between MERCOSUR and the Pacific Alliance.

The report was specially prepared to be presented at the Seminar on "*Dialogue on Regional Integration: Pacific Alliance and Mercosur*," which was held on November 24, 2014 in Santiago de Chile (Peña 2014d), based on the agreements reached in the Punta Mita Summit. The seminar was held with the presence of the public and the media; and it was opened by the President of Chile. In her opening remarks she urged for dialogue and to "dream out loud." The initial presentation was made by the Chancellor of Chile, in where he outlined the main strategic ideas of convergence in diversity and the objectives of the dialogue that was to take place at the Seminar. In this regard, it should be noted that the Ministers of Foreign Affairs of the member countries of both schemes had a working meeting two weeks earlier, in Cartagena de Indias, Colombia, in which the central theme of the seminar was addressed.

The abovementioned ECLAC report helps verify the density of the network of agreements and existing relations between the countries from the Alliance and MERCOSUR. It is a network that has intensified in recent decades, especially in some of its connections, such as those in the bilateral trade between Chile, Peru and Colombia, on the one hand, and Brazil and Argentina, on the other. For example, the partial agreements signed between these countries, within the framework of the LAIA, and the relations between MERCOSUR and the Andean Community of Nations, have already produced a complete tariff reduction between Chile and MERCOSUR countries (100 percent). The percentages are also high in the cases of Peru (88 percent) and Colombia (90 percent). Another relevant fact is that in 2013 intra-MERCOSUR trade represented 14 percent of the global trade of its member countries, while intra-Alliance trade represented only 3.5 percent. In the first case, the percentages are much more significant if one considers the trade of manufactures. In turn, exports of the countries of the Alliance to MERCOSUR are higher than intra-Alliance (in 2013, intra-Alliance exports were US\$19,500 million whereas those destined to MERCOSUR totaled US\$23,700 million). Chile, Colombia and Mexico exported more to MERCOSUR than to the Alliance countries. Additionally, data on the trade of services and investments –even if incomplete– reveals the intensity of the relations between the Pacific Alliance and MERCOSUR countries, especially with Argentina and Brazil.

As a result of the rich dialogue generated at the Seminar in Santiago de Chile it became clear that participants value the idea of "convergence in diversity." They view it as the most appropriate strategy in the current global economic and political context and as a reflection of how much has been gained in the relations between its members after more than fifty years of regional integration efforts.

As pointed out from the beginning of the Seminar, first by President Bachelet and later by Chancellor Muñoz, convergence does not imply unifying the two integration schemes nor engaging in tariff negotiations (without prejudice to strengthening the existing ones within the scope of the LAIA). It does imply, however, recognizing and respecting the differences between the objectives and the methods of both schemes, and also even between the trade and development strategies and policies of its member countries.

Various issues were identified as deserving priority action. These were mentioned by several participants of the Dialogue of Santiago and also in the ECLAC report. Among others, the main ones were: physical connectivity; trade facilitation; production linkages and SME participation in them. Moreover, student exchanges, including reciprocal internships between companies; the development of tourism; diagnostic capabilities on global economic competition; innovation and scientific and technological development, and monitoring and participation in international trade negotiations, both at the global multilateral level and at the interregional level.

With regard to the relations with other regions, the need to coordinate positions on events of importance for Latin America (for example with China and the EU) was pointed out. In some of these cases the Community of Latin American and Caribbean States (CELAC) has a central role in coordinating the positions of the countries of the region. The coordination of positions in relation to the G20 meetings and the Conference on Climate Change (COP21), to be held in Paris in December of 2015, was also mentioned.

In our opinion, the meeting left positive results. The first of these was to place MERCOSUR and the Pacific Alliance, each with its own objectives and methodologies, in the broader context. Adding to the dialogue the strong more recent challenges that are emerging at the global level and of the opportunities that are opening up for a region that counts, as one of its main assets, the fact that it belongs both to the Pacific and to the Atlantic and that has a significant potential for developing products and services linked with agribusiness, energy and mining, among others (Lula and Lagos 2014). The second result was to identify those issues and sectors where it is feasible to have shared approaches between all or some of the countries of both schemes. And the third result was to show that the dialogue and the exchange of views with the participation of representatives from governments, production and labor sectors and the academia, is the most recommended way to expand the agenda for the construction of a region in which convergence in diversity predominates.

### **Some Conclusions**

Perhaps the main challenge that was posed as a result of the Santiago de Chile Seminar is to devise and recognize the need to develop short agendas and road maps for the priority areas of future joint action between the members of the different integration schemes. It is a challenge that involves governments but also business, labor and academic institutions.

On that occasion it was also confirmed that the existing institutional framework of the region opens a wide range of possibilities in terms of the areas through which to harness the momentum and pursue the development of those joint actions identified, as well as of those that are favored in the future.

If inserted in common institutional and regulatory frameworks, such as the LAIA at the regional Latin American level, or a renewed and strengthened WTO at the global multilateral level, this would neutralize the systemic fragmentation trends observed today.

It is an idea that may be central so that the agreements that are being negotiated contribute to the goal of achieving reasonable guidelines for regional and global governance. It involves reconciling the partial scope approaches with a joint vision that is essential for promoting world trade in a favorable context for peace and political stability and, at the same time, for the economic and social development of all countries.

Showing that this is possible might be a worthy goal to nourish the agenda of cooperation between Latin American countries. Its effects would then transcend the regional scope. It will require, however, a good dose of perseverance, technical imagination and political will.

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# Regional Integration in Latin America: A Diagnosis of the Crisis

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## Abstract

Initiatives built around what is known as ‘political concertation,’ whose theoretical basis is the so-called ‘post-neoliberal integration’ have pushed the integration process into a permanent headlong rush forward. This analysis aims to present a general diagnosis of the integration process and describe the short and long-term options for interregional cooperation. Cooperation in different spheres could be a useful option to the current issues among the various players involved until a solution is found – the Andean Community (CAN) and MERCOSUR within UNASUR, and MERCOSUR and the Pacific Alliance–. From this perspective, this paper analyses the emergence of the Alliance in relation to its capacity to be, or to come to be, a catalyst for the future of integration.

## Introduction

In Latin America there is a universal consensus among political, economic and social players about the positive virtues of regional integration. The process is seen as a catalyst for economic growth and as an important instrument to reduce national inequalities and increase social cohesion. The problem with this is the cost of integration and the necessary effort involved, as there is a common belief –even promoted by the governments themselves– that the process is not only inevitable but a sure winner also.

If progress towards regional integration is to be made, Latin American countries should tackle a number of reforms to facilitate the convergence of their institutions and economies which, at the same time, can help them escape the middle-income trap. But for that to happen it would be necessary to clarify the objectives, sort out the goals and dispense with the rhetoric that usually accompanies the process, without jettisoning politics, without which progress is impossible.

From the rhetoric point of view, the idea of integration is usually accompanied by the concept of the *Patria Grande*, the ancestral voice that assures that a successful process throughout the region is inevitable. Thus, the idea is that certain teleological and ahistorical instincts have forged a feeling of regional belonging that has existed since the beginning of times - UNASUR’s founding treaty (UNASUR 2008) notes that one of its leading aims is to affirm regional identity as a ‘dynamic factor in international relations.’ Regional integration sometimes appears to be more a question of reaffirming an identity than of converging



interests.

Once beyond the first threshold of unanimity, the problems appear, concerning answers to basic definitions almost completely lacking. What is to be integrated? What sort of integration is required? In what political, economic and energy issues is progress to be made? Should all countries integrate simultaneously?

The lack of clear answers to these questions has led to sharp divergences in the integration process. Half way through the first decade of the 21<sup>st</sup> century, coinciding with the surge in the cost of energy products, energy was presented as the catalyst of integration. The prevailing belief was that the mere existence of state-owned hydrocarbon companies would make things easier. But, in the same way that the process began, it ended by fizzling out. Sometimes the correct questions were just not made, while others the medium and long term inquiries were ignored, although both are vital in questions such as these.

The weaknesses of the plans for regional integration are clear in the G-20, even with a strong Latin American presence. The region has been incapable of speaking with a single voice. The presence of Argentina, Brazil and Mexico has not been sufficient to hammer out a common position with the rest of the region in regards to the most pressing issues of the international economic and financial agenda. The same can be said about the negotiations with China and the EU. All the intergovernmental talks with China are bilateral. With the EU, the situation is somewhat more complicated, despite the initial European position of only negotiating with regional or sub regional integration entities, such as the CAN, MERCOSUR or the Central American Integration System (SICA). At the end, an Association Agreement was the only reached with Central America, while the remaining accords were signed with four individual countries: Chile and Mexico, on the one hand, and Colombia and Peru, on the other. It is no coincidence that these four countries are the founding members of the Pacific Alliance. Overcoming its original misgivings, Ecuador is on the verge of finalising its negotiation with the EU in similar terms to Colombia and Peru.

### **Regional Integration in Crisis**

If one were to define the present state of Latin American integration it could only be described as in crisis. Latin America is more than ever a divided region. It is not a split into opposing blocs but separated by multiple divisions, which are difficult to bring together. A result of this crisis is that the CAN has practically dissolved since Venezuela's exit in 2006.

It is striking that Latin America has such an overabundance of regional integration schemes –Community of Latin American and Caribbean States (CELAC), UNASUR, MERCOSUR, CAN, SICA, Bolivarian Alliance for the Peoples of our America (ALBA), Pacific Alliance, and many more– all of them incapable of cooperating efficiently with each other. To the contrary, they merely

indulge in a constant headlong rush forward, with new initiatives remaining incapable of resolving the problems faced by their predecessors.

Since the beginning of the 21<sup>st</sup> century, the integration process, which until then had revolved around trade and the economy, has shifted towards political cooperation. The stance of certain regional governments regarding free trade and the Free Trade Area of the Americas (FTAA) prompted the creation of ALBA and the signing by Cuba, Venezuela and Bolivia of the People's Trade Agreement (TCP).

Although politics cannot be relegated to the side-lines in this type of processes, the excessive politicisation of Latin American integration, heightened by the presidentialism character of many regimes in the area and their consequent bent for presidential diplomacy, has tainted institutions such as MERCOSUR. The creation of UNASUR and CELAC as purely political bodies is a good example of the phenomenon.

Free trade was at the heart of integration since the creation of the Latin American Free Trade Association (LAFTA) in 1960 until its demise in 1980. At the high point of imports-substitution industrialisation policies, both frontiers and customs barriers were the main obstacle to the expansion of intraregional trade and integration. The weakness of intraregional trade is proverbial and that is precisely one of integration's main weaknesses.

In the absence of common interests there is a weaker incentive to generate synergies. Intraregional trade accounts for around 19 percent of Latin American and Caribbean foreign trade, far below Asia-Pacific's 56 percent and the EU's 70 percent (Eclac 2014b). According to Eclac, in 2013/14 the highest proportion of intra sub-regional trade was recorded by the Central American Common Market, at 23.1 percent the only sub-region above the regional average (Eclac 2014a). At the opposite extreme is the CAN at 8.5 percent, while MERCOSUR is at 14.6 percent. In relation to Latin American intraregional trade and based on 2011 data, while the Pacific Alliance came in at 11.8 percent, MERCOSUR reached 26.2 percent.

## **The Obstacles to Integration**

The weakness of the current integration process can be approached from a number of angles. Several interpretations are made from a clearly discursive, mainly political stance, with a self-exculpatory purpose. The idea is to justify the scant progress achieved by pointing to the process' novel character while in fact it is as old as Europe's. Another explanation is that integration is failing to progress because of the frontal opposition of outside forces, namely the US and, to a lesser extent, the EU: if Latin America has been unable to integrate it is because foreign powers are preventing it. However, what the current regional fragmentation proves is that it is more difficult now than in the past to make most countries agree regarding certain issues on the international agenda or in votes in suprana-

tional bodies such as the UN and the OAS.

By attributing the lack of success to the novelty of the process or to foreign conspiracies, the debate on the current state of integration is delayed indefinitely. Although the issue is widely disputed in academic circles, it should be subject to a profound intergovernmental debate both regionally and sub regionally. At the same time, the issue should be dealt openly, at a national level, by Latin America's governments and societies.

A contrary effect to the desired objective has also been caused by 'presidential diplomacy.' The excessively central role played by presidents in foreign policy, along with the hyper-presidentialism prevailing in most of the countries, debases that of the technical experts, advisors and specialists. The trend was further aggravated at the time of the so-called 'turn to the left' because of the belief that a greater coincidence between politics and ideology would not only facilitate integration but also speed it up.

Despite the hopes laced on political convergence, things did not turn out as expected. Halfway through the first decade of the 21<sup>st</sup> century, when the process was at its peak and it was thought that the personal chemistry between presidents would pave the way for success, a number of bilateral conflicts broke out. In contrast to the past, they were no longer connected to traditional border disputes, but to economic and political motives, as in the paper-mill spat between Argentina and Uruguay.

Finally, we should not disregard the prevalent idea that integration can only bring benefits, with no costs or sacrifices involved for either countries or societies, particularly those with lower economic growth or social cohesion. This also leads to the premise that integration must simultaneously involve all the countries in the region. At the medium and long term these ideas make integration more difficult because they have a negative effect on the convergence process and on the efforts each government should make. Along with overblown rhetoric, there are two further significant hindrances to integration: overblown nationalism and an absence of leadership (Malamud 2010).

The emergence of nationalism was simultaneous in all Latin American republics at the start of the 19<sup>th</sup> century and was a key factor in the formation of their national identities. Since then, nationalism has permeated all political ideologies, from the far right to the far left. Even indigenism has absorbed a strongly nationalistic component. Nationalism has distorted the idea of sovereignty in the region. Sovereignty is usually understood as territorial sovereignty, the fatherland and its values, rather than civic sovereignty. As for regional integration, progress is impossible without relinquishing a minimum of sovereignty to supranational institutions.

The absence of leadership makes it difficult for integration processes to progress significantly. Neither of the two major countries, Brazil and Mexico, has been willing to take on the costs of leading the process, arguing, among other reasons, that their governments possessed only limited resources. Hugo Chávez

attempted to fill the leadership void by investing a large volume of funds and even political capital in the venture. But, the Bolivarian attempt to monopolize integration was rejected by a number of countries. Following Chávez's death the project has been further questioned, although not openly so far.

The absence of leadership has been aggravated by the historical disagreements between Brazil and Mexico. This is the reason why no answer has been found to what should be the subject of regional integration: Latin America or South America? The latter is Brazil's preferred option, as it excludes Mexico. The reasoning of Itamaraty, both public and private, is that following the signing of the North America Free Trade Agreement (NAFTA) Mexico turned its back on Latin America. In contrast, Latin America is Mexico's favoured option, despite its involvement being marginal and merely rhetorical for quite some time.

The vision of South American integration should not conceal the imbalances between Brazil and the other countries of South America, as is evident in MERCOSUR, where the small countries complain about how they are treated by the big ones. Brazil has a common frontier with all of the region's countries, except Chile and Ecuador. But imbalances are evident when comparing sizes, surfaces areas, income and per capita income. Hence, a regional integration process focused on Latin America and with Brazil and Mexico as its main promoters would diminish Brazil's image as South America's hegemonic power, behaving much like the US, which is an image that deeply distresses the Brazilian elites.

### **The Roles of UNASUR and CELAC: How Useful Are they for Integration?**

Over the past decade two regional integration bodies have emerged, in different but overlapping geographical areas, although in both blocks political dialogue has been more important than other considerations. Both have been presented as models for 'post-neoliberal regionalism,' with this theoretical perspective even being used to justify their coexistence. Furthermore, some experts on regional integration view the coexistence of MERCOSUR, UNASUR and CELAC positively, as concentric circles, which might boost more than hinder integration.

UNASUR was created in 2008 with all South American countries involved while the CELAC was set up in 2010. Although a large number of countries belong to both organisations, on this occasion neither the links nor the coordination mechanisms between the two were decided upon. Neither did anyone take any time to explain why the two were necessary simultaneously.

Their coexistence poses future serious problems. For how long can the fiction that the simultaneous existence of UNASUR and CELAC reinforces integration rather than weakening it be sustained? If South American, Latin American and Caribbean countries wish to move ahead—~~in~~ this way they will have to decide at some point what to do and which agreement to suppress. If they opt for Latin American it will be UNASUR that will have to disappear, despite having a far better and more complex political-administrative structure. But the region's

governments must promote a broader debate on the future of integration and start to make the necessary decisions.

The primacy of political dialogue over economic or commercial considerations is evident in the inception of UNASUR. According to its founding charter, “the Union of South American Nations has as its aim to build, in a participatory and consensual manner, a space for integration and union in the cultural, social, economic and political spheres among its peoples, prioritising political dialogue, social policies, education, energy, infrastructures, financing and the environment, among others, with the object of eliminating socioeconomic inequality, achieve social inclusion and citizen participation, strengthen democracy and reduce asymmetries in the framework of strengthening the sovereignty and independence of States” (UNASUR 2008). UNASUR began by focusing on political dialogue and the creation of sectorial councils. There are currently 12 South American councils, which deal with a large number of issues, although none of them tackles trade.

UNASUR initially implemented some important initiatives to resolve internal problems in certain countries, such as the regional crisis in Bolivia or the military uprising against Rafael Correa in Ecuador. The initiatives were carried out from the perspective that the countries in UNASUR would be able to solve their own problems without resorting to outside help. However, UNASUR was either unwilling or unable to intervene in bilateral conflicts. In all cases the solution was reached in extraordinary presidential summits, in emergency sessions rather than through standard institutional mechanisms. Over the past two years UNASUR’s mediating role has declined, as was made evident in the attempt for dialogue between the government of Nicolás Maduro and the Venezuelan opposition.

CELAC was also the convergence of two distinct initiatives. On the one hand, Mexico was interested in regaining its prominence in Latin America, while, on the other, Venezuela and the ALBA countries, with Cuba to the fore, aimed to recreate the Organisation of American States (OAS) but excluding the US and Canada. Its main achievement was to get Cuba back into a Latin American institution, although it did not return to any continental body since Havana did not request its re-admittance to the OAS.

### **The Current Situation and the Emergence of the Pacific Alliance**

Beyond anything that can be said about the originality and specificity of Latin American integration, in the medium to long terms the coexistence of two institutions such as UNASUR and CELAC, more than promoting integration, has given rise to an almost insurmountable obstacle to the intended objective. The rhetoric of the *patria grande* has led to the belief that this institutional coexistence is actually an instance of Latin American richness and creativity. However, what it actually denotes is the lack of definition about what it is that should be integrat-

ed.

The formal constitution of the Pacific Alliance changed some things and introduced some interesting novelties (Malamud 2012). The Alliance's impact has been greater following Hugo Chávez's exit from the Latin American scene, as his strong regional leadership has had no successor. Simultaneously, Venezuela's serious economic difficulties have prevented its government from continuing to finance a particular integration project led by the ALBA.

The Alliance's creation has reintroduced, first, the centrality of trade and the economy to integration. Following the creation of ALBA and the demise of ALCA, free trade was condemned, political convergence took centre stage and the concept of post-neoliberal or post-capitalist regionalism began to gain ground, ushered in by open regionalism.

Secondly, and based on pure pragmatism, the Alliance resolved the question of what to integrate: Latin America or South America? Among the four founder members there are three South American countries and one North American nation. Among those with the status of observers, who may be the next members, there are two Central American nations: Costa Rica and Panama. The Alliance's existence is a challenge to Brazil and its South American project.

Third, it has reinvigorated the role of companies and private entrepreneurs in the integration process, after having been relegated by the excessive statism of a large number of the region's governments. The Pacific Alliance's Business Council is formally linked to the organisation. As for the role to be played by entrepreneurs in the regional integration process, the good news was the resolution of the border dispute between Chile and Peru by the International Court of Justice at The Hague and the response of the two parties involved.

Another important initiative to foster the free circulation of capitals and services is the Integrated Latin American Market (MILA), made up of the stock exchanges of Bogotá, Lima and Santiago and which have just been joined by Mexico. With the latter, their market capitalisation adds up to US\$1.2 billion, compared with Brazil's US\$1.5 billion (IADB 2014). A significant hindrance is the lack of sufficiently harmonised regulations and sufficiently coordinated supervisors. A greater regional integration of financial institutions would increase competition and the quality of regional financial services.

### **The Difficult Relations between the Pacific Alliance, MERCOSUR and ALBA**

The Alliance's main objectives are: (1) to build, on a participatory and consensual basis, a well-integrated space to steadily progress towards the free circulation of goods, services, capital and people; (2) foster growth, development and competitiveness to ensure greater well-being, overcome socioeconomic inequality and enhance social inclusion; and (3) to become a platform for political coordination, and economic and commercial integration, and for the region's projection in the rest of the world, with a particular focus on Asia-Pacific. The Alliance has a

large potential because its members share the same economic model, have compatible monetary and exchange rate policies and strong financial institutions.

In contrast to other regional or sub regional integration projects, the Alliance's four member countries have signed free-trade agreements (FTA) with each other, along with the many FTAs they have signed with much of the rest of the world, starting with the US and the EU. The degree of openness the Alliance economies have attained contrasts with those of MERCOSUR and ALBA.

For a variety of reasons the Alliance has caused a feeling of rejection among the ALBA countries and a degree of indifference, or even disdain, of certain MERCOSUR countries such as Argentina and Brazil. The Alliance emergence has led the ALBA to seek a common position to face up to it. Thus, it is promoting an economic zone for "shared and complementary development, in solidarity, respecting asymmetries, beyond mere trade," to which it hopes to attract CARICOM and MERCOSUR.

The proliferation of statements along with the markets' preferences for the potential of the Alliance's members led to talk of a conflict between the Pacific and the Atlantic, or between the Alliance and MERCOSUR. In fact, the slowdown in the Brazilian economy was contrasted with the success of the new regional powers (with Colombia having recently overtaken Argentina to third place in the regional ranking), increasing the bitterness of the criticism by both Argentina and Brazil.

## **Conclusions**

The first conclusion should be that regional integration is in crisis and that the entire region's governments –or at least the major ones– should promote a profound debate about the integration characteristics and process. To do this, the current state of fragmentation must be recognised and presented not as a catastrophe but as an opportunity to embark on a systematic search for viable solutions. One of the most important questions to be answered is about the object of integration, what is to be integrated, because this issue cannot be left to the vagaries of fate or to the good intentions of those involved in such a delicate situation.

From this perspective, it is obvious that integration should not be presented simply as a process for the construction of an identity. Integration should basically revolve around the convergence of different national interests to a point where solid institutions can be built. It is not only a case of fomenting the convergence of policies or ideologies but also of the need to allow the coexistence of different natures that are able to cohabit in the same integration bodies without having to engage in open conflict with their opponents.

Contrary to what has been affirmed of late, that the significant progress achieved over the past decade by UNASUR and the CELAC has been due to the region's progressive governments, in reality the fact is that this has been one of

the process's main weaknesses. This is not because these governments are of a specific political bent but because of the implied uniformity. Regional integration is not speeded up by governments coinciding in their ideologies but by the possibility of starting to share permanent interests. These national interests are above any circumstantial change brought about by the existence of different governments, especially bearing in mind that one of the chief characteristics of democracy is the peaceful alternation of power. It is necessary to definitively discard integration proposals that serve to justify certain specific ideological models. In this respect, the so-called 'post-neoliberal regionalism' has acted as a justification for the swing towards political convergence and the relegation of trade and the economy as the backbone interconnecting the region. In fact, what integration requires are long-term proposals to help focus on issues from a strategic perspective, simultaneously incorporating politics with trade and the economy.

The emergence of the Pacific Alliance has shaken up the regional integration scene. It has served not only to again bring up the question of what is the object of integration –South America or Latin America– and to resolve it through direct action, but also to again bring to the fore the role of trade and the economy along with that of private initiative.

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