

ARGENTINE - BRAZILIAN  
ECONOMIC INTEGRATION:  
An Early Appraisal\*

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Attempts have been made at Latin American regional integration since the late 1950s, but on each occasion, high expectations have met with disappointing failures. In July 1986, however, a new phase began in the history of Latin American integration as Presidents Raúl Alfonsín of Argentina and José Sarney of Brazil signed the Argentina-Brazil Economic Integration Pact (ABEIP).<sup>1</sup>

At its inception, the ABEIP generated a great deal of enthusiasm for political as well as economic reasons. In political terms, the ABEIP process began at a time when Argentina and Brazil were emerging from long periods of military rule, and it represented a means of reinforcing the consolidation of democracy in both countries. Moreover, the ABEIP symbolized a historic landmark in Argentine-Brazilian relations, which had traditionally been characterized by rivalries and disputes over regional leadership in South America. The establishment of the ABEIP implied that in the future, these relations would be shaped by a cooperative spirit that could have constructive repercussions throughout the subcontinent. In economic terms, the ABEIP would potentially unite two of the largest markets in South America, which accounted for more than two-thirds of the region's population as well as its industrial and agricultural production. In addition, the ABEIP marked a new development

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in the economic integration of Latin America in its efforts to avoid past mistakes while introducing innovative features. In essence, the ABEIP was based on an unprecedented formula for gradual unification that allowed new partners to join in the future.

Since the first protocols were signed in 1986, however, progress for the ABEIP has gradually come to a halt. Why should this be the case? Did structural differences in economic development and market size prove too big to be overcome? Or have the governments involved failed to coordinate their macroeconomic policies? Or were its economic provisions conceptually sound but not implemented due to administrative problems? Or is the impasse attributable to ensuing political instability in Argentina and Brazil that has prevented Alfonsín and Sarney from pushing further initiatives and fostering support among interest groups for the integration effort?

This article will contend that a combination of structural, financial, administrative, and political problems together account for the ABEIP having reached a standstill after its very promising start. I will argue here that the main drive behind the integration effort was the political willingness of the two presidents rather than the initiative of grass-roots economic and social groups.

The article consists of eight sections. The first examines the theoretical foundations of previous integration efforts. The second presents the circumstances that led to the accords. The third analyzes the main characteristics of the ABEIP (particularly the most important first protocol) and compares it with early experiences. The fourth describes how the accords have progressed since the signing of the first protocols. The fifth appraises the results achieved so far from political and economic points of view. The sixth discusses the structural, financial, administrative, and political problems encountered by the ABEIP. The seventh draws some lessons from the ABEIP experience, and the eighth discusses the ABEIP's prospects in the near future.

#### **THEORETICAL FOUNDATIONS AND EXPERIENCES OF LATIN AMERICAN INTEGRATION**

Since the 1950s, the main proponent of regional economic integration has been the Economic Commission for Latin America (ECLA), spearheaded by its director at the time, Raúl Prebisch. According to the ECLA perspective, economic integration represented a means of furthering the process of import-substituting industrialization that was already underway in the region. ECLA economists argued that the low level of international competitiveness of domestically produced industrial goods, coupled with the limited markets provided in Latin America, would sooner or later lead to exhaustion of the first stage of the import-substitut-

ing industrialization process and result in unused productive capacity. Regional integration was regarded as a means of providing a market large enough to satisfy economies of scale, which in turn would deepen import substitution. In this way, Latin American industries could produce at full capacity and over time would lower their costs, increase their production, and eventually become competitive internationally. Moreover, to avoid fragmentation and duplication, countries would complement each other's industrial production through specialization. Nonreciprocity and preferential treatments were to be granted depending on the level of economic development of individual countries. Tariff barriers, however, would be erected against nonregional competitors in order to give Latin American products an edge.

In a contrasting view, free-trade economists like Roberto Campos of Brazil and Roberto Alemann of Argentina contended that specialization, preferential treatments, and complementarity would lead to price distortions, resource misallocation, and trade diversion that would prevent countries from importing cheaper goods from producers outside Latin America. Yet despite their divergent views, many free-traders supported integration for different reasons. They favored customs unions as a means of allowing the free interplay of market forces so that industries would be forced to improve product quality while cutting costs if they wanted to survive. The outcome expected was increased economic efficiency.

The Treaty of Montevideo, which gave birth in 1960 to the Latin American Free Trade Association (LAFTA), represented neither ECLA's nor the free-trade economists' point of view. Instead, it reflected an uneasy compromise of the two contending views that from the outset prevented any serious integration effort like that advocated by Prebisch. The main proponents of LAFTA—Argentina, Brazil, and Chile—were mainly seeking trade expansion rather than integration. LAFTA was established as a free-trade area, as opposed to the preferential trade area supported by ECLA economists. The treaty included certain provisions concerning complementarity and differential treatment, but they were relegated to a secondary role. From the beginning, LAFTA was handicapped by the sharp differences in levels of economic development among member countries and the lack of political willingness of national decision makers to proceed toward greater economic integration. The absence of a political commitment left governments extremely vulnerable to opposition by economic groups that feared the importation of highly competitive products. Moreover, further progress toward regional integration was undermined by the lack of a mechanism for avoiding imbalances in bilateral trade, difficulties in negotiating financial arrangements for the payment of traded goods, shortages in foreign exchange, and inadequate preferential treatments for less industrialized countries,

all of which eventually contributed to LAFTA's failure. Given these difficulties, some countries opted to establish more narrowly conceived, subregional integration efforts like the Andean Pact in 1969. The liberalization cum stabilization policies adopted in the mid-1970s by Argentina, Chile, and Uruguay practically abolished preferential treatments with member countries and further weakened LAFTA as an organization capable of accomplishing regional goals.

The creation in 1980 of the Latin American Integration Association (LAIA) in Montevideo virtually sanctioned the end of LAFTA and represented a response to some of its shortcomings. For example, LAIA openly pursued bilateral or multilateral preferential treatments that had not been granted to other member countries. A third party wishing to join a bilateral agreement could only negotiate entry as long as it belonged to LAIA and respected LAIA rules and procedures. While LAIA was not a supranational organization and did not share LAFTA's ambitious goals, it is fair to say that LAIA acted as an umbrella organization in which member countries could engage in a variety of bilateral or multilateral integration or trade schemes. This is exactly what happened under the ABEIP, which was born within the framework initially established by LAIA.

#### BACKGROUND OF THE ABEIP

The late 1970s witnessed a turnaround in bilateral trade between Argentina and Brazil. Throughout the 1960s and the 1970s (except for 1971 and 1975), Argentina achieved a trade surplus with Brazil. This trend was reversed in 1980, however, partly as a consequence of the liberalization policies adopted in 1979 by Minister of the Economy José Martínez de Hoz, which opened Argentina to a substantial influx of highly competitive Brazilian imports. From 1980 until 1985, Brazil's trade balance with Argentina remained consistently positive. Successive Argentine governments in the early 1980s adopted protectionist measures against Brazilian goods partly in an attempt to reverse the situation and partly as a response to the tight import regulations enforced by Brazil at the time. These measures failed, however, merely provoking a deterioration in the commercial relations between the two countries as the Brazilian government reacted in kind by imposing even more restrictions on Argentine imports. The result was that overall trade between the two countries declined markedly. Argentina's total exports to Brazil fell from 765 million dollars in 1980 to 496 million dollars in 1985, while Brazil's exports to Argentina fell from 1.1 billion dollars to 611 million during the same period (see table 1). In addition, the composition of trade between 1970 and 1985 underwent a substantial change. Brazil began to diversify its exports to Argentina. Agricultural products, as a share of total exports,

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TABLE 1 *Argentine Bilateral Trade with Brazil, 1975–1988 (in millions of U.S. dollars)*

	<i>Argentine Exports to Brazil</i>	<i>Brazilian Exports to Argentina</i>	<i>Total</i>	<i>Balance</i>
1975	213	383	597	- 170
1976	422	331	753	+ 91
1977	465	373	838	+ 92
1978	577	347	924	+230
1979	686	654	1,340	+ 31
1980	765	1,092	1,857	- 327
1981	595	880	1,475	- 285
1982	567	666	1,233	- 99
1983	338	655	993	- 316
1984	478	853	1,331	- 375
1985	496	612	1,108	- 115
1986	698	690	1,388	+ 8
1987	539	819	1,359	- 280
1988	573	971	1,544	- 398

Source: Informe de Comercio Exterior, Secretaría de Industria y Comercio Exterior, República Argentina.

Note: All figures have been rounded to the nearest million. Discrepancies in totals are the result of rounding.

declined from 34.3 percent in 1975 to 16.3 percent in 1984. But Argentine agricultural exports to Brazil during this period remained steady, contributing to more than half of the total bilateral trade (Hirst 1987). Brazilian exports of manufactures to Argentina increased in share from 44 percent in 1975 to 67 percent in 1984, while Argentine manufactured exports declined from 49 percent to 26 percent over the same period (the slump was compensated by an almost equal increase in semi-manufactured goods of primary origin).<sup>2</sup> While Brazil increased by a third the share of its manufactures at the expense of agricultural products, Argentina's manufactures were halved. Thus between 1975 and 1984, Argentina dropped from being the sixth-ranked exporter to Brazil to the ninth. In the same period, Brazil rose from being the fourth-ranked exporter to Argentina to the second. In terms of bilateral trade (as a percentage of total trade), it can be seen from table 2 that Brazil is a more important commercial partner to Argentina than vice versa. In fact, in the period from 1981 to 1985, Argentina's exports to and imports from Brazil averaged 5.9 percent and 13.8 percent of its trade. The comparable figures for Brazil were 3 percent and 2.8 percent respectively.

Although Argentine and Brazilian military administrations tried to improve their commercial ties in the late 1970s and early 1980s, they had little success (Hirst 1989, 36–39). The key to the turnaround in bilateral relations proved to be the divergent political agendas of the

TABLE 2 *Bilateral Trade between Argentina and Brazil as a Percentage of Total Trade, 1981-1987*

	Argentina		Brazil	
	Exports (%)	Imports (%)	Exports (%)	Imports (%)
1981	6.5	9.3	0.8	2.5
1982	7.4	12.5	3.3	2.7
1983	4.3	14.5	3.0	3.0
1984	5.9	18.6	3.2	3.1
1985	5.8	14.5	2.1	3.4
1986	10.2	14.6	3.1	4.9
1987	8.7	14.4	3.1	3.0

Source: Secretaría de Industria y Comercio Exterior de la República Argentina.

new civilian administrations that took office in 1983 in Argentina and 1985 in Brazil.

The initiative for starting negotiations, which led eventually to the signing of the first protocols, came from President Alfonsín, who made economic integration a top priority of his government. Several major political motives can be identified in the Argentine initiative. First, such a move would end centuries of rivalry and misunderstanding and lead to a new pattern of inter-American relations that could benefit the rest of Latin America. Second, if successful, the integration process could be extended to other LAIA countries, thus enhancing the ABEIP's political clout.<sup>3</sup>

In economic terms, the strong trade imbalance (which affected Argentina negatively) combined with the fall in trade volume between the two countries. The time was thus ripe for bold action to rebalance the situation. This initiative was also envisaged as part of the Alfonsín administration's new development strategy. Planners reasoned that both the import-substituting industrialization model adopted from 1930 to 1976 and the neoconservative experiment imposed by the military dictatorship from 1976 until 1982 had proved detrimental to long-term growth. This goal could be achieved instead by reorienting manufactures (traditionally produced to supply domestic demand) toward the export market through bilateral agreements that seemed best-suited to this end, given the failure of previous multilateral integration attempts (Hirst 1988, 8). The logical approach when employing this export strategy was to initiate an integration process with Brasília so that Argentine manufactures could access a market four times the size of their own and thus boost their exports.

As for Brazilian motives, a combination of diplomatic and economic reasons favored creation of the ABEIP. The increasing importance of the Latin American market for Brazilian exports in the 1980s convinced

Itamaraty, the Brazilian foreign ministry, to pursue a more active commercial policy in the region via bilateral accords. This factor, combined with the Reagan administration's decision to give priority to U.S.–Mexican rather than U.S.–Brazilian relations in Latin America, led to a significant reorientation of Brazil's foreign policy. In March 1985, President Sarney stated that one goal of his administration was to pursue closer political and economic ties with its Latin American neighbors, particularly Argentina. Such an approach would allow Brazil to meet its commercial needs while exercising a more prominent and independent role in the region. Finally, an integration accord with Argentina could serve the macro-economic goal of the Comisión de Política Aduanera (CPA) of gradually diminishing the high level of protectionism in the Brazilian economy. The opening of some manufacturing sectors to foreign competition thus represented a first attempt to force domestic prices to approximate international prices.

Alfonsín's initiative could not have come at a better moment. Argentina and Brazil were no longer divided by any significant dispute, and Argentina had even acknowledged Brazil's prominent political and economic role in Latin America (Selcher 1985). Both administrations favored demilitarizing the South Atlantic to keep it free of East-West confrontations.<sup>4</sup> They also perceived the integration process as a means of achieving three complementary goals: becoming less dependent on fluctuations in the international market, boosting economic growth, and bringing stability to bilateral trade. For all these reasons, both countries were eager to improve their political and trade relations. Consultations at the diplomatic level were conducted throughout 1985 and ended on 30 November of the same year with the signing of the Acta de Iguazú, which proclaimed "the strong political will to accelerate the process of bilateral integration in harmony with the efforts of regional development and cooperation."<sup>5</sup>

Thus it appears that the main drive behind the integration process was not so much pressure from industrial and agricultural interest groups as the converging political interests of the Sarney and Alfonsín administrations. The foreign ministries of both countries were charged with defining the agreements and coordinating the role of other governmental agencies to be involved in executing them. In Argentina the Ministerio de Relaciones Exteriores was joined by the new Secretaría de Industria y Comercio Exterior, while the Ministerio de Economía assumed a passive role (Hirst 1988, 10). In Brazil all departments related to the economic sphere were more or less involved along with the foreign ministry. Among the most active were the foreign ministry, the Banco Central do Brasil, and the Comisión de Política Aduanera (Hirst 1988, 6–7).

While this initiative generated great enthusiasm in Argentina, particularly among entrepreneurs, some skepticism was expressed in

Brazil. Despite the rhetoric of government officials, Brazilian business circles were more concerned with the pragmatic aspects of a possible integration with Argentina. Specifically, these groups focused on reducing Argentine tariff barriers, holding on to their share of the Argentine market, and eventually going back to the export levels achieved in 1980. The differing attitudes of the Argentine and Brazilian entrepreneurs reflected in part the size of the respective markets and their potential for expansion (Camilión 1987, 8). Some Brazilian exporters considered the Argentine market too small and too unstable and believed that North America and Europe offered better prospects for economic expansion. In contrast, firms whose production was primarily designed for domestic needs feared that lowering protective barriers would shrink their market share. More generally, many Brazilian commentators pointed out that the discrepancy between the two countries in financial and industrial infrastructures, capital accumulation, investments, competitiveness, and economic capacity posed costs of adjustment that would be too high for Argentina to bear.

#### THE ARGENTINE-BRAZILIAN COOPERATION AND INTEGRATION PACT

Intense negotiations between the diplomatic and economic delegations of the two countries continued through the first half of 1986. On 30 July 1986 in Buenos Aires, Sarney and Alfonsín signed twelve protocols that constituted the core of the integration process. Some protocols were framed according to LAIA guidelines, which allowed the two countries to evade the preferential treatment clause affecting third parties (one of the main tenets of LAFTA) while leaving open the possibility of other LAIA members joining the bilateral agreements at a later time. According to the *Acta de Integración Argentina-Brasil*, the integration program included six major points:

First, the program would adopt a gradualist approach to be developed in yearly stages according to the decisions reached by a bilateral commission that would meet twice a year. The commission would monitor implementation of the program and negotiate new accords. At each stage, a limited number of new projects would be developed regarding capital goods and the service sector.

Second, the program would not necessarily lead to specialization of the economies involved. Rather, it would aim at stimulating intrasectoral complementarity through a quantitatively and qualitatively balanced exchange among sectors through trade expansion.

Third, it would foster technological modernization to promote greater efficiency in allocating resources between the two economies.



This goal would be reached through preferential treatment clauses with third parties.

Fourth, the program would be selective, giving priority to those products (such as capital and agricultural goods) in which a high degree of intrasectoral integration already existed. This goal would require negotiating product by product to avoid bottlenecks in the flows of services, factors, and goods.

Fifth, the program would lead to the progressive harmonizing of the economic policies of both countries. And sixth, it would depend for its execution on the active involvement of the private sector through consultation with government officials and economic incentives.

The most important provision, Protocol 1, dealt with capital goods.<sup>6</sup> It was designated as the core of the program because of the advantages that this sector offered in balancing trade and potential for expansion. This protocol was intended to create a customs union for a number of goods based on a list that would be negotiated annually. According to this protocol, the two parties would agree to three points: trading goods by lifting tariff and nontariff barriers, maintaining common external tariffs for third parties, and granting capital goods not included in the list the same treatment as that given to a third party for purchases in the public sector.

According to Protocol 1, each country was to propose a "universe" of eligible products from which they would select a smaller number to be included in a common list for negotiation. The existing differences between Argentina and Brazil in production costs and exchange rates, as well as the concern of Argentine entrepreneurs that such differences could deepen the existing trade imbalance, led the two governments to set up corrective measures. The protocol stipulated that when either country experienced a deficit exceeding 10 percent of total transactions, a balancing mechanism would activate via trade loan financing of up to 200 million dollars. With a deficit exceeding 20 percent, the assistance of a binational investment fund (created by Protocol 7) would finance investments of the country suffering the deficiency to increase its capital goods production and exports to the other partner. In the event that the deficit exceeded 40 percent of total trade, the two parties would agree to adopt additional measures compatible with the exchange-rate situation in both countries. This last corrective mechanism, however, was framed in rather vague terms. The targets for bilateral trade in this sector were set at 300 million dollars in 1987, 400 million in 1988, 550 million in 1989, and 750 million by 1990, for a total target of two billion dollars in four years.<sup>7</sup>

The second significant protocol, Protocol 2, concerned the supply of wheat. It established a joint commission to coordinate the policies of the two countries on producing, distributing, and transporting wheat. The goal of this protocol was to set up a quota of Argentine exports of wheat to

Brazil as a means of compensating for the previous trade imbalance. Argentina planned to sell Brazil 1.4 billion tons in 1987 and 2 billion by 1990.

When compared with previous integration attempts, the ABEIP seemed to set a more realistic and pragmatic agenda. Its most distinctive aspect was that rather than establishing a grand integration scheme, it emphasized gradualism, starting with bilateral trade based on a limited number of accords to be expanded slowly according to economic developments in both countries. Second, the ABEIP chose to promote trade liberalization for those sectors considered to best meet the needs of each other's market (that is, capital goods). Third, it contemplated preferential treatment clauses to stimulate trade and investments. Fourth, the ABEIP tried to promote a balanced bilateral trade through a compensation mechanism. Fifth, it created a basis for gradually expanding the agreements to third parties, a feature that could eventually elevate the ABEIP to higher stages of economic integration. Finally, it specified a timetable for periodic contacts between government officials to assess the progress achieved, make the necessary adjustments, and foster new initiatives.

#### *Evolution of the ABEIP since the First Accords*

As noted, one important aspect of the ABEIP was the possible inclusion of third parties belonging to LAIA. The first country to be considered as a potential candidate to join the Argentine-Brazilian integration effort was Uruguay, a logical addition given its geographical proximity and traditional commercial ties with both neighbors. In December 1986, Alfonsín and Sarney met a second time and agreed to strengthen the ABEIP before incorporating Uruguay into the integration process. Uruguay was nevertheless encouraged to sign separately the same bilateral agreements with Argentina and Brazil in order to smooth the transition toward a future trilateral accord. On that occasion, five new protocols were added concerning steel production (Protocol 13), surface transport (14), maritime transport (15), communications (16), and nuclear cooperation (17).

In May 1987, Sarney and Alfonsín met in Montevideo with Uruguayan President Julio María Sanguinetti for a round of talks concerning the Argentine-Brazilian economic integration scheme and rescheduling of the foreign debt.<sup>8</sup> Although no agreements were reached, Sanguinetti secured his counterparts' pledge to negotiate Uruguay's participation in the integration process in the near future.<sup>9</sup>

In July 1987, Sarney and Alfonsín met again in the Argentine city of Viedma to sign two new protocols on cultural affairs (18) and public administration (19). This meeting, however, occurred at a moment when the euphoria created by the 1986 Argentine trade surplus with Brazil was

beginning to fade. Argentine industrialists were in fact complaining that the import controls adopted by Brasília at the end of 1986 and the instability of the Brazilian economy were jeopardizing the integration effort.

The two presidents announced the creation by the end of October of a new currency that was symbolically named the *gaucho* (Protocol 20). The gaucho was expected to insulate Argentine-Brazilian trade from fluctuations in the exchange rate and would encourage trade with Uruguay, which was to adopt the gaucho as well.<sup>10</sup> Further, this trading currency was to compensate for the frequent shortage of foreign exchange and could be a useful means of payment with a third trading partner (for example, a country exporting to Argentina would be paid in gauchos and could use that currency for its purchases in Brazil). Each central bank was to issue gauchos worth 200 million dollars and thus contribute to the 400-million-dollar bilateral credit facility created by the 1986 accords. The creation of the gaucho, Sarney's visit to the Argentine nuclear plant of Pilcaniyeu,<sup>11</sup> and the signing of several new protocols in Viedma were all symbolic acts intended to convey the seriousness of the two countries' plans to achieve economic integration. The Viedma meeting led to the signing of ten more agreements that took several steps: extending the 1986 trade agreements until 1999; enlarging preferential treatment to a new number of capital goods; developing biotechnology cooperation; creating an Argentine-Brazilian school; and regulating maritime transportation.

In November 1987, the two countries also signed an agreement on petrochemicals that was to take effect in 1989. It included provisions for bilateral tariff concessions and a 20 percent ad valorem tax on imports of the same product coming from a third country. The agreement also established a mechanism allowing for a surplus of bilateral trade to be converted into credit for investments in the petrochemical sector of the country experiencing the negative trade balance.

In February 1988, Alfonsín and Sarney met with President Sanguinetti in Montevideo and formally invited Uruguay to join the protocols of integration. The following April in Brasília, the three presidents signed the Act of Alvorada, which sanctioned Uruguay's adherence to the ABEIP. Officials of all three countries hailed the agreement as the initial step toward creating a Latin American common market. Sarney and Alfonsín went on to sign a pact pledging peaceful use of nuclear energy and regular exchanges of information on nuclear technology, an agreement aimed at dissipating old fears that Argentina or Brazil might exploit nuclear proliferation to achieve regional supremacy.<sup>12</sup> Thereafter Sarney and Alfonsín signed sixteen more agreements. The most important of these, addressing the motor vehicle industry under Protocol 21, allowed each country to export duty-free to the other five thousand cars in 1989 and ten thousand in 1990 (spare parts were excluded). This protocol was

viewed as a great leap forward because it concerned an industrial sector of great importance to both countries that had traditionally been sheltered from foreign competition.<sup>13</sup> Protocol 22 covered the food industry that involved at least some degree of processing and specified a list of tariff concessions.

After March 1988, however, negotiations for additional accords slowed down considerably. The widening trade deficit incurred by Argentina absorbed most of the bilateral talks during the following summer. Meanwhile, the ABEIP became a secondary issue with Presidents Alfonsín and Sarney, whose priorities were now combating rampant inflation (which had increased more than 900 percent in Brazil and 260 percent in Argentina by the end of 1988) and defending themselves from mounting political opposition to their economic policies. Faced with domestic opposition, the two leaders found it increasingly difficult to sustain the initial pace of integration. This difficulty was particularly evident in Buenos Aires, where the protectionist lobby was arguing that Brazil was getting the best out of the deal. Lacking the strong presidential leadership that had fostered the ABEIP's inception, the two negotiating teams became increasingly isolated within their administrations. They were consequently unable to commit their governments to new agreements, which had to be postponed until the winter.

At the end of November 1988, in an attempt to revitalize the ailing ABEIP, Sarney and Alfonsín signed a new treaty calling for the achievement of a common market within a ten-year period. According to the treaty signed in Buenos Aires, the integration process was to follow a two-stage formula. First, all tariff and nontariff barriers on goods and services would gradually be eliminated, and in the second stage, financial and trade policies would be harmonized. The treaty also called for other states to join five years after its implementation. But despite the treaty's seeming significance, it was greeted in both countries with skepticism. On closer inspection, it failed to set a specific timetable for implementing the two stages and its provisions remained vague at best. A new protocol (23), signed on the same occasion, addressed the development of border regions but was of secondary importance. Further, Brazil agreed to purchase 326 Argentine aircraft and to construct a pipeline so that Argentina could supply Brazil with 3 million cubic meters of natural gas. These accords sought to reduce the trade balance, which had favored Brazil in both 1987 and 1988.<sup>14</sup>

A new sign of hope came in late August 1989, when newly elected President Carlos Menem of Argentina went to Brazil to meet with Sarney and reaffirm his administration's intention to strengthen the integration effort. Some fifteen new agreements were signed, but the greatest achievement was Brazil's conceding a 500-million-dollar line of credit for import-

ing Argentine foodstuffs and technology in an attempt to restore balance to the trade deficit.

#### RESULTS OF THE ABEIP

As noted previously, the first protocols were signed at a time when both countries were undergoing heterodox stabilization plans (the Plan Austral in Argentina and the Plan Cruzado in Brazil). The initial success of the Brazilian plan in lowering inflation and increasing the purchasing power of wages and salaries spurred demand in Brazil for Argentine goods. This favorable situation led to a 25 percent increase in bilateral trade in 1986 over the previous year. Such a favorable trend may explain the ABEIP's ambitious targets and the widespread optimism that heralded it. When the Brazilian economy began to overheat again toward the end of 1986, however, the *Cartera de Comércio Exterior* (CACEX) initiated policies aimed at curtailing imports while increasing exports to remedy the country's current accounts deficit, which was deteriorating rapidly due to the consumption drive generated by the Cruzado. This response seriously affected Argentine exports because CACEX resisted applying the preferential treatment clauses previously negotiated.

Thus by the time the ABEIP accords on capital goods and wheat went into effect in January 1987, they faced a radically changed situation. CACEX restrictions continued throughout 1987 and led to new rounds of hard negotiations. Common tariffs for third parties were postponed until 1990, which made the ABEIP not a customs union, as originally planned, but a less ambitious free-trade zone for capital goods.<sup>15</sup> Moreover, trade in spare parts was reduced to fixed percentages. Other difficulties arose from the varying criteria and procedures used by state enterprises to select their suppliers, which limited the access of the other country's goods.

The mounting difficulties encountered by the ABEIP since its inception made it impossible to maintain the schedule for enlarging the common list of Protocol 1 as planned (Porta 1989, 16). To the universe of 224 products agreed upon in 1986, only 126 new items were added in 1987 and 129 in early 1989, well below early projections (Hirst 1989, 78). Part of the reason is the fact that while Brazil was able to offer a larger and more diversified list of negotiable capital goods, Argentina's list was always smaller and concentrated in a few sectors.

Given this scenario, what were the actual results? In overall trade, Argentina experienced a deficit of 279 million dollars in 1987 and 398 million in 1988, a serious deterioration when compared with the 79-million-dollar surplus of 1986 (see table 1). Conversely, Brazil's exports climbed from 690 million dollars in 1986 to 819 million in 1987 (an 18.7

percent increase over 1986) and to 971 million in 1988 (18.5 percent more than in 1987). In 1987 and 1988, bilateral trade amounted to 1.4 and 1.5 billion dollars respectively, making up 11 percent of Argentina's commerce as compared with 3.5 percent of Brazil's.

In actuality, the ABEIP was inaugurated at a moment when significant change in the composition of Argentine exports to Brazil was already under way. Agricultural exports, which in 1984 represented 81 percent of total exports, dropped to 62.1 percent by 1987, whereas industrial exports jumped from 19 percent to 37.9 percent over the same period.<sup>16</sup> On the other side, 90 percent of Brazilian exports to Argentina consisted of primary and industrial goods (capital goods represented 22 percent).

Uruguay, for its part, recorded a cumulative trade deficit with Argentina and Brazil of 118 million and 139 million dollars respectively in 1987 and 1988, with exports to both countries declining.<sup>17</sup> The fall of Uruguayan exports to its two neighbors resulted from the recession experienced in Argentina and Brazil at the beginning of 1987. But because Uruguay has signed only the protocol concerning surface transportation so far, it is hard to imagine how the ABEIP could have retarded the country's bilateral trade.

Whether the ABEIP helped generate an unbalanced bilateral trade between Argentina and Brazil, contrary to its stated goals, is a matter of dispute in both countries. Brazilian critics ascribe the reduction of federal farm subsidies to the integration process,<sup>18</sup> and agricultural producers in Southern Brazil have argued that they are paying a dear price because of the accords.

Meanwhile, Argentine critics have contended that their country's sales to Brazil dropped not merely due to deteriorating prices for primary goods or scarce Argentine supply for industrial products. They point out rightfully that Brasilia applied strong restrictions on imports at the end of 1986 and throughout 1987 as part of the stabilization policies being implemented to balance its current accounts.<sup>19</sup> For instance, in 1987 Brazil did not buy 150,000 of the 1.4 billion tons of Argentine wheat agreed upon in Protocol 2 due to increased domestic production and a drop in market demand. A similar problem arose in 1988. If one considers that the wheat sale (30 percent of Argentine exports to Brazil) was conceived as a means of balancing the trade deficit, the seriousness of the issue becomes evident. Although Brazil agreed to purchase other primary goods to make up for the difference, the protocol's fulfillment was impaired, and the incident put a strain on bilateral negotiations.

To these charges, the Argentine authorities have replied that the results so far have been positive and that bilateral trade in the products covered by Protocol 1 was virtually balanced. The deficit, they argue, is to be explained by the fact that while 60 to 80 percent of Argentina's exports are negotiated, only 56 percent of Brazil's exports are covered by the

TABLE 3 *Bilateral Trade in Capital Goods between Argentina and Brazil, 1984-1988*  
(in millions of U.S. dollars)

	<i>Capital Goods</i>			<i>Common List of Protocol 1</i>		
	<i>Exports</i>	<i>Imports</i>	<i>Balance</i>	<i>Exports</i>	<i>Imports</i>	<i>Balance</i>
1984	8.9	65.6	-56.7			
1985	16.2	64.9	-48.7			
1986	31.3	58.5	-27.2	3.0	9.0	- 6.0
1987	50.1	100.4	-50.3	18.3	22.2	- 3.9
1988	51.0	83.5	-32.5	35.5	33.1	+2.4

Sources: For 1984-1987, Porta (1989, 18-20, 35). The figures for 1988 are preliminary estimates by the Secretaría de Industria y Comercio Exterior.

agreements. In other words, Brazil has been more effective in promoting exports in those areas not covered by the ABEIP.<sup>20</sup>

Polemics apart, it seems clear that Protocol 1 should not be blamed for the Argentine deficit. The data in table 3 suggest that overall Argentine exports of capital goods to Brazil rose from 31 million dollars in 1986 to 51 million in 1988, a net increase of 60 percent. Brazilian exports followed a similar trend as they increased by 73 percent, jumping from 58 million in 1986 to 83 million in 1988. Goods exported under Protocol 1 showed an even sharper increase. Within the same period, Argentina's exports rose from 3 million to 35 million dollars, while Brazil's climbed from 9 million to 33 million.

Looking again at table 3, it can be seen that Argentina's trade deficit in this sector, after a sharp drop in 1986 (to a negative 27 million dollars), worsened slightly in 1988 (to a negative 32 million), well below levels reached in 1984. But the contribution of Protocol 1 to this deficit seems negligible. The deficit resulting from this protocol dropped from 6 million dollars in 1986 to 3.9 million in 1987 and eventually turned into a surplus of 2.4 million.

If anything, Protocol 1 spurred exports in both countries, accounting for 27 percent of the capital goods trade in 1987 and 51 percent of its increase. The impact on Argentina was greater than on Brazil. Porta has estimated that in 1987, goods traded under this protocol were responsible for 80 percent of the Argentine total increase and 30 percent of Brazil's (1989, 18). In composition, Argentine exports were much more concentrated in a few products, with machine tools making up 55 percent of total exports (table 4). Brazilian exports were much more diversified and their share more balanced (see table 5). At a more general level, Argentine-Brazilian trade climbed from 1.4 million dollars during 1986 to 1.5 million in 1988 (up 11.2 percent). The increase occurred largely in manufactures (see table 6).

TABLE 4 *Argentine Exports to Brazil under Protocol 1 in 1987*

<i>Product Group</i>	<i>Exports FOB (in 1,000s of U.S. dollars)</i>	<i>Protocol 1 Exports (%)</i>	<i>Argentine Exports as % of Brazilian Imports</i>
Machine tools	10,200.7	55.8	16.9
Packaging machinery	1,427.8	0.1	19.7
Plastic and glass machinery	1,287.0	7.0	7.4
Pumps and turbopumps	1,288.5	6.7	5.1
Farm equipment	850.7	4.7	55.0
Electrical equipment	677.6	3.7	9.6
Food processors	575.0	3.1	40.9
Drying machinery	547.8	3.0	24.5
Valves	305.3	1.7	1.5
Drills	256.6	1.4	27.4
Mechanic conveyors	254.9	1.4	71.0
Paper machinery	200.0	1.1	12.0
Selected subtotal	17,856.9	97.7	
Total	18,272.3	100.0	8.9

Source: Porta (1989, 43).

In all likelihood, the most important factor underlying the Argentine trade deficit in 1987 and 1988 is the difference in economic policies adopted by the two governments. As noted, in late 1986 and early 1987, Brazil began to restrict imports and boost exports. Argentina, in contrast, tried to stabilize its economy by opening its market during a phase of recession. According to the former Argentine Secretary of Industry and Foreign Trade, Roberto Lavagna (a promoter and central negotiator of the original accords), this divergence in economic policies gave Brazil a great opportunity to increase its exports to Argentina.<sup>21</sup>

Given the lack of precise data on negotiated trade and the short period covered, it is difficult to make a firm assessment of the impact of the ABEIP. Two tentative conclusions can be drawn at this point, however. First, the data on capital goods trade shown in table 3 seem to support the Argentine government's claim that Protocol 1 actually promoted new Argentine exports to Brazil and a more balanced trade. Second, the ABEIP contributed to almost twice the participation of capital goods in bilateral trade, which climbed from 6.5 percent in 1986 to 11.1 percent in 1987. Argentine exports in the same period rose from 4.5 percent to 9.3 percent and its exports from 8.5 percent to 12.3 percent (see table 7). Nevertheless, the target of 300 million dollars' worth of bilateral trade was not met, as 1987 recorded a total of only 40 million. This outcome implies that although Protocol 1 made some strides forward, its impact remains



TABLE 5 *Brazilian Exports to Argentina under Protocol 1 in 1987*

<i>Product Group</i>	<i>Exports FOB (in 1,000s of U.S. dollars)</i>	<i>Percentage of Exports under Protocol 1</i>
Electric ovens	2,974.5	13.4
Machinery for construction industry	2,677.8	12.1
Plastic injectors	2,629.6	11.9
Mechanic elevators and conveyors	2,102.8	9.5
Industrial filters	1,048.4	0.7
Harvesters	1,046.8	4.7
Irrigation equipment	868.7	3.9
Cooking and heating equipment	786.5	3.5
Machine tools	739.1	3.3
Pumps for liquids	734.9	3.3
Drills	672.1 <sup>a</sup>	3.0
Industrial refrigerators	642.3	2.9
Manual pneumatic tools	609.7	2.8
Industrial sewing machinery	525.4 <sup>a</sup>	2.4
Industrial ovens	486.5	2.2
Valves	474.6	2.1
Machinery for electric cable industry	469.0	2.1
Insulators for electric switches	454.9 <sup>a</sup>	2.0
Rolling mill for food industry	327.3	1.5
Selected subtotal	20,270.9	91.3
Total	22,194.7	100.0

Source: Porta (1989, 44).

<sup>a</sup> Products included in the second common list.

limited when compared with its share of the total trade in capital goods for each country, particularly Brazil (see table 8).

Argentine and Brazilian observers argue that although Protocol 1 increased Argentine-Brazilian bilateral trade only modestly, when one takes into account all the problems it faced, the results look promising. Porta points out that its immediate effects were expansion of commerce, more balanced trade, creation of new export lines, and new investments in sectors that benefited from the accords (1989, 28–32). He acknowledges nevertheless that the lack of a coherent industrial policy in Argentina and the discrepancy between domestic macroeconomic policies and ABEIP tenets have reduced the ABEIP to a vehicle of commercial promotion rather than one of economic integration. On the contrary, Mónica Hirst stresses its achievements in terms of bilateral relations and technological cooperation (1989, 107).

The protocols other than Protocols 1 and 2 either have yet to become operative or are just beginning to be implemented. The protocol on steel (13) has remained a declaration of intent to coordinate domestic policies in

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The protocols other than Protocols 1 and 2 either have yet to become operative or are just beginning to be implemented. The protocol on steel (13) has remained a declaration of intent to coordinate domestic policies in

undermined bilateral trade. Because of the existence of strong opposition forces to the ABEIP, Alfonsín and Sarney decided to make the agreements they signed safe from political vicissitudes by embodying them in formal treaties. Although the treaties could still be revoked by the national legislatures, they would be much harder to deactivate than mere executive agreements.

#### PROBLEMS UNDERLYING THE ABEIP

It has been argued here that the impasse reached by the ABEIP at the end of 1988 resulted from a combination of structural, financial, administrative, and political problems. Let us now examine the reasons for these problems.

##### *Structural Problems*

A crucial problem affecting bilateral trade results from the discrepancy between Argentine wages and salaries when compared with those in Brazil. Labor costs have generally diverged considerably in Brazil and Argentina in that nonskilled labor is cheaper in Brazil while skilled labor is cheaper in Argentina. Consequently, depending on the technological content of a product, one of the two countries often enjoys an advantage over its partner, even when all other factors are equal. Moreover, labor legislation in Argentina has proved to be much less flexible than that in Brazil and has often been blamed for causing high industrial prices in Argentina. These two factors combined have made it possible for Brazilian goods to be more competitive than their Argentine counterparts in bilateral as well as international trade.

Compounding the situation is the fact that the Brazilian market is four times larger than that of Argentina and thus provides an outlet for Argentine primary and manufactured exports. But a large discrepancy also exists in the average index of nationally produced capital goods, which is about 80 percent in Brazil compared with 35 percent in Argentina. Moreover, the tariff structures of the two countries differ considerably. The nominal tariff rate was 75 percent in Brazil as compared with 23 percent in Argentina during 1984 (Baumann 1988, 6). Disparities also exist in production costs and productivity in capital goods (Porta 1989, 6-10; Hirst 1989, 78), raw materials, electrical power and fuels, transportation, and capital, with Brazil generally occupying a stronger position (see table 9).

Furthermore, since the early 1980s, the debt burden has forced Latin American countries to implement stabilization policies aimed at reducing imports. As a result, regional trade has declined by 30 percent and Latin American imports by as much as 37 percent between 1980 and

1985.<sup>24</sup> Yet the need to earn hard currencies to service the debt has led Latin American countries to boost their exports outside Latin America. As Renato Baumann has noted, this situation could impinge on integration efforts:

When a country has a trade deficit with non-Latin American countries, intensification of intra-regional trade may be justified on the grounds that trade deviation may have positive effects over the trade balance. But if, on the contrary, a given country has a trade surplus with nonmembers—as has been the case in recent years for both Brazil and Argentina—trade deviation towards larger intra-zone trade flows may involve a reduction of such surpluses and hence (if regional trade does not involve hard currencies) smaller foreign reserves to face the debt service. (Baumann 1988, 9)

The problem of trade deviation was raised at a recent conference by a representative of the U.S. Department of Commerce, who expressed concern that the ABEIP could become a new hub for economic protectionism in South America.<sup>25</sup> As yet, however, the International Monetary Fund, the World Bank, and private creditors have not raised such questions.

### *Financial Problems*

Both countries have suffered from severe limitations in internal financing due to low capital formation, lack of foreign loans, the debt-service problem, and exchange-rate policies. Usually, Latin American governments have tried to solve the problem posed by low capital formation by resorting to foreign loans. But the large foreign debt that Argentina and Brazil have incurred, coupled with their inability to service interest payments, has severely limited foreign capital financing. As noted, the two countries attempted to remedy such a constraint by creating the gaucho and bilateral credit financing. This solution was only a temporary one, however. Argentina carried into 1988 a deficit of 398 million dollars, which exhausted the 400 million dollars of trade financing sooner than expected. Moreover, given the need for U.S. dollars, granting credit or accepting payments in national currencies (which would be determined in hard currency) put a strain on ability to service the debt.<sup>26</sup>

A related problem is that of harmonizing exchange rates. Because of the high inflation rates experienced by Argentina and Brazil, sudden devaluations have been declared that have hurt bilateral trade. Minimal coordination took place between the two countries in this regard, reflecting the different macroeconomic policies chosen to promote economic stabilization. The Brazilians began to restrict imports and to foster exports while sustaining a relatively high level of economic activity. The Argentine economic team, in contrast, tried from the fall of 1987 to the spring of 1989 to fight inflation by opening up the domestic market during a deep

TABLE 9 Indicators of Production Costs in Argentina and Brazil (Domestic Costs Calculated in U.S. Dollars in Values Typical of the Second Half of 1986)

	Brazil	Argentine Estimates				
		1 <sup>a</sup>	2 <sup>b</sup>	3 <sup>c</sup>	4 <sup>d</sup>	5 <sup>e</sup>
Basic raw materials						
Steel	100	124				
Steel sheets	100	167				
Bobbin sheets	100	167				
Cold laminated steel sheets (1.5 mm)	100		120		128	
Hot laminated steel sheets (3–8 mm)	100	101	147			
Aluminum alloy	100	189				
Aluminum	100		139	181	143	
Zinc	100		140		133	
Electrolytic tin	100				251	
Natural rubber	115		100			
Synthetic rubber	114		100			
Power						
Kw electric power	100			138	217	
Diesel oil	132		100	105		
Gasoline	100			137		
Kerosene	125		100	102		
Transportation						
Port services	100	621				
Labor cost						
Unskilled manpower minimum salary	100	154		155		
Hourly minimum wage	100			111		
Capital						
Regulated real interest rate (restricted)	121	100				100
Accessible real interest rate						
Supporting production credit	100					630
Short-term credit	100					1196

Source: Hirst (1989, table 31).

<sup>a</sup> Various sources.

<sup>b</sup> *Novedades Económicas*, no. 68 (Aug. 1986); and IEERAL, no. 71 (Nov. 1986).

<sup>c</sup> SFC-INTAL, *Indicadores de sector externo: hoja de situación*, no. 25.

<sup>d</sup> López Aufranc, "Las distorsiones de la economía Argentina," *Ambito Financiero*, 10 May 1986.

<sup>e</sup> ADIBA, Asociación Industriales de la Provincia de Buenos Aires, internal survey; and *Ambito Financiero*, 1 Oct. 1986.

recession. Accordingly, each country has pursued its own exchange, fiscal, and monetary policies while paying little attention to the other country's actions. This unilateral approach diverged from the complementary policies in place when the first protocols were signed. The Austral and Cruzado plans actually exhibited many similarities in theoretical and normative aspects due to frequent contacts between the economic teams of the two countries at the time. When the two plans collapsed, however, differing stabilization policies were inaugurated. Thus although the negotiating teams understood that successful integration required the two governments to maintain a stable exchange rate between their currencies, these teams had no say in the redesigning of macroeconomic policies.

A third problem has been the vagueness of the protocols. For instance, Protocol 1 failed to explain what was to be done about price distortions created by government subsidies. Nor did it specify what course of action was intended for nontariff barriers or any timetable for eliminating them. Other distortions created by export incentives were not addressed by the protocol nor was the role of foreign subsidiaries for capital goods clarified. All these factors combined to further complicate implementation of the accords and undermined their effectiveness.

#### *Administrative Problems*

Both bureaucracies have tended to be slow in processing import-export paperwork, particularly in Argentina. Private entrepreneurs in both countries have lamented the inefficiency and lack of cooperation between the bureaucracies in charge of bilateral trade.

A second factor has resulted from the strong protectionist practices adopted by both countries. As noted, the Brazilian agency CACEX adopted restrictions on Argentine imports, contrary to the spirit of the ABEIP. Protectionist measures developed in part from strong industrial and agricultural groups in both countries that lobbied effectively to prevent the opening of domestic markets. Middle- and small-sized industries that had been sheltered from foreign competition were particularly vocal in their opposition. This response was frequent among companies whose products were not included in the universe of Protocol 1. It was even more widespread among firms that were not participating in the integration but saw their direct competition across the border doing so (Porta 1989, 24). The attitude of most multinational corporations was similar, as the experience with the automobile accord testifies. The reason was that multinationals in these countries were set up to exploit the domestic market under oligopolistic conditions and do not wish to jeopardize their privileges. Even trade unions made it clear that if integration were to endanger jobs, then the government should act otherwise.<sup>27</sup>

The other side of the coin is that custom receipts have normally represented a large source of governmental revenues. Consequently, diminishing or abolishing interzonal tariff barriers according to the integration process deprived the governments involved of substantial resources. This loss of revenue has forced them to seek alternative sources of financing at a time when they have exhausted most of their available means and have been experiencing increasing pressure to raise revenues to finance the budget deficit. Thus the bureaucrats involved in the integration projects tried to broaden the list of goods enjoying tariff elimination or preferential treatment while the economic teams carrying out stabilization policies resisted such attempts. This kind of resistance, compounded by the problems caused by different macroeconomic policies, prompted the resignation of Secretario de Industria y Comercio Exterior Roberto Lavagna in 1987. His resignation was followed in 1988 by that of Jorge Romero, the diplomat from the Argentine foreign ministry in charge of the ABEIP.

A third problem has been the governments' failure to apply the clauses prescribing compensation mechanisms in cases of unbalanced trade. The mechanisms turned out to be rather vague, leaving too much room for varying interpretations and thus creating confusion and reciprocal misunderstanding, if not suspicion. As a consequence, once the imbalance on bilateral trade surfaced in 1987, the mechanisms failed to be implemented as planned.

### *Political Difficulties*

As discussed, the protocols were signed in a moment of economic euphoria in Brazil and relative price stability in Argentina, when Alfonsín and Sarney were enjoying widespread support. Since then, however, their prestige has steadily eroded. Following the collapse of the Austral and Cruzado plans, both economies attempted piecemeal stabilization measures to thwart inflation. The situation became particularly severe in 1988 in Brazil and in mid-1989 in Argentina, when each country experienced spiraling hyperinflation. One consequence of the profound economic recession was that Alfonsín and Sarney lost important midterm congressional elections in 1987 and 1988 respectively. Afterward, they faced stiff opposition from the congresses and from interest groups that disrupted their political agendas. As a result, presidential initiative for further accords declined. This outcome can be ascribed to the nature of the ABEIP itself, which originated out of the political will of both presidents to emphasize bilateral relations at an unprecedented level. As political instability escalated in both countries, it became increasingly difficult for Alfonsín and Sarney to overcome internal opposition to further integra-



tion, particularly because of economic recession and ABEIP's scant results achieved thus far.

Moreover, despite the widespread consensus that greeted the first protocols, presidential initiatives were not reinforced by supportive economic and social groups, which were not organized either spontaneously or by the governments. This absence was particularly notable in Brazil, where the main ABEIP supporters remained clustered in the foreign ministry and some state companies. The integration issue was thus confined to the presidents and their technical advisors, which left the economic sectors affected by the protocols in a somewhat passive position. As noted earlier, the reorientation of macroeconomic policies provoked serious interbureaucratic cleavages between the foreign ministries and those of the economy. By mid-1989 most of the Argentine top officials who had negotiated the accords had left the Alfonsín administration. A similar pattern occurred in Brazil, where the foreign ministry became increasingly isolated due to the changed situation at the Ministério de Economia. In April 1987, economy minister Dilson Funaro, who favored the ABEIP, was replaced by Luis Carlos Bresser Pereira. The latter resigned in December of the same year and was replaced by Mailson de Nóbrega, whose anti-inflationary program coincided with CACEX's restrictive policies.

Debate over the merits and feasibility of the integration effort has rarely transcended academic discussions or official speeches. Clearly, grass-roots movements, trade unions, and the public at large have been absent from the integration process. With Alfonsín's and Sarney's terms expiring in 1989 and 1990 respectively, doubts and uncertainties have arisen about whether their successors will be as enthusiastically committed to the process of integration. Thus far Menem seems to have dissipated such fears in Argentina with his recent trip to Brazil indicating his willingness to take up where Alfonsín left off. But the ABEIP's prospects remain unclear in Brazil, where presidential candidates have as yet made no clear commitment to it.

#### LESSONS OF THE ABEIP

What can be learned from the ABEIP's brief experience? First, the ABEIP confirms the general attitude toward integration demonstrated by Latin American decision makers over the years. Latin Americans have viewed economic integration not as a means of achieving the broader goal of political union, as in the case of the European Economic Community, but as a worthy end in itself. In line with this philosophy, the ABEIP (like its predecessors) has been regarded mainly as a way of boosting economic activity, absorbing excessive production, satisfying mutual market needs, and improving diplomatic relations.

Given these premises, the approach taken by Alfonsín and Sarney

has been pragmatic and narrower in scope than that undertaken in Western Europe. Unlike some previous attempts in Latin America, the ABEIP has made no commitments to political union, as evidenced by the fact that the ABEIP did not create a supranational institution with binding authority. The Andean Pact tried such an experiment in the late 1960s but achieved little success and soon became obsolete. In contrast, Argentina and Brazil under the ABEIP have retained national control over key policy areas that might have been threatened had such an institution been created. Analysts must therefore take into account the significant difference in the meaning and goals of Latin American integration, as distinguished from those of the European Economic Community, when assessing the ABEIP's overall impact.

A second aspect concerns the dynamism of the integration effort. It appears in retrospect that both Alfonsín and Sarney believed that the ABEIP alone could create the basis for self-sustained growth. On the contrary, any integration process must be supported by exchange, industrial, agricultural, and investment policies with a common or at least compatible philosophy. Lacking such conditions, the advantages of an integration scheme over a simple commercial agreement are lost, and sooner or later the integration effort will come to a standstill.

A third point deserving attention is the problem posed by the economic crisis. Initiating an integration process in times of volatile economic stability means taking a gamble. The ABEIP experience clearly demonstrates the difficulty of seeking economic integration when partners are suffering hyperinflation, as was the case in Brazil at the end of 1988 and in Argentina since April 1989. Integration is no substitute for economic stability—to the contrary, it is instead a basic prerequisite. Countries experiencing sluggish growth rates, large foreign debts, and rampant inflation are ill-equipped to withstand the opening of their markets via integration. Such a step could seriously jeopardize some of their domestic producers, who will necessarily lobby against it. Thus unless economic stability can be achieved, it is hard to foresee any future for the ABEIP, or for any integration process operating under similar economic constraints.

The ABEIP experience also underscores again the importance of making national macroeconomic policies compatible with the objectives set up by the integration process. Part of the blame for ABEIP's lack of success can be attributed to this problem, which is common to any integration effort. More specifically, the coordination of exchange policies seems to assume a crucial importance in trade flow. This necessity is explicitly recognized in Protocol 1, which calls for "a relationship of a type of exchange rates within the currencies of both countries . . . that is balanced and sufficiently stable." The point being made here, however, is

that this objective should be translated into practice. If not, the prospects for a durable and stable integration are at best bleak.

Lack of macroeconomic coordination, in turn, is closely related to the problem posed by the different development strategies chosen by Argentina and Brazil in recent decades, particularly in the area of industrial development. Argentina has fostered an inward-looking approach that has created a highly protected and inefficient industry producing mostly for the domestic market. Brazil followed a similar path until the 1960s, when the military regime began to emphasize industrial exports while keeping import barriers high. By 1981 manufactured goods had replaced primary goods as the country's main export sector. As a consequence, Brazil has promoted an aggressive export policy that contrasts with the rather passive attitude of the Argentines. Until the Alfonsín administration, the Argentine approach stressed growth through expansion of the domestic market, leaving to agricultural exports the task of generating the exchange rate necessary to subsidize industry (Baldinelli 1986). These different development strategies have created strong vested interests that will coalesce if challenged. ABEIP negotiators adroitly ignored the whole question, implying the overcoming of the strong domestic opposition of groups that have thrived under the Sarney and Alfonsín administrations. Both presidents made some attempts to address the problem but had little success. Their legislative proposals for privatizing public companies, rationalizing the state sector, and reforming the host of special privileges enjoyed by many private enterprises have been defeated in both congresses.<sup>28</sup> But to guarantee the continuing forward motion of the integration process, regardless of the administration in office, it is necessary for the countries involved to agree on compatible development strategies over the long term. This requisite applies to the ABEIP as well as to any integration effort, particularly in developing countries. A common understanding regarding a subregional strategy for economic development would allow the defining of priorities compatible with domestic goals. Without such definition, irreconcilable national interests will surface sooner or later and doom the whole scheme, as happened with LAFTA and the Andean Pact before it.

At a more political level, the kind of top-down integration approach taken by the ABEIP, which resulted from decisions made by a small number of politicians and bureaucrats, has its advantages and disadvantages. On the one hand, this approach gives a government free reign in the short-run to pursue whichever policies decision makers consider important. On the other hand, such policies encounter strong opposition from the economic interests affected, which can effectively lobby to undermine domestic political support for integration. This outcome has almost invariably ended by isolating the policymakers, and it

partially explains why Latin American integration efforts, after some initial success, have often collapsed. The bottom line is that as long as an integration effort rests solely on the initiative of presidents and a few ministries, its degree of success will be linked too directly to the fortunes and misfortunes of the administration that is attempting to implement the process. Instead, governments should actively encourage the creation of a pro-integration lobby that can serve to counterbalance protectionist and isolationist groups, as has happened in the EEC. To this end, governments should broaden the base of support for integration by promoting greater involvement of economic interests in shaping the negotiation process and by persuading the public of the advantages that economic integration can bring.

#### CONCLUSIONS

The economic integration process between Argentina and Brazil, recently joined by Uruguay, constitutes a significant landmark in Latin American history. The ABEIP's greatest achievements to date have been diplomatic. Most notably, Argentina and Brazil have succeeded in transforming their longstanding rivalry into a cooperative relationship. As argued at the outset, the ABEIP was able to get off the ground thanks to the political and economic stability that Argentina and Brazil were enjoying in early 1986. The policymakers involved probably initiated the integration process in the belief that the positive political and economic trends occurring in 1986 would continue in the immediate future. This optimism translated into setting presidential meetings every six months that were planned to signal clearly to the public that a new pattern in policy-making at the regional level was underway and should be taken seriously. At the same time, however, this rapid timetable created expectations for increasing the pace and scope of the integration process that exceeded the capacity of the presidents and their bureaucracies to sustain such goals over the longer term. Two indications that political pressure prevailed over economic considerations are the vagueness of some hastily drafted protocols as to practical provisions and the subsequent inclusion of Uruguay before the ABEIP was consolidated. The ABEIP's vulnerability became evident as the evaporation of political and economic stability eventually impaired progress toward further accords.

On taking the entire scenario into account, it is no surprise that the ABEIP's economic results have been less impressive than expected, especially given the structural, financial, and administrative problems that have plagued the ABEIP's brief history. Moreover, it is premature to speak of the ABEIP as a common market, official declarations notwithstanding.<sup>29</sup> It can be more accurately described as an integration process that begins by liberalizing capital goods trade. Given the problems discussed,

the ABEIP's future prospects are not rosy. At this point, it is hard to imagine the ABEIP going further than it already has. The deep economic recession affecting the countries involved, coupled with their political instability, has already slowed the pace of economic integration. The year 1990 will probably be one of transition and reassessment of priorities for policymakers. Ill-specified protocols and the compensation mechanisms for bilateral trade deficits need to be implemented or redesigned. Clear understanding must be reached on what tariff and nontariff barriers ought to be, how preferential treatment schemes should work in practice, and how to deal with export subsidies and the foreign corporations affected. As respected Brazilian economist Edmar Bacha has pointed out: "If they [the governments] were serious about improving trade, they would lower tariffs and try to stabilize the economies."<sup>30</sup>

Future prospects depend, above all, on the political leaders who will rule Argentina and Brazil in the 1990s. The ABEIP began as a political creature born of initiatives by Alfonsín and Sarney. If the succeeding presidents of both countries are willing to pursue the integration effort, they must first promote macroeconomic policies that are compatible with the other country's and with the protocols already signed. This approach will require greater effort at fostering political support for the integration effort. Alfonsín's successor, President Menem, has made a positive move to keep the ABEIP alive, a remarkable gesture considering the gravity of the Argentine situation at the moment. Much now depends on what Sarney's successor is willing and able to do in this regard. It is likely that as long as the two countries face serious economic crises, the integration issue will remain low on the new administrations' political agendas. In sum, the ABEIP needs renewed commitment from both incoming administrations in the months to come if it is to survive as an effective means of achieving subregional integration. Without such commitment, the ABEIP will go down as yet another unsuccessful attempt in the troubled history of Latin American integration.

## NOTES

1. For further reading on the subject, see Hirst's edited 1988 work and Baumann and Lerda (1987).
2. See Hirst (1989), tables 21 and 22.
3. Alfonsín also hoped that the ABEIP could pave the way for an agreement with Brazil on forming a common front for renegotiating the external debt. Such an approach would have strengthened the two countries' bargaining position vis-à-vis the U.S. government, the International Monetary Fund, and foreign banks. Matters remained at the rhetorical level, however, and each government eventually decided to manage the problem in its own way. In 1987 Brazil called for a debt moratorium while Argentina kept bargaining with both the International Monetary Fund and the World Bank.
4. Unstable political conditions in the South Atlantic would pose a serious threat to Brazil's exports to the Andean countries because most of its commercial traffic goes through the Straits of Magellan.

5. The text of the act was printed in *Integración Latinoamericana*, no. 110 (March 1986): 70-90.
6. The subjects of the individual protocols signed covered a wide range: (1) capital goods, (2) wheat, (3) supply of foodstuffs, (4) expansion of commerce, (5) binational enterprises, (6) finance, (7) binational investment fund, (8) energy, (9) biotechnology, (10) economic research, (11) nuclear energy, and (12) aeronautics cooperation.
7. It was also expected that half the products in the "universe" would be negotiated by 1990. An important clause of Protocol 1 was that 80 percent of the composition of goods must be national in origin. See Porta (1989), 11-13.
8. Public opinion in Uruguay about joining the ABEIP was divided. The Sanguinetti administration strongly favored the idea, arguing that Uruguay could export its surplus dairy products, beef, wool, textiles, basic metals, leather, and fish and thus balance its growing import bill. Critics of the proposal argued two disadvantages: the high degree of dependence on Argentine and Brazilian markets, which tend to be unstable, could be detrimental in the long run; and the relatively lower competitiveness of Uruguayan industry could produce a serious trade imbalance. See Hirst (1989), 87-97.
9. It should be noted that Uruguay had achieved bilateral conventions with Argentina in 1974 (CAUCE) and with Brazil in 1976 (PEC), which have been well implemented and rather successful, particularly for Uruguay.
10. The unit value of the gaucho was to equal the International Monetary Fund's special drawing rights of \$1.27 U.S. dollars. Each country's central bank was to issue gauchos using credits made available through LAIA. The new agreements were extended to Uruguay through bilateral negotiations with Argentina and Brazil.
11. No other head of state had ever been allowed to see the uranium-enrichment plant.
12. Moreover, Sarney reciprocated Alfonsín's invitation to the Pilcaniyeu nuclear plant by taking him to the Aramar nuclear experimental center.
13. The small number of vehicles to be exported can probably be explained by the strong lobby exercised by some car industries. For instance, Argentine car manufacturers are less internationally competitive than their Brazilian counterparts.
14. The decision engendered strong reactions in both countries. The Argentine chemical sector (traditionally one of the most protected) was particularly vocal in its opposition, arguing that the gas sale would give Brazil the necessary input for producing petrochemical products, which would compete directly with Argentine products. See *Buenos Aires Herald*, 2 Dec. 1988, p. 2.
15. The literature on international trade categorizes integration efforts according to five types based on their breadth and scope: partial reduction of common trade barriers (area of preferential treatment); elimination of tariff barriers (free zone); reduction of barriers and the definition of a common set of tariffs for imports from third parties (customs union); the establishment of free movement for international factors (common market); and the creation of a common set of macro policies and common currencies (economic union).
16. According to 1987 data from the Instituto Nacional de Estadística y Censos.
17. See Hirst (1989), t. 40.
18. See *Latin American Regional Report Brazil*, July 1988, p. 6.
19. See *Clarín*, 3 July 1988 (Buenos Aires), p. 10.
20. According to government officials in Buenos Aires, part of the blame should be placed on multinational corporations that took advantage of tariff concessions (granted for negotiated products and for products included in Article 1 of the Acuerdo de Alcance Parcial de LAIA) to place major orders with Brazil. According to official sources, Brazil exported 60 million dollars worth of steel in 1987 while Argentina sold nothing to its commercial partner. In 1988 other companies linked to the chemical and pharmaceutical sectors imported goods totaling 80 million dollars. See *Clarín*, 21 July 1988, p. 11. This line of argument sounds a little suspicious, however. If companies purchase abroad by using bilateral concessions, responsibility for approving the transaction always rests with governmental officials.
21. My interview with Roberto Lavagna, Secretario de Industria y Comercio Exterior, Buenos Aires, 15 Aug. 1988.

22. "Sarney and Alfonsín Discuss Integration," *Latin American Regional Report Brazil*, 5 Jan. 1989, p. 6.
23. The Argentine and Brazilian military establishments have shown considerable interest in the project. Two meetings were organized by the general staffs in Buenos Aires (April 1987) and São Paulo (April 1988), where economic and strategic repercussions of the ABEIP were examined and elicited favorable comments.
24. See Garcia Munhoz (1987), 95.
25. Conference, "The Argentine-Brazilian Integration Program: An Early Assessment," held at the Wilson Center, Washington, D.C., 13 Dec. 1988.
26. See Sant'Ana (1987), 105.
27. Carlos Moyano Llerena, "Divisas, aduanas y soberanía," *La Nación*, 9 Aug. 1988, p. 9.
28. In August 1989, the Argentine Congress approved President Menem's state reform law enabling the federal government to privatize state companies.
29. See Lerda and Baumann (1987), 24.
30. As stated on the *British Broadcasting Corporation Latin America*, 20 July 1987.

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