

# CRS Report for Congress

## **Mercosur: Evolution and Implications for U.S. Trade Policy**

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J. F. Hornbeck  
Specialist in International Trade and Finance  
Foreign Affairs, Defense, and Trade Division



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# Mercosur: Evolution and Implications for U.S. Trade Policy

## Summary

Mercosur is the Common Market of the South established by Brazil, Argentina, Uruguay, and Paraguay in 1991 to promote economic integration and political cooperation among the four countries. Since then, Mercosur has struggled to achieve deep economic integration, but has maintained a cooperative economic and political framework, which has also become an influential voice in determining the fate of the hemisphere's regional integration initiatives. In particular, the U.S. vision for hemispheric integration, the Free Trade Area of the Americas (FTAA), has stalled largely because of opposition from within Mercosur, which in turn has focused on its own, albeit limited, expansion.

The Mercosur pact calls for an incremental path to a full integration, but after 15 years, only a limited customs union has been achieved. From the outset, Mercosur struggled to reconcile a basic inconsistency in a pact of partial economic union: how to achieve economic integration, while also ensuring that the benefits would be balanced among members and that each country would retain some control over its trade, production, and consumption structure. This delicate balance faced overcoming serious structural and policy asymmetries that became clear when Brazil and Argentina experienced financial crises and deep recessions. These economic setbacks disrupted trade flows among members, causing friction, the adoption of protectionist measures, and a retreat from the commitment to deeper economic integration.

For now, Mercosur has turned to expanding rather than deepening the agreement. Many South American countries have been added as "associate members" and Mercosur has reached out for other South-South arrangements in Africa and Asia – all limited agreements and unlikely paths to continental economic integration. Internal conflicts have highlighted Mercosur's institutional weaknesses and slowed the integration process. On July 4, 2006, Venezuela signed an accession agreement to become its first new full member, making Mercosur the undisputed economic counterweight to United States in the region, but raising questions about how Venezuela's membership may shift regional political and trade dynamics.

It appears that Mercosur has opted to emphasize its expansion both in the region and with other developing countries over agreements with its largest developed country trade partners, looking to the World Trade Organization (WTO) as the preferred alternative for achieving many of its trade policy goals. Nonetheless, U.S.-Mercosur commercial and economic ties are expanding and the United States is pursuing deeper bilateral trade relations with Uruguay that could provide new ideas for a broader integration commitment. The alternative may be for Mercosur and the United States to expand their mutually exclusive bilateral agreements, increasing the potential for overlapping trading systems, which few, if any, view as either economically or administratively optimal.

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# Mercosur: Evolution and Implications for U.S. Trade Policy

On March 26, 1991, Brazil, Argentina, Uruguay, and Paraguay signed the Treaty of Asunción, establishing the Common Market of the South (Mercado Común del Sur — Mercosur) with the intention of strengthening sub-regional development and cooperation through economic integration. Since then, Mercosur has struggled to achieve deep economic integration, but has maintained a cooperative economic and political framework, which has also become an influential voice in determining the fate of the hemisphere's regional integration initiatives. In particular, the U.S. vision for hemispheric integration, the Free Trade Area of the Americas (FTAA), has stalled largely because of opposition from within Mercosur.<sup>1</sup> Venezuela's July 2006 signing of an accession agreement only reinforces Mercosur as the undisputed economic counterweight to the United States in the region and raises further doubts over the prospects for a hemispheric-wide trade agreement. This report examines the evolution of Mercosur as it relates to U.S. trade policy in Latin America. It will be updated periodically.

## U.S.-Mercosur Trade Prospects

The Mercosur countries are experiencing an extended period of strong economic growth after a deep recession caused by financial crises in Brazil (1999) and Argentina (2001). They currently have competitive exchange rates, stable macroeconomic conditions, and strong growth in exports and foreign direct investment largely because of the global commodity price boom. Commodity prices, however, cut two ways. Although strong agricultural prices have fueled export growth, the rising price of oil has offset some of these gains for the net oil importers (Venezuela being the exception), contributing to deteriorating current account balances over the past year. Within Mercosur, Brazil dominates the trade relationship, running a sizable and growing trade surplus with the rest of the pact.<sup>2</sup>

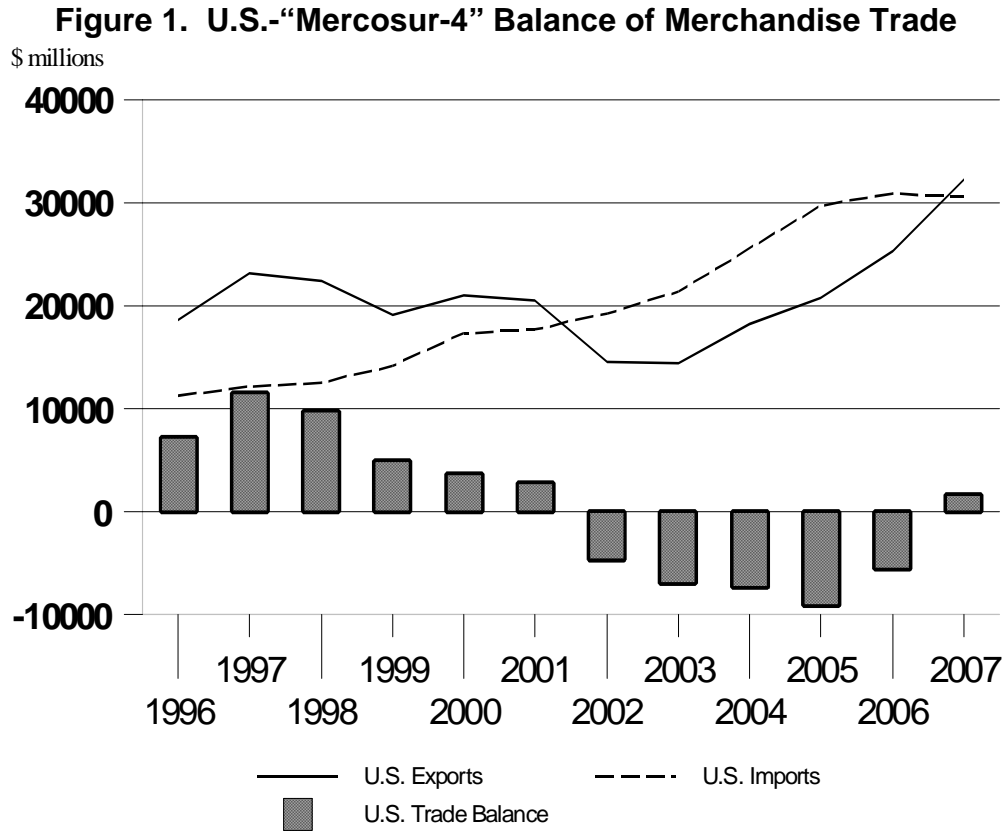
Mercosur has a well-diversified trade relationship with the world. In 2006, the European Union (EU) was Mercosur's largest trade partner, capturing 25% of total trade, followed by Asia with 22%, and the United States with 19%. By contrast, the four Mercosur countries together accounted for only 3.0% of total U.S. trade. With the recent addition of Venezuela, the "Mercosur 5" make up 3.6% of total U.S. trade,

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<sup>1</sup> For more on the FTAA, see CRS Report RS20864, *A Free Trade Area of the Americas: Status of Negotiations and Major Issues*, by J. F. Hornbeck.

<sup>2</sup> Inter-American Development Bank (IDB). Integration and Regional Programs Department. *Mercosur Report No. 12: 2006-2007*. Washington, D.C. February 2008. pp. 4-6.

the increase accounted for almost entirely by U.S. imports of Venezuelan oil. Collectively, the “Mercosur 4” would rank 9<sup>th</sup> for U.S. exports and 14<sup>th</sup> for U.S. imports, slightly ahead of Brazil by itself, the largest economy in South America, responsible for 80% of total Mercosur trade with the United States.<sup>3</sup>



Data Source: U.S. Department of Commerce.

Patterns in U.S. merchandise trade with the “Mercosur-4” appear in **Figure 1** (country data for all five appear in **Appendix 1**). Note that trends are heavily skewed by Brazil’s large economy. U.S. imports of Mercosur goods rose steadily from 1996 to 2006, paralleling growth in the U.S. economy. Expansion of U.S. exports, by contrast, was flat from 1996 to 2001 and then fell as import demand collapsed around deep recessions in Brazil and Argentina. U.S. exports rebounded in 2004 as the Mercosur economies recovered, and by 2007, the U.S. trade balance turned from deficit to surplus for the first time since 2001. The U.S. trade surplus reflects growth in demand in all four Mercosur countries. For Brazil, U.S. imports actually declined slightly in 2007, as U.S. exports rose by 28%. U.S. exports have been helped by Brazil’s strong economic growth resulting in increased demand for U.S. inputs such as aircraft engines and parts, as well as the strong appreciation of Brazil’s currency relative to the U.S. dollar.

Major U.S. exports to Mercosur include mostly capital and high technology goods such as mechanical and electrical machinery (computers, vehicles, aircraft,

<sup>3</sup> U.S. Department of Commerce data as presented in the World Trade Atlas.

medical equipment, and pharmaceuticals). The primary U.S. imports are components for machinery and vehicles, agricultural products, and oil if Venezuela is included. Specifically, the United States imports primarily machinery and mineral fuel from Brazil, mineral fuel and processed foods from Argentina, sugars and woods from Paraguay, and meat and woods from Uruguay. Despite being a relatively small U.S. trade partner, Mercosur contains two of South America's largest economies, and so prospects for growth in trade and investment drive, in part, ongoing U.S. interest in maintaining cordial and cooperative relations, as does the expectation for deeper Western Hemisphere integration, perhaps including, at some point, the FTAA.

## Formation and Institutional Development

Mercosur evolved from a series of 1980s bilateral agreements between Brazil and Argentina. It was conceived as a way to foster new levels of political and economic openness and cooperation following a prolonged period of mutual distrust, much of it taking place under military dictatorships in both countries. In addition, as the South American economies moved away from an import substitution model of development to one based increasingly on trade openness, a regional trade agreement made sense given the four countries were "natural trade partners," sharing geographical, cultural, and economic complementarities.<sup>4</sup> In fact, Uruguay and Paraguay pressed hard to expand the arrangement to a four-country common market to improve their trade prospects, or at the least, ensure that they would not be isolated by a bilateral economic pact between their two largest neighbors.<sup>5</sup>

Mercosur, therefore, evolved from economic and political circumstances that emphasized the need to preserve and enhance the Brazil-Argentine bilateral relationship, while fostering cautious ambitions for sub-regional economic integration that could also serve as a platform for the four countries' insertion into the global economy. Ultimately, as one scholar has observed, meeting expectations is critical, and Mercosur's success rests on the provision of consistent reciprocal market access and a "framework for cooperation" that promotes mutual economic growth and development.<sup>6</sup> It is the difficulty in achieving this standard, as shall be seen, that has been at the root of persistent discontent within Mercosur.

Formally, the Treaty of Asunción established Mercosur as a common market among Brazil, Argentina, Uruguay, and Paraguay for the stated purpose of

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<sup>4</sup> Vaillant, Marcel. Mercosur: Southern Integration Under Construction. *IPG*. February 2005. p. 53.

<sup>5</sup> The addition of Uruguay and Paraguay raised a fundamental debate about Mercosur's purpose. Despite the charter having well-defined integration and development goals, Brazil and Argentina have viewed Mercosur as a political project as well. Paraguay and Uruguay, by contrast, have emphasized its economic priority, with some observers insisting that Mercosur gets off track when it operates from a political agenda. See Lacalle de Herrera, Luis Alberto. Mercosur: Project and Perspectives. *Diplomacy, Strategy & Politics Review*. Brasilia: April/June 2007, pp. 186-193. (Note, Mr. Lacalle was president of Uruguay 1990-1995 and played an instrumental role in the negotiation and creation of Mercosur.)

<sup>6</sup> Vaillant, op.cit., pp. 53-54.

accelerating economic development and social justice. The goal envisioned improved living conditions for all member countries through “balanced and managed growth in trade flows.”<sup>7</sup> The treaty followed guidelines compatible with the Latin American Integration Association (Asociación Latinoamericana de Integración — ALADI), a regional trade organization that provides a common, yet flexible framework for establishing sub-regional trade pacts that encourages inclusiveness and minimal harm to non-members. These pacts may be both “regional and partial in scope,” in contrast to the U.S. free trade agreement (FTA) model that tends to be comprehensive. For example, Mercosur adopted as basic tenets “gradualism, flexibility, and balance,” and allows for the negotiated accession of other countries.<sup>8</sup>

Mercosur followed an incremental path to a common market, beginning with a transition period (1991-95) in which it operated as an increasingly comprehensive free trade agreement (FTA) based on a schedule of automatic tariff reductions. The formal jump to a common market was made on January 1, 1995, but in reality, Mercosur became (and remains) only a partial customs union.<sup>9</sup> It adopted a common trade policy and a schedule of common external tariffs (CETs) that applies to 80% of tariff line items, but with some very important exceptions for sensitive sectors such as sugar, automobiles, capital goods, computers, and other technology products. The exceptions were to be phased out by 2006, but many have been extended to 2011, requiring a set of complex rules of origin.<sup>10</sup>

In addition, there are weaknesses with the CET, a core requirement of a true customs union. The CET can be levied twice, first when a good initially enters a Mercosur country, and again if it crosses into another member country. Between the double taxation and multiple exceptions problems, resolving application and uniform enforcement of the CET remains an important unaddressed issue. The double taxation issue is a particular problem for Paraguay, which will suffer significant revenue losses without some type of comprehensive customs revenue sharing plan because most goods enter the Mercosur area through one of the other three countries.<sup>11</sup> The incompleteness of the customs union fosters asymmetry issues (discussed below) that are at the root of Mercosur discontent, and that also suggest that the achievement of a full common market remains a distant, if not illusory goal.

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<sup>7</sup> Costa Vaz, Alcides. Trade Strategies in the Context of Economic Regionalism: The Case of MERCOSUR. In: Aggarwal, Vinod K., Ralph Espach, and Joseph S. Tulchin, eds. *The Strategic Dynamics of Latin American Trade*. Washington, DC. Woodrow Wilson Center Press. 2004. pp. 234-35.

<sup>8</sup> Porrata-Doria, Jr., Rafael A. *MERCOSUR: The Common Market of the Southern Cone*. Durham: Carolina Academic Press. 2005. pp. 14-16.

<sup>9</sup> A free trade agreement (FTA) eliminates tariffs on goods exchanged among participating countries. In a customs union, members also adopt a common external tariff (CET) and common trade policy toward third-party countries. A common market takes the next step of allowing for the free flow of all factors of production (capital and labor) among members.

<sup>10</sup> IDB. *MERCOSUR Report No. 10: 2004-2005*. February 2006. Washington, D.C. p. 70 and Vaillant, op. cit. p. 55.

<sup>11</sup> IDB. *MERCOSUR Report No. 11: 2005-2006*. February 2007. Washington, D.C. pp. 45-47.

The Treaty of Asunción also provided for macroeconomic policy coordination and harmonization of policy legislation at the sectoral level (e.g. energy, agriculture, industry, technology). Some macroeconomic policies, such as exchange rates, have been forced toward complementarity by economic events, but differences remain significant and full coordination of policy is not currently feasible. The rationale for sectoral cooperation rests on inter-country factor mobility being pursued gradually, allowing comparative advantage to work, while easing the integration adjustment process. Nonetheless, sectoral issues and disputes remain a continuing challenge, especially between Brazil and Argentina, as does cross-border movement of goods both within Mercosur and to third country markets.

All parties were required to accept a common set of rights and obligations (Article 2), with little allowance for special and differential treatment for smaller economies. There were many follow-on protocols. Among the most important was the December 17, 1994 Protocol of Ouro Preto, which formally established the common market and extended the institutional framework accordingly. Mercosur adopted a democratic commitment clause in 1996, and there were two protocols that clarified and expanded the dispute settlement process, the last being the Olivos Protocol signed on February 18, 2002, and implemented two years later.<sup>12</sup> Dispute settlement, however, is largely unenforceable and reflects a continuing problem of Mercosur's institutional effectiveness.

Three more recent developments call into question Mercosur's functional institutional capacity. First is the expansion of its membership. Venezuela signed an accession agreement on July 4, 2006 (discussed in detail below), but has been reticent to take on all commitments of the customs union, especially the CET. In December 2006, Bolivia also requested to upgrade its status from associate to full member, although it is reluctant to relinquish its membership in the Andean Community of Nations (Comunidad Andina de Naciones — CAN), as would be required under Mercosur rules.

Second is the new Mercosur Parliament established in December 2006 and headquartered in Montevideo. It comprises 18 representatives from each full member country and has as its primary goal to work toward harmonization of national laws and policies, but it has no authority over national government bodies.<sup>13</sup> Already a point of contention, it has come under criticism for being either too weak to be meaningful, or risking unequal national representation relative to the participating countries' population. In either case, it is viewed by some as raising even more questions over the institutional strength of Mercosur.<sup>14</sup>

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<sup>12</sup> For details on the legal documents, see Porrata-Doria, *MERCOSUR: The Common Market of the Southern Cone*.

<sup>13</sup> Latin American Weekly Report. *Mercosur Meeting Ends on Sour Note*. December 19, 2006. p. 7.

<sup>14</sup> The Argentine Chamber of Exporter, for one, has raised concerns over the inherent weaknesses of the Mercosur Parliament. Camara de Exportadores. Instituto de Estrategia Internacional. *Parlamento del Mercosur: ¿La Voz de los Ciudadanos en la Integración?* Buenos Aires, July 2006. pp. 6-7 and 27-28. See also: Lacalle, op. cit., p. 190.



Third is creation in 2006 of a \$100 million Structural Convergence Fund, financed mostly by Brazil and Argentina, effectively amounting to a transfer of resources to the smaller countries to help ameliorate the inequalities of Mercosur. It provides funding for development and infrastructure projects, destined primarily for Uruguay and Paraguay, but may not be a sufficient response as a compensatory mechanism for acknowledged trade asymmetries within the pact.<sup>15</sup>

## Intra-Mercosur Trade and Internal Dynamics

Intra-Mercosur trade relations have had an uneven and at times troubled history. A combination of internal policy contradictions, diminishing expectations, and a hostile external economic environment in the late 1990s resulted in uneven trade benefits and recurring recriminations against the incomplete customs union. The return of a highly beneficial global economic environment has alleviated some friction, but has not eliminated the need to make policy adjustments or to address concerns raised by the two smallest members of Mercosur. These issues again collectively point to a consistent criticism of Mercosur: its weak institutions and incomplete integration. Too frequently, decision making is the product of political agreement, often on a bilateral basis rather than a rules-based bloc-wide determination. This ad hoc approach to process generates much of the conflict within the customs union, raising questions about the level of commitment to completing the quadrilateral economic integration scheme.<sup>16</sup>

## Intra-Mercosur Trade Trends

As Mercosur lowered tariffs, intra-Mercosur trade was expected to grow relative to trade with third-party countries. As seen in **Figure 2**, this was the initial response from 1991 to 1998, with the jump in intra-Mercosur exports also due to its growth from an initially small base, other economic reforms, and the decade's lengthy global economic expansion. There is, however, an equally evident sudden collapse of intra-Mercosur exports, which fell from 25% of total trade in 1998 to 11% in 2002, before renewing an upward climb to 15% by 2007.<sup>17</sup> This setback reflects a fall in aggregate demand linked to the region's economic crises, intra-Mercosur tariff increases in response to internal Mercosur problems, and Argentina's pressure to lower the CET on capital goods, demonstrating a still strong dependence on trade with developed countries for products not available in the region.<sup>18</sup>

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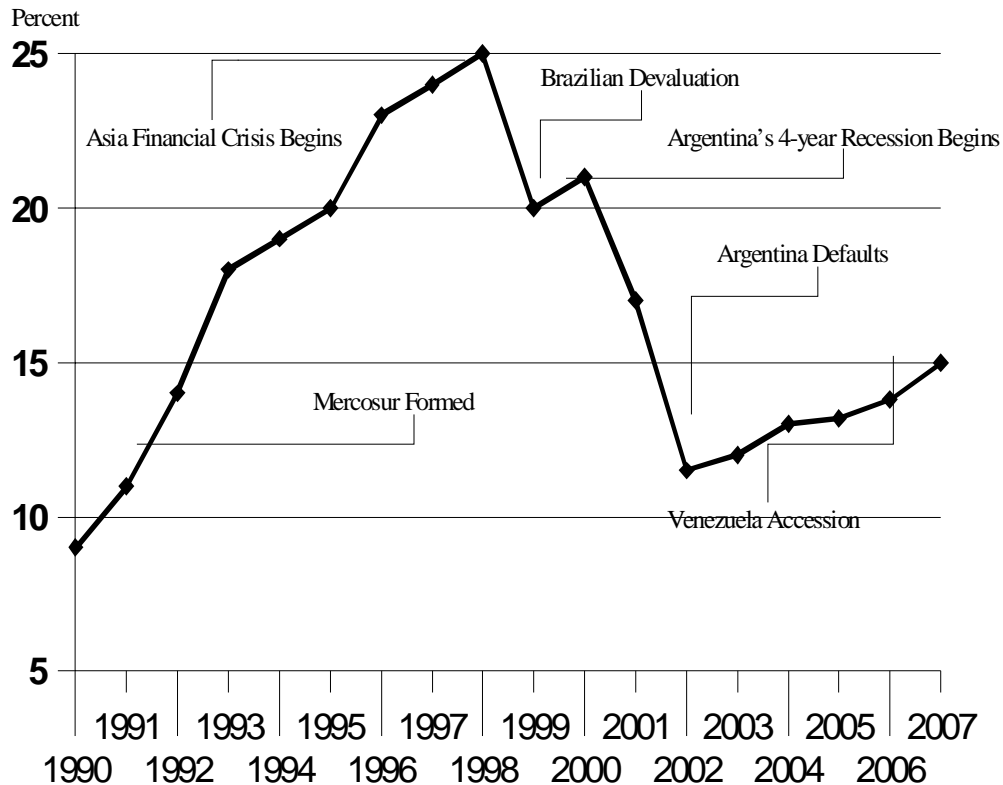
<sup>15</sup> IDB, *MERCOSUR Report No. 12*, pp. 40-41.

<sup>16</sup> Phillips, Nicola. *The Southern Cone Model: The Political Economy of Regional Capitalist Development in Latin America*. London: Routledge, Taylor & Francis Group, 2004. p. 96.

<sup>17</sup> By comparison exports are 60% of intra-EU trade. Intra-Mercosur trade dependence varies by country. In 2005, Mercosur captured 9.8% of Brazil's total trade (exports plus imports) compared to 26.7% for Argentina, 38.8% for Uruguay, and 50.8% for Paraguay.

<sup>18</sup> Phillips, op. cit., pp. 89 and 94-95.

**Figure 2. Intra-Mercosur Exports as Percent of Total Mercosur Exports, 1990-2007**



Source: Inter-American Development Bank. *Mercosur Report No. 12.*, p. 20

From the outset, Mercosur struggled to reconcile a basic inconsistency of partial economic union: how to balance trade integration and equity of member benefits, while retaining some semblance of national control over trade, production, and consumption structure. Natural or structural asymmetries are at the heart of the problem given the pact integrates four economies with huge discrepancies in size, structure, resource endowment, and level of development. In addition to the absolute differences in size, relative differences can fluctuate widely over time. For example, the size of Argentina's economy (GDP) tends to be half that of Brazil's, yet this metric has ranged from a high of 60% in 1992 to a low of 22% in 2002 because of dramatic shifts in relative economic performance, in this case punctuated by the prolonged recession and financial crisis in Argentina.<sup>19</sup>

These structural differences can be compounded by "policy asymmetries" that arise from incongruities in fiscal, monetary, industrial, exchange rate, and other policies. Either type of asymmetry can dramatically alter commercial flows, causing large trade imbalances that can threaten the stability of intra-Mercosur relations as seen in **Figure 2**. When they operate in tandem, the Mercosur policy adjustment

<sup>19</sup> Heymann, Daniel and Adrián Ramos. *MERCOSUR in Transition: Macroeconomic Perspectives*. United Nations. Economic Commission for Latin America and the Caribbean (ECLAC). Santiago, Chile. December 2005. p. 17.

framework has proven to be vulnerable, particularly at times when the countries face external economic shocks.<sup>20</sup>

Such a confluence of events occurred in the 1990s following a series of global shocks that spilled over into Mercosur. The July 1997 Asian financial crisis was the first shock, followed by the Russian default in the summer of 1998. These crises directly affected investor confidence in Brazil, causing extensive capital flight in the fall of 1998, which in turn led to Brazil's steep currency devaluation in January 1999 and the abandonment of its fixed exchange rate stabilization program. With Argentina's strict dollar convertibility regime still in place at the time, the two countries faced a significant "exchange rate policy asymmetry" that altered trade patterns. The sudden trade imbalance was compounded by Argentina's lengthy recession that also began in 1998, leading to its own, far more serious, financial crisis. Argentina's crisis led to the abandonment of its fixed exchange rate regime in December 2001 and subsequent sovereign debt default.

Mercosur's leaders, aware of macroeconomic weaknesses exposed by these crises, proposed a Mercosur Relaunch program as early as May 2000. It formally reaffirmed a commitment to deeper integration, but the Relaunch enthusiasm soon faded as it proved unable to overcome the effects of the financial crises, including the spread of recession to Uruguay and Paraguay and the dramatic fall in trade between Argentina and Brazil (90% of intra-Mercosur commercial exchange).<sup>21</sup> Intra-Mercosur relations became increasingly strained, with Argentina applying temporary restrictions on Brazilian imports, further reducing trade and diminishing incentives for deeper economic integration.

By 2002, the Mercosur economies had all hit bottom and began to rebound, as reflected in intra-Mercosur trade. Problems with intra-bloc trade imbalances, however, remained. As the data in **Appendix 2** demonstrate, all four countries show a linear increase in intra- and extra-Mercosur trade and, with the exception of Paraguay, expanding trade surpluses in their extra-Mercosur trade relations. A core issue remaining is the persistent and growing trade deficits that each country runs with Brazil. A related concern involves the accumulating trade deficits that Paraguay and Uruguay have with Argentina.

## **Asymmetries: Country Perspectives**

The specific asymmetry issues discussed above manifest differently for each country. Two commonly cited threads are the expanding trade deficit with Brazil, particularly since the region began its economic recovery (see **Appendix 2**), and unequal investment and trade in industrial goods. Brazil is seen as the undisputed winner on both counts and is the most ardent supporter of Mercosur for political as well as economic reasons. Interestingly, it is also the least trade dependent member of Mercosur, with total Mercosur trade amounting to no more than 10% of its world

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<sup>20</sup> For details, see IDB, *MERCOSUR Report No. 10*, pp. 39-41.

<sup>21</sup> Bouzas, Roberto. *Mercosur After Ten Years*. In: Tulchin, Joseph S. And Ralph H. Espach, eds. *Paths to Regional Integration: The Case of Mercosur*. Woodrow Wilson International Center for Scholars. Washington, DC. 2002. p. 120.

trade. By contrast, intra-Mercosur trade accounts for 25%-30% of Argentine trade. The two smaller countries are even more dependent on their larger neighbor's markets, but Mercosur has fallen to only 38% of their total exports, down from recent highs of 59% for Uruguay and 41% for Paraguay. This trend may suggest that both countries are reacting to perceived inequalities and structural impediments by diversifying their trade outside of Mercosur.

Both Paraguay and Uruguay have made numerous formal proposals to solve the asymmetry issue. To date, some changes in rules and other technical requirements have been made to improve trade opportunities for the small countries.<sup>22</sup> The most salient development was creation of the Structural Convergence Fund, which has been slow in becoming operational and has only approved its first projects in 2007. So far the asymmetries issue has not been resolved and remains a major challenge to the long-term success of Mercosur.

**Argentina.** Argentina has numerous trade disputes with Brazil, heightened since the post-crisis period when it began to run large trade deficits with Brazil (see data in **Appendix 2**). The structure of these deficits were a particular problem because they were weighted toward high value-added industrial goods, competing directly with Argentina's plans to restart its own industrial sector.<sup>23</sup> The imbalance became increasingly severe; Argentine exports fell from 14% of Brazilian imports in 1998 to 9% in 2007. Brazilian exports, in contrast, rose from 22% to 33% of Argentine imports. The growing imbalance resulted from numerous factors: 1) new exchange rate equilibriums that favored Brazilian goods in the Argentine market over U.S. and European products; 2) a post-recession jump in Argentine aggregate demand; 3) Brazil's export promotion policy emphasizing greater use of domestic inputs, and structural factors in the trade composition of the Mercosur countries.<sup>24</sup>

An analysis of Mercosur trade composition suggests that Brazil's trade surplus is driven considerably by falling import shares of the smaller Mercosur economies, presenting two structural problems not easily addressed. First, the export supply produced by the Mercosur countries does not correspond strongly with Brazil's import demand. Second, Argentine and Uruguayan exports may be less competitive relative to those from countries outside the Mercosur bloc. They also compete closely with one another in the Brazilian market. Together these trends suggest that a natural correction in the Mercosur trade flows may not be likely, leading to Argentina's continued demand for administered remedies to address certain chronic sectoral trade imbalances (e.g. appliances, textiles, paper).

Current administered agreements include the use of voluntary export restraints, quotas, and export taxes.<sup>25</sup> One important example is the Competitive Adaptation Mechanism (CAM) agreed to by Brazil and Argentina in February 2006, over the

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<sup>22</sup> See IDB, *Mercosur Report No. 12*, p. 37 for a discussion of the specific rule changes.

<sup>23</sup> IDB, *MERCOSUR Report No. 11*, pp. 30-32, Heymann and Ramos, *MERCOSUR in Transition*, p. 20, and World Trade Atlas.

<sup>24</sup> *Ibid.*

<sup>25</sup> IDB, *MERCOSUR Report No. 10*, p. 47 and *MERCOSUR Report No. 11*, pp. 35-39, 128.

strong objections of Brazilian industry. It permits protective measures in cases where imports “cause or threaten to cause damage” to a domestic product or industry (safeguards). A convoluted process, it allows for both voluntary export restraints and tariff rate quotas. The CAM was a major policy shift for Mercosur and raises multiple issues. First, it is a bilateral arrangement established under the ALADI system and so not governed by Mercosur. Second, import restrictions represent a retreat from the stated free trade philosophy of Mercosur. Third, the CAM has no enforcement mechanism under ALADI. In short, it compounds existing institutional problems and may undermine the Mercosur agreement even as it attempts, so far unsuccessfully, to restore balance to the largest bilateral relationship within it.<sup>26</sup>

**Paraguay and Uruguay.** The two smaller Mercosur partners face similar trade asymmetries, but also react against the uneven exercise of power. Linked to Mercosur by a natural trade relationship, both Paraguay and Uruguay have still had to respond to structural impediments to their exports. In part, trade asymmetry is a function of their relatively small economies, but the major issue is the disparity between Mercosur’s stated intent to help all members attain their development goals and the actual functioning of the agreement itself. The treaty’s incomplete integration can impede Paraguay’s and Uruguay’s exports, does not provide special and differentiated treatment, and often allows bilateral “diplomacy” to circumvent formal decision-making mechanisms.<sup>27</sup> The safeguards mechanism adopted by Brazil and Argentina is one example, which appears to contradict the principle of reciprocity in rights and obligations. Ad hoc restrictions on trade are another major area of complaint.

Paraguay and Uruguay are not in identical situations and so each has advocated different remedies. Historically Paraguay’s economy has been the most dependent on Mercosur. As a small agricultural economy, geographically remote and landlocked, it depends on its neighbors for export routes to third countries, particularly when river access is seasonally limited. Paraguay is also the poorest and least developed Mercosur member, and so relies on the Mercosur’s promises of market access, enforceable obligations, and integration for its fledgling manufacturing industries. Paraguay’s exports have at times been blocked by bureaucratic restrictions in both Brazil and Argentina and private sector complaints have had little success in resolving what they believe amounts to protectionist non-tariff barriers (NTBs). Paraguay has expressed interest in exploring the possibility of receiving trade preferences within Mercosur as one remedy, but cannot envision leaving Mercosur.<sup>28</sup>

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<sup>26</sup> Haskel, David. Bilateral Agreements: Argentina, Brazil Start Safeguard System To Shield Industries from Mutual Imports. *International Trade Reporter*. February 7, 2006. p. 247, Inter-American Development Bank. *Southern Common Market: New Integration and Co-operation Agreements Between Argentina and Brazil*. [<http://www.iadb.org/intal>], and IDB, *MERCOSUR Report No. 11*, pp. 52-58.

<sup>27</sup> Phillips, op. cit., p. 99.

<sup>28</sup> Osava, Mario. Latin America: Mill Conflict Continues to Delay Integration. *Inter Press Service*. January 4, 2008 and author’s interviews with public and private officials in Asunción, November 2007.

Uruguay faces many of the same NTB problems as Paraguay, but with a higher per capita income, developed port network (direct access to third countries), and more diversified economy, its options for trade expansion both within and outside of Mercosur are greater. It too looks to the Mercosur agreement to fulfill its promises of market access and enforceable obligations. Finding a balance both within and outside Mercosur, including exploring deeper bilateral relationships with the EU and the United States is the challenge for Uruguay. Frustrated by past vulnerability to Argentina's financial crisis and Brazil's periodic barriers to trade, Uruguay has opted to diversify its trade with the world where possible, but its policy options are hindered because it cannot change or ensure enforcement of the Mercosur agreement, it cannot leave Mercosur, nor can it formally negotiate outside it.<sup>29</sup>

The asymmetry issue suggests a certain implicit political hold that Brazil has over the Mercosur derived from its disproportional economic power. By presiding over an incomplete customs union, it can selectively limit the free movement of imports to suit its sectoral needs (at a cost to the other countries equal to the high tariff on capital goods or forgone trade for example), and can also inhibit movement of goods from the smaller countries bound for countries within Mercosur or outside it. Brazil's dominant economic and political-institutional control over the Mercosur has therefore at times fostered a resentment among the smaller countries, increasing their interest in pursuing third country trade arrangements.

Uruguay has responded in part by exploring deeper trade affiliations outside the pact. On November 4, 2006, following U.S. Senate approval, a Bilateral Investment Treaty (BIT) between the United States and Uruguay went into force. Uruguay also sought and received permission from Brazil to explore an FTA with the United States. It subsequently decided to pursue a Trade and Investment Framework Agreement (TIFA) with the United States, which was signed on January 25, 2007. A Joint Commission on Trade and Investment provides the means for ongoing U.S.-Uruguay discussions regarding opportunities for specific trade deals.

The TIFA approach is flexible and allows Uruguay to deepen trade relations with the United States without compromising its Mercosur commitments. Uruguay has linked its desire to develop closer U.S. trade ties with its concern over increasing "bilateralism" between Argentina and Brazil. In December 2006, Argentina responded by criticizing Uruguay for attempting to circumvent Mercosur in its quest to diversify its trade relations, again pointing to an internal strife based on a trade pact that does not appear to operate as promised.<sup>30</sup> Many in Uruguay are not indifferent to this viewpoint and in an ideal world would like to pursue an FTA with the United States in a way that would not compromise its standing with Mercosur.

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<sup>29</sup> Ibid and IDB, *Mercosur Report No. 12*, p. 40.

<sup>30</sup> Haskel, David. Uruguayan President Turns Down Offer to Negotiate Free Trade Agreement with U.S. *International Trade Reporter*. BNA, Inc. October 5, 2006. p. 1440 and Argentina Blasts Uruguay's Pursuit of Free Trade with Non-Mercosur Nations. *International Trade Reporter*. BNA, Inc. January 4, 2007. p. 22.

## The “Pulp Mill” Conflict

Uruguay’s construction of a pulp mill opposed bitterly by Argentina is another conflict within Mercosur. Constructed by a Finnish firm on the Uruguay River, the mill represents the largest single foreign investment project in Uruguay and is expected to provide significant long-term employment opportunities.<sup>31</sup> Argentina alleges that Uruguay is in violation of a bilateral environmental protocol the two countries signed in 1975 and that the plant presents potentially harmful environmental effects that could negatively affect Argentina’s national territory, including a resort area across the river from the construction site.

A World Bank review concluded that the plant poses no serious environmental problems, but did suggest that construction and production design changes could reduce the risk of environmental hazard even further. The World Bank’s International Finance Corporation provided \$100 million to finance the project and the issue continues to spawn protests and diplomatic flare-ups. Periodically, Argentine protesters continue to block bridges over the Uruguay River, disrupting trade and tourist traffic between the two countries. Uruguay has responded at times by closing the border. It also turned to the Mercosur system for dispute settlement. A September 2006 ruling by the Mercosur Ad-Hoc Arbitration Tribunal found that Argentina had failed to live up to its commitment to ensure the free movement of people, goods, and services under the pact, but no award was made.<sup>32</sup>

Argentina also filed a petition for arbitration with the International Court of Justice (ICJ) at The Hague. The ICJ denied Argentina’s request for an injunction to terminate construction. It also declined to require that Argentina take actions to remove protesters. Uruguay subsequently filed a counter claim, arguing that Argentina has failed to take such action. Additional mediation efforts in Madrid and New York ameliorated the the conflict temporarily, but the pulp mill began operations in November 2007 even as the parties awaited a final ruling from the ICJ. Brazil has chosen not to mediate and the ongoing dispute highlights the lack of an effective dispute settlement system within Mercosur.<sup>33</sup>

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<sup>31</sup> Latin American Weekly Report. *Pressure Builds Over Pulp Mill*. August 9, 2007. Originally, the dispute involved a second plant to be built by a Spanish firm. This plant has been relocated, defusing it as an issue.

<sup>32</sup> Inter-American Development Bank. Institute for the Integration of Latin America and the Caribbean. *Dispute Between Argentina and Uruguay: Arbitration Tribunal Award*. *INTAL Monthly Letter*. September 2006 and *Latin American Weekly Report*. November 15, 2007. This episode points to what one scholar observes to be Mercosur’s highly politicized dispute settlement and decision-making processes, which can allow for resolutions based on “political whim, unilateral action, and non-observance of agreed policy commitments.” Phillips, op. cit., p. 99.

<sup>33</sup> One Year On, Small Dispute Threatens to Fracture Mercosur. *Latin American Regional Report. Brazil and Southern Cone*. April 2006. p. 1 and Osava, Mario. *Latin America’s Mill Conflict Continues to Delay Integration*. Inter Press. January 4, 2008.

## Mercosur External Issues

Although Mercosur began strictly as a four-party integration plan, changing internal and external circumstances led the customs union to consider expanding its membership in various ways and to consider the merits of seeking trade arrangements with third party countries and trade groups. As part of its charter, Mercosur remains formally open to the addition of new members.

### Mercosur Outreach

In 1996, Chile and Bolivia joined as the first “associate members.” Since then, Mercosur has continued to enter into “economic complementarity agreements” with most of South America, under ALADI guidelines. Associate membership is a limited arrangement, largely focused on the long-term pursuit of a free trade agreement, often emphasizing sector-specific agreements and cooperation. It does not convey membership status per se, and while members may attend meetings, they have no voting rights, do not participate in the internal functions of Mercosur, and are not required to adopt the CET.<sup>34</sup>

In October 2004, after years of talks, Mercosur and the Andean Community signed a trade pact, giving all Andean countries the equivalent of associate membership. Two months later, this breakthrough led directly to creation of the South American Community of Nations, later renamed the Union of South American Nations (UNASUR), a loosely-conceived pact including 12 countries (those in Mercosur, CAN, along with Chile, Guyana, and Suriname). The CAN and UNASUR in many ways are not true regional agreements; they have some common rules, but details on market access and other specific provisions are bilateral arrangements between each Mercosur country and the CAN. Brazil also granted numerous unilateral concessions to ensure the UNASUR agreement would be completed.<sup>35</sup> These constraints limit prospects for deep continental integration. Nonetheless, sectoral initiatives, such as the proposed South American gas pipeline, already reflect increased cooperation and collective self-determination in the region, which is also now alive in the institutional presence of the CSN.

Mercosur’s other negotiations have experienced mixed success. Trade talks with the EU for a joint Mercosur-EU FTA and the Western Hemisphere countries for a proposed Free Trade Area of the Americas (FTAA) have both come to an impasse over the inability to reach an agricultural agreement acceptable to Brazil. Brazil has also declined U.S. and EU overtures for “WTO-plus” arrangements on market access for industrial goods, services trade, enforceable intellectual property rights, and investment provisions. Continuing interest will depend in part on the outcome of the Doha Round.<sup>36</sup> South-South trade talks have advanced only in limited form.

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<sup>34</sup> Porrata-Doria, *MERCOSUR: The Common Market of the Southern Cone*, pp. 123-124.

<sup>35</sup> IDB, *MERCOSUR Report No. 10*, p. 93.

<sup>36</sup> Unlike the United States, which will consider engaging the Mercosur countries in bilateral talks, the EU prefers to negotiate bloc-to-bloc, which would reinforce rather than diminish (continued...)



Mercosur has begun preliminary discussions with a host of countries that include China, India, SACU, Canada, the Russian Federation, Korea, Egypt, Morocco, and Pakistan. None has moved beyond a simple framework agreement.<sup>37</sup>

## Venezuelan Accession

On July 4, 2006, Mercosur agreed to accept Venezuela as the first additional full member of the pact. The accession protocol was accelerated in mid-2006 at the behest of President Hugo Chávez, who viewed it as supportive of his effort to unify South America and advance his “Bolivarian agenda” that generally stands in opposition to U.S. influence in the region. The accession takes full effect only after formal parliamentary approval by all four Mercosur countries. To date, only Argentina and Uruguay have voted to approve.<sup>38</sup>

The early stages of the accession process was expected to be longer and more involved because of two significant hurdles: Venezuela’s membership in the CAN, which would not have been allowed under Mercosur protocols; and the requirement to adopt the Mercosur CET. Venezuela dispensed with the first issue by defiantly withdrawing from the Andean trade pact in April 2006. Citing Peru and Colombia’s negotiations for FTAs with the United States as contrary to CAN’s and Latin America’s best interests, President Chávez left the pact specifically to join Mercosur. To address the second issue, Mercosur, under Brazil’s leadership, negotiated to give Venezuela four years to comply with the CET, with other obligations of the pact not completely phased in until 2014.<sup>39</sup>

Mercosur may have many incentives to bring Venezuela into the fold. The addition of a fifth member adds to the economic strength of the bloc, which would comprise three-quarters of South American GDP. Venezuela also promised immediate selective duty-free treatment for imports from Paraguay and Uruguay, with no requirement for reciprocal treatment until 2013. Venezuela may increase the potential for intra-Mercosur trade as a relatively large Latin American market that also offers sectoral complementarity and energy security with its vast oil reserves and plans for a regional pipeline.

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<sup>36</sup> (...continued)

Mercosur’s functioning as a customs union.

<sup>37</sup> IDB, *MERCOSUR Report No. 10*, pp. 90 and 96-100.

<sup>38</sup> United Nations. Economic Commission on Latin America (ECLAC). *Latin America and the Caribbean in the World Economy 2006*. Santiago, August 2007. p. 132.

<sup>39</sup> Mercosur. Protocolo de Adhesión de la República Bolivariana de Venezuela al Mercosur. Artículo 4. July 4, 2006. Haskel, David. Mercosur, Venezuela Agree on Protocol for Caracas Accession to Trading Bloc. *International Trade Reporter*. BNA, Inc. June 1, 2006. p. 837. The accession process has been criticized by, among others, former Brazilian Ambassador to the United States Rubens Barbosa, who stated that “In the European Union they negotiate the terms of entry, and then the country joins. Here, we’re doing it the other way around, which is craziness...” Rohter, Larry. Venezuela Wants Trade Group to Embrace Anti-Imperialism. *The New York Times*. January 18, 2007.

A more thorough analysis of the potential trade effects, however, suggests that the trade and economic benefits for Mercosur may be easily overstated. Currently, Mercosur trades little with Venezuela and estimates of trade growth are modest at best, given limitations in the accession protocol (exemptions and other restrictions) and current tariff preferences that already apply to a high proportion of goods expected to benefit from the agreement. Trade between Mercosur and Venezuela averages no more than 3% of the pacts total world trade, with the exception of Uruguay where crude oil constitutes 12% of total imports. The energy sector promises the greatest benefit through deeper cooperation in energy supply, but which could also be achieved without Venezuela's full integration into Mercosur. In addition, Venezuela's access will complicate trade policy coordination within the expanded bloc, both regionally and multilaterally.<sup>40</sup>

The political motivations and ramifications for Venezuela's accession may be even more of an issue. Concern has grown, for example, over certain of President Chávez's policies that may be construed as hindering democracy, which in turn could be considered a direct challenge to Mercosur's democratic clause. Brazilian Foreign Minister Celso Amorim has reaffirmed his view that Mercosur's primary goal from the start has been to consolidate democracy in South America. Chávez's decision to close a key radio station (viewed by some as suppressing freedom of speech) and his one-time plan to alter the Venezuelan Constitution to abolish presidential term limits (viewed by some as a direct assault on the democratic process) raised concern over real and perceived undemocratic behavior in Venezuela. This issue has escalated with some members of the Brazilian Senate continuing to argue for postponement of a vote to consider Venezuela's accession.<sup>41</sup>

Although Venezuela remains a non-voting member until the accession is ratified, it does have a voice in Mercosur affairs, increasing its influence on intra-pact and external trade negotiations. The marginal effect may be to strengthen resolve by some countries to challenge U.S. influence in South America, although there are also moderating influences in all countries. Uruguay and Paraguay could also view Venezuela as having a diluting force on Brazil's political dominance in the pact, but opinions seem divided at present in both countries.

Venezuela's accession, however, may have unintended regional consequences should countries outside Mercosur be put in a position of having to choose between a U.S. or Mercosur trade agreement. Peru has even suggested forming a new trade bloc, the Community of the Pacific, which would include countries with complementary trade arrangements: the United States, Canada, Mexico, the Central

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<sup>40</sup> A detailed analysis of the potential trade effects of Venezuela's access may be found in: IDB, *Mercosur Report No. 11*, pp. 99-117 and see also, ECLAC, *Latin America and the Caribbean in the World Economy*, pp. 132-134.

<sup>41</sup> See Magalhaes, Luciana and Katia Cortes. Brazil Senator Says Venezuela Deadline on Mercosur 'Unfeasible.' *Bloomberg*. July 4, 2007, Haskel, David. Venezuela's Mercosur Partners Downplay President Chávez's Nationalization Pledges. *International Trade Reporter*. January 18, 2007, and Wheatley, Jonathan and Richard Lapper. Left Turn Ahead? How Lula's Plan Could Condemn Brazil to Mediocrity. *Wall Street Journal*. February 21, 2007.

American countries, Panama, Colombia, Peru, and Chile.<sup>42</sup> This prospect may be further reinforced by Bolivia's request to become a full member of Mercosur, although it appears reluctant to give up its membership in the CAN and accept the tariff convergence challenge inherent in adapting to the Mercosur CET.<sup>43</sup>

## Mercosur and the Doha Round

The current, and now long-extended, WTO multilateral round of trade negotiation highlights other interesting institutional constraints within Mercosur. As a customs union with a supposed common external trade policy and CET, Mercosur would theoretically need to approach the Doha Development Round with some common, if not identical, trade negotiation objectives, or risk differing country policies undermining the integration scheme. Mercosur has responded by creating an ad hoc consultation and coordination group to address the Doha negotiations. The bloc, however, does not approach the WTO as a united voice, but Doha negotiations are exploring the possibility of a more flexible approach to address the interests of the customs union.<sup>44</sup>

Brazil has taken the negotiating lead and perhaps has the most to gain from the Doha Round on both political and economic grounds, but it is not clear that positions benefitting Brazil will always be those supported by the other Mercosur countries.<sup>45</sup> Although there has been broad agreement in the realm of agricultural issues, as part of the broader developing country consolidated response to developed country WTO positions, there is less agreement in the areas of nonagricultural market access and services. The most sensitive areas with respect to maintaining a cohesive customs union are in setting tariff levels and determining sensitive product lists that each country may elect to receive special treatment under a WTO agreement. Given there will be limits on the number of tariff lines permitted, large differences in both these areas among Mercosur countries could lead to either a breach of the customs union rules, or those of the Doha agreement. Balancing these goals in the WTO negotiations is a challenge for the four Mercosur countries and should the Doha Round stall indefinitely, it is possible that alternative paths to global integration may take on renewed emphasis.<sup>46</sup>

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<sup>42</sup> Chauvin, Lucien O. Peru Proposes New Trade Bloc of Hemisphere Nations on Pacific Coast. *International Trade Reporter*. BNA, Inc. August 3, 2006. p. 1172. For a detailed summary of the environmental, legal, and economic issues, see IDB, *MERCOSUR Report No. 11*, pp. 69-76.

<sup>43</sup> ECLAC, *Latin American and the Caribbean in the World Economy*, p. 132.

<sup>44</sup> IDB, *MERCOSUR Report No. 11*, p. 94 and Costa Vaz, *Trade Strategies in the Context of Economic Regionalism: The Case of MERCOSUR*, p. 256 and Washington Trade Daily. *US, EU Brazil on 'Flexibilities.'* March 11, 2008.

<sup>45</sup> On Brazilian trade strategy and the WTO, see CRS Report RL33258, *Brazilian Trade Policy and the United States*, pp. 5-6 and 15.

<sup>46</sup> IDB, *MERCOSUR Report No. 11*, p. 94-97.

## The Mercosur-Israel Free Trade Agreement

On December 18, 2007, after four years of negotiations, Israel signed a free trade agreement at the Mercosur Summit with the four member countries, the first such agreement with a country outside the Western Hemisphere. The agreement is limited largely to market access for merchandise trade, allowing for full free trade to be phased in within 10 years. Mercosur and Israel have a near even balance of trade in their \$1 billion commercial relationship. Mercosur exports mostly agricultural products and imports technology goods. Although this arrangement is highly complementary, treatment of agricultural exports and capital goods imports has been a stumbling block for the Mercosur countries, and particularly Brazil, in trade negotiations with the EU, the United States, and at the Doha Round. Safeguards and other restrictions will apply during the transition period to full free trade.<sup>47</sup>

## China-Mercosur Trade

Mercosur and China have no formal trade agreement in effect, but bilateral trade has grown tremendously in recent years. In 2007, Mercosur exported \$16.1 billion of goods to China, importing \$19.7 billion. China represented 7.2% of Mercosur's exports and 11.2% of its imports. Total trade between China and the four Mercosur countries ranges from a low of 11% of total foreign trade for Uruguay to 18% for Argentina and Brazil, and a high of 28% for Paraguay (importing mostly computer and other electronic equipment).<sup>48</sup> Mercosur's commodity exports and imports of labor-intensive goods explain most of the recent strong growth in this relationship.<sup>49</sup> Such strong trade growth also presents problems for Mercosur because manufactured imports displace local products. China's expanding trade surplus would be even bigger were it not for the world prices of agricultural commodities currently driving Mercosur's export values, suggesting that as China becomes a larger trade partner, the deficit could widen. The prospect for a deteriorating bilateral trade balance has led both Brazil and Argentina to pursue anti-dumping cases and resort to use of import licenses, voluntary export restraints, and higher tariffs.<sup>50</sup>

## Implications for U.S. Trade Policy

Mercosur came to life as both a Brazilian-Argentine political project and a broader economic integration scheme among four contiguous, but highly differentiated countries. Mercosur has fostered a prolonged period of cooperation in a region with a long history of conflict, an important achievement in both political and economic terms. Still, it is a limited customs union and remains intact despite its "incompleteness" in part because: 1) there is no simple alternative for its

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<sup>47</sup> Global Insight. *Mercosur Signs Deal with Israel*. December 19, 2007 and Haskel, David. *Mercosur Concludes FTA with Israel*. *International Trade Reporter*. December 20, 2007.

<sup>48</sup> World Trade Atlas.

<sup>49</sup> IDB, *Mercosur Report No. 12*, pp. 23-24

<sup>50</sup> *Ibid.*, pp. 24 and 45-46.

members; 2) there is an unknown, but perceived serious downside risk to its dissolution, and; 3) there is always the vague hope that promises of institutional improvements will produce more equitable outcomes. The result remains an uncomfortable status quo in which form (e.g. the new Parliament) often supercedes function (e.g. deeper integration).

Economic integration based on mutual growth in trade and development is at the heart of the Mercosur charter, but given shortfalls in achieving this goal, it is likely that a persistent dissatisfaction among the smaller partners may continue, particularly given Brazil's political and economic dominance and Mercosur's inability to address institutional disagreements. Deeper economic integration promises to resolve some problems, but there appears to be little chance for movement in that direction in the near future.

Instead Mercosur has opted to pursue new institutional bureaucracies (the Parliament) and outreach to third countries, albeit on a very limited basis. The Parliament is in its infancy and Mercosur has not been able to consummate a trade agreement with its most important trade partners, the United States and the EU. South-South agreements and expansion of associate membership to South American countries has progressed, but only as limited market access arrangements. The big, but questionable move is the accession invitation to Venezuela, which has also had problems. Venezuela has been given leeway in adopting Mercosur commitments, which has undermined the pact's cohesiveness,<sup>51</sup> and could end up shifting the political orientation of Mercosur, while providing only relatively small trade effects.

Historically, the United States has supported Mercosur as a potential complementary path to meeting its own goal of Western Hemisphere economic integration, but U.S.-Mercosur trade is small and Mercosur has shown little enthusiasm for supporting U.S. initiatives for a hemispheric-wide trade agreement. The addition of Venezuela would likely solidify this position. Although Mercosur has resisted the FTAA as envisioned by the United States, Venezuela is the only country in Latin America to reject the idea unequivocally.

It appears that Mercosur has opted to emphasize its expansion both in the region and with other developing countries over agreements with its largest developed country trade partners, looking to the World Trade Organization (WTO) as the preferred alternative for achieving many of its trade policy goals. Nonetheless, U.S.-Mercosur commercial and economic ties are expanding and the United States is pursuing deeper bilateral trade relations with Uruguay that could provide new ideas for a broader integration commitment. The alternative may be for Mercosur and the United States to expand their mutually exclusive bilateral agreements, increasing the potential for overlapping trading systems, which few, if any, view as either economically or administratively optimal.

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<sup>51</sup> Obiko Pearson, Natalie. Chávez Hosts 6-Nation Trade Summit. *Associated Press*. July 5, 2006.

## Appendix A. U.S. Merchandise Trade with Mercosur

(\$ millions)

Country	2003	2004	2005	2006	2007	% Change 2006-07	% Change 2003-07
<b>U.S. Exports</b>							
Brazil	11,211	13,897	15,372	19,231	24,628	60.2%	119.7%
Argentina	2,437	3,388	4,122	4,776	5,855	42.0%	140.3%
Uruguay	327	326	357	482	640	79.3%	95.7%
Paraguay	484	623	896	911	1,237	38.1%	155.6%
Mercosur 4	14,459	18,234	20,747	25,400	32,360	56.0%	123.8%
Venezuela	2,831	4,767	6,421	9,002	10,199	58.8%	260.3%
Mercosur 5	17,290	23,001	27,168	34,402	42,559	56.7%	146.1%
Mexico	97,412	110,834	120,365	133,979	136,541	13.4%	40.2%
LAC*	51,946	61,465	72,407	88,969	107,528	48.5%	107.0%
Latin America	149,358	172,299	192,772	222,948	244,070	26.6%	63.4%
World	724,771	818,775	905,978	1,036,635	1,162,708	28.3%	60.4%
<b>U.S. Imports</b>							
Brazil	17,910	21,160	24,436	26,367	25,636	4.9%	43.1%
Argentina	3,170	3,745	4,584	3,979	4,495	-1.9%	41.8%
Uruguay	256	580	732	512	492	-32.8%	92.2%
Paraguay	53	59	52	58	68	30.8%	28.3%
Mercosur 4	21,389	25,544	29,804	30,916	30,691	3.0%	43.5%
Venezuela	17,136	24,921	33,978	37,134	39,897	17.4%	132.8%
Mercosur 5	38,525	50,465	63,782	68,050	70,588	10.7%	83.2%
Mexico	138,060	155,902	170,109	198,253	210,799	23.9%	52.7%
LAC*	78,829	98,647	122,873	133,676	134,773	9.7%	71.0%
Latin America	216,889	254,549	292,982	331,929	345,572	18.0%	59.3%
World	1,257,121	1,469,704	1,673,455	1,853,939	1,953,699	16.7%	55.4%
<b>U.S. Balance of Trade</b>							
Brazil	-6,699	-7,263	-9,064	-7,136	-1,008		
Argentina	-733	-357	-462	797	1,360		
Uruguay	71	-254	-375	-30	148		
Paraguay	431	564	844	853	1,169		
Mercosur 4	-6,930	-7,310	-9,057	-5,516	1,669		
Venezuela	-14,305	-20,154	-27,557	-28,132	-29,698		
Mercosur 5	-21,235	-27,464	-36,614	-33,648	-28,029		
Mexico	-40,648	-45,068	-49,744	-64,274	-74,258		
LAC*	-26,883	-37,182	-50,466	-44,707	-27,245		
Latin America	-67,531	-82,250	-100,210	-108,981	-101,502		
World	-532,350	-650,929	-767,477	-817,304	-790,991		

**Source:** Table created by CRS from U.S. Department of Commerce data.

\* Latin America and the Caribbean, except Mexico.

## Appendix B. Intra- and Extra-Mercosur Merchandise Trade by Country

(in U.S. \$ millions)

	2002	2003	2004	2005	2006
<b>Argentina</b>					
<b>Mercosur Total Trade:</b>	8,628	10,845	15,451	19,348	23,540
– Brazil	7,345	9,366	13,331	16,770	20,395
– Paraguay	596	741	905	964	1,129
– Uruguay	665	718	1,214	1,614	2,016
<b>Mercosur Trade Balance:</b>	2,792	469	-1,829	-3,929	-3,642
– Brazil	2,310	-33	-2,121	-4,100	-4,131
– Paraguay	86	151	139	54	113
– Uruguay	419	372	154	306	376
<b>Extra-Mercosur Total Trade</b>	26,071	32,945	41,570	49,726	57,066
<b>Extra-Mercosur Trade Balance</b>	9,927	15,619	13,959	15,630	15,948
<b>Mercosur as % of Total Trade</b>	24.9%	24.8%	27.1%	28.0%	29.2%
<b>Brazil</b>					
	2002	2003	2004	2005	2006
<b>Mercosur Total Trade:</b>	8,981	11,477	15,425	18,162	23,000
– Argentina	7,090	9,234	12,945	16,154	19,771
– Paraguay	942	1,182	1,170	1,280	1,527
– Uruguay	896	942	1,190	1,344	1,624
<b>Mercosur Trade Balance:</b>	-2,359	-133	2,399	4,590	4,901
– Argentina	-2,405	-112	1,801	3,676	3,657
– Paraguay	176	232	574	642	935
– Uruguay	-74	-134	114	356	927
<b>Extra-Mercosur Total Trade</b>	98,611	109,867	143,832	173,697	205,865
<b>Extra-Mercosur Trade Balance</b>	15,490	24,957	31,294	40,167	41,173
<b>Mercosur as % of Total Trade</b>	8.4%	9.5%	9.7%	9.5%	10.1%

Total trade = exports + imports. Trade balance = exports - imports.

Source: World Trade Atlas, reporting national account data.

**Appendix B. Intra- and Extra-Mercosur Merchandise Trade by Country  
(continued)**

(in U.S. \$ millions)

	2002	2003	2004	2005	2006
<b>Paraguay</b>					
<b>Mercosur Total Trade:</b>	1,398	1,817	2,388	2,472	2,779
– Argentina	344	469	722	739	903
– Brazil	831	1,043	1,134	1,172	1,385
– Uruguay	223	302	513	535	481
<b>Mercosur Trade Balance:</b>	-292	-349	-656	-652	-933
– Argentina	-274	-337	-518	-525	-565
– Brazil	-125	-193	-508	-530	-631
– Uruguay	107	184	389	429	363
<b>Extra-Mercosur Total Trade</b>	1,063	1,290	1,890	2,396	4,404
<b>Extra-Mercosur Trade Balance</b>	-267	-274	-370	-872	-2,410
<b>Mercosur as % of Total Trade</b>	56.8%	58.5%	55.8%	50.8%	38.7%
<b>Uruguay</b>					
	2002	2003	2004	2005	2006
<b>Mercosur Total Trade:</b>	1,576	1,752	2,229	2,630	3,308
– Argentina	654	728	911	1,172	1,380
– Brazil	822	1,752	1,162	1,281	1,659
– Paraguay	76	59	75	76	84
<b>Mercosur Trade Balance:</b>	-345	-336	-538	-876	-1,062
– Argentina	-428	-418	-202	-638	-778
– Brazil	42	12	-192	-369	-493
– Paraguay	48	37	43	36	32
<b>Extra-Mercosur Total Trade</b>	2,249	2,636	3,805	4,591	5,400
<b>Extra-Mercosur Trade Balance</b>	215	344	341	339	226
<b>Mercosur as % of Total Trade</b>	41.2%	40.0%	36.9%	36.4%	38.0%

Total trade = exports + imports. Trade balance = exports - imports.

Source: World Trade Atlas, reporting national account data.