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Industrial Restructuring and Economic Integration: The Outlook for Mercosur

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1. Introduction (*)

The prevalence of exchange rate instability and the fragility of economic ties between the region's nations stand as two fundamental stumbling blocks to creation of the Southern Common Market, or Mercosur. History has no record of successful experiences in economic integration involving economies with these particular characteristics.

In an earlier paper (Araujo Jr. 1991b), I discussed how exchange rate policies might be harmonized within a context where inflation has not yet been defeated. I showed that it is feasible to fix the real exchange rate, albeit transitorily, and that such a measure could contribute to lasting macroeconomic adjustment.

The present paper explores the conditions under which

(*) This paper was prepared for the United Nations Industrial Development Organization (UNIDO). I would like to thank Honório Kume and Lia Valls Pereira for information provided on the import policies currently enforced by Mercosur members and on the recent evolution of governmental talks concerning the Southern Common Market project.

Mercosur could alter the pattern that has governed relationships between the region's economies in recent decades, presupposing that the monetary question has been resolved. Section 2, based on the latest progress in international trade theory, describes the typology of effects that economic integration would in principle have on productive structures and trade flow. Section 3 presents the qualifications that must be made when applying this analytical approach to the Mercosur case. Section 4 comments on the agenda of steps to be taken by Mercosur governments in the coming years. Lastly, section 5 provides a summary of the paper's main conclusions.

2. Industrial Configuration, Industrial Location, and Trade Patterns

During the decade of the eighties, the theories of international trade and of industrial organization moved together to form one unified area of knowledge, as the result of two converging processes. On the one hand, the long cycle of challenges to the Ricardo-Heckscher-Ohlin-Samuelson version of the theory of comparative advantages came to a close within the trade pattern debate. This controversy, inaugurated with Prebish's theses and Leontief's paradox, produced invaluable new tools useful in analyzing contemporary international economics -- for example, Linder's ideas, the product cycle theory, and intra-industry trade indexes. However, up until the beginning of the eighties, these tools served only to subsidize partial criticisms of established theory. Since then, with the advent of Helpman and

Krugman's approach (1985), it has become possible to incorporate these tools into a new theory that stresses economies of scale and imperfect competition as key factors in explaining international trade. This theory does not abandon the fundamental thesis of the previous theory -- that trade is worthwhile whenever there exist disparities between two economies' opportunity costs -- but it adds two important observations: (a) not always are the variables labor costs and factor proportions explicative of opportunity costs and (b) it is not enough to identify the origin of comparative advantages; the rhythm of change must also be taken into account.

On the other hand, in the realm of the literature on industrial organization, the Schumpeterian competition and contestable market theories emphasized the importance of interactions between technical progress, competition, and market size and thereby encouraged research of topics related to Helpman and Krugman's approach.(*) In view not only of the economies of scale and of scope inherent to contemporary technology but also of the business strategies that must be implemented to take advantage of these potential gains and of the dimensions of the final demand vector for goods and services produced by that technology, there is a growing number of sectors wherein only firms of a global scope can survive. Therefore, any current analysis of industrial dynamics must necessarily include an

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(*) The Schumpeterian competition theory is described in Nelson and Winter (1982) and the contestable market theory, in Baumol et al. (1982).

analysis of trade patterns, and visa versa.

In his latest book, Geography and Trade (1991), Paul Krugman has made another notable contribution to this integrated vision of industrial dynamics. He argues that the topic of trade would still remain relevant even under the drastic hypothesis that the current trend toward formation of unified economic spaces were carried to its ultimate consequences and all national borders were to disappear. Goods and services would nevertheless continue to be produced in one location and consumed in another, due to the combined influence of three main factors:

(a) the size and geographic distribution of consumer markets;

(b) transportation costs;

(c) economies of scale.

This model does not consider the above factors to be exogenous variables that explain trade volume but to be products of historical events, of technical progress, and of economic policy. Central to the model is its return to classic themes from studies on regional economics. Once a certain industrial park has been established, locational economies begin to operate, attracting new investments as a direct function both of the size of the market already in existence and of the economies of scale inherent to the new ventures and as an inverse function of the relation between transport costs for productive inputs and for final goods.

The ensuing process of industrial concentration will be governed by (a) the pace of technological innovations, which can

affect either transport costs or economies of scale; (b) the performance of other existent industrial parks; and (c) public or private decisions to set up new parks in other regions.

Two applications of Krugman's model are particularly relevant to the purpose of this paper. One has to do with the political economy of protection and the other, with the theory of economic integration.

Some sixty years ago, John Maynard Keynes amazed the academic community with what has become a time-honored declaration: "I sympathize, therefore, with those who would minimize, rather than those who would maximize, economic entanglement between nations. Ideas, knowledge, art, hospitality, travel -- these are things which should of their nature be international. But let goods be home-spun whenever it is reasonably and conveniently possible; and, above all, let finance be primarily national. Yet, at the same time, those who seek to disembarrass a country of its entanglements should be very slow and wary. It should not be a matter of tearing up roots, but of slowly training a plant to grow in a different direction."(*)

Through Krugman's model, it is possible not only to reconcile Keynes' heresy with academic canons but also to go a long ways toward conciliating protectionists and liberals in their longstanding polemic. Indeed, whenever the prospects for growth on a local market, plus trends in technical progress, make

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(*) Cited by Harrod (1972), p. 526.

it feasible to plan changes in opportunity costs, it is worth investing in the creation of new industrial parks, as long as the costs of temporary protection of infant industries do not surpass the present value of expected social benefits.

One worry that often haunts economic integration projects are the dissimilarities in the levels of efficiency displayed by the productive structures involved in the project. Common sense tells us that the dismantling of trade barriers means that only the most competitive industries in each nation will outlive like industries in the other nations. Although this may in fact be beneficial in the long run, the short-run costs of industrial relocation may be unbearable for certain countries.

It is interesting to note, however, that in the case of the European Common Market and of the European Free Trade Association this was practically a non-existent problem. Krugman's model shows us that these cases were not exceptional, since the formation of a unified economic space will have other effects that tend to override the problem of industrial relocation.

In principle, three kinds of effects are foreseeable. The first is simple trade growth, with no change in existing industrial configurations. This would be the case with industries which, prior to integration, were already operating according to international standards of quality and efficiency in more than one member nation. After integration, intra-industry trade flow would appear, based essentially on product differentiation and market segmentation strategies -- as exemplified by sales of

Beaujolais in Venice and of Valpolicella in Lyon, of the Fiat Uno in London and the Rolls Royce in Rome, of sherry in Glasgow and Drambuie in Madrid, and so on.

Secondly, economic integration may produce changes in company product mixes, as a consequence of mergers, acquisitions, and partnership formation or of the restructuring of individual companies, so as to exploit the economies of scale and scope generated by the integration project. Examined from a sectorial perspective, these changes would mean that each country would begin to display industrial configurations better adjusted to the characteristics of available technologies and to market dimensions. In this case, the benefits of integration would result mainly from intra-industry specialization: type-X lathes would be produced in Argentina and type-B, in Brazil; colorings and pigments in Montevideo and paints in São Paulo.

The third kind of effect would be industrial relocation, something that would tend to occur where inequalities in competitiveness could not be corrected by means of the modifications described in the previous paragraph. This consequence obviously becomes an obstacle to integration in those cases in which the productive structures of member nations are so dissimilar that they do not generate opportunities for the other two types of effects to take hold.

3. Mercosur: Foreseeable repercussions

Given the peculiarities of the region's economic ties in recent decades, application of the typology of effects described above requires some preliminary qualifications in the case of Mercosur. We must first consider the geographic distribution of trade between Mercosur countries, as depicted in table 1. On the one hand, over the past thirty years Paraguay and Uruguay have tended to concentrate their transactions within the area of the Latin American Integration Association (Aladi), destination of up to 40% to 50% of these two nations' foreign trade more recently. On the other hand, Brazil has diversified its trade partners while almost always channeling over 50% of its foreign commerce to the EEC and the US but only 10% to 15% to Aladi. Argentina's behavior has lain somewhere in the middle: at the beginning of the sixties, its trade with Latin America was slightly more than 10%, whereas during the second half of the eighties the figure reached a peak of 25%.

This trade pattern is partly a natural result of disparities in both the size and the level of complexity of these economies' productive structures. However, the influence of three additional factors must be noted: the style of industrial growth prevailing in the region through the end of the seventies, the foreign debt crisis, and exchange rate instability.

The defining feature of an industrial policy aimed at import substitution is its restrictions on the entry of foreign products that compete with local goods. In Brazil, where the creation of

Table 1

Regional Distribution of Foreign Trade by Mercosur Nations

Period/Area	Argentina	Brazil	Paraguay	Uruguay
1961/1963				
Aladi	12.8	10.7	27.2	14.5
US	18.4	35.6	23.7	6.0
EEC	50.1	27.0	28.1	26.1
Others	18.7	26.7	21.0	53.4
Total	100.0	100.0	100.0	100.0
1970/1972				
Aladi	21.5	9.9	29.3	24.8
US	15.8	27.0	18.5	8.4
EEC	43.1	33.4	32.5	39.1
Others	19.6	29.7	19.6	27.7
Total	100.0	100.0	100.0	100.0
1980/1982				
Aladi	21.3	15.0	47.7	37.1
US	16.5	18.2	7.8	9.0
EEC	25.8	20.3	19.7	21.9
Others	36.4	46.5	24.8	32.0
Total	100.0	100.0	100.0	100.0
1986/1988				
Aladi	25.4	12.0	45.5	40.1
US	14.5	23.8	8.5	10.7
EEC	29.5	24.7	23.6	23.7
Others	30.6	39.5	22.4	25.5
Total	100.0	100.0	100.0	100.0

Source: Aladi

new branches of activity has systematically generated domestic market reserves for existing national firms, this strategy can be seen taken to its extreme. As a consequence, Brazilian trade policy has been unable to adequately fulfil the role that inherently falls to large economies participating in regional integration processes: promoting trade by creating purchasing power in neighboring economies through imports from those neighbors.

The foreign debt crunch of the first half of the eighties aggravated this perverse characteristic of the Brazilian economy, as reflected in table 2. From 1980 through 1983, Brazilian imports from what now forms Mercosur dropped 46%. In response, intra-regional trade fell in an equal proportion, and Brazil's own balance of payments problem was exacerbated as the nation's trade balance with the region plummeted from US$ 816 million to US$ 463 million.

As I showed in two earlier papers (Araujo Jr. 1991a, 1991b), in recent decades sharp exchange rate variations have become an endemic disease in all of Latin America. While exchange rate instability may not be an obstacle to trade growth, it does trammel the closing of long-term international contracts between independent firms. I will examine the consequences of this problem later in this paper, when I analyze the behavior of intra-industry trade between Argentina and Brazil.

The recovery of regional commerce during the second half of the eighties, illustrated in table 2, was possible thanks to a

Table 2

Brazilian Trade with Mercosur Nations: 1980/1990

in US millions

Year	B R A Z I L			Intra-MERCOSUR Trade (4)	Brazilian Share (1+2)/(4)
	Exports (1)	Imports (2)	Balance (3)		
1980	1812	996	816	3434	0.82
1981	1703	802	901	2995	0.84
1982	1112	797	315	2353	0.81
1983	999	536	463	1836	0.84
1984	1322	646	676	2289	0.86
1985	987	700	287	1950	0.87
1986	1215	1089	126	2636	0.87
1987	1306	810	496	2531	0.84
1988	1637	954	683	3003	0.86
1989	1367	1906	(539)	3717	0.88
1990	1197	2237	(1040)	4036	0.85

Source: Mercosur Index

set of bilateral agreements that were forerunners to the Treaty of Asunción, which in turn was to give rise to the Mercosur project in March 1991. From 1986 through 1988, the governments of Argentina and Brazil signed twenty-two protocols meant to enforce the Program for Economic Integration and Cooperation between the two countries, while Argentina and Uruguay worked to expand Cauce (the Argentinean/Uruguayan Agreement on Economic Cooperation) and Brazil and Uruguay renegotiated PEC (Trade Expansion Program).

Despite the success attained on the trade level, these bilateral agreements failed to erase two blemishes marring relations between these economies: the systematic generation of Brazilian superavits -- a pattern broken only in 1989 and 1990, when the cruzeiro was highly overvalued (see Araujo Jr. 1991a) -- and the absence of stable intra-industry transactions. Accumulating trade surpluses while making no equivalent compensatory investment in neighboring nations meant that on the one hand Brazil was underutilizing trade potential, by inadequately stimulating the region's buying power, and that on the other hand the region's central banks were periodically forced to renegotiate debts. Before moving on to a discussion of possible solutions to this dilemma (section 4), and in order to assess the probable impact on Mercosur, we must consider the final peculiarity of this project: intra-industry trade.

The intra-industry transactions examined in the literature are regular trade flows that result from the exploration of economies of scale and of standards of competition based on product differentiation and market segmentation. Three kinds of

flow may exist: (a) intra-company trade; (b) the import of goods that compete with local supplies; and (c) the purchase and sale of inputs between independent companies under long-term contracts. Intra-industry trade indicators measure the degree of integration between the economies under analysis and encompass not only the ties between productive structures but also the interactions between markets for final goods.

Opportunities for this kind of trade between Mercosur members have been scarce in recent decades due to Brazil's excessive protectionism and to exchange rate instability. Indeed, the only feasible modality has been intra-company trade and even then under quite restricted circumstances.

One reflection of these conditions is the behavior of Argentinean and Brazilian companies operating within both economies. According to Guia Interinvest, in 1986 Argentinean capital had participation in 130 companies in Brazil while, according to the Atlas Financeiro, only 15 Brazilian companies had subsidiaries in Argentina in 1989. But none of these firms appears on the list of the 300 largest exporters and importers responsible for bilateral trade over the past 5 years, contrary to what typically occurs in the case of headquarters and their branches.

Table 3 provides a more complete picture of the evolution of intra-industry trade between Argentina and Brazil. Within a selected set of industries, data cover all branches that at least once in 1975, 1980, 1985, or 1987 reached intra-industry trade

Table 3

Argentinean/Brazilian Intra-industry Trade: 1975/1987

Industry	1975		1980		1985		1987	
	Bi	(X+M)	Bi	(X+M)	Bi	(X+M)	Bi	(X+M)
Petroleum products	2.8	1.3	6.3	22.8	6.4	10.4	16.9	36.1
Organic chem.prod.	72.5	2.9	92.0	9.1	29.2	9.3	45.8	21.5
Combustion engines	83.0	4.4	30.0	22.8	76.7	12.7	78.2	20.9
Office machines	99.2	20.2	16.9	20.7	4.7	3.9	0.5	3.8
Pumps & compressors	46.7	7.1	89.2	20.9	92.4	7.6	62.3	11.9
Electrical appliances	13.0	4.8	81.2	26.8	84.6	3.8	73.0	3.7
Car parts	39.2	7.6	68.2	54.5	90.0	62.7	79.2	91.8
Prod. for phot.& film etc.	67.9	1.3	89.3	19.3	66.6	28.9	85.5	25.9

Source: Banco do Brasil's Foreign Trade Office (CACEX)

Bi = Intra-industry trade index = 1 - $|X-M|/(X+M)$

X = Brazilian exports in millions of current US dollars

M = Brazilian imports in millions of current US dollars

indexes of no less than 40% and total transactions of over US$ 20 million simultaneously. Of the eight sectors achieving such performance, only two did so on more than one occasion: car parts and products for photography, film, and other goods.

Ever since the start of the eighties, the car-part industry has recorded high intra-industry trade indexes and a growing trade volume. Strictly speaking, this is perhaps the only effective example of intra-industry trade within Mercosur, albeit limited to the operations of just three multinational companies. As Fonseca (1989) has pointed out, the Argentinean and Brazilian subsidiaries of Autolatina, Fiat, and Saab-Scania boast sole responsibility for this feat.

The firms classified under "products for photography, film, and miscellaneous other goods" also presented high intra-industry trade indexes but a less substantial trade volume. This industry encompasses an extremely heterogeneous set of goods and distinct patterns of competition. Items range from scientific instrumentation and medical equipment to toys, and thus these indexes may, for instance, reflect exports of dolls and imports of lenses.

Despite the fragility of current ties between Mercosur economies, the data presented in tables 2 and 3 suggest that the integration project may have a relevant impact not only at the trade expansion level but also at the level of company restructuring. In 1986, in response to a timid set of liberalizing measures, the rhythm of trade level recovery proved

that there is still much trade potential left to be exploited. Furthermore, intra-industry trade indexes showed that, if exchange rate stability were the rule, Brazil and Argentina would enjoy symmetrical opportunities for specialization in important areas of the chemical and metal-mechanical industries and in final consumer goods. Thus, any possible relocation costs that might arise could be offset by gains coming from the other two kinds of integration effects.

4. Industrial Policy and the Common Foreign Tariff

If Mercosur is to realize its full potential, in terms of the above effects, exchange rate stability is not the only prerequisite to be met. Companies must also enjoy similar conditions of competition in all four nations. If this is not the case, strongholds of resistance to integration may take root in those industries where regional differences in profitability are prompted by institutional asymmetries or asymmetries in economic policy.

The effort to harmonize governmental goals, legislation, and public agency conduct calls for an agenda of measures comprising three different timetables. Theoretically, all three of these went into effect on March 26, 1991, when the Treaty of Asunción was signed. The final deadline for the first timetable is December 31, 1994, the date by which trade barriers between the four economies are to have been abolished. The second timetable has no precise end date but will expire upon achievement of all the conditions that define a common market

(i.e., identical policies -- or at least less divergent ones -- in the monetary, fiscal, exchange, trade, industrial, and agricultural areas). Although official discourse claims that this will be accomplished by 1994, that target date is known to be unrealistic. Fulfillment of the third timetable will be an even lengthier process because it entails enforcement of an industrial strategy capable of guaranteeing that Mercosur's productive system keeps pace with international technical progress.

Through December 1994, customs tariffs will suffer linear, across-the-board reductions at six-month intervals. Three matters will merit top-priority treatment in the interim: (a) taxes charged solely on local production -- in the case of Brazil, this would include such workers' compensation funds as PIS and FINSOCIAL (as well as the proposed tax on drafted checks, should the Brazilian Congress go ahead with its current idea of creating this preposterous mechanism); (b) regulation of supplies of agricultural products; and (c) significant disparities between effective protection structures vis-à-vis third markets, which encourage the breaking of rules of origin, via triangular import schemes.

In integration projects, taxes on the value of production and other charges that do not affect imports can easily discourage local industry since calculations quickly disclose the ensuing bias in favor of goods produced in other nations within the project's economic community. When the government is unable to abolish this form of discrimination directly, simply by eliminating such taxes, countervailing duties must be imposed in

order to forestall legitimate resistance to integration. However, enforcing this alternative, even transitorily, is not a simple matter since it exposes an apparent flaw in the integration project. In the case of Mercosur, a sensible solution would be to conduct a complete, precise survey of such taxes within the four member nations and to negotiate their effective revocation by 1994.

Due to its singular characteristics -- seasonal variations and the possibilities of crop failure or overproduction -- the agricultural sector does not fit readily into automatic liberalization schemes. To keep these uncertainties from thwarting progress toward integration in other areas, it is advisable to separate agricultural sector talks by setting up a forum charged with regulating the regional supply of agricultural products. In its initial years of operation, this forum would merely be a coordinating and consultancy mechanism bringing together the four nations' agricultural ministers. Each semester, forecasts for regional production and supply would be evaluated and decisions made on any necessary adjustments in price policies, subsidies, intra-regional trade, and trade with third markets. As was the case in Europe, the region's agricultural policies would gradually be unified through these coordination and consultation activities.

According to the guidelines set out in the Treaty of Asunción, Mercosur will adopt a common foreign tariff by 1994. But the history of other integration projects and the recent evolution of Brazilian trade policy suggest it is most unlikely

this goal will be met. Since 1987, customs tariff reform has been the topic of talks between the government and private business in Brazil. Under the Collor Administration, a timetable has been defined for gradually reducing tariff rates through 1994. This means it will have taken nearly eight years to achieve what may be only a partial transition from one trade regime to another.

Indeed, the tariff structure that will go into effect in 1994 is only a first step toward a new and as yet incomplete structure. In the first place, no guidelines have yet been defined for determining further changes in the structure and, second, as is, it contains distortions that will most likely demand correction prior to 1994.

Table 4 shows the levels of effective protection foreseen for 1994, according to Brazilian government calculations (non-tariff taxes or subsidies have not been taken into account). Of the sixty-four total sectors, seven will be unprotected (*) and two will have protection levels of over 30%, that is, the car industry (62.5%) and radio, TV, and sound equipment (36%). These distortions may be prevented from provoking cries for changes in custom tariffs if they are offset by other taxes, subsidies, or variations in the real exchange rate.

To gain an idea of the exact dimension of the effort needed to establish a common foreign tariff within Mercosur, one would need to compare the effective protection structures existing in

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(*) The unprotected sectors are: mining of non-metallic minerals, extraction of crude and natural gas, coal, cement, petroleum refining, pulp, and wheat milling.

the four member nations. Since no information is available on effective protection, I have used nominal indexes.(*)

Tables 5 and 6, which show average and maximum import duties and the dispersion of nominal protection levels, provide initial subsidies for this question. As can be noted, current tariff structures (**) are a strong incentive to unfair trade practices in view of the profits to be made through triangular import schemes. In the eighty-seven chapters of the nomenclature, differences of more than ten percentage points can be found between average rates for the four nations within one same chapter.

Therefore, harmonization of import policies will affect almost all sectors of these economies. Since it is impracticable to achieve harmonization in one single round of talks, an agenda of priorities must be defined, stipulating which goals are to be met by 1994 and which can be assigned longer deadlines. Tables 7 and 8 present data essential to these definitions.

(*) Nominal protection indexes should be interpreted with caution, above all when referred to the averages for nomenclature chapters, since these chapters often encompass goods from various industries. In some cases, the information may be completely distorted. In Brazil, for example, the average tariff rate for chapter 87, which includes cars, tractors, bicycles, and other vehicles, will be 24.2% in 1994 while effective protection of the car industry will be 62.5%, as indicated earlier.

(**) In the case of Brazil, the tariffs used are those foreseen for 1994.

Table 4

Levels of Effective Protection Foreseen for Brazil in 1994

Level of Protection	No. of Sectors
Negative	7
0 to 10%	10
10 to 20%	17
20 to 30%	28
Over 30%	2

Source: Brazil, Ministry of the Economy, Coordenadoria Técnica de Tarifas (CTT)

Table 5

Customs Tariffs in Mercosur Nations

Country	Average	Maximum
Argentina	9.6	35.0
Brazil	14.2	40.0
Paraguay	16.0	72.0
Uruguay	21.5	30.0

Source: CTT

Table 6

Mercosur: Dispersion of Nominal Protection Levels

Degree of Dispersion	No. of Chapters
0 to 10	8
10 to 20	62
20 to 30	20
Over 30	5

Source: CTT

Degree of dispersion:
Difference between the maximum and minimum values of average duties, by chapter of the customs nomenclature, in effect among Mercosur nations.

Table 7 shows that some disparities are devoid of any economic significance or are confined to one single nation and can thus be easily corrected. An example of the first kind of disparity is the aircraft industry, which in this region exists only in Brazil, although the highest tariff rates are charged by Paraguay and Uruguay. The textile industry illustrates the second situation: levels of effective protection in Argentina, Brazil, and Uruguay are apparently similar when one looks at duties on cotton, synthetic fibers, fabrics, and wearing apparel. However, in Paraguay the cotton fabric industry can be considered unprotected since the tariff on basic inputs is higher than that on the final product, while wearing apparel is overprotected.

Table 8 reveals something else that may facilitate talks considerably: the similarities between Mercosur nations' structures of foreign trade with the rest of the world. All four Mercosur economies are net importers of energy, chemical, mechanical, electric, and electronic products and net exporters of agricultural/food, textile, and leather goods.

We can thus conclude that the list of priority items in implementation of a common foreign tariff is in fact quite short; it will consist basically of chemical products, capital goods, and mechanical and electro-electronic components, since these not only are relevant items in the four nations' import structures but also display technical characteristics that hamper strict application of rules of origin. As a way of streamlining the agenda for the talks and of lending credibility to the

Table 7

Mercosur: Average Import Duties

Chapter	Argent.	Brazil	Parag.	Urug.
Live animals	0.0	0.0	11.6	22.3
Meat	1.1	10.0	35.5	25.4
Fish & shellfish	0.0	9.4	10.1	24.4
Milk & dairy prod.	0.0	19.4	31.2	23.3
Grains	0.0	9.6	11.2	14.8
Milling	0.0	10.4	14.6	28.4
Seeds	0.0	8.1	11.7	16.0
Misc. foodstuffs	3.3	20.0	13.1	25.9
Beverages & vinegar	11.3	19.7	26.7	26.8
Cotton	14.7	12.5	24.8	25.5
Synthetic fibers	20.1	19.3	13.3	22.7
Fabrics	22.0	20.0	20.2	28.6
Wearing apparel	22.0	20.0	34.9	29.8
Hides & leather	11.0	5.0	41.0	10.0
Footwear	22.0	20.0	34.7	26.7
Boilers & machinery	14.9	19.6	9.9	21.4
Electric machines	10.8	19.9	15.9	22.3
Rail vehicles	17.6	20.0	0.6	13.6
Cars & tractors	15.1	27.2	12.4	24.2
Aircraft	2.0	5.7	15.5	12.2
Inorg.chem.prod.	5.2	4.6	3.1	13.5
Organic chem.prod.	2.4	12.2	3.0	12.6
Pnarmaceutical prod.	3.1	12.6	8.9	19.8
Nat. & chem. fertil.	3.2	3.7	0.0	22.5
Misc. chemical prod.	4.0	18.0	4.7	21.1
Pulp	0.0	0.0	4.4	16.4
Paper & cardboard	8.6	10.5	19.5	23.9

Source: CTT

Table 8

Mercosur Members' Trade Balances with Rest of World: 1986/1988

(Percentage over transactions in each sector, three-year ave.)

Sector	Argent.	Brazil	Parag.	Urug.
Energy	(1.5)	(10.3)	(11.4)	(6.4)
Agric./food	42.8	19.5	24.5	25.5
Textiles & leather prod.	5.7	5.8	1.0	32.7
Wood, paper, & others	(0.2)	2.7	0.2	(0.5)
Chemical products	(8.2)	(3.0)	(6.1)	(9.8)
Steel	1.6	9.7	(1.1)	(0.4)
Non-ferrous metals	1.2	2.3	(0.1)	(0.1)
Mechanics	(7.3)	(1.9)	(8.8)	(5.5)
Motor vehicles	(1.5)	3.9	(5.2)	(1.9)
Electric material	(1.9)	(1.2)	(2.7)	(0.9)
Electronics	(6.1)	(1.7)	(12.7)	(5.0)

Source: Aladi

integration program, the list could also include any merchandise whose tariff harmonization would be simple.

The remaining customs tariffs can be harmonized over time, as economic policies gradually converge. In the agricultural sector, the ministerial coordination and consultancy forum would manage imports over the next few years. A common foreign tariff would come into being gradually, in response to the unification of agricultural policies. In the case of products like cars and other durable consumer goods, any triangular import schemes could easily be discouraged by applying rules of origin. Lastly, in industries like pulp, where tariffs are null in Argentina and Brazil because production is competitive, decreased protection in Paraguay and Uruguay can await the advent of a common industrial policy in the region.

Negotiations concerning a common foreign tariff would be simplified substantially if Mercosur adopted an industrial strategy along the lines of that announced by the EEC in November 1990 in the document entitled "Industrial Policy in an Open and Competitive Environment." Since Brazilian industry would be the main reference point for the strategy to be drawn up, its government would need to put forth a special effort toward that end.

As in the European case, the long-term goals of this strategy would be to guarantee the international competitiveness of Mercosur's productive system and to avert systematic imbalances in intra-regional economic relations, against a

backdrop of growth, stable prices, and improved income distribution. The conditions required to achieve this would be similar to those employed by the EEC and other developed nations: public investment in education, science, and technology; use of the state's buying power; and reliance on a finance system able to offer long-term credit. Theoretically, all of this is contained in the Treaty of Asunción. It only needs to be enforced.

5. Conclusion

Despite the obstacles to be overcome, Mercosur is a viable project. The potential synergy of the participating economies should allow for the formation of a community open to international competition and capable of incorporating contemporary patterns of welfare.

As in all other integration experiences, the governments of Mercosur nations share a non-transferable duty: they must build the institutional frame of a new market. This will depend on a lengthy process of negotiations whose logic is not one of mercantile bargaining nor one of imperialist pressure but one of cooperation within the venturesome political exercise of shared national sovereignty. As I have shown in this paper, such an enterprise can be developed gradually, over the course of many years, as long as its intermediary goals are realistically defined -- but thus far this has not been the road taken by Mercosur.

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