Central American Report

Secretaría de Integración Económica Centroamericana
SIECA

2004-2006

Integration and Regional Programs Department
Institute for the Integration of Latin America and the Caribbean - INTAL

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ABBREVIATIONS & ACRONYMS

AAGR	Average Annual Growth Rate
ASEAN	Association of Southeast Asian Nations
ATC	Agreement on Textiles & Clothing
AV	Added Value
BCH	*Banco Central de Honduras*
BCN	Banco Central de Nicaragua
c.a.	cumulative annual
CABEI	Central American Bank for Economic Integration
CACM	Central American Common Market
CARHCO	Central American Retail Share Company
CAUCA	Central American Uniform Customs Code *Código Aduanero Uniforme Centroamericano*
CBERA	Caribbean Basin Economic Recovery Act
CBI	Caribbean Basin Initiative
CCAD	Central American Commission for Environment & Development *Comité Ejecutivo de Integración Económica*
CEIE	Executive Committee for Economic Integration *Comité Ejecutivo de Integración Económica*
CET	Common External Tariff
CINDE	Costa Rican Coalition for Development Initiatives *Coalición Costarricense de Iniciativas para el Desarrollo*
CMC	Meso-American Council for Competitiveness *Consejo Mesoamericano de Competitividad*
CNZF	Nicaragua National Free Trade Zone Commission *Comisión Nacional de Zonas Francas de Nicaragua*
COEXPORT	El Salvador Exporters Corporation *Corporación de Exportadores de El Salvador*
COMIECO	Council of Ministers for Central American Integration *Consejo de Ministros de la Integración Centroamericana*
COMITRAN	Sectoral Council of Transport Ministers *Consejo Sectorial de Ministros de Transporte*
COMTELCA	Central America Regional Technical Telecommunications Commission *Comisión Técnica Regional de Telecomunicaciones de Centro América*
CU	Customs Union
DCs	Developing Countries
DR-CAFTA	Central America-Dominican Republic-United States Free Trade Agreement

EAP	Economically Active Population
ECLAC	Economic Commission for Latin America & the Caribbean
EU	European Union
FAUCA	Central American Single Customs Form
	Factura Única Centroamericana
FDI	Foreign Direct Investment
FINDE	Nicaraguan Development Institute Fund
	Fondo del Instituto Nicaragüense de Desarrollo
FTA	Free Trade Agreement
FTA	Free Trade Area
FTAA	Free Trade Area of the Americas
GATT	General Agreement on Tariffs &Trade
GDP	Gross domestic product
GE CAPITAL	General Electric Capital Corporation
GSP	Generalized System of Preferences
HDI	Human Development Index
HIID	Harvard Institute for International Development
HIPC	Highly Indebted Poor Countries
HS	Harmonized System
HSBC	HSBC Banking Group
HTS	Harmonized Tariff Schedule
IDB	Inter-American Development Bank
IMF	International Monetary Fund
INCAE	Central American Institute of Business Administration
	Instituto Centroamericano de Administración de Empresas
INT/ITD	Integration, Trade & Hemispheric Issues Division
	División de Integración, Comercio y Asuntos Hemisféricos
INTAL	Institute for the Integration of Latin America and the Caribbean
Invest in Guatemala	Guatemala Investment Promotion Agency
	Agencia de Promoción de Inversión en Guatemala
IOE	International Office of Epizootics
IPPC	International Plant Protection Convention
MCC	Millennium Challenge Corporation
MDRI	Multilateral Debt Relief Initiative
MFN	Most Favored Nation
MSMEs	Micro, Small & Medium Enterprises
NAFTA	North American Free Trade Agreement
NPV	Net Present Value
OAS	Organization of American States

OECD	Organisation for Economic Cooperation & Development
p.a.	per annum
p.p.	percentage points
PPP	Puebla Panama Plan
PROESA	Promoting Investment in El Salvador
	Promoviendo Inversión en El Salvador
PROEXPORT	Colombia Export Promotion Agency
	Agencia de Promoción de Exportaciones de Colombia
ProNicaragua	Nicaraguan Investment Promotion Agency
	Agencia de Promoción de Exportaciones de Nicaragua
REER	Real Equilibrium Exchange Rate
S&P	Standard & Poor's
SICA	Central American Integration System
	Sistema de Integración Centroamericana
SIECA	Secretariat for Central American Economic Integration
	Secretaría de Integración Económica Centroamericana
SITC	Standard International Trade Classification
SMEs	Square Meter Equivalents
TACA	Central American Air Transport
	Transportes Aéreos Centroamericanos
TPL	Tariff Preference Level
UN Comtrade	United Nations Commodity Trade Statistics Database
UNCTAD	United Nations Conference on Trade & Development
UNDP	United Nations Development Programme
USAID	United States Agency for International Development
USITC	United States International Trade Commission
VESTEX	Guatemalan Apparel & Textile Commission
WB	World Bank
WDI	World Development Indicators
WTO	World Trade Organization
YOY	year-on-year

Contents

FOREWORD

The Subregional Integration Reports series represents an effort by the Institute for the Integration of Latin America and the Caribbean (INTAL) to promote knowledge and circulate information about the integration process currently underway in Latin America and the Caribbean.

The Central American Common Market (CACM) is one of the region's most salient experiences. This subbloc comprises Costa Rica, El Salvador, Guatemala, Honduras and Nicaragua, all signatories of the 1960 General Treaty on Central American Economic Integration.

In Report N° 3, INTAL aims to provide an overview of the evolution and principal developments in the Central American integration process, addressing a broad readership including government officials, academics, civil society and the private sector. The Report is also published in English with the express aim of reaching a still wider readership.

In general terms Report N° 3 covers the period 2004-2006. The coordination and editing of the final draft were the responsibility of Ricardo Carciofi, INTAL Director, and Jaime Granados, a Trade Specialist from the Integration, Trade and Hemispheric Issues Division of the Integration and Regional Programs Department (INT/ITD) of the Inter-American Development Bank (IDB).

The chapters of the document were written by the following people from INT/ITD and INTAL: Chapter I by Romina Gayá and Alejandro Ramos, Chapter II by Ziga Vodusek and Carolina Mary Rojas Hayes, Chapter III by Jaime Granados and Daniel Vázquez, and Chapters IV and V by Jaime Granados.

Readers are invited to send their comments and/or suggestions on how to improve the scope and focus of future publications in order to help us continue to live up to the expectations awoken by previous reports.

Contents

INTRODUCTION

The present Report aims to provide an overview of the current state of integration in Central America (Costa Rica, El Salvador, Guatemala, Honduras and Nicaragua). It focuses particularly on trade and economic issues, but also highlights the importance of other functional cooperation issues, in particular, the Plan Puebla Panama (PPP). It does not deal with political or social integration.

Chapter I provides an overview of the international context facing the region,[*] its macroeconomic position, the main features of economic policy in CACM countries, the state of play regarding incomes and employment, and the main economic challenges Central America faces in order to make the most of the processes of economic integration it supports.

Chapter II looks at the evolution, composition, destination and origin of trade and investment in the region. It takes into account the differences in quantitative analysis when including or excluding trade generated in the context of special regimes (duty-free zones and inward processing regimes), which for practical purposes are here referred to as *maquila*s.

Chapter III focuses on the current state of formal integration, above all on the advances in the Free Trade Areas (FTAs), Customs Union (CU) and the Puebla Panama Plan (PPP), as well as the new integration paradigms and the major challenges ahead.

Chapter IV concentrates on issues in the Agreement of Central America-Dominican Republic-United States Free Trade Agreement (DR-CAFTA), focusing on the difficulties involved in its approval and implementation, the set of issues surrounding complementary agendas, the first visible effects of the Agreement, and its potential impact on Central American integration.

Chapter V provides a summary of the main issues and major challenges facing Central American countries in stepping up integration, as well as other factors with a significant impact on the nature and intensity of integration, such as the upcoming negotiations with the European Union (EU).

As mentioned in the foreword, this Report takes 2004-2006 as its period of reference. The bulk of the information in Chapter I -a macroeconomic overview- runs up to 2006, while Chapter II -an overview of trade and investment- is based on statistics for 2003-2005 and, data permitting, 2006. The remaining chapters explore some of the events in January 2007.

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* Although in IDB/INTAL terminology Central America is officially a "subregion", it is also here referred to as a "region".

Contents

EXECUTIVE SUMMARY

In 2004-2006, Central America made significant efforts to complete its free trade area (FTA), further its Customs Union (CU) and launch the Central America-Dominican Republic-United States Free Trade Agreement (DR-CAFTA). There have been several breakthroughs on the road to economic union, but the process is still only at the halfway stage. The subregion's political forces are in agreement over the need to intensify the integration dynamic and move it forward. Yet, in the course of this work, significant limitations have emerged.

The global economic climate has been relatively mild over the period. Exports have been dynamic, but terms of trade have steadily worsened. Thus, despite the growing importance of remittances, the current account deficit remains high. Foreign investment has had a positive impact, but Central America remains vulnerable to the potential slowing of growth in its main trading partners (particularly the United States), rising international interest rates and high oil prices. Competition from Asia in the export markets raises questions over the sustainability of current trade flows.

The FTA is virtually complete. Nevertheless, removal of the few remaining tariff and non-tariff barriers is required, as is the launch of intrabloc trade facilitation initiatives. The regional market may serve as a launchpad for the internationalization of Micro, Small and Medium Enterprises (MSMEs). The work of finalizing CU is very important, but there are very difficult still internal and external challenges to breach. The Common External Tariff (CET) has to be concluded. A framework has to be created that allows free internal circulation. Policies and trade instruments applicable to trade with third countries (free trade agreements) have to be coordinated. The legal framework has to be reinforced and trade negotiations more tightly coordinated.

DR-CAFTA was approved in five of the seven countries and the early benefits are beginning to show. The difficulties in its approval and implementation tested the region's governance and demonstrated the limitations of the political regime and its institutions. Complementary agendas were cause for intense debate. DR-CAFTA has stimulated wider discussion in the region, such as necessary macroeconomic reforms, new sectoral policies, sustainable development and social equity. The adoption of mechanisms to maximize opportunities and minimize sectoral and social vulnerabilities is significant. Their application cannot be deferred by virtue of the Agreement's sensitive commitments being back-end loaded. Generally speaking, DR-CAFTA would seem to have more positive than negative effects on Central America's integration process, although there is always a risk of not obtaining the desired payback.

The negotiation of an Association Agreement between the European Union (EU) and Central America is a window of opportunity for the subregion. The negotiation will be difficult and complex but, if all goes well, it could have a very positive impact on Central American integration. The lessons of the DR-CAFTA negotiation should be capitalized upon on this occasion, particularly the lessons learned from social participation and complementary agenda design.

It will be important in the future to have a broader, more coherent vision of Central American integration. There are at present independent trade, policy and functional cooperation initiatives. Integration is in continuous flux and must be monitored closely to equip it with the appropriate framework of policies, institutions and rules for each step of the way.

The importance of integration is there for all to see. However, there are clearly strong external factors affecting it. The United States and Europe continue to play crucial roles, although new actors like Mexico are becoming increasingly important.

I. MACROECONOMIC OVERVIEW

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During the period 2003-2006 the world economy expanded faster than in previous years. Such dynamism -especially from the United States (US) recovery- fuelled growth in Central American Common Market (CACM) countries via greater demand for exports and soaring remittances. Similarly, high levels of international liquidity translated into increased foreign investment in the subregion, especially in financial capital.

Despite the favorable environment, CACM economies grew more slowly than in the late 1990s and performed more poorly than the rest of Latin America. This relative underperformance can be explained by two unfavorable factors in the external environment. On the one hand, the rise in the international price of raw materials hurt Central America as a net importer of petroleum, foodstuffs and other basic products. This increase worsened the terms of trade, intensified the trade deficit and generated inflationary pressure. Moreover, Central American light manufacturing exports have lost dynamism in the face of competition from China and other Asian countries in their major target market, the United States. The real appreciation against the dollar reinforced this trend.

The recovery phase beginning in 2003 translated into a modest increase in investment, which only accelerated toward 2006. Costa Rica, Nicaragua and El Salvador made efforts towards raising internal saving, destined, in Costa Rica and Nicaragua's case, to improving the balance of net exports, while in El Salvador's case, it has in part been allocated to investment. The opposite was seen in Honduras and Guatemala, where recovery has been fuelled more by external saving, reflected in more intense growth in imports over exports.

In 2003-2006, the bloc's current account deficit remained steady in terms of GDP, although there have been significant changes in its composition compared to previous years. The negative balance of trade in goods rose substantially, as imports expanded faster than exports. Growth in external sales was fundamentally due to the increase in volume, whereas purchases from the rest of the world were dominated by the price effect. The deficit in trade in goods was partially offset by positive variations in the balances of services, income and, mainly, transfers, driven by remittances from emigrants. In the financing of the current account deficit, foreign direct investment (FDI) lost ground against financial capital flows, an influx of which enabled the subregion to accumulate international reserves.

The CACM countries sought to establish fiscal discipline and reduce public deficits, objectives that were threatened by the price rise in commodities and by natural disasters. Despite certain improvements (such as the relief of Honduras and Nicaragua's external debts) the public accounts continued to show a high degree of fragility. Moreover, in a context of financial opening and high dollarization of the subregion's economies, the margin of action of monetary policy in containing inflation was limited, although the vulnerability of financial systems was alleviated to an extent.

A. The International Context

The Global Economic Environment

The world economy expanded steadily in 2003-2006, faster than the average for previous years: 4.8% cumulative annual average (c.a.) in the period as against 3% c.a. in 1990-2002. The acceleration in global trade was even sharper, up 17% c.a. in 2003-2005, almost triple the previous period.

The current expansive phase has been strongly marked by the policies implemented by the US authorities after the end of a period of intense sustained growth in GDP and investment in 2001. Exceptional fiscal and monetary measures prevented the worsening of the crisis in the United States and, through trade and financial channels, stimulated activity in various countries. Low interest rates and abundant liquidity in financial markets, the rising prices of raw materials (due to the vigor of demand and, in some cases, geopolitical uncertainty) and the falling prices of many industrial products (due to increased competition and productivity) transmitted growth and alleviated several countries' external sectors. The upward influence of Chinese demand on the international price of raw materials and the deflationary pressures of its light manufacturing exports should be underlined.

Although the shockwave ended up spreading to Japan and the European Union (EU) in 2005-2006, signs of weakening in US activity appeared over the course of 2006. Progressive rises in the interest rate and an excess of household debt began to cool off real estate activity -one of the mainstays of the recovery- as did high energy prices. This slowed the pace of US growth in the course of the year, with an outlook of further weakening in 2007. The gross domestic product (GDP) expanded to a year-on-year (YOY) rate of close to 3% in the second half, as against 3.6% in the first, whereas the dollar weakened against the backdrop of the United States' acute external imbalance. For its part, China's GDP grew by 10.7%, slightly up on the previous year, but with higher net exports and lower investment due to restrictive policies implemented mid-year. Compared with its role in previous years, China projected itself more as a competitor -albeit a marginal one- than a claimant in the world market.

The CACM in the International Arena

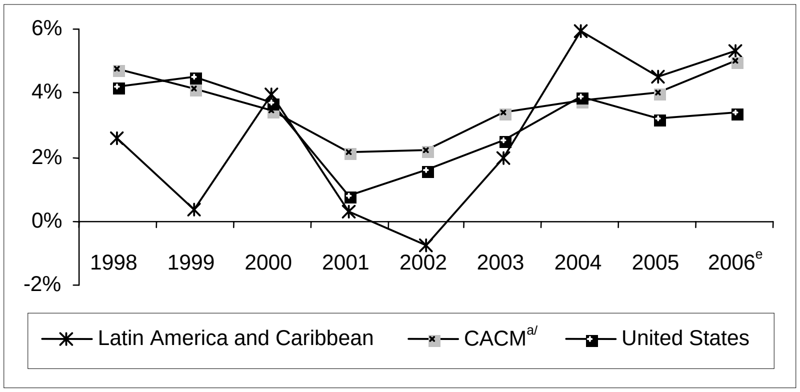
The recovery of US GDP and, to a lesser extent, the growth of the Asian countries, Mexico and the EU stimulated activity in the CACM through increased demand for its main exports and through a remarkable increase in remittances from Central Americans resident overseas (especially in the United States). Increased tourist activity, FDI and financial capital flows (the latter thanks to liquidity and the low interest rates prevailing in international markets) positively impacted the subregion's economies.[1]

Nevertheless, in all CACM countries except Honduras, GDP rose slower than it did in the late 1990s. Compared to the rest of Latin America and other developing countries (DCs), it can be seen that the CACM's recovery driven by the favorable international context has been a modest one. This backwardness is due largely to two factors preventing the bloc from benefiting from the external environmet to the same extent as other Latin American economies like Venezuela, Brazil, Argentina or Chile (Figure 1).

Firstly, the escalation of the international price of raw materials hurt the CACM, as these countries are net importers of petroleum, foodstuffs and other commodities. This rise drove up internal inflation, slowed GDP growth and worsened the terms of trade, contributing to a rise in the deficit of trade in goods. This had an additional fiscal cost for El Salvador and Honduras, which both give subsidies to offset the rises.

[1] Costa Rica, El Salvador (whose debt has been described as an "investment grade since 1997") and Guatemala took advantage of low international interest rates to place debt in external markets under advantageous conditions compared to the past. According to the information available, international bond issues in 2003-2006 reached US$ 0.800, US$ 1.935 and US$ 0.680 billion respectively. Honduras and Nicaragua have restricted access to international capital markets due to their debt reduction programs (ECLAC [2006j] p. 199).

FIGURE 1
CACM, LATIN AMERICA AND CARIBBEAN, AND UNITED STATES: GDP
(1998-2006 - Real YOY Variation)



Notes: [e] Estimates.

[a/] Simple Average Growth Rate for the five countries.

Source: ECLAC and IMF.

Secondly, the subregion was negatively affected by a loss of competitiveness to China and other Asian countries in labor-intensive manufacturing. As will be seen in Chapter II, the textile and clothing industry was among those most hurt by such competition, especially after the Agreement on Textile and Clothing (ATC) of the World Trade Organization (WTO) regulating the application of import quotas expired at the end of 2004. Although the negative impact of China's advance is not as marked as in the case of Mexico or the Dominican Republic, CACM shipments of these products to the United States -its main destination- fell from 2005, Nicaragua being the only country to buck the trend. It is worth highlighting that apparel accounted for more than half the bloc's exports to the United States.

B. The CACM's Macroeconomic Evolution

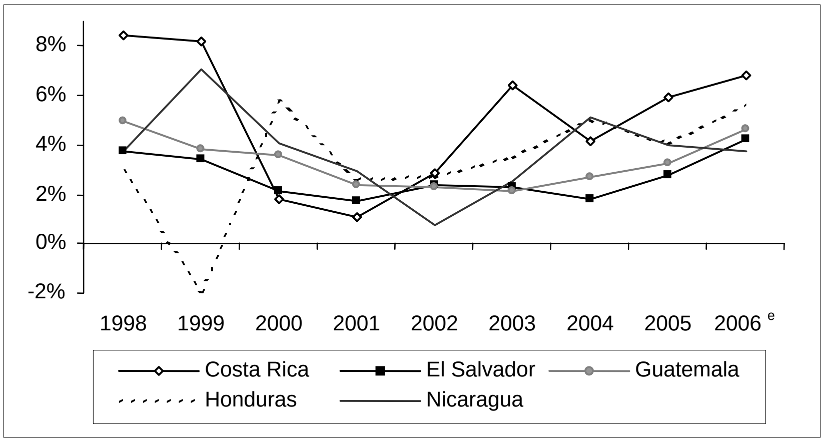
Stylized Facts of the Recent Evolution of the Level of Activity

CACM economies grew by 4% c.a. in 2003-2006.[2] Expansion was slower in the first two years, but speeded up in all the member countries, except Nicaragua, from 2005. The international environment did not affect the subregion's countries uniformly, nor was the behavior of internal demand components the same.

The most dynamic were Costa Rica and Honduras, whose GDPs were up 5.8% and 4.5% c.a. respectively, above the Latin American average. Guatemala and El Salvador had the lowest growth at 3.2% and 2.7% c.a. respectively. The acceleration in the rate of expansion since 2005 is encouraging, though not enough to catch the most dynamic countries in the subregion or the Latin American average (4.4%). In Nicaragua GDP grew by 3.8%, tailing off in 2005-2006 (Figure 2).

[2] Simple average growth rate for the five countries.

FIGURE 2
CACM: GDP BY COUNTRY
(1998-2006 - Real YOY Variation)



Notes: e Estimates.

Source: ECLAC.

Growth Patterns of CACM Economies: Saving, Investment and Net Exports

The phase of contraction in the world economy, which began to be apparent in 1997 with the Asian crisis and bottomed out in 2001 with the minor recession in the US economy, affected CACM countries' activities in two ways. First, from the standpoint of GDP growth, the episode was relatively benign, limited as it was to bringing about a slowing of the economies without any of the five countries recording true shrinkage, unlike several South American economies (Figure 1).

Second, there was a more significant effect on gross fixed capital investment, an essential investment component.[3] This was a variable that fell significantly and whose recovery has been rather slow and less intense than Latin America taken as a whole (Figure 3). If we take the simple average for the five CACM economies' rates of variation in gross domestic real fixed capital investment,[4] it can be seen that the variable expanded on average 9.1% c.a. in 1991-1998 -albeit with wide swings. In 1999-2002 however, growth was only 0.7% and was negative in 2000-2001. In these four years, this variable experienced a fall in the five countries, with notable shrinkage in Nicaragua, Honduras and Guatemala in 2000 (11.1%, 7.6% and 8.8% respectively).

During the recovery phase in 2003-2004, the growth of this investment component was fairly modest, with behavior reminiscent of the cycle of the US economy in which, unlike previous fluctuations, expansion was led by consumption rather than investment (Ramos and Ryd [2005]). In 2005-2006 however, gross fixed capital formation tended to accelerate. According to preliminary figures for 2006, this was the first year this variable was not negative in any of the countries, with average growth for the bloc at 7.9%. But the 5% rate for the four-year period is below the regional Latin American average of around 9%.

A more detailed view by country of the pattern of growth in 2003-2006 emerges on examining the intensity of growth in the different spending components (consumption, investment,[5] exports and imports) as

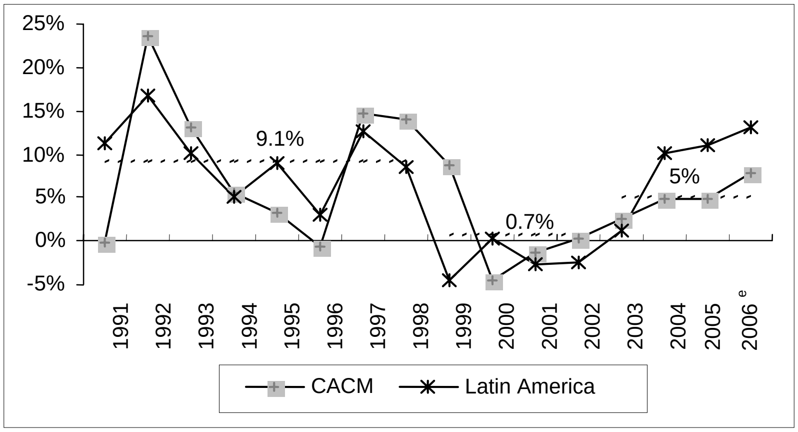
3 Investment (or gross domestic capital formation) consists of gross domestic fixed capital formation and inventory variation.

4 Measured at constant prices in year-2000 US dollars in line with ECLAC methodology. We chose to analyze the rate of variation of investment, not the investment rate itself (investment/GDP) due to problems of scale with the indicator in some CACM countries.

5 Fixed Capital + Inventory Variation.

compared to the expansion of GDP, namely, through the product elasticity exhibited by these aggregates in the accounts at constant prices (Figure 4).[6]

FIGURE 3
CACM AND LATIN AMERICA: GROSS REAL FIXED CAPITAL INVESTMENT GROWTH
(1991-2006 - Real YOY Variation)[a/]



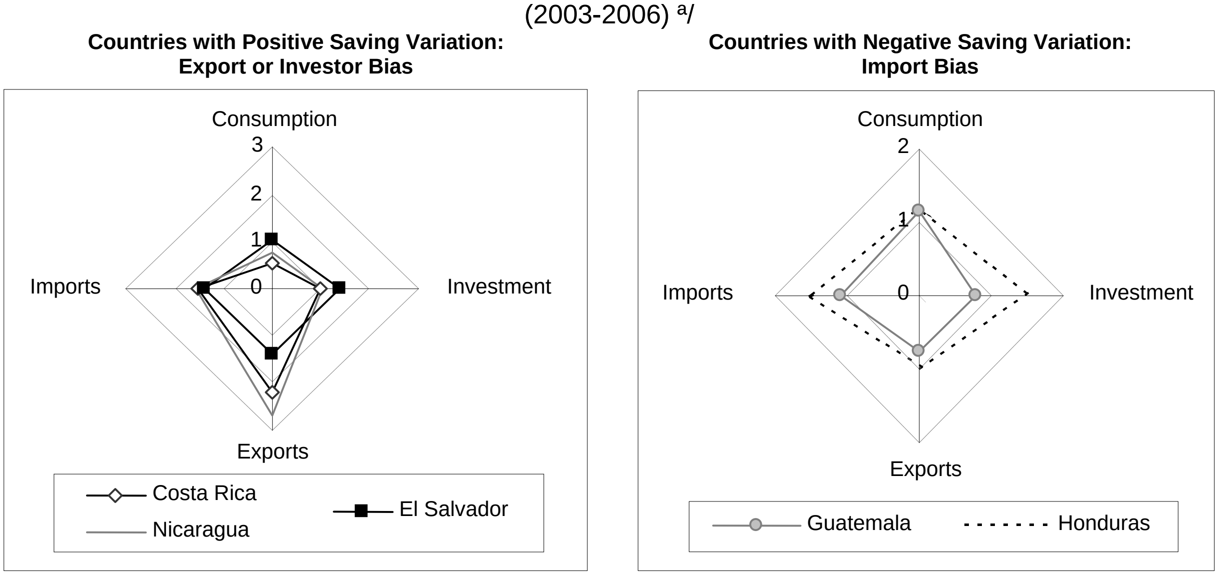
Notes: The horizontal lines denote the average growth rate of investment in the CACM in the respective periods.

[e] Estimates.

[a/] Simple average YOY variations of countries in each aggregate.

Source: Based on ECLAC data.

FIGURE 4
CACM: SPENDING COMPONENT ELASTICITY BY COUNTRY
(2003-2006) [a/]



Notes: Consumption: Private spending and government spending on end consumption.

Investment: Gross Domestic Capital Investment = Gross Domestic Fixed Capital Investment + Inventory Variation.

Exports: includes (maquila and non-maquila) goods and services.

Imports: includes (maquila and non-maquila) goods and services.

[a/] 2006: Estimates.

Source: Based on ECLAC data.

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6 For details, see Annex I, Table A2.

If we consider the intensity of the rise in consumption in relation to GDP, two differentiated types of behavior in the CACM emerge. On the one hand, consumption in Costa Rica, El Salvador and Nicaragua remained relatively tight in terms of variations in GDP, with elasticity below or equal to 1; on the other, elasticity in Guatemala and Honduras was above 1. In the first group recovery then meant a drive toward internal saving, since consumption grew proportionally less than GDP. This was particularly true of Costa Rica and Nicaragua, where the main destination of this surplus was not investment, but improving the balance of net exports -the alternative use of the saving generated. This is clearly expressed in the greater elasticity in exports over imports. In El Salvador, however, the relative restriction of consumption signified a degree of expansion in investment.

However, in the second group -Guatemala and Honduras- the recovery has had an opposite slant, leaning toward consumption rather than internal saving. Imports grow more intensely than exports in these countries, indicating that growth has tended to rely on external saving. In Guatemala, this saving basically financed consumption (investment elasticity there is low), while in Honduras capital formation played a more important part in the recovery, mainly thanks to heavy investment in energy and telecommunications in 2003-2004.

The External Sector

The world economic climate since 2003 has had positive and negative effects for the CACM countries' external sectors, as reflected in the different components of their balances of payments (Table 1).[7] Historically, these countries recorded a current account deficit in their balance of payments, which in 1995-1999, averaged 4.8% of GDP.[8] Net financial capital flows, especially FDI, in this period of reference offset this negative balance, although Nicaragua and Honduras also needed exceptional financing.

TABLE 1
CACM: [a/] EVOLUTION OF THE BALANCE OF PAYMENTS
(1995-2006 - % GDP)

Concept	1995-1999	2000-2002	2003-2006 [b/]
Current Account	-4.8	-5.3	-5
Goods [c/]	-7.2	-10.7	-14.2
Services	-0.4	0.3	0.5
Income	-2.8	-2.7	-2.3
Transfers	5.6	7.8	11.1
Capital and Financial Accounts [d/]	4.1	5.4	6.2
Foreign Direct Investment	2.5	2.4	2.4
Financial Capital [d/]	1.6	3	3.8
Overall Balance	-0.8	-0.4	1.2
Reserves Variation [e/]	-1.4	-0.7	-1.7
Exceptional Financing	2.2	0.6	0.4

Notes: [a/] Average for the five countries.
[b/] 2006: Estimates.
[c/] These data are of domestic balances of payments. They do not tally with those in Chapter 2 due to the levying of imports in FOB value and to the different ways each country handles maquila exports and imports.
[d/] Includes errors and omissions.
[e/] The minus sign indicates a rise in the reserves.
Source: Based on ECLAC data.

[7] The figures in Table 1 do not correspond to a consolidated balance of payments for the CACM, but to the sum of each country's different components.

[8] Since 1980, only El Salvador has recorded a current account surplus, in 1980 and 1986-1988.

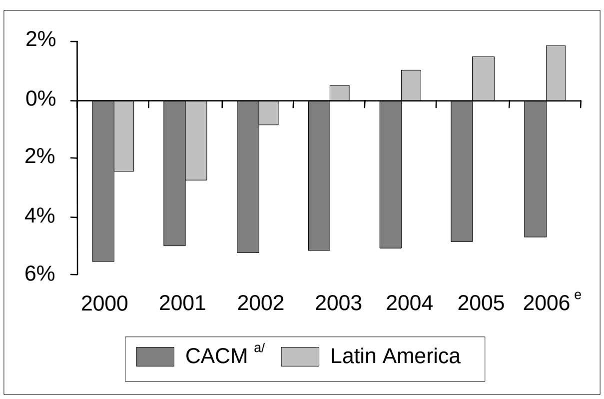
The climate in 2003-2006 led to stabilization of the current account deficit at a high level (5% of GDP), in sharp contrast with the marked improvement in other Latin American countries, especially South America (Figure 5). At the same time, there was a significant modification in the deficit's financing mechanism: the importance of financial capital inflows increased (now representing 3.8% of GDP, more than double 1995-1999), while the importance of FDI held relatively steady at 2.4% of GDP. As a result of the sharp influx of capital, the overall balance[9] went into surplus in 2003, the accumulation of international reserves being reinforced. In this respect the CACM resembles other developing economies both within the region and globally. For its part, the importance of exceptional financing waned, going from 2.2% of GDP in 1995-1999 to just 0.4% in the last four-year period.

The stabilization of the negative current account balance, however, was not without significant modifications in its components. In particular, the goods account deteriorated sharply, with a deficit representing 14.2% of GDP in 2003-2006, 7 percentage points (p.p.) up on the average for 1995-1999. The worsening of the negative balance of trade in goods was offset by positive movements in two areas of the current account: the balance of services and particularly by the high growth in transfers, including remittances from emigrant workers.

- Trade in Goods and Services -

As pointed out above, the CACM's trade deficit in goods and services deepened in 2003-2006, rising from US$ 8,100 million to US$ 13,700 million with a rise of around 19% c.a. During the period, exports of goods and services grew by 10.6% c.a., accelerating in relation to 2000-2002, during which they fell 0.9% on average each year due to the world economic recession. Imports of goods and services, for their part, expanded at a rate of 13.2% each year.

FIGURE 5
CACM AND LATIN AMERICA:
CURRENT ACCOUNT BALANCE
(2000-2006 - % GDP)

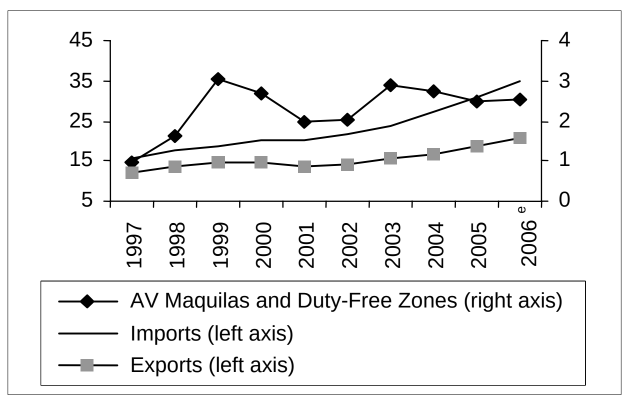


Notes: [e] Estimates.

[a/] Weighted average balance for the five countries.

Source: ECLAC.

FIGURE 6
CACM: [a/] EVOLUTION
OF TRADE IN GOODS
(1995-2006 - US$ billion)



Notes: [e] Estimates.

[a/] Total for the five countries.

Source: ECLAC.

The asymmetrical dynamic of *goods exports and imports* (Figure 6) has raised the deficit, as will be been seen in Chapter II. Indeed, the negative balance of trade in goods expanded to 15.7% of GDP in 2006, as against 12.3% recorded in 2003. The lower growth in CACM exports should be attributed mainly to the

9 The sum of the current account and the capital and financial accounts, including any errors and omissions.

evolution of prices. In terms of exported volume in 2003-2006, the bloc achieved a rate slightly higher than the total for Latin America and the Caribbean -7.9% against 7% for the region as a whole (Figure 7). It is thus the price factor that hurt CACM countries appreciably, whose export sector has made a great effort to increase the volume of supply.

In the case of imports, however, volume growth is slightly lower at 6.4%, as against 9.5% (consistent with levels of activity also below the regional average), while the prices of products imported by the CACM grew more than in Latin America and the Caribbean as a whole. In particular, these countries have been hit by the rising price of raw materials, in first place petroleum. The price of this fuel was multiplied 2.5 times in 2002-2006 and, although its rate of growth slowed over the last year, it stands at record levels.

This unfavorable dynamic in the prices of trade in goods naturally signifies a deterioration of the *terms of trade* to the tune of 2.4% c.a. in 2003-2006.[10] In fact, this decline is a fundamental factor in the deterioration of the balance of goods in the period: at constant prices, the negative balance would have represented 10.7% of GDP, while at current prices it reached 14.2%. In other words, 3.5 p.p. of the average deficit of the four-year period can be attributed, all things being equal, to the negative evolution of the terms of trade.

As pointed out in Central American Report N° 2 (INTAL [2004]), the subregion's countries signed a free trade agreement (FTA) with the United States and the Dominican Republic (DR-CAFTA: Central America-Dominican Republic-United States Free Trade Agreement), which has already come into effect in most signatory countries. This instrument consolidates the preferential access of Central American exports granted to them unilaterally by the United States -through the Caribbean Basin Initiative (CBI) and the Generalized System of Preferences (GSP)- and extends the quotas on certain specific products. Furthermore, it is foreseeable that imports from the United States will grow faster in coming years, as implementation means that 80% of US industrial exports and more than 50% of agricultural products will immediately enter the Central American market tariff-free (USTR [2005]). Duty on the rest of the items is to be eliminated in 10- and 15 year-periods respectively -20 in the case of sensitive products.[11]

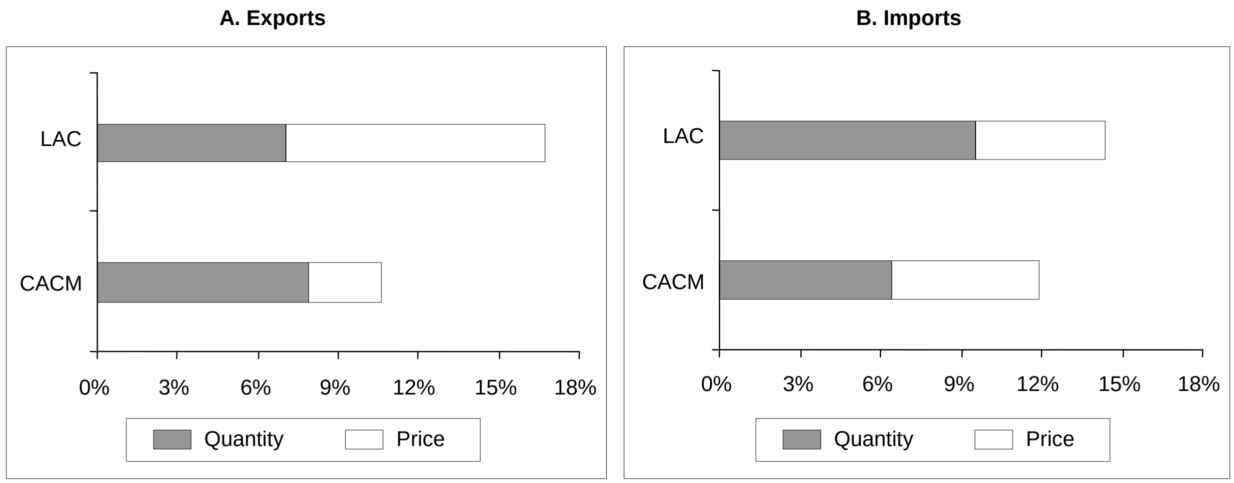
Given the United States' importance as an external supplier to the bloc, it is to be hoped that opening will generate net trade creation: that is, that increased purchases from the United States will translate into new imports rather than substitution of purchases from other sources. This may involve an increase in the CACM's trade imbalance.

Trade in services has been a compensating factor in the deterioration in the balance of goods, with a surplus equivalent to 0.5% of GDP in 2003-2006 for the bloc as a whole. This, however, conceals a highly mixed result, for at country level, Costa Rica alone records a surplus of 5% of GDP in this account, while the other countries have deficits ranging from 0.5% of GDP (El Salvador and Guatemala) to close on 2.5% (Honduras and Nicaragua). Except Guatemala, the other CACM members have shown improvements in this balance in recent years, basically due to the progressive rise in residual net income from *tourism*. This activity has significant potential for the subregion but has, to date, only been consolidated in Costa Rica, whose income in 2006 was around US$ 1.3 billion (5.7% of GDP or 0.9 times net FDI). In the other four countries, tourism is embryonic, with total revenues standing at around US$ 1 billion for that year, but is subject to various promotion policies.

[10] Estimate for the CACM based on ECLAC data: the index of each country is weighted with their total foreign trade.

[11] See Chapter IV for further information on the impact of DR-CAFTA.

FIGURE 7
CACM, AND LATIN AMERICA AND CARIBBEAN:
BREAKDOWN OF TRADE GROWTH BY PRICE AND QUANTITY
(2003-2006 [a/] - Growth Rates [b/])



Notes: [a/] 2006: Estimates.

[b/] Continuous rates: the sum of the rate of growth of quantities and prices is equal to the rate of growth of value.

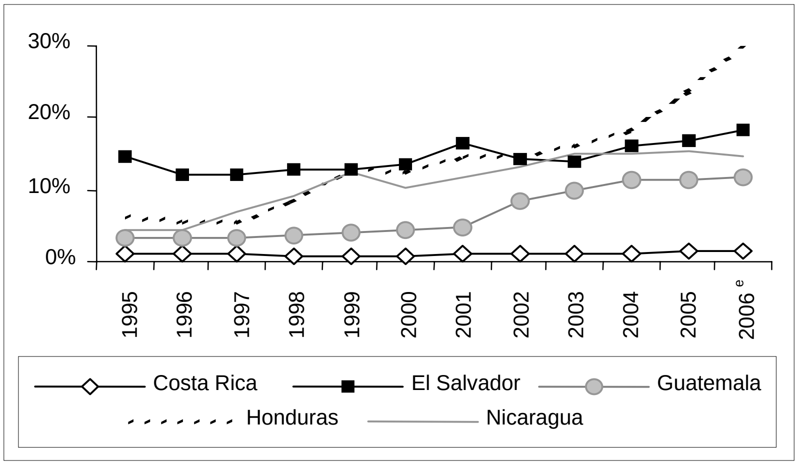
Source: Based on ECLAC data.

- Current Transfers and Income Balances -

One of the most noteworthy aspects of the evolution of CACM countries' balance of payments (excepting Costa Rica) is the high growth and amounts reached by remittances of emigrant workers, the main component in the *current transfers balance* (Figure 8). For the bloc as a whole, the positive balance for this item in 2003-2006 represented 11.1% of GDP, 5.3 p.p. above the level of the second half of the 1990s. In relation to exports and FDI, transfers also reached very significant proportions (Table 2). For the 2003-2006 average, this category in El Salvador, Guatemala and Nicaragua represented 16.4%, 11% and 15% of GDP respectively. The great leap suffered by current transfers in Honduras in the last two years (close on 30% of GDP in 2006) is associated with the wave of emigration caused by the devastation of Hurricane Mitch in 1998. More generally, the phenomenon is linked to the difficult conditions prevailing in these countries' labor markets.

Without a doubt, the flows of remittances contributed significantly to easing the trade deficit and thus stabilizing the negative current account balance. All the same, the cumulative total of the increase in transfers in 2003-2006 (US$ 5.6 billion) only accounted for close to half the loss attributable to the deterioration in the terms of trade in those years. The export effort and the relative weakness of imports (in terms of volume), in tandem with the increase in remittances, account for the fact that the external deficit has not increased and that there has been no macroeconomic adjustment of any magnitude.

FIGURE 8
CACM: BALANCE OF CURRENT TRANSFERS BY COUNTRY
(1995-2006 - % GDP)



Note: [a] Estimates.

Source: Based on ECLAC data.

TABLE 2
CACM AND LATIN AMERICA: RELATIONSHIP OF CURRENT TRANSFERS WITH EXPORTS AND FDI
(2000-2006 - Ratios - Period Average)

Country	Exports [a]		FDI [b]	
	2000-2002	2003-2006 [c]	2000-2002	2003-2006 [c]
Costa Rica	0.03	0.04	0.28	0.30
El Salvador	0.69	0.80	7.37	11.98
Guatemala	0.44	0.92	7.94	17.05
Honduras	0.45	0.69	4.33	6.24
Nicaragua	0.53	0.50	2.44	2.93
CACM [d]	0.43	0.59	4.47	7.70
Latin America [d]	0.07	0.09	0.44	1.18

Notes: [a] Balance of current transfers/goods exports (FOB value).

[b] Balance of current transfers/net FDI inflow.

[c] 2006: Estimates.

[d] Weighted average for the countries.

Source: Based on ECLAC data.

In 2003-2006, the deficit in the CACM's *income balance* averaged 2.3% of GDP. This result implies a small improvement of 0.6 on the balance for 1995-2000, although this behavior was not uniform within the subregion. Costa Rica and Nicaragua displayed significant decreases in the deficit explained respectively by the lower outflows of earnings of the subsidiaries of the foreign enterprises and the reduction in debt services. In Guatemala and Honduras, the improvement in GDP terms was very slender, while in El Salvador the negative balance rose due to government and banks' higher interest payments, and the rise in the outflows of earnings.

Box 1
REMITTANCES AND THE REAL EXCHANGE RATE IN CENTRAL AMERICA

Remittances from Central American residents overseas have grown rapidly in recent years, reinforcing their importance as a source of financing the trade deficit and becoming a key element in improving the real incomes of the poorest families. They therefore have the backing of the authorities.[a/]

Fajnzylber and López [2006] believe that transfers from migrants in El Salvador, Guatemala and Honduras are associated with a drop in poverty and inequality, a phenomenon also seen in Nicaragua. They go on to claim that remittances increase access to education for children and improve access to health services.

Nevertheless, the scope of these transfers in relation to the recipient economies poses certain challenges to economic policy. Undoubtedly, the most significant is to prevent "Dutch disease", namely, preventing the influx of remittances from creating a real appreciation of currencies that will reduce competitiveness in the tradable sector.

There is no consensus over the relationship between migrants' transfers and the appreciation of the real exchange rate in Central America. For example, Izquierdo and Montiel [2006] analyzed the experience of six Central American countries (among them, those of the CACM, excepting Costa Rica) between 1985-2004. They concluded that, despite the sharp rise in remittances during the period, the Real Effective Exchange Rate (REER) was relatively stable. In Honduras and Nicaragua, the impact of remittances on the REER is not significant.

Whatever the case may be, the results obtained for El Salvador and Guatemala are controversial. Remittances would have driven up the REER in El Salvador had fiscal policy not acted in the opposite direction to preserve stability. The Guatemalan situation is more complex, as the conclusions differ according to whether the increase in remittances in 2002-2004 is seen as a temporary or permanent phenomenon. In the latter case, the currency is undervalued in relation to the REER and an appreciation is necessary.

Other studies endorse the hypothesis of "Dutch disease". Fajnzylber and López ([2006] p. 42) argue that in 2000-2003 the increase in remittances in El Salvador, Guatemala and Honduras combined with a fall in the real exchange rate, over and above a possible new lower REER. Along the same lines, a work by ECLAC ([2006c] p. 38) states that the increase in remittances is the main factor behind the real appreciation recorded by Guatemala and Honduras between the early 1990s and mid-2006 (24% and 18% respectively).

Notes: [a/] "Remittances ought not to be classified as official development aid; they are private financial flows arising from family support and are in response to every human being's right to assist the livelihood and welfare of others on an individual basis. This right should be recognized and safeguarded, as should the recipients' right. States should refrain from enacting any legislation or adopting coercive measures that work counter to this right. We must facilitate the sending of remittances, by reducing their costs and guaranteeing access to banking services. We shall strive to provide opportunities that encourage better use of these flows in activities of production and investment that favor the migrants' families and communities of origin". (Ibero-American Community of Nations [2006]).

[b/] The REER enables the goals of internal balance (full employment and equilibrium in the non-tradable goods market) and external balance (current account balance sustainability) to be achieved simultaneously in the long term.

- Financial Capital, FDI and Reserves Variation -

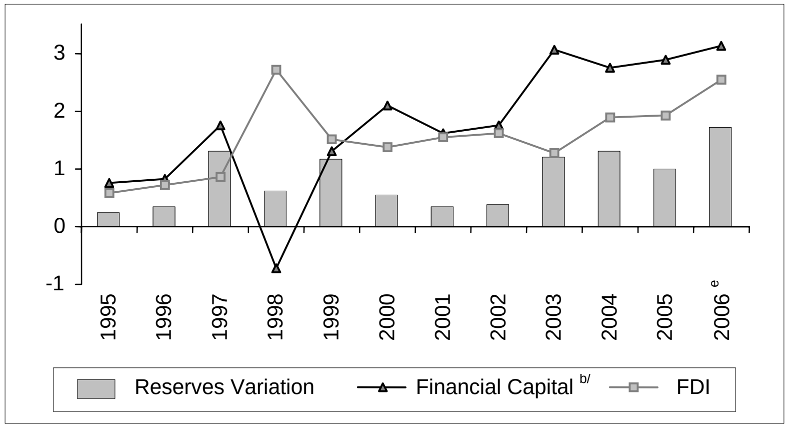
During the period of contraction in 2001-2002 marked by the US recession, CACM countries' annual net inflow of *financial capital*[12] was US$ 1.7 billion, exceeding the shrinkage prompted by the Asian and Russian crises of 1997-1998 (Figure 9). These inflows rose markedly when the world economy began to recover in 2003. It may be estimated that on average US$ 3 billion *per annum* (*p.a.*) came in in 2003-2006, almost double the inflows of financial capital in 2001-2002.

In other words, in this growth phase of the world economy, characterized by low interest rates and high liquidity, CACM countries have secured relatively more investments aimed at taking advantage of differentials in financial yield rather than increasing the economy's productive capacity. The United States change of tack in monetary policy since April 2004 to more restrictive positions did not see a reversal of these flows.[13]

[12] This includes the sum of the net balances of the capital and financial accounts and any errors and omissions, minus FDI.

[13] In Costa Rica, however, there was a minor financial crisis in 2004, triggered by rising US interest rates. This caused capital gains from government securities to fall, affecting several investment funds. The crisis was brought under control by purchase interventions on the part of the central bank.

FIGURE 9
CACM: [a] EVOLUTION OF FINANCIAL FLOWS, FDI AND RESERVES VARIATION
(1995-2006 - Billion of US$)



Notes: [e] Estimates.
[a/] Total for the five countries.
[b/] Capital Account + Account Financial + Errors and Omissions - FDI.
Source: ECLAC.

The rise in *international reserves* (an average of US$ 1.3 billion *p.a.* in 2003-2006) largely reflects the inflow of financial capital, wich conditioned the conduct of exchange and monetary policy. On the one hand, the strong growth in the level of reserves pushed local currencies upward and, on the other, involved strong monetization of this income and the consequent need for the central banks to issue more debt to offset the increase in the money supply.

In the four-year period we have been analyzing, *net FDI* flows[14] equaled 2.4% of the bloc's GDP, the same proportion recorded in 1995-2000, though they now show less a volatile growth trajectory than before, characterized by major privatizations of public services. According to preliminary figures, there was a strong influx of FDI in 2006 (30% up on the previous year). This would attenuate the relative weakness of these flows observed up to 2005, when they grew less than in Latin America and the Caribbean as a whole. The main beneficiaries of the inflows were Costa Rica and Guatemala.

As we shall see in Chapter II, the highest level of FDI in terms of GDP was recorded in Honduras, followed by Nicaragua, Costa Rica and El Salvador. This type of investment remains marginal in Guatemala. According to the information available, El Salvador is the only CACM member whose outward foreign direct investment is at all significant. The internationalization of Salvadorian companies is led by the financial sector, which has gained a presence elsewhere in the subregion in recent years. In this context, El Salvador's investment overseas represented over 45% of the country's received FDI flows in 2006.

- Development Aid and External Debt Relief Initiatives -

In 2003-2005 the CACM countries received on average US$ 1.6 billion in official development assistance.[15] Although their share of total aid to DCs fell from 3.1% in 1996-2000 to 1.9% during this period, assistance to the subregion in *per capita* terms was four times the average received by the other DCs.

[14] The data included in this section correspond to the net FDI of domestic balances of payments.

[15] This includes official concessional-type flows to DCs, with a grant elements of at least 25%. Source: OECD.

Most of the foreign financial assistance within the bloc is focused on Honduras and Nicaragua, particularly within the framework of the initiatives of *Highly Indebted Poor Countries* (HIPC) and the *Multilateral Debt Relief Initiative* (MDRI) (Box 2). Since Nicaragua reached the HIPC ‘decision point' in December 2000, it has received debt relief of US$ 3.762 billion (nominal value) from various multilateral and bilateral creditors, almost 60% of the total reduction foreseen. After meeting the requirements of the ‘completion point' in early 2004, the public external debt/GDP ratio fell from 161% in 2003 to 86% in 2006 (Source: CBN [2006] and ECLAC).

In the case of Honduras, public external debt in 2006 represented 33% of GDP as against 69% in 2003. Most of the reduction materialized after April 2005, when it reached the ‘completion point.' In 2005 and the first eight months of 2006, relief rose to US$ 682 million (Source: ECLAC, CBH [2006b] p. 18, and CBH [2005a] p. 30).

It should be stressed that, at the end of 2006, El Salvador agreed a program with the *Millennium Challenge Corporation*[16] (MCC) to stimulate growth and reduce poverty in the north of the country. Through this package, El Salvador will receive US$ 461 million over five years (Source: MCC).

Box 2
WHAT ARE DEBT RELIEF INITIATIVES?

The HIPC and MDRI Initiative involves programs promoted by the International Monetary Fund (IMF) and the World Bank (WB), whose objective is to help highly indebted poor countries reduce the burden of external debt to sustainable levels and free up resources for the implementation of poverty reduction programs. To do this, they are devising an integral action plan for the international financial community.

To be eligible for the HIPC program a country must have a *per* capita income of below US$ 885, display satisfactory results in executing IMF and WB-supported programs, and demonstrate an unsustainable external debt even after applying traditional relief mechanisms. A debt is considered sustainable when its Net Present Value (NPV) is below or equal to 1.5 times exports of goods and services (mobile average for the three previous years).

The process of the HIPC Initiative consists of two stages. In the first, the beneficiary country establishes a three-year schedule of satisfactory results according to adjustment programs agreed with the IMF and WB, and draws up a preliminary poverty reduction strategy to be implemented to the extent possible. Multilateral creditors grant financing under preferential conditions, the Paris Club reprograms interest payments under traditional mechanisms (up to 67% of the NPV of the eligible debt), and other bilateral and commercial creditors grant treatment better than or equal to that granted by the Paris Club. This stage concludes with the "decision point", at which the IMF and WB Directorate authorizes the country to receive assistance within the framework of the HIPC Initiative, should sustainability of the debt not be achieved through traditional mechanisms. The relief received by a country is set and the conditions for reaching the ‘culmination point' are established.

In the second phase, the country must continue to fulfill the programs' requirements backed by the IMF and WB, and to draw up and meet the poverty reduction strategy for at least one year. The Paris Club and the multilateral, bilateral and commercial creditors reprogram the debt services under more advantageous conditions than the previous stage (interim relief). Lastly, when the country meets all the conditions stipulated in the "decision point", it reaches the "culmination point", at which all the creditors grant the relief necessary to achieve the sustainability of the debt. This reduction is granted without imposing additional conditionalities on economic policy.

Prominent among the requirements for Honduras and Nicaragua to benefit from debt relief envisiond by the HIPC Initiative are fiscal reordering (modification of the taxation model, cuts in public spending and a priority on spending on poverty), certain reforms in financial, provisional, educational and health systems, privatization of public corporations, reduction of employment, adjustment of tariffs for certain public services, and so on and so forth.

A fundamental principle of the HIPC Initiative is that the resources freed up by debt cancellation be redirected to poverty reduction programs. The funds destined for these programs are equivalent to the difference between the contractual service of the debt after traditional relief and the service to be paid after HIPC relief. With this objective in mind, the WB, the IMF and the African Development Fund implemented the MDRI Initiative in 2006, which envisions the irrevocable initial cancellation of the outstanding defrayed debt until the end of 2004 for countries reaching the culmination point.

Source: CBN [2005a] and WB.

[16] The MCC is a US Government program designed to aid some of the world's poorest countries.

C. Economic Policy: Instruments and Results

Fiscal Policy

Central American fiscal policies are currently less procyclical than they were. In this expansive phase, the bloc's countries have sought to establish discipline and reduce the deficit, objectives that have been threatened by the rise in the petroleum price and damage caused by natural disasters. Despite major advances, the public accounts remain fragile, unlike other Latin American economies.

Over the last four years, El Salvador, Guatemala, Honduras and Nicaragua implemented measures that increased the share of tax collection in GDP by a few points. Yet, despite these efforts, the tax burden remains low both in relation to its potential and to other Latin American countries.[17] In Costa Rica an ambitious tax reform project was drawn up yet was declared unconstitutional in 2005. It is currently being redesigned.

CACM countries in 2005 showed lower levels of overall fiscal deficit in terms of GDP than in previous years. Guatemala is the only case where public accounts worsened, as tax revenue fell (just 10.2% of GDP) and expenditure on repairs after natural disasters increased. The primary balance (the fiscal balance excluding interest payments) improved, particularly in Costa Rica, El Salvador and Nicaragua.

CACM countries face an important challenge in the medium term, as DR-CAFTA will generate a serious loss of collection when tariffs on imports from the United States dry up. According to the estimates of the Integration and Regional Programs Department (INT) of the Inter-American Development Bank (IDB), full implementation of the agreement will translate into a decrease in tariff revenue of somewhere between 0.32% and 1.10% of GDP (Nicaragua and Honduras respectively). As a result of its accelerated liberalization program, Costa Rica would suffer the highest short-term losses (0.41% of GDP in the first year). Consequently, these countries will have to make a considerable effort to boost revenue from taxes if they are to avoid increasing the public deficit (Table 3).[18]

TABLE 3
CACM: LOSS OF DR-CAFTA-RELATED TARIFF COLLECTION BY COUNTRY
(% GDP - Base year 2001)

Country	Year 1	Year 5	Year 10
Costa Rica	0.41	0.51	0.62
El Salvador	0.17	0.24	0.38
Guatemala	0.17	0.26	0.39
Honduras	0.36	0.66	1.10
Nicaragua	0.13	0.22	0.32

Source: Barreix, Villela and Roca (2004) cited in Rey de Marulanda [2006].

The picture regarding public debt is very mixed. Guatemala, Costa Rica and El Salvador took advantage of global liquidity to meet their financing needs. The first two privileged the local placement of bonds, while

17 In countries where collection in terms of GDP is so low, development assistance plays a key role in budget support.

18 These estimates only include the impact of the direct effect of loss of tariffs. They do not take into account the indirect effects (falling collection of other taxes based on CIF values plus import tariffs), elasticity (the net result of the probable rise in the imported volume of now cheaper, tax-free goods and the concomitant rise in internal revenue collection), substitution (lower revenues as a result of trade diversion) and induced effects (a change in the collection of all taxes as a result of the new production and consumption structure emerging from the new integration into the international economy). It can be expected that all these effects will bring about a fiscal cost lower than the direct effect. (Barreix, Villela and Roca (2004) cited in Rey de Marulanda [2006].)

the latter did so in international markets. In 2003-2006, the burden in relation of GDP financial obligations remained stable in El Salvador, and fell in Guatemala and Costa Rica.[19] Guatemala's debt is the lowest in the bloc (18% of GDP), while Costa Rica's and El Salvador's stand at around 40%. Honduras and Nicaragua have levels well above the Latin American average and their access to international financial markets has been restricted under the abovementioned debt relief initiatives (Box 2).

Exchange and Monetary Policy [20]

The international context in 2003-2006 was a key factor determining the authorities' monetary and exchange problems. The behavior of the commodities markets -especially petroleum- caused inflation to accelerate, while the rise in workers' remittances and the inflow of financial capital pressured towards a nominal appreciation of currencies, while also enabling international reserves to be accumulated.

It should be borne in mind that financial opening and the high degree of dollarization are structural conditions that reduce the instrumentation the CACM's central banks have at their disposal to reign in the inflation rate. To do this, control of an interest rate or of monetary aggregates is only effective to a point, as these variables are largely determined by factors outside the authorities' control. The dynamic of the interest rates thus correlates closely with that of the rate of US federal funds, though the relative levels are undoubtedly strongly influenced, among other things, by a country's volume of public debt.

Furthermore, there was a loss of functions of domestic currencies in all countries in the bloc. This becomes apparent on looking at the proportion of credit in dollars: in 2003-2006, this indicator averaged 83.4% in Nicaragua, 48% in Costa Rica, 29.6% in Honduras and 25.1% in Guatemala. At the far end of the spectrum is El Salvador, whose authorities opted for total dollarization in 2001, thereby ceasing to exercise control over monetary policy.[21]

The widespread degree of dollarization indicates that, in practice, it is the nominal exchange rate that acts as an anchor on price levels in these economies, a circumstance the central banks have adapted to in various ways. Up to October 2006, Costa Rica had a sliding exchange rate model adjusted periodically on the basis of a known rule. Nicaragua also maintains a system of preannounced devaluation with a daily dollar rate. In Honduras, the Central Bank establishes as a rule a dollar 'floor price' by which it sells foreign currency. Since 2001, only Guatemala has moved toward a nominal anchor model based on inflation targets and a set exchange rate in a market in which the central bank marginally intervenes to ease the volatility of the dollar price without seeking to affect its level.

In 2003-2006, these models underwent important variations. A system of upward sliding exchange-rate bands was established in Costa Rica, with a view to flexibilizing the exchange rate, thus reducing

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[19] Here, the total national debt in 2004-2005 went from 43.1% to 41.1% of GDP. However, interest payments represent a heavy burden estimated at around 7 percentage points of GDP. Furthermore, the implicit nominal rate of the central government's debt in colóns (defined as interest paid/stock) is around 20% *p.a.*, a figure that sets a floor for active interest rates. Part of the debt is "quasifiscal", that is, originating in circumstances where the central bank has been obliged to adopt fiscal functions, for example borrowing overseas at rates not covered by the return on treasury instruments. The adverse disparity in the return on assets and liabilities brought about the decapitalization of the bank, which suffers a self-sustaining borrowing dynamic.

[20] Source: Based on data from CACM central banks.

[21] As early as the 1980s, most of these countries began to experience the growing dollarization of their monetary systems driven by episodic inflation, in some cases linked to civilian confrontations or exchange crises. The persistence of negative current account balances has been a historical factor in the depreciation of currencies caused in fact by the adoption of an exchange rate peg for the price level. More recently, growing trade and financial integration with the United States, in which the flow of remittances is by no means a minor phenomenon, has strengthened the circulation of the dollar. Furthermore, the programmed devaluation models have reinforced dollarization by establishing predictable paths for the dollar price, use of which is becoming ubiquitous even for agents with no dollar income. Dollarization weakens the ability to control money supply, creates risks of exchange troughs in debt structures (which may occur in financial crises), and ends the possibility to gain in exchange competitiveness.

inflationary inertia and the level of dollarization, by revealing to agents the exchange risk concealed by the earlier model. As the exchange rate remained systematically at the bottom of the ranking, the central bank announced in January 2007 that it would not alter the limit. As of 2004, the amount of preannounced devaluation in Nicaragua was reduced (currently 5% *p.a.*) with a view to lowering the inflation floor produced by the exchange policy. In Honduras, there were changes in policy instruments and the devaluation model. In the first case, a monetary policy rate was set in 2005 for short-term open market operations with a view to conveying the authority's intentions to the market. Additionally, the dollar price formation rule governing sales of foreign currencies was modified by incorporating -alongside inflation differentials with trading partners- deviations regarding programmed levels of accumulated reserves. Positive variations thus involve a reduction in the rate of depreciation of the lempira. Guatemala has continued to move forward in implementing its inflation targets model.

The great policy dilemma in the context of abundant inflows of capital and remittances in 2003-2006 has been how the central banks have dosed out the combination of the accumulation of reserves, on the one hand, and a lower level of currency depreciation (or an appreciation) on the other. In 1995-2000, the average nominal devaluation reached 11.9%, 5.3%, 10.1% and 11.1% in Costa Rica, Guatemala, Honduras and Nicaragua; in 2003-2006 these numbers fell to 9.4%, -0.7%, 3.7% and 5.4% respectively. Implicitly or explicitly, it was therefore sought, through the slower pace of nominal devaluation to contain the acceleration of inflation brought on by the rise in commodity prices by applying an exchange rate peg.

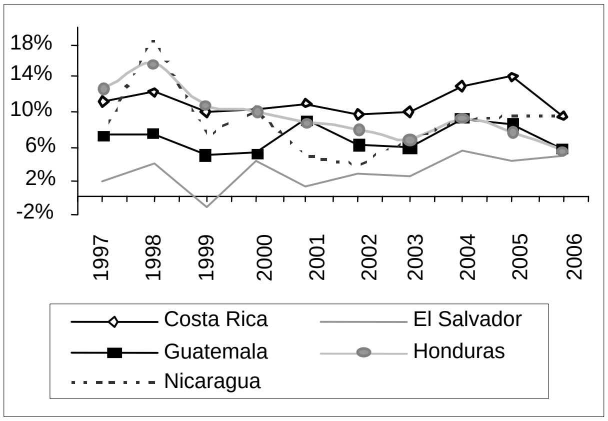
Since the accumulation of reserves and debt payment are also important objectives for several central banks, the issuing institutions made purchase interventions to reduce the financial system's vulnerability. The effects were twofold. First, they checked the appreciation of currencies, which naturally produces the influx of capital and remittances. Second, they expanded the monetary base, a result that had to be offset in all countries by sterilization operations. To this effect, various stabilization instruments were put in place and, more importantly, monetary policy was coordinated with fiscal austerity measures. This type of operation was performed in Costa Rica, Nicaragua and Guatemala throughout 2003-2006. The latter proved to be the country most willing to accept an appreciation of its currency. In almost all the others there was also a certain loss of exchange competitiveness, caused not just by the slower pace of nominal devaluation, but also by accelerating inflation.

Inflation

At one time or another in 2003-2006, all CACM countries showed an acceleration of inflation compared to the previous half decade, in contrast with the average for Latin America and the Caribbean, where prices rose more slowly than in Central America. Over the last four years, Costa Rica recorded the highest inflation (11.6% c.a. as against 10.7% c.a. in 1998-2002), followed by Nicaragua (8.6% c.a.), Guatemala (7.4% c.a.) and Honduras (7.2% c.a.). Only in El Salvador did consumer prices rise less than the Latin American average (4.3% against 6.7% c.a.), although this rate is still high if one bears in mind that the economy is totally dollarized: indeed, it is 1.6 p.p. above average US inflation during this period and almost double the rise in El Salvador's prices during the previous half decade (Figures 10-11). A slowing of the pace of price rises was recorded in most of the countries in 2006.

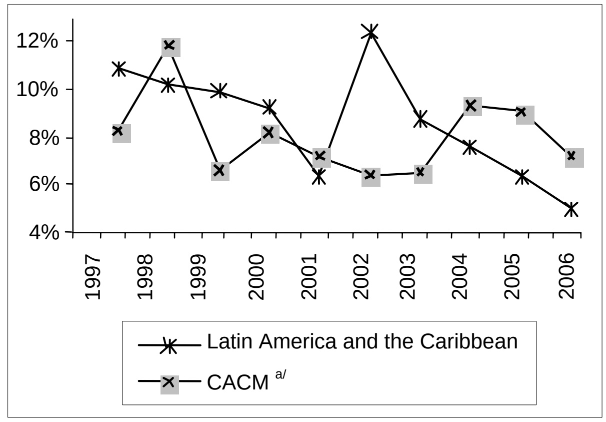
Inflation in the five countries was driven by the rise in the international price of raw materials, particularly petroleum and agricultural products with the greatest impact on the basic basket. Natural disasters and other supply factors (in the agricultural sector) also impacted on price levels. To a large extent, these elements counteracted the efforts of central banks to reach their inflation targets. Significantly, although the lower Salvadorian rates are linked to dollarization of the monetary system, subsidies on transport, electrical energy and some foodstuffs also softened the impact of the price rise in raw materials.

FIGURE 10
CACM:
CONSUMER PRICE INDEX BY COUNTRY
(1997-2006 - YOY % Variation
in December each year)



Source: ECLAC.

FIGURE 11
CACM AND LATIN AMERICA AND THE CARIBBEAN: CONSUMER PRICE INDEX
(1997-2006 - YOY % Variation
in December



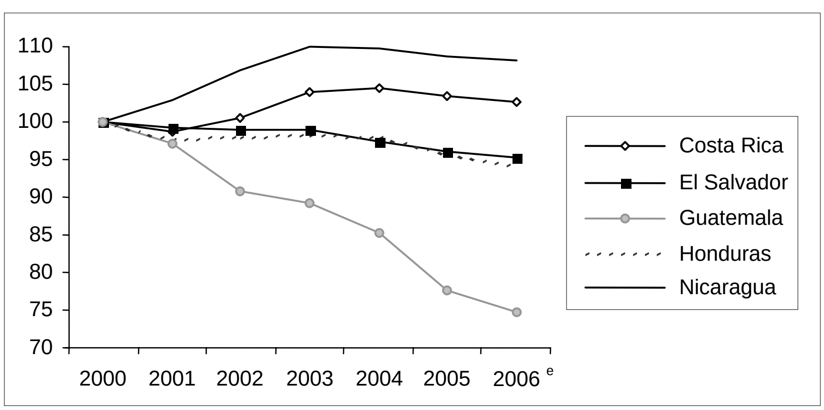
Note: a/ Simple average for the five countries.

Source: ECLAC.

The Real Exchange Rate

The evolution of CACM countries' real exchange rate over the last four years was mixed (Figure 12). Guatemala recorded the greatest loss of competitiveness against both the dollar and the currencies of its main trading partners. The quetzal was 17.5% up on 2002 levels against the US currency, reflecting not only accelerating inflation, but a certain nominal revaluation.

FIGURE 12
CACM: REAL EXCHANGE RATE AGAINST THE US DOLLAR BY COUNTRY
(2000-2006 - Indexes 2000=100)



Notes: The fall (rise) of the index expresses appreciation (depreciation) of the domestic currency.

e Estimates.

Source: Based on ECLAC data.

In the same period, the lempira was also up against the dollar in real terms, although less so than the Guatemalan currency (4%). The inflation differential for El Salvador was also unfavorable, with real appreciation of 3.5% against the United States. In Costa Rica, the application of the sliding nominal exchange rate up to October 2006 enabled the accelerating inflation to be offset, resulting in a degree of real depreciation of the colón (2.1%). It is highly likely that the exchange band model will reverse this trend in the context of capital inflow. In Nicaragua, the córdoba depreciated by 1.3% in real terms.

D. Incomes and Employment

The CACM countries' *per capita* GDP in 2003-2006 rose on average 2.3% c.a. Although this rate was faster than previous years, it is substantially lower than the average increase recorded in Latin America (2.9% c.a.), even when compared to the second half of the 1990s.[22] In expanding more slowly, Central American countries are widening the gap with the rest of the region. At current prices, GDP *per* CACM inhabitant is US$ 2,510, less than half the Latin American average (US$ 5,100).

It must be stressed that evolution in the CACM was extremely mixed. Indeed in 2003-2006, Costa Rica and Honduras's GDP *per* inhabitant showed a clear acceleration compared to the late 1990s, growing in real terms at 3.9% and 2.1% c.a. respectively. In Nicaragua, El Salvador and Guatemala, however, *per capita* GDP growth could not recover the expansion rate of 1995-1999. In Nicaragua, it rose 1.8% c.a., while in El Salvador and Guatemala the gap was more significant, in relation to both the rest of the subregion and to its own performance in the past, with GDP *per* inhabitant only rising 0.9% and 0.6% c.a. respectively in 2003-2006 (Table 4).

These disparities are also seen when measuring the level of GDP *per* capita in dollars. Indeed, in Costa Rica it reaches US$ 5,050, double the average for the subregion. Guatemala and El Salvador are slightly above average at US$ 2,700 and US$ 2,600 respectively, while in Honduras and Nicaragua, the poorest economies, GDP *per* inhabitant does not reach half this value, standing at US$ 1,150-US$ 1,000 respectively (Source: ECLAC).

TABLE 4
CACM: EVOLUTION OF PER CAPITA GDP BY COUNTRY
(Real Annual Cumulative % Variation)

Country	1995-1999	2000-2002	2003-2006 [a/]
Costa Rica	2.8	-0.2	3.9
El Salvador	1.8	0.1	0.9
Guatemala	1.9	0.3	0.6
Honduras	-0.1	1	2.1
Nicaragua	3.2	0.5	1.8

Note: [a/] 2006 Estimates.

Source: ECLAC.

[22] This contrast is even more marked when we compare the CACM with the faster-growing South American countries: the *per* capita GDP of Argentina, Chile, Uruguay and Venezuela rose 6% c.a. on average in 2003-2006 (simple average for the four countries). Growth rates correspond to GDP *per* capita value in dollars at constant prices for 2000. CACM data correspond to the simple average for the five countries. The 2006 data are estimates (Source: ECLAC).

The differences are also seen in other social indicators. According to the Human Development Index (HDI)[23] drawn up by the United Nations Development Programme (UNDP), Costa Rica is the only country above the Latin American average (0.838 and 0.751 respectively). This country's HDI is 17% higher than the CACM average and the lowest levels of welfare are found in Guatemala, Honduras and El Salvador.

Urban unemployment has fallen in all CACM countries in recent years. The (simple) average unemployment rate for the five countries in the bloc was down slightly from 7% in 2003 to 5.6% in 2006.[24] Though this index is low in comparison with many DCs, underemployment and informality remain extremely high and, in some countries, over a third of the economically active population (EAP) have employment difficulties. All the same, one encouraging fact is that registered labor is on the increase, particularly in Nicaragua where formal employment grew 7% c.a. in 2003-2005.

E. Conclusions

The international context in 2003-2006 was fairly kind to CACM economies, though to a lesser extent than other Latin American countries. In this context, Central America improved on certain macroeconomic indicators and accelerated growth compared to the previous three-year period, but showed a lag compared to the rest of the region and to its own performance in the late 1990s.

The outlook for the near future suggests the world context will pose greater challenges for CACM countries. The slowing of global growth -particularly in the United States- could halt the momentum of Central American exports, remittances and FDI flows in a scenario where the oil price remains at record highs.

DR-CAFTA will consolidate trade preferences in the US market, but the competitiveness of the Asian countries in light manufacturing will keep Central American exports on their toes. In addition, a possible upward trend in international interest rates may affect countries with greater need of public and private sector financing. All these elements may aggravate the external imbalance, which has already reached alarming levels. The bloc's countries need to improve on this performance and this will require a combination of policies of productive development, innovation and fiscal reform to stimulate internal saving, while offsetting losses in customs revenue. The drive toward integration and its correlate of benefiting from increased scales, infrastructure development and third market access is certainly a positive element. By itself, however, it is inadequate and needs to be backed up with complementary policies.

[23] HDI consists of indicators for length and health of lifespan (measured according to life expectancy), education (measured by adult literacy rate and combined gross rate of enrollment in primary, secondary and tertiary education) and decent standard of living (measured by GDP *per* capita in dollars). HDI ranges between 0 and 1, 1 being the highest possible. Data for 2004 (UNDP [2006]).

[24] The household survey was not carried out in Guatemala in 2005-2006 and therefore the 2004 level was used. In Nicaragua's case, the latest information available (2005) was used.

Contents

II. AN OVERVIEW OF TRADE AND INVESTMENT

The economic integration of the CACM countries into the international economy has proceeded at a rapid pace since the beginning of the 1990s, as the region embarked on the process of trade liberalization and opening up to foreign investment. The intensification of trade relations can be associated with several developments: unilateral trade liberalization greatly reducing average tariffs, the signing of bilateral and plurilateral free trade agreements and, significantly, trade concessions from the industrialized countries, first among them the United States. At the same time, trade between Central American countries increased rapidly with the progress of economic integration within the CACM. The growth in trade flows led to the increased importance of the external sector in Central America's economies, a phenomenon stimulated even more by waves of maquiladora company and duty-free zone-related trade (henceforth simply 'maquila').

In terms of recent trends, after a period of stagnation in the early 2000s, exports rose from 2003. In 2003-2005, total external sales (including maquila) grew on average 9.5% p.a. Extraregional non-maquila exports (11.3%) and intraregional exports (11.2%) soared in particular, while maquila exports showed signs of a significant but weaker momentum (8.3%). After 2003, the ratio of maquila exports to GDP in the subregion has been falling.

Despite the overall rise in exports, the chronic deficit in the subregion's foreign trade did not decline. Including maquila sector transactions, it reached almost 18% of GDP in 2005. As shown in Chapter 1, an important factor in this was the deterioration in the terms of trade since 2000. Nor have rising exports enabled the downward trend in the subregion's competitiveness as a share of world imports to be reversed.

As stated, intraregional trade flows grew faster in 2003-2005 than total export flows (including maquila). This rate is more than double the 4.5% p.a. increase recorded in these exchanges in 2000-2002. Guatemala was by a long chalk the main originator of this growth, while there was a contraction of these flows in Honduras. Intraregional exports were the most important for El Salvador in 2003-2005, accounting for more than half non-maquila external sales. However, they were the least prominent for Honduras, at around a fifth of the total.

Naturally, the relative expansion of intraregional flows increased the importance of the CACM as a market, making it the main destination of non-maquila exports, slightly ahead of the United States. At the same time, the participation of the EU as an export destination has fallen away sharply: in 2005, it was just half what was in the 1990s.

With DR-CAFTA, which consolidates and expands US market access, and the upcoming negotiations with the EU aiming at establishing a free trade area, the Central American countries have an opportunity to significantly increase their levels of export and competitiveness. However, to achieve this goal will be a serious challenge, both in terms of improving their export strategy in areas not covered by maquila regimes and in maquila transactions.

In fact, the future of maquiladora exports is tinged with uncertainty. On the one hand, the international obligations agreed in the framework of the WTO require the removal of export subsidies after 2009, which would affect the competitiveness of such activities. On the other hand, there is growing competition from Asian countries, in particular China, in the sectors that traditionally operate under these regimes. The recent stagnation and even decline in clothing exports of the isthmus -with the exception of Nicaragua- is a tangible early indicator of this problem.

As integration within the CACM progresses and trade facilitation between the countries continues apace, increased intraregional trade flows can be expected in years to come. In this respect, as we shall argue in

Chapter 3, the establishment of the Customs Union (CU) is cricual, as is tariff and standards harmonization. Similarly, the multilateral application of DR-CAFTA in the context of accumulation rules of origin for goods could contribute to the development of supply chains and links between countries in the subregion.

If compared to the previous three years, FDI flows to Central America rose sharply in 2003-2005. However, if these flows are seen as a percentage of GDP, there emerge stagnation and coefficients below the late 1990s. The countries receiving most FDI were Costa Rica and Honduras. In sectoral terms, services and maquila were the most important receptors. The major source of FDI remains the United States with almost half the total inflows, while the EU countries' share fell sharply to below 15%. Intraregional flows in 2003-2005 were down on 2000-2002 as a proportion of total FDI. El Salvador is the main investor in the subregion where the development of regional Central American enterprises has been notable in recent years.

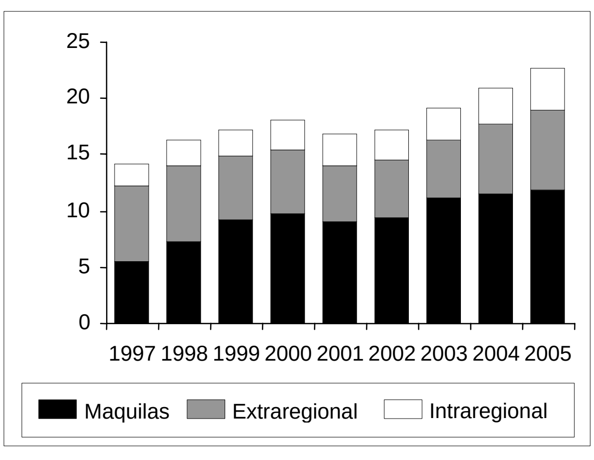
In the rest of this Chapter, we deal first with the evolution of Central American countries' foreign trade in goods with partners from outside the subregion and then, in greater detail, with subregional trade. The presentation and analysis of extraregional trade is analyzed along two lines: on the one hand, with the inclusion of exports under special regimes such as maquiladora enterprises and, on the other, only taking into account exports of the "domestic" economy, sometimes referred to as 'definitive exports.' We go on to give an overview of investment flows to and within the subregion, and lastly, the chapter closes with a brief description of certain investment activities by Central American enterprises.

A. The Evolution of Total Trade

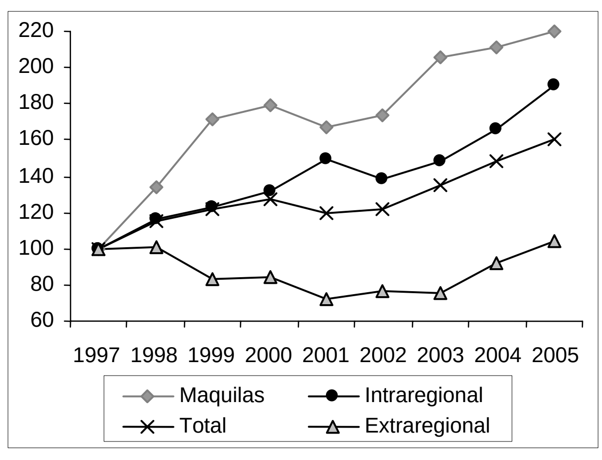
In the late 1990s, maquila-originated exports (including duty-free export zones) had a great impact on the CACM countries' total goods exports. However, as non-maquila exports fell in the same period, growth in total exports was only moderate (Figures 13a and 13b and Table A8).

FIGURE 13
CACM: TOTAL, EXTRA/INTRAREGIONAL AND MAQUILA EXPORTS
(1997-2005)

GRAPH 13.a. (US$ billion)



GRAPH 13.b. (Indexes, 1997 = 100)



Note: Maquila includes duty-free export zones.

Source: Based on data from UN-Comtrade/SITC Rev. 2, Secretariat for Central American Economic Integration (SIECA: *Secretaría de Integración Económica Centroamericana*), the United States International Trade Commission (USITC) and the Central Bank of Costa Rica (CBCR).

In the current decade it is possible to distinguish two periods in the evolution of the export total. First, in 2000-2002, a slight fall in total exports was recorded, affecting both maquila exports and non-maquila extraregional exports, while those to the subregion itself did not fall, even when they shrank in 2002. The recession in the United States, the most important trading partner for the Central American countries, was the most significant factor behind this drop in total exports. Second, in 2003-2005, exports recovered, with all categories recording high growth. Thus extraregional non-maquila exports grew 11.5% p.a. Intraregional exports were up 11.2%, while maquila exports rose more slowly (8.3%). The return of growth in the United States was again the main factor behind this behavior.

Maquila operations, as measured by the sum total of their exports and imports, contributed significantly to Central American trade openness (Table 5). The coefficient of total trade openness now stands at over 70% of GDP, but it should be noted that it has not made any significant progress since 2000. The openness of the economy fell in 2001-2002 as a result of the macroeconomic deceleration affecting all trade flows. In 2003-2005, with the expansion of total exports, the openness indicator rose again, although showing the relative lack of dynamism of maquila-associated trade.

In terms of another competitiveness indicator -namely, penetration in global markets calculated as a country or region's share in world imports- we find that the CACM countries' overall position has been steadily deteriorating in recent years (Figure 14). This involves both exports measured by including maquila and exports of the 'domestic' economy. In the first case, the share fell from 0.31% in 1999 to 0.21% in 2005, and in the second, from 0.17% in 1998 to 0.10% in 2005. Although this deterioration can be attributed to an extent to the impact of the dynamic growth of Chinese and other Asian countries' exports in terms of global exports, it also reflects the relatively low competitiveness of most Central American countries: according to the Global Competitiveness Index (GCI), the CACM's five member countries were on average 81st of 125 countries in 2005; Latin American countries on average came 73rd.[25]

TABLE 5
CACM: TRADE OPENNESS COEFFICIENT [a/]
(1997-2005 - % GDP)

	Average			2000	2001	2002	2003	2004	2005 [b/]
	1997-1999	2000-2002	2003-2005						
Total (Non-Maquila + Maquila)	69.2	69.7	72.5	72.4	68.4	68.3	71.3	73.3	73
Total (Non-Maquila + Maquila AV)	48.7	46.3	48.9	48.1	45.2	45.5	47.1	49.7	49.9
Total (Non-Maquila)	45.2	42.6	45.2	43.5	42.1	42.4	42.9	45.9	46.8
Extraregional	36.9	33.6	36.3	34.4	32.7	33.6	34.3	37.0	37.7
Intraregional	8.3	9.1	8.9	9.1	9.3	8.7	8.6	8.9	9.1
Total (Maquila) [c/]	24	27.1	27.3	28.9	26.3	25.9	28.4	27.4	26.1
Memorandum Item: Maquila Added value	3.5	3.6	3.7	4.6	3.2	3.1	4.2	3.7	3

Notes: [a/] The trade openness coefficient is defined as the ratio of total exports and imports of goods to GDP. GDP for Honduras and Nicaragua may be underestimated and the opening coefficient may as a result be overestimated.

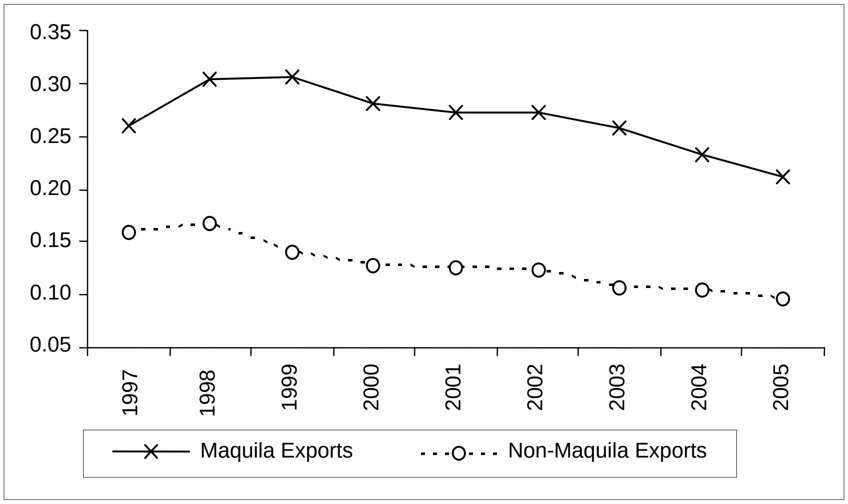
[b/] Preliminary data for 2005.

[C/] Maquila includes duty-free export zones.

Source: Based on data from UN-Comtrade/SITC Rev. 2, SIECA, ECLAC and Central American Central Banks.

[25] Under this classification, Costa Rica occupies 56th place, El Salvador 60th, Guatemala 95th, Nicaragua 96th, and Honduras 97th (World Economic Forum [2005]).

FIGURE 14
CACM'S SHARE OF EXPORTS IN WORLD TRADE
(1997-2005 - % of world Imports)



Notes: The data for Guatemala in maquila exports for 1997-2001 correspond to textile and clothing exports to the United States.

Maquila includes duty-free export zones.

Source: Based on data from UN-Comtrade/SITC Rev. 2, SIECA, USITC and CBCR.

B. Non-Maquila Exports

Analyzing the evolution of exports of the 'domestic' economy in greater detail -in other words, excluding maquila- a sharp rise was seen in 2003-2005 estimated at 11.3% p.a. The rates for 2004 (18.5%) and 2005 (13.9%) had an influence on this result (Table 6). In terms of main trading partners, exports to the United States recovered strongly, even more so those destined for Latin American and, to a lesser extent, Asian countries, which however began from a lower base.

For much of the last decade, intraregional exports grew at rates substantially above extraregional exports. This was true of the latter half of the 1990s -14.2% against 1.6% (Table A12)- and continued in 2000-2002, when intraregional exports recorded positive growth, while extraregional exports fell. In the more recent period (2003-2005), both categories of exports recorded high growth indexes (over 11%) but extraregional sales were the most dynamic factor in this expansion. Thus, on average in 2004-2005, this area accounted for around 70% of growth, while sales in the subregion contributed 30%. The United States was the most dynamic destination in extraregional sales (Table 6).

However, as already pointed out, exports within the subregion were also an extremely important factor if we take a longer period. Indeed, in 2000, 2001 and 2003, it is this outflow that led to the highest contribution to total growth, offsetting the low (or negative) growth indexes for extraregional exports (Table A12).

The trends in export growth outside the maquila regime have brought about changes in the export market share. The proportion of exports destined for the CACM rose sharply early in the current decade, consolidating at around 34% in 2004-2005 -a figure that makes it the most prominent market, slightly ahead of the United States (Figure 15 and Table A12). It is necessary to stress the EU's falling or stagnant share as an export destination and the emergence of Latin America in 2005.

TABLE 6
CACM: NON-MAQUILA EXPORTS
(1995-2005)

Value (US$ million)	Average		2003	2004	2005 [a]	% AAGR [b]	
	1995-1999 [b]	2000-2002 [b]				2000-2002	2003-2005 [a]
Total	*8,067*	*7,957*	*7,954*	*9,429*	*10,739*	*-0.5*	*11.3*
Extraregional	6,123	5,228	5,069	6,189	7,031	-2.4	11.5
United States	2,965	2,581	2,495	3,150	3,567	-2.6	12.4
EU-25	1,834	1,173	1,072	1,279	1,442	-10.2	11.7
Latin America	501	568	615	745	1,144	-1.4	28.1
Asia	263	217	227	235	333	3.5	15.1
Others	560	689	660	779	545	17	-8.3
Intraregional	1,944	2,729	2,885	3,241	3,708	4.5	11.2
Contribution to YOY Variation [c]	**Average**					**Average**	
Total Growth	*8.4*	*-0.5*	*1.5*	*18.5*	*13.9*	*-0.5*	*11.3*
Extraregional	5.2	-1.7	-0.9	14.1	8.9	-1.7	7.4
United States	2.6	-1.2	-0.7	8.2	4.4	-1.2	4
EU-25	1.1	-1.7	0.4	2.6	1.7	-1.7	1.6
Latin America	0.8	-0.1	0.7	1.6	4.2	-0.1	2.2
Asia	0.3	0.1	0	0.1	1	0.1	0.4
Others	0.4	1.2	-1.3	1.5	-2.5	1.2	-0.7
Intraregional	3.1	1.2	2.4	4.5	5	1.2	3.9

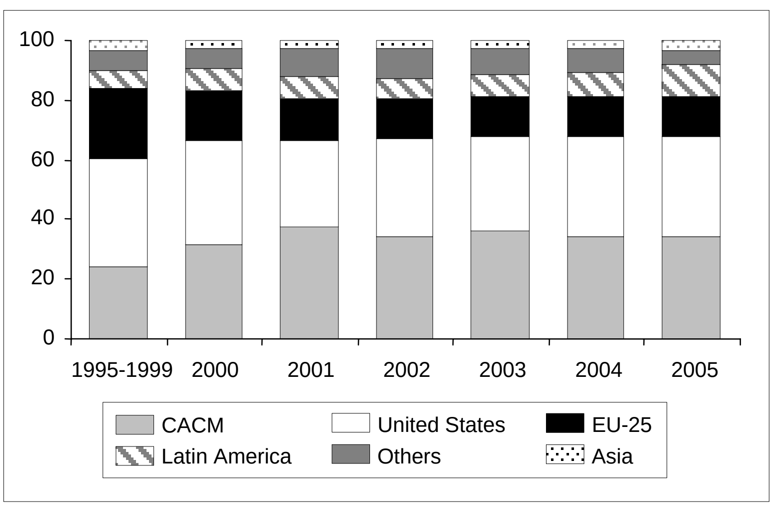
Notes: [a] Preliminary data for 2005.

[b] AAGR: Simple Average Annual Growth Rate.

[c] Contributions to growth are calculated by multiplying the rate of variation of exports to a specific destination by the weight of the destination in the total exported during the relevant year. The sum of these contributions corresponds to the total growth rate. SIECA data have been used for El Salvador (2005) and Guatemala (2005).

Source: Based on data from UN-Comtrade/SITC Rev. 2, SIECA and the CBCR.

FIGURE 15
CACM: NON-MAQUILA EXPORTS BY COUNTRY/REGION OF DESTINATION
(1995-2005 - % of total)

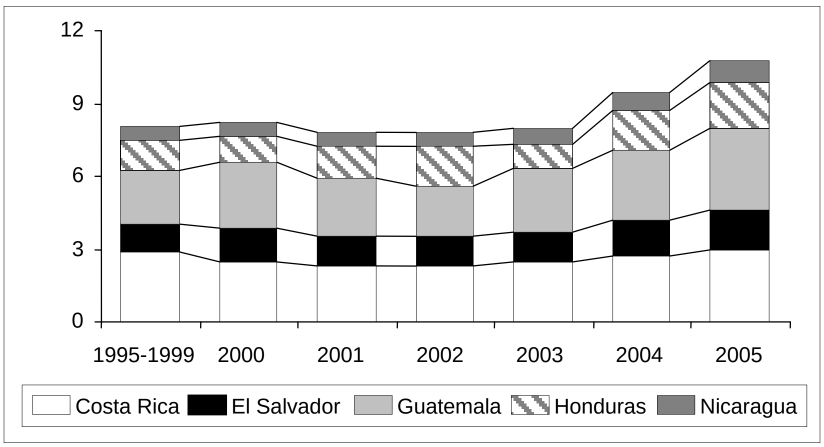


Source: Based on data from UN-Comtrade/SITC Rev. 2, SIECA and the CBCR.

If we look at the countries of origin of non-maquila exports, the highest contributor is Guatemala (Figure 16). Its share was 31% of the total in 2005, 3 p.p. up on the 1995-1999 average. A rise in share was also seen in Honduras, El Salvador and Nicaragua, at the expense of Costa Rica whose market share in non-maquila exports fell by 8 p.p. in 2005 to 28%.

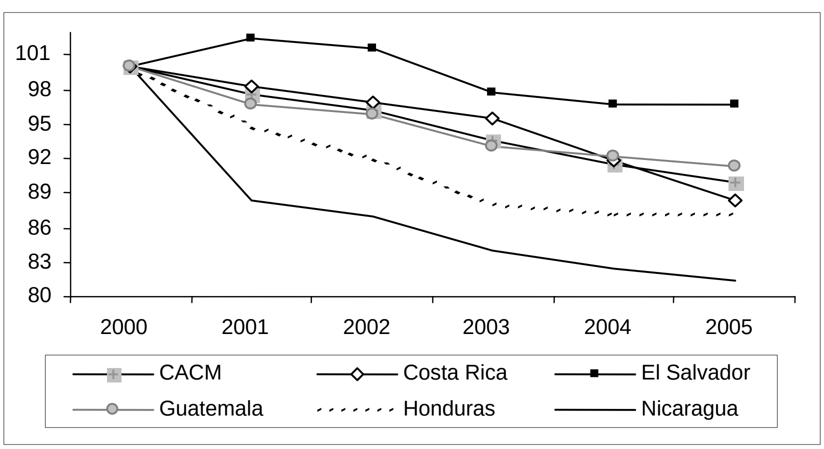
Taken en bloc, the CACM countries' terms of trade have deteriorated steadily since 2000 (Figure 17). This situation is seen in all countries, with the partial exception of El Salvador. It is caused by far more intense growth in import than export prices. For the latter, a comparison of the 2005 level with that of 2000 gives growth of 1.4% (7.1% and 4% for Guatemala and El Salvador respectively), while the respective rate of import prices was 10.7% -20.4% for Nicaragua (see Chapter 1) (ECLAC data).

FIGURE 16
CACM: NON-MAQUILA TOTAL EXPORTS BY COUNTRY OF ORIGIN
(1995-2005 - US$ billion)



Source: Based on data from UN-Comtrade/SITC Rev. 2. SIECA and Central Bank of Costa Rica.

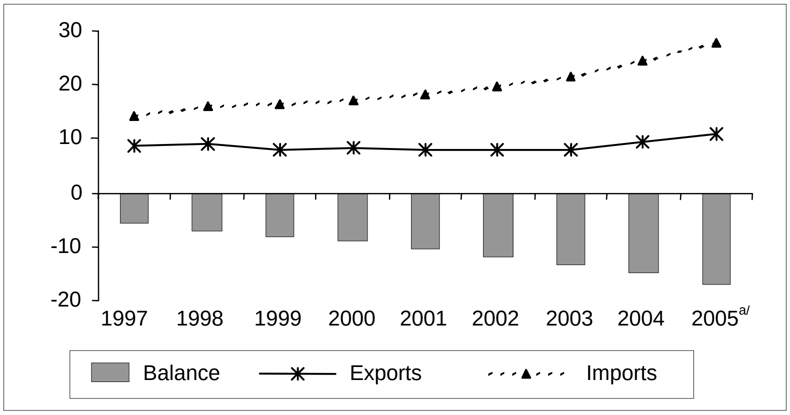
FIGURE 17
CACM: TERMS OF TRADE
(1995-2005 - Indexes 2000=100)



Source: Based on ECLAC data.

Traditionally, the level of Central American goods imports far exceeds exports, producing a high chronic deficit in this balance. The deficit has increased in recent years: in a measurement excluding maquila, the imbalance in 2005 reached US$ 16.895 billion, almost triple the 1995-1999 average of US$ 6.077 billion (Figure 18 and Tables A13 and A14). Thus measured, this deficit represented a record, being equal to 20.9% of the subregion's GDP. The imbalance involves trade with all the main partners and is higher for Latin America (US$ 6.38 billion in 2005). The reason for this lies largely in the region's high dependence on petroleum imports, with Venezuela as the major supplier, but with a high volume of imports also from Mexico, and in recent years, from the rising levels of purchases from Brazil and, to a lesser extent, Argentina.[26]

FIGURE 18
CACM: BALANCE OF NON-MAQUILA TRADE IN GOODS
(1995-2005 - US$ billion)



Notes: [a/] Preliminary data for 2005. SIECA Data have been used for El Salvador (2005) and Guatemala (2005). Information for Costa Rica is based on CBCR data.

Source: Based on data from UN-Comtrade/SITC Rev. 2. SIECA and the CBCR.

The Central American countries are clearly faced with the challenge of increasing their exports of non-maquila products. DR-CAFTA consolidates and extends US market access, and negotiations to establish an FTA with the EU are in the pipeline. Although these agreements mean that Central America has wide and expanding access for its exports in these markets, the major challenge is to take these opportunities and achieve a significant increase in its external sales (Chapter IV).

C. Exports under the Maquila Regime

The upsurge in maquiladora production in Central American countries was associated with the process of liberalization and the revision of legislation and regulations governing foreign trade and investment, which took place in the 1990s, but for which there are precedents as early as the 1980s.[27] The main objective was

[26] In 2003-2005, CACM countries' average imports from Mexico totaled US$ 1.922 billion (an average annual increase of 18%), US$ 908 million from Venezuela (+19%), US$ 907 million from Brazil (+48%), and US$ 236 million from Argentina (+63%). Data from UN-Comtrade.

[27] The establishment of maquilas and duty-free zones was directly linked to concessions on imports granted by the industrialized countries, first and foremost the United States, which granted tax-free access to certain products under given conditions in the context of initiatives like the Caribbean Basin Economic Recovery Act (CBERA), the first version of which came into force in 1984. Apart from allowing the temporary import of tariff-free inputs and the subsequent export of the tariff-free end product to the US market, operations under these regimes are also exempt from taxes like income or profit tax for a number of years. Exports are subject to specific rules of origin, particularly restrictive for textiles and clothing.

to attract foreign investment, contribute to the increase and diversification of exports, and create new employment opportunities.

It should be noted that the available statistical data on maquila trade for most Central American countries are extremely limited. This gets in the way of analysis, as there is no exhaustive information available on country of destination and sectoral composition, or by product. This is reflected in exports and even more in imports associated with maquila transactions, in particular regarding information prior to 1997.

In the latter half of the 1990s, maquila exports underwent a rapid expansion, taking in textiles and clothing, as well as other products such as electronic components and medical equipment (Tables 7 and A15).[28] By way of illustration, in 1997-1999, the exports of maquila products from all Central American countries grew by an annual average of 30.9%. By 1999, exports under this regime had reached US$ 9.3 billion, overtaking non-maquila exports (US$ 8 billion) for the first time.

This peak was leveled off by the deceleration of the US economy in 2001-2002, which meant lower growth and even a contraction in the sector's exports. Although a new dynamism was seen with the recovery of the US economy from 2003, growth came about at much lower rates than in the last decade. All the same, the maquila's importance is illustrated by the fact that, in 2005, its exports represented 111% of 'domestic' exports. The main target market is the United States.

Costa Rica is the main exporter of (mainly electronic) products originating in duty free zones. These account for around a third of Central America's total maquila exports. Costa Rica's exports in 2001-2002 were affected negatively with a decline in demand from the US electronics industry. Maquila exports from Honduras, the second largest exporter of these products, also fell while the other countries recorded positive growth. Prominent in the context of the general increase in maquila exports in 2003-2005 are the high growth rates of Nicaraguan exports, averaging over 25% p.a.

The overall added value of maquila production (calculated as the difference between its exports and imports) for the CACM countries rose in 2000-2002 and 2003-2005, reaching an average of US$ 2.715 billion in the latter period (Table 8). However, this variable fell markedly in 2004-2005, a phenomenon resulting from widely mixed trends at the country level. In the case of the Costa Rican maquila's added value, which exhibits high volatility, there was a very significant drop in these years, as in 2001. More limited in scope, a decrease also affected the variable in El Salvador and Guatemala. However, in Honduras and Nicaragua, the added value of maquiladoras displayed steady growth in this period.

Looking at the maquila's added value in relation to exports of these activities, stagnation is seen, and even a certain reversal: in 2003-2005, the ratio stood at 0.235, just slightly above the 0.234 of the previous three years, but below the 0.256 level attained in 1997-1999.

It should be noted that the maquila's added value corresponds to the trade balance for these activities which, being positive, helps to ease the Central American countries' high deficit in the balance of goods. The average positive balance in 2003-2005 thus contributed to reducing the subregion's total deficit from 20.3% to 16.6%, the equivalent of 3.7% of GDP (Table A10).

[28] While El Salvador, Guatemala, Honduras and Nicaragua's exports under this regime are concentrated in textile and clothing products, Costa Rica's mainly comprise electronic components.

TABLE 7
CACM: MAQUILA EXPORTS [a/]
(1997-2005)

Value (US$ million)	Average		2003	2004	2005	% AAGR [b/]	
	1997-1999	2000-2002				2000-2002	2003-2005
CACM	7,343	9,438	11,172	11,472	11,942	0.6	8.3
Costa Rica	2,561	3,018	3,635	3,621	4,072	-8.3	11.3
El Salvador	1,191	1,672	1,873	1,921	1,818	9.9	1.3
Guatemala	1,125	1,609	1,825	2,105	2,002	11.1	5.9
Honduras	2,285	2,849	3,405	3,229	3,368	2.2	9.1
Nicaragua	180	291	434	597	682	21	25.6
% Share	**Average**					**Average**	
Costa Rica	34.9	31.9	32.5	31.6	34.1	31.9	32.7
El Salvador	16.2	17.7	16.8	16.7	15.2	17.7	16.2
Guatemala	15.3	17.1	16.3	18.3	16.8	17.1	17.1
Honduras	31.1	30.2	30.5	28.1	28.2	30.2	28.9
Nicaragua	2.5	3.1	3.9	5.2	5.7	3.1	4.9

Notes: [a/] Maquila includes duty-free export zones.

[b/] AAGR: Simple Average Annual Growth Rate.

The data for Costa Rica, El Salvador, Guatemala (as from 2002) and Nicaragua correspond to information given by these countries' Central Banks. The data for Guatemala in 1997-2002 correspond to US textile and clothing imports. The data for Honduras were calculated as the difference between non-maquila exports from Honduras to the world and total world imports from Honduras.

Source: Based on data from UN-Comtrade/SITC Rev. 2. SIECA, USITC and Central Banks.

TABLE 8
CACM: MAQUILA ADDED VALUE [a/]
(1997-2005 - US$ million)

Region / Country	Average			2000	2001	2002	2003	2004	2005 [b/]
	1997-1999	2000-2002	2003-2005						
CACM	1,882	2,215	2,715	2,676	1,954	2,016	2,900	2,750	2,495
Costa Rica	819	715	883	1,222	427	496	1,151	885	613
El Salvador	336	473	457	456	489	474	494	464	414
Guatemala	262	372	394	374	396	346	419	442	322
Honduras	398	555	816	542	534	589	704	792	951
Nicaragua	68	101	165	82	109	112	133	167	195

Notes: [a/] Maquila includes duty-free export zones.

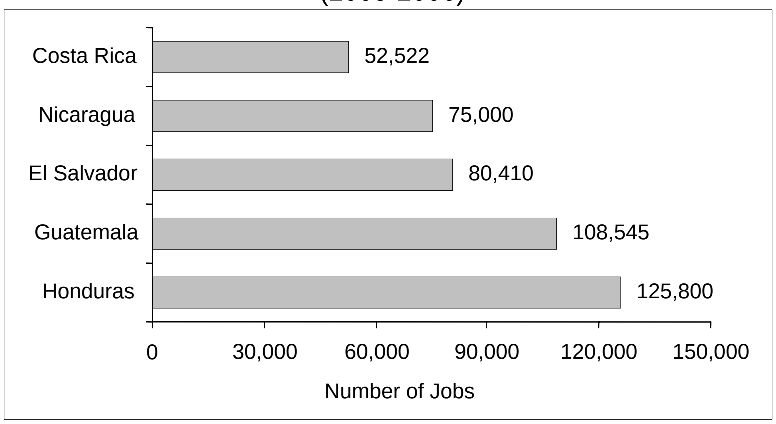
The added value corresponds to the difference between maquila exports and imports. Maquila data for Costa Rica, El Salvador and Guatemala (as from 2002) and Nicaragua correspond to the information given by these countries' central banks. The data for maquila added value for Guatemala prior to 2002 correspond to ECLAC information. The figures for Honduras have been calculated as the difference between exports from Honduras to the world and world imports from Honduras. Costa Rica's 1995-1999 average only includes data from 1997 on. The data for Guatemala only include those covered by Decree 29-89 of the Guatemalan Congress (Promotion and Development of Export and Maquila Activity Act).

[b/] Preliminary data for 2005.

Source: Based on data from UN-Comtrade/SITC Rev. 2. SIECA, ECLAC and Central Banks.

Export-oriented maquiladora production is an important source of employment. In 2005-2006, this sector in Central America directly employed some 440,000 people (Figure 19). Although many of the jobs are low-skilled, especially in the textile and clothing industry, in Costa Rica's case numerous skilled and highly skilled jobs were created, especially in the electronics industry. This is reflected in the added value *per* employee generated in the different countries: in Honduras this reached an average of close to US$ 6,500 for 2003-2005, while in Costa Rica it stood at US$ 22,600.

FIGURE 19
CACM: MAQUILA JOBS [a/]
(2005-2006)



Note: [a/] Maquila includes duty-free export zones. Only jobs from the textile and clothing sector are included for Guatemala.

Source: Based on data from the Costa Rican Trade Promotion Agency (PROCOMER - *Promotora del Comercio Exterior de Costa Rica*), the El Salvador Economy Ministry, VESTEX (Guatemala), the Central Bank of Honduras, Nicaragua's Free Trade Zone Corporation (CZF - *Corporación de Zonas Francas*) and the WB.

Where the future is concerned, maquiladora production raises several dilemmas and questions over policy.[29] Although the maquila has brought with it many benefits for the Central American countries, such as attracting fresh investment, increasing and diversifying exports and, even more importantly, generating fresh employment, it is a fact that this kind of production has established few links to the "domestic economy" and, consequently, its added value generally remains fairly low.

Moreover, the sustainability of this form of production is in doubt. Two issues should be underlined regarding this situation. On the one hand, maquila production regimes in Central America must meet the obligations and commitments assumed at multilateral level by these countries in the context of the WTO. In this respect, tax incentives awarded to companies operating in duty-free export zones are considered as export subsidies and, as such, are to be removed by early 2009[30] in countries where *per capita* GDP is over US$ 1,000. Currently, only Honduras and Nicaragua have a *per capita* GDP below this frame (at 1996 prices). The prospect of the removal of these tax incentives in Costa Rica, El Salvador and Guatemala is linked to reforms and broader taxation issues, as well as to the subject of taxation policy coordination at Central American level, as will be seen below in the discussion on CU.

[29] For further information on and analysis of the treatment of the duty-free export zones in integration agreements and multilateral negotiations, see Granados [2005].

[30] Bearing in mind possible extensions, the effective date for the removal of tax incentives is late 2009.

The second doubt over the sustainability of maquila production concerns the competitiveness of clothing manufacture, one of the main activities in this area. As pointed out in Chapter 1, this is one of the Central American industries most affected by competition from China. The share of Central American clothing manufacturers[31] in the imports of their main buyer, the United States, fell throughout the period analyzed from 11% in 2002 to 8.4% in 2006, while China's share increased from 13.6% to 28.7%. Certainly, other Latin American countries like Mexico or the Dominican Republic have been even more badly hit, as the garments they sell the United States display a greater degree of similarity to Chinese garments than those produced on the isthmus (Granados et al. [2006] pp. 16-21).

However, despite this relative difference, the competitiveness problems of Central American manufacturers seem to be worsening. Two substages can be identified in the evolution of US purchases of these products from the CACM in 2003-2006. In 2003-2004, Central America lost market share but its exports of clothing rose by 3.7% c.a. In 2005-2006, however, these exports fell in absolute terms at an annual average of 3.9%. At the same time, in those two years, the sales of their main competitor, China, rose by 31.7%, strengthening its presence in the US clothing market.

TABLE 9
US TEXTILE IMPORTS [a/]
(2000-2006)

US$ million	2000	2001	2002	2003	2004	2005	2006 [e]
Total	*63,585*	*63,292*	*64,170*	*69,415*	*74,455*	*79,690*	*82,995*
China	7,290	7,620	8,720	11,000	13,700	20,700	23,778
Rest of Asia	24,900	24,400	24,200	26,100	27,600	28,100	30,053
CACM	6,695	6,872	7,040	7,175	7,575	7,370	6,989
Costa Rica	827	772	727	591	519	484	472
El Salvador	1,620	1,660	1,700	1,750	1,750	1,640	1,423
Guatemala	1,490	1,620	1,670	1,770	1,960	1,830	1,679
Honduras	2,420	2,440	2,510	2,580	2,750	2,700	2,547
Nicaragua	338	380	433	484	596	716	867
Mexico	9,300	8,690	8,370	7,810	7,570	6,950	6,189
Dominican Republic	2,400	2,260	2,180	2,160	2,110	1,920	1,625
Rest of Latin America	1,600	1,450	1,460	1,870	2,200	2,350	2,242
Rest of the World	11,400	12,000	12,200	13,300	13,700	12,300	12,084

Notes: [a/] Chapters 61, 62 and 63 of the HS are included.

[e] Estimates based on data for the first eleven months of the year. In contrast with the rest of Chapter, which covers 2003-2005, the inclusion of the 2006 figures for this heading is due to the need to illustrate the evolution of the garment trade after the expiry of the ATC in January 2005.

Source: Based on USITC data.

All the same, it has to be stressed that the impact of these changes in the US garments market on the Central American countries is not uniform. Although exports from Costa Rica suffered the sharpest fall (10.2% c.a.), the negative impact is less visible than in other countries in the subregion, as garments only represented 14.8% of total sales to the United States in 2003-2006. Elsewhere in the CACM, however, they constitute more than half the exports to this destination, with a maximum of 83.9% in El Salvador.

[31] Chapters 61, 62 and 63 of the Harmonized System (HS).

In positive contrast to this situation is the performance of Nicaraguan sales to the United States (60.9% of which corresponds to garments). Nicaraguan sales have been immune from the Chinese advance. Indeed, exports of these products to the US market grew by 19% c.a., increasing their market share by 0.7% in 2002 to 1% in 2006.

Nicaragua differs from its partners in the region in its lower labor costs[32] and the existence of other incentives for the clothing industry. It may maintain tax exemptions on the maquila after 2010. Within DR-CAFTA it also obtained preferential rules of origin for garments, which will allow Nicaragua to acquire raw materials at lower prices than its competitors.[33] Also prominent are the investments being made to improve the clothing industry's competitiveness, particularly in the preparation of raw materials and infrastructure development.

D. Intraregional Trade

A measurement of the relative importance of intraregional trade -defined as the sum of exports and imports excluding the maquila- with the CACM countries as origin or destination shows that, from 2000, these flows represent around 9% of regional GDP, proportionally higher than the 1990s (Table 10). This figure has changed little since 2000 and has great variability from one country to another, with Nicaragua and Honduras in the upper band and Costa Rica in the lower.

TABLE 10
INTRAREGIONAL TRADE OPENNESS COEFFICIENT EXCLUDING MAQUILA[a/]
(1995-2005 - % GDP)

Region / Country	Average			2000	2001	2002	2003	2004	2005 [b/]
	1995-1999	2000-2002	2003-2005						
CACM	7.8	9.1	8.9	9.1	9.3	8.7	8.6	8.9	9.1
Costa Rica	5.3	5.1	5.3	5.3	5.2	4.9	5.1	5.3	5.6
El Salvador	9.9	11.3	11.1	11.9	11.2	10.9	10.7	11.2	11.4
Guatemala	6.3	7.5	7.7	7.4	8.8	6.4	7.7	7.9	7.6
Honduras	11.5	14.6	13	13.3	14.1	16.4	12	12.9	14.1
Nicaragua	13.5	16.7	16.2	16.6	15.5	17.8	15.5	15.4	17.7

Notes: [a/] The trade openness coefficient is defined as the ratio of total exports and of goods imports to GDP. GDP for Honduras and Nicaragua may be underestimated and the opening coefficient may as a result be overestimated.

[b/] Preliminary data for 2005.

SIECA Data have been used for El Salvador (2005) and Guatemala (2005). The data for Costa Rica correspond to information from the CBCR.

Source: Based on data from UN-Comtrade/SITC Rev. 2, SIECA, CBCR and ECLAC.

[32] Nicaragua's average hourly wage in 2004 stood at about US$ 0.7 as against US$ 1.2 in Honduras, US$ 1.4 in El Salvador and Guatemala, and US$ 2 in Costa Rica. These wages include benefit contributions, but not production incentives. Source: ProNicaragua with data from The Economist Intelligence Unit, FINDE Honduras, PROESA, Invest in Guatemala, PROEXPORT, CINDE and CNZF.

[33] Nicaragua was granted a preferential tariff preference level (TPL) for fabric inputs of 100 million m^2 imported from anywhere in the world, with 5 years' free access to the US market for end products and with gradual phasing out by year ten. Costa Rica obtained a 2-year TPL for 500,000 m^2 of woolen garment inputs (subject to extension), with tariffs in the US market equivalent to 50% of the Most Favored Nation (MFN) tariff.

Furthermore, if we look at the importance of the CACM as an export destination excluding maquila, it represented 35.1% of total export on average in 2003-2005. This figure is a fair bit above the average for the latter half of the 1990s, when the region represented 24.1% of export outflows (Table 11). In 2005, the Central American market accounted for 55% of the exports of El Salvador, 42% of Guatemala's and 34% of Nicaragua's. If we compare 2000-2002 and 2003-2005, reverses -in general slight- can be seen in some countries in terms of the relative importance of intraregional exports in their external sales.

However, as the appreciable rate at which this variable grew in 2003-2005 (11.2%) was very similar to the rate for total exports, its relative weight remained fairly stable across the board. The relative importance and rate of Guatemala's sales to the subregion contributed by far the most to these growth rates in the period. Costa Rica and El Salvador also contributed to this dynamism. However, a contraction was recorded in the case of Honduras, the only country whose level of intraregional exports in 2005 was lower than in 2002 (Table 11 and Figure 20).

TABLE 11
CACM: INTRAREGIONAL GOODS EXPORTS, EXCLUDING MAQUILA
(1995-2005)

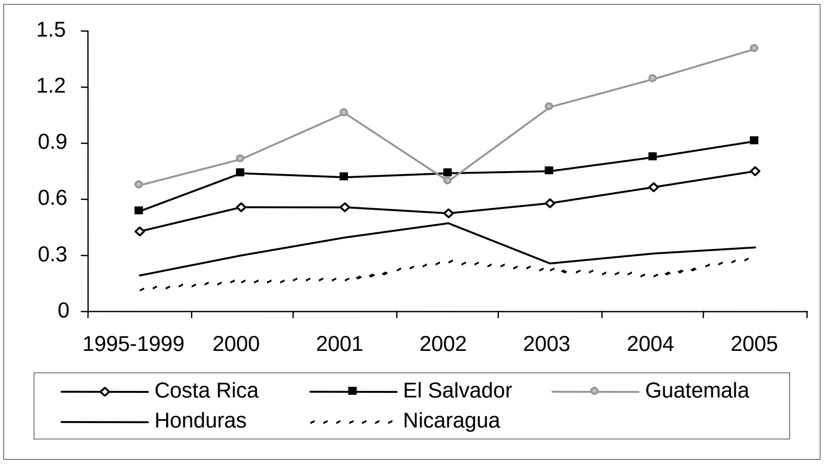
Value (US$ million)	Average		2003	2004	2005[a/]	% AAGR [b/]	
	1995-1999	2000-2002				2000-2002	2003-2005 [a/]
CACM	1,944	2,729	2,885	3,241	3,708	4.5	11.2
Costa Rica	431	547	575	666	751	-0.4	12.8
El Salvador	538	734	746	822	914	6.1	7.4
Guatemala	673	858	1,089	1,248	1,404	-0.3	27.6
Honduras	188	387	252	313	345	16.9	-3.8
Nicaragua	115	203	223	192	294	24.8	7.2
% Share of Total Exports, excluding maquila	**Average**					**Average**	
CACM	24.1	34.4	36.3	34.4	34.5	34.4	35.1
Costa Rica	15.2	23.2	23.3	24.8	25.4	23.2	24.5
El Salvador	46.5	58.2	59.4	55.7	55.2	58.2	56.8
Guatemala	29.6	36.0	41.3	42.6	41.6	36.0	41.8
Honduras	15.4	28.7	25.4	19.4	18.3	28.7	21.1
Nicaragua	19.8	33.8	36.8	26.4	33.9	33.8	32.4

Notes: [a/] Preliminary data for 2005. SIECA data have been used for El Salvador (2005) and Guatemala (2005).

[b/] AAGR: Simple average annual growth rate.

Source: Based on data from UN-Comtrade/SITC Rev. 2. SIECA and CBCR.

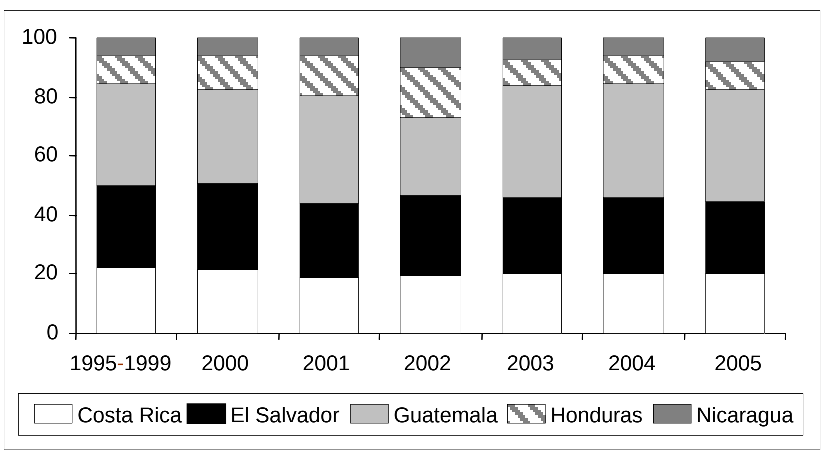
FIGURE 20
CACM: INTRAREGIONAL EXPORTS BY COUNTRY
(1995-2005 - US$ billion)



Source: Based on data from UN-Comtrade/SITC Rev. 2. SIECA and CBCR.

If composition is analyzed by origin of intraregional exports, Guatemala has the largest relative share, with almost 38% of the total in 2005 (Figure 21 and Table A17). Its share has risen around 3 p.p. since 1995-1999 in contrast to an almost equally significant decline in El Salvador and Costa Rica, with 25% and 20% respectively. Like Guatemala, Nicaragua has increased its share.

FIGURE 21
CACM: SHARE IN INTRAREGIONAL EXPORTS BY COUNTRY, EXCLUDING MAQUILA
(1995-2005 - % of total)



Source: Based on data from UN-Comtrade/SITC Rev. 2, SIECA and CBCR.

The major importer at intraregional level is El Salvador with over US$ 1 billion in 2005, followed closely by Guatemala (Tables 12 and A18). Costa Rica, on the other hand, is far and away the country that least depends on regional market goods. In terms of the intraregional trade balance, the situation is very clear: Guatemala and Costa Rica have a growing positive balance over the years, while the other three countries show a systematic deficit, the highest in the case of Honduras.

TABLE 12
CACM: INTRAREGIONAL IMPORTS AND BALANCE OF TRADE IN GOODS, EXCLUDING MAQUILA
(1995-2005 - US$ million)

Intraregional Imports	Average		2003	2004	2005 [a]	% AAGR [b]	
	1995-1999	2000-2002				2000-2002	2003-2005 [a]
CACM	1,944	2,853	3,009	3,338	3,769	7.9	8.2
Costa Rica	277	296	313	321	361	1.4	5.5
El Salvador	558	820	867	946	1,015	9.6	7.4
Guatemala	408	730	831	908	986	18.6	7.4
Honduras	350	539	584	661	830	11.2	11.4
Nicaragua	351	468	413	501	576	-4.8	9.5
Intraregional Trade Balance [c]	**Average**					**Average**	
Costa Rica	153.9	250.8	262.8	344.5	390.1	250.8	332.5
El Salvador	-19.6	-86.0	-121.2	-123.9	-100.8	-86.0	-115.3
Guatemala	265.4	128.2	257.8	339.6	417.7	128.2	338.4
Honduras	-162.2	-152.5	-331.9	-347.8	-485.1	-152.5	-388.3
Nicaragua	-236.7	-265.3	-190.8	-309.6	-282.7	-265.3	-261.0

Notes: [a] Preliminary data for 2005. SIECA Data have been used for El Salvador (2005) and Guatemala (2005).

[b] AAGR: Simple Average Annual Growth Rate.

[c] The sum of the five countries' balances is not null, as the national statistical data offices do not harmonize the information gathered.

Source: Based on data from UN-Comtrade/SITC Rev. 2, SIECA and CBCR.

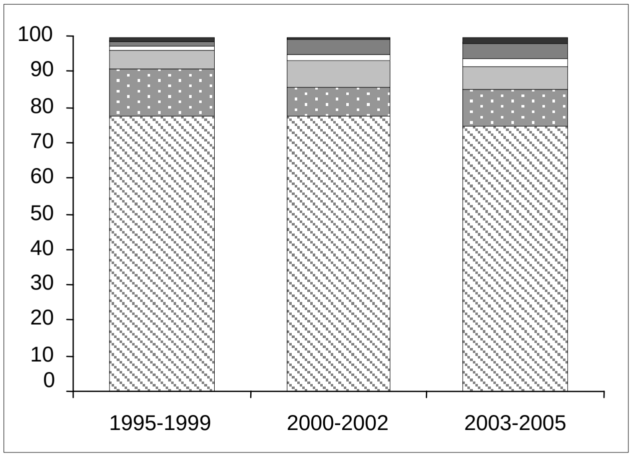
E. The Sectoral Composition of Exports

The sectoral composition of the CACM countries' exports varies according to their manner and destination. On the one hand, extraregional exports excluding maquila are heavily concentrated in food products, which account for three quarters of total exports. Manufacturing is well behind, followed by raw materials (Figure 22a). If the maquila is included, the situation changes significantly, as manufactured products then predominate, accounting for two thirds of the total, while foodstuffs represent 28% (Figure 22b). If we focus on intraregional exports, it can be seen that manufactured products are responsible for more than 60% of the total, and foodstuffs about 30% (Figure 22c). This distribution has not altered greatly in recent years.

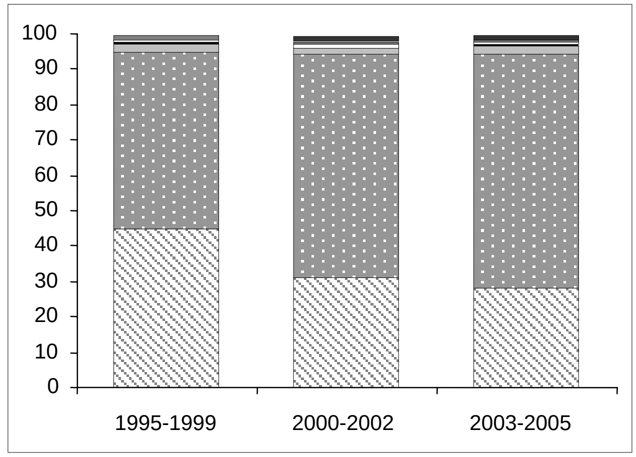
A closer analysis of the nature of exports can be performed at the 'products' level, defined as 6-digit items in the HS. At this level, when we focus on the total exported including maquiladoras activities, two diametrically different types of goods stand out: on the one hand, industrial exports from the maquiladora sector such as textiles and clothing (in all countries) or electronic components (in Costa Rica) and, on the other, traditional primary agricultural products such as tropical fruits, coffee and sugar (in all countries) (Figure 23 and Table A21). This contrast very clearly illustrates the dual nature of the region's export sector, as well as the lack of linkage between the two types of production.

FIGURE 22
CACM: SECTORAL COMPOSITION OF EXPORTS
(1995-2005 - % of total - Period Average)

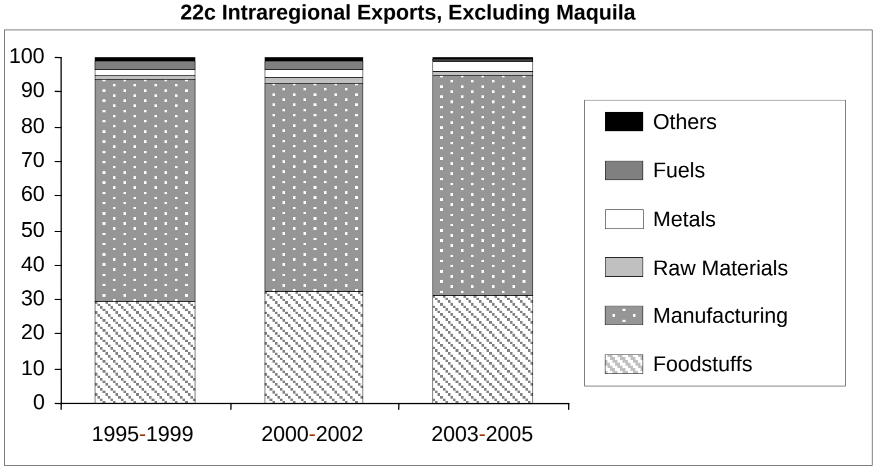
22a. Extraregional Exports, Excluding Maquila



22b. Extraregional Exports, Ixcluding Maquila



22c Intraregional Exports, Excluding Maquila

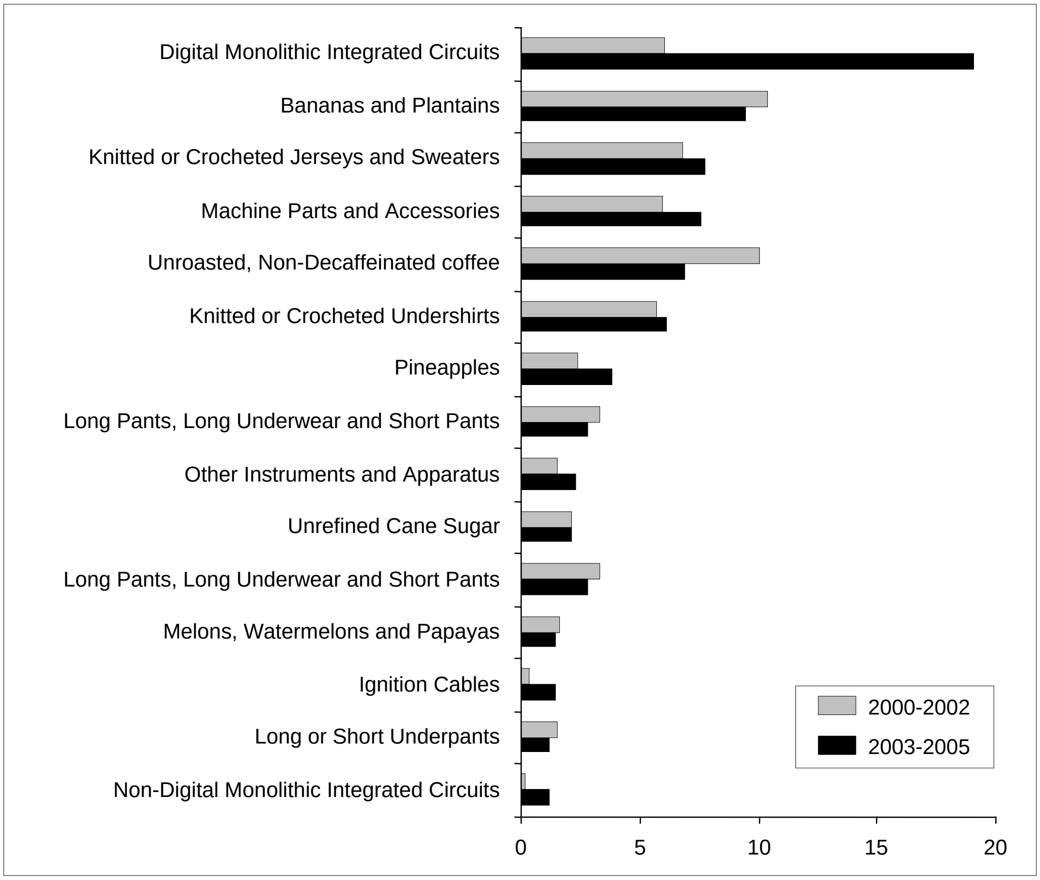


Source: Based on data from UN-Comtrade/SITC Rev. 2, SIECA and Central Banks.

If we look at intraregional exports, there is a preponderance of manufactured goods, such as medications and food preparations (Figure 24 and Table A23), followed in importance by products for mass consumption such as soap. There is also intraregional trade in certain manufactures, mainly steel inputs.

Medicaments, which are the most important good in intraregional exports, figure in a prominent position in both the exports and imports of practically all five countries (Table 13). These items are the main product exported by Guatemala and Costa Rica and El Salvador's second most important. At the same time, they are Nicaragua's main import, Guatemala and Honduras's second largest, Costa Rica's third and El Salvador's fifth. In the same vein, certain processed foods and other products manufactured for mass consumption also have a notable presence at both export and import level in all the countries. These phenomena demonstrate the importance of intraindustry trade in most countries in the subregion. A different trend is seen in the trade of Nicaragua, whose main exports consist of primary foodstuffs (products from the meat and beans sector), while its most important imports are manufactured goods.

FIGURE 23
CACM: MAJOR EXPORT PRODUCTS, INCLUDING MAQUILA
(2000-2005 - % of total)

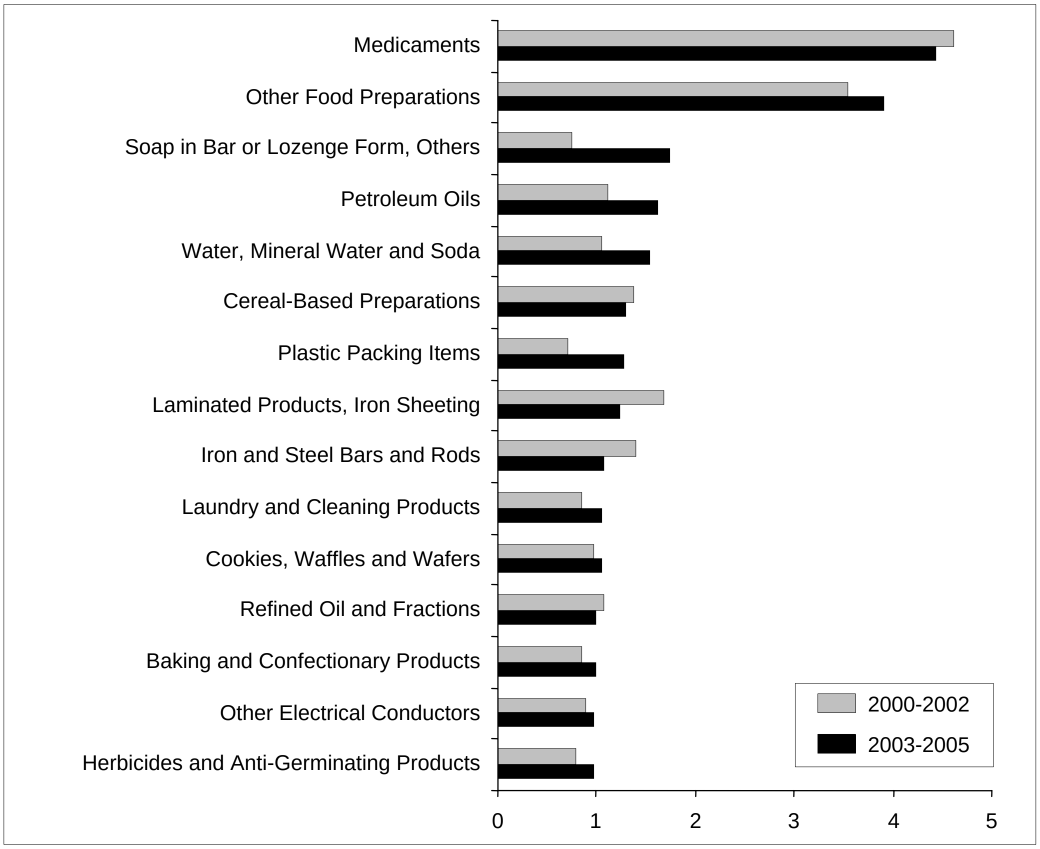


Note: Based on rest-of-the-world imports of CACM products.

Source: Based on UN-Comtrade data, 1996 HS at 6 digits.

In the near future, stepping up the Central American integration process, especially in the context of establishing the CU and tariff and standards harmonization, is bound to have a positive impact on intraregional trade flows (Chapter III). Furthermore, the multilateral application of the commitments and disciplines in DR-CAFTA in the context of provisions incorporating accumulation rules of origin for goods, will foreseeably facilitate the development of productive chains and supply chains between CACM countries, also aiming at the intensification of trade within the region.

FIGURE 24
CACM: MAIN INTRAREGIONAL EXPORTS
(2000-2005 - % of total)



Notes: Including maquila exports for Costa Rica (2000-2005) and Guatemala (2005). Exports for El Salvador are excluded.

Source: Based on UN-Comtrade data, 1996 HS at 6 digits.

TABLE 13
CACM: 5 MAIN INTRAREGIONAL EXPORTS AND IMPORTS BY COUNTRY
(2003-2005 - Yearly period average)

Exports			Imports		
Description	**Value (US$ million)**	**% Share**	**Description**	**Value (US$ million)**	**% Share**
Costa Rica			**Costa Rica**		
Other Food Preparations	101	15.2	Laundry and Cleaning Preparations	18	5.3
Medications, Others	74	11.2	Beans	14	4.1
Sanitary Towels, Tampons and Diapers	28	4.3	Medications, Others	14	4.1
Electrical Conductors	24	3.7	Cereal-Based Preparations	12	3.7
Sauces, Condiments, Others	23	3.5	Petroleum, Oils	10	3.1

TABLE 13 (CONTINUED)

Exports			Imports		
Description	Value (US$ million)	% Share	Description	Value (US$ million)	% Share
El Salvador			**El Salvador**		
Petroleum Oils	39	5 .0	Electrical Energy	29	3.1
Medicaments, Others	29	3.7	Soap in Bar or Tablet Form, Others	23	2.6
Toilet Paper	28	3.6	Other Food Preparations	23	2.5
Cereal-Based Preparations	27	3.4	Water, Mineral Water and Sodas	22	2.4
Laundry and Cleaning Preparations	25	3.1	Medicaments, Others	20	2.2
Guatemala			**Guatemala**		
Medicaments, Others	49	3.9	Other Food Preparations	45	5.0
Water, Mineral Water and Sodas	33	2.6	Medicaments, Others	42	4.6
Cereal-Based Preparations	23	1.9	Bottles, Jars and Similar Items	20	2.2
Herbicides	22	1.8	Cardboard and Corrugated Paper	17	1.9
Toothpaste	22	1.7	Toilet Paper	17	1.9
Honduras			**Honduras**		
Soap in Bar or Table t Form, Others	39	12.8	Other Food Preparations	38	5.5
Palm Oil, Others	16	5.2	Medicaments, Others	32	4.7
Cigarettes	13	4.4	Water, Mineral Water and Sodas	19	2.7
Baking and Confectionary Products	10	3.4	Toilet Paper	17	2.5
Vitamins, Others	8	2.7	Iron and Steel Bars, Corrugated Iron	15	2.2
Nicaragua			**Nicaragua**		
Deboned Beef	28	11.9	Medicaments, Others	22	4.5
Livestock	27	11.5	Palm Oil, Others	15	3.1
Fresh Beef, Carcasses	15	6.5	Food Preparations, Others	14	2.8
Black Beans	12	5.2	Flat Iron and Steel Sheeting	13	2.7
Cheese	11	4.5	Cigarettes	13	2.6

Note: The averages for El Salvador correspond to 2003-2004.

Source: Based on UN-Comtrade data, 1996 HS at 6 digits.

F. Extra and Intraregional FDI in the CACM

In 2003-2005, the total FDI to CACM countries was up by a high 31% on the previous three years, with an accumulated total of almost US$ 5.8 billion. Part of this growth is explained by the relatively low levels reached in 2000-2002, marked by the slowing of global economic activity. In terms of distribution by country of destination, these flows were concentrated mainly in Costa Rica with almost 40% of the total, while Honduras received a quarter of investment. It is worth highlighting the scant importance of Guatemala as a receptor, with just 8.5% of the total.

TABLE 14
CACM: FDI BY COUNTRY OF DESTINATION
(1997-2005)

Value (US$ million)	Average			2003	2004	2005 [a/]
	1997-1999	2000-2002	2003-2005			
CACM	1,686	1,468	1,926	1,405	2,070	2,302
Costa Rica	546	509	743	575	794	861
El Salvador	460	220	320	130	407	425
Guatemala	304	266	165	131	155	208
Honduras	155	266	467	368	465	568
Nicaragua	222	207	231	201	250	241
% Share						
CACM	100.0	100.0	100.0	100.0	100.0	100.0
Costa Rica	32.4	34.7	38.6	40.9	38.3	37.4
El Salvador	27.2	15.0	16.6	9.2	19.6	18.4
Guatemala	18.0	18.1	8.5	9.3	7.5	9.0
Honduras	9.2	18.1	24.2	26.2	22.4	24.7
Nicaragua	13.2	14.1	12.0	14.3	12.1	10.5
% GDP						
CACM	3.1	2.4	2.6	2.1	2.8	2.8
Costa Rica	3.8	3.1	4.0	3.3	4.3	4.3
El Salvador	3.8	1.6	2.0	0.9	2.6	2.5
Guatemala	1.6	1.3	0.6	0.5	0.6	0.7
Honduras	3.0	4.2	6.1	5.3	6.2	6.8
Nicaragua	6.2	5.2	5.1	4.9	5.6	4.9

Notes: [a/] Preliminary data for 2005. The figures include FDI, in maquila and duty-free export zones. The maquila for Honduras is included as from 2000.

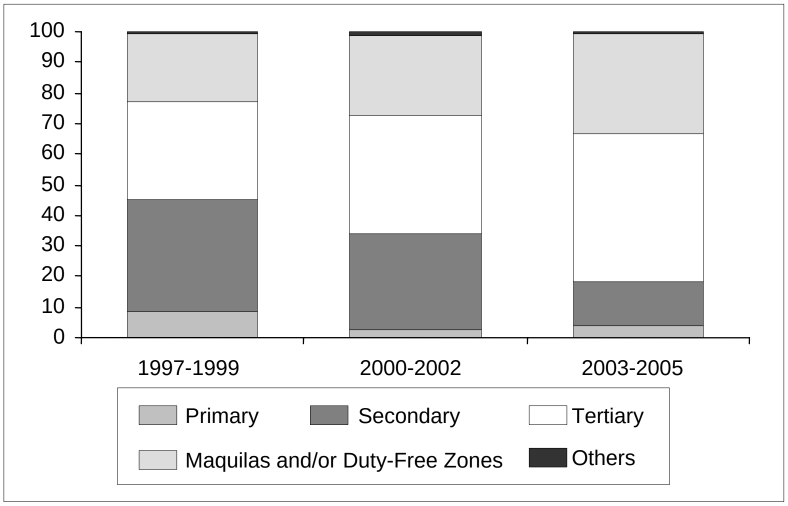
GDP for Honduras and Nicaragua may be underestimated and their opening coefficients may be overestimated as a result.

Source: Based on data from UNCTAD's *World Investment Report*, ECLAC, and Central American Central Banks.

The FDI flows recorded represent relatively low proportions of GDP: 2.6% in the three years in question, ranging from 6.1% in the case of Honduras to 0.6% in Guatemala. Despite this growth, the FDI/GDP ratio stagnated in 2003-2005 against the previous three years, influenced by the fact that the ratio in the case of Guatemala shrank by 0.7 p.p. of GDP (Tables 14 and A30). The comparison of the entire period beginning in 2000 with 1997-1999 is even more adverse, as the FDI/GDP coefficient in the latter three-year period was 3.1%. In other words, it has not been possible to reach the dynamism of these flows of the late 1990s, a dynamism that was certainly heavily influenced by the exceptional processes of privatization. Also in comparison to other sources of foreign currencies -especially remittances, as explained in detail in Chapter 1- the FDI dynamic was relatively weak.

In sectoral terms, services and maquila were the prime destinations of FDI.[34] The tertiary sector received a total of US$ 2.54 billion as against US$ 1.407 billion in 2000-2002. Among the most dynamic subsectors were communications (especially in El Salvador), trade (in Nicaragua and Honduras) and real estate in Costa Rica.[35] The second most dynamic sector was the maquila sector, with investments in 2003-2005 of US$ 1.754 billion, almost double the previous period. This performance is related to the relative recovery of maquila exports discussed in section C. There were contractions in flows targeting the secondary sector, particularly investments in energy and public services, as well as those targeting agribusiness (Figure 25 and Table A31).

FIGURE 25
CACM: SHARE OF FDI BY TARGET SECTOR
(1997-2005 - % of total)



Notes: Guatemala is excluded due to lack of data. Investment in Costa Rica's real estate sector are included as from 2002.

Source: Based on data from UNCTAD's *World Investment Report* and Central American Central Banks

As for geographical composition, extraregional FDI represented almost 95% of the total in 2003-2005. In this period, almost US$ 5 billion (excluding Guatemala) came in under the heading of extraregional investment, 51% up on the three previous years. The United States remained the major investor with 47% of the total, followed by Latin America with 22%, 16 p.p. of which correspond to investment from Mexico. The latter region doubled its share and overtook the flows from the EU, with 15% of the total.

The cumulative total of intraregional FDI in 2003-2005 was around US$ 318 million, 6% of the total FDI received.[36] This proportion is 3 p.p. down on the previous three years (Figure 26 and Table A32). El Salvador was the main investor in the region with 60.3% of these flows, while flows originating in Guatemala reached 27% of the total. The largest receptors were Honduras and Nicaragua, each one with 35% of the investments. This is a striking result, as it involves the less developed countries in the subregion (Table 15).

The lack of systematized statistical information on the intraregional FDI target sector limits analysis of its dynamics. However, in the next section some regional enterprises are analyzed that enable us to illustrate certain sectoral trends in FDI.

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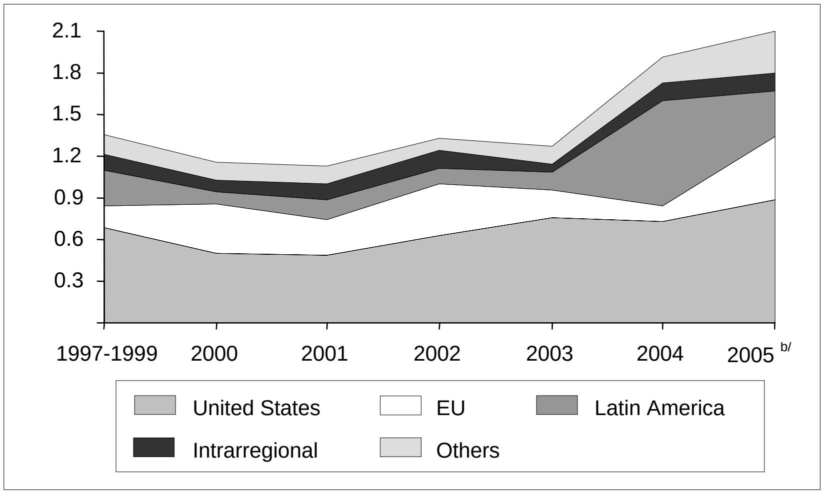
[34] Due to a lack of data, the analysis of distribution by sector and country of origin excludes information of FDI flows to Guatemala.

[35] Costa Rica only has only been entering investments in this sector since 2002.

[36] This is an estimate on the basis of partial information, the amount of intraregional investment to Guatemala being unknown.

FIGURE 26
CACM: FDI BY COUNTRY/REGION OF ORIGIN [a/]
(1995-2005 - US$ billion)



Notes: [a/] Guatemala is excluded, as there are no statistical data on FDI origin. The figures include FDI in the maquila and duty-free export zones. The maquila for Honduras is included as from 2000.

[b/] Preliminary data for 2005.

Source: Based on data from UNCTAD's *World Investment Report* and Central American Central Banks.

TABLE 15
CACM: INTRAREGIONAL FDI MATRIX
(2003-2005 - Cumulative Flows during the Period - US$ million)

Destination / Origin	Costa Rica	El Salvador	Guatemala	Honduras	Nicaragua	Total 2003-2005	% Intraregional FDI
Costa Rica	-	-2	n.a.	9	11	17	5.3
El Salvador	57	-	n.a.	51	84	192	60.3
Guatemala	6	32	n.a.	37	12	86	27
Honduras	-1	12	n.a.	-	3	15	4.6
Nicaragua	5	-12	n.a.	15	-	9	2.7
2003-2005 Total	*67*	*30*	*n.a.*	*111*	*109*	*318*	
% Intraregional FDI	*21.1*	*9.5*	*n.a.*	*35*	*34.4*		*100*

Notes: The origin of FDI is calculated as the sum of the FDI from the country in each of the other countries. Direct FDI to and from Guatemala is excluded.

Source: Based on data from UNCTAD's *World Investment Report* and Central American Central Banks.

G. Regional Enterprises

Certain anecdotal information available[37] enables us to identify three major trends in the emergence and evolution of regional enterprises: (1) regional enterprises have developed as a market expansion strategy; (2) there have been mergers and acquisitions of regional enterprises by companies external to the region; and (3)

[37] The major Central American economic information media.

some regional companies have made investments outside the CACM.[38] Occasionally regional enterprises first expand in the region and are then bought by others or expand into markets outside Central America.

In recent years the market expansion strategy has been apparent in the services sector and, to a lesser extent, in manufacturing. The investments in the subsectors of real estate, tourism and retail trade by large business groups in the region -such as El Roble or Simán y Poma from El Salvador, or Carrión from Honduras- extend across the isthmus. The trend is also seen in smaller traders like Sula and Esquimo of Honduras and Nicaragua, and Pops and Musmani of Costa Rica. There are also some enterprises expanding operations in the secondary sector in Central American countries, as with the Costa Rican group, Numar (América Economía [2005 and 2006]).[39]

There is also evidence of the sale of regional Central American enterprises to multinationals. These are strategic acquisitions or mergers enabling external enterprises to acquire the infrastructure and market knowledge of local companies. For local enterprises, this is an opportunity to capitalize on their past investments and/or access the technologies that multinationals can transfer via these transactions. In the retail trade sector, the most famous case is US multinational Wal-Mart, which in recent years took control of 50% of the Costa Rica and Guatemala regional enterprise, *Central American Retail Holding Company* (CARHCO). Other recent cases are the acquisitions of regional banks by international financial conglomerates such as GE Capital, Citibank, Scotia Bank and HSBC.

Not all the big Central American conglomerates have been acquired by multinational enterprises. In fact, several intraregional enterprises have ventured into the international market. This is the case with El Salvador's TACA airlines, which dominated the Central American market for more than 15 years and has subsidiaries in Mexico and Peru. The other case is the food trader, Pollo Campero, whose franchise model has more than 200 branches across Central America, Mexico, Ecuador, the United States and Spain.

In the future, the implementation of DR-CAFTA and other trade agreements may mean that intraregional foreign investment is galvanized still further. The new advantages of market access that DR-CAFTA brings represent opportunities to take advantage of each country's competitive advantages and to develop value chains of products for export, particularly to the United States. DR-CAFTA's reduction in tariffs could also increase consumer goods imports, which could strengthen the conglomerates of regional retailers who market this type of product. Also, the intensification of intraregional investment could serve as a basis for expansion into the market outside the region, including in the US.

[38] Henceforth, the information is not limited exclusively to 2003-2005, but covers trends over the last 6 years.

[39] These trends are also recognized by other authors such as Rosenthal [2006].

Contents

III. THE CURRENT STATE OF TRADE INTEGRATION IN CENTRAL AMERICA

This chapter offers an analysis of the Central American trade integration process from the point of view of its progress, limitations and outlook in the short- and medium-term. The period under analysis runs from January 2004 to December 2006. In general terms, a clear intensification of official efforts to step up regional integration can be seen in this period. The process, however, is not free of complexity, unconcluded initiatives and inconsistencies difficult to fathom without deeper investigation into the nature of the process and its actors, and the external and internal forces that help shape integration in Central America.

Locating the origin and beginning of the current trend to step up Central American integration can be a complex task. Ever since the General Treaty on Central American Economic Integration (*Tratado General de Integración Económica Centroamericano*) of 1960, Central America aspired to a Common Market to lever up its industrialization strategy through import substitution, then in vogue. The 1970s and 1980s saw a dizzying series of ups and downs in the process and demonstrated its limitations. With the 1990 Protocol of Guatemala and the 1991 Protocol of Tegucigalpa, regional integration was redesigned to act as a platform for positioning the Central American countries in the global economy. To achieve this a series of waystations were mapped out: embarking upon improvements to the Central American FTA, continuing with CU and eventually reaching economic union.

Given this ambitious map, it might be reasonable to argue that by advancing on the road to CU -still unconcluded- the subregion is already halfway between a basic FTA and the far more advanced stage of economic union. The new millennium brought with it an intensification of the need to step up regional integration, as this issue -and in particular the issue of CU- has only been clearly visible on the five countries' presidents' radar since 2002, as we will see. However, despite this political attention and the technical advances recorded, there is still half the distance to go, which involves completing CU and continuing with economic union, both of which are only seen as viable in the long term.

The nature and intensity of the events in 2004-2006 enable us to state that the main determining factor in this new drive to step up integration is threefold. First, there is nowadays a clearer conviction among the five governments that the viability and development of small countries in a globalized world is down to unification of its markets, joint external negotiations and collective efforts in the multiple facets of functional integration. This is an important acknowledgment. The new *afectio societatis* was not demonstrated with such intensity in the immediate past. One only has to look at the number of presidential summits and declarations, and ministerial resolutions devoted to CU and other trade integration-related issues in these two years to be convinced (Table 19). This does not mean, however, that there is consensus on every issue currently under discussion. As we will see, there are many tough issues to still agree on. What is clear is that, on the one hand, there has been the political will to create a CU, but that, on the other, the obstacles faced to date are difficult to surmount. What is prevalent among trade policymakers is the interpretation that a CU cannot be dictated either by political declaration or decree, nor against the tide of political realities in a democratic context. More political negotiation at national and regional level will be needed, as will greater effort to develop trade capacity, mainly in the public sector.

The private sector is in general agreement over the importance of regional markets. Indeed, a study commissioned from the Central American Institute of Business Administration (INCAE - *Instituto Centroamericano de Administración de Empresas*) by the IDB recently indicated that stepping up regional integration -principally completing CU- is one of the priorities identified in order to make more of the opportunities offered by the Central American market.[40]

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[40] See the recent INCAE document [2006].

This convergence of wills from governments and private sectors leads one to think that the construction of regional integration will continue to be an important issue in the short and medium term, even though, as will be shown, completing the second half of the process will take a good deal longer.

Second, although the combined negotiation of DR-CAFTA and the architecture of its contents is creating centripetal and centrifugal forces for regional integration, the former is more likely to prevail over the latter. The multilateral application of the Agreement's disciplines and the accumulation clause on the origin of inputs and processes creates two strong incentives to step up formal and real integration in Central America. Further reference will be made to these issues and the controversy surrounding them in Chapter 4 of this Report.

Third, the preference shown by the EU to move forward in negotiating an Association Agreement with a united, integrated Central America helps focus trade policymakers' attention on stepping up regional integration. The process of dialogue and prenegotiation between the two blocs in 2004-2006 has demonstrated Europe's insistence on having an extremely well-organized partner. This is achieved insofar as there is CU in Central America. The situation has certainly galvanized the subregion's governments in that direction.

In short, factors accelerating the official initiative toward improvement of CU have emerged in the last two years. The determining factors for this wave of enthusiasm lie in the recent past. The factors are endogenous in nature but possess a strong exogenous component as well. The intensity of the agenda and support for the subregion's productive sectors indicate that the intensification agenda has enjoyed a good degree of consensus. However, as we will see, the agenda already shows serious limitations that will determine the true potential for progress hereafter.

On the other hand, the Puebla Panama Plan (PPP) has gradually acquired momentum as an initiative and is contributing in an increasingly important way to strengthening functional integration in the subregion. From Mexico to Colombia, the PPP has a different membership to traditional Central American integration. It is a reality: integration in this subregion reaches out geographically to other countries and regions, albeit partially. Its dynamism in such issues as transborder interconnection and regional infrastructure development reinforces the action carried out in terms of CU. The PPP has demonstrated that an expanded subregion has been a good mechanism to attract the attention of presidents and contributions from international financing organizations to projects of supreme importance for all its members, actually creating new dimensions in regional integration in Central America. Yet it will still be important to strengthen the PPP even further and insert it -along with the CU and the other efforts toward functional integration being made in the subregion- in a broader, more coherent framework of policies and in a strengthened regional institutionality.

By way of explanation, this section examines the advances, the issues outstanding and the inconsistencies of the process within the framework of three dimensions of Central American integration: the FTA, improvement of the CU and advances in the PPP.[41]

[41] Central American integration has many other facets, such as functional cooperation over issues like infrastructure, environmental protection, strengthening of labor markets, disaster prevention, health, electrical and telecommunications interconnection, regional institutional reform, civil society, gender and youth, public safety and defense, political dimensions (legislative, judicial) and so on and so forth. Many of these dimensions are in a phase of significant dynamism. However, unless the issue is relevant to the PPP, this Report only focuses on the above three dimensions or facets for reasons of space and specialization.

A. A Free Trade Area for Central America

There is a well-developed FTA in Central America. Although there are still flaws to be corrected, almost all products are free of tariffs and non-tariff measures. There are also regional regulations governing intraregional trade, which are regularly reviewed.

In the period in question, the ministers responsible for Central American integration brought in three different exercises in reduction and removal of tariff and non-tariff barriers to intraregional trade and certain trade regulations governing intraregional trade were reviewed. The three exercises were as follows:

First, efforts continued to remove products from Annex A of the General Agreement and more products were incorporated in intra-Central American free trade.[42] Ministers liberalized the products in Table 16 within the subregion during this period.

TABLE 16
PRODUCTS INCLUDED IN INTRAREGIONAL FREE TRADE

Distilled Alcoholic Beverages	Ethyl or Non-Methylated Alcohol	Petroleum Derivatives
Honduras - Costa Rica	Costa Rica - Guatemala	Honduras - Costa Rica
Honduras - Guatemala	Costa Rica - Honduras	Honduras - Guatemala
Honduras - Nicaragua	Costa Rica - Nicaragua	Honduras - Nicaragua

Source: Based on information in CEIE Resolution 05/2006 of June 16, 2006.

The composition of Annex A is summarized in Table 17.

TABLE 17
PRODUCTS INCLUDED IN ANNEX A

Restrictions Common to the Five Countries	Bilateral Restrictions
-Unroasted Coffee -Cane Sugar	-Roasted Coffee: Costa Rica with El Salvador, Guatemala, Honduras and Nicaragua -Ethyl Alcohol: El Salvador with Honduras and Costa Rica -Petroleum Derivates: Honduras with El Salvador -Distilled Alcoholic Beverages: Honduras with El Salvador

Source: Based on information from the Annex to CEIE Resolution #05/2006, which also contains specific measures by product.

Second, in terms of suppressing non-tariff measures, there have also been some remarkable advances. As indicated in the previous Report (INTAL [2004]), ministers had started a process of identification and removal of non-tariff measures in 2000 in the shape of technical standards, sanitary and phytosanitary measures, as well as charges and unfounded administrative actions. The process reduced such measures from 60 in 2000 to 35 in 2002 and 13 by the end of 2003. In the Report's period of reference, other measures have been removed, but not all. According to information provided by the countries themselves on the web page of the Secretariat for Central American Economic Integration (SIECA) at *http://www.sieca.org.gt*, by the end of 2006 there were five measures left that were identified as contrary to free trade and that have been -and in some cases still are- the subject of consultation between countries with a view to settling their restrictive nature. These measures are summarized in Table 18.

[42] Annex A lists products that are not subject to free trade and must therefore pay the MFN tariff, or that are affected by an import ban or an import license issued prior to determining whether internal production of it exists or not.

TABLE 18
REPORTED NON-TARIFF MEASURES IN INTRA-CENTRAL AMERICAN TRADE

Reporting Country	Reported Country	Measure
Honduras	El Salvador	Shipments of oranges to be fumigated with methyl bromide.
Costa Rica	El Salvador	Broken rice (*miga de arroz*) is subject to a sanitary measure to avoid supposed contamination by rice acari.
El Salvador	Nicaragua	Health records rejected for "Alusor suspension" product.
El Salvador and Costa Rica	Guatemala	The Customs Authority houses grants the Single Customs Declaration in duty-free zones, fiscal customs storehouses and temporary warehouses only for domestic haulage contractors, even if shipment is destined for other countries.
Costa Rica	Honduras	The Agriculture Secretariat blocks chicken imports and byproducts, as Costa Rica reported Avian Infectious Laryngotracheitis in one area.

Source: Based on information from the SIECA, Group of Measures Against Intraregional Free Trade, December 4, 2006.

Third, Central America has also made significant progress in the removal of unjustified sanitary and phytosanitary requirements in intra and extraregional trade. Indeed, the Council of Ministers for Economic Integration (COMIECO - *Consejo de Ministros de la Integración Económica*) launched a process for identifying and removing unjustified requirements resulting in the approval of a list of 469 vegetable products that will be exempt from import authorization and phytosanitary export certification, being deemed not to present significant risks for the subregion.[43] In the context of CU, the COMIECO on the same occasion approved another series of sanitary and phytosanitary provisions, referred to below.

The three previous exercises performed in this period may have an important effect on the generation and facilitation of intraregional trade. It is hoped, however, that in the short term progress will be made in incorporating more products in intraregional free trade, that sanitary and phytosanitary requirements will be simplified and rationalized even further, and that any remaining or future non-tariff measures will be removed. The Extraordinary Summit of Heads of State and Government of the Countries of the Central American Integration System (SICA: *Sistema de Integración Centroamericana*) of March 9, 2006 had agreed that dates should be established by July 31 of that year in order to liberalize the tariff for all products within the subregion. On finishing the current Report, this goal had not been achieved due to agreement not being reached on time over this aspect. This is illustrative of the political difficulties faced by the process when dealing with traditionally more sensitive topics.

Advances were also made in the framework of the FTA over intraregional trade regulations.[44] However, many of these regulations predate the period of reference and therefore this Report does not evaluate them. Within the period in question, however, new Central American Regulations were negotiated on the Origin of Goods, incorporating the new single Spanish-language version of the Harmonized System (HS), as well

[43] See COMIECO Resolution 117/2004, June 28, 2004.

[44] The five countries have been agreeing a series of intraregional regulations for over a decade. These are (1) the Central American Regulations on the Origin of Goods (*Reglamento Centroamericano sobre el Origen de las Mercancías*); (2) the Central America Regulations on International Land Traffic (*Reglamento sobre el Régimen de Tránsito Aduanero Internacional Terrestre*); (3) the Trade Disputes Settlement Mechanism (*Mecanismo de Solución de Diferencias Comerciales*); (4) the Central America Regulations on Sanitary and Phytosanitary Measures (*Reglamento sobre Medidas y Procedimientos Sanitarios y Fitosanitarios*); (5) the Central American Regulations on Unfair Trade Practices (*Reglamento Centroamericano sobre Prácticas de Comercio Desleal*); (6) the Central American Regulations on Safeguard Measures (*Reglamento Centroamericano sobre Medidas de Salvaguardia*); (7) the Central American Regulations on Standardization Measures, Metrology and Authorization Procedures (*Reglamento Centroamericano de Medidas de Normalización, Metrología y Procedimientos de Autorización*); (8) the CAUCA and its regulations; and (9) the new Central American Regulations on Customs Valuation (*Reglamento Centroamericano sobre la Valoración Aduanera de las Mercancías*). The last five instruments are applied to both intraregional and extraregional trade and are therefore referred to again when dealing with the issue of CU below.

as the fourth amendment to this nomenclature.[45] Furthermore, new Central American Regulations on Customs Valuation the Goods were agreed in the period, to which we will refer below, as they are also applicable to extraregional trade and were promoted in the context of CU. The same goes for the Central American Uniform Customs Code (CAUCA - *Código Aduanero Uniforme Centroamericano*) and its regulations governing both intra- and extraregional trade.

In terms of registers, the Technical Groups and Subgroups on Food and Drink, Medications and Suchlike, Agricultural Inputs and Hydrocarbons have also made some advances. Progress has been made in standards convergence (which is hoped one day to facilitate mutual recognition of sanitary records) for procedures for registering cosmetic[46] and hygiene products,[47] food and drink (effective only in four countries),[48] seeds[49] and agrochemicals.[50] According to SIECA's data, mutual recognition over household pesticides, public and industrial health, and natural products was finalized at technical level, but has not yet been approved. According to the same source, the recognition of the official national laboratories of the Member States has already been approved. However, rather than mutual recognition, what is occurring in Central America is the harmonization or standards convergence of registration procedures and their documentation. It has so far not been feasible to move toward mutual recognition mechanisms, as the parameters and technical specifications for products, processes and services included in individual countries' technical regulations are different and require regional harmonization. Although upward harmonization is aimed at in the future, especially in the foods sector (medications are seen as more problematic), the subregion has not as yet done any work in this direction.

It should be pointed out here that this effort of regulation only covers intra-Central American trade. In other words, though each country's parameters and technical specifications for the products, processes and services apply to domestic and to regional and extraregional products and suppliers, the new approval and registration procedures and their documentation only benefit products of Central American, not extraregional origin. It is hoped that in the future there will be a movement toward a single registration mechanism for all products, regardless of their origin, and that, consequently, free circulation of registered products will be allowed within the CU. Consequently, the progress made should be within the bounds of the FTA and it is not yet right to label them as progress in constructing the CU.

Central America has also made important progress in intraregional regulation of trade in services and in investment flows. In these areas, the region tried to establish an instrument to promote integration in the five countries through trade in services, and investor and investment flows. As with second generation FTAs, it has been sought to make these efforts a complement to the disciplines laid down in the FTA in terms of goods.

Central America has indeed been negotiating an Agreement on Investment and Trade in Services for several years. This Agreement -which has a similar structure to the investment and service chapters of the latest FTAs- should be accompanied by a series of national annexes with each country's commitments regarding consolidation or opening for each service and investment sector, as well as respective reserves. In other words, it seeks to create a basic framework of disciplines to supply transparency and protection guaranties to service providers and investors in the region. Furthermore, as stated in these chapters, a mechanism for dispute settlement between the Member States and the other country's investors is included.

[45] COMIECO Resolution 181/2006.

[46] COMIECO Resolution 124/2004, October 19, 2004. This resolution is currently under review to make operative such issues as registry, labeling and mutual recognition procedures.

[47] COMIECO Resolution 125/2004, October 19, 2004.

[48] COMIECO Resolution 121/2004, July 29, 2004, Costa Rica does not as yet participate in this resolution.

[49] COMIECO Resolution 119/2004, June 28, 2004.

[50] COMIECO Resolution 118/2004, June 28, 2004.

One of the reasons why the Treaty has not yet come into effect in all countries is that negotiation of the countries' sectoral annexes is still underway. It is hoped that it will come into effect very soon and that it will provide a chance to evaluate the real scope of this instrument in terms of coverage, services included and future management of the sectors or subsectors reserved, as well as its relationship to other trade agreements.

One question arising with this Treaty is its relationship to DR-CAFTA. As explained in Chapter IV, the multilateral application of DR-CAFTA will also mean the Agreement can be applied between Central American countries. The answer given by some of the Agreement's negotiators is that DR-CAFTA's chapters on services and investments will effectively be applied at intraregional level but that the Central American Agreement and its annexes are compatible with DR-CAFTA and go deeper than this Agreement. As DR-CAFTA steps up Central American integration and the process involves multilateralization, the net result is that the combination of both texts -the Agreement and DR-CAFTA- will bring the region a richer, deeper legal regime.

Finally, the Central America Trade Dispute Settlement Mechanism, which has generated good results to date, has nevertheless been subjected to a complete revision to finetune its procedures.[51] A new version of the mechanism was approved on July 29, 2006.[52] This seeks to speed up some of its procedures. For example, a short 10-day term was established for a Member State to express its interest in participating in a dispute as a third party. The term for respective consultations when a good at the heart of the dispute is extremely perishable was halved. The possibility of directly requesting the setting up of the arbitration tribunal was established (bypassing previous discussion stages at the Council of Ministers level) when a country does not answer a call for consultation. And specific terms were established for arbitration tribunals to perform their tasks and issue their findings. In addition, Model Rules for Procedures and a Code of Conduct for Arbitrators were approved.

B. Central American Customs Union

In terms of stepping up integration in Central America, the greatest impetus has been in CU. As shown above, in this Report's period of reference, official activity has seen a great deal of dynamism at all levels. One only has to look at Table 19 showing the frequency of presidential summits to see the number of times each summit has tackled the question of Central American integration in general and CU in particular. This gives us a better idea of the political importance attached to these issues in the last two years.

Although the process of improving CU has brought out serious contradictions, which we will refer to later, the work began in a relatively orderly fashion. In 2002, a framework and a plan of action were laid out. These have been executed and periodically reviewed. On March 24, 2002, the region's presidents had approved the first Plan of Action for Central American Economic Integration to speed up the process of CU creation. Several technical work groups were formed on this occasion to perform the appointed tasks.[53] However, it was not until June 29, 2004, that a more structured working framework was established to move forward in terms of CU. On that date, the General Framework for the Negotiation of CU in Central America was approved. This lays out the vision, objectives and principles, as well as a negotiation structure (see Framework in Annex III of this Report).

[51] By 2006, eleven cases had been aired in the subregion. These include three between El Salvador and Nicaragua over dairy and poultry products, two between El Salvador and Guatemala over vodka and aguardiente, and one between Costa Rica and Guatemala, also over diary products.

[52] COMIECO Resolution 170/2006.

[53] Though Costa Rica did not initially join in these efforts, it did do so at the Presidential Summit of June 20 that same year.

TABLE 19
SUMMITS AND TRADE INTEGRATION

Year	N° of Presidential Summits	Inclusion of Regional Integration	Inclusion of CU
1986	1	0	0
1987	1	0	0
1988	0	0	0
1989	4	0	0
1990	2	2	0
1991	3	2	0
1992	2	2	1
1993	1	1	0
1994	3	2	0
1995	2	1	0
1996	1	0	0
1997	4	2	0
1998	2	0	0
1999	3	0	0
2000	4	1	0
2001	8	2	0
2002	10	5	2
2003	4	2	1
2004	8	8	6
2005	14	5	2
2006	10	5	5

Source: Based on information from the SIECA web page.

From this Framework emerged the first major thematic guidelines for the groundwork, as well as the major limitations. Indeed, from the structural composition of the work it can be deduced that technical concerns will concentrate on tariffs, customs, taxation and migration. The technical groups would approach the issues of tariffs, registration, agriculture, safeguards, intellectual property, origin, standardization and sanitary and phytosanitary measures. In addition, the need became apparent early on for establishing other technical groups to handle work on issues like customs legislation, risk management and inspection, traffic, customs value of goods, customs procedures, internal taxation and unfair trade practices. With this battery of technical works, Central America launched the most serious drive toward CU in its history.

Nevertheless, from the outset, serious limitations in the agenda have been visible. The Framework laid out a series of works designed to tackle elements that are distinctly easier -or not as complex- to put into practice, namely, those that can be tackled and resolved at intra-Central American level between the five countries. But a CU has external dimensions (such as FTA and multilateral negotiations) that must be approached and coordinated with third countries, and these dimensions, possibly due to the difficulties they entail, were not the subject of a mandate in this Framework. The subregion chose the path of least resistance to embark upon the job of deepening regional integration. Given the importance of this omission for the formation of a true CU, this issue will be analyzed later.

Progress

The SIECA has recently published a report on the progress to date in the execution of all these works (SIECA [2006b]). Although following a different structure, a very brief (but more analytical and critical) summary will be given here of these efforts during the period of reference. We will then look at the main problems faced and the tasks still to be accomplished.

The work done has concentrated on the following ten areas:

1) Customs Administration

A new CAUCA was elaborated and approved during the period. This Code modernizes and updates the five countries' customs procedures, includes a new chapter on international traffic and, more importantly, establishes common disciplines in areas where the previous Code referred the issue to each country's internal legislation.[54] The Code was adopted by all the countries except Costa Rica, which has to subject it to approval by its Legislative Assembly. The CAUCA is currently being regulated. According to the SIECA's report, the regulation work is 70% complete. Also being worked on is the update of the Regulations on International Customs Traffic and implementation is underway of a new Single Manual of Customs Procedures. The countries are implementing the Codes of Conduct for Officials and Employees of Customs Services and for Auxiliaries of the Public Customs Function, the bases of which were defined by the Customs Committee. A legislation project has been drawn up on Contraband and Customs Fraud and is currently being examined by the COMIECO. Finally, the Integrated Manual of Procedures for Regional Inspection was completed, but the work on operative programs to facilitate its application is still ongoing.

2) Customs Facilitation

With Guatemala and El Salvador playing leading roles, integrated windows were set up with personnel from both countries so that customs users have only to make a single stop at the border. In 2004, this model was replicated on the two countries' Honduran/Nicaraguan borders. Guatemala and El Salvador also began to reduce the physical inspection of goods-based risk analysis, random inspection and ex-ante and ex-post controls, a trend that spread to the other countries and continues to be widespread. Costa Rica is the only country that, to date, has not participated in this initiative due to its lack of legal grounds. In the opinion of technical officials from this country, the integrated windows entail aspects of extraterritoriality in terms of the functions of customs and border personnel, an aspect that requires a special legal framework not currently in place.[55] Costa Rica should rectify this situation soon so as not to fall too far behind in the process of stepping up integration.

Implementing CU requires the coordination of many other technical elements at customs level. With various degrees of progress, the region has developed or is still developing work on such matters as units of risk, regional risk criteria, information exchange formats, inspection of operations under inward processing regimes and courier offices, the single customs declaration, training, electronic transmission of the Declaration on International Traffic and the Declaration on the Central American Single Customs Form (FAUCA - *Factura Única Centroamericana*), guarantee mechanisms for international traffic and the single declaration for travelers.

[54] The CAUCA was adopted by COMIECO via Resolution 01/2006 (COMIECO-EX).

[55] Interview with COMEX officials, San José, Costa Rica, February 1. 2007.

3) Strengthening External Customs

As a requirement for removing intraregional border positions the subregion has been developing a plan to strengthen external or peripheral customs. To do this, Guatemala, El Salvador, Honduras and Nicaragua are implementing a pilot plan in certain intraregional customs that enables the electronic dispatch of documents and a freer flow of goods from peripheral customs in any of these countries to the customs of destination in the importing country. In some cases, this enables direct delivery to the importer's warehouse. This mechanism, however, is only in place between neighboring pairs of countries. There are already draft regulations to bring in electronic dispatch and direct delivery between all the countries. It is hoped that progress will be made in this respect during the course of 2007. Costa Rica has not been participating in the interconnection process, as it has stated a preference for internal computer systems consolidation (or "TICA" as it is known), proceeding immediately to interconnection with the other countries in the CU.

4) Customs Valuation

Since the entry into effect of the WTO's Customs Valuation Agreement after the conclusion of the Uruguay Round, countries had repealed the regional instrument governing customs valuation in Central America. However, the creation of CU was the occasion to reverse this centrifugal movement by approving new Central American Regulations on Customs Valuation in 2004.[56] These Regulations, which will become another chapter of the CAUCA, develop the obligations acquired by the countries in the context of the WTO. In addition in this period, the Customs Committee also approved a simplified procedure for dispatch and determining the value for samples with no commercial value, and another for determining the value of goods subject to successive sales.

5) The Common External Tariff

The issue of the CET is perhaps the most controversial of all the activities involved in the efforts to attain CU. According to SIECA information, 95% of tariff lines are currently harmonized or have a harmonization model agreed and underway, with 5% still pending.[57] In 2004-2006, some progress has been seen in this respect, the level of CET harmonization in 2002 being 85% (INTAL [2004]). This is in itself a very significant achievement for the subregion.

Nevertheless, the region has shown limitations in this effort to harmonize the 352 lines making up the remaining 5%, many of which involve highly sensitive agricultural products.[58] Indeed, the Summit of Heads of State of March 9, 2006, provided that a program should be agreed by July 31 that year in order to complete tariff harmonization. The program was to respect certain very general and ambiguous criteria:

-short-term harmonization for products not produced in the region;

-medium-term harmonization for industrial and agribusiness products produced in the region and certain agricultural products;

-long-term harmonization for highly sensitive products in line with proposals presented by the productive sectors or according to recommendations of the Tariff Technical Group in line with specific criteria such as the relation with DR-CAFTA's tax relief deadlines.

[56] COMIECO Resolution 115/2004, June 28, 2004.

[57] El Salvador, for example, has different textile tariffs than the other countries, but these will be harmonized by the end of 2007. See Article 3 of COMIECO Resolution 180/2006 of November 9, 2006. In the past there was a significant degree of tariff deharmonization in the chapters of the HS on vehicles due to the fact that the countries had different classification nomenclatures for these goods. However, the nomenclature for these chapters was also harmonized with the recent implementation of the fourth amendment of the HS via the same Resolution.

[58] For several reasons, many of these products were subject to highly uneven tariff levels: processes of tariffication for agricultural products in the WTO without regional coordination, tariff increases for reasons of protection, application of safeguard measures, etc.

According to the SIECA, this date was postponed to December 31, 2006, as it was not possible to reach agreement over the program. On that date, however, agreement was again not reached over the harmonization program for the remaining tariff lines. In other words, the process seemed to be reaching its real limits, at least during the current period of momentum in stepping up integration.

The five most important causes of these limitations in CET improvement are:

First, the lack of agreement between governments over how to execute harmonization. Some countries proposed a long-term convergence model (bound in certain cases to the DR-CAFTA liberalization deadlines) whose ultimate goal would be the lower MFN tariff applied by the five countries for each tariff line in question. Inversely, other countries proposed that convergence should be upward, which may entail future renegotiations of the bound tariffs in WTO.[59]

Second, the opposition to a tariff cut by the productive sectors affected, which also argue that downward harmonization entails risks in the current context of distorted international agricultural markets, as well as the lack of regional capacity to identify triangulations of agricultural products and control their sanitary and phytosanitary quality.

Third, a degree of political wear-and-tear is currently being seen in some governments due essentially to efforts to approve DR-CAFTA. This limits their ability to manage trade policy issues -at least in the short term- especially regarding possible unilateral tariff cuts.

Fourth, the rejection by some governments of the possibility of a tariff renegotiation with the WTO that will impose on the Central American countries the obligation -under Article XXVIII of the General Agreement on Tariffs and Trade (GATT)- to give equivalent trade concessions to third countries affected by any tariff increases.

Fifth, the difficulties inherent in designing a regional convergence program in the middle of a process of tariff negotiation in the Doha Development Agenda, over which the region's countries have divergent positions.

As we can see, these problems are not minor ones. Yet it is still feasible to think of a long-term downward convergence model, possibly consisting of a package including the option, under very exceptional circumstances, to increase certain specific tariffs on certain products in certain countries. Such an exceptional increase would aim to settle certain very specific protectionist pressures that often become necessary in order to be able to approve a wider-ranging package of downward measures. The downward trend would minimize the need for renegotiation in WTO, a renegotiation that in any event must be coordinated at regional level in order to offset certain negative effects on third countries by the positive effects stemming from the general impact of the five countries' downward harmonization.

All the same, as the convergence program would be long-term, any specific renegotiation would also take place in the medium-to-long term, that is, when the tariff applied reaches the level of the bound tariff. Furthermore, as many of the countries that have initial negotiating rights in the WTO and would participate in any renegotiation are countries with whom there is or will be free trade in the future (the United States, the EU, Canada, etc.), the negative impact on them is minimum. This could ease the pressure of any renegotiation.[60]

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[59] The discussion about CET harmonization has, however, neglected the other focus of CET problems, namely, the perforations caused by non-joint FTAs with different models for tariff removal signed by the countries. We will come back to this later.

[60] Under GATT Article XXVIII of 1994 and its Understanding issued at the Uruguay Round, any renegotiation of bound tariff rates is to be undertaken with countries that, during Central American countries' membership of the GATT, participated in this negotiation and formally registered their interest in participating should the consolidated levels be renegotiated. The countries with "initial negotiating rights" at the level of individual products are those registered as such in every country's list of tariff concessions in the GATT.

This long-term approach should not generate too much opposition from the productive sectors potentially affected. It would involve one small step back in order to take two strides forward. The logic of the proposal is that, if free trade with each country's major trading partners is accepted in most of these products, there is all the more reason for a mere tariff reduction with third partners to be allowed. It is enough to coordinate the reduction properly in cases where third countries are current or potentially important suppliers. The negotiation positions in the Doha Development Agenda should also be coordinated. The whole process may be complex, but it can also be technically and politically viable if carried out before the current momentum to step up Central American integration runs its course.

In summary, the region has made significant efforts on the issue of improving the CET but is unable to complete tariff harmonization. Given that the existence of deharmonized items denaturalizes the essence of CU and free circulation, it is important for the subregion to continue with renewed efforts in order to complete the CET. Though it is rather unrealistic to expect harmonization in the short term, it is possible to agree now a long-term convergence model with a clear north. Efforts of this nature have the important virtue of imbuing integration, the process of CU construction and, ultimately, the region's credibility with new momentum. The risk is that the other efforts toward improving the CU outlined here will not be continued if tariff harmonization does not lead the way in the exercise.

6) Common Trade Regulations

As shown above, in order to improve CU, Central America has been working to develop common trade regulations for over a decade. Many of these regulations are exclusively applied to intraregional trade and were mentioned above in the section on the Central American FTA. Some of these regulations, however, are also or only applied to extraregional trade and form part of the common trade regulations affecting third countries in a CU.[61] During the period of reference there has been some progress in the following:

- The General Principles for the Administration of Food and Agricultural Input Donations have been agreed.[62] These principles arose from the need to control the distorting effects of the goods donated by third countries or by individual countries on regional production;

- The General Principles for the Administration of Tariff-Rate Quotas on Agricultural Products were approved.[63] These basic disciplines obey the need to recognize to some extent the multiple modalities of managing tariff-rate quotas, modalities that are of economic importance given that they determine who are the ultimate beneficiaries of the rents from those tariff-rate quotas;[64]

- Work is currently underway on a review of the Central American Regulations on Unfair Trade Practices and the Central American Regulations on Safeguards. The real challenge of a CU in these areas consists in establishing regional investigations and adoption of any future antidumping duties, countervailing or safeguard measures.

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[61] The regulations are the Central American Regulations on Unfair Trade Practices, the Central American Regulations on Safeguard Measures, the Central American Regulations on Standardization Measures, Metrology and Authorization Procedures, the CAUCA and its regulations, and the new Central American Regulations on Customs Valuation.

[62] COMIECO Resolution 145/2005, September 26, 2005.

[63] COMIECO Resolution 144/2005, September 26, 2005.

[64] Various different quota administration models are used across the region: first in time, first in law, proration, public auction via agricultural exchanges and track records.

7) Common Collection

This is a new issue for Central America. A true CU requires mechanisms for common tariff revenue collection and when internal border taxes are collected, as they are in Central America, the need also arises to start a process of tax harmonization and permanent cooperation between customs authorities and tax administrations.

At the Extraordinary Summit of March 9, 2006, the Central American Heads of States agreed that the Agreement on Compatibilization of the Tax Systems of the Member States of the Central American CU should be adopted at the latest by June 30 that year. This goal was achieved. The Mutual Assistance and Technical Cooperation Agreement between Central American Tax and Customs Administrations was to be adopted by April 30, a mandate that was fulfilled effectively on April 25. To implement these two agreements, the countries' Internal Revenue Directors are in the process of discussing and approving a management plan to make them operational.

However, this exercise of taxation compatibilization is heavily restricted. Indeed, harmonization of political and technical components are limited to questions such as the generating event and the Central American Single Invoice Form, but does not get as far as the essential thing, namely, harmonization of taxation rates, and a common collection and distribution mechanism. In other customs unions, such as the EU, border collection is not divided, but instead goes to the community budget for community projects. In Central America, however, this option is still a very long way off, as countries have a significant fiscal dependence on tariffs and other taxes levyable at borders. They also find it premature to propose the substitution of national programs by regional programs. In their place, they raised other alternatives for the distribution of common collection in the period. These alternatives are to assign the job of collection to the country of entry, to the country of final destination or to distribute collection between both countries under a formula yet to be agreed. The implications of each of these alternatives are being carefully weighed up and progress is expected in 2007. Despite the difficulties, the very fact that such delicate issues are being worked on in the region is in itself a good sign.

8) Sanitary Regulation

On dealing with the subject of the FTA above, this Report referred to the process of rationalization of sanitary and phytosanitary requirements for 469 products. The process of removal of procedures in obtaining import permits and phytosanitary export certificates also affects imports from third countries. For this reason, the rationalization of requirements forms part of the efforts to implement and improve the common regulations applicable to third countries in the context of CU.

In addition, there were other advances during the period of reference. These were in the areas of common sanitary procedures. The COMIECO approved the Phytosanitary Surveillance Formats (*Formatos de Vigilancia Fitosanitaria*), a Procedures Manual for the award of the Sanitary Guide for Animal Transportation (*Guía Sanitaria de Movilización de Animales*) within the CU territory and the Guide itself, the Animal Health Epidemiological Surveillance Formats (*Formatos de Vigilancia Epidemiológica para uso en Salud Animal*), the Zoosanitary Standards and Procedures (*Normas y Procedimientos Zoosanitarios*) for aquatic and equine species, the Sanitary Criteria applicable for trade in animals and animal products and by-products within the CU territory; the Manual of Good Animal Husbandry Practices in Primary Production (*Manual de Buenas Prácticas Pecuarias en la Producción Primaria*), Rule NIMF-11 (of the International Convention of Phytosanitary Protection (CIPF: *Convención Internacional de Protección Phytosanitary*) "Pest Risk Analysis for Pest Quarantine" (*Análisis de Riesgo de Plagas para Plagas Cuarentenarias*), the sanitary risk analysis requirements for the Sanitary Code for Terrestrial Animals (*Código Sanitario para Animales Terrestres*) of the International Office of Epizootics (IOE), the IOE's international poultry standard, the Zoosanitary Requirements and

Procedures for Cattle (*Requisitos y Procedimientos Zoosanitarios para Bovinos*) of the IOE's Terrestrial Animal Health Code; and the IOE-recommended Veterinary Services Assessment Manual.[65]

9) Technical Regulations

There was also intense work in drawing up and adopting Central American technical regulations, essentially in such products as land transport units, hydrocarbons,[66] the stability of medications, pharmaceutical[67] and petroleum products.[68]

It should be stressed that progress has been made in Central America regarding WTO-coordinated notification of sanitary and phytosanitary measures, as well as of the technical regulations approved. Although no single notification is being made, a common format has been agreed, and delivery dates and answers to the questions and matters raised by members of the WTO are being coordinated.

Lastly, it is extremely important to remember that none of the subregion's countries has sufficient (or any) capacity for verification of compliance with technical regulations in many of the products subject to registry. And it is very limited in other areas such as transport units, hydrocarbons and others. Consequently, many of these harmonization efforts come to naught. The benefits of sanitary prevention and regional consumer safety are highly vulnerable. Central America must pay a lot of attention to these issues at national and regional level if it is to make headway on CU issues. Again, if the institutions of a country do not have technical confidence in the work performed by the other country's institutions, the short-term outlook for the free circulation of goods in the region is not good.

10) The Regulatory Framework and Institutions

The region has recognized that the current regulatory framework is quite inadequate to build a true CU.[69] Consequently, during the period of reference, the need to design and put into effect a new regulatory framework with appropriate regional institutions to support this important and complex challenge has been debated at technical and vice ministerial levels. Central America has had the benefit of technical assistance from the EU in these deliberations. The genuine advances materializing, however, are minimal. Yet the discussion has been extremely rich and seems to be headed in the right direction. Indeed, after much deliberation, a first annotated index of what would be a critical route to a new regulatory framework with a new institutionality was finally approved in December 2006.[70] Although the index only mentions the issues, the annotations made at the foot of each header reveal that the region has finally straightened out the elements sine qua non for the construction of a true CU. The Index contains 16 headings: the free circulation of goods, the tariff regime, the customs regime, origin, sanitary and phytosanitary measures, technical barriers to trade, trade remedies, trade in services, goods transport, external trade policy, competition policy, government procurement, intellectual property, dispute settlement, tax provisions and institutionality. The general direction signaled by this Index suggests that, today, the challenges to

65 COMIECO Resolution 117/2004, June 28, 2004.

66 COMIECO Resolution 152/2005, November 30, 2005.

67 COMIECO Resolution 166/2006, July 28, 2006.

68 COMIECO Resolutions 167/2006 and 169/2006, July 28, 2006.

69 The Guatemala and Tegucigalpa Protocols, and the presidential declarations constitute programmatic documents that do not produce true legal disciplines for the creation of CU. In this context, establishing the appropriate legal instruments is a priority in order to give credibility to the attempt to step up efforts toward a CU in the region.

70 San José Declaration, Point 12 a), December 16, 2006.

improve CU seem clearer. Again, this is a significant achievement. The overarching question to be answered in the near future is whether, by taking this path, Central America will build a true CU or opt for a rhetoric of headings and headers without real legal content in favor of regional integration.

Pending Issues and Inconsistencies

Despite the significant progress mentioned above, the countries have a backlog of work, and practices and measures not fully consistent with the logic of a CU. In this respect, a more consistent pro-regional integration change in attitude is still missing. As pointed out above, the Framework for the establishment of CU pragmatically opted to begin, at the internal level, works with the best chance of success. The results are -generally- positive, although there is still a long way to go. The external dimensions, however, are cause for more serious doubts. This section deals with the main trends to be seen at present.

A. Individually Negotiated FTAs

Perhaps the most marked inconsistency -preceding the current momentum to improve CU- lies in the existence of certain FTAs that the countries have signed individually or as subgroups. This practice began with the negotiations of an FTA between Costa Rica and Mexico in the early 1990s and, remarkably, still continues to this day. The FTAs already signed and the negotiations of FTAs currently underway individually or in subgroups are listed in Table 20:

TABLE 20
NON-JOINT FTA NEGOTIATIONS

Country or Country Subgroup	Trading Partner	Status
Costa Rica	Mexico	Signed in 1994
Nicaragua	Mexico	Signed in 1997
Guatemala, El Salvador, Honduras (Northern Triangle)	Mexico	Signed in 2001
Costa Rica	CARICOM	Signed in 2005
Guatemala	Taiwan	Signed in 2006
Nicaragua	Taiwan	Signed in 2006
El Salvador, Honduras	Taiwan	Signed in 2006
Guatemala, El Salvador, Honduras (Northern Triangle)	Colombia	Negotiations underway
Guatemala, El Salvador, Honduras and Nicaragua (CA-4)	Canada	Negotiations underway

Source: Based on SIECA information.

The regulatory framework for an FTA with Panama was jointly agreed, but with separate negotiations over market access to separate markets (tariffs, services, investments and government procurement). To date, only El Salvador has completed these negotiations since 2003, although it is hoped the other countries will conclude them in the short term, as this dynamic has accelerated substantially in the last few months. The same was true of Chile: a joint regulatory framework signed in 1999 was agreed, but with separate negotiations over market access, which have the same potential for fragmentation.

These FTAs, which account for an ever greater share of extraregional trade, imply the existence of tariff elimination programs that do not take into account their effects on the CET. When a Central American country or subgroup of countries has commitments to tariff elimination with a third country, the CET is perforated, the CU's logic is broken, a need prevails to maintain rules of origin within the CU for these products and the possibility of the free circulation of these goods within the Central American customs territory is eliminated, at which point customs, fiscal, sanitary and other controls that have been used in the absence of a CU are required once again.

Certainly, the fact that DR-CAFTA has important products with different models of tariff elimination for each country means that the Agreement is guilty of the same vice described here. However, as shown above (we will come back to this in the next chapter), DR-CAFTA could act as a catalyst for the long-term improvement of the Central American CET. The countries should therefore try, wherever possible, to harmonize tariff elimination models, as well as exclusions of FTA products with a genuine, fully operative CU in the region. This task is extremely complex and can only be realized in the long term, as it entails, among other things, the harmonization of rules of origin. This issue falls within the framework of work carried out as part of the PPP, at least as far as the FTAs signed in Meso-America (Central America, Panama and Mexico) are concerned. However, progress is extremely limited due to the difficulties involved and tight international negotiation agendas. Given the scant negotiating power of the region's countries in this area, it will be difficult to persuade any trading partners with whom trade agreements are in place (Chile, Canada, Taiwan) to launch renegotiations of agreements already signed.

The fact that there were bilateral and not coordinated FTAs in the 1990s was much more comprehensible in those days than to observe the continuation of the trend today. In the 1990s, the centripetal forces of integration were far less powerful. Today the landscape has changed substantially. That is why the non-joint negotiations undertaken in the last two or three years raise doubts over the letter and spirit of the countries' commitments to forge a more united Central America through CU. This excessive pragmatism -which in the past may have been more justified- is difficult to understand today and, what is worse, difficult to correct its effects on regional integration.

The mention at this point of the most serious inconsistencies in the construction process of the CU is unavoidable. On the one hand, the presidents attempt to promote it and constantly instruct ministers and technicians to press on with its construction. However, certain countries embark on opposite trajectories by initiating FTA negotiations non-jointly. This is tantamount to the simultaneous construction and deconstruction of the CU. It is our duty to point out that presidential and ministerial declarations are voided of content through such actions. The events become obstacles to stepping up CU and the discourse is largely reduced to rhetoric. This is a very serious issue in Central America and one that must be solved soon.

B. Different Multilateral Tariff-Rate Quotas

As a result of the countries' non-coordinated individual participation in the multilateral negotiations of the Uruguay Round in 1986-1993, the tariff-rate quotas agreed for an important series of highly sensitive agricultural products are nationally applicable. In other words, the quotas were fixed at country level, not at subregional level. These quotas were agreed for different products and different amounts.[71] The tariff-rate quotas are on such products as dairy products, chicken, sausages, pig meat and beef, natural honey, apples, prefried potatoes, garlic, onions, avocados, sugar, corn, beans, rice, wheat flour, soy flour, tuna and textile products.

Such differentiated conditions of access mean that it would be impossible to grant and accept conditions of free regional circulation for those products -the very essence of a CU- and, once again, generate the need to maintain rules of origin and border regimes of inspection and sanitary control -the diametrical opposite of a CU! Furthermore, despite the recent emergence of general disciplines agreed at regional

[71] The figures for each country's authorized tariff-rate quotas within the context of the WTO are as follows: Costa Rica 27, El Salvador 11, Guatemala 22 and Nicaragua 9. Honduras did not negotiate tariff-rate quotas at the Uruguay Round.

level for tariff-rate quota administration, these disciplines are general and enable the adoption of national mechanisms which in reality are very different, as we mentioned earlier. Therefore, when there are different market access mechanisms in each country, the internal logic of a CU unravels.

This lack of coordination over tariff-rate quotas is perhaps the most salient characteristic in a much broader phenomenon, namely, the lack of intraregional coordination in multilateral trade negotiations regarding market access. In the context of those negotiations, as in the current Doha Development Agenda, more than 150 countries are negotiating different formulas and mechanisms for tariff elimination and reduction, with the possibility of agreeing exceptions, safeguards, sectoral approaches, special treatment, differentiated speeds and suchlike for specific products, both agricultural and industrial. The fact that the region's countries are not participating in these negotiations jointly and in a coordinated way -factoring into their proposals the need to maintain the logic of a CU- exacerbates the problems -present and future- to do with improving Central American trade integration.

Other than for tariff-rate quotas, this issue had not been critical until today because the commitments to tariff reduction agreed during the processes of joining the GATT or at the Uruguay Round impacted on tariffs bound at very high levels that did not in the end affect the effectively applied tariff rates. This situation, however, tends to disappear by virtue of the fact that the bound tariffs converge with the ones applied. For this reason, it will be important for the five countries to look to the maintenance and integrity of the CET when negotiating at the WTO.

- Other Factors Conditioning Market Access -

Just as FTAs and tariff-rate quotas compromise the integrity and logic of the CET, the application of other contingent protection instruments can have the same effects and it is necessary for the region to tackle them adequately. Indeed, areas like the application of antidumping duties, countervailing and safeguard measures, compensation measures and retaliatory measures in cases of tariff renegotiation and dispute settlement should ideally be implemented regionally by carrying out a regional investigation and enforcing these measures at regional level. Not to do so would imply the existence of differentiated market access conditions for certain products, which is incompatible with the idea of CU. Work is currently being done on the technical update of certain regional regulations that discipline these instruments in the context of CU construction. However, public information about the degree or progress and the direction of this work is scarce. Yet the countries will be doing the intensification of regional integration no favors if they handle these instruments in a way incompatible with the improvement of the Central American CU in the terms outlined above.

The same can be said for certain elements in intellectual property protection. For example, if the conditions of patentability or test data protection for a product are different in the region's five countries, there would be a rush for patentability or protection toward the less rigorous country. This, combined with an intraregional free circulation policy, would lead to patentability or protection dodging in the other four countries. Therefore, a CU also enforces the need to jointly agree specific disciplines regarding intellectual property.

The positive thing is that, as indicated, the current framework for the CU and a new institutionality shows signs -though still very vague- of going in the right direction.

Paradigm Shift: The Real Challenge

A more integrated region could generate very positive results. The expansion of regional markets and their better operation would make Central America a more attractive area for FDI with all the revenue of foreign currencies, job creation and knowledge transfer that this entails. A more integrated market may generate more intraregional exports (important as a niche for hundred of thousands of Micro, Small and Medium Enterprises (MSMEs) in the region and as a strategy to help eradicate poverty), as well as exports with more value added from the region to the rest of the world. CU may, furthermore, impact indirectly on a greater intraregional flow of tourists who are not traveling due to the border difficulties they encounter. Last, trading partners will show more interest in an integrated market of several dozen million inhabitants than in a fragmented group of small countries. They may consequently be more inclined to develop new cooperation and trade facilitation programs.

Yet, as we have seen in this section, forming a true CU involves a genuine paradigm shift. CU implies that trade policies should no longer be thought of in national but in regional terms. It involves a significant shift in the mindset of the main actors. There is no quick or easy fix in accomplishing this. Completing a CU involves accepting its horizontality regarding trade policy. The regional CU touches on virtually all the issues of current domestic trade policy: industrial protection levels, trade discipline, public institutions, and national and international actors, both public and private. Under the framework of a CU, these policies -or certain elements in them- cannot be formulated neglecting the regional issue.

The practical challenges are, of course, important. In order to launch a CU there must be greater confidence in the other countries' institutions. More financial and human resources should be given over to the management of the model. Private sectors and civil society at large must do the same. Their discussions with national governments must be expanded in order to interact more with the entire region's private sectors and civil societies. Likewise, their costs will increase through having to participate geographically in broader processes of trade coordination.

Nevertheless, reaping the benefits of deep integration may more than make up for these costs. The world trend is toward better positioning of a country or region's productive capacities in global value chains. Central America is right to jump on the wagon of stepping up intraregional integration while inserting itself in international markets equally or more aggressively. In order to maximize the opportunities from such international insertion, the region must tread the other half of the road to much deeper integration.

Many of the difficulties being experienced by the region in concluding CU lie in the fact that, from the outset, the sequence of external negotiation decisions ran in parallel to national exploitation of windows of opportunity offered by trading partners outside the region. Perhaps quite rightly, the countries made the most of the occasion and negotiated multiple FTAs, individually or in subgroups. The sequence should ideally have started with the CU. However, by the mid-1990s, this sequence would have been extremely complex to implement for many reasons. The regional market was deemed very small and high-risk. Last generation agreements were sought to show other more important partners, like the United States, that the region's countries were willing and able to play major league. And reciprocal trade opportunities were required outside the region in order to sustain the processes of unilateral opening begun in the 1980s. Hence, the processes of trade opening, which had unilateral, multilateral and regional components -the Free Trade Area of the Americas (FTAA)- had necessarily to advance and to complement each other in one way or another. Today, however, now that the region needs to order these elements more efficiently, the exercise is far more complex.

C. The Puebla Panama Plan

At almost six years old, the PPP is still a relatively new initiative compared to other integrating trends in Central America. Its progress in implementing its project portfolio -and in managing ongoing projects with guaranteed funding of US$ 4 billion- lead one to believe that its stability as a mechanism of Meso-American development is gradually being consolidated, leaving behind the shadow of failure or of being an ephemeral political initiative. To give some idea of the progress and the extent of the interventions under the PPP, there are 4,092 kilometers of highways under construction, restoration, expansion or signaling in the region (PPP [2006]). Furthermore, in the last two years, its solidity and stability have increased and it has become an institutionalized mechanism[72] comprising a series of entities responsible for managing the portfolio in the present and the future. These entities have executive, advisory and technical functions in order to conceive, define and implement sectoral integration and regional development projects (PPP [2004]).

There have also been changes in the PPP's membership in the last year, with the inclusion of Colombia as a "full member".[73] Colombia now joins the "founders" Belize, Costa Rica, El Salvador, Guatemala, Honduras, Mexico, Nicaragua and Panama, as a beneficiary of the action undertaken under the Plan, which indicates rising confidence levels in the region regarding the mechanism's solidity and effectiveness. With this degree of consolidation, it is not now unreasonable to claim that the PPP effectively has a very good chance of being consolidated as an instrument to promote development and regional integration. This may have profound effects on Central American trade integration. However, the results could be improved if it is sought to produce -and exploit- the synergies developed by other regional initiatives like DR-CAFTA or CU, which are moving forward under their own internal dynamic.[74]

No other substantial changes in the Plan's nature, objectives or vision have been identified in the last two years other than those described above. But everything seems to point to the fact that this situation will change in the short term. Taking advantage of the visit of heads of state and government officials participating in the PPP to attend his inauguration on December 1, 2006, the Mexican President proposed holding a special meeting in the first half of 2007 to review the PPP's priorities and objectives, but not without reaffirming beforehand his administration's commitment to this mechanism (Presidential Office of the Mexican Republic [2006]). The President also stressed the fact that, for his administration, Latin America is a priority, which leads one to believe that this new attitude will be of benefit to the PPP. It was no coincidence that President Felipe Calderón's first international visit was to Guatemala. At all events, it is necessary to keep a lookout for the probable refocusing or redefining of the Plan's objectives, followed by its relaunch.

The PPP's global portfolio currently consists of 99 projects across 8 initiatives in the framework of 2 axes: (1) the Human Development Axis and its Environment[75] and (2) Productive Integration and Competitiveness Axis.[76] In order to implement it a global investment of US$ 7.7 billion[77] has been

[72] This fact was sanctioned by the region's Heads of State and Government in 2004 on the signing in Managua, Nicaragua, of the accord institutionalizing the PPP Mechanism.

[73] Colombia was incorporated with full member status after applying in July 2006.

[74] The PPP was launched in 2001 in the framework of the Tuxtla Dialogue and Consensus Mechanism. The Plan initially sought convergence of the Meso-American development strategy proposed by Mexico with the Central American Agenda for the 21st Century, published by INCAE/HIID (Harvard Institute for International Development).

[75] The development axis takes in the Meso-American Initiative of Human Development (*Iniciativa Mesoamericana de Desarrollo Humano*), the Meso-American Initiative of Sustainable Development (*Iniciativa Mesoamericana de Desarrollo Sostenible*) and the Meso-American Initiative of Prevention and Mitigation of Natural Disasters (*Iniciativa Mesoamericana de Prevención y Mitigación de Desastres Naturales*).

[76] The integration axis takes in the Meso-American Initiative for Transport (*Iniciativa Mesoamericana de Transporte*), the Meso-American Initiative for Telecommunications (*Iniciativa Mesoamericana de Telecomunicaciones*), the Meso-American Initiative for Energy (*Iniciativa Mesoamericana Energética*), the Meso-American Initiative for Trade Facilitation and Competitiveness Building (*Iniciativa Mesoamericana de Facilitación del Comercio y Aumento de la Competitividad*) and the Meso-American Initiative for Tourism (*Iniciativa Mesoamericana de Turismo*).

deemed necessary, with more than 90% going to the 57 projects under the integration axis.[78] The transport initiative is the most important in the global portfolio, requiring US$ 6.1 billion in investment terms, almost 80% of the total scheduled for the entire PPP.[79] Due to the scope of this Report, we will only be reviewing the state of the integration axis.[80]

From the point of view of implementation of the axis, the above figures suggest that the mechanism has made significant headway. Unfortunately, since its makeup is dynamic (allowing the continuous incorporation of projects subject to defined qualification criteria),[81] it is difficult to take a detailed measurement of its general progress. Therefore, the overview of the current state of the Plan presented below is based on analysis of the implementation of the current portfolio of the integration axis.

As shown in Table 21, despite the conclusion of just 3 projects, less than a third of the portfolio is at the design stage and implementation is already underway for 50%.[82] If we add in the fact that it has secured financing equivalent to 55% of the estimated total investment, this axis as it stands at present can be said to be viable and stands every chance of being completed successfully.

TABLE 21
PROGRESS OF PPP INTEGRATION, PRODUCTIVITY AND COMPETITIVENESS AXIS PROJECTS

Degree of Progress	-	→	→	+
Initiative / Stage	**D**	**FM**	**E**	**C**
Transport	6	n.a.	16	0
Telecommunications	6	1	0	0
Energy	3	3	6	2
Trade and Competitiveness	2	1	4	1
Tourism	0	3	3	0
Total	*17*	*8*	*29*	*3*

Notes: D: Design; FM: Financial Management; E: Execution; C: Complete; n.a.: not available.

Source: Based on PPP information [2006], June 2005-June 2006.

Of all the projects it contains, the construction of the Pacific Corridor stands out. This is an alternative to the Pan-American Highway (*Carretera Panamericana*) running from Puebla to Panama and has an approximate investment of US$ 1.4 billion. This roadway is highly significant for the region's trade integration, as it will create a road that meets international standards, reducing the distance between the two points by 300

77 The number of projects may change, as may the projected investment for their execution. These figures are up to January 2006 (Source: PPP. http://www.planpuebla-panama.org).

78 Budget percentages are divided among the initiatives as follows: Transport 80.13%; Energy 8.95%; Telecommunications 0.80%; Trade and Competitiveness 0.28%, and Tourism 0.04% (PPP [2006]).

79 The financing already obtained for the transport initiative is equivalent to almost 50% of the total scheduled for the entire plan.

80 The state of the human development axis or its constituent process of project execution were only considered in cases where the PPP is discussed as a unitary mechanism.

81 Like the methodology for the approval of new projects, the complete listing of the criteria can be consulted online at the PPP's official site. Two examples of the criteria are promoting Central American integration and at least three member countries becoming involved (Source: General PPP Criteria. "¿Cómo gestionar proyectos?", available at *http://www.planpuebla-panama.org/main-pages/metodologia-proyectos.htm.*

82 Of the 17 projects at the design stage, 6 are Transport-related, 6 Telecommunications-related, 3 Energy-related and 2 Trade and Competitiveness-related (PPP [2006]).

kilometers. Road access will be complemented by arteries and corridors developed under other national or regional projects that will connect both air- and seaports, tourist areas and population centers.

Certainly, there are other initiatives not yet incorporated under the PPP that will bring benefits for trade integration, if consensus is reached over their inclusion. There is the construction of the regional fiber optic network, the development of regional rail and air- and seaport systems, the regional coordination of strategies for technology updating, or for the development of private national trade research institutes.[83]

This leads us to conclude that the PPP's reported impact on Central American integration should not only be considered in terms of obtaining tangibles such as roadways. Important intangibles have already been produced or are at the implementation stage, such as the Harmonization of Phytosanitary and Sanitary Standards project (*Armonización de Normas Fitosanitarias y Sanitarias*), the Modernization of Customs and Border Crossings (*Modernización de Aduanas y Pasos Transfronterizos*) or the Meso-American SME Support Program (*Programa Mesoamericano para Apoyo a PyMEs*), which are of equal importance to the region.

The next 5 years represent a great challenge for the PPP, mainly in terms of integration. During this period, the mechanism must successfully complete and renew much of the current integration portfolio, and redefine the direction to be taken in the context of an agenda covering a Central America more committed to CU, the wholehearted implementation and application of DR-CAFTA, a North American Free Trade Agreement (NAFTA) eroded by the bilateral preferences agreed in recent years, an FTAA in a state of lethargy, and the explosion of preferential bilateral agreements signed by the members of the Plan.

It may be advisable in this discussion of the PPP to mention certain key areas to achieving better functional integration in the region. In order to promote integration it may be important to incorporate other institutional actors and reinforce their presence in the process. Energy projects would, for example, benefit from the presence of the Central American Commission for the Environment and Development (CCAD - *Comisión Centroamericana de Ambiente y Desarrollo*). Telecommunications also need greater coordination. Although for the time being this issue should continue to be dealt with within the PPP, the ultimate objective must be to strengthen the Regional Technical Telecommunications Commission (COMTELCA - *Comisión Técnica Regional de Telecomunicaciones*). Improvements should also be made to the Sectoral Council of Ministers of Transport (COMITRAN - *Consejo Sectorial de Ministros de Transporte*) with a view to not only extending its functional scope to sea- and airports, but also its geographical range to partners other than the five CACM countries. Perhaps more in the spirit of the PPP. Lastly, the Meso-American Council for Competitiveness (CMC: *Consejo Mesoamericano de Competitividad*) can be strengthened to act as a forum for discussion of issues and initiatives to promote a better climate for business in the region.

There are still many issues to be broached in trade integration for Central and Meso-America, some of them in the realm of infrastructure. The PPP is in a position to be an ideal tool to move forward in these areas as a proven forum for reaching agreements and discussing at a high political and technical level important and complex regional initiatives that can benefit extensively from the presidential momentum. However, it should be borne in mind that the experience of recent years dictates that only those initiatives with clear regional benefits will be approved, and that, to be successful and sustainable, these must be accompanied by the strengthening of regional institutions in the relevant sector. The PPP may be a meeting point to discuss and implement certain advances in the regional process of trade integration, but the Plan's fate ultimately depends on the next meeting of Member Heads of State and Government.

[83] These plans are still at the study or discussion stage; only in some cases have preliminary or prefeasibility studies been made.

Contents

IV. CENTRAL AMERICA AND DR-CAFTA

Few trade agreements have had or will ever have the kind of scope and impact on the Central American subregion as DR-CAFTA. The Agreement's very contents and the economic and political importance of the United States for Central America make this instrument an unprecedented initiative in the subregion.

This chapter will not deal with the content of the Agreement, as this was done in the last version of this Report (INTAL [2004]). There are also many summaries of it available (e.g. IDB/ECLAC/OAS Tripartite Committee [2005] and Costa Rican Ministry of Foreign Trade [2004]). Nor is this the occasion to tackle issues related to the effects, opportunities and challenges posed by the Agreement for the subregion's countries, a subject about which, despite a lack of concrete conclusions, much has already been written (e.g. WB [2005a], USITC [2004], Salazar-Xirinach and Granados [2004], Todd, Winters and Arias [2004], Agosin and Rodríguez [2005], RUTA Project [2006] and Giordano and Vialou [2007]).

This Report will therefore limit itself to a brief look at the five most prominent aspects of DR-CAFTA in 2004-2006: (1) the difficulties of the process of DR-CAFTA approval in the Central American countries; (2) the processes of the Agreement's implementation; (3) its initial effects; (4) the problems of complementary agendas; and (5) DR-CAFTA's potential impact on Central American integration.

A. Difficulties in DR-CAFTA Approval

The discussion surrounding DR-CAFTA has always been complex in all the countries. Although it was supported by very important sectors in the region, the Agreement has always been opposed by certain sectors who feel directly affected by its process of liberalization. It is also criticized by other sectors of civil society that see DR-CAFTA as a supposed threat to public health, the environment and social and labor-related advances, or by certain academic sectors hold doubts on the benefits of the current development model, that is, the strategy of insertion in the global economy, and who see in the Agreement its clearest expression, as indeed it is it.

DR-CAFTA was signed by the seven countries' Executive Powers on August 5, 2004. The state of legislative approvals and implementation of DR-CAFTA at the end of 2006 are shown in Table 22.

TABLE 22
DR-CAFTA APPROVALS AND IMPLEMENTATION
(To December 2006)

Country	Legislative Approval	Votes (For/Against)	Implementation
El Salvador	December 17, 2004	49/30	March 1. 2006
Honduras	March 3, 2005	124/4	April 1, 2006
Guatemala	March 10, 2005	126	July 1, 2006
United States	July 27, 2005 (House of Representatives)	217/215 (House of Representatives)	See dates for individual countries
	June 30, 2005 (Senate)	54/45 (Senate)	
Dominican Republic	September 6, 2005	118/4	Pending
		20 Abstentions	
Nicaragua	October 11, 2005	49/37	April 1, 2006
Costa Rica	Pending	Pending	Pending

Source: Based on press and SICE information.

Unlike the several formally similar trade agreements negotiated in the past by the Central American countries, DR-CAFTA has always been at the center of a war of words (though to a far lesser extent today) and even mass demonstrations in the streets of all the Central American capitals. With the United States as a counterpart, this opposition contained shades of ideology.

Furthermore, the vast majority of sectors supporting the Agreement are made up of business sectors -no longer just the export sectors, but others that will even take on US competition in the medium and long term- and of associations and similar schools of thought close to the process of trade opening in the countries. Private chambers and other union associations have come out in favor of the process. Certain sectors of labor in the export industries have also expressed their support.

In certain countries like Nicaragua and Costa Rica, the difficulties were magnified even further when debate of the Agreement coincided with elections -always an occasion for heated argument between the various political factions about the issues of the day. This led to the politicization of DR-CAFTA in these two countries, which hindered a straightforward discussion based on the merits and demerits of the initiative.

In Costa Rica, where approval was a very long-drawn-out process, the debate has been hindered exponentially, as all these factors converged with a highly effective mobilization of oppositional forces from the public union sectors, while the previous Pacheco Administration (2002-2006) -which negotiated the Agreement- played a very passive role in the efforts to win legislative approval.[84] In addition, certain political figures (including two former presidents) and factions from the traditional parties have also openly expressed their dissatisfaction with the Agreement.

In May 2006, the Arias Administration (2006-2010) inherited a body of public opinion highly divided over DR-CAFTA and had to undertake the tough task of negotiating its approval by the Legislative Assembly, along with the Agreement's 13 implementation laws and a complementary agenda.

Discussion of the Agreement has become more difficult in Costa Rica insofar as some of its commitments to liberalization involve the relatively rapid dismantling of state telecommunications and insurance monopolies, which had for decades been considered an example of effective state administration by certain sectors (public unions and others). However, although other sectors like investors or consumers acknowledge the virtues of the model of state intervention, in their view these issues had recently become bottlenecks for development and they therefore supported their dismantling. The other DR-CAFTA countries clearly were not faced with a political challenge of equivalent complexity in approving the Agreement, as they had already implemented unilateral liberalization and privatization processes in these important sectors in the past. In Costa Rica too, previous governments -like that of Miguel Ángel Rodríguez (1998-2002)- had failed in the attempt to promote telecommunications and insurance opening, a process that had already left a first trail of confrontation and opposition to these issues.

The process in the Dominican Republic has also been complex. As we saw above, despite the Agreement being approved by the Legislative Power on September 6, 2005, its implementation has been delayed due to the appropriate implementation laws not being passed. We will come back to this.

The processes of legislative approval were tempestuous and carry on being so in countries where they are still underway. The most common criticisms range from arguments about the dizzying speed and lack of consultation over approval, about shady deals and political pacts, about the Agreement being yet another expression of a global insertion model that has generated no widespread results, to the absence of accompanying policies in the Agreement. The approval processes, however, seemed to have been carried out within the countries' individual frameworks of institutionality and legality, although many legislative

84 President Abel Pacheco limited himself to sending the Agreement to the Legislative Assembly on October 23, 2005.

regulations were certainly interpreted and manipulated to the limits of their tolerance. The DR-CAFTA approval process in the United States was no exception to this, as a great deal of maneuvering from the Bush Administration was needed to get the amount of votes required for the Agreement's approval, especially in the House of Representatives (Wall Street Journal [2005] p. A2).

In general terms, the effects of the difficulties and delays in approving DR-CAFTA have been felt more keenly in those countries where approval was more prolonged. In Costa Rica, where the situation is more critical, the domestic private sector overwhelmingly expressed its frustration. The newspapers also tell of cases of enterprises pulling out of the country in order to relocate in countries that had already approved the Agreement. This happened with a zipper manufacturer that decided to move to El Salvador, as the DR-CAFTA rule of origin would probably not have allowed the manufacturer to sell garments containing these zippers made in a country that was not at the time part of the Agreement -even if the garments had been put together in other DR-CAFTA countries. Even though other considerations may have influenced the business decision, it is highly likely that the DR-CAFTA trade preference and its potential for input accumulation were significant factors. There have also been cases of high-tech enterprises suspending new investments until such time as the Agreement comes into effect.[85] The effects of this delay, however, do not seem to have been serious, though they may end up being if the impasse in that country continues.[86]

In a word, public debate surrounding DR-CAFTA was triggered by a convergence of factors:

i) The clash of perceptions harbored by those who see themselves as winners and those who feel vulnerable to an economic opening agreement with the major trading partner and investor of all the countries in the region and the Dominican Republic. This process offers opportunities for exporters (e.g. textile manufacturing, agriculture for export, high technology and tourism) and consumers, but is seen as a threat by certain productive sectors facing US competition, like agriculture for domestic consumption (e.g. rice, poultry, pork, certain dairy products, peanuts), food and drinks, light manufacturing and employees of state telecommunications and insurance enterprises. The latter were particularly effective in Costa Rica in mobilizing sectors of public opinion and other public unions against the Agreement.

ii) This led to a fragmentation of public opinion and eventually the politicization of the debate. In this context, ruling parties and opposition feel the need to risk serious political capital in this debate. The politicization was considerably greater in countries where the process has been postponed and/or countries that have had to undergo electoral processes.

iii) The presence of strong ideological dimensions surrounding the debate: these are the result of the supposed economic, environmental and social impact of the negotiation and of the fact that it involves the United States, an issue that has always triggered controversy in Latin America.

B. DR-CAFTA Implementation Processes

The process of the Agreement's approval was also followed by highly complex implementation processes.[87] DR-CAFTA's wide-ranging and ambitious contents meant that its launch would demand a great deal of work, particularly for the Central American countries and the Dominican Republic, albeit with the permanent monitoring and cooperation of the United States.

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85 Among more recent newspaper articles, see La Nación [2007].

86 On the costs associated with non-approval of DR-CAFTA in Costa Rica, see the ideas in IDB [2006c].

87 By "implementation" this Report means the tax of setting the Agreement in motion. This involves preparing public administrations, drafting new laws and legal and regulatory reforms to execute the Agreement's initial commitments (other commitments have been back-end loaded, sometimes for several years), and implementing the new legal provisions. It also includes the function of educating private sectors and civil society at large on specific issues in the Agreement. This Report will not, however, be commenting on this function.

In general terms, besides being an ambitious trade opening process, DR-CAFTA can be characterized as a process of north-south regulatory and institutional migration. In other words, through the Agreement, the Central American countries and the Dominican Republic committed to adopting a series of legal institutes and new legal concepts applicable to almost all matters. Areas like transparency, non-discrimination, the administrative and legal responsibility of the State, the administrative processes of prior consultation, trade facilitation, automation and electronic government, monitoring of effective compliance with legislation and so on constitute well-consolidated legal institutes and concepts in the United States. But this is not the case in all Central American countries or the Dominican Republic, nor to the full extent laid down in the Agreement.

Many of these legal institutes and concepts obey good practices and principles of good public policy in general. Under these circumstances, DR-CAFTA has clearly been received as an institutional development effort in the Central American countries and the Dominican Republic. As we have pointed out, some of these institutes are not new to these countries' legislations and their implementation is therefore quite a lot easier. However, many of the institutes and concepts have to be consolidated and strengthened even further in order to reach the stage of what the Agreement demands. This, however, normally happens because of the issue of strengthening the human, technical and financial resources to perform the relevant tasks.[88]

Other institutes and concepts, however, are totally new and -at least some of them- obey specific policy preferences on the part of certain sectors in the United States that wield a deal of influence in Congress and over the Executive Power, on issues of intellectual property, for example. This hampers their implementation slightly, as they are somewhat alien to the Central American environment and belong to more developed institutional setting, such as the United States.

In any event, broadly speaking, the DR-CAFTA implementation process can be divided into three basic stages: (1) determination of the set of measures forming the customary minimum required to set the Agreement in motion; (2) design and implementation of this set of measures; and (3) verification by the trade authorities of the remaining DR-CAFTA countries that the measures have effectively been adopted in each country.

For the first stage, the seven countries held joint bilateral meetings to determine the total set of measures to be adopted for the Agreement's entry into effect. To do this long lists of each country's commitments were drawn up. Furthermore, measures were established whose implementation each country considers more important in each of the other countries. This was essentially a closed discussion process between the seven trading partners where levels of participation varied substantially, with the United States very much in control of defining which topics are high-priority and which are to be implemented as such in the remaining countries.

The second stage constituted a mainly national process, although to bring it to fruition the Central American countries and the Dominican Republic received -and still receive- technical and financial consultancy from international development and funding organizations like the IDB and the Central American Bank for Economic Integration (CABEI), as well as the United States Agency for International Development (USAID). The remaining six countries can also bring up their observations at this stage about the contents of the laws and regulations of the Agreement's implementation although, again, the US trade authorities followed this process in each country very closely.

[88] Bearing in mind these needs, DR-CAFTA has a chapter on cooperation over trade capacity building to follow up and track down answers to the problems identified. Save in the case of labor and environmental cooperation, where the United States has undertaken to offer the region US$ 40 million a year over five years, DR-CAFTA does not, however, include a specific, explicit promise from that country to generate fresh cooperation funds.

The third stage -the stage of verification by the trade authorities of the other countries in the Agreement that a member country is implementing the text satisfactorily- consists of verification that the conditions agreed for implementation are in place and a date subsequently set for the Agreement to come into effect.

Each of these three stages had and continues to have significant degrees of complexity, explained by a lack of development of the institutional capacity for their realization. In Central America and the Dominican Republic, albeit with varying degrees of intensity, many of these difficulties are associated with the endemic problems of lack of financial resources, lack of specialized human resources (in part due to the fact that some of the Agreement's negotiators-supposed experts in its details- for one reason or another, no longer work with the governments) and lack of organizational capacity. Other difficulties, in particular the delays in approving laws and other international agreements required by the Agreement (on intellectual property, for example) are explained by the customary complexities of the political and legislative processes of some of these countries, notably the Dominican Republic and Costa Rica. As we have seen, the approval processes have not been easy and have generated social and political polarization, which has further repercussions for the Agreement's implementation.

Implementation has been delayed in the Dominican Republic because the United States stated the need to approve certain international agreements, laws and regulations in the verification process as a prerequisite for the Agreement's entry into effect, mainly in areas such as intellectual property, taxation, public sector purchasing and trade distribution. The Caribbean country has gradually approved this additional legislation (or amended existing legislation to meet its commitments to DR-CAFTA) and it is hoped the Agreement will come into effect in early 2007.

As we have mentioned, the other countries' trade authorities have the option to monitor the internal processes of the second and third phases. The United States has been very proactive in exercising this prerogative. Indeed, this country makes of it not only an expression of support and guidance in many of these matters, but also a mechanism to influence the direction and effectiveness of the de rigueur minimum of high-priority measures, and their content and approval. And, as is customary in the ratification processes of international agreements, the US authorities set a specific date for the Agreement's implementation in agreement with the relevant country, when and only when they are certain the appropriate implementation measures have been adopted. This explains the differences in the dates of the Agreement's entry into effect between the United States and the other countries that have implemented it to date.

This strong presence of the US Government at the implementation phase -which, as pointed out, is the prerogative of any subject of international public law when negotiating agreements- shows that the United States does not want to let things happen at the other governments' pace or according to their vision. Instead, it is taking advantage of the momentum and expectations involved in the imminent approval of the Agreement to ensure the main committed measures of interest to it are effectively and satisfactorily implemented in the other six countries. The trend here is, perhaps, to seek compliance with obligations through the efforts to take advantage of the immediate opportunities created by the Agreement, instead of possibly having to resort to forcing compliance via the relevant dispute settlement mechanism. In addition, the United States is seeking the most immediate progress possible on the enjoyment of the concessions and disciplines negotiated to provide US exporters and investors with effective business opportunities which, among other things, will help to offset the domestic political cost of the Agreement.

Such approaches also help clarify the existence of some of the most important concessions the Agreement has scheduled for each country for the stage immediately after approval: a political economy of pressure is generated through implementation of the Agreement and internal dynamics are thus set up, favoring the entry into force of implementation laws and regulations that would otherwise be more difficult to approve.[89]

Last, it is necessary to point out that the practical difficulties in the Agreement's implementation have also arisen in the United States. In the area of textiles and clothing for example, Salvadorian exporters reported problems at US customs in the early days of the Agreement's entry into effect. Indeed, there were cases of goods shipments dispatched in order to benefit from the Agreement's preferences and having to pay import duty on entering the United States.[90] The US customs had to issue alternative guidelines and procedures for DR-CAFTA on March 3, 2006, as this authority had not updated the automated tariff systems. The problems were soon solved. Yet this comment is still valid in that it points up the difficulties inherent in the implementation of complex trade agreements, a situation also experienced in countries with greater resources and institutional development like the United States.

As shown above, the countries were not alone in this implementation process. International financial organizations -among them the IDB- supported this implementation stage via non-reimbursable technical and financial cooperation at national and regional levels. The IDB has also provided financing programs for most of the countries for the Agreement's negotiation and implementation, and/or the stage of transition to free trade. The funding of essential items in the complementary agendas was an important component in this support. Box 3 includes the IDB's main support initiatives for the negotiation, implementation and transition to DR-CAFTA in the Central American countries and the Dominican Republic.

To conclude this section it is worth remarking that the difficulties in implementation are highly likely to continue for some months or even a few years longer. They are due, in short, to a combination of factors: the difficulties inherent in DR-CAFTA's regulatory complexity and the ambitiousness of its scope, the inadequate institutional development of the Central American countries and the Dominican Republic including funding problems, pressure from the United States on these countries to comply with certain measures -whether committed to in the negotiation or not- as a prerequisite for the Agreement's entry into effect, and the complexities inherent in each individual country's governance and political difficulties.

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89 This prerogative of "verification" was also exercised by other countries in the subregion on other occasions in their negotiations with each other. Costa Rica, for example, postponed implementation of the FTA between Central America and the Dominican Republic in its territory for almost two years because it was not happy with the implementation of certain tariff-rate quotas in the Dominican Republic negotiated in that country's favor. The underlying logic of these situations is that one has to take advantage of the current climate in order to secure a good launch for the respective trade agreement and thus avoid problems in the future. As a prerequisite in negotiations with other countries in the hemisphere, the United States requested the solution of certain problems faced by its investors in those countries. However, most Central American negotiators agree that the United States exploits the current climate to demand from the countries the approval of other mechanisms and provisions not included in the text of DR-CAFTA. The best example of this is the issue of certain sanitary and phytosanitary understandings that had to be adopted by the countries implementing the Agreement. Under these understandings, the countries are to accept as adequate the sanitary certifications issued by the respective US authorities when the US exports certain agricultural products. When importing such agricultural products, on the other hand, the United States will not accept as adequate certification issued by the Central American health authorities, but may demand additional sanitary requirements, including onsite inspections and processing plant certification by the American health authorities and so on and so forth (Inside US Trade [2006]).

90 Information provided by the El Salvador Exporters Corporation (COEXPORT) in the News section of their web page at *http://www.coexport.com*, March 10. 2006.

Box 3
IDB SUPPORT FOR DR-CAFTA

The IDB has set out to confront the challenges emerging from the negotiation of DR-CAFTA, both for the seven countries as a whole, and for the Central American countries and the Dominican Republic. The IDB has implemented both financial and non-financial initiatives.

Non-Financial Operations

Analysis

- -Main challenges and opportunities for DR-CAFTA
- -Potential impact of DR-CAFTA on the rural economy
- -Legal modifications required for implementation of DR-CAFTA
- -Integration Research Network (RedINT)

Development of National Plans of Action

- -Definition of national plans of action
- -Execution of the national plans of action

Training

- -Computable general equilibrium model
- -Challenges of DR-CAFTA and the national agenda
- -DR-CAFTA regime of origin
- -Sharing information with Congresses
- -Support for El Salvador negotiation

Dissemination of information

- -Video on DR-CAFTA
- -Comparative study of DR-CAFTA and Chile's FTA with the USA

Technical and logistical support

- -Coordination of institutional donors in DR-CAFTA negotiations

Regional Technical Cooperation in support of DR-CAFTA's labor aspects

- -Regional Technical Cooperation for training judges
- -Regional Technical Cooperation - Promotion of a Culture of Compliance

Regional Technical Cooperation in support for implementation and understanding of the effects of DR-CAFTA

- -Support for implementation of DR-CAFTA's Chapter on Intellectual property
- -Support for implementation of Tariff-Rate Quotas and Application of Special Agricultural Safeguards
- -Support for Agriculture Ministries' Policy Units
- -Strengthening of national and regional capacities in trade and the environment in the context of DR-CAFTA
- -Assistance to Central American SMEs on technical requirements of market access under the Central America-United States FTA
- -Opportunities and technical requirements of market access under the DR-CAFTA FTA
- -Improving competitiveness of textile and clothing industry
- -Impact of DR-CAFTA on prices of drugs: AIDS

National Technical Cooperation

- -Support for Honduran Government over DR-CAFTA implementation.

Financial Operations

Investment loans to improve competitiveness

- -Costa Rica
- -Honduras

Trade sector facility loans

- -Guatemala
- -Nicaragua
- -Dominican Republic

C. The First Visible Effects of DR-CAFTA

Although it is still too early to make a first evaluation of DR-CAFTA (this will have to be done the moment reliable data become available), there is certainly evidence that the Agreement is beginning to generate certain benefits. The evidence is at present anecdotal and should not give way to grand-sounding generalizations. Indeed, early indications are beginning to show rising exports to the United States, the establishment of investors wishing to take advantage of Central America's conditions and the Agreement's tariff preferences, job creation, improvement of certain countries' country risk classification in international debt markets and improvement of certain trade procedures there.

Some examples are listed below:

1) *Rising Exports to the United States*: Nicaragua's exports to the United States in 2006 were 24% up on 2005. Although this increase is not entirely due to the Agreement, it has helped substantially. DR-CAFTA quotas for Nicaragua on meat and sugar were, for example, utilized to the full. Exports of non-traditional agricultural products from El Salvador to the United States were also up on the previous year. In particular, the area of mini-vegetables like okra rose by over 25% to US$ 555,000 in 2006 (Salvadorian Ministry of Economy [2006]). Though not spectacular, this shift is important for El Salvador's rural producers and could be the start of an export boom in this sector. The situation in Honduras and Guatemala is similar.

2) *FDI*: In Nicaragua, ITG-Cone Denim announced its plans to invest US$ 100 million in a new denim plant to take advantage of its being the only Central American country to have negotiated a TPL. This mechanism allows local industry to use up to 100 million Square Meter Equivalents (SMEs) of cloth from any part of the world to assemble garments in that country and still comply with the rule of origin required under DR-CAFTA to obtain tariff-free access in the US market. Since the Agreement came into effect, a dozen fabric and clothing manufacturers have followed ITG-Cone Denim and confirmed new investments in Nicaragua of around US$ 256.5 million as ProNicaragua, Nicaragua's investment attraction agency, informs. There seems to be the same enthusiasm in other sectors like financial services, where mergers and acquisitions have entered a new stage of dynamism. This year, for example, HSBC acquired the Banistmo Group, a leading banking group in the region with operations in Panama, Colombia, Costa Rica and Nicaragua. Stephen Green, the President of HSBC Holdings plc, is on record as saying, "This exciting event will give HSBC a strong presence in a fast-growing economic region which, with the ratification of CAFTA, has great promise" (ProNicaragua [2006]).

3) *Job Creation*: Recent statistics from the Guatemalan Apparel and Textile Commission (VESTEX) show that employment has risen in the sector. At the end of 2006, the sector had 3,000 new direct jobs as against the previous year due, in the opinion of factory owners, to approval of DR-CAFTA. The number of new indirect jobs is estimated to be similar. This is a response to new orders from US buyers. Furthermore, new investors are expected to generate many more new jobs. According to ProNicaragua, the incoming investment could soon create around 8,650 new jobs.

4) *Improvements to Country Risk Classification*: Invest in Guatemala, the Guatemalan national investment attraction agency, says that Standard & Poor's (S&P) has reclassified Guatemala's country risk from BB- to BB. Roberto Sifon, an S&P executive, stated that several factors contributed to this positive reclassification, particularly the entry into effect of DR-CAFTA. Other risk classification firms did the same: Fitch reclassified Guatemala to BB+ in February 2006 and Moody's to BA2 in May of the same year (Invest in Guatemala [2006]).

5) *Improvements to Trade Procedures*: In preparation for DR-CAFTA, the region's countries have simplified and improved trade procedures and strengthened trade institutions. With IDB support,

> Nicaragua, for example, is now offering on-line export procedures. Exporter no longer have to stand in line for hours with armsful of documents. This has positive repercussions for operators exporting to the rest of the world. It also has a significant demonstrative effect regarding the virtues and potential of electronic government in both the country and the subregion as a whole.

There is further evidence of positive impacts. In Guatemala, for example, the number of enterprises registering in the Commercial Registry in 2006 was up 15% on 2005. The Registry's Director, Arturo Saravia, explains that the rise is due to implementation of DR-CAFTA, as a perception among informal enterprises has spread that the Agreement has brought trade opportunities that can be exploited, which is more feasible through formalized enterprises. This reinforces the idea that the Agreement may be helping to strengthen the institutionalization and formalization of the subregion's sectors.

All this helps to create a positive attitude in investors and business people both inside and outside Central America. In other words, there are clearly legible signs that the business climate is beginning to change for the better. In addition, DR-CAFTA and the other trade agreements already signed make opening policies more difficult to reverse. Such regulatory stability gives investors confidence, even with the advent of governments with differing views. This was one of the positive impacts forecast for DR-CAFTA.

It should be remembered, however, that in the medium and long term, we must also expect other less favorable sectoral impacts when the existing trade protection falls as a result of DR-CAFTA's tariff elimination program. This is nowadays a predictable, measurable and inevitable effect of any trade opening process. There will also be a need to evaluate the potential worsening of the trade deficit and its macroeconomic impact, as well as the possible effects of disinvestment deriving from trade rerouting: some regional production could be displaced by imports from the United States. Central America will be faced with the serious challenge of dealing with such scenarios and this is bound to be an issue of prime importance for the subregion in the near future.

D. The Problems with Complementary Agendas

There is a general perception in the subregion that free trade is a necessary but insufficient condition for promoting national and regional economic development. One or more FTAs are unable by themselves to create the conditions necessary to promote sustainable economic growth. It has been said time and again that FTAs are not a panacea for development. Having recognized this, the countries have understood that it is essential for the Agreement to be accompanied by other public policies that help to maximize opportunities and minimize sectoral and social vulnerabilities. To do this, the most sophisticated visions have considered it important to work on three main fronts: (i) a healthy and appropriate macroeconomic framework; (ii) a set of microeconomic interventions that foster the better use of the opportunities presenting themselves; and (iii) a social development strategy that helps to counter social vulnerabilities -all in the context of sustainable development. Once these conditions are properly resolved, DR-CAFTA can be a real instrument for development and growth.

Of course, this is where the easy rhetoric stops. The difficulties arise when it comes to determining the specific actions to be taken and their means of funding. Defining and executing this in the current contexts of governance and institutionality in Central America and the Dominican Republic has proved to be an enormous problem.

Due to length of this Report, this section cannot look at countries individually.[91] Nor will it provide a summary of the state of the components of the countries' complementary agendas, due partly to the

[91] See the first attempts at systematization and analysis of the complementary agendas of DR-CAFTA made in 2006 in the context of the LATN Network (Red LATN), available at *http://www.latn.org.ar*: Meza [2006]; Arauz [2006]; Carrera [2006] and Ángel [2006].

problems inherent in these agendas described above. This section will restrict itself to making a brief generalization about the difficulties experienced by the governments of Central America and the Dominican Republic in participating in, defining, financing and implementing the complementary agendas, and to a brief mention of the main criticisms of these agendas.

It must be first remembed what a complementary agenda is and differentiate it from an implementation agenda. As it has been seen, an implementation agenda belongs to a set of measures including laws, regulations, policies and guidelines, designed to bring into effect and directly implement obligations and commitments arising from the Agreement. The implementation agenda is executed from such time as preparations to bring the Agreement into effect get underway until the fall of the last tariff twenty years after its entry into effect. Of course, most of the agenda's components are implemented during its first years of life. This includes training in the Agreement's contents for both public and private sectors. It also includes instrumentation of the Agreement, for example, updating automated trade information and processing systems in economy or trade ministries, one-stop-shops at customs and in other government institutions. It includes acquiring equipment to carry out these tasks, improving basic infrastructure and recruiting human resources, among other things. All FTAs and other trade agreements -such as the agreements of the Uruguay Round- required an implementation agenda.

DR-CAFTA is, however, the first trade agreement to be accompanied by major discussion of a complementary agenda. A complementary agenda is understood as a set of economic policy measures designed to create the conditions to exploit the opportunities in the Agreement and reduce the vulnerabilities directly arising from its application. It ultimately obeys the objective of tackling structural problems via different types of interventions, including physical trade infrastructure, vocational and technical training institutions, institutional strengthening to promote exports and attract investment, regulatory frameworks, improving the business climate (including such areas as promoting the rule of law, improving justice administration, greater protection of property rights including intellectual property, etc), adjustment funds for the transition to free trade, reinforcement of provisional systems for displaced workers, strengthening the capacity to adopt contingent protection measures, modernizing customs, improving domestic sanitary and phytosanitary management, and any other area or sector where DR-CAFTA can have an effect and which requires government intervention either to boost opportunities or reduce vulnerabilities.

The first problem with DR-CAFTA's complementary agendas was one of participation in defining them. This process ties up with the dynamic of the interaction between the Executive and Legislative Powers in their negotiations and with the participation and influence of the other actors gravitating around it. Each country has its own mechanisms of civil and political participation -some more open than others, some with more proactive civil societies than others, all with very strong participation in the most affected private sectors or benefited by the process of trade opening in general. Where the process was more closed, there were fewer problems in setting the agendas' contents. Naturally, such exclusion constitutes the first serious problem. In countries where the process is more open and participative, the problem has always been how to reach consensus over the agenda. As it is impossible to please all sectors, the classic dilemma of political economy inevitably arises, namely, the distribution of the Agreement's benefits and costs.

The second problem -closely related to the first- was determining the agendas' components. Here many and various questions arose: determining what is urgent and what not, what the correct sequence, scope and depth of interventions is, balancing the pressures and demands from productive sectors who feel affected and are calling for compensation, defending the interests of more vulnerable and less articulate sectors of society, and so on. Again, as happens with any political process, participation or exclusion largely determine the contents of complementary agendas. There are countries where the content is essentially aimed at maximizing opportunities rather than minimizing vulnerabilities, the private sector having far more influence over political decisions than the social sectors affected. As a result, the sectors affected have pointed out the lack of supportive measures. They accuse the government of being partial and emphasize the injustice and inconsistency of the agendas.

As we have seen, both the participation and determination of the contents have had to go through the countries' ordinary processes of political decision-making and this has thrown into relief the limitations and problems of governance they are experiencing.

The third problem, which has had a fundamental impact on the contents of agendas in some countries, is to determine the likelihood of financing these agendas. As shown, some of the programs of a complementary agenda are extremely expensive and long-drawn-out. Consequently, defining how to cover costs is essential to their success. A mixture of sources has been utilized to date, including funds of their own, non-reimbursable international cooperation and external funding. But new problems soon arose. Indeed, the limitations immediately arising are due to the short supply of fiscal and cooperation resources in the first and second case, and the capacity for external borrowing in the third. There are countries like Costa Rica, whose chronic tax deficit does not grant them the budgetary flexibility for wide-ranging undertakings in these complementary agenda areas. The impossibility of far-reaching tax reform -again, for reasons of governance and lack of consensus- will seriously limit the ability to respond. Other HIPC countries like Honduras and Nicaragua have a low capacity for external borrowing and therefore also have a low capacity to respond to the challenges ahead.

The fourth problem has been the poor quality of implementation of some of the components of the complementary agendas. Not only do the above funding problems influence their viability, implementation and success, but the lack of clarity and articulation of these components often tarnishes good results. When hard-to-satisfy expectations are created among sectors, new frustrations and dissatisfactions arise that may have a negative impact on appraisals of the Agreement and its results. Nicaragua's complementary agenda, for example, has an adequate general guideline and components of great importance for the proper use of the Agreement, but many of these ideas are extremely general and not appropriately articulated and specified, that is, how the activities will be performed or with what funds (DR-CAFTA [2005]). They are consequently difficult to manage.

As can be seen, there is a very narrow dividing line between a DR-CAFTA complementary agenda and a national development plan. This comes as no surprise, for the Agreement is extremely far-reaching as an instrument of trade liberalization and adoption of new standards and procedures for implementing many trade and investment-related procedures. Its impact will be general in terms of sectors, widespread in terms of territory, deep in terms of policies and long-lasting in terms of chronology. Therefore, approaching its main challenges and opportunities involves rethinking a significant number of policy and economic development goals. In all other respects, complementary agendas cannot be called on to solve instantly and with a single expedient the factors that have stood in the way of the region's growth for decades and that have perpetuated poverty and high distributive inequality. It is obvious but necessary to make the observation that the region's economic and social problems predate DR-CAFTA in their origin by quite some way. The main structural difficulty lies in the fact that there is no political or financial regime capable of assimilating and processing so many demands simultaneously. Furthermore, exceptional political leadership is required to handle so many weighty variables and to lead both public and sectoral opinion down the same road. These difficulties have meant agendas are criticized as incomplete, insufficiently funded, inconsistent and, in some cases, unexecutable.

We should remind ourselves at this point that the most emphatic effects of DR-CAFTA will come in the medium-to-long term. There is an element of excess when sectors demand the immediate solution of specific problems to tackle negative effects of DR-CAFTA that will emerge in eight, twelve, fifteen or twenty years. It is highly likely that governments will seek to solve the most serious problems in good time. It is extremely hard politically and financially to solve everything at the outset. For these reasons, it is advisable to see complementary agendas as dynamic, long-term processes that are not fully defined now, but which must be the subject of periodic rethinks based on the needs and political and financial contexts of the moment. The Agreement's fiscal costs are already well-known, as mentioned, and substitution of fiscal resources is an area into which government attention can be channeled in search of effective answers.

Finding a solution to the problems is no easy task. Perhaps the best blend for success is to have the economic wisdom to diagnose problems of this nature and find the best answer with the few available resources, as well as to have the political wisdom to balance so many disparate interests in the appropriate timeframes. A framework of broad participation is essential, but breadth must not breed inaction. Strong leadership is indispensable in coordinating complementary agendas coherently in parallel with the Agreement's implementation. As most of the most sensitive trade commitments -like agricultural tariff elimination- are very long-term, there is time to work on these programs. It will be important to appropriately synchronize the programs with the opening commitments. To do this it will be vital to keep the channels of communication and coordination with the productive and social sectors affected by the Agreement open.

These lessons of the DR-CAFTA process must be capitalized on if the complementary agenda of the EU Association Agreement is to be tackled more efficiently. In this sense, poverty and sustainability impact assessments, before, during and immediately after the negotiations can help identify the elements of a possible agenda with clearer definition of the actors, problems and policy interventions needed. In addition, this kind of evaluation can help to state more precisely the scope of cooperation to be granted by the EU in the context of the Association Agreement.

E. DR-CAFTA's Impact on Central American Integration

An initiative as wide-ranging as DR-CAFTA is bound to have a major impact on the intra-Central American integration process. This section briefly discusses this dimension, which is also not without its controversy.

DR-CAFTA will have both a real and a formal impact on Central American integration. However, it is important at the outset to say that the issue has created opposition. There are those who feel DR-CAFTA will create difficulties in improving CU. Those holding this belief argue that the existence in DR-CAFTA of tariff elimination programs with certain differences by country (sensitive products that will not be subject to tariff elimination in identical timeframes, or different exclusions -for example corn in Guatemala, Honduras, Nicaragua and El Salvador; or potatoes and fresh onions in Costa Rica) means that it will be virtually impossible to agree a CET for these products.

On the other hand, there are those who claim the Agreement will have a positive general impact. Although such differences are recognized in the tariff liberalization schedules, which do not effectively provide the option of agreeing a CET in the short term, the fact that these very products are subject to tariff elimination models with the main trading partner of all -the United States-[92] represents what has perhaps been the most powerful catalyst in finalizing a CET in the subregion in the long term. The 5% of products pending harmonization are virtually the same as those over which the countries negotiated different timeframes for tariff elimination. This is why there is already a light at the end of DR-CAFTA's tunnel. As shown when reviewing the issue of advances in the CET of the CU, DR-CAFTA can serve as a guideline to complete harmonization of this 5% -though definitely not in the short or medium term. There are also further arguments, as we shall see further on.

[92] Except for the above exclusions of corn, potatoes and fresh onions.

As mentioned earlier, DR-CAFTA is a centripetal force in Central American integration insofar as the multilateral nature of its application and the accumulation rules of origin make it so. We will now explain these concepts.

By "multilateral" application, it should be understand that the Agreement is mandatory for the seven DR-CAFTA countries. In other words, any single country can demand compliance from the other six. This "multilaterality" differs from the "bilaterality" of other agreements negotiated jointly by Central America like, for example, those with the Dominican Republic in 1998 and Chile in 1999. These two agreements are applicable between each individual Central American country and each of the two trading partners. In other words, while one Central American country can demand compliance of another Central American country with the obligations of DR-CAFTA (precisely why it is considered multilateral), it is not possible to do the same kind of thing in the context of the agreements with Chile and the Dominican Republic. This has important formal and trade repercussions, for the multilateral nature of DR-CAFTA establishes de jure intraregional trade disciplines in areas where previously there were none, for example, in public sector purchasing, trade in services, the treatment of foreign investment, or labor and environmental standards.

In this respect, it has been claimed that DR-CAFTA sets a new floor in these areas (González [2005]). This interpretation is true, but it must be qualified. By making these chapters of DR-CAFTA its own and applying them in the intra-Central American milieu, the subregion has not adopted a new floor but a new framework with lateral and upper limits. With this decision, Central America has not only set a floor it cannot go below, but has also built walls and a ceiling that it may find very hard to go beyond. It has adopted a regulatory approach in these areas that may preclude other national or regional policy options structurally incompatible with this approach. The repercussions of this issue should be studied more thoroughly.

Another repercussion of DR-CAFTA is that, by virtue of its multilateral application, Annex A of the General Treaty on Central American Economic Integration (*Tratado General de Integración Económica Centroamericana*) -which has already listed the exclusions to intra-Central American free trade for almost half a century) will cease to exist in the long term (no longer than twenty years) when DR-CAFTA moves these same products into free trade (with the exceptions of sugar and coffee, which have rightly been excepted).[93] This is also a positive consequence in favor of intra-Central American free trade and integration.

Furthermore, DR-CAFTA can contribute to deeper "real" integration, since the clause on accumulation of processes and inputs between the seven countries could boost effective integration for these countries' productive processes in order to export products of greater value added to each other, with certain exceptions. DR-CAFTA goes still further by allowing accumulation of inputs -subject to quantitative limitations- for the textile industry from Canada and Mexico.[94]

In short, on analyzing the effects of DR-CAFTA on regional integration, there would seem to be more arguments in favor of the positive and optimistic stance than the negative one. DR-CAFTA can galvanize the improvement of the CET in the long term (which would support improvement of CU), eventually establish a framework of very important intra-Central American disciplines, promote real integration by generating regional value added, and in the long term, help to remove the exclusions in Annex A. In any event, it is worth keeping a close eye on these issues in the years.[95] Central American integration is a regional public good worth looking after. As we saw in Chapter II, Central America -in aggregate terms- is the subregion's second largest trading partner, recently overtaking the EU. Consequently, both the

[93] For a more detailed explanation of this issue, see Granados and Cornejo [2006].

[94] This is extremely important, as it opens up a major precedent for the future convergence of trade agreements in the Americas.

[95] A new tariff negotiation with other trading partners such as the EU may once again hamper harmonization of the CET. The countries must therefore make a significant effort toward the coordination and convergence of the negotiation processes.

government and private sectors must give Central American integration attention commensurate with its importance, which is, as we have seen, considerable.

In conclusion, DR-CAFTA experienced serious difficulties in its approval and implementation in 2004-2006. It is still experiencing them. However, these phases are starting to be overcome by most of the governments that have implemented it and it is beginning to bear positive fruit, the improvement in the business climate being, perhaps, the most notable of these. The first elements of the complementary agendas has begun to be implemented and may start generating positive results soon. They are described by some as inadequate, lacking in funding and difficult to implement. Nevertheless, we should look at the agendas as dynamic programs to be periodically reviewed in sync with the Agreement's medium- and long-term effects. It is excessively demanding -and even unnecessary- to expect the effects of DR-CAFTA to be tackled today, when it will be years before they fully emerge. Finally, though the issue is a controversial one, it is reasonable to expect DR-CAFTA to have a positive net impact on regional integration in Central America. The landscape we have been viewing in this chapter forces us to conclude that DR-CAFTA is proving to be an extremely complex economic and political phenomenon that will go on testing the productive capacity of the business sector in Central America, the governance of the subregion and the leadership of its political class. There are lessons to be learned here for the upcoming negotiations with the EU.

V. CONCLUSIONS: OUTLOOK AND CHALLENGES FOR CENTRAL AMERICAN ECONOMIC INTEGRATION

Contents

The foregoing chapters have shown Central America is making significant efforts to finalize its FTA, step up CU and launch DR-CAFTA. The subregion is at the halfway stage on the road to economic union. But there is still a great deal of work to do to finish the task. This Report bears witness to the political will to move forward among Central American leaders, but also to the fact that major obstacles and contradictions remain ahead. This chapter summarizes the economic climate for integration, the perspectives of the process and the changes of tack needed to achieve true progress in intensifying Central American integration.

The Economic Climate: The global context was relatively benign for Central American economies during the period of reference, though less so than for other Latin American countries. The future may have greater challenges in store. A deceleration in global growth, especially in the United States, could check the momentum of Central American exports, remittances and FDI flows in a scenario where the oil price remains at record highs. The competitiveness of Asian countries in light manufacturing represents a challenge to Central American exports, even when they have preferential access from DR-CAFTA to US markets. A rise in interest rates could affect countries with greater need for public and private sector financing. This combination may aggravate the existing external imbalance. Countries must improve on this performance, which requires a combination of productive development, innovation and fiscal reform policies to stimulate internal saving and offset losses in customs revenue. The momentum toward integration, infrastructure development and access to markets of others countries is certainly positive. By themselves, however, these policies are insufficient and must be supported by complementary policies promoting systemic competitiveness, sustainable development and support for vulnerable productive and social sectors.

The Central American sector external is becoming increasingly important. Extraregional non-maquila exports and intraregional exports grew considerably, while maquila exports showed less momentum. However, the increase in exports did not halt the subregion's chronic foreign trade deficit, caused partly by deterioration in the terms of trade from 2000. Nor did this increase stop the downward trend in the subregion's overall competitiveness. In this context, intraregional trade flows recorded a high growth rate, averaging over 11% in 2003-2005. This upward trend has boosted the importance of the CACM as an export market, making it the main destination of non-maquila exports, slightly ahead of the United States. At the same time, the share of the EU as an export market has fallen away sharply. In 2005, it dropped to almost half 1990 levels. The great challenge lies in increasing exports within and without the maquila regime and their value added. It is becoming necessary to expand markets and renew the instruments of export promotion, including the participation of MSMEs in the export process. To make the region's comparative advantages more dynamic it will be important to strengthen technological innovation and labor training, facilitate financing for new productive activities and promote business development services. FDI flows to Central America rose sharply in 2003-2005 compared to the previous three years. However, if these flows are seen as a percentage of GDP, they are stagnant, well below the share reached in the late 1990s. The United States remains the main investor in the region, with almost half the total inflows, while the participation of the EU countries fell away abruptly to below 15%. Central America must capitalize on the opportunity presented by DR-CAFTA to generate opportunities for foreign investment. It is important to rejuvenate the institutions and instruments that attract investment. Finally, if the process of international insertion continues positively and the region is able to transform production and take advantage of these areas, the matter of the huge outstanding social debt could be dealt with more effectively. The Central American countries, both collectively and individually, require the implementation of policies aimed at the social protection of the most vulnerable groups, but also of those designed to create conditions of greater equality through education and health in order to participate in the job market.

Free Trade Area: Central America moved forward in improving its FTA. Intraregional trade is becoming increasingly dynamic, as we have seen. This can open up new opportunities for generating even more trade, strengthening regional productive chains and boost regional and foreign investment. Additionally, the regional market can provide a better springboard for MSMEs in their process of global insertion, at least in the early stages. This, in turn, can contribute to better vertical and horizontal integration of MSMEs in productive chains, which promises to contribute in one way or another to the eradication of poverty. The multilateral nature of DR-CAFTA, as well as its clause covering regional accumulation of inputs and processes can reinforce such potential. However, the trade authorities must redouble their efforts to remove any tariff and non-tariff barriers still in force, as well as developing aggressive trade facilitation initiatives and spreading trade opportunities offered by regional markets.

Customs Union. Central America is making significant progress in building a CU. However, it will take much clear thinking and leadership from the trade authorities in order to understand the demands involved in full CU and to have the mettle to implement them. It will require the substantial strengthening of the institutional capacity of many of the supervisory and regulatory agencies (sanitary, phytosanitary, environmental, customs, tax, etc.) that would perform many of the tasks required by a CU. It will take much more creativity and effort to mobilize the private sector in order to overcome the caginess today over the issue of harmonization of the remaining tariff lines to finalize the CET. The other trading partners with whom non-joint FTAs are already in place will have to be convinced that it will be necessary to begin a process of convergence or renegotiation -albeit in the long term- to bring domestic trade policies into line with the new paradigm of a Central American CU. A new legal framework will have to be defined to meet the new needs of the CU and set out a new institutionality according to the demands of the moment - an institutionality that may even require elements of supranationality. This aspect has been avoided in the subregion for many years, but its time is coming. It will be essential to significantly restrict any non-joint negotiations with third countries. None of this looks easy. The authorities should rethink this process by designing an appropriate critical path to reach their ultimate goal. A robust program embodied in solid legal instruments will generate the momentum necessary to continue moving forward, galvanize other cooperation efforts in functional integration and generate greater credibility for the efforts the subregion has been making at such great cost and for so long.

Preparing for DR-CAFTA: Central America took a giant stride forward in approving and embarking upon implementation of DR-CAFTA. DR-CAFTA has tested the leadership of governments and showed up the limitations and problems of governance in the subregion. These teething troubles, however, have gradually been surmounted and, with the notable exception of Costa Rica and the Dominican Republic, the countries are today sailing the calm waters of the Agreement's initial benefits. Nevertheless, it will be important to monitor its development and early impact very closely, as well as preparing for the strongest economic (largely predictable) effects particularly in terms of agriculture. The complementary agendas have been criticized for being incomplete, lacking in financing and difficult to execute. These criticisms contain a deal of truth, though in some cases the problems referred to are explained by the difficulties involved in managing such a politically charged package as DR-CAFTA and the measures required to bolster it. The agendas should therefore be understood as dynamic processes that could not reasonably resolve problems to emerge in the long term overnight. This is particularly true in terms of supporting the future adjustment of the most vulnerable productive and social sectors directly affected by the Agreement. Although work to comprehend and tackle these impacts must be undertaken, the plans to deal with these impacts must be executed in the medium-to-long term, mainly where agriculture for domestic consumption and other rural sectors depending on it are concerned. This does not imply, however, that the work of analysis be left until the effects occur. The task of analysis must start now. What *is* urgent is to strengthen the institutional capacity to meet the coming tasks head on and to promote greater use of the opportunities offered by the Agreement. In this order of things, government entities devoted to sanitary and phytosanitary matters, customs controls of all kinds, export promotion, investment attraction, strengthening MSMEs, technical and financial regulation, consumer protection, regulation of services, protection of the environment and workers' rights must be strengthened.

Association with Europe. Another great challenge for the region in 2007 is the negotiation of the Association Agreement with the EU. As mentioned in Chapter II, the European bloc has recently lost ground in trade and investment in Central America. After DR-CAFTA, the EU may not intend to lose its presence and opportunities for trade and political coordination with the region. There are many reasons why negotiating the Association Agreement will be very different for Central America from negotiating DR-CAFTA. First, because the Association Agreement has a very different structure to an FTA with the United States. Its three components -trade, cooperation and political coordination- demand different strategies and impose different new demands on negotiators. Second, because the EU requires high levels of intra-Central American coordination and intensification of integration, which as we have seen, is an enormously challenging task. Third, because given the subregion's productive structures and European sensitivity (mainly in agriculture and textiles) the EU will probably start the discussions with a strong defensive stance that may reduce trade incentives for Central America. For this reason, Central America will have to make unprecedented efforts of coordination in the negotiations in order to obtain attractive concessions on trade and cooperation. The Agreement with the EU is an opportunity the region should not let slip. It would bring the region nearer to closing the circle of its insertion process with its main trading partners. Furthermore, as mentioned in Chapter 3, this negotiation is expected to have an important effect on stepping up integration in Central America.

The negotiation of DR-CAFTA has left many lessons in Central America to be learned and assimilated for the negotiation with Europe, one of the main ones being the need to accompany the negotiations with parallel in-depth consultation exercises with civil society and analysis of the possible impact of the negotiation on certain productive and social sectors. This would contribute to more precise knowledge of the consequences of the negotiation and to the definition of the components of a complementary agenda, thus avoiding many of the problems posed today by the issues of DR-CAFTA agendas. Similarly, these exercises can help coordinate the cooperation component of a future Association Agreement more effectively. In this sense, poverty and sustainability impact assessments on poverty and sustainability performed by the EU in negotiating Association Agreements are important, but Central America must also be in a position to perform its own.

The negotiation with the EU could involve a dimension that may alter the composition and size of the CU, namely, the Panama factor. Panama was a country that, despite negotiating certain FTAs with other individual trading partners within and outside the region, does not participate in the deep integration launched by Central America in the 1960s. This situation may change in the near future and the catalyst for such change is precisely the EU's condition that, for it to start talking about integration with Panama, Panama will have to become part of a more united Central America in sustaining dialogue over matters of integration. Consequently, Panama is currently looking on this scenario with a great deal of interest and the situation has major repercussions both for the region and for Panama itself: for the region, because it involves extending the model and the opening of new possibilities for trade; for Panama, because it must reach consensus over a program of adherence to the Central American model (including the sensitive topic of agricultural liberalization), while discussing the agreement with the EU. This process will be extremely involved. Panama, however, rightly sees it as a window of opportunity. Its privileged geoestrategic position, the widening of the Panama Canal and its experience in trade, logistical and financial services distribution means that the country can substantially develop its role as a global trader if it consolidates free access to the largest world markets of all, namely, the United States, Asia and Europe. Negotiations of an FTA with the United States (where all that is left is to negotiate the chapters on environmental and labor issues) have advanced a great deal. It will apparently be able to go on negotiating with the EU providing it does so within a more united Central America. It has some FTAs with Asian countries (Taiwan and Singapore) and should pursue that opening with these countries. This new side to

Panama within Central America will be very interesting to watch in the years to come and opens up a fresh dimension of complexity and opportunity for the region.

Closing the Circle? Asia: Asia is also a great challenge and opportunity for Central America.[96] The size of its markets, the dynamism of its economic and trade growth, its growing prominence in the distribution of political and economic power across the world makes Asia a continent where trade relations will, of necessity, intensify in the future. The geographical position of Central America regarding the markets of North America and Europe may mean that the region can offer certain incentives to trade cooperation with Asia. Of course, the competitiveness of the Asian region also poses a serious challenge, not only to production in Central America but to exports to the United States in particular, as seen in this Report. The next step for Central America after Europe could be approach to the region through new joint FTAs or other alternative mechanisms. China, Taiwan, South Korea, Singapore, the countries of the Association of Southeast Asian Nations (ASEAN) and, to a far lesser extent, Japan and India, may constitute Central America's gateways to Asia.

What About Latin America? Central America's trade flows with the rest of Latin America, particularly South America, also display a degree of dynamism, without being particularly important markets. However, as the idea of the FTAA vanishes, the possibility of strengthening Central American integration with Latin America as a whole becomes more difficult, notwithstanding the current FTAs (with Mexico and Chile) and the one still under non-joint negotiation (with Colombia). There have been proposals over the promotion of trade convergence between the Latin American countries of the Pacific wich have negotiated trade agreements with the United States.[97] But all these are incipient ideas in a concept that is constantly in the mind of Latin Americans (Latin American integration), but which is exposed to the harsh realities of the low levels of intra-Latin American trade and investment, to the prevailing differences in outlook over international integration modalities and, recently, to the ideological polarization that is starting to be perceived. It is difficult to envision how to promote greater short-term Central American integration with the rest of South America. There is much rhetoric but little real progress. These are two regions that, deliberately or not, frequently turn their backs on each other at the level of trade.

A Wider View of Integration: This Report takes a partial look at integration in Central America. As mentioned at the start, there are dimensions of functional and policy cooperation that have been deliberately left aside. The analysis of the aspects tackled, however, makes it clear that Central America needs to articulate its integration process more coherently and consistently. If we factor the dimensions left aside into the analysis, the need becomes more critical still. Indeed, Central America is currently trying to make progress along several avenues in matters of integration: trade integration, functional integration (a very broad area) and policy integration. The problem lies in the fact that these avenues follow their own particular dynamics and their communicating vessels are few and far between. The regional institutions supporting each of these avenues at best have trouble coordinating with one another. The national institutions dealing with the issues of each avenue face a similar situation at local level. The differences in SICA membership[98] and the advent and expansion of the PPP make the variable geometry already existing in Central America more acute, not to mention the problems of coherence and coordination of the vision. Central America has, in recent years, attempted to strengthen this unique, coherent vision of

[96] See the IDB report on Latin America and the Caribbean's trade relations with China (IDB [2005] and [2006d]; Devlin, Estevadeordal and Rodríguez-Clare [2006]). There will soon be a report available on the region's trade relations with India.

[97] See the Joint Declaration of the Forum on the Latin American Pacific Basin Initiative (*Foro Sobre la Iniciativa de la Cuenca del Pacífico Latinoamericano*), signed by the Trade Ministers of Mexico, Guatemala, El Salvador, Honduras, Panama, Colombia, Ecuador, Peru and Chile in Santiago de Cali, Colombia, on January 30, 2007. See also the proposal by Robert Zoellick, former US Trade Representative, in his article *Happily Ever AAFTA*, in the Wall Street Journal, January 8, 2007.

[98] The five CACM countries plus Belize, Panama and Dominican Republic participate in the SICA's political process.

the integration process, and a new institutionality for the SICA is indeed being worked on.[99] But, once again, the SICA is not the SIECA, and neither of these institutions covers the issues or the membership of the PPP. The compartmentalization of issues at national and regional levels hampers the overall view and its effective articulation.

A generous interpretation of this situation may diagnose this symptom as simple growth pains. And this may be so. According to this line of argument, it may be hoped that the need to improve coordination of the initiatives and their institutions, and to introduce any relevant adjustments may emerge over time. The opposite problem of regional overinstitutionalization is thus avoided. However, in order not to lose sight of the wood for the trees, it is advisable in the short term to periodically take the pulse of all avenues of integration and make public their progress, stagnation and reverses. It is difficult for any governmental, private, national or international actor to maintain such a complete overview of Central American integration. Once this is achieved, more robust pillars for integration in Central America -including relevant regional institutions- can be designed and built to facilitate effective insertion in international markets.

Integration in Central America is in a constant state of flux. It has been drawn, overwritten and redrawn cyclically since the 1960s. Although there are still some contradictions outstanding, the last few years have reflected a strong political will to integration, mainly trade integration. Countries have again internalized the importance of integration and regional markets. Exogenous factors such as the role of the United States, the EU and even Mexico's proactivity in the region, all play an essential role in better understanding the current dynamic of integration, a dynamic very different to what it was in the past. Today a process of opening and integration with the world can be seen that has opened up the way to a highly variable geometry, with multiple avenues of work, multiple trade, political and functional processes operating simultaneously with scant mutual coordination. The agreement with the United States establishes a new framework for integration in Central America. The PPP demonstrates its usefulness and can serve to bring out some of the traditional outlines of integration and functional cooperation. External negotiations have the potential to galvanize expansion of CACM membership. They are all dynamic forces that can help to reshape Central American integration long term. If a total overview is achieved, if the challenges are interpreted correctly, if contradictions are eradicated, and national and regional policy interventions are designed properly, Central America could achieve extremely solid integration. If, on the other hand, leadership proves inadequate, integration may stagnate and the opportunity to use it as an instrument for insertion and regional economic development will be lost.

[99] See the Joint Declaration of the 24th Ordinary Meeting of SICA Heads of State and Government of June 29, 2004.

Contents

ANNEX I. MAIN MACROECONOMIC INDICATORS

TABLE A1
CACM: GROSS DOMESTIC PRODUCT BY COUNTRY
(1999-2005 - Real YOY % variation)

Year	Costa Rica	El Salvador	Guatemala	Honduras	Nicaragua
1999	8.2	3.4	3.8	-1.9	7.0
2000	1.8	2.2	3.6	5.7	4.1
2001	1.1	1.7	2.3	2.6	3.0
2002	2.9	2.3	2.2	2.7	0.8
2003	6.4	2.3	2.1	3.5	2.5
2004	4.1	1.8	2.7	5.0	5.1
2005	5.9	2.8	3.2	4.1	4.0
2006 [e]	6.8	4.2	4.6	5.6	3.7

Note: [e] Estimates.

Source: ECLAC.

TABLE A2
CACM AND MEMBER COUNTRIES: AVERAGE ANNUAL GROWTH RATES FOR GDP AND SPENDING COMPONENTS AND PRODUCT ELASTICITY
(1998-2006 - % and ratios)

Country or Bloc	1998-2002 (%)	2003-2006 (%)	Product Elasticity (Ratio)
CACM [a/]			
GDP to Market Prices	3.3	4.0	
Total Consumption	3.8	3.6	0.98
Gross Domestic Capital Formation	5.2	4.5	1.15
Goods Exports and Services	4.8	7.2	1.45
Goods Imports and Services	6.3	6.4	1.57
Costa Rica			
GDP to Market Prices	4.5	5.8	
Total Consumption	2.5	3.2	0.56
Gross Domestic Capital Formation	9.8	5.7	0.99
Goods Exports and Services	8.4	12.7	2.18
Goods Imports and Services	6.2	8.9	1.54
El Salvador			
GDP to Market Prices	2.7	2.7	
Total Consumption	2.8	2.7	1.02
Gross Domestic Capital Formation	4.8	3.7	1.37
Goods Exports and Services	7.2	3.7	1.37
Goods Imports and Services	6.4	3.7	1.39

TABLE A2 (CONTINUED)

Guatemala			
GDP to market prices	3.4	3.2	
Total Consumption	4.0	3.7	1.17
Gross Domestic Capital Formation	12.3	2.5	0.79
Goods Exports and Services [b/]	0.2	2.4	0.75
Goods Imports and Services [b/]	9.5	3.4	1.09
Honduras			
GDP to Market Prices	2.4	4.5	
Total Consumption	4.9	5.5	1.2
Gross Domestic Capital Formation	-0.5	6.6	1.46
Goods Exports and Services	2.4	4.4	0.97
Goods Imports and Services	4.2	6.7	1.47
Nicaragua			
GDP to Market Prices	3.7	3.8	
Total Consumption	4.8	3.0	0.78
Gross Domestic Capital Formation	-0.2	3.9	1.02
Goods Exports and Services	6.9	10.4	2.7
Goods Imports and Services	4.8	6.0	1.55

Notes: [a/] Simple average for the five countries.

[b/] The 2003-2006 data are not comparable with the 1998-2002 data, as there is no information on exports and imports of the Guatemalan maquila prior to 2002.

Source: Based on ECLAC data.

TABLE A3
CACM: RETAIL INFLATION BY COUNTRY
(1999-2006 - Consumer Price Index YOY % Variation in December every year)

Year	Costa Rica	El Salvador	Guatemala	Honduras	Nicaragua
1999	10.1	-1.0	4.9	10.9	7.2
2000	10.2	4.3	5.1	10.1	9.9
2001	11.0	1.4	8.9	8.8	4.7
2002	9.7	2.8	6.3	8.1	4.0
2003	9.9	2.5	5.9	6.8	6.6
2004	13.1	5.4	9.2	9.2	8.9
2005	14.1	4.3	8.6	7.7	9.6
2006	9.4	4.9	5.8	5.3	9.5

Source: ECLAC.

TABLE A4
CACM: REAL EXCHANGE RATE BY COUNTRY
(2000-2006 - Domestic currency units per US$ - Indexes 2000=100)

Year	Costa Rica	El Salvador	Guatemala	Honduras	Nicaragua
2000	100.0	100.0	100.0	100.0	100.0
2001	98.6	99.1	97.0	97.7	102.8
2002	100.4	98.8	90.7	97.9	106.7
2003	104	99.0	89.1	98.2	109.9
2004	104.4	97.3	85.2	97.8	109.7
2005	103.5	96.1	77.5	95.9	108.7
2006 [e]	102.6	95.3	74.8	93.9	108.1

Note: [e] Estimates.

Source: Based on ECLAC data.

TABLE A5
CACM: *PER CAPITA* GDP BY COUNTRY
(1999-2006 - Current US$)

Year	Costa Rica	El Salvador	Guatemala	Honduras	Nicaragua
1999	4,116	2,025	1,671	859	770
2000	4,063	2,093	1,718	929	794
2001	4,093	2,159	1,824	962	815
2002	4,119	2,195	1,977	964	780
2003	4,203	2,267	2,059	992	779
2004	4,372	2,342	2,202	1,051	837
2005	4,632	2,469	2,492	1,139	896
2006 [e]	5,054	2,615	2,722	1,157	1,003

Note: [e] Estimates.

Source: ECLAC.

TABLE A6
CACM AND SELECTED COUNTRIES: HUMAN DEVELOPMENT INDEX
(Data for 2004)

HDI Ranking [a/]	Country / Bloc	HDI [b/]
1	Norway	0.965
48	Costa Rica	0.841
77	Latin America [c/]	0.751
101	El Salvador	0.729
107	CACM [c/]	0.716
112	Nicaragua	0.698
117	Honduras	0.683
118	Guatemala	0.673
177	Niger	0.311

Notes: [a/] Over a total of 177.

[b/] HDI is a compound indicator covering three dimensions of human welfare: income (*per capita* GDP), education (adult literacy rate and gross rate of primary, secondary and tertiary enrollment) and health (life expectancy at birth). Its value ranges from 0 to 1, 1 being the maximum level of welfare and 0 the minimum.

[c/] Simple average for the region's countries.

Source: UNDP.

TABLE A7
CACM: URBAN UNEMPLOYMENT RATE BY COUNTRY
(1999-2006 - % of EAP)

Year	Costa Rica	El Salvador	Guatemala	Honduras	Nicaragua
1999	6.2	6.9	n.a.	5.3	10.7
2000	5.3	6.5	n.a.	n.a.	7.8
2001	5.8	7.0	n.a.	5.9	11.3
2002	6.8	6.2	5.4	6.1	11.6
2003	6.7	6.2	4.4	7.6	10.2
2004	6.7	6.5	4.4	8.0	9.3
2005	6.9	7.3	n.a.	6.5	7.0
2006 [e]	6.0	5.7	n.a.	5.2 [a/]	n.a.

Notes: [e] Estimates.

[a/] Data corresponding to May.

Source: ECLAC.

ANNEX II. MAIN TRADE AND INVESTMENT INDICATORS

TABLE A8
CACM: TOTAL GOODS EXPORTS
(1997-2005 - Value in US$ million / YOY % variation)

Value	1997	1998	1999	2000	2001	2002	2003	2004	2005 [a/]	Average		
										1997- 1999	2000- 2002	2003-2005 [a/]
Total	*14,135*	*16,354*	*17,279*	*18,004*	*16,899*	*17,283*	*19,126*	*20,901*	*22,681*	*15,923*	*17,395*	*20,903*
Non-Maquila Total	8,697	9,069	7,973	8,240	7,794	7,837	7,954	9,429	10,739	8,580	7,957	9,374
Extraregional	6,747	6,797	5,580	5,667	4,881	5,137	5,069	6,189	7,031	6,375	5,228	6,096
Intraregional	1,951	2,272	2,392	2,573	2,913	2,700	2,885	3,241	3,708	2,205	2,729	3,278
Maquila Total [b/]	5,438	7,285	9,306	9,764	9,105	9,447	11,172	11,472	11,942	7,343	9,438	11,529
YOY Variation												
Total	…	*15.7*	*5.7*	*4.2*	*-6.1*	*2.3*	*10.7*	*9.3*	*8.5*	*10.7*	*0.1*	*9.5*
Non-Maquila Total	11.3	4.3	-12.1	3.4	-5.4	0.5	1.5	18.5	13.9	1.2	-0.5	11.3
Extraregional	9.6	0.8	-17.9	1.6	-13.9	5.2	-1.3	22.1	13.6	-2.5	-2.4	11.5
Intraregional	17.7	16.5	5.3	7.6	13.2	-7.3	6.9	12.3	14.4	13.2	4.5	11.2
Maquila Total [b/]	…	34.0	27.7	4.9	-6.7	3.8	18.3	2.7	4.1	30.9	0.6	8.3

Notes: [a/] Preliminary data for 2005.

SIECA data have been used for El Salvador (2005) and Guatemala (2005).

[b/] The maquila data (which includes duty-free export zones) for Costa Rica, El Salvador and Guatemala (as from 2002), and for Nicaragua correspond to information given by the countries' central banks. The data for Guatemala (1997-2002) correspond to USITC. Guatemala only includes data covered by Decree 29-89 of the Guatemalan Congress (Export Activity and Maquila Promotion and Development Act). The Honduras maquila data has been calculated as the difference between exports from Honduras to the world and world imports from Honduras.

Source: Based on data from UN-Comtrade/SITC Rev. 2, USITC, SIECA and Central Banks.

TABLE A9
CACM: TOTAL GOODS IMPORTS
(1997-2005 - Value in US$ million / YOY % variation)

Value	1997	1998	1999	2000	2001	2002	2003	2004	2005 [a/]	Average		
										1997-1999	2000-2002	2003-2005 [a/]
Total	*18,659*	*21,812*	*22,477*	*24,201*	*25,329*	*27,149*	*29,707*	*33,15*	*37,081*	*20,983*	*25,560*	*33,313*
Non-Maquila Total	14,206	16,142	16,219	17,113	18,179	19,718	21,435	24,427	27,634	15,522	18,337	24,499
Extraregional	12,25	13,778	13,833	14,395	15,322	16,732	18,427	21,089	23,865	13,287	15,483	21,127
Intraregional	1,956	2,364	2,386	2,718	2,857	2,986	3,009	3,338	3,769	2,235	2,853	3,372
Maquila Total [b/]	4,453	5,67	6,258	7,088	7,15	7,43	8,272	8,723	9,447	5,461	7,223	8,814
YOY Variation												
Total	…	*16.9*	*3.0*	*7.7*	*4.7*	*7.2*	*9.4*	*11.6*	*11.9*	*10.0*	*6.5*	*11.0*
Non-Maquila Total	15.6	13.6	0.5	5.5	6.2	8.5	8.7	14	13.1	9.9	6.7	11.9
Extraregional	14.0	12.5	0.4	4.1	6.4	9.2	10.1	14.5	13.2	8.9	6.6	12.6
Intraregional	26.6	20.9	1.0	13.9	5.1	4.5	0.7	10.9	12.9	16.1	7.9	8.2
Maquila Total [b/]	…	27.3	10.4	13.3	0.9	3.9	11.3	5.5	8.3	18.8	6.0	8.4

Notes: [a/] Preliminary data for 2005.

SIECA data have been used for El Salvador (2005) and Guatemala (2005).

[b/] The maquila data (which includes duty-free export zones) for Costa Rica, El Salvador, and Guatemala (as from 2002), and for Nicaragua correspond to information given by the countries' central banks. The data for Guatemala (1997-2002) correspond to USITC for exports; imports were estimated as exports of maquila-maquila added value (Source: ECLAC). Guatemala only includes data covered by Decree 29-89 of the Guatemalan Congress (Export Activity and Maquila Promotion and Development Act). The Honduras maquila data has been calculated as the difference between exports from Honduras to the world and world imports from Honduras.

Source: Based on data from UN-Comtrade/SITC Rev. 2, USITC, SIECA and Central Banks.

TABLE A10
CACM: TOTAL TRADE BALANCE IN GOODS
(1997-2005 - US$ million / % GDP)

Value	1997	1998	1999	2000	2001	2002	2003	2004	2005 [a]	Average		
										1997-1999	2000-2002	2003-2005 [a]
Total	*-4,524*	*-5,458*	*-5,198*	*-6,197*	*-8,430*	*-9,865*	*-10,580*	*-12,248*	*-14,400*	*-5,060*	*-8,164*	*-12,410*
Non-Maquila Total	-5,509	-7,072	-8,246	-8,873	-10,384	-11,882	-13,481	-14,998	-16,895	-6,942	-10,380	-15,125
Extraregional	-5,504	-6,981	-8,252	-8,728	-10,441	-11,595	-13,358	-14,901	-16,834	-6,912	-10,255	-15,031
Intraregional	-5	-92	6	-144	56	-286	-123	-97	-61	-30	-125	-94
Maquila Total [b]	984	1,615	3,048	2,676	1,954	2,016	2,900	2,750	2,495	1,882	2,215	2,715
% GDP												
Total	*-9.1*	*-10.0*	*-9.3*	*-10.6*	*-13.7*	*-15.2*	*-15.5*	*-16.7*	*-17.8*	*-9.5*	*-13.2*	*-16.6*
Non-Maquila Total	-11.0	-13.0	-14.8	-15.2	-16.8	-18.3	-19.7	-20.4	-20.9	-13.0	-16.8	-20.3
Extraregional	-11.0	-12.8	-14.8	-15.0	-16.9	-17.9	-19.5	-20.3	-20.8	-12.9	-16.6	-20.2
Intraregional	0.0	-0.2	0.0	-0.2	0.1	-0.4	-0.2	-0.1	-0.1	-0.1	-0.2	-0.1
Maquila Total [b]	2.0	3.0	5.5	4.6	3.2	3.1	4.2	3.7	3.0	3.5	3.6	3.7

Notes: [a] Preliminary data for 2005.

[b] Maquila includes duty-free export zones.

Source: Based on data from UN-Comtrade/SITC Rev. 2, ECLAC, SIECA and Central Banks.

TABLE A11
CACM: TRADE OPENNESS COEFFICIENT [a/]
(1997-2005 - % GDP)

Openness Coefficient, Non-Maquila	1997	1998	1999	2000	2001	2002	2003	2004	2005 [b/]	Average		
										1997-1999	2000-2002	2003-2005 [b/]
CACM	*45.9*	*46.4*	*43.4*	*43.5*	*42.1*	*42.4*	*42.9*	*45.9*	*46.8*	*45.2*	*42.6*	*45.2*
Costa Rica	51.9	52.9	43.2	42.2	40.0	41.3	43.4	44.4	47.9	49.3	41.2	45.2
El Salvador	38.8	36.4	34.4	39.1	36.8	36.0	37.5	40.2	41.5	36.5	37.3	39.7
Guatemala	34.8	37.3	38.3	39.3	38.2	35.9	37.6	39.2	38.5	36.8	37.8	38.4
Honduras	76.2	77.3	70.8	59.7	62.8	71.6	62.7	75.9	80.8	74.7	64.7	73.2
Nicaragua	63.1	58.4	59.6	59.7	56.2	60.5	61.2	65.2	68.9	60.4	58.8	65.1
Openness Coefficient, Maquila [c/]												
CACM	*19.8*	*23.8*	*27.9*	*28.9*	*26.3*	*25.9*	*28.4*	*27.4*	*26.1*	*24.0*	*27.1*	*27.3*
Costa Rica	19.3	30.3	39.1	34.4	30.5	32.5	35	34.4	38.8	29.5	32.5	36
El Salvador	16.3	16.9	18.4	21	20.4	21.2	21.6	21.4	19.0	17.2	20.9	20.6
Guatemala	9.8	10.4	12.0	13.6	13.6	13.1	13.0	13.8	11.6	10.7	13.5	12.8
Honduras	76.1	82.6	84.5	93.9	79.7	72.6	88.9	76.9	72.5	81.1	82.1	79.4
Nicaragua	7.8	8.2	8.5	9.6	11.8	14.5	17.9	22.8	23.8	8.2	12.0	21.5
Openness Coefficient, Total A (Non-Maquila + Maquila)												
CACM	*65.8*	*70.2*	*71.3*	*72.4*	*68.4*	*68.3*	*71.3*	*73.3*	*73*	*69.2*	*69.7*	*72.5*
Costa Rica	71.2	83.2	82.2	76.6	70.5	73.8	78.3	78.8	86.7	78.9	73.6	81.3
El Salvador	55.1	53.3	52.8	60.1	57.1	57.2	59.1	61.6	60.4	53.7	58.2	60.4
Guatemala	44.6	47.7	50.3	52.9	51.8	49.1	50.6	53.0	50.1	47.5	51.3	51.2
Honduras	152.3	159.9	155.2	153.6	142.5	144.2	151.7	152.8	153.4	155.8	146.7	152.6
Nicaragua	71.0	66.6	68.1	69.3	68.0	75.0	79.1	88.0	92.8	68.6	70.8	86.6

TABLE A11 (CONTINUED)

	1997	1998	1999	2000	2001	2002	2003	2004	2005 [b/]	Average		
										1997-1999	2000-2002	2003-2005 [b/]
Maquila Added value												
CACM	*2.0*	*3.0*	*5.5*	*4.6*	*3.2*	*3.1*	*4.2*	*3.7*	*3.0*	*3.5*	*3.6*	*3.7*
Costa Rica	1.3	3.5	11.4	7.7	2.6	2.9	6.6	4.8	3.1	5.4	4.4	4.8
El Salvador	2.6	2.8	3.0	3.5	3.5	3.3	3.3	2.9	2.4	2.8	3.4	2.9
Guatemala	1.2	1.5	1.6	1.9	1.9	1.5	1.7	1.6	1.0	1.4	1.8	1.4
Honduras	5.4	8.1	9.4	9.0	8.3	9.0	10.1	10.5	11.4	7.7	8.8	10.7
Nicaragua	1.8	1.9	2.0	2.1	2.6	2.8	3.2	3.7	4.0	1.9	2.5	3.6
Openess Coefficient, Total B [d/] (Non-Maquila + Maquila Added value)												
CACM	*47.9*	*49.4*	*48.9*	*48.1*	*45.2*	*45.5*	*47.1*	*49.7*	*49.9*	*48.7*	*46.3*	*48.9*
Costa Rica	53.2	56.4	54.5	49.8	42.6	44.2	49.9	49.2	51.0	54.7	45.6	50.0
El Salvador	41.4	39.2	37.5	42.6	40.3	39.3	40.7	43.2	43.9	39.3	40.7	42.6
Guatemala	36.0	38.8	39.9	41.2	40.1	37.4	39.3	40.8	39.5	38.2	39.6	39.9
Honduras	81.6	85.4	80.2	68.7	71.1	80.5	72.9	86.4	92.2	82.4	73.4	83.8
Nicaragua	64.9	60.3	61.6	61.8	58.8	63.3	64.4	68.9	72.9	62.3	61.3	68.7

Notes: [a/] The openness coefficient is defined as the ratio of the sum of exports and imports of goods over GDP.

[b/] Preliminary data for 2005.

[c/] Maquila includes duty-free export zones.

[d/] Total B (Non-Maquila + Maquila Added value) seeks to remove the double levying of maquila imports, as exports in this sector are equivalent to maquila imports + their added value.

GDP for Honduras and Nicaragua may be underestimated and their openness coefficients may as a result be overestimated.

Source: Based on data from UN-Comtrade/SITC Rev. 2, ECLAC, SIECA and Central Banks.

TABLE A12
CACM: NON-MAQUILA GOODS EXPORTS BY COUNTRY/REGION OF DESTINATION
(1995-2005 - Value in US$ million, % share and contribution to YOY variation)

Value	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005 [a/]	% AAGR		
												1995-1999	2000-2002	2003-2005 [a/]
Total	*6,787.0*	*7,811*	*8,697.0*	*9,069.0*	*7,973.0*	*8,240.0*	*7,794.0*	*7,837.0*	*7,954*	*9,429*	*10,739.0*	*8.4*	*-0.5*	*11.3*
Extraregional	5,336.0	6,154	6,747.0	6,797.0	5,580.0	5,667.0	4,881.0	5,137.0	5,069	6,189	7,031.0	1.6	-2.4	11.5
United States	2,357.0	2,973	3,355.0	3,275.0	2,863.0	2,923.0	2,269.0	2,551.0	2,495	3,150	3,567.0	7.1	-2.6	12.4
EU-25	1,853.0	1,970	2,016.0	1,884.0	1,450.0	1,372.0	1,105.0	1,041.0	1,072	1,279	1,442.0	3.7	-10.2	11.7
Latin America	280.0	343	595.0	704.0	584.0	582.0	563.0	560.0	615	745	1,144.0	19.6	-1.4	28.1
Asia	353.0	208	273.0	271.0	207.0	196.0	229.0	227.0	227	235	333.0	17.1	3.5	15.1
Others	494.2	660	507.8	662.3	476.6	593.6	715.2	758.1	660	779	545.5	7.8	17.0	-8.3
Intraregional	1,451.0	1.657	1,951.0	2,272.0	2,392.0	2,573.0	2,913.0	2,700.0	2,885	3,241	3,708.0	14.2	4.5	11.2
Share												**Average**		
Total	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*
Extraregional	78.6	78.8	77.6	74.9	70.0	68.8	62.6	65.5	63.7	65.6	65.5	76.0	65.6	64.9
United States	34.7	38.1	38.6	36.1	35.9	35.5	29.1	32.5	31.4	33.4	33.2	36.7	32.4	32.7
EU-25	27.3	25.2	23.2	20.8	18.2	16.7	14.2	13.3	13.5	13.6	13.4	22.9	14.7	13.5
Latin America	4.1	4.4	6.8	7.8	7.3	7.1	7.2	7.1	7.7	7.9	10.6	6.1	7.1	8.8
Asia	5.2	2.7	3.1	3.0	2.6	2.4	2.9	2.9	2.9	2.5	3.1	3.3	2.7	2.8
Others	7.3	8.5	5.8	7.3	6.0	7.2	9.2	9.7	8.3	8.3	5.1	7.0	8.7	7.2
Intraregional	21.4	21.2	22.4	25.1	30.0	31.2	37.4	34.5	36.3	34.4	34.5	24.0	34.4	35.1
Contribution to YOY Variation														
Total Growth	*23.3*	*15.1*	*11.3*	*4.3*	*-12.1*	*3.4*	*-5.4*	*0.5*	*1.5*	*18.5*	*13.9*	*8.4*	*-0.5*	*11.3*
Extraregional	19.4	12.1	7.6	0.6	-13.4	1.1	-9.5	3.3	-0.9	14.1	8.9	5.2	-1.7	7.4
United States	4.5	9.1	4.9	-0.9	-4.5	0.8	-7.9	3.6	-0.7	8.2	4.4	2.6	-1.2	4.0
EU-25	9.5	1.7	0.6	-1.5	-4.8	-1.0	-3.2	-0.8	0.4	2.6	1.7	1.1	-1.7	1.6
Latin America	0.0	0.9	3.2	1.3	-1.3	0.0	-0.2	0.0	0.7	1.6	4.2	0.8	-0.1	2.2
Asia	3.5	-2.1	0.8	0.0	-0.7	-0.1	0.4	0.0	0.0	0.1	1.0	0.3	0.1	0.4
Others	1.9	2.4	-1.9	1.8	-2.0	1.5	1.5	0.5	-1.3	1.5	-2.5	0.4	1.2	-0.7
Intraregional	3.9	3.0	3.8	3.7	1.3	2.3	4.1	-2.7	2.4	4.5	5.0	3.1	1.2	3.9

Notes: [a/] Preliminary data for 2005. SIECA data have been used for El Salvador (2005) and Guatemala (2005), and CBCR data for Costa Rica (1997-2005).

Percentage share t is calculated as a percentage of the total. Contributions to growth are defined as growth weighted by the proportion over the total.

AAGR: Simple Average Annual Growth Rate.

Source: Based on data from UN-Comtrade/SITC Rev. 2, SIECA and Central Bank of Costa Rica.

TABLE A13
CACM: NON-MAQUILA GOODS IMPORTS BY COUNTRY/REGION OF ORIGIN
(1995-2005 - Value in US$ million, % share and contribution to YOY variation)

Value	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	% AAGR		
												1995-1999	2000-2002	2003-2005 [a/]
Total	*11,860*	*12,294.0*	*14,206.0*	*16,142.0*	*16,219.0*	*17,113*	*18,179.0*	*19,718.0*	*21,435.0*	*24,427.0*	*27,634.0*	*11.3*	*6.7*	*11.9*
Extraregional	10,391	10,749.0	12,250.0	13,778.0	13,833.0	14,395	15,322.0	16,732.0	18,427.0	21.089.0	23,865.0	6.1	6.6	12.6
United States	5,202	5,426.0	6,133.0	6,765.0	6,555.0	6,330	6,231.0	7,462.0	8.046.0	8,513.0	9,173.0	7.2	4.9	7.1
EU-25	1,335	1,248.0	1,376.0	1,600.0	1,507.0	1,628	1,668.0	1,947.0	2,303.0	2,512.0	2,493.0	10.7	9.1	8.9
Latin America	1,904	2,013.0	2,570.0	2,678.0	2,941.0	3,581	3,814.0	3,573.0	4.059.0	5,114.0	7,524.0	9.6	7.3	28.9
Asia	931	924.0	1,043.0	1,525.0	1,401.0	1,265	1,675.0	1,768.0	2.059.0	2,488.0	3.013.0	34	9.4	19.5
Others	1,019	1,136.3	1,127.7	1,209.6	1,428.5	1,592	1,934.5	1,982.3	1,960.1	2,462.6	1,662.6	12.5	11.8	-2.7
Intraregional	1,469	1,545.0	1,956.0	2,364.0	2,386.0	2,718	2,857.0	2,986.0	3.009.0	3,338.0	3,769.0	14.2	7.9	8.2
Share												**Average**		
Total	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*
Extraregional	87.6	87.4	86.2	85.4	85.3	84.1	84.3	84.9	86.0	86.3	86.4	86.4	84.4	86.2
United States	43.9	44.1	43.2	41.9	40.4	37.0	34.3	37.8	37.5	34.9	33.2	42.7	36.4	35.2
EU-25	11.3	10.2	9.7	9.9	9.3	9.5	9.2	9.9	10.7	10.3	9.0	10.1	9.5	10.0
Latin America	16.1	16.4	18.1	16.6	18.1	20.9	21.0	18.1	18.9	20.9	27.2	17.1	20.0	22.4
Asia	7.9	7.5	7.3	9.4	8.6	7.4	9.2	9.0	9.6	10.2	10.9	8.2	8.5	10.2
Others	8.6	9.2	7.9	7.5	8.8	9.3	10.6	10.1	9.1	10.1	6.0	8.4	10.0	8.4
Intraregional	12.4	12.6	13.8	14.6	14.7	15.9	15.7	15.1	14.0	13.7	13.6	13.6	15.6	13.8
Contribution to YOY Variation														
Total	*17.3*	*3.7*	*15.6*	*13.6*	*0.5*	*5.5*	*6.2*	*8.5*	*8.7*	*14.0*	*13.1*	*10.1*	*6.7*	*11.9*
Extraregional	15.4	3.0	12.2	10.8	0.3	3.5	5.4	7.8	8.6	12.4	11.4	8.3	5.5	10.8
United States	9.0	1.9	5.7	4.4	-1.3	-1.4	-0.6	6.8	3.0	2.2	2.7	4.0	1.6	2.6
EU-25	1.6	-0.7	1.0	1.6	-0.6	0.7	0.2	1.5	1.8	1.0	-0.1	0.6	0.8	0.9
Latin America	3.2	0.9	4.5	0.8	1.6	3.9	1.4	-1.3	2.5	4.9	9.9	2.2	1.3	5.8
Asia	-0.1	-0.1	1.0	3.4	-0.8	-0.8	2.4	0.5	1.5	2.0	2.1	0.7	0.7	1.9
Others	1.7	1.0	-0.1	0.6	1.4	1.0	2.0	0.3	-0.1	2.3	-3.3	0.9	1.1	-0.3
Intraregional	2.0	0.6	3.3	2.9	0.1	2.0	0.8	0.7	0.1	1.5	1.8	1.8	1.2	1.1

Notes: [a/] Preliminary data for 2005. SIECA data have been used for El Salvador (2005) and Guatemala (2005), and CBCR data for Costa Rica (1997-2005).
Percentage share is calculated as a percentage of the total. Contributions to growth are defined as growth weighted by the proportion over the total.
% AAGR: Average Annual Growth Rate.

Source: Based on data from UN-Comtrade/SITC Rev. 2, SIECA and CBCR.

Table A14
CACM: NON-MAQUILA TRADE BALANCE IN GOODS
(1995-2005 - Balance in US$ million)

Value	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005 [a/]	Average		
												1995-1999	2000-2002	2003-2005 [a/]
Total	*-5,073*	*-4,483*	*-5,509*	*-7,072*	*-8,246*	*-8,873*	*-10,384*	*-11,882*	*-13,481*	*-14,998*	*-16,895*	*-6,077*	*-10,380*	*-15,125*
Extraregional	-5,055	-4,594	-5,504	-6,981	-8,252	-8,728	-10,441	-11,595	-13,358	-14,901	-16,834	-6,077	-10,255	-15,031
United States	-2,844	-2,453	-2,779	-3,490	-3,692	-3,407	-3,962	-4,912	-5,551	-5,363	-5,606	-3,052	-4,094	-5,507
EU-25	0,518	0,722	0,639	0,284	-0,058	-0,255	-0,563	-0,905	-1,231	-1,233	-1,051	0,421	-0,574	-1,172
Latin America	-1,624	-1,671	-1,975	-1,974	-2,357	-2,999	-3,251	-3,013	-3,444	-4,368	-6,380	-1,920	-3,088	-4,731
Asia	-0,579	-0,716	-0,769	-1,254	-1,194	-1,069	-1,446	-1,541	-1,831	-2,253	-2,680	-0,902	-1,352	-2,255
Others	-0,525	-0,476	-0,620	-0,547	-0,952	-0,998	-1,219	-1,224	-1,300	-1,684	-1,117	-0,624	-1,147	-1,367
Intraregional	-0,018	0,112	-0,005	-0,092	0,006	-0,144	0,056	-0,286	-0,123	-0,097	-0,061	0,001	-0,125	-0,094

Notes: [a/] Preliminary data for 2005. SIECA data have been used for El Salvador (2005) and Guatemala (2005), and CBCR data for Costa Rica (1997-2005).

The intraregional balance is distinct from zero due to differences between the countries in the way they report trade flows.

Source: Based on data from UN-Comtrade/SITC Rev. 2, SIECA and CBCR.

TABLE A15
CACM: MAQUILA EXPORTS [a]
(1997-2005 - Value in US$ million, % share and contribution to YOY variation)

Value	1997	1998	1999	2000	2001	2002	2003	2004	2005 [b]	% AAGR 1997-1999	% AAGR 2000-2002	% AAGR 2003-2005 [b]
CACM	*5,438*	*7,285*	*9,306*	*9,764*	*9,105*	*9,447*	*11,172*	*11,472*	*11,942*	*30.9*	*0.6*	*8.3*
Costa Rica	1,319	2,381	3,985	3,355	2,714	2,985	3,635	3,621	4,072	74.0	-8.3	11.3
El Salvador	1,055	1,185	1,333	1,609	1,650	1,757	1,873	1,921	1,818	12.4	9.9	1.3
Guatemala	978	1,150	1,246	1,497	1,628	1,700	1,825	2,105	2,002	13.0	11.1	5.9
Honduras	1,923	2,388	2,546	3,072	2,816	2,658	3,405	3,229	3,368	15.4	2.2	9.1
Nicaragua	163	182	196	231	296	347	434	597	682	9.7	21.0	25.6
Share											**Average**	
CACM	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*
Costa Rica	24.2	32.7	42.8	34.4	29.8	31.6	32.5	31.6	34.1	33.2	31.9	32.7
El Salvador	19.4	16.3	14.3	16.5	18.1	18.6	16.8	16.7	15.2	16.7	17.7	16.2
Guatemala	18.0	15.8	13.4	15.3	17.9	18.0	16.3	18.3	16.8	15.7	17.1	17.1
Honduras	35.4	32.8	27.4	31.5	30.9	28.1	30.5	28.1	28.2	31.8	30.2	28.9
Nicaragua	3.0	2.5	2.1	2.4	3.3	3.7	3.9	5.2	5.7	2.5	3.1	4.9
Contribution to YOY Variation												
Total Growth	…	*34.0*	*27.7*	*4.9*	*-6.7*	*3.8*	*18.3*	*2.7*	*4.1*	*30.9*	*0.6*	*8.3*
Costa Rica	…	19.5	22.0	-6.8	-6.6	3.0	6.9	-0.1	3.9	20.8	-3.5	3.6
El Salvador	…	2.4	2.0	3.0	0.4	1.2	1.2	0.4	-0.9	2.2	1.5	0.3
Guatemala	…	3.2	1.3	2.7	1.3	0.8	1.3	2.5	-0.9	2.2	1.6	1.0
Honduras	…	8.6	2.2	5.7	-2.6	-1.7	7.9	-1.6	1.2	5.4	0.4	2.5
Nicaragua	…	0.3	0.2	0.4	0.7	0.6	0.9	1.5	0.7	0.3	0.5	1.0

Notes: [a] Includes duty-free export zones. Maquila data for Costa Rica, El Salvador and Guatemala (as from 2002), and for Nicaragua correspond to the information given by the countries' central banks. For Guatemala only exports covered by Decree 29-89 of the Guatemalan Congress (Export Activity and Maquila Promotion and Development Act) are considered. The data for Guatemala (1997-2002) correspond to USITC. The Honduras maquila data has been calculated as the difference between exports from Honduras to the world and world imports from Honduras.

[b] Preliminary data for 2005.

Contributions to growth are defined as growth weighted by the proportion over the total.

% AAGR: Average annual growth rate.

Source: Based on data from UN-Comtrade/SITC Rev. 2, USITC, SIECA and Central Banks.

TABLE A16
CACM: MAQUILA IMPORTS [a/]
(1997-2005 - Value in US$ million, % share and contribution to YOY variation)

Value	1997	1998	1999	2000	2001	2002	2003	2004	2005 [b/]	% AAGR		
										1997-1999	2000-2002	2003-2005 [b/]
CACM	*4,453*	*5,670*	*6,258*	*7,088*	*7,150*	*7,430*	*8,272*	*8,723*	*9,447*	*18.8*	*6.0*	*8.4*
Costa Rica	1,154	1,886	2,187	2,133	2,287	2,489	2,484	2,736	3,459	39.7	4.5	12.1
El Salvador	764	847	955	1,153	1,161	1,283	1,379	1,457	1,404	11.8	10.6	3.2
Guatemala	766	865	959	1,123	1,232	1,355	1,406	1,663	1,680	11.9	12.3	7.7
Honduras	1,667	1,960	2,036	2,530	2,283	2,068	2,702	2,437	2,417	10.7	1.7	6.7
Nicaragua	103	113	122	148	188	236	301	430	487	9.0	24.6	28.0
Share											**Average**	
CACM	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*
Costa Rica	25.9	33.3	34.9	30.1	32.0	33.5	30.0	31.4	36.6	31.4	31.9	32.7
El Salvador	17.2	14.9	15.3	16.3	16.2	17.3	16.7	16.7	14.9	15.8	16.6	16.1
Guatemala	17.2	15.3	15.3	15.9	17.2	18.2	17.0	19.1	17.8	15.9	17.1	18.0
Honduras	37.4	34.6	32.5	35.7	31.9	27.8	32.7	27.9	25.6	34.8	31.8	28.7
Nicaragua	2.3	2.0	1.9	2.1	2.6	3.2	3.6	4.9	5.2	2.1	2.6	4.6
Contribution to YOY Variation												
Total Growth	...	*27.3*	*10.4*	*13.3*	*0.9*	*3.9*	*11.3*	*5.5*	*8.3*	*18.8*	*6.0*	*8.4*
Costa Rica	...	16.4	5.3	-0.9	2.2	2.8	-0.1	3.1	8.3	10.9	1.4	3.8
El Salvador	...	1.9	1.9	3.2	0.1	1.7	1.3	0.9	-0.6	1.9	1.7	0.5
Guatemala	...	2.2	1.6	2.6	1.5	1.7	0.7	3.1	0.2	1.9	2.0	1.3
Honduras	...	6.6	1.3	7.9	-3.5	-3.0	8.5	-3.2	-0.2	4.0	0.5	1.7
Nicaragua	...	0.2	0.2	0.4	0.6	0.7	0.9	1.6	0.7	0.2	0.5	1.0

Notes: [a/] Includes duty-free export zones. The maquila data for Costa Rica, El Salvador and Guatemala (as from 2002), and for Nicaragua correspond to the information given by the countries' central banks. For Guatemala only exports covered by Decree 29-89 of the Guatemalan Congress (Export Activity and Maquila Promotion and Development Act) are considered. The data for Guatemala (1997-2002) correspond to USITC for exports; imports were estimated as maquila- maquila added value exports (Source: ECLAC). The Honduras maquila data has been calculated as the difference between exports from Honduras to the world and world imports from Honduras.

[b/] Preliminary data for 2005.

Contributions to growth are defined as growth weighted by the proportion over the total. % AAGR corresponds to Average Annual Growth Rate.

Source: Based on data from UN-Comtrade/SITC Rev. 2, USITC, SIECA and Central Banks.

TABLE A17
CACM: INTRAREGIONAL GOODS EXPORTS[a/]
(1995-2005 - Value in US$ million, YOY Variation, % share and contribution to YOY variation)

Value	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005 [b/]	Average		
												1995-1999	2000-2002	2003-2005 [b/]
CACM	*1,451*	*1,657*	*1,951*	*2,272*	*2,392*	*2,573*	*2,913*	*2,700*	*2,885*	*3,241*	*3,708*	*1,944.5*	*2,728.7*	*3,278.0*
Costa Rica	350	384	411	479	532	558	559	524	575	666	751	431.2	546.8	664.0
El Salvador	416	455	576	616	627	740	723	740	746	822	914	538.0	734.5	827.4
Guatemala	566	578	683	748	790	815	1,059	700	1,089	1,248	1,404	672.9	857.9	1,247.0
Honduras	37	139	159	305	299	296	399	466	252	313	345	187.8	386.9	303.5
Nicaragua	83	101	121	122	145	164	174	270	223	192	294	114.6	202.7	236.0
Share														
CACM	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*
Costa Rica	24.1	23.2	21.1	21.1	22.2	21.7	19.2	19.4	19.9	20.5	20.2	22.3	20.1	20.2
El Salvador	28.7	27.5	29.5	27.1	26.2	28.8	24.8	27.4	25.9	25.4	24.7	27.8	27.0	25.3
Guatemala	39.0	34.9	35.0	32.9	33.0	31.7	36.4	25.9	37.7	38.5	37.9	35.0	31.3	38.0
Honduras	2.5	8.4	8.2	13.4	12.5	11.5	13.7	17.3	8.7	9.7	9.3	9.0	14.2	9.2
Nicaragua	5.7	6.1	6.2	5.4	6.1	6.4	6.0	10.0	7.7	5.9	7.9	5.9	7.4	7.2
YOY Variation														
CACM	*17.2*	*14.2*	*17.7*	*16.5*	*5.3*	*7.6*	*13.2*	*-7.3*	*6.9*	*12.3*	*14.4*	*14.2*	*4.5*	*11.2*
Costa Rica	22.3	9.9	7.0	16.7	10.9	4.8	0.2	-6.2	9.8	15.7	12.7	13.4	-0.4	12.8
El Salvador	17.7	9.4	26.6	7.0	1.7	18.1	-2.4	2.4	0.8	10.2	11.2	12.5	6.1	7.4
Guatemala	19.1	2.2	18.2	9.5	5.5	3.2	29.9	-34.0	55.7	14.6	12.5	10.9	-0.3	27.6
Honduras	-8.1	276.9	15.0	91.4	-2.1	-1.0	34.7	17.0	-45.9	24.1	10.4	74.6	16.9	-3.8
Nicaragua	-1.0	21.9	19.8	1.0	18.4	13.2	5.9	55.3	-17.5	-13.9	53.1	12.0	24.8	7.2
Contribution to YOY Variation														
Total Growth	17.2	14.2	17.7	16.5	5.3	7.6	13.2	-7.3	6.9	12.3	14.4	14.2	4.5	11.2
Costa Rica	5.2	2.4	1.6	3.5	2.3	1.1	0.1	-1.2	1.9	3.1	2.6	3.0	0.0	2.6
El Salvador	5.0	2.7	7.3	2.1	0.5	4.8	-0.7	0.6	0.2	2.6	2.8	3.5	1.6	1.9
Guatemala	7.3	0.8	6.4	3.3	1.8	1.1	9.5	-12.3	14.4	5.5	4.8	3.9	-0.6	8.3
Honduras	-0.3	7.0	1.3	7.5	-0.3	-0.1	4.0	2.3	-7.9	2.1	1.0	3.0	2.1	-1.6
Nicaragua	-0.1	1.3	1.2	0.1	1.0	0.8	0.4	3.3	-1.8	-1.1	3.1	0.7	1.5	0.1

Notes: [a/] Non-Maquila.

[b/] Preliminary data for 2005.

SIECA data have been used for El Salvador (2005) and Guatemala (2005), and CBCR data for Costa Rica (1997-2005).

Percentage share is calculated as a percentage of the total. Contributions to growth are defined as growth weighted by the proportion over the total.

Source: Based on data from UN-Comtrade/SITC Rev. 2. SIECA and CBCR.

TABLE A18
CACM: INTRAREGIONAL GOODS IMPORTS [a/]
(1995-2005 - Value in US$ million, YOY Variation, % share and contribution to YOY variation)

Value	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005 [b/]	Average		
												1995-1999	2000-2002	2003-2005 [b/]
CACM	*1,469*	*1,545*	*1,956*	*2,364*	*2,386*	*2,718*	*2,857*	*2,986*	*3,009*	*3,338*	*3,769*	*1,943.8*	*2,853.5*	*3,371.7*
Costa Rica	235	250	296	310	295	289	291	308	313	321	361	277.3	296.0	331.5
El Salvador	470	506	576	599	637	821	820	820	867	946	1,015	557.6	820.4	942.7
Guatemala	291	243	411	608	485	615	777	798	831	908	986	407.6	729.7	908.6
Honduras	244	287	341	429	449	502	503	612	584	661	830	350.1	539.4	691.8
Nicaragua	228	260	331	418	519	490	465	448	413	501	576	351.2	467.9	497.0
Share														
CACM	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*
Costa Rica	16.0	16.2	15.1	13.1	12.4	10.6	10.2	10.3	10.4	9.6	9.6	14.6	10.4	9.9
El Salvador	32.0	32.7	29.5	25.3	26.7	30.2	28.7	27.5	28.8	28.3	26.9	29.2	28.8	28.0
Guatemala	19.8	15.7	21.0	25.7	20.3	22.6	27.2	26.7	27.6	27.2	26.2	20.5	25.5	27.0
Honduras	16.6	18.6	17.4	18.2	18.8	18.5	17.6	20.5	19.4	19.8	22.0	17.9	18.9	20.4
Nicaragua	15.5	16.8	16.9	17.7	21.8	18.0	16.3	15.0	13.7	15.0	15.3	17.7	16.4	14.7
YOY Variation														
CACM	*15.9*	*5.2*	*26.6*	*20.9*	*1.0*	*13.9*	*5.1*	*4.5*	*0.7*	*10.9*	*12.9*	*13.9*	*7.9*	*8.2*
Costa Rica	1.9	6.0	18.7	4.6	-4.6	-2.2	0.7	5.7	1.5	2.8	12.2	5.3	1.4	5.5
El Salvador	18.1	7.6	13.9	4.0	6.4	28.8	-0.1	0.0	5.8	9.1	7.3	10.0	9.6	7.4
Guatemala	-0.3	-16.6	69.4	47.8	-20.2	26.8	26.4	2.7	4.2	9.3	8.6	16.0	18.6	7.4
Honduras	56.5	17.6	18.8	25.9	4.8	11.8	0.2	21.7	-4.6	13.1	25.7	24.7	11.2	11.4
Nicaragua	20.1	13.9	27.5	26.2	24.2	-5.5	-5.2	-3.6	-7.8	21.3	15.0	22.4	-4.8	9.5
Contribution to YOY Variation														
Total Growth	*15.9*	*5.2*	*26.6*	*20.9*	*1.0*	*13.9*	*5.1*	*4.5*	*0.7*	*10.9*	*12.9*	*13.9*	*7.9*	*8.2*
Costa Rica	0.3	1.0	3.0	0.7	-0.6	-0.3	0.1	0.6	0.2	0.3	1.2	0.9	0.1	0.5
El Salvador	5.7	2.4	4.6	1.2	1.6	7.7	0.0	0.0	1.6	2.6	2.1	3.1	2.6	2.1
Guatemala	-0.1	-3.3	10.9	10.0	-5.2	5.4	6.0	0.7	1.1	2.6	2.3	2.5	4.0	2.0
Honduras	6.9	2.9	3.5	4.5	0.9	2.2	0.0	3.8	-0.9	2.6	5.1	3.7	2.0	2.2
Nicaragua	3.0	2.2	4.6	4.4	4.3	-1.2	-0.9	-0.6	-1.2	2.9	2.2	3.7	-0.9	1.3

Notes: [a/] Non-maquila.
[b/] Preliminary data for 2005.
SIECA data have been used for El Salvador (2005) and Guatemala (2005), and CBCR data for Costa Rica (1997-2005).
Percentage share is calculated as a percentage of the total. Contributions to growth are defined as growth weighted by the proportion over the total.

Source: Based on data from UN-Comtrade/SITC Rev. 2. SIECA and Central Bank of Costa Rica.

Table A19
CACM: INTRAREGIONAL TRADE BALANCE IN GOODS [a/]
(1995-2005 - in Million of US$)

Value	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005 [b/]	Average		
												1995-1999	2000-2002	2003-2005 [b/]
Costa Rica	114	135	115	170	236	269	268	216	263	345	390	153.9	250.8	332.5
El Salvador	-54	-51	0	17	-11	-80	-98	-80	-121	-124	-101	-19.6	-86.0	-115.3
Guatemala	274	335	272	141	305	200	282	-98	258	340	418	265.4	128.2	338.4
Honduras	-207	-148	-181	-124	-151	-207	-105	-146	-332	-348	-485	-162.2	-152.5	-388.3
Nicaragua	-145	-159	-210	-295	-374	-326	-291	-178	-191	-310	-283	-236.7	-265.3	-261.0

Notes: [a/] Non-maquila.

[b/] Preliminary data for 2005.

SIECA data have been used for El Salvador (2005) and Guatemala (2005), and CBCR data for Costa Rica (1997-2005).

Source: Based on data from UN-Comtrade/SITC Rev. 2, SIECA and CBCR.

TABLE A20
CACM: SECTORAL COMPOSITION OF EXPORTS
(1995-2005 - % of Total)

Extrareional, excluding Maquila	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005 [a/]	Average		
												1995-1999	2000-2002	2003-2005 [a/]
Total	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*
Raw Materials	4.4	5.3	5.2	5.7	5.5	5.9	7.3	9.1	6.8	6.3	6.1	5.2	7.5	6.4
Foodstuffs	76.7	72.5	78.3	81.6	79.2	79.6	80.9	72.1	76.9	74.0	73.3	77.7	77.5	74.7
Metals	0.7	1.3	1.6	1.3	1.2	1.7	1.3	2.0	2.4	2.8	2.9	1.2	1.7	2.7
Fuels	1.0	1.6	2.0	1.5	2.5	4.4	4.0	4.9	5.0	3.9	4.6	1.7	4.4	4.5
Manufacturing	14.5	19.0	12.4	9.2	10.7	7.5	5.7	10.9	7.1	11.3	11.7	13.2	8.0	10.0
Others	2.6	0.3	0.5	0.7	0.9	0.8	0.9	0.9	1.8	1.6	1.4	1.0	0.9	1.6
Extraregional, including Maquila														
Total	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*
Raw materials	3.3	3.2	2.7	2.2	2.1	2.0	2.2	2.2	1.9	2.4	2.3	2.7	2.1	2.2
Foods	53.4	49.2	46.3	41.7	33.2	31.8	32.0	28.6	27.0	28.9	29.1	44.8	30.8	28.3
Metals	0.4	0.6	0.8	0.4	0.6	1.1	0.9	1.1	1.1	0.8	0.9	0.6	1.0	0.9
Fuels	0.5	0.6	0.7	0.5	0.4	0.5	0.5	0.5	0.4	0.7	0.8	0.5	0.5	0.6
Manufacturing	41.2	45.2	48.6	53.3	61.2	62.6	62.2	64.9	67.6	65.5	65.1	49.9	63.2	66.1
Others	1.1	1.2	0.9	1.8	2.4	2.0	2.2	2.8	2.0	1.8	1.7	1.5	2.3	1.8
Intraregional, excluding Maquila														
Total	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*
Raw materials	1.7	2.2	1.6	1.4	1.1	1.2	2.0	1.4	1.1	1.2	1.1	1.6	1.5	1.1
Foods	26.6	26.7	26.6	36.5	31.4	31.3	29.7	35.9	31.3	30.2	31.4	29.6	32.3	31.0
Metals	0.7	1.8	2.5	1.6	1.9	2.5	2.9	2.8	2.9	2.9	1.7	1.7	2.7	2.5
Fuels	2.3	2.2	4.6	2.9	3.7	3.7	3.2	2.8	1.4	1.4	1.3	3.1	3.2	1.4
Manufacturing	68.6	66.9	64.8	57.6	61.9	61.3	62.1	57.2	63.2	64.3	64.5	63.9	60.2	64.0
Others	0.0	0.2	0.0	0.0	0.0	0.1	0.0	0.0	0.0	0.0	0.0	0.1	0.0	0.0

Notes: [a/] Preliminary data for 2005, SIECA data have been used for El Salvador (2005) and Guatemala (2005).

Source: Based on data from UN-Comtrade/SITC Rev. 2 and SIECA.

TABLE A21
CACM: 20 MAIN EXPORT PRODUCTS INCLUDING MAQUILA
(2000-2005 - Average, Value in US$ million and % Share)

2000-2002					2003-2005				
Subitem	Description	Value	% Share	Cumulative Share	Subitem	Description	Value	% Share	Cumulative Share
080300	Bananas and Plantains	1,811	10.4	10.4	854213	Digital Monolithic Integrated Circuits	3,988	19.1	19.1
090111	Unroasted, Non-Decaffeinated Coffee	1,740	10	20.4	080300	Bananas and Plantains	1,970	9.4	28.5
611020	Knitted or Crocheted Sweaters	1,191	6.8	27.3	611020	Knitted or Crocheted Jerseys and Sweaters	1,625	7.8	36.3
854213	Digital Monolithic Integrated Circuits	1,048	6	33.3	847330	Machine Parts and Accessories	1,577	7.5	43.8
847330	Machine Parts and Accessories	1,043	6	39.3	090111	Unroasted, Non-Decaffeinated Coffee	1,436	6.9	50.7
610910	Knitted or Crocheted Undershirts	998	5.7	45.0	610910	Knitted or Crocheted Undershirts	1,279	6.1	56.8
620342	Long Pants, Briefs and Short Pants	580	3.3	48.3	080430	Pineapples	797	3.8	60.6
080430	Pineapples	416	2.4	50.7	620342	Long Pants, Briefs and Short Pants	588	2.8	63.4
170111	Unrefined Cane Sugar	369	2.1	52.9	901890	Other Instruments and Apparatus	481	2.3	65.7
620462	Long Pants, Briefs and Short Pants	354	2	54.9	170111	Unrefined Cane Sugar	448	2.1	67.9
610510	Men's Cotton Shirts	286	1.6	56.5	620462	Long Pants, Briefs and Short Pants	405	1.9	69.8
080719	Melons, Watermelons and Papayas	276	1.6	58.1	080719	Melons, Watermelons and Papayas	308	1.5	71.3
610711	Long or Short Underwear	264	1.5	59.6	854430	Ignition Cables	301	1.4	72.7
901890	Other Instruments and Apparatus	262	1.5	61.1	610711	Long or Short Underwear	254	1.2	73.9
621210	Brassieres	251	1.4	62.6	854230	Non-Digital Monolithic Integrated Circuits	251	1.2	75.1
620520	Men's Cotton Shirts	249	1.4	64.0	611030	Knitted or Crocheted Jerseys and Sweaters	249	1.2	76.3
610821	Panties	243	1.4	65.4	610821	Panties	238	1.1	77.5
030613	Frozen Shrimp	230	1.3	66.7	030613	Frozen Shrimp	235	1.1	78.6
610990	Knitted or Crocheted Undershirts	197	1.1	67.9	621210	Brassieres	229	1.1	79.7
060491	Foliage, Branches and Other Plant Parts	179	1	68.9	610462	Pants, Aprons and Overalls with Suspenders, Briefs and Short Pants	205	1.0	80.7
	Top 20 Exports Total	*11,984*	*68.9*			*Top 20 Exports Total*	*16,864*	*80.7*	

Notes: Maquila includes duty-free export zones. Export figures correspond to the sum of imports of the rest of the world from the CACM.

Source: Based on UN-Comtrade data, 1996 HS at 6 digits.

Table A22
CACM: 20 MAIN IMPORT PRODUCTS INCLUDING MAQUILA
(2000-2005 - Average, Value in US$ million and % Share)

2000-2002					2003-2005				
Subitem	**Description**	**Value**	**% Share**	**Cumulative Share**	**Subitem**	**Description**	**Value**	**% Share**	**Cumulative Share**
270900	Crude Petroleum and Bituminous Mineral Oils	524	2.0	2.0	271000	Petroleum Oils excluding Crude Oils	1,546	4.6	4.6
600292	Other Knitted Cotton Fabrics	488	1.9	4.0	854213	Metal-Oxide-Semiconductors	1,047	3.1	7.8
854213	Metal-Oxide-Semiconductors	469	1.8	5.8	600292	Other Knitted Cotton Fabrics	827	2.5	10.3
880240	Airplanes and Other Aircraft	455	1.8	7.6	300490	Medicaments, Others	402	1.2	11.5
610910	Cotton T-Shirts and Undershirts	451	1.8	9.3	270900	Crude Petroleum and Bituminous Mineral Oils	373	1.1	12.6
300490	Medicaments, Others	328	1.3	10.6	852520	Transmitters with Built-In Receptors	355	1.1	13.7
271000	Petroleum Oils excluding Crude Oils	247	1.0	11.6	870323	Other Personal Transport Automobile Vehicles	318	1.0	14.6
870323	Other Personal Transport Automobile Vehicles	234	0.9	12.5	880240	Airplanes and Other Aircraft	298	0.9	15.5
620342	Men's Cotton Pants	227	0.9	13.4	854290	Electronic Integrated Circuits and Microstructures	257	0.8	16.3
210690	Food Preparations, Others	206	0.8	14.2	100590	Corn, Others	231	0.7	17.0
611790	Other Clothing Accessories	192	0.7	14.9	847330	Machine Parts and Accessories	221	0.7	17.6
852520	Transmitters with Built-In Receptors	174	0.7	15.6	870421	Automobile Vehicles for Goods Transport	217	0.7	18.3
100590	Corn, Others	172	0.7	16.3	210690	Food Preparations, Others	215	0.6	18.9
621210	Brassieres	165	0.6	16.9	600230	Other Knitted Fabrics	192	0.6	19.5
847330	Machine Parts and Accessories	154	0.6	17.5	100190	Wheat and Maslin, Others	192	0.6	20.1
100190	Wheat and Maslin, Others	150	0.6	18.1	520512	Cotton Yarns	172	0.5	20.6
621790	Other Clothing Accessories, Parts	150	0.6	18.7	600210	Other Knitted Fabrics.	165	0.5	21.1
870421	Automobile Vehicles for Goods Transport	127	0.5	19.2	620342	Men's Cotton Pants	155	0.5	21.6
580710	Labels, Badges and Similar Woven Items	116	0.5	19.7	610910	Cotton T-Shirts and Undershirts	147	0.4	22.0
480411	Kraft Cardboard and Paper	112	0.4	20.1	480411	Kraft Cardboard and Paper	141	0.4	22.4
	Top 20 Imports Total	*5,139*	*20.1*			*Top 20 Imports Total*	*7,473*	*22.4*	

Note: Maquila includes duty-free export zones. Import figures correspond to the sum of exports of the rest of the world from the CACM.

Source: Based on UN-Comtrade data, 1996 HS at 6 digits.

TABLE A23
CACM: 20 MAIN INTRAREGIONAL EXPORT PRODUCTS [a/]
(2000-2005 - Average, Value in US$ million and % Share)

2000-2002					2003-2005				
Subitem	**Description**	**Value**	**% Share**	**Cumulative Share**	**Subitem**	**Description**	**Value**	**% Share**	**Cumulative Share**
300490	Medicaments	126	4.6	4.6	300490	Medicaments	146	4.4	4.4
210690	Other Food Preparations	96	3.5	8.2	210690	Other Food Preparations	128	3.9	8.3
721041	Laminated Products, Iron Sheeting	46	1.7	9.8	340119	Soap in Bar or Table t Form, Others	57	1.7	10.1
340111	Soap in Bar and Table t Form	45	1.6	11.5	271000	Petroleum Oils	53	1.6	11.7
721420	Iron and Steel Bars and Rods	38	1.4	12.9	220210	Water, Mineral Water and Sodas	50	1.5	13.2
190410	Cereal-Based Preparations	38	1.4	14.2	190410	Cereal-Based Preparations	43	1.3	14.6
170490	Other Confectionary Items without Cocoa	34	1.2	15.5	392330	Plastic Packing Items	42	1.3	15.8
271000	Petroleum Oils	30	1.1	16.6	721041	Laminated Products, Iron Sheeting	41	1.2	17.1
481910	Paper and Cardboard Boxes	30	1.1	17.7	721420	Iron and Steel Bars and Rods	35	1.1	18.1
151190	Refined Oil and Fractions	29	1.1	18.8	340220	Laundry and Cleaning Preparations	34	1.0	19.2
220210	Water, Mineral Water and Sodas	29	1.1	19.8	190530	Cookies, Waffles and Wafers	34	1.0	20.2
481840	Sanitary Towels, Tampons and Diapers	29	1.0	20.9	151190	Refined Oil and Fractions	33	1.0	21.2
481810	Toilet Paper	27	1.0	21.9	190590	Other Baking and Confectionary Products	32	1.0	22.2
190530	Cookies, Waffles and Wafers	27	1.0	22.9	854459	Other Electrical Conductors	32	1.0	23.2
701091	Carafes, Bottles, Jars, and Other Glass Containers	26	1.0	23.8	380830	Herbicides and Anti-Germinating Products	32	1.0	24.2
720429	Other Scrap Steel	26	0.9	24.8	481910	Paper and Cardboard Boxes	31	0.9	25.1
151110	Untreated Oils	24	0.9	25.7	481810	Toilet Paper	30	0.9	26.0
854459	Other Electrical Conductors	24	0.9	26.5	701092	Plugs, Lids and Other Glass Stoppers	30	0.9	26.9
340220	Laundry and Cleaning Preparations	23	0.9	27.4	210390	Other Sauces and Sauce Preparations	30	0.9	27.8
071332	Beans	23	0.8	28.2	481840	Sanitary Towels, Tampons and Diapers	29	0.9	28.7
	Top 20 Exports Total	*771*	*28.2*			*Top 20 Exports Total*	*942*	*28.7*	

Notes: [a/] With maquila (which includes duty-free export zones) for Costa Rica (2000-2005) and Guatemala (2005). El Salvador’s exports for 2005 are excluded.

Source: Based on UN-Comtrade data, 1996 HS at 6 digits.

TABLE A24
CACM: 20 MAIN INTRAREGIONAL IMPORT PRODUCTS [a/]
(2000-2005 - Average, Value in US$ million and % Share)

2000-2002					2003-2005				
Subitem	**Description**	**Value**	**% Share**	**Cumulative Share**	**Subitem**	**Description**	**Value**	**% Share**	**Cumulative Share**
300490	Medicaments, Others	102	3.6	3.6	300490	Medicaments, Others	124	3.7	3.7
210690	Food Preparations, Others	84	3	6.5	210690	Food Preparations, Others	117	3.5	7.1
721041	Flat Iron and Steel Sheeting	52	1.8	8.4	190410	Cereal-Based Preparations	53	1.6	8.7
721420	Iron and Steel Bars and Rods	45	1.6	9.9	220210	Water, Mineral Water and Sodas	52	1.6	10.3
340220	Laundry and Cleaning Preparations	45	1.6	11.5	392330	Bottles, Jars and Similar Items	50	1.5	11.8
340111	Soap in Bar and Table t Form	42	1.5	13	340119	Soap in Bar and Table t Form, Others	49	1.4	13.2
190410	Cereal-Based Preparations	42	1.5	14.5	481810	Toilet Paper	47	1.4	14.6
481910	Cardboard and Corrugated Paper	36	1.3	15.8	340220	Laundry and Cleaning Preparations	47	1.4	16
220210	Water, Mineral Water and Sodas	32	1.1	16.9	721420	Iron and Steel Bars and Rods	41	1.2	17.2
271600	Electrical Energy	31	1.1	18	190590	Baking and Confectionary Products	38	1.1	18.3
481810	Toilet Paper	30	1	19	190530	Cookies, Waffles and Wafers	38	1.1	19.5
701091	Plugs, Lids and Other Glass Stoppers	30	1	20.1	721041	Flat Iron and Steel Sheeting	37	1.1	20.6
340119	Soap in Bar or Table t Form, Others	29	1	21.1	240220	Cigarettes	33	1	21.5
190530	Cookies, Waffles and Wafers	28	1	22.1	151190	Palm Oil, Others	33	1	22.5
481840	Sanitary Towels, Tampons and Diapers	28	1	23.1	481910	Cardboard and Corrugated Paper	31	0.9	23.4
110220	Cornflour	27	0.9	24	481840	Sanitary Towels, Tampons and Diapers	30	0.9	24.3
151190	Refined Oil and Fractions	26	0.9	24.9	854459	Electrical Conductors	30	0.9	25.2
854459	Electrical Conductors	26	0.9	25.8	210390	Sauces, Condiments, Others	29	0.9	26.1
190590	Baking and Confectionary Products	25	0.9	26.7	701092	Plugs, Lids and Other Glass Stoppers	29	0.8	26.9
230990	Animal Feed	24	0.9	27.6	271000	Petroleum, Oils	27	0.8	27.7
	Top 20 Imports Total	*787*	*27.6*			*Top 20 Imports Total*	*934*	*27.7*	

Notes: [a/] With maquila (which includes duty-free export zones) for Costa Rica (2000-2005) and Guatemala (2005). El Salvador's exports for 2005 are excluded.

Source: Based on UN-Comtrade data, 1996 HS at 6 digits.

TABLE A25

COSTA RICA: 20 MAIN INTRAREGIONAL EXPORTS/IMPORTS [a/]

(2003-2005 - Average, Value in US$ million and % Share)

Exports					Imports				
Subitem	**Description**	**Value**	**% Share**	**Cumulative Share**	**Subitem**	**Description**	**Value**	**% Share**	**Cumulative Share**
210690	Other Food Preparations	101	15.2	15.2	340220	Laundry and Cleaning Preparations	18	5.3	5.3
300490	Medicaments, Others	74	11.2	26.5	071333	Beans	14	4.1	9.5
481840	Sanitary Towels, Tampons and Diapers	28	4.3	30.7	300490	Medicaments, Others	14	4.1	4.1
854459	Electrical Conductors	24	3.7	34.4	190410	Cereal-Based Preparations	12	3.7	7.8
210390	Sauces, Condiments, Others	23	3.5	37.9	271000	Petroleum, Oils	10	3.1	3.1
841821	Compension Refrigerators	19	2.8	40.7	610721	Cotton Nightdresses and Pajamas	9	2.7	5.8
701092	Plugs, Lids and Other Glass Stoppers	18	2.7	43.4	240220	Tobacco Cigarettes	8	2.6	2.6
721041	Laminated Products, Iron Sheeting	18	2.7	46	330610	Toothpaste	8	2.4	5
190530	Cookies, Waffles and Wafers	15	2.3	48.3	400122	Natural Rubber	7	2	2
392330	Plastic Packing Items	14	2.1	50.4	110100	Wheat Flour	6	1.7	3.7
550810	Synthetic Fiber Thread	12	1.8	52.2	392321	Items for Ethylene Polymer Packing	5	1.6	1.6
151190	Refined Oil and Fractions	11	1.7	53.9	481810	Toilet Paper	5	1.6	3.2
380820	Fungicides	9	1.4	55.3	210690	Other Food Preparations	5	1.4	1.4
210320	Ketchups and Other Tomato Sauces	9	1.4	56.7	721049	Iron and Steel Laminates, Others	4	1.3	2.7
380830	Herbicides	9	1.3	58	620342	Long Pants, Briefs and Short Pants	4	1.2	1.2
391723	Tubes and Tubing Accessories	9	1.3	59.3	340111	Soap in Bar and Table t Form	4	1.2	2.4
040120	Milk with 1-6% Fat	9	1.3	60.6	640399	Leather Shoes, Others	4	1.1	1.1
401110	Automobiles Tires	9	1.3	61.9	210410	Soup, Pottage and Broth Preparations	4	1.1	2.2
732111	Gas-Fuelled Stoves	9	1.3	63.2	380820	Fungicides	3	1	1
040221	Powdered Milk	8	1.2	64.4	380810	Insecticides	3	1	2.1
	Top 20 Exports Total	*427*	*49*			*Top 20 Imports Total*	*147*	*40*	

Note: [a/] With maquila (which includes duty-free export zones).

Source: Based on UN-Comtrade data, 1996 HS at 6 digits.

Table A26
EL SALVADOR: 20 MAIN INTRAREGIONAL EXPORTS/IMPORTS
(2003-2005 - Average, Value in US$ million and % Share)

Exports					Imports				
Subitem	Description	Value	% Share	Cumulative Share	Subitem	Description	Value	% Share	Cumulative Share
271000	Petroleum Oils	39	5	5	271600	Electrical Energy	29	3.1	3.1
300490	Medicaments, Others	29	3.7	8.7	340119	Soap in Bar or Table t Form, Others	23	2.6	5.7
481810	Toilet Paper	28	3.6	12.3	210690	Other Food Preparations	23	2.5	8.3
190410	Cereal-Based Preparations	27	3.4	15.8	220210	Water, Mineral Water and Sodas	22	2.4	10.6
340220	Laundry and Cleaning Preparations	25	3.1	18.9	300490	Medicaments, Others	20	2.2	12.9
210690	Other Food Preparations	24	3.1	22	020130	Deboned Beef	20	2.2	15.1
392330	Plastic Packing Items	18	2.3	24.3	151190	Refined Oil and Fractions	17	1.9	17
481910	Paper and Cardboard Boxes	16	2.1	26.4	020110	Beef Carcasses	15	1.7	18.7
190490	Cereal-Based Products	14	1.7	28.1	151620	Vegetable Fats and Oils and Fractions	15	1.7	20.4
220210	Water, Mineral Water and Sodas	13	1.7	29.8	80300	Banana Trees and Plantains	14	1.6	22
721420	Iron and Steel Bars and Rods	13	1.7	31.5	151110	Untreated Oils	14	1.6	23.5
220290	Water, Mineral Water and Sodas, Others	12	1.5	33	070200	Fresh and Refrigerated Tomatoes	13	1.5	25
720917	Laminated Products, Iron Sheeting	12	1.5	34.5	040630	Melted Cheese	11	1.2	26.2
760429	Aluminum Bars and Frames	12	1.5	36	040690	Other Cheeses	11	1.2	27.4
392410	Plastic Plates and Dishes	12	1.5	37.5	721420	Iron Bars Grooves and Reliefs	10	1.1	28.6
300420	Antibiotics	10	1.3	38.7	010290	Bovine Livestock	10	1.1	29.7
841821	Compension Refrigerators	9	1.2	39.9	721041	Iron Bars, Corrugated Iron	10	1.1	30.7
190530	Cookies, Waffles and Wafers	9	1.2	41.1	392330	Plastic Packing Items	9	1	31.7
200980	Fruit and Vegetable Juices	9	1.2	42.2	730630	Pipes for Oil Pipelines	9	1	32.7
170490	Confectionary Items without Cocoa	9	1.1	43.3	240220	Cigarettes	9	1	33.7
	Top 20 Exports Total	*340*	*43.3*			*Top 20 Imports Total*	*305*	*33.7*	

Source: Based on UN-Comtrade data, 1996 HS at 6 digits.

TABLE A27
GUATEMALA: 20 MAIN INTRAREGIONAL EXPORTS/IMPORTS [a/]
(2003-2005 - Average, Value in US$ million and % Share)

Exports					Imports				
Subitem	**Description**	**Value**	**% Share**	**Cumulative Share**	**Subitem**	**Description**	**Value**	**% Share**	**Cumulative Share**
300490	Medicaments, Others	49	3.9	3.9	210690	Other Food Preparations	45	5	5
220210	Water, Mineral Water and Sodas	33	2.6	6.6	300490	Medicaments, Others	42	4.6	9.6
190410	Cereal-Based Preparations	23	1.9	8.4	392330	Bottles, Jars and Similar Items	20	2.2	11.8
380830	Herbicides	22	1.8	10.2	481910	Cardboard and Corrugated Paper	17	1.9	13.7
330610	Toothpaste	22	1.7	11.9	481810	Toilet Paper	17	1.9	15.5
721041	Laminated Products, Iron Sheeting	22	1.7	13.7	190590	Baking and Confectionary Products	14	1.6	17.1
300450	Vitamins	22	1.7	15.4	340119	Soap in Bar or Table t Form, Others	14	1.6	18.6
271112	Propane	19	1.5	16.9	481840	Sanitary Towels, Tampons and Diapers	14	1.5	20.2
210410	Soup, Pottage and Broth Preparations	18	1.5	18.4	190530	Cookies, Waffles and Wafers	14	1.5	21.7
271000	Petroleum, Oils	18	1.5	19.8	721420	Iron and Steel Bars and Rods	14	1.5	23.2
850610	Magnesium Batteries	18	1.4	21.2	190410	Cereal-Based Preparations	14	1.5	24.7
690890	Ceramic Slabs and Tiles, Others	17	1.3	22.6	271000	Petroleum, Oils	13	1.4	26.1
721420	Iron and Steel Bars and Rods	16	1.3	23.8	220290	Water, Mineral Water and Sodas, Others	12	1.4	27.4
391723	Tubes and Tubing Accessories	16	1.3	25.1	190490	Cereal-Based Products	12	1.4	28.8
340220	Laundry and Cleaning Preparations	16	1.2	26.3	720410	Waste and Waste Products	11	1.3	30.1
330300	Perfumes and Toilet Waters	16	1.2	27.6	854459	Electrical Conductors	11	1.2	31.3
340290	Laundry and Cleaning Preparations, Others	15	1.2	28.8	220210	Water, Mineral Water and Sodas	11	1.2	32.5
380810	Insecticides	14	1.2	29.9	340220	Laundry and Cleaning Preparations	10	1.1	33.6
151620	Vegetable Fats and Oils and Fractions	14	1.1	31	481910	Cardboard and Corrugated Paper	9	1	34.6
340119	Soap in Bar or Table t Form, Others	14	1.1	32.2	481920	Cardboard Boxes	8	0.9	35.5
	Top 20 Exports Total	*401*	*32.2*			*Top 20 Imports Total*	*323*	*35.5*	

Note: [a/] With maquila (which includes duty-free export zones) for 2005.

Source: Based on UN-Comtrade data, 1996 HS at 6 digits.

TABLE A28
HONDURAS: 20 MAIN INTRAREGIONAL EXPORTS/IMPORTS
(2003-2005 - Average, Value in US$ million and % Share)

Exports					Imports				
Subitem	Description	Value	% Share	Cumulative Share	Subitem	Description	Value	% Share	Cumulative Share
340119	Soap in Bar or Table t Form, Others	39	12.8	12.8	210690	Other Food Preparations	38	5.5	5.5
151190	Refined Oil and Fractions	16	5.2	18.0	300490	Medicaments, Others	32	4.7	10.2
240220	Cigarettes	13	4.4	22.3	220210	Water, Mineral Water and Sodas	19	2.7	12.9
190590	Baking and Confectionary Products	10	3.4	25.7	481810	Toilet Paper	17	2.5	15.4
293629	Vitamins	8	2.7	28.5	721041	Iron and Steel Bars, Corrugated Iron	15	2.2	17.6
721420	Iron and Steel Bars and Rods	7	2.4	30.9	10290	Bovine Livestock	12	1.7	19.4
481910	Cardboard and Corrugated Paper	7	2.3	33.2	190410	Cereal-Based Preparations	12	1.7	21.0
170490	Confectionary Items without Cocoa	7	2.2	35.4	721420	Iron and Steel Bars and Rods	11	1.6	22.6
854459	Electrical Conductors	6	1.9	37.3	110220	Cornflour	11	1.6	24.2
392330	Bottles, Jars and Similar Items	6	1.9	39.2	190590	Baking and Confectionary Products	11	1.6	25.8
761410	Electrical Cables and Plaited Bands	5	1.8	41.0	210390	Sauces, Condiments, Others	10	1.5	27.2
290410	Hydrocarbon Derivates	5	1.8	42.8	392330	Bottles, Jars and Similar Items	10	1.4	28.6
070200	Fresh and Refrigerated Tomatoes	5	1.6	44.4	391723	Tubes and Tubing Accessories	10	1.4	30
151110	Untreated Oils	5	1.6	46.1	481840	Sanitary Towels, Tampons and Diapers	9	1.3	31.4
210320	Ketchups and Other Tomato Sauces	4	1.3	47.4	190530	Cookies, Waffles and Wafers	9	1.3	32.7
320990	Paints and Varnishes	4	1.2	48.6	340290	Laundry and Cleaning Preparations, Others	9	1.3	34.0
392321	Items for Ethylene Polymer Packing	3	1.1	49.7	230990	Animal Feed	9	1.3	35.2
482020	Notebooks	3	1.1	50.8	701092	Plugs, Lids and Other Glass Stoppers	8	1.2	36.4
481920	Cardboard Boxes	3	1	51.8	854459	Electrical Conductors	8	1.2	37.6
210690	Other Food Preparations	3	0.9	52.7	210410	Soup, Pottage and Broth Preparations	7	1	38.6
	Top 20 Exports Total	*160*	*52.7*			*Top 20 Imports Total*	*267*	*38.6*	

Source: Based on UN-Comtrade data, 1996 HS at 6 digits.

Table A29
NICARAGUA: 20 MAIN INTRAREGIONAL EXPORTS/IMPORTS
(2003-2005 - Average, Value in US$ million and % Share)

Exports					Imports				
Subitem	**Description**	**Value**	**% Share**	**Cumulative Share**	**Subitem**	**Description**	**Value**	**% Share**	**Cumulative Share**
020130	Deboned Beef	28	11.9	11.9	300490	Medicaments, Others	22	4.5	4.5
010290	Bovine Livestock	27	11.5	23.3	151190	Palm Oil, Others	15	3.1	7.6
020110	Beef in Carcasses	15	6.5	29.9	210690	Food Preparations, Others	14	2.8	10.4
071332	Beans	12	5.2	35.1	721041	Flat Iron and Steel Sheeting	13	2.7	13.0
040690	Other Cheeses	11	4.5	39.6	240220	Cigarettes	13	2.6	15.6
110100	Wheat Flour	8	3.5	43.1	392330	Bottles, Jars and Similar Items	12	2.5	18.1
040630	Melted Cheese	8	3.4	46.5	190410	Cereal-Based Preparations	12	2.4	20.5
071333	White Beans	8	3.2	49.8	340119	Soap in Bar or Table t Form, Others	12	2.4	22.9
271000	Petroleum, Oils	7	2.9	52.6	252310	Unpulverised Cement (Clinker)	8	1.7	24.6
210111	Coffee Extracts, Essences and Concentrates	5	2.3	54.9	190530	Cookies, Waffles and Wafers	8	1.7	26.3
120220	Huskless Peanuts or Monkey Nuts	5	2.1	57.0	721049	Iron and Steel Laminates, Others	8	1.6	27.8
040221	Powdered Milk	5	2.0	59.0	701092	Plugs, Lids and Other Glass Stoppers	8	1.5	29.3
220210	Water, Mineral Water and Sodas	4	1.8	60.9	220210	Water, Mineral Water and Sodas	7	1.5	30.8
190590	Baking and Confectionary Products	4	1.7	62.6	721420	Iron and Steel Bars and Rods	7	1.5	32.3
020230	Deboned Frozen Beef	4	1.7	64.2	391723	Tubes and Piping Accessories	7	1.3	33.6
691010	Ceramic Washbowls and Toilets	4	1.6	65.8	340220	Laundry and Cleaning Preparations	7	1.3	35.0
210112	Coffee Preparations	3	1.4	67.2	110100	Wheat Flour	6	1.2	36.2
440710	Coniferous Woods	3	1.4	68.5	481810	Toilet Paper	5	1.1	37.3
240110	Non-Deveined and Non-Denerved Tobacco	3	1.1	69.7	850610	Manganese Dioxide	5	1.0	38.3
210500	Ice Creams, including Cocoa	3	1.1	70.8	170490	Confectionary Items without Cocoa	5	1.0	39.3
	Top 20 Exports Total	*167*	*70.8*			*Top 20 Imports Total*	*195*	*39.3*	

Source: Based on UN-Comtrade data, 1996 HS at 6 digits.

TABLE A30
CACM: FDI BY COUNTRY OF DESTINATION
(1997-2005 - Flows, Value in US$ million, Share in Total and % GDP)

Value	1997	1998	1999	2000	2001	2002	2003	2004	2005[a]	Average		
										1997-1999	2000-2002	2003-2005[a]
Total	*850*	*2,682*	*1,528*	*1,386*	*1,580*	*1,438*	*1,405*	*2,070*	*2,302*	*1,686*	*1,468*	*1,926*
Costa Rica	407	612	619	409	460	660	575	794	861	546	509	743
El Salvador	59	1,104	216	174	279	208	130	407	425	460	220	320
Guatemala	84	673	155	230	456	111	131	155	208	304	266	165
Honduras	128	99	237	307	234	255	368	465	568	155	266	467
Nicaragua	172	195	300	267	150	204	201	250	241	222	207	231
Share												
Total	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*
Costa Rica	47.9	22.8	40.5	29.5	29.1	45.9	40.9	38.3	37.4	37.1	34.8	38.9
El Salvador	6.9	41.1	14.1	12.5	17.6	14.5	9.2	19.6	18.4	20.7	14.9	15.8
Guatemala	9.9	25.1	10.1	16.6	28.9	7.7	9.3	7.5	9.0	15.0	17.7	8.6
Honduras	15.0	3.7	15.5	22.2	14.8	17.8	26.2	22.4	24.7	11.4	18.2	24.4
Nicaragua	20.3	7.3	19.6	19.2	9.5	14.2	14.3	12.1	10.5	15.7	14.3	12.3
% GDP												
Total	*1.7*	*4.9*	*2.7*	*2.4*	*2.6*	*2.2*	*2.1*	*2.8*	*2.8*	*3.1*	*2.4*	*2.6*
Costa Rica	3.2	4.3	3.9	2.6	2.8	3.9	3.3	4.3	4.3	3.8	3.1	4.0
El Salvador	0.5	9.2	1.7	1.3	2.0	1.5	0.9	2.6	2.5	3.8	1.6	2.0
Guatemala	0.5	3.5	0.8	1.2	2.2	0.5	0.5	0.6	0.7	1.6	1.3	0.6
Honduras	2.7	1.9	4.4	5.1	3.7	3.9	5.3	6.2	6.8	3.0	4.2	6.1
Nicaragua	5.1	5.4	8.0	6.8	3.6	5.1	4.9	5.6	4.9	6.2	5.2	5.1

Notes: [a] Preliminary data for 2005.

The figures include FDI in the maquila (which includes duty-free export zones). The maquila for Honduras is included as from 2000.

GDP for Honduras and Nicaragua may be underestimated and as a result the shares in GDP may be overestimated.

Source: Based on data from UNCTAD's *World Investment Report* and Central American Central Banks.

TABLE A31
CACM: FDI BY SECTOR OF DESTINATION
(1997-2005 - Flows, US$ million)

Value	1997	1998	1999	2000	2001	2002	2003	2004	2005 [a]	Average		
										1997-1999	2000-2002	2003-2005 [a]
Total	707	2,009	1,373	1,156	1,129	1,332	1,277	1,915	2,095	1,363	1,206	1,762
Primary	71	98	171	18	49	33	-3	125	72	113	33	65
Agriculture and Fisheries	49	67	112	-7	38	4	-25	84	57	76	12	39
Mining	21	31	59	25	11	29	22	41	15	37	22	26
Secondary	173	859	468	515	225	383	248	169	358	500	374	258
Agribusiness	10	34	27	44	49	25	49	3	39	24	39	31
Industry	135	167	195	269	145	325	192	202	373	166	246	256
Energy and Public Services	29	657	246	202	31	34	7	-36	-54	311	89	-28
Tertiary	258	595	472	300	559	548	511	1,004	1,025	442	469	847
Trade	143	162	168	137	96	115	110	180	268	158	116	186
Communications	17	270	72	11	144	209	173	491	186	119	121	283
Real Estate	13	25	2	24	25	27	41	212	239	14	25	164
Financial Services	0	62	121	43	85	32	-11	10	143	61	53	47
Tourism	79	61	85	52	112	76	88	41	54	75	80	61
Other Services	6	14	24	32	98	90	110	71	135	15	73	105
Maquila [b]	195	454	244	311	260	364	511	603	640	298	312	585
Others	10	5	17	13	37	3	10	14	0	11	18	8

Notes: [a] Preliminary data for 2005.

[b] The figures include FDI in the maquila (which includes duty-free export zones). The data for Guatemala are excluded. The maquila for Honduras is included as from 2000.

Source: Based on data from UNCTAD's *World Investment Report* and Central American Central Banks.

TABLE A32
CACM: FDI BY COUNTRY/REGION OF ORIGIN
(1997-2005 - Flows, Value in US$ million and % Share)

Value	1997	1998	1999	2000	2001	2002	2003	2004	2005[a/]	Average		
										1997-1999	2000-2002	2003-2005 [a/]
Total A	*850*	*2,682*	*1,528*	*1,386*	*1,580*	*1,438*	*1,405*	*2,070*	*2,302*	*1,686*	*1,468*	*1,926*
Total B	*707*	*2,009*	*1,373*	*1,156*	*1,129*	*1,332*	*1,277*	*1,915*	*2,095*	*1,363*	*1,206*	*1,762*
Extraregional	602	1,904	1,238	1,059	1,023	1,205	1,212	1,785	1,973	1,248	1,096	1,656
United States	401	907	757	500	490	632	763	733	881	688	541	793
EU - 25	63	311	88	364	254	362	196	115	463	154	326	258
Latin America	44	523	207	73	147	124	121	756	327	258	115	401
Asia	25	29	30	41	16	8	27	7	4	28	21	13
Others	71	135	155	82	117	79	104	174	297	120	93	192
Intraregional	105	105	135	97	106	127	66	130	122	115	110	106
% Share												
Total B	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*	*100.0*
Extraregional	85.1	94.8	90.2	91.6	90.6	90.5	94.9	93.2	94.2	90.0	90.9	94.1
United States	56.7	45.1	55.2	43.3	43.4	47.4	59.8	38.3	42.1	52.3	44.7	46.7
EU - 25	8.8	15.5	6.4	31.5	22.5	27.2	15.4	6.0	22.1	10.2	27.0	14.5
Latin America	6.2	26.0	15.1	6.3	13.0	9.3	9.5	39.5	15.6	15.8	9.5	21.5
Asia	3.5	1.4	2.2	3.5	1.4	0.6	2.1	0.4	0.2	2.4	1.8	0.9
Others	10.0	6.7	11.3	7.1	10.4	6.0	8.1	9.1	14.2	9.3	7.8	10.5
Intraregional	14.9	5.2	9.8	8.4	9.4	9.5	5.1	6.8	5.8	10.0	9.1	5.9

Notes: [a/] Preliminary data for 2005.

Total A: Including totals for Guatemala.

Total B: Excluding Guatemala.

The figures include FDI in the maquila (which includes duty-free export zones). The maquila for Honduras is included as from 2000.

Source: Based on data from UNCTAD's *World Investment Report* and Central American Central Banks.

Contents

ANNEX III. A GENERAL FRAMEWORK FOR CUSTOMS UNION NEGOTIATION IN CENTRAL AMERICA

June 29, 2004

The legal instruments of Central American integration define the stages by which the States have chosen to accomplish economic integration. Realization of CU is mandatory in such efforts. To achieve this Central America is doing its best to consolidate freedom of trade in goods regardless of their origin (subject to nationalization in one or other of the Member States of products from third countries), freedom of trade in services and the mobility of people in the region.

To reap the maximum benefits from CU in Central America it is important for negotiations to be conducted pragmatically and straightforwardly to reach a satisfactory agreement in a reasonable timeframe. It is ratified that the job of conducting the negotiations will fall to Central America's Council of Ministers for Economic Integration (COMIECO - *Consejo de Ministros de la Integración Económica*). The following ideas are presented to this effect in connection with the process of CU negotiation.

1. Vision

To gradually and progressively achieve CU and bring to a close this stage of the Central American integration process through the coordination, harmonization and convergence of economic policy, bearing in mind that the expansion of domestic markets through integration is a necessary requirement in boosting development in the region.

2. Objective

To achieve fair and sustainable economic and social development for Central American countries, and to translate this into the wellbeing of their populations and the growth of all member countries through a process enabling the transformation and modernization of their productive, social and technological structures, to raise competitiveness and to achieve efficiently and dynamically reinsert Central America in the international economy. In other words, this objective is the basic objective of the Economic Integration Subsystem as provided for in Article 3 of the Protocol of Guatemala, which refers to the objectives and principles of Central American economic integration.

3. General Principles

1. *Legality*: Strict adherence to the Constitutions of Member States, as well as the legal and institutional framework of the SICA and its complementary and derivative instruments as laid down in Section d) of Articles 1 and 5 of the Protocol of Guatemala.

2. *Graduality*: CU is to be reached through programs enabling this phase to be achieved gradually and progressively, as stated in Articles 5 and 15 of the Protocol of Guatemala and in Literal e) of Article 4 of the Protocol of Tegucigalpa. This does not prevent two or more countries from expediting their integration commitments. These decisions are only binding for those approving them, according to the principle of promptness as stated in Articles 6 and 52 of the Protocol of Guatemala.

3. *Flexibility*: Progress should meet the needs of the countries linked to this effort and attend to the convergence of wills and policies as defined in Literal b) of Article 1 and in Article 5 of the Protocol of Guatemala.

4. *Consensus*: This implies the adoption by consensus of the programs to be established in order to achieve the objective as stated in Articles 5, 15 and 52 of the Protocol of Guatemala.

5. *Transparency*: This will guarantee a procedure open to access by the public and the publicity of the resolutions adopted by the Subsystem's Organs as stated in Article 5 of the Protocol of Guatemala and Article 10 of the Protocol of Tegucigalpa. In other words, it privileges consultations with the sectors involved. All sectors linked to decision-taking in matters of economic integration should be kept fully informed and decisions should be widely circulated.

4. Negotiation Structure

1. COUNCIL OF MINISTERS FOR ECONOMIC INTEGRATION (COMIECO) MEETINGS: The forum of the COMIECO consists of Ministers responsible for economic integration matters in each Member State, as stated in Paragraph 1 Article 38 of the Amendment to the Protocol of Guatemala.

2. VICE MINISTERS FOR ECONOMIC INTEGRATION MEETINGS: The forum of Vice Ministers for Economic Integration consists of Vice Ministers responsible for matters of economic integration in each Member State. It is the job of this forum to assist the COMIECO in its Meetings, to be familiar with any matters and recommendations emerging from the meetings of Integration, Customs, Internal Revenue and Migration Directors, and directors of technical groups and committees, as well as studying and deciding certain matters delegated to it by the Council of Ministers.

3. DIRECTORS MEETINGS:

a) *Economic Integration Directors*: The Economic Integration Directors' Meetings are the technical forum for assessment and proposal in matters of intraregional trade. It is this forum's job to define tariff policy and inform the Vice Ministers for Economic Integration.

b) *Customs Directors*: The Customs Directors' Meetings are the technical forum for assessment and proposal in matters of intraregional customs. It is this forum's job to define customs policy and inform the Vice Ministers for Economic Integration.

c) *Internal Revenue Directors*: The Internal Revenue Directors' Meetings are the technical forum for assessment and proposal in matters of internal revenue. It is this forum's job to define taxation policy, harmonize technical structures (including collection mechanisms), and inform the Vice Ministers for Economic Integration.

d) *Migration Directors*: The Migration Directors' Meetings are the technical forum for assessment and proposal in matters of migration. It is this forum's job to define migratory policy to facilitate the mobility of Central Americans in the region and inform Vice Ministers for Economic Integration.

4. TECHNICAL GROUPS AND COMMITTEES MEETINGS: A simple structure is favored, which yet enables the various negotiation areas for the components of CU to have access to the relevant specialists and timeframes for their respective negotiations. The following groups and committees are already part of the institutional fabric of certain areas of the economic integration process:

a) A Tariff Technical Group

b) A Registries Technical Group

c) An Agricultural Group

d) A Safeguards Group

e) An Intellectual Property Group

f) A Rules of Origin Group

g) A Standardization Committee

h) A Sanitary and Phytosanitary Measures Committee

5. SECRETARIAT: The SIECA will attend all meetings as a Secretariat at ministerial, vice ministerial, directorial, group and committee levels.

6. PRODUCTIVE SECTOR PARTICIPATION: The participation of the private sector in the negotiations will be under the modality of the attached room in negotiation meetings at the levels of Ministers, Vice Ministers, Directors and Negotiation Groups. All necessary national spaces will be made available to enable a timely, transparent process of consultation with the productive sectors, as agreed in COMIECO-25 Resolution N° 102-2002 of December 12, 2002.

5. The Modalities of Meetings

To further consolidation of CU in the timeframes established by the Presidents, it will be necessary to immediately follow up on the negotiations and results of each of the work areas as follows:

1. The Technical Groups and Committees meetings will be held simultaneously and coordinated through meetings of Economic Integration Directors, who will receive reports on the groups and committees' results and issue any relevant instructions;

2. Vice Ministers for Economic Integration will assemble at the end of this meeting to receive the Economic Integration Directors' report, provide any necessary guidelines and draw up the report for the Ministers' meeting;

3. The Ministers for Economic Integration will provide periodic guidelines.

6. Cooperation

Given the region's level of development, the promotion of cooperation of friendly countries and organizations such as the European Union and the Inter-American Development Bank is felt to be of vital importance in implementing specific projects in high-priority areas for each Member State. To achieve this the region feels it is advisable to step up the activities of the Cooperation Coordination Committee, consisting of each country's Vice Minister for Foreign Trade -or some appointed representative- and the Director for Foreign Trade. The Committee will be responsible for handling all cooperation matters relating to the trade agenda of the Central American Integration Ministries, while recognizing that there is an opportunity to forge alliances between the region and the various different trading partners and international organizations in order to support Central American countries in reaping the benefits of this process, for example the use of the social cohesion fund.

7. Central American Integration Commissioners

This forum will support the Council of Ministers for External Relations and the Intersectoral Council of Ministers for External Relations and Ministers of Economic Integration (COMIECO).

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