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# The Trade and Cooperation Nexus: How Does the Mercosur-EU Process Measure Up?

Robert Devlin  
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Ekaterina Krivonos

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# THE TRADE AND COOPERATION NEXUS: HOW DOES THE MERCOSUR-EU PROCESS MEASURE UP?

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*The objective of this study is to analyze the interaction between trade and non-trade cooperation in some of the today's major regional initiatives, particularly those between developing and industrialized countries. The study suggests a framework to explore what the paper calls a "trade and cooperation nexus". The modalities of this nexus can take different forms. For instance, non-trade cooperation may be an integral part of a formal trade or integration agreement, or may take place independently of such an agreement, as an ex-ante, ex-post or parallel agreement. This paper analyzes the EU approach, which proposes an unusually tight trade and cooperation nexus based on a three-pillar approach uniting political, economic and trade cooperation under a single umbrella agreement. Theoretically this approach should be attractive, especially in North-South agreements, because the promise of linking free trade with cooperation programs could enhance the benefits of the former for both parties. However, while innovative, the nexus is challenging in its construction and delivery. The paper will explore EU efforts in this area in the broader context of what is happening in other North-South initiatives.*

## I. INTRODUCTION

The objective of this study is to analyze the interaction between trade and non-trade cooperation in some of the today's major regional initiatives, particularly those between developing and industrialized countries. The study suggests a framework to explore what we call a "trade and cooperation nexus".

Today many regional cooperation initiatives are initially launched via formal integration agreements that eliminate trade barriers as part of creation of a free trade area or customs union. There are, however, a large number of other areas in which cooperation can take place to the mutual advantage of all actors. Non-trade-related cooperation may be an integral part of an integration agreement, or may take place independently of such an agreement. This latter form of interaction has been termed "functional cooperation" by Balassa [1961].

An increasing number of regional initiatives go beyond trade, covering such vital areas as movement of labor and capital, industrial development, infrastructure, energy and environmental protection, etc. Furthermore, the political dimension of regional agreements has become increasingly important.

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A three-pillar approach uniting political, economic and trade cooperation under a single umbrella agreement is a distinguishing characteristic of the new EU approach to North-South relations. This and other models that attach increasingly more importance to non-trade cooperation along with establishment of FTAs are the most recent expression of the New Regionalism.

As we will see, the EU approach is quite unique as it proposes an unusually tight trade and cooperation nexus. Theoretically this approach should be attractive, especially in North-South agreements, because the promise of linking free trade with cooperation programs could enhance the benefits of the former for both parties. However, while innovative, the nexus is challenging in its construction and delivery. The paper will explore EU efforts in this area in the broader context of what is happening in other initiatives that link developing and industrialized countries.

## **II. THE NEW REGIONALISM AND THE EMERGENCE OF "NORTH-SOUTH" AGREEMENTS**

The 1990s witnessed a wave of New Regionalism in Latin America (Devlin and Estevadeordal [2001]; Ethier [1998]). The "newness" of the New Regionalism went beyond the rebirth of integration initiatives after the collapse of the region's traditional Post-War schemes during the crisis years of the eighties.

The New Regionalism of the 1990s was led by trade agreements with objectives of creating free trade areas or common markets. The big defining difference between the two periods was the policy environment that the new integration initiatives were designed to support. The policy framework encircling the "old" Post-War regionalism involved an inward-looking and protectionist/state-led import substitution strategy (often in the context of authoritarian regimes).

Meanwhile, the New Regionalism is inserted into a framework of policy reform that promotes open and competitive private market-based economies in a modern democratic institutional setting.

The change in the global policy framework contributed to a fundamental change in the modalities and instruments of regional integration. Liberalization of the regional market paralleled a dramatic reduction of external protection: the traditional laborious positive lists for regional trade liberalization were abandoned for more automatic schedules with limited negative lists; and free trade objectives went beyond goods to incorporate so-called new issues such as services and intellectual property. Moreover, with regional trade responding energetically to liberalized regional markets, commercial interdependence has increased in Latin America, creating new demands for non-trade related cooperation in areas such as protection of democracy, macroeconomic policy, infrastructure, disaster management, etc.

But perhaps the most dramatic change in character was the shift from the region's traditional Latin American intra-regional focus ("South-South") for integration to growing interest in interregional ("North-South") agreements, which link up commercially with industrialized countries in reciprocal free trade (in contrast to the traditional non-reciprocal relationships) and in cooperation programs. This is something that would have been politically inconceivable before the new policy framework. The trend is seen in Mexico joining NAFTA and its signing a free trade agreement with the EU; Canadian free trade areas with Costa Rica and Chile; Chilean negotiations for a free trade area with the U.S. and its recent signing of an agreement with the EU; EU negotiations with Mercosur and the Caricom countries, Central American negotiations with the U.S., the Western Hemisphere's Free Trade Area of the Americas (FTAA) process, and the participation of several Latin American countries in APEC.

Latin America's interest in pursuing industrialized country interregional trade agreements involves more than securing stable access to major markets. The broader motive is to secure a firmer anchor for policy reform and attraction of foreign direct investment. These North-South interregional initiatives tend to lock-in and add credibility to the broad trade-related disciplines that accompany free trade agreements; they induce other modernizing reforms through the effects of competition and learning by doing, and they can be an instrument for competing internationally for foreign



direct investment as risk premiums are lowered on account of association with a stable and credible industrialized country.

As for the industrialized market countries, their motives also have gone beyond mercantilist market access as such. For sure, "doing business" is a motive. But others exist, such as promoting political stability and development in the poorer countries; gaining a beachhead in a low wage market for the purpose of outsourcing segments of the chain of production to achieve enhanced national competitiveness; influencing indirectly negotiation agendas in the WTO; strategic market positioning in the globalized world economy; offsetting the effects of preferences that a prospective partner country may have granted other countries, etc.

### III. THE CONCEPT OF A TRADE AND COOPERATION NEXUS

Cooperation between governments can be defined as mutual adjustment of state policies to achieve outcomes that all prefer to the status quo. This policy cooperation is usually voluntary as well as necessary for the extraction of mutual benefits for all participants.

In this context a regional integration agreement, or alternatively functional cooperation, is a type of "impure" public good that we will call a regional public good.<sup>1</sup> Cooperation requires some degree of subordination of the members' sovereignty to the interests of the group, which is always associated with certain costs to the participants. However, the benefits of cooperation, i.e. the benefits of the public good, usually cannot be fully internalized. This characteristic tends to induce the underproduction of regional public goods *vis-à-vis* their optimal social levels.

The achievement of consensus on collective actions is handicapped by informational asymmetries and political and institutional limitations on establishing certainty regarding commitments. The outcomes of strategic interaction depend on many factors that characterize the particular situation. To a large extent the size and the relative power of the actors are important determinants. Another important feature is the existence of focal points of contact, or areas of consensus (equilibriums), that for one reason or another may seem "obvious" to the players. The actors' cultural background and past experiences are important in establishing focal points. The informational role of preparatory working groups in trade negotiation processes has proven instrumental value for developing focal points.

Formal regional integration agreements involving a set of mutual rights and obligations can be political, economic or both. However, mutually beneficial regional cooperation is possible in practically any single field of public policy, ranging from security matters to environmental and labor standards. Hence formal integration through the removal of barriers to trade in the context of a free trade area or customs union is simply one of the forms in which cooperative action can begin to take place. However, given the differences in the pay-off structures, negotiations in some areas of cooperation may be more or less complicated and take more or less time than in others. In the context of formal regional integration, it is clear that some issues are discussed and negotiated ahead of others, depending on the potential benefits, complexity and complementarities as well as the priorities given to the issues by each government.

We distinguish between trade-related cooperation (usually in the context of a formal trade agreement) where parties make an effort to harmonize standards related to traded goods and services, public procurement, customs procedures etc., and other forms of non-trade cooperation. One of the two types of cooperation may emerge alone, they both can emerge parallel to each other (i.e., a formal trade and integration agreement with functional cooperation emerging on an *ad hoc* basis in other areas), or non-trade cooperation may be integrated with trade in a "single-track" approach creating "a trade and cooperation nexus". Regional integration processes may establish their initial roots through successful non-trade cooperation and incorporate trade-related issues at a later stage, even though, as we will see immediately below, the opposite is usually the case.

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<sup>1</sup> A pure public good is non-exclusive and indivisible, while an impure public good is only partially so (Sandler [1992]).

Trade agreements are invariably the point of departure for regional economic integration for several reasons. First, trade can attract support from well organized private business communities. Second, unlike many other economic arrangements, the mutual benefits of trade agreements and their distribution can be reasonably assessed ex-ante by participants and monitored and enforced ex-post as they usually contain very precise disciplines and the institutions/procedures (including WTO rules) for negotiating and administrating cross-border trade are already in place. Third, trade agreements accommodate nationalistic sentiments of society as they can be designed in ways that initially involve only very limited loss of national sovereignty, as in the case of free trade areas. Trade negotiations also do not demand resource transfers. On the other hand, the difficulty of negotiating non-trade issues is related to the very nature of such issues: whereas preferential trade arrangements are concerned with *removal* of trade-distorting policies, cooperation in other economic areas as well as in social and cultural fields requires *introduction* of additional policies, which is more difficult to deal with. Finally, a critical mass of regional trade among partners acts as a "hanger" on which other forms of cooperation can be functionally draped.

Indeed, growing and mutually beneficial commercial interdependence among partners typically induces demands for expanded economic cooperation to exploit more fully the revealed advantages of a maturing regional market. Moreover, demands for non-economic and even political cooperation arise from the social externalities generated by closer economic ties. In effect, the centripetal forces of trade among partners can be an effective handmaiden of deeper integration whether planned or not. There is the contemporary example of Western Europe where growing interdependence through trade has served to drive forward a political agenda of certain partners of the agreement for very deep integration and broad-based cooperation. As a result, regional market opening became functional to widening the scope of cooperation, or in the words of Garcia and Glocker [2000], to "integration by stealth". As commitments have deepened, even the multilateral trading system has increasingly encompassed more and more issues which originally were not identified with trade. The recent international debate on labor and environmental standards in the production of traded goods is an example of the pressure to further expand the frontier of cooperation as multilateral commitments to liberalize trade enter advanced stages of development.

The North-South agreements can be divided into agreements that only cover trade (T), agreements for cooperation without a trade component (C) and agreements that cover both preferential trade and cooperation simultaneously (T+C). Appendix I shows that North-South cooperation agreements can be quite comprehensive in scope, involving trade-related cooperation, economic cooperation, political cooperation, social and cultural initiatives, environmental protection, human resource development and science and technology, just to mention some.

As mentioned, cooperation can be in a donor-recipient type with implicit or explicit one-way resource transfers between partners, purely intergovernmental programs without net resource transfer implications, or some mix of the two. In North-South interregional cooperation one would expect some presence of the donor-recipient model in addition to purely intergovernmental schemes.

A distinction should also be made depending on the instruments used to achieve cooperation; for example, whether cooperation evolves through informal channels without any official budgetary or technical support, or cooperation is couched in more structured operational terms involving

formal mechanisms to identify and agree on priorities and objectives and agreed procedures to implement the outcomes of deliberations/negotiations coupled with programmed budget support.

Trade liberalization and non-trade cooperation can evolve almost entirely independently. In many cases, however, the two components are closely related. One would expect that when economic integration is launched with the deep objectives of a common market (common external tariff and free movement of factors of production) or more, the agreement will not only anticipate regional free trade, but also systematic cooperation in trade-related and non-trade areas, creating a trade and cooperation nexus (T+C). This approach may save costs associated with negotiations as well as development and administration of the cooperation programs but add the risks of getting bogged down with a large number of complex issues.

However a strict "business only" free trade area may more quickly capture the mutual interest of the parties and serve in practice as a solid beachhead for more comprehensive future cooperation. In effect, as trade successfully deepens, a trade-based model without any systemic plans for cooperation beyond the free trade itself may at a later stage create incentives for incorporation of more difficult cooperation into the agreement, perhaps first trade-related, but then expanding to non-trade areas. In this scenario the relationship evolves from trade (T) to a trade and cooperation nexus [(T)→(T+C)].

Another model involves agreements where an initial framework of cooperation only (C) in economic and/or non-economic areas leads, through success and growing recognition of broader opportunities, to the point where parties eventually launch a formal trade and integration agreement, creating a trade and cooperation nexus [C→(T+C)].

It is possible that the agreement produced in the course of negotiations ends up being a more deep or shallow agreement than initially intended by the parties. Or, a protracted negotiation period produces a series of agreements that replace or supplement one another. With many issues on the negotiating table, sometimes conflicting, it is not surprising that having a particular agreement design in mind, the negotiators are sometimes forced to take a step back and substitute some of the intended components of the agreement for another. Or, if a unified approach is anticipated, it may become necessary to negotiate one part of the agreement at a time, perhaps starting with trade and moving later towards a trade and cooperation nexus.

An overview of Post-War initiatives more or less bears out the models suggested above. Agreements launched with an initial official framework, or objective, of "very deep integration" have typically started out with a trade and cooperation nexus (T+C) built into the initiative. This is illustrated in the Latin American and Caribbean "old" subregional integration schemes which were committed to development of a common market as well as the "new" subregional schemes such as the Andean Community. The other extreme is shallow agreements such as free trade areas which are "business only" (T) in their initial intent. Examples here are NAFTA, the new bilateral trade agreements in Latin America and the Latin American Free Trade Association (LAFTA) of the 1960s.

Meanwhile, Western Europe is a good example of where deepening trade interdependence through (T) evolved into comprehensive (T+C). One also now observes increasing pressures on NAFTA partners to move from (T) to the direction of (T+C). The movement from (C) to (C+T) is a less frequently observed model; ASEAN is perhaps the most outstanding example.

Finally there are three modern North-South plurilateral initiatives which are interesting variants of the (T+C) model and lead us to our central points. The first is the Western Hemispheric Summit process, which involves a free trade negotiation coupled loosely with a confederation of somewhat autonomous non-trade cooperation initiatives involving more than 20 areas. This cooperation is a mix of intergovernmental and donor-recipient type. The donor-recipient type cooperation (aid and technical assistance) is being delivered in the framework of an informal "outdoor" contracting market where supply and demand clear only very imperfectly, at least up to now (Devlin [2001]).

Then there is the APEC process where there also is a package of trade and non-trade cooperation initiatives. The non-trade cooperation component (more than 25 initiatives) is largely of the intergovernmental type, while the trade component is a loose confederation of voluntary MFN trade liberalization exercises with the goal of reaching free trade by 2010 or 2020 for industrialized and developing countries, respectively.

Finally, there is the EU-Mercosur Interregional Association Agreement, which is currently being negotiated, and proposes the novel EU approach of a "single undertaking", which in principle systemically integrates more than 25 initiative areas in political dialogue, cooperation and reciprocal free trade under a single umbrella agreement.

## IV. TRADE AND COOPERATION IN NORTH-SOUTH AGREEMENTS

### Asia-Pacific Economic Cooperation Forum (APEC)

The APEC differs from most other regional agreements, since the organization acts as an umbrella for different types of arrangements and agreements. Initially an informal forum of dialogue, the organization has developed into a main vehicle for promoting economic and technical cooperation and trade among its 21 members.<sup>2</sup>

At the first Economic Leaders' Meeting in 1993 the parties agreed to make cooperative efforts to address the challenges of global change, promote the free exchange of goods, services and investment and work towards broadly-based economic expansion, higher living and educational standards and sustainable growth that respects the natural environment. In the following years the Meetings focused on development of mechanisms for achievement of these goals.

Free trade was placed on the agenda in 1994, when the parties declared the very ambitious goal of "free and open trade and investment in the Asia-Pacific by 2010 for developed member economies and 2020 for developing ones". To achieve the objectives each member country agreed to elaborate an Individual Action Plan (IAP). In the following year, the Osaka Action Agenda established three pillars of APEC activities: trade and investment liberalization, business facilitation, and economic and technical cooperation. The specific areas for cooperation were later proclaimed to be developing human capital, fostering safe and efficient capital markets, strengthening economic infrastructure, harnessing technologies of the future, promoting environmentally sustainable growth and encouraging the development of small and medium-sized enterprises. Today, the main issues on the APEC agenda are further opening of the markets, strengthening of the multilateral trading system and sustaining the economic recovery in the APEC area.

At each year's Ministerial Meeting, members define and fund work programs for APEC's three committees, one sub-committee, eleven working groups<sup>3</sup> and other APEC fora. The committees are the Committee on Trade and Investment (CTI), the Economic Committee (EC) and Budget and Management Committee (BMC). The work of these committees focuses on moving forward with the two most important agendas of APEC: Trade and Investment Liberalization and Facilitation (TILF) and Economic and Technical Cooperation (ECOTECH).

The CTI aims to create an APEC perspective on trade and investment issues and to pursue liberalization and facilitation initiatives. The CTI is responsible for implementation of the Osaka Action Agenda (OAA) by overseeing work on TILF, including work on tariffs, non-tariff measures, services, deregulation, dispute mediation, implementation of WTO obligations, investment, customs procedures, standards, mobility of business people, intellectual property rights, competition policy,

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<sup>2</sup> APEC Members: Australia, Brunei Darussalam, Canada, Chile, People's Republic of China, Hong Kong, Indonesia, Japan, Korea, Malaysia, Mexico, New Zealand, Papua New Guinea, Peru, Philippines, Russia, Singapore, Taiwan, Thailand, USA and Vietnam.

<sup>3</sup> Working groups on agricultural technical cooperation, energy, fisheries, human resources development, industrial science and technology, marine resource conservation, small and medium enterprises, telecommunications and information, tourism, trade promotion and transportation.

government procurement and rules of origin. The core activity of CTI is implementation and enhancement of the Collective Action Plans (CAPs) which are the main vehicle for advancing APEC's TILF agenda. The main function of the EC is to analyze economic trends and issues in the APEC region thus provide an analytical basis for advancing the TILF and ECOTECH agendas. Furthermore, the EC serves as a forum for member states to exchange information and views.

Gradually adding new areas of cooperation to the agenda, the APEC leaders envision deep integration consistent with the single-track approach. However, up to now, actual trade liberalization within APEC has been little more than implementation of unilateral liberalization policies that the countries had planned to pursue in any event. Hence as a trade liberalization initiative APEC has suffered from a lack of credibility and flagging momentum. It has, however, excelled at cooperation (C), especially of the intergovernmental type. In sum, while organized as a trade and cooperation nexus (T + C) in practice APEC has been largely a cooperation exercise.

## **North-American Cooperation**

### *The North American Free Trade Agreement (NAFTA)*

Cooperation among the North-American states was established exclusively with the objective of "doing business"; i.e., from the beginning the regional ties were focused on trade (and investment).

As a comprehensive trade agreement, NAFTA, which entered into force on January 1<sup>st</sup> 1994, covers market access for goods and services, elimination of barriers to investment, government procurement, customs procedures, standards-related measures, rules of origin, intellectual property rights and includes provisions for dispute settlement. Tariffs between US and Canada were eliminated in 1998 building upon the US-Canada Free Trade Agreement. Under NAFTA, the Parties committed to elimination of nearly all tariffs by 2008 and removal of many non-tariff barriers, such as import licenses. Some sectors have special treatment under the Agreement, such as automotive, textiles, energy and some agricultural goods. The provisions for trade in goods include guidelines for adoption and enforcement of sanitary and phytosanitary measures.

When the plans for NAFTA were announced in 1990 by President Bush and President Salinas of Mexico, it was intended as a pure commercial agreement with the main objectives of opening up markets for trade and investment. However, the announcement created substantial opposition to the project by some U.S. producers and workers (and in some Mexican circles), who felt threatened by low Mexican wages and poor environmental standards. The emerging agreement was seen by critics as a program to "give away American jobs". Their worst-case scenario for the joint market was loss of U.S. competitiveness while nurturing the low labor standards of Mexican workers and environmental damage.

In 1992 the new Clinton administration, with a view to achieving ratification of NAFTA in Congress, sought to pacify labor unions as well as environmental groups by expanding the focus of the North-American economic cooperation beyond the internationally accepted trade disciplines of a second generation free trade area by including cooperation on labor and environmental standards. In effect, the U.S. insisted that establishment of a FTA should go hand-in-hand with efforts to improve labor standards in Mexico and improve environmental and health conditions on the

border. Mexico resisted an integrated approach to (T+C) as there were fears that labor and environmental standards were just a smokescreen for protectionist interests and furthermore would establish an unwanted precedent for other trade negotiations. The outcome was the so-called side agreements, which came into force at the same time as NAFTA, but were legally independent of the trade liberalization disciplines.

Two side-agreements were signed: the North-American Agreement on Environmental Cooperation (NAAEC) and North-American Agreement on Labor Cooperation (NAALC). Neither Agreement is a tool for any sort of harmonization or standardization. Rather, both are designed to promote transparency of legal frameworks in each member state and support an exchange of information.

The declared objectives of NAAEC are to foster protection and improvement of the environment, promote sustainable development, strengthen cooperation between the parties on environmental laws and policies and promote transparency and public participation in the development and improvement of environmental regulation. Each country is responsible for establishing and maintaining its own high level of environmental protection and improving environmental laws without lowering standards to attract investment. Each Party agrees to effectively enforce its environmental laws through the use of inspectors, monitoring compliance and pursuing the necessary legal means to seek appropriate remedies for violations. Each Party must also provide a report on the state of its environment, develop environmental emergency preparedness measures, promote environmental education, research and development, assess environmental impacts, etc.

Three separate bodies have been established to support the objectives of the Agreement: the Commission for Environmental Cooperation (CEC), the Border Environment Cooperation Commission (BECC) and the North American Development Bank (NADBank). The CEC serves all three NAFTA parties, while BECC and NADBank are bilateral EU-Mexico institutions. The CEC was established to oversee implementation of the Agreement, compile information from each country and monitor the abilities of the Parties to meet the obligations. Furthermore, CEC acts as a forum for discussion of the means to achieve the goals of NAAEC. CEC reviews petitions from the public and investigates complaints from citizens related to the commitments made under NAAEC. The Commission can furthermore initiate dispute settlements if requested by a government of a member country.

BECC and NADBank were established to assist communities on both sides of the US-Mexican border in coordinating and carrying out environmental infrastructure projects to fulfill the obligations of NAAEC. BECC is responsible for development, coordination and implementation of such projects, assessment of their feasibility and arranging public and private financing for them. BECC certifies applications for financing to be submitted to the NADBank, which is an international financial institution established and capitalized in equal parts by the United States and Mexico. The projects financed by NADBank must be related to potable water supply, wastewater treatment or municipal solid waste management and be located within the border region.

Labor cooperation is structured in a similar manner. The objectives of NAALC are to improve working conditions, encourage labor-related cooperation, exchange of information, and promote enforcement of labor law and transparency in its administration. As in the case of environmental regulation, each country maintains complete sovereignty in the formulation of labor law and policies. The obligations under the Agreement include adoption of high labor standards by each



Party and compliance with and enforcement of labor law through appropriate government actions. The Parties are committed to ensuring transparency and public awareness of their laws, regulations and procedures. Furthermore, the Parties committed to promote the 11 Labor Principles set out in Annex 1 to the Agreement.<sup>4</sup>

NAALC is supported by two international institutions: the ministerial-level Council and the trinational Labor Secretariat and a domestic institution: a National Administrative Office (NAO) created in each country within the labor ministries. The Council and the Secretariat form the Commission for Labor Cooperation, which is the institutional framework for cooperative activities and intergovernmental consultations, as well as for independent evaluations and dispute settlement related to the enforcement of labor laws. NAOs serves for the exchange of information among the governments and coordinates cooperative activities of the Commission, which include seminars, conferences, joint research projects and technical assistance.

The non-trade related cooperation is narrowly defined as a process of consultation, exchange of information and increasing transparency and public awareness of laws and regulations. More effective administration of environmental and labor laws and greater understanding of each country's practices are the final, not intermediate, goals of this type of cooperation. Cooperation does not involve any policy adjustment or resource transfer. Moreover, no systematic projects or programs take place -coordination happens largely on an *ad-hoc* basis. Therefore, North-American cooperation is not a tight (T+C) nexus. In practice it is closer to a "business only" (T) arrangement with labor and environmental cooperation programs tacked on the side by the unilateral insistence of the U.S. that such agreements be a condition for Mexico's membership in NAFTA. However, sharply growing commercial links among the partners are already serving as a beachhead for public discussion of ideas for deepening cooperation within NAFTA and broadening that cooperation to other areas (e.g., monetary, migration issues and security) not originally envisioned by any of the partners. However, fundamental deepening beyond the commercial relationship does not seem imminent.

## **Hemispheric Cooperation**

### *Summit of the Americas*

The Summit of the Americas is a process of institutionalized meetings at the highest political level among the 34 Organization of American States (OAS) member states. They aim to develop comprehensive hemispheric cooperation in strategic areas, including trade, democratization and human rights, fight against terrorism, corruption and drugs, infrastructure, etc. Economic cooperation centers on creation of the Free Trade Area of the Americas (FTAA).

The process was initiated by the Clinton administration in 1993, when Vice President Al Gore announced the plans for a new hemispheric Summit at a meeting in Mexico City. The U.S.

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<sup>4</sup> Freedom of association and protection of the right to organize; the right to bargain collectively; the right to strike; prohibition of forced labor; protections for children and young persons; minimum employment standards; elimination of employment discrimination; equal pay for women and men; prevention of occupational injuries and illnesses; compensation in cases of occupational injuries and illnesses; protection of migrant workers.

government offered to host the Summit in Miami and circulated a proposal of 14 initiatives to be placed on the Hemispheric agenda.<sup>5</sup> In the following months consultations within regional and issue-specific subgroups took place to reach consensus on the initiatives and a detailed Plan of Action. Three negotiating strategies were employed simultaneously: bilateral consultations between the U.S. and other countries, discussions within geographical regions (Caribbean, Central America and South America) and meetings within self-selected groups of countries with interest in particular issues. Together, the three approaches - bilateralism, geography-based plurilateralism and issue-specific coalition-building formed a process that was termed "Cascading Modular Multilateralism". As the result of the consultation process, a Plan of Action for the Summit was drawn up with 23 initiatives (see Appendix II) and 150 action items. Initiatives were approved at the meeting of Vice Foreign Ministers two weeks before the Miami Summit.

The Miami Summit took place in December 1994 and produced a Declaration of Principles and a Plan of Action signed by all 34 Heads of State and Government. The Summit identified the countries responsible for the implementation of the mandates ("Responsible Coordinators"). The task of the Responsible Coordinators is to assign an agency or department within their government to design and execute projects and programs to fulfill the Summit mandate.

In the following years, two multilateral follow-up mechanisms were created to encourage activities agreed upon by the Summit and to monitor the progress made by each country. The Summit Implementation Review Group (SIRG) is composed of representatives from all the countries of the Hemisphere ("National Coordinators"). The Review Group receives reports from the Responsible Coordinators and is equally responsible for coordinating and implementing the mandates of the Miami Plan of Action. The SIRG holds approximately four regular meetings plus one ministerial-level meeting each year and reports annually to the Foreign Ministers on the progress achieved. The Ministerial Meetings produce Ministerial Declarations which identify mechanisms for creating progress in each sector: education, justice, health etc. A parallel follow-up mechanism within the OAS is the Special Committee in Inter-American Summits Management (CEGGI), which hears reports from the various OAS units and offices and occasionally from other international organizations and reports to the OAS General Assembly.

International and regional organizations play an important role in the implementation of the Summit process. Each of the organizations involved has responsibilities related to specific Summit issues.

The actual fulfillment of obligations assumed under the Summits is the responsibility of each participating State. National programs to support the Summit commitments are undertaken and reviewed by each country and reported to the SIRG. To honor their obligations, the countries may apply for program financing in the participating international organizations. No joint funds for implementation of projects or systematic mobilization of cooperation programs exist in the Summit process.

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<sup>5</sup> (a) Democratization: no to corruption, battle plan against the cartels, regulatory reform, making civil society work and enhance OAS capacity to strengthen democracy; (b) Economic Integration: Hemispheric free trade, capital movements liberalization and infrastructure; and (c) Sustainable Development: Education, health care, microenterprises, energy, nature conservation and environmental protection.

Building upon the Miami Summit, the subsequent Summits expanded the scope of cooperation and adjusted the activities under each initiative. Summit of the Americas on Sustainable Development in Bolivia (1996) led to consensus on incorporating economic, social and environmental elements in development cooperation and produced a Plan of Action with initiatives in five areas: Health and Education; Sustainable Agriculture and Forestry; Sustainable Cities and Communities; Water Resources and Coastal Areas; and Energy and Minerals. The Second Heads of State Summit in Chile (1998) gave more emphasis to social policies and the essential matters of the Hemispheric Agenda, such as democratization, human rights and free trade. The new Plan of Action contained 27 initiatives, most following lines of the first Summit with education gaining center stage. The Third Summit, which took place last year in Quebec City, Canada, focused on three major themes (or "baskets"): Strengthening Democracy; Creating Prosperity; and Realizing Human Potential. The first two baskets - with their focus on democracy and economic integration - have been central to the process since Miami. The third 'basket' primarily addresses social issues and contains a commitment to inclusion and greater equity.

Turning to the specific mandates, it is clear that the Free Trade Area of the Americas is the leading initiative in the area of economic integration and probably the most consistently dynamic component of the entire Summit process. With a clear objective, priority status for most of the participating countries (particularly in Latin America and the Caribbean), an agreed timetable (the negotiations are to be concluded by 2005) and well structured working/negotiating groups with strong collective financial, technical and logistical support (provided by the Organization of American States -OAS-, the Inter-American Development Bank -IDB-, and the Economic Commission for Latin America and the Caribbean -ECLAC-) the FTAA process has steadily advanced and far surpasses progress in other economic areas, such as hemispheric capital markets or infrastructure. Areas that are not directly related to economic integration for which maturing Summit process has brought some progress are democratization, human rights, justice, combating drugs, fight against terrorism, education and disaster management.

Envisaged as an initiative for creating progress in a number of areas, with a view to consolidate democracy and foster economic prosperity, the Summit process can be described as a (T+C) project. However, most progress is being achieved in negotiations of the FTAA, where there has been strong political interest of most governments, disciplined organization and skilled negotiators, and quantifiable objectives, all coupled with systematic financial, technical and logistical support from the IDB, OAS and ECLAC. Many other Summit initiatives have suffered from less well defined political commitments, capacity constraints in Summit-related-Ministries, organizational bottlenecks, objectives which are difficult to quantify and monitor and less than systematic support mechanisms. There also has been a tendency to add new initiatives at each Summit without having necessarily consolidated the original objectives or establishing priorities. In sum, the hemispheric initiative has been set out as a (T+C) nexus; however, while excelling at (T), the (C) component has had an emerging credibility problem. Finally, although the sharpest focus of the Summit is market access and trade-related cooperation, it has served to keep Latin American and Caribbean countries engaged in the Summit process as a whole and its broad agenda. Moreover, if the FTAA materializes in 2005, it will generate pressure for truly effective hemispheric cooperation in other areas of the Summit agenda.

## EU External Cooperation

### *Overview*

The EU's approach to North-South Agreements has evolved rapidly. Its earliest forms reflected a first generation strategy that emerged in the 1970s, where cooperation with Latin America was in the context of formal Development Cooperation. This entailed one-way financial and technical assistance and was often complemented by non-reciprocal trade preferences. In the 1980s a second generation of agreements emerged, providing for continued Development Cooperation but adding so-called Economic Cooperation. The latter was designed not so much as aids but rather as a program with mutual benefits for the partner country and Europe; for instance the promotion of two-way trade and investment flows. Beginning in the early 1990s third generation framework agreements emerged which substantially broadened the stress on Economic Cooperation, especially in trade and investment areas. In the year 2000 Economic Cooperation accounted for 17% of total EU Cooperation in the region. The more advanced countries of the region were the primary targets of economic cooperation; for example in 1990-1998 more than 50% of EU financial commitments to Argentina and Mexico consisted of Economic Cooperation (IDB [2002]).

In the mid 1990s a fourth generation approach emerged. It attempted to adapt cooperation to the different needs of countries and subregional blocs. More advanced countries were to evolve towards a "partnership of mutual interest" with the EU, which would include not only traditional Economic Cooperation but also a move to reciprocal free trade. The primary targets of the new approach were Mexico, Chile and Mercosur. In this new phase agreements were based on the three pillars of political dialogue, cooperation and reciprocal liberalization of trade. The latter was a major departure from previous agreements (*Ibidem*).

In general, there are two types of cooperation which can unfold between the European Union and a third party: development cooperation or cooperation in a broader sense, which may include economic cooperation, political dialogue and reciprocal trade liberalization. The first type, which in reality is a unilateral act from the EU's side rather than cooperative action as such, is primarily concerned with poverty alleviation through one-way transfers from the EU. This approach has dominated the external relations of the EU with developing countries, mainly in the Sub-Saharan Africa and Caribbean, since the creation of the European Community. The second type of cooperation is a fairly new concept that contributes a special character to the new generation of agreements. These agreements are increasingly dominating EU relations with Latin America. Finally, the EU relations with some of the Union's closest neighbors go beyond conventional cooperation in the case when the third parties are candidates for the EU accession.

There is some ambiguity in the way the terms development cooperation and economic cooperation are used by the EU as they often overlap one another. The term development cooperation only applies to African, Caribbean and Pacific countries (ACP), including South Africa. For Latin America this term does not apply, but economic cooperation often involves projects that promote development, such as elimination of rural and urban poverty.

When the EU signs a cooperation agreement with a country or a region, the Commission prepares a Country Strategy Paper (CSP), which, based on the relevant agreement, contains the EU's strategy towards the third party and instruments for carrying out cooperation. Building upon CSP,

the Commission then signs a Memorandum of Understanding with the partner country/region. The Memorandum serves as a basis for all financial transfers from the Commission to the recipient. Furthermore, a Financing Proposal is prepared by the European Commission in close collaboration with the recipient country or region, containing a timetable for the technical and financial implementation of the projects or programs and duration of the different phases of implementation. The Directorate-General for Development (DG DEV) and Directorate-General for External Relations (DG RELEX) negotiate agreements, prepare CSPs, identify and formulate programs for ACP countries and the rest of the world, respectively. At the moment, a decentralization process is taking place within the Commission, placing more responsibility for project implementation and evaluation in the EU Delegations in the recipient countries/regions. Each type of cooperation is financed through an assigned line in the Commission's budget.

#### - EU development policy -

Development Cooperation falls under Community competence and hence the commitment of Commission's finance to development assistance does not require ratification by the Member States, once all the necessary procedures within the Community have taken place. Community policy should be "complementary to the policies pursued by the Member States". The agreed procedures emphasize the need to coordinate national development policies and states. The main mechanism for coordination of the national development policies is the biannual meeting of the Development Council consisting of the Member States' Development Ministers.

The common policy has focused on promoting sustainable development, poverty reduction and support of integration of developing countries into the world economy. Development cooperation is to be built on the principles of democracy, human rights and the rule of law.

As the European Union's main decision-making body consists of the Ministers of Member States, the Council of Ministers plays a crucial role in shaping external relations, including relations with developing countries. The Community's development strategy is decided by Council resolution. In its communication to the European Council of April 26 2000, the European Commission proposed new guidelines for Community's development policy. The proposal concentrates on six areas of development cooperation: the link between trade and development; regional integration and cooperation; support for macro-economic policies and the promotion of equitable access to social services; transport; food security and sustainable rural development; and institutional capacity-building. The overall goal is to build a link between trade and development, which would help developing countries benefit from globalization, enabling them to enhance the positive effects of greater openness while minimizing adjustment costs. Promotion of human rights and democracy, improvement of cooperation with civil society and support to good governance and the rule of law are also fundamental.

#### - Trade and Cooperation Agreements -

The Treaty of Nice signed in February 2001 (but not ratified by all Member Countries) adds additional provisions for cooperation with the third parties to the Community legislation by inserting Title XXI (Economic, Financial and Technical Cooperation with Third Countries).

Under this framework, to initiate negotiations, the European Commission must make recommendations to the Council. The Council then issues the necessary authorization to the Commission, which conducts the negotiations in consultation with special committees appointed by the Council and within the framework of such directives as the Council may issue. From the Commission, the members of the negotiation committees usually include representatives from Directorates General (DG) for Trade, as well as from the DG for External Relations and the DG on Agriculture. The Council, acting by a qualified majority, decides on the conclusion of the agreements. Unanimity is required for agreements that involve adoption of internal rules and for agreements establishing an association involving reciprocal rights and obligations. The agreement has to be ratified by the parliaments of the Member States, if it contains sections which exceed the Community competence (for example economic cooperation).<sup>6</sup>

By signing the cooperation agreements with the Community, the developing countries commit to comply with the provisions of the agreement. If any of the terms are violated, for instance by abusing human rights, the Community can launch a consultation process with the partner country, which in the most severe cases may result in economic sanctions.

As mentioned, in the recent years, the trend has been to transform pure development aid programs into a framework of full-scale economic cooperation agreements, which includes creation of reciprocal free trade and emphasis on political dialogue.

### *EU and South Africa*

As in the case with the other ACP countries, the EU's policy towards South Africa is formulated by the Commission's DG Development. However, the country's high income relative to other ACPs has caused the EU's approach towards South Africa to differ from its conventional development assistance approach.

Prior to the change of government in 1994, the Community's external policy towards South Africa was concentrated on maintaining a balance between commercial interests on the one hand and official condemnation of the apartheid regime on the other. After the fall of apartheid, a formal EU cooperation agreement with the new South African government became politically possible. The first formal agreement between the EU and the new South African government was signed at the end of 1994. The main objectives of the agreement were to promote respect for human rights and democracy, and to support sustainable development by intensifying related cooperation programs, including trade. The cooperation efforts were financed through the newly established European Program for Reconstruction and Development in South Africa (EPRD), focusing on a small number of selected development programs dedicated to strengthening institutions, good governance, education and health. This agreement, however broad and vague in its formulation, paved the way for future negotiations concerning trade and cooperation.

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<sup>6</sup> In strict legal terms, development policy and external cooperation remain in the realm of the European Economic Community (EEC), as instituted by the legal status of the Community laid out in the Treaty establishing the European Economic Community. Therefore reference is always made to the Community, not the European Union, as the party negotiating and concluding cooperation agreements with the third parties.

In 1994, South Africa sought membership of the Lomé IV Convention that underpinned relations with ACP countries.<sup>7</sup> The EU rejected the accession request on the grounds of a possible erosion of the preferential status of other ACP countries, most of which are far less developed than South Africa. Requests for partial accession were also denied, but in April 1997, a decision to grant South Africa a so-called qualified membership was approved. This meant that South Africa's involvement was limited to technical and cultural cooperation and participation in the institutions of the Convention, implying that South Africa neither could benefit from preferential access to the European market, nor receive the EDF funding granted to other ACP countries. Instead, the EU proposed to establish a free trade area with South Africa over the course of ten years. South Africa became a qualified member of Lomé in 1998 and a partner in the ACP's new Cotonou Agreement in 2000, with the important caveat that trade arrangements were negotiated separately under the new EU-South Africa Cooperation Agreement.

The new Trade, Development and Cooperation Agreement (TDCA) signed on October, 1999 covers all areas not dealt with in the context of South Africa's Lomé/Cotonou membership. The main objectives of the TDCA are:

- the creation of a framework for future dialogue between the parties;
- the provision of support to the transition process in South Africa;
- the promotion of regional cooperation and economic integration in the Southern African region;
- the expansion and reciprocal liberalization of mutual trade in goods and services;
- the encouragement of South Africa's integration into the world economy; and
- to promote cooperation of mutual interest between the EU and South Africa.

The essential element of the TDCA is the respect for democratic principles and fundamental human rights. Furthermore, the parties are committed to the promotion of good governance. The political dialogue, which is an important part of the Agreement, is intended to encourage these principles.

The most important and far-reaching part of the TDCA is Title II on Trade. In accordance with the provisions of the Agreement and in conformity with the rules of the WTO, a free trade area will be phased in over a period lasting, on the South African side, a maximum of 12 years and, on the Community side, a maximum of 10 years. This is the first North-South agreement between the EU and another party which includes reciprocal free trade (although only partial in agricultural goods). The negotiation process was very long and difficult due to concerns for asymmetry and differentiation, on the one hand, and the sensitivity of European agricultural imports on the other. The biggest problems related to the FTA were resolved, each in different ways: after protracted negotiations the Agreement of Wines and Spirits was finally signed on January 28, 2002, whereas in the area of fisheries the parties agreed "not to agree", i.e. negotiations for fisheries have been suspended until the parties are ready to reconsider the issue.

To implement the provisions on cooperation, a Country Strategy Paper for South Africa for 2000-2002 was prepared by the Commission and approved by the Member States. The main instrument

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<sup>7</sup> The EU's relationship with the ACP countries is outlined below.

of cooperation between the EU and South Africa is technical and financial assistance administered by the EPRD. The four focal areas chosen for provision of support under the Program are: poverty reduction, private sector development, regional integration and commitment to good governance, human rights and democratization.

Every three years a triennial program is negotiated with the South African government, building on the EU development policy and priorities and the provisions of both the TDCA and the Cotonou Agreement. The program (the Multiannual Indicative Program) identifies a limited number of core areas for cooperation ("focal sectors"), for which specific projects and programs are subsequently designed and negotiated with South African authorities. € 885.5 million are committed for the period 2000-2006 with €125 million budgeted for 2002 and €127 million for 2003. The tentative MIP for 2000-2002 allocates 50-60% for poverty reduction projects, 15-20% for private sector development, 15-20% for support to the rule of law and promotion of human rights and ±10% for support to regional integration.

The TDCA has not yet fully entered into force. Pending membership ratification, the Parties have agreed to apply the Agreement provisionally and partially from January 1<sup>st</sup> 2000. The sections that apply provisionally are those for which ratification is not required as they fall under "Community competence". These sections concern development assistance and certain trade issues. Trade-related cooperation and economic cooperation do not apply at this stage. Economic cooperation, for which no practical experience exists so far, is envisaged in the form of reciprocal cooperation supported by exchange of information and promoting of contacts between operators.

### *EU and Mexico*

Even though EU's relations with Mexico have traditionally been less focused on development aid than for example the ACP countries, the first formal cooperation agreement between Europe and Mexico signed in 1975 covered mainly development assistance. It was replaced in 1991 by the Framework Agreement that sought to "expand and diversify trade between the parties and to step up cooperation in trade, economic matters, science and technology and financial matters". The Agreement included for the first time articles on trade-related cooperation. The vehicle for trade facilitation involved technical cooperation between entrepreneurs and customs authorities. No preferential market access was discussed at that point. The main focus of the Agreement was on improvement of economic links through opening up of new markets, facilitation of investment flows and encouraging job-creation, cooperation between economic operators and cooperation in rural development, environmental protection and science. Other provisions under the Agreement covered cooperation in transport, public health and tourism. Thus, the Framework Agreement covered cooperation in trade facilitation and economic cooperation, but there were no provisions on trade liberalization as such. From 1990 to 2000 EU support for Mexico involved over €132 million worth of cooperation projects.

The new EU-Mexico Agreement -The Economic Partnership, Political Coordination and Cooperation Agreement- was signed in 1997 as a fourth generation three-pillar Agreement. Also called the Global Agreement, it entered into force in October 2000, following ratification by the Parliaments of the 15 Member States. Trade, falling under the Community competence, was negotiated first due to pressure from Mexican authorities who insisted that this was their top priority in any



agreement. Since trade negotiations proceeded fairly smoothly (Mexico's agricultural exports do not represent a threat to European producers), it was decided to move ahead with the FTA without waiting for the full ratification of the Global Agreement. Trade negotiations took place in the framework of the Interim Agreement of 1997, which committed the parties to setting up a timetable for "bilateral, progressive and reciprocal liberalization of tariff and non-tariff barriers to trade in goods". Furthermore, the Interim Agreement allowed the Joint Council to negotiate the rules for public procurement, competition, intellectual property and other trade-related disciplines. The Interim Agreement had to be ratified only by the EU Parliament, which significantly speeded up the procedure.

The FTA negotiations were concluded in November 1999, the corresponding agreement was signed in March 2000 and the FTA covering both goods and services officially entered into force on July 1, 2000 by the Decision of the EU-Mexico Joint Council. The trade agreement set up a scheme for gradual and reciprocal trade liberalization over the course of 10 years. This two-stage approach allowed the parties to conclude FTA negotiations and start reaping the benefits of more open trade earlier than would have been possible if the fourth generation agreements' Single Undertaking approach had been pursued. Ratification of the Global Agreement meant that the Interim Agreement ceased to exist. Since cooperation and political dialogue fall under the competence of the Member States, these components were activated only after ratification by all EU countries; i.e. when the Global Agreement entered into force.

The Global Agreement states that the parties would institutionalize and intensify political dialogue based on respect for the principles of democracy and human rights. The four priority areas of cooperation are promotion of the rule of law, economic cooperation, social development and reduction of inequality and scientific and technical cooperation. Economic cooperation relates, first of all, to cooperation in trade-related issues and support to small and medium-sized enterprises. Furthermore, the Commission supports the EU-Mexico Business Dialogue and Civil Society Dialogue, both of which are implicitly parts of EU-Mexico relations, but are not institutional mechanisms of the Global Agreement; i.e., they are entirely private sector initiatives. There is a potential for negotiation of sector-specific cooperation agreements. No specific projects or programs have been identified yet. A Country Strategy Paper (CSP) for Mexico was under preparation and is expected to become available in 2002. The CSP establishes a timeframe for cooperation in the coming years and identifies priorities at every time period. Starting in 2002, project identification (based on CSP) and evaluation is the responsibility of the EU Delegation in Mexico.

Awaiting ratification of the Global Agreement by the Member States, the Commission did not approve any cooperation projects in 2001. Prior to that, the bulk of financing went to schemes carried out by non-governmental organizations, such as a €7.4 million program in support of refugees from Guatemala. Other schemes concerned environmental protection (preservation of marine reserves) and cooperation in health (health systems and HIV/AIDS national accounts). Two large programs have been approved in 2002 so far: an €15 million social development project in the South-East of Mexico and a program to facilitate the implementation of the FTA.

The EU-Mexico Joint Council is responsible for building on the three pillars of the EU-Mexico agreement. The programming will lead into a Memorandum of Understanding between the parties. The Memorandum must contain the exact figures for the cooperation budget and the shares that

each side will contribute to the specific programs. Political dialogue is an important part of the program, giving special attention to the issues of terrorism and promotion of human rights.

### *EU and Mercosur*

The relations with Mercosur constitute the most recent example of the EU's effort to combine political dialogue, economic cooperation and trade liberalization into a single package. The integrated approach is even more pronounced in this case, since the Commission has a mandate from the Council to negotiate an Interregional Association Agreement as a Single Undertaking, meaning that the Agreement will enter into force as a whole, without any partial interim agreements.

The basis for the present EU-Mercosur relationship was set out by the Inter-Regional Framework Cooperation Agreement that was signed in 1995 and which fully entered into force on July 1, 1999. Whereas the main objective of the Framework Agreement was to pave the way for negotiations of a new Interregional Association Agreement, it also contained provisions for current cooperation between the EU and Mercosur, focusing on technical assistance in support of the integration process within Mercosur. Three main sectors have been identified as priority areas: strengthening of Mercosur institutions, development of economic and trade structures in the region and support to Civil Society. To fulfill the provisions of the Framework Agreement, a Regional Memorandum of Understanding between the EU and Mercosur was signed, establishing multiannual guidelines for cooperation programs. Under this framework, large sums were allocated, *inter alia*, for enhancing cooperation in customs procedures within Mercosur. The second part of the customs project was approved in 2001.

Cooperation in social fields takes place at the regional level and all projects are formulated as joint endeavors for the countries of Mercosur. The position of the EU is that social problems and inequality should be dealt with in regional context. Thus, the EU provides support to the Economic and Social Consultative Forum, an internal Mercosur entity.

Apart from interregional cooperation, the EU's relationship with the individual countries in the Southern Cone emerges through bilateral cooperation. Bilateral relations are formalized in the Commission's Country Strategy Papers and the Memorandums of Understanding which are signed with each country. The priority areas are different for each nation. For example, in the case of Argentina, priority is given to supporting SMEs and promoting social development. In Brazil, the projects supported by the EU include protection of the Amazon, alleviation of urban poverty, institutional reforms at the ministerial level and taxation reforms. In the coming years the focus of country cooperation is expected to shift in favor of intensified efforts to achieve goals at a regional level. When the new Interregional Agreement will enter into force, all previous arrangements, including the bilateral programs, will be revoked.

Negotiations for the new Interregional Association Agreement were formally launched in June 1999 at the Summit of Heads of State and Government of the EU and Latin America and Caribbean (LAC) in Rio de Janeiro. Three years of preparatory work prior to actual trade negotiations -which included four rounds of meetings plus a marathon session of meetings in Punta del Este in November 1997- produced over 20 trade studies and created three joint working groups. The first meeting of the EU-Mercosur Cooperation Council was held in November 1999 in Brussels. At

this meeting the parties established a Biregional Negotiations Committee (BNC) to provide general management of the negotiations on trade and cooperation and agreement on the structure, methodology and calendar for negotiations. The future of the political dialogue was discussed in February 2000 during the Ministerial Meeting of the EU, Mercosur, Chile and Bolivia in Portugal.

The initial round of actual negotiations took place during the first meeting of the BNC in April 2000 in Buenos Aires. The Committee established the objectives, principles, methodology, structure and initial work program for negotiations on three separate issues: political dialogue, cooperation and trade liberalization. Apart from bilateral and reciprocal elimination of barriers to trade, cooperation will encompass trade-related matters such as government procurement, facilitation of investment flows, protection of intellectual property rights, competition policies and dispute settlement. Cooperation negotiations took place for the first time at the Second Round, held in Brussels in June 2000. The negotiations for the free trade area and non-trade related cooperation take place parallel to one another. The Commission presented its tariff offer to Mercosur at the 5<sup>th</sup> Round, and the Mercosur presented its offer at the 6<sup>th</sup> Round in October 2001. Mercosur's offer covered only about 38% of the tariff lines, whereas the EU's covered 96%. During the last Round the parties also made substantial progress in preparing the text of the Agreement in the fields of science, telecommunications, energy and transport. Furthermore, for the first time the entire text of the Institutional Framework and Political Dialogue was discussed.

Subsequent meetings focused on moving forward with the chapter on political dialogue. The parties discussed major issues addressed at the EU-LAC Summit in May 2002 in Madrid, approved a series of business facilitation measures, and agreed on a Ministerial level meeting in July 2002.

Of the three pillars that will form the future Association Agreement, the most complex is trade. In particular, negotiations of agricultural trade liberalization run into difficulties, given the very high level of competitiveness of agricultural goods in Mercosur and the EU's protectionism in this field. Economic cooperation and political dialogue also face problems in the view of the current crisis in Argentina and a degree of discord among the partners. Indeed, due to complex political factors and economic problems in the region the negotiation process has been slowing down in recent months. Hopefully there will be major progress during 2003, resulting in a Draft Association Agreement for 2004.

At present, cooperation between the regions focuses on support to the integration process within Mercosur, with highest priority being given to strengthening the internal market, macro-economic coordination and the social dimension of integration. Under the future Agreement it is expected that the main goal of cooperation will be to provide support for implementation of the FTA, i.e. cooperation will be mainly trade-related and supportive of the economic instruments of Mercosur.

Three different categories of cooperation are under negotiation (corresponding to the Commission's budget lines for external cooperation): economic cooperation, financial and technical cooperation and social and cultural cooperation. Economic cooperation covers all sectors within the association relationship focused on trade: agriculture, fisheries, environmental protection, etc. Negotiations of this component have not yet been finalized. The texts for the financial and technical cooperation as well as for social and cultural cooperation have been finalized. The first component covers mainly institutional capacity building, whereas the second involves support to social development

at the regional level. Cooperation projects will be co-financed, with approximately 60% covered by the EU and the remaining 40% financed by Mercosur.

Since the new agreement is negotiated as single undertaking, a step-wise approach applied in the case of Mexico is not now envisioned. Once the whole text of the accord is in place, the agreement will enter into force after ratification by all member states' parliaments.

Even though it is too early to draw conclusions about the final outcomes of the EU-Mercosur negotiations, it is already clear at this point that the FTA will be the engine of cooperation between the parties, while at the same time it is the most difficult part of the Agreement to negotiate. It would seem that prior to achieving any agreement, Mercosur must reaffirm its common external tariff and the EU should be prepared to offer something significant in the area of agriculture.

### *EU and ACP Countries*

The ACP countries form a group of 77 African, Caribbean and Pacific countries. The ACP group includes most of the world's poorest countries. Since many of them are former European colonies, the ACP countries are particularly favored by the EU for North-South type of cooperation.

The EU's development approach towards the ACP countries was always largely focused on eradicating poverty by applying development aid and preferential access to the EU market. Thus, trade and non-trade issues were equally important from the very beginning as reflected in the Lomé Convention, which were operational since 1975. The focus of aid shifted each time a new Convention was signed, beginning with support to a large number of traditional basic-needs projects, then promoting such issues as industrial cooperation, financial and technical aid and later shifting to sectoral development in agriculture and fisheries and rural development. The last of the Conventions, Lomé IV, introduced the concept of structural adjustment and a number of cross-cutting themes such as human rights, democracy and women's rights. The Lomé Conventions' main achievement was the significant preferential margin granted to the ACP countries for many of their exports to the EU.

A whole new generation of cooperation agreements was launched in 2000 by the Conotou Agreement which aims to modify the relationship established in the Lomé Conventions. The new framework aims at restructuring financial aid and transforming the preferential trade agreement into a full-scale FTA between the EU and ACP countries. Thus, the Agreement seeks to redefine cooperation and evolve closer to a fourth generation three-pillar agreement.

The main goals of the political dialogue are peace-building, conflict prevention and resolution, encouragement of respect for human rights, democracy, rule of law and good governance. The main component of cooperation is poverty alleviation. The new poverty reduction strategy proposed under the Agreement applies an integrated approach "taking into account at the same time the political, economic, social, cultural and environmental aspects of development". In particular, the Agreement supports investment, private sector development and macroeconomic and institutional reforms. The aggregated amount of development aid for the period 2000-2005 is €15.2 billion.

The trade component of the Agreement establishes that the parties will maintain the present trade regime for the preparatory period of 2000-2008, during which the parties will negotiate a new trading arrangement. Formal trade negotiations started in September 2002 and the new trade agreement will enter into force no later than January 1<sup>st</sup> 2008. At least 12 years of transition period is expected.

Thus, the trade relations and cooperation between the EU and the ACP countries aim at a single-track approach, with a wide range of issues accompanying trade arrangements, which are now in a transitional phase. However, cooperation is largely of the donor-recipient type as it involves financing of cooperation programs through the European Development Fund. Thus, the arrangement is of the (C) type that the Commission wants to push to a (C+T) and that may be organized by geographic subregions (e.g. CARIFORUM) instead of the single ACP agglomeration.

### **Other Integration Processes: ASEAN**

Another umbrella-type of organization, the Association of South East Asian Nations (ASEAN) was founded to promote peace, stability and development in the region. Today the Association has 10 members, uniting all of South-East Asia.<sup>8</sup> The political and security cooperation is one of the cornerstones of ASEAN. The important agreements promoting peace and security include the 1971 Declaration designating Southeast Asia as a Zone of Peace, Freedom and Neutrality (ZOPFAN), the Treaty of Amity and Cooperation in Southeast Asia and the Declaration of ASEAN Concord in 1976, and the Southeast Asia Nuclear Weapon-Free Zone Treaty of 1995. The ASEAN Regional Forum (ARF) was established in 1994 as a means of consultation and confidence building among the member countries.

The economic cooperation within ASEAN initially concentrated on programs for joint ventures and complementation schemes among ASEAN governments or companies, such as the 1976 ASEAN Industrial Projects Plan, the 1981 ASEAN Industrial Complementation scheme, and the 1983 ASEAN Industrial Joint-Ventures scheme. In the nineties, however, the focus shifted towards opening up of the economies and preparing for deeper integration. In January 1992 the ASEAN Free Trade Area (AFTA) was established through a schedule of accelerated tariff reductions -the Common Effective Preferential Tariff scheme. In September 1994 the ASEAN member countries decided to speed up the establishment of AFTA by reducing the initial period of 15 years to 10.<sup>9</sup> Other areas of economic cooperation are industrial development, infrastructure, e-commerce and food, agriculture and forestry, all supported by cooperation programs or framework agreements.

Another dimension of intra-regional cooperation is so-called Functional Cooperation, which deals with human and social development. More specifically, cooperation in this area focuses on human resource development, with emphasis on women and youth, eliminating poverty, disease and illiteracy, rural development policies, productive jobs for low-income groups, especially in the rural areas and taking concerted action to curb the abuse and traffic in narcotics and drugs. Concern for the environment was expressed in environmental commitments of the member states

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<sup>8</sup> Brunei D., Singapore, Thailand, Malaysia, Indonesia, Philippines, Cambodia. Laos P.D.R, Myanmar, Vietnam.

<sup>9</sup> More recently ASEAN agreed to permit any member countries to accelerate their liberalization in certain sectors.

in the Hanoi Plan of Action and, more explicitly, in the Strategic Plan of Action on Environment for 1999-2004.

In conclusion, launched primarily as a security convention and a forum of cooperation, ASEAN evolved towards establishment of a free-trade area. This is one of the rare cases, when regional integration starts as cooperation only (C), is followed up by free trade negotiations, and evolves into single-track type of cooperation (T+C).



## V. CONSTRUCTING A TRADE-COOPERATION NEXUS

The three big "North-South" interregional initiatives (APEC, Western Hemisphere and EU-LAC) mentioned above have ambitious trade and cooperation nexuses. As stressed earlier, given that the initiatives have a configuration of asymmetric capacities due to the mix of very wealthy countries and much poorer developing countries, combining free trade areas with cooperation raises the prospects of producing a mutually beneficial and socially efficient interregional public good.

The two components of the nexus are mutually supportive. As an example, a reciprocal cooperation program which helps exporters of the partner countries identify trade and investment opportunities in the interregional market could provide impetus to the trade negotiations and energize trade once an agreement is reached. Another example: reciprocal cooperation in education and best practices is supportive of the development and trade objectives. Meanwhile donor assistance type programs could, for instance, provide technical support to the developing countries in the negotiation and implementation of agreements, thereby ensuring more sustainable commitments and more effective participation. Likewise, cooperation that aids infrastructure development, technical education, and democratic processes can help foster trade and investment. So there is no doubt that a trade and cooperation nexus is a desirable objective in initiatives designed to deepen North-South relationships.

In these big North-South interregional initiatives, the free trade component is clearly the priority area of most of the developing countries as they seek to eliminate trade barriers in their major export markets, which still protect goods for which they have a comparative advantage, such as textiles, agriculture and food processing. They also want to secure that access in a legal framework involving the rights and obligations of a formal free trade agreement in order to anchor their economies and attract investors. And importantly, free trade agreements are viewed as a way "to import" institutional modernization. As for cooperation, this is important too, but often a secondary objective and within cooperation the most immediate interest often is in trade-related assistance.

In contrast, the industrialized countries have often given relatively more priority to advancing the cooperation agenda. On the one hand, the developing country markets are a relatively small share of their total trade, and the trade negotiations typically hone in on sensitive sectors with strong political constituencies at home, which are resisting liberalization and globalization more generally. On the other hand, cooperation programs are closely linked to promoting existing and politically consolidated priorities in national foreign policy, economic and aid agendas.

Given this dichotomy, it is not surprising that the FTAA emerged only with great difficulty in the 1994 Miami Heads of State Summit agenda and only after Latin American countries conditioned their participation in the Summit's cooperation agenda by the incorporation of the aforementioned free trade negotiation (Hayes, 1996). Likewise, Mexico conditioned its willingness to enter into a three pillar Agreement (trade, political dialogue and cooperation) with the EU to the assurance that a full-fledged free trade agreement was going to be part of it, and that it would enter into force no later than the two other components. A whole new set of institutional provisions for the negotiations of the Mexico-EU agreement (the Interim Agreement) were put into place in order to make the Mexican goal possible. Serious trade negotiations also emerged only slowly in the EU-Mercosur process and then under pressure from the Mercosur partners, who had the option of focusing exclusively on the advancing FTAA negotiations.



Aside from the problem of the asymmetric priorities just mentioned, simultaneously advancing in a free trade and cooperation nexus, while highly desirable, is in practical terms, extremely difficult. It may be easier to establish the linkage in the cases when the North-South agreement is signed with relatively poor countries. The reason for this is that the cooperation component is traditionally supported by donor-recipient transfers from the North where an important part of the dynamic is unilateral. Mercosur is not a strong candidate for aid, and hence we can expect cooperation to be more reciprocal in nature, which means that the time consuming forces of consensus building will be important. Moreover, while a single undertaking is conceptually impeccable, the sake of EU-Mercosur negotiations may very well suffer from the complexity and political dynamics of such an agreement.

Experience suggests that to succeed, there is a need, *inter-alia*, to give priority attention to a limited number of programs at any one time, to have clearly identified objectives and work programs, quantifiable targets, political leadership in the particular program areas, capable national counterparts and a support structure, including adequate technical, logistical and financial backing. Lacking these, initiatives can stall soon after the Declaration of Heads of State.

Moreover, there are reasons to believe that an ambitious trade and cooperation initiative will have a higher chance of prospering if there is a dynamic trade component at its core. The promise of more trade and freer market access is a pillar for a sustainable North-South partnership and can endogenously drive cooperation in areas other than trade. Trade also has the advantage of a clear objective and established modalities and rules. Indeed, the forward momentum in the FTAA negotiations is a major reason for Latin America's continued interest in the broader Hemispheric initiative despite the poor performance of many of the cooperation programs to date.

In contrast, cooperation programs can have a more problematical setting. They generally encompass activities with more diffuse objectives, more difficult project identification and design, higher administrative costs, inevitable political spillovers, often difficult to measure results and can, depending on the subject matter, demand sizeable budget outlays. Moreover, moving forward in cooperation programs does not unambiguously generate endogenous forces leading to a free trade area. Indeed, the APEC initiative, which had been advancing steadily in the area of cooperation, nevertheless seems to be petering out due to the loss of direction in the trade liberalization process. In any event, developing countries in North-South initiatives sometimes interpret the cooperation programs proposed by their industrialized counterparts as a type of "camouflage" to avoid confronting free trade negotiations.

## **VI. IS THE MERCOSUR-EU (MEU) PROCESS A BEST PRACTICE?**

The trade and cooperation nexus in the Western Hemisphere process and APEC is very loose. APEC has advanced much more in cooperation than free trade, while in the Western Hemisphere process the reverse is the case. In other words the nexus at this stage is weak. APEC's cooperation program has an important reciprocal component and benefits from interest of some Northern members wishing to promote cooperation among themselves irrespective of trade as such. The Western Hemisphere process has suffered from too many cooperation programs that have too few quantifiable objectives/benchmarks, too little systematic technical, logistical and financial support, and perhaps too much heterogeneity among the 34 countries in terms of their needs, interests and capacity to implement cooperation programs.

The MEU process on paper is an innovative arrangement in North-South relations as the nexus is formally draped by a single undertaking legally subscribed in a formal Interregional Association Agreement (IAA). Moreover, the process includes a third pillar of political dialogue. It focuses on a relatively homogeneous group of LAC countries with a common integration project, and geographical cultural and historical ties. The EU also prepares programming papers to orient its relation with the region, negotiates a memorandum of understanding with the partner and develops programmed multi-year budget lines. Hence, the structured approach makes one look to the MEU as a potential best practice that offers lessons for the uneven Western Hemisphere and APEC processes.

However, the very slow progress on the trade front in the MEU process could disengage the countries and stall development of an eventual Association agreement. Moreover, to the extent that the parties are looking to the Doha Development Agenda negotiations to breakdown the barriers to a EU-Mercosur agreement in agro-trade, it must be remembered that target date of 2005 for a Doha agreement is enormously ambitious and may not be achieved. Finally, postponement of an agreement means that Mercosur loses an opportunity to enhance its credibility at a time when there are serious problems in this area and Mercosur watches while other LAC countries such as Chile and Mexico are moving ahead with successfully completed EU agreements.

What to do? One possibility is for the potential partners to aim for a sub-par agreement that would be committed to upgrading -via an integrated rendezvous clause- after a Doha agreement. Thus Mercosur would have to reestablish its common and external tariff and probably underachieve in its immediate market access goals and the EU would have to do the same for new issue areas such as services, government procurement, investment, etc. The configuration of sub-par agreement also would need some creativity to pass as WTO consistent.

Another alternative to keep the parties engaged is for the EU to follow the Mexican approach of an Interim Agreement, but this time in the area of Cooperation and Dialogue. Moreover, the cooperation component could focus on "post-trade negotiation" priorities that would enhance the effectiveness of the eventual trade agreement that would complete the 3-pillar Association Agreement, e.g. programs to enhance Mercosur's European and local firms' exports to the EU; institutional strengthening in areas where new issue trade disciplines will have to be implemented, capacity building in using modern rules of origin, support for EU-Mercosur business, labor, academic and NGO networks, etc.

By giving special attention to "post-negotiation" cooperation the two parties would signal their commitment to a free trade area and stay engaged in trade and investment related activities which have clearly defined objectives and benefits and a capacity to endogenously drive other areas of cooperation and dialogue. Moreover, the program would benefit from the EU's programming papers, Memorandum of Understandings and line item financing.

## APPENDIX I

### AREAS OF COOPERATION COVERED BY THE PRESENT AGREEMENTS

Areas of Cooperation							
Agreement Name	Trade-related Cooperation	Non-trade Cooperation					
		Economic	Political	Social and Cultural	Environment	Human Resources and Science & Technology	Other
EU-ACP	Competition policy, intellectual property rights, standardization and certification, sanitary and phytosanitary measures, trade-related environment and labor standards, consumer policy and protection of consumer health	Investment, private sector development, macro-economic and structural reforms, economic sector development, tourism, fisheries and food security	Human rights, democratization, rule of law, good governance, peace-building, conflict prevention and resolution	Social sector development, poverty reduction, health, youth and gender issues and cultural development	Environment and natural resources	Education and training	Regional integration and cooperation, institutional development and capacity building
EU-Mexico	Public procurement, competition, intellectual and industrial and commercial property rights, technical regulations and standards, sanitary and phytosanitary measures, protection of human and animal health	Liberalization of capital movements, and payments, industrial cooperation, investment promotion, financial services, cooperation on small and medium-sized enterprises, agriculture, mining, energy, fisheries, transport, tourism, statistics, consumer protection and data protection	Human rights and democratization	Social affairs, poverty reduction, health, refugees and cultural cooperation	Environment and natural resources	Science and technology, information and communication, education and training	Regional cooperation, and combating drug-related crimes

Areas of Cooperation							
Agreement Name	Non-trade Cooperation						
	Trade-related Cooperation	Economic	Political	Social and Cultural	Environment	Human Resources and Science & Technology	Other
APEC	Deregulation, dispute mediation, implementation of WTO obligations, customs procedures, standards and conformance, intellectual property rights, competition policy, government procurement and rules of origin	Macroeconomic policy, financial stability, structural reforms, economic infrastructure, business facilitation, financial systems, free movement of investments, mobility of business people, capital markets, energy, tourism, fisheries, transportation, telecommunications, small and medium enterprises, agriculture, rural infrastructure, food production and biotechnology	Political dialogue through Ministerial Meetings	Social safety, social development and gender integration	Environmental protection and marine resource conservation	Industrial science and technology, human resources development, knowledge and skills development, information and communications technology and electronic commerce	Emergency preparedness
ASEAN	Customs, dispute settlement, standards and conformance	Macroeconomic and financial stability, freeing movement of capital, investment facilitation, industrial development, infrastructure, food, agriculture and rural development, forestry, mining, energy, tourism, transport and communication	Political and security cooperation	Human and social development, poverty reduction, women and youth issues, cultural cooperation	Environment	Science and technology, human resources development, information and communications technology and electronic commerce	Combating the abuse and traffic in narcotics and drugs and transnational crime

Nota: (1) Environment and Transport Investment Support program (ISPA) and Agricultural and Rural Development Support (SAPARD).

**APPENDIX II**  
**THE INITIATIVES DRAWN BY THE MIAMI SUMMIT**

1. Strengthening Democracy
2. Human Rights
3. Invigorating Society
4. Cultural Values
5. Combating Corruption
6. Drugs / Money Laundering
7. Terrorism
8. Mutual Confidence
9. Free Trade in the Americas
10. Capital Markets Liberalization
11. Hemispheric Infrastructure
12. Energy Cooperation
13. Telecommunications
14. Science and Technology
15. Tourism
16. Access to Quality Education
17. Basic Health Care Services
18. Women in Society
19. Microenterprise
20. White Helmets
21. Sustainable Energy Use
22. Biodiversity
23. Pollution Prevention



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