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From a North American to an American Community: The 21st Century Challenge of Integration

Men are powerless to secure the future; institutions alone fix the destinies of nations.[1]
—Napoleon

For many years, Mexico warned its neighbors of the perils of getting too close to the United States, either politically or economically. Independence and sovereignty depended on setting clear limits on the relationship with the northern colossus. Latin American leaders did not share Mexico's history, but they understood the need to protect their nationalist flank, and so few sought close relations or risked opening their economies. When the Mexicans proposed a free trade agreement with the United States, replacing their veto on good relations with an affirmation, they opened a door through which virtually every country in the hemisphere requested permission to enter. In December 1994, President Clinton invited the hemisphere's 33 other leaders to enter the US market—although, of course, that was not the way the Summit of the Americas agreement was described. The leaders only pledged to negotiate a Free Trade Area of the Americas by 2005. Nevertheless, the agenda of the negotiations was the outline of NAFTA, and so it is not inaccurate to describe the FTAA as a widening of NAFTA. The prospects for success, however, also depended on Latin America's progress in two areas: imple-

1. *Imperiale Séance*, 7 June 1815, quoted in World Bank, *World Development Report 1997* (New York: Oxford University Press), 29.

mentation of economic and political reforms[2] and other free trade initiatives in the hemisphere. A few such agreements—like Mercosur—were new, but most had originated in the 1960s with the first wave of regional integration. The Andean Pact, the Central American Common Market (CACM), the Caribbean Community—these schemes had run out of steam, were fractured by national rivalries, or were wracked by civil wars. Yet in the 1990s, these old schemes were not just dusted off; they were invigorated and transformed.

Let us first describe the development and progress of these subregional trade agreements. Next, we will explore whether it would be wiser to deepen NAFTA or widen it to the FTAA and whether the sequence matters. Then we will shift from the hemispheric implications to the question of how these talks will affect the next round of world trade negotiations. We will conclude the chapter by returning to North America and making the case for overcoming inertia and constructing a Community that will illuminate a path for rich and poor countries alike.

The Trend toward Integration

NAFTA was not the ignition switch that started the other integration movements in the Americas, but it did put wind in their sails. The regional schemes were products of similar causes and circumstances. Most of the countries of Latin America had undertaken structural economic reforms in the mid-1980s in response to the debt crisis. All were compelled to take the same medicine—restore fiscal discipline, privatize state-owned corporations, maintain a realistic exchange rate, and reduce barriers to trade and investment. As a result, average tariff levels declined in Latin America from more than 40 percent in the mid-1980s to 12 percent in the mid-1990s, and trade raced ahead—averaging 12 percent annual growth for the period 1990-97.[3] Intraregional trade grew considerably faster than extraregional trade in the 1990s, and this was due to the rebirth of subregional trade agreements.

The Andean Community, originally established in 1969 as the Andean Pact, negotiated a four-country free trade area by 1993 and a partial customs union between three members (Colombia, Ecuador, and Venezuela) 2 years later. Peru agreed to join in 1995, and by 2000, the free trade area was largely complete. In addition, the presidents established the

2. For a thorough analysis of the status of the economic and political reforms undertaken by individual Latin American and Caribbean governments as a prelude to successful negotiations for a Free Trade Area of the Americas, see Jeffrey J. Schott, *Prospects for Free Trade in the Americas* (Washington: Institute for International Economics, 2001).

3. Inter-American Development Bank, Department of Integration and Regional Programs, *Integration and Trade in the Americas* (Washington, 2000), 2, 7.

Andean Presidential Council, which meets regularly, they strengthened the Andean Court of Justice, and they pledged to establish a common market by 2005.[4] Intraregional trade grew by an annual average of 18 percent in the 1990s, three times faster than the region's trade with the world.

The Caribbean Community (CARICOM), founded in 1973 with 13 members, subsequently expanded to include Haiti and Suriname. With a combined gross product of $20 billion, and a population of 6 million (excluding Haiti), the Caribbean governments remain vulnerable to economic shocks from the world market or large neighbors. Nonetheless, beginning in the 1990s, they took steps to open their economies. They implemented a free trade area and made considerable progress toward a common external tariff (CET) and a single market. CARICOM's free trade agreement with the Dominican Republic came into force in January 2001, and it signed an agreement to enhance commercial links with Cuba in July 2000. On 18 May 2000, President Clinton signed the US-Caribbean Basin Trade Partnership Act, which provides the same free access to the US market in apparel that Mexico had received because of NAFTA. Intraregional trade in CARICOM in the 1990s grew at an annual rate of 12 percent, which was double the rate of the region's trade with the rest of the world.

The Central American Common Market was probably the most successful economic pact in the developing world in the 1960s and early 1970s, but civil wars and tensions between the countries halted its progress by 1980. In 1993, the countries signed the Protocol of Guatemala, which reaffirmed their goals of a customs union and a common market. But they also pledged to implement a low common external tariff. In 2000, they achieved their goal of a CET of 0-15 percent. At the same time, Guatemala and El Salvador formed a customs union and decided to collect tariffs together. The other countries are negotiating to join. CACM also negotiated free trade agreements with Canada, Chile, the Dominican Republic, and Mexico. Intraregional trade increased by 15 percent a year in the 1990s, 20 percent faster than their trade with the world.

The most spectacular advance in subregional integration occurred among historical rivals in the Southern Cone. Argentina and Brazil joined with Paraguay and Uruguay in 1991 to establish Mercosur, or the South American Common Market. Tariffs were dismantled according to the schedule that they initially approved, and a CET of 0-20 percent was in place by January 1995. This represented a very sharp reduction in protection for the area—from an average tariff of 41 percent in 1986 to less than 13 percent in 1999. By 1997, the governments had negotiated an agreement for the free movement of capital and services.

4. For a good update and analysis of each trading scheme, see *ibid.*, 28-54.

Perhaps because of the region's closer ties to Europe, Mercosur defined itself in terms that went beyond just economic cooperation. They agreed to develop together regional infrastructure in transport, energy, and telecommunications. And in 1998, the four countries signed a Declaration on Workers' Rights and a separate agreement to support democracy, human rights, and a "peace zone." The Mercosur countries have also negotiated associate membership with Bolivia and Chile, and are consulting with the Andean Community. Although Mercosur has been tested by the financial crisis in Brazil and rising unemployment in Argentina, it has continued to expand and deepen economic cooperation. The member governments have reached a sectoral agreement on automotive trade, and they are negotiating ways to harmonize immigration policies (through a Mercosur passport and greater workforce mobility), financial statements and statistics, and macroeconomic coordination. Most important has been Mercosur's extraordinary growth of intraregional trade—averaging 19 percent a year during the 1990s, almost three times higher than the rate of growth of their world trade.

Before the economic opening and invigoration or creation of regional trade agreements, Latin America had found its position in the international economy deteriorating. But in the last decade of the 20th century, Latin America halted its decline and began to improve its position. The region's growth in trade (10.8 percent in value terms) significantly exceeded that of the world (6.6 percent).[5]

The expansion and strengthening of these subregional agreements was due not just to a convergence of economic policies among Latin American governments but also to two equally powerful currents—democracy and globalization. Since the mid-1970s, when the military governments in Ecuador and Peru pledged to transfer power to civilians in free elections, Latin America gradually moved toward democracy. By the 1990s, every country in the hemisphere, except Cuba, had competitive elections judged by all parties and the international community as free and fair. Although democracy's roots were shallow and fragile in numerous countries, that fact promoted greater democratic solidarity among the civilian presidents and reinforced the trend toward economic cooperation. At the same time, the restoration of democratic rule brought to power new leaders who learned a lesson from Asia's exceptional economic progress and export-promotion strategies. Those countries in Asia and elsewhere that were most open to globalization tended to grow faster and reduce poverty more than those that protected their economies. For all these reasons, the new subregional trading efforts are much more serious than previous ones. Although it is still too soon to know whether they will culminate in free trade areas, customs unions, or common markets—let alone a

5. *Ibid.*, 9.

Free Trade Area of the Americas—they have already made substantial progress. If they can accept the NAFTA version of the *acquis communautaire* (the changes in national policy required for membership in the European Union), then Latin America might permanently secure their trade, economic, and democratic reforms.

The Road to the Free Trade Area of the Americas

After the 1994 Miami Summit, the hemisphere's trade ministries began to document existing trade policies and regulations of each country and organize a comprehensive database. At the Santiago summit in 1998, the leaders officially launched trade negotiations and organized them in nine negotiating groups that reflected the chapters of the NAFTA agreement: market access; agriculture; government procurement; services; investment; intellectual property; subsidies, antidumping, and countervailing duties; competition policy; and dispute settlement. In addition, the governments established other committees on business facilitation, electronic commerce, civil society, and smaller economies. The trade ministers produced a bracketed text of a draft agreement for the Third Summit of the Americas in Quebec in April 2001, and the leaders there reaffirmed their commitment to conclude negotiations for an FTAA by January 2005 and complete ratification by the end of that year.

US government officials pointed to the list of committees and meetings as signs of progress, though there was little. The only real progress in trade liberalization occurred outside these negotiations—in the implementation of existing subregional agreements and the proliferation of bilateral and plurilateral free trade arrangements. Since 1992, Latin American governments have negotiated 18 trade agreements with each other. Even more significant was that the five agreements negotiated before 1995 were narrow, in the sense that they sought to eliminate only tariffs and nontariff barriers. After NAFTA, however, all 13 agreements went beyond tariffs and nontariff barriers to include numerous NAFTA issues, including harmonization of policies on services, intellectual property rights, and competition policies.[6] In that sense, NAFTA redefined the trade agenda. This progress, however, was outside the FTAA. Why were there no serious discussions within the many FTAA committees, despite the pledges of participating governments? There are several reasons.

First, as trade barriers declined, inefficient industries began to suffer in all countries. The rich countries feared cheap imports, and the poor countries feared competing against more advanced countries. Firms that

6. *Ibid.*, 46-48, for a list of the agreements and a description.

are fearful are more motivated to influence the political process, and the prevalence of democratic institutions throughout the Americas made it easier for them to shape policy. Second, Brazil, with about half of South America's population and gross product, wanted time to consolidate Mercosur and extend it to the other South American countries. Toward this goal, President Fernando Cardoso summoned his counterparts from every country in South America to a summit in Brasilia in September 2000 to establish a South American Free Trade Agreement that would negotiate with NAFTA on the basis of greater equality. Most South American governments wanted to expedite, not slow the process, but their options were limited. Third, Canada and Mexico were not eager to share their exclusive access to the world's largest market, and after the passage of the Caribbean Basin Act, the nations in the Caribbean and Central America were in less of a hurry as well. The fourth reason, however, is pivotal for explaining the lack of genuine progress toward an FTAA: the US president was unable to obtain fast-track negotiating authority from Congress, and without a clear sign that the United States was prepared to commit itself to costly trade-offs, no other government wanted to make premature sacrifices.

What was the problem in the United States? The Congressional elections in 1994 not only brought the Republicans to power in Congress, but they polarized the two political parties, particularly on trade. The Republicans became more laissez-faire—rejecting any labor or environmental agreements, though they had accepted them a year before in NAFTA—and the Democrats became more reliant on labor unions and thus less interested in free trade. President Clinton was not able to build a bridge across this chasm. President Bush announced in Quebec in April 2001 that "trade-promotion authority" was a high priority, and Robert Zoellick, the president's trade representative, set to work to cobble together a coalition in Congress to approve a bill.

Brazil, with its dominant position in South America, raised legitimate questions about several protectionist tactics, such as the use of countervailing duties by the United States and other countries. A successful FTAA will need to respond to these concerns, and this is likely to occur because Brazil and the United States will cochair the last stage of the negotiations. Despite the need to take into account the concerns of Brazil, one should keep in mind the relative economic weight of Brazil and Mercosur as compared with the United States and NAFTA (see table 8.1). The gross product of all the Americas in 1998 was roughly \$10.8 trillion, of which the United States accounted for \$8.2 trillion, or 76 percent. Canada and Mexico add another 9 percent to the total, giving NAFTA a towering 85 percent of the market of the Americas.

Although it is the second largest economy in the Americas, Brazil accounts for only 7 percent of the total market, and its exports are less than 4 percent of the hemisphere's total exports. Two-way trade between Brazil and the United States was $30 billion in 2000; with Mexico, it was nearly $250 billion. More than 60 percent of all US exports to Latin America went to Mexico in 2000. In brief, Latin America needs the US market much more than the United States needs Latin America's.

There is another way of looking at the trade data, however. In 1999, US exports to its two neighbors were $253.5 billion, roughly 40 percent above its exports to the 15-nation European Union, and more than 3.5 times its exports to China and Japan (see table 8.2). If one adds the rest of the Latin American market, US exports climb an additional $55 billion, making it double the EU market and more than 4 times that of China and Japan. South America constitutes a small supplementary market for US goods at this time; the question is whether the FTAA would expand that market, as NAFTA did for Mexico. Although South America has made important progress in reducing its protectionism in the last decade, it remains one of the most protected middle-income regions of the world. If Brazil received the same trade treatment as Mexico, and if it lowered its trade barriers to the level of Mexico's, then US-Brazil trade would have tripled to about $86 billion in 2000, according to calculations by Schott and Hufbauer.[7] The FTAA could contribute to the internationalization of the Brazilian economy, much as NAFTA did for Mexico, and it could represent the fastest-growing market for US goods.

From a narrow economic perspective, the United States does not have an immediate or compelling need to complete the FTAA—or, for that matter, to deepen NAFTA. The motive for doing so would be to take advantage of future potential. A deeper NAFTA would facilitate the competitiveness of the North American economy; it would, if designed properly, accelerate equitable growth in Mexico and eliminate unnecessary tensions and transaction costs among the three countries. A wider NAFTA would mean an expanding market. Together, they could give additional ballast to an emerging democratic and prosperous hemisphere.

Widen or Deepen?

Which should come first? Should Canada, Mexico, and the United States deepen NAFTA, or should they give priority to widening it to the rest of the Americas? The Europeans chose to widen the European Community beyond the original six countries before they deepened it, and they found that each stage of deepening became progressively harder. It took Europe several decades of trial but mostly error to get to the point where a single currency was possible, and even today, several members have not

7. Jeffrey J. Schott and Gary C. Hufbauer, "Whither the Free Trade Area of the Americas?" *The World Economy* 22, no. 6 (August 1999), 765-82.

Table 8.1 Basic indicators for the Americas

Group or country	Population, 1998 (millions)	GDP (billions of dollars) 1980	GDP (billions of dollars) 1998	Exports (billions of dollars) 1983	Exports (billions of dollars) 1998	Imports (billions of dollars) 1983	Imports (billions of dollars) 1998
North America	396	3,198.5	9,202.7 (85 percent of all)	371	1,287.20	401.3	1,478.8
United States	270 (68.2)	2,709 (84.7)	8,210.6 (89.2)	256.7 (69.2)	914.9 (71.1)	309.5 (77.1)	1,097 (74.2)
Canada	30 (7.6)	266 (8.3)	598.9 (6.5)	85 (22.9)	243.6 (18.9)	76.6 (19.1)	241 (16.3)
Mexico	96 (24.2)	223.5 (7.0)	393.2 (4.3)	29.3 (7.9)	128.7 (10.0)	15.2 (3.8)	140.7 (9.5)
Mercosur	202	356.9	1,238 (11 percent of all)	39.9	111	34	148.9
Brazil	166 (73.8)	234.9 (65.8)	778.3 (62.9)	23.5 (59.0)	57.8 (52.0)	20.5 (60.4)	78.6 (52.8)
Argentina	36	77	344.4	9.2	28.2	6.5	37.5
Paraguay	5	4.6	8.6	0.4	1	0.7	3
Uruguay	3	10.1	20.2	1.3	4.3	1.2	4.7
Andean Community	109	138	289.3 (2.7 percent of all)	26	46.5	21.4	62
Venezuela	23 (21.2)	69.4 (50.3)	105.8 (36.6)	15 (57.7)	18.5 (39.7)	9.0 (42.2)	20.8 (33.6)
Colombia	41	33.4	91.1	3.8	14.9	6.2	20
Peru	25	20.6	64.1	3.7	7	3.4	12.2
Ecuador	12	11.7	19.8	2.6	4.8	2	6.6
Bolivia	8	2.8	8.6	0.8	1.3	0.8	2.4

Caricom[a]	14.1	4.1	9.4	1.4	2.9	2.3	4.8
Haiti	8	1.5	2.8	0.2	0.1	0.4	0.6
Jamaica	3	2.6	6.6	1.2	2.8	1.9	4.2
CACM	32	21	48.4	4.4	12.8	5.6	19.1
Guatemala	11 (34.3)	7.9 (34.3)	19.3 (39.9)	1.2 (27.2)	3.1 (24.1)	1.4 (24.4)	5.2 (27.5)
El Salvador	6	3.6	12.1	0.9	1.5	1.1	3.5
Costa Rica	4	4.8	10.2	1.1	5.6	1.2	5.8
Honduras	6	2.6	4.7	0.8	1.9	1	2.8
Nicaragua	5	2.1	2	0.5	0.7	0.9	1.8
The Americas[b]	790	3,726.1	10,803.9	444.4	1,464.3	467.6	1,721.1

CACM = Central American Common Market.
Caricom = Caribbean Common Market.

a. CARICOM export and import data were only available for Haiti and Jamaica.

b. Chile, Dominican Republic, and Panama are included in the numbers for the Americas, but Cuba as well as some members of CARICOM are not because World Bank statistics did not include them.

Note: Numbers in parentheses are percent of the total.

Sources: For GDP, exports and imports: World Bank, *World Development Report 1999/2000: Entering the 21st Century*, 252-3, 268-9. For population: World Bank, *World Development Indicators 2000*, table 1.1, 13.

Table 8.2 US Exports to North America, South America, the European Union, Japan, and China, 1980-99
(millions of dollars)

Year	North America[a]	South America and Caribbean Basin[b]	EC/EU	Japan and China
1980	55,476	23,600	58,855	24,545
1985	66,922	17,221	45,776	26,487
1990	111,953	25,129	86,424	50,391
1995[c]	173,518	49,949	123,671	76,097
1999[c]	253,509	55,156	151,814	70,577

EC/EU = European Community or European Union.

a. North America is defined as including Canada, Mexico, and the United States.

b. The Caribbean Basin is defined as the governments of the Caribbean and Central America.

c. Data include exports of manufactured goods, agricultural goods, and all services.

Sources: US International Trade Administration, *U.S. Foreign Trade Highlights* (1985, 1988, 1992); Bureau of the Census, *Statistical Abstract of the United States* (various issues); International Trade Administration, *U.S. Total Exports to Individual Countries*, 1991-1999, http://www.ita.doc.gov/PRFrameset.html.

accepted the euro. Despite frequent summit meetings, Europe's leaders insist on retaining a veto on key decisions. This has made it difficult to consider reducing the mountain of subsidies provided under the Common Agriculture Policy. It has postponed a decision to change the formula for the regional policy to allow for the European Union's next enlargement. Absent a decision, the Union would bankrupt its budget. The Treaty of Nice in 2000 made limited progress in these directions, but still the Irish public rejected it in a referendum on 8 June 2001. It is difficult to deepen an organization after it has been widened.

Canada, Mexico, and the United States would promote market efficiency if they widened NAFTA to the rest of the Americas and deepened North American integration. Widening means an enlargement of the market, permitting even greater economies of scale. Deepening involves the reduction of internal barriers or distortions. Deepening is a far more complicated and difficult process, because it goes to the heart of how each government regulates its economy and provides for its citizens' welfare. Moreover, each government has groups, policies, or national symbols that it feels a need to protect. The Canadians, for example, are attached to their comprehensive health care system, regardless of its cost and its delays. The Mexicans are averse to allowing foreigners control of their petroleum. And the US sugar industry has rebelled at any effort to remove its subsidies. In each of these areas, an efficient policy would quickly collide with a powerful interest or symbol, making harmonization or compromise difficult.

Beyond these controversial areas, governments would benefit from negotiating uniform standards—for example, on safety, product design, or labeling, or on eliminating subsidies to declining industries or farms. Still, none of these decisions would be easy, and that led Doran—one of the most perceptive students of the debate on widening versus deepening—to characterize widening as ''seductive'' and relatively easy and deepening as ''painful'' but more important.[8] He favors both deepening and widening, but he believes that ''deepening ought to precede widening, because widening adds diversity, and diversity leads to conflict over priorities and goals.''[9] Whenever a new country joins the community, it often slows the integration process or vetoes the next steps. But his argument is based on a broader point:

> A liberal area based on advanced liberalization of trade, investment, and other rules that impinge on the economy will be much more of a community, and will be much more market efficient, than a looser, more diverse trade grouping of larger size that is still groping for a common denominator of progressive liberalization and standardization. Optimally, therefore, deepening ought to precede widening.[10]

Doran's argument is, to a great extent, based on the EU experience, but does it apply to the Americas? Once the FTAA is completed, the dispute-settlement mechanism would provide a built-in cost to any government trying to retreat or defect. Moreover, the FTAA will provide an incentive to deepen, because the removal of policy distortions will lead to more effective global competition. The major difference between North America and the European Union is the dominance of the United States. That has obvious disadvantages, but an advantage is that many of the decisions to deepen could be done in a de facto manner. Those who trade will follow the US standards. This may be what occurs on dollarization. Businesses find it easier to use the dollar as a standard, and over time, governments may find the decision on currency made for them. So it is quite possible that the dichotomy between widening and deepening might not be as compelling in the Americas as in Europe.

Moreover, a single approach toward integration might not be needed in the Americas; some deepening and widening can be done at the same time. If the three governments of North America decide to deepen their

8. For a thoughtful analysis of these issues, see the following two essays by Charles F. Doran: ''When Building North America, Deepen Before Widening,'' in *A New North America: Cooperation and Enhanced Interdependence*, ed. Charles F. Doran and Alvin Paul Drischler (Westport, CT: Praeger, 1996), 65-89; and ''Whither North America?'' in *Toward a North American Community*, ed. Donald Barry (Boulder, CO: Westview Press, 1995), 271-81.

9. Doran and Drischler, *New North America*, xv, 66.

10. *Ibid.*, 69.

relations and establish some common organizations, the rest of the Americas can choose to follow or remain outside.

With regard to the question of which trade strategy makes the most sense for the United States, it is worth recalling that the very nature of the US political system seems to work against strategic thinking on trade—or, for that matter, on almost any field. There are simply too many actors and too much pressure, and that great hydra-headed, multibranched monster called the US government often ambles on several tracks at the same time. Strategists are often frustrated by a style that seems to dissipate US energies rather than concentrate them, but they should relax in this case: The objective of integrating the hemisphere might be best achieved by a multipronged approach. The United States should move quickly on negotiating the FTAA, and it should consult with its NAFTA partners on ways to deepen their relations. It might very well discover that the more channels one pursues, the greater the chance of achieving them all—at least in trade policy. One more benefit of *multiple trade negotiations* is that Latin Americans might prefer that to an approach in which Washington is applying its full weight.

Having said that, it would still be desirable if the United States had a plan with some priorities. First, it should deepen the North American Community and build organizations that will ensure that the integration process is smooth and effective. Second, it should continue to provide a support system under the Caribbean Basin countries, which are small, vulnerable, and strategically important. And third, Brazil and the United States should cooperate to bring the FTAA to an expedited conclusion.

The FTAA's members should be encouraged to adopt and adapt the organizations that are designed for a North American Community. For example, the idea behind the North American Commission—that a multinational advisory group could formulate a North American agenda—could be adapted to a wider FTAA. The Americas will need a hemispheric agenda, and the plans generated by the NAC—for example, on transportation or energy—could be adapted to the broader Community.

The Western Hemisphere and the WTO

Distinguished economists like Jagdish Bhagwati and Milton Friedman feared that NAFTA and other regional agreements could be stumbling blocks, preventing the Uruguay Round of Global Trade Negotiations from reaching a conclusion.[11] In fact, the opposite occurred. Soon after Congress

11. Jagdish Bhagwati, "Jumpstarting GATT," *Foreign Policy* 83 (Summer 1991); and "Milton Friedman Criticizes Regional Trade Agreements," *El Financiero International* (Mexico City), 1 June 1992, 3. For a full discussion of this debate as to whether NAFTA would be a stumbling or a building block, see Robert A. Pastor, *Integration with Mexico: Options for U.S. Policy* (New York: Twentieth Century Fund Press, 1993), chap. 6.

approved NAFTA, Europe and Japan, evidently fearful that the United States might exercise its regional option, accelerated the global trade talks, and they were completed in months.

The reason is that within each of the three great trade areas, one global power exerts disproportionate influence. Economically, the United States is preeminent in NAFTA; Japan plays a similar role in East Asia; and Germany does so in the European Union. What unites these three trading powers is the recognition that their global power is rooted in a rule-s-based, worldwide system. Their economies would be harmed if their only market were a regional one. All three have compelling interests in maintaining a world trading system. To the extent that the United States can deepen and widen its relationships in the western hemisphere, the world will also be better off, and Latin America will have options that it did not have in the past. The regional agreements also aim to create more efficient units for global trade and production by harmonizing or eliminating those barriers to trade and investment that have resisted global efforts. In brief, such ''open'' regional trade agreements are building, not stumbling, blocks.

There is another reason why proliferating regional integration agreements stimulate rather than impede serious global negotiations. In June 1999, the heads of state of the Mercosur countries and the European Union met in Rio de Janeiro to launch negotiations for ''reciprocal trade liberalization, without excluding any sector and in accordance with WTO rules.'' Within a year, Mexico completed a free trade agreement with the European Union as well. Why? The Mercosur-European Union (MEU) talks were, in the view of Robert Devlin, an economist at the Inter-American Development Bank, ''the EU's strategic response to the launch of the FTAA negotiations. As for Mercosur, the MEU process offered the promise of increased leverage for its FTAA negotiations.''[12]

The *absence of negotiations* is the *worst disease* for free trade. The *best medicine* is *more agreements*, provided that they are nondiscriminatory and open, because they stimulate competition and encourage each group to catch up to its competitors.

Although the regional trade schemes define rules for businesses, the political dimension should not be overlooked. Democracy has not only increased the chances that regional trade agreements would be reached and maintained; these agreements have helped to maintain democracy among their members. The most obvious case in Latin America is Paraguay: Argentina and Brazil openly threatened the Paraguayan military that their country would be expelled from Mercosur if they dared overthrow their government.[13]

12. Robert Devlin, *The Free Trade Area of the Americas and MERCOSUR-European Union Free Trade Processes: Can They Learn Something from Each Other?* INTAL-ITD Occasional Paper 6 (Washington: Inter-American Development Bank, 2000), 7.

13. For an excellent case study, see Arturo Valenzuela, *The Collective Defense of Democracy: Lessons from the Paraguayan Crisis of 1996*, report to the Carnegie Commission on Preventing Deadly Conflict (New York: Carnegie Corporation, 1999).

From the beginning, the European Union encouraged democracy on its periphery by denying entry to Greece, Portugal, and Spain until each had free elections. Over time, the Union has become more insistent that its members and future members adhere to democratic principles, and the snub against Austria for electing a right-wing government was a recent public reminder of that. Since the Treaty of Amsterdam, the Union has insisted that entry by Eastern European governments would require adherence to very specific political criteria.

Democracy is valuable in the Americas precisely because its political history has been plagued by dictatorship. As the 21st century dawns, each country in the hemisphere, except Cuba, is committed to maintaining and deepening its democracy and helping its neighbors as well. But just as in economics, the political deepening of democracy is more problematic than its widening, partly because there is no consensus on what deepening means or how to do it. Some scholars equate deepening with consolidation, and define both as institutional and attitudinal respect for political systems of vertical and horizontal accountability.[14] Vertical accountability—between leaders and people—relies on free and fair election procedures that are judged as such by all the major political parties. Horizontal accountability means that each major institution of government respects other institutions' boundaries. The executive does not attempt to close the legislature or the courts; the courts obey the laws and the constitution, not the military, president, or prime minister; and the legislature is careful to respect the constitution if it finds just cause to impeach the president or members of the court. Many countries in Latin America have a fourth branch of government—an election commission and court—and the autonomy of those institutions is designed to safeguard both axes of accountability.

The principal risks to Latin America's democracies seem to stem from the weakness of their political parties, the hubris of their leaders, the paucity of well-crafted laws and regulations, and the arbitrariness of enforcement. Deepening democracy requires the careful development of political parties and the construction of legal restraints on the abuse or corruption of power. Almost all of the responsibility for preserving democracy rests with the people and institutions in each country, but the last line of defense is collective action. The FTAA, therefore, needs to incorporate a chapter on democracy that defines the rules for entry, punishment, and suspension of governments. In Quebec, the summit leaders announced their support for a "democracy clause" that would preclude unconstitutional regimes from being represented at summit meetings. But the leaders

14. See, e.g., Andreas Schedler, Larry Diamond, and Marc F. Plattner, eds., *The Self-Restraining State: Power and Accountability in New Democracies* (Boulder, CO: Lynne Rienner Publishers, 1999); and Larry Diamond, *Developing Democracy: Toward Consolidation* (Baltimore: Johns Hopkins University Press, 1999).

failed to define violations of democracy or the specific steps that the Community would take in response. An effort by the Peruvian government to develop a "Charter on Democracy" was set back at an OAS General Assembly in June 2001, but the OAS has continued to pursue negotiations to achieve consensus on such a Charter.

Entry into the FTAA should require acceptance of the rules and procedures of democracy. Elections need to be free and fair, and all major parties need to view them as such. The FTAA should associate with the Inter-American Court of Human Rights, based in Costa Rica, which should delegate to a distinguished committee the responsibility to observe and oversee any electoral disputes that cannot be settled by domestic institutions. All citizens of the Americas should have the right to petition before this body and seek redress both from their government and from the FTAA institutions. Serious violations of democracy should be judged like a trade dispute, in which a failure to comply with the court's decision would elicit sanctions of some sort—perhaps a withdrawal of trade privileges. A coup d'état would naturally evoke suspension from the FTAA, just as it would from the OAS, and the multilateral development banks would halt loans to the regime.

The Americas should accept nothing less. Indeed, the FTAA should go beyond the questions of membership or suspension and propose ways to nurture the roots of democracy, particularly in its weak neighbors. This democratic dimension would give real meaning to the concept of the Community of the Americas.

The Strategic Challenge of the 21st Century

Since the Second World War, the world has witnessed a remarkable expansion of free markets and trade. This has been both cause and consequence of the transfer of technology, the compression of distance and communications, the spread of universal values of human rights and democracy, and the strengthening of the rule of law within countries and among them. People, businesses, and societies have connected with each other in ways that have permitted the quality of life to improve demonstrably in all but the most isolated, poorest nations of the world. A global system has been created by private initiative and by decisions of nation-states.

This integration process has arrived at a critical moment. New forms of governance need to be established if the process is to continue, grow, and become more equitable. Global institutions—like the World Trade Organization—are not suited to negotiating the rules of deeper integration. There are too many members with too many diverse interests at too many levels of development. The noise of Seattle in November 1999 was just one sign of the WTO's incapacity to address this next challenge. The best arena is regional bodies, although even at this level there will be a clamor.

One of the most important challenges for the international community at the beginning of the 21st century is to define the space that will permit middle-income developing countries to graduate to the industrial world of trade and development. This is not to minimize the more serious problem of assisting the poorest people in the poorest countries, but other institutions—notably the World Bank and the regional development banks—are suited for that task.

NAFTA has been innovative in four ways and, as such, is a model for addressing this global, 21st century challenge. First, it has brought together countries on disparate levels of development whose histories are laden with deep-seated suspicion. Second, it has gone beyond eliminating tariffs and nontariff barriers, and has regulated and harmonized a range of policies in many sectors including foreign investment, services, and intellectual property rights. Third, it has recognized the importance of incorporating workers' and environmental rights, although it has done so only by insisting that each country enforce its own rules. Fourth, it has established a dispute-settlement mechanism to resolve trade and investment problems. These provisions have been implemented, some more effectively than others. But the problems that North America has encountered are not due to what NAFTA includes, but rather to what it omits.

The United States and its neighbors should proceed to establish a North American Community, but not at the price of a Free Trade Area of the Americas. Rather, both initiatives should be pursued simultaneously. The competition would be helpful. The deepening of NAFTA can preserve a special relationship among the three nations of North America, and its model might be of use to the FTAA in the future.

NAFTA's Premise and Promise

NAFTA's premise was that if the continent's three nations dismantled the barriers to trade and investment, the magic of a free market would better the lives of everyone. The free market is wonderfully designed to produce diverse and inexpensive goods, but it provides no answers to the collective problems that inevitably emerge from the market's failures, or even its successes. Without multinational organizations and uniform rules, the three governments cannot clean up pollution at their borders; they cannot reduce or stop illegal migration; they cannot manage or eliminate the hidden and illegal dimension of integration (drug trafficking, transnational crime, and money laundering); they cannot address the unevenness of taxes and welfare; and they cannot reassure those groups in each country that fear integration will endanger their livelihoods and values.

This book has developed a set of general principles and numerous specific proposals to allow the North American countries to redefine their relationship and thus to help them jump over the next hurdle of integration. First, the three countries should establish a North American Commission composed of distinguished individuals who are appointed *by* the three governments but are not *in* any of the governments. This Commission would set a continental agenda for the leaders of the three countries to forge new ways to facilitate integration. Second, the Commission should propose a North American Plan for Transportation and Infrastructure and should seek initial funding from the World Bank and the Inter-American Development Bank, with the understanding that the three governments would eventually provide the funds directly to build a North American network of roads, railroads, and shipping.

Third, the three governments need to devise collective mechanisms to handle the illegal flow of people, arms, goods, drugs, and so on across their borders. Numerous experiments are under way to find ways to untangle the dilemma between erasing trade barriers and impeding illegal trade, but even new devices—such as transponders—require a new kind of governance, because at the current time, there are too many jurisdictions within the three countries, let alone between them, to allow for a uniform standard. This challenge of devising practical systems of North American governance should be addressed by NAC and the three governments.

Fourth, I propose that the three governments create a development fund based on a regional policy that aims to lift the poorest regions of North America, much as the European Union has narrowed the disparities between its rich and poor member countries. Such a fund, which initially could be assisted and administered by the World Bank and Inter-American Development Bank, would invest most of its resources in infrastructure and education. The infrastructure should include new and modern roads from the border to the center and the south of Mexico, where it would link with the new Puebla-Panama Corridor. The fund also should establish community colleges in the poor states of Mexico, and also perhaps develop courses or research institutes on North American affairs in Canada and the United States. These colleges could also improve education in poor areas. The United States should work with its two neighbors to make sure that the Fund is well-financed so that it would do for North America what the European Union's Structural and Cohesion Funds have done for its four poorest members. It could lift both the economies and the spirits of the poor areas and begin to create a spirit of community that would have positive spillover effects on all the countries.

Such a proposal is quixotic if the governments remain bound to the old concept of sovereignty. The historic shield—the defense of sovereignty—stemmed from fear of the foreign, but modern democratic leaders have redefined sovereignty to permit them to reach across borders to deal with transnational problems. Public opinion surveys suggest that the people in all three countries are much less interested in abstract debates about sovereignty than about improving their lives and dealing with issues that their governments seem helpless to address. In this case, the lesson to be drawn from Europe's experience is eminently pertinent to North America. A French scholar defined that problem and the opportunity:

> Governments are naturally obsessed by issues of nationality. When emotion tends to color objective interests, disputes get more complex. Europe's citizens, however, are much more relaxed than their elected representatives about largely symbolic matters. They do not think in terms of sovereignty or nationality. They want to know who is in charge, who is responsible . . .[15]

People are far more pragmatic than their leaders give them credit for being. They are prepared to try radical ideas if they think doing so will improve the economy and their lives. Organizations count, however. Joining any international organization involves new obligations and constraints on a nation-state's behavior, but if one believes in a fair process and a uniform set of rules, then one wants to make sure the rules apply to everyone—and are enforced. In the end, such a system permits greater certainty, reliability, and trust and thus reduces transaction costs across the board. In that sense, *countries do not cede sovereignty, nor do they diminish their abilities by integration*. The *opposite* seems closer to the truth. Such agreements permit more efficient development, more effective autonomy, and greater ability to address transnational problems.

Why should we move toward a North American Community and from there to a Free Trade Area of the Americas? There are two simple answers to the question: It is the best way to avoid serious problems, and it is the best way to seize outstanding opportunities. In the middle of 2000, a Canadian trade negotiator wrote to other Canadians: "Should the current nine-year economic expansion in the United states weaken or end, Canadians may be reminded once again of how ugly US trade politics can become, how much Canada relies on good rules and procedures to keep US protectionism in check, and how the increasing sophistication and reliability of those rules and procedures have provided Canada with the capacity to resist US protectionist pressures."[16] The same argument applies in all three countries.

Unless the three governments develop policies to cover new problems, there is no certainty that existing rules will endure turbulent seas. If the United States fails to implement the agreement on sugar or trucks; or if

15. Dominique Moisi, "Caught between Enlargement and Globalization," *Financial Times*, 15 January 2001, 17. Moisi is the deputy director of the French Institute of International Relations.

16. Michael Hart, "The Role of Dispute Settlement in Managing Canada-U.S. Trade and Investment Relations," in *Canada Among Nations 2000: Vanishing Borders*, ed. Maureen Appel Molot and Fen Osler Hampson (New York: Oxford University Press, 2000), 94.

Mexico avoids its obligations on telecommunications; or if Canada refuses to modify or dismantle its agricultural marketing boards—then NAFTA could wither, and no country would escape the pain.

The United States has long understood that instability in Mexico could not be contained at the border. That is the national security rationale that underlies NAFTA. Migration pressures will not diminish in the short term, but a serious internal crisis could precipitate a massive outflow of refugees. A failure by Mexico to develop its natural gas and oil industry would not only hurt its development, it would not help California's. A union strike in Windsor, in Puebla, or in Detroit would quickly close down auto plants in the other cities. Unemployment would spread without regard to the border. Currency crises in Canada or Mexico or a recession in the United States would spread to the other parts of North America like the flu. *A problem in one part of North America can no longer be contained from affecting the other parts*, and that simple fact ought to concentrate our minds on the importance of transforming NAFTA into a Community.

Fear can motivate, but it can also paralyze. Hope and opportunity are better reasons to construct a model Community in North America. Already, North America's market is larger than that of the European Union, and industry is refashioning itself on a truly continental landscape. At the same time, trucks cannot cross the borders, and there is no organization to anticipate problems or plan for the continent's development.

The process of integration among disparate countries is not linear. Indeed, as trade and investment expands, it often triggers a reaction. Inefficient producers or worried unions seek protection, and politicians come to their defense. The other governments in the Free Trade Agreement then feel the same pressures from other businesses or unions, and the agreement risks unraveling. Similarly, as social integration through migration intensifies, subterranean anxieties are stoked, and nativist reactions, like "Proposition 187," are the result. This is the "Newtonian conundrum": every movement toward integration evokes an opposite, though not always equal, reaction. As the continent becomes more homogenous, it unleashes disintegrative pressures—from the Zapatistas in the south to the Bloc Quebecois in the north—that seek autonomy.

To sustain NAFTA, the three governments have to do more than just prevent defections. They need to deepen their collaboration and ensure that the benefits of freer trade are shared with those who pay the price of wider competition. A few voices can be heard calling for new North American institutions and policies to deepen NAFTA. In Canada, former Foreign Minister Lloyd Axworthy told a meeting at the North American Institute: "We all share the same concerns about wanting to deal with illicit drug trade, safeguard against terrorism and criminal activity. But we must develop a common, coordinated approach to these problems, not try to solve them by creating barriers for everybody that result in impossible lineups. We have not yet articulated what living together in a North American Community really means.''[17]

From the south, President Fox of Mexico has proposed a common market: ''We must be better friends, neighbors, and partners. By building up walls, by using arms, by dedicating billions of dollars like every [US] border state is doing to avoid migration—this is not the way to go. Instead of solving the problem, it has gotten worse.''[18] His vision is the boldest. He wants to double foreign investment in Mexico to $20 billion annually and seeks a fund—similar to the one based on EU regional policy and the one proposed in this book—that would permit Mexico to grow by 7 percent a year and narrow its income gap with the United States. He recognizes that is the only way to stem migration northward.

US President Bush has a unique opportunity to structure a relationship that will have a profound effect not just on Canada and Mexico but also on the United States. It will require resources, new organizations, difficult negotiations, and most of all, a new perspective on the region. A commentator for the *Toronto Star* posed the issue concisely: ''So the challenge is to create a North American Community whose vision goes far beyond trade and investment but without sacrificing cultural identity and core national institutions and values.''[19]

The North American Community has much to learn from the European Union—about both what it should adapt and what it should avoid. But the New World does not want to replicate the bureaucracy of the Old or the many instruments the Union uses to reduce disparities between rich and poor countries. What distinguishes the North American approach from the European is the respect for the market. This market orientation has permitted North American efficiencies and the economies of scale that have helped fuel the region's restructuring and development. And indeed, the European Union is trying to replicate the US market's policies on labor flexibility and uniform standards.[20]

What Canada, Mexico, and the United States need is a North American perspective and a few lean organizations that can help coordinate the three

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17. ''Notes for Remarks by the Minister of Foreign Affairs to a Meeting of the North American Institute,'' Santa Fe, NM, 21 August 1998.

18. Cited in Kevin Sullivan and Mary Jordan, ''Fox Seeks New Cooperative Era for North America,'' *Washington Post*, 14 August 2000, A1.

19. David Crane, ''NAFTA Lacks a Sense of Community,'' *Toronto Star*, 23 August 1998.

20. See, e.g., Frits Bolkestein and Anna Diamantopoulou, ''Workers without Frontiers; Governments Should Promote a Genuinely Free Market for Labour across Europe,'' *Financial Times*, 29 January 2001, 17. The authors are European commissioners for the internal market and for employment and social affairs, respectively. The article makes the case for facilitating the mobility of workers across countries and firms, much as the United States already does.

countries' multiple levels of governance and can accelerate integration without harming laggard regions. One option is to wait and let the market do its work, as the US South did for nearly 100 years. Or one can hasten the process by making targeted investments in infrastructure and education. What North America could learn most of all from the European Union is commitment. From its 1999 budget of $120 billion, the Union used about a third—$40 billion—for Structural and Cohesion Funds to reduce the disparities between rich and poor countries. Europe's gross product is smaller than North America's, and yet the Union spends about six times more on aid for its poor members as the United States spends on assisting its poor states. And the Union has programmed that annual aid to grow to about $70 billion by 2006.

If Canada and the United States contributed just 10 percent of what the European Union spends on aid, and if Mexico invested it wisely in infrastructure and education, Mexico could start to grow at a rate twice that of its northern neighbors. The psychology of North America would change quickly, and the problems of immigration, corruption, and drugs would look different. North America would have found the magic formula to lift developing countries to the industrial world, and that would be the 21st-century equivalent of the shot heard round the world.