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MEGA-TRADE AGREEMENTS: challenges to Brazil's foreign policy

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EDITORIAL

BRAZILIAN FOREIGN POLICY CHALLENGED

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The apparent insulation of Brazil from the recent emergence of mega-trade agreements and the adoption of measures in recent years to foster the industrial and technological deepening — as provided in Inovarauto[1] and the changes in the pre-salt oil exploration regime — have reignited the old debate on the advantages and disadvantages of protection. According to the conventional economic theory, trade liberalization tends to induce global society to a division of labor more conducive to the expansion of gains in productivity and income in the long term by contributing to the enhancement of the comparative advantages derived from the natural resource allocation among countries, despite possible sectoral losses in the short term. Alternative approaches, on the other hand, provide a number of arguments justifying intervention, such as infant industry protection — under the assumption that comparative advantages can be "created" through deliberate processes of industrialization —, income distribution, national security, food security, in addition to

1 A Brazilian federal program created in 2012 to promote the production chains of the auto industry.

several problems that can result from the specialization of a country in the production of commodities.

Even if recognizing the need for the regulation of international trade by national governments, for the reasons described above and others, such as dumping and unfair trade, economic theory also points out the risk that any allocative distortions, resulted from government intervention in the functioning of markets, generate excessive costs to society. The conventional discourse points out the risk that the "government failures" will eventually become greater than the "market failures" that we seek to correct. In his article, Thomas Kang presents the recent academic debate about the costs and the benefits of trade protection, taking into account that in economic policy the discussion often assumes dogmatic proportions and seems to have no end. For Kang (p.11), the central issue apparently is not whether or not to protect, but "how and how much to protect."

The World Trade Organization (WTO) was created in order to supervise and coordinate the adoption of international trade liberalization measures. Since 1995, the Organization has replaced the General Agreement on Tariffs and Trade (GATT), which emerged from a set of international institutions created in post-war times, from the Bretton Woods Agreements. The GATT intended to stimulate free trade multilaterally, arbitrating differences among countries in their liberalization processes, in order to avoid repeating the protectionist escalation observed in the interwar period. Such task, now performed by the WTO, has been complex, as it involves a number of disparities between countries, which have become even more evident after the subprime crisis in the U.S. Not surprisingly, therefore, the rounds of multilateral negotiations led by the WTO have advanced with difficulties. The Doha Round, launched in 2001 and without prospects for a conclusion, highlights this phenomenon.

In parallel with the negotiations through the WTO, regional trade agreements known as Preferential Trade Agreements (PTAs) have gained increasing importance. From this process, two mega trade agreements have recently emerged: the Trans-Pacific Partnership (TPP), involving 12 countries in Asia and the Americas, and the Transatlantic Trade and Investment Partnership (TTIP), involving the U.S. and the European Union. Such agreements transcend the tariff reduction process, covering broader issues, such as non-tariff barriers, the creation of supranational mechanisms for dispute settlement, intellectual property rights, labor standards, currency manipulation, government procurement, the environment, etc. In other words, those mega agreements establish a new regulatory framework for international trade. In his article, Robson Valdez addresses the PTAs in a historical perspective, highlighting the wave of regionalism that began with the European Community and the North

American Free Trade Agreement (NAFTA) and reached its climax, in recent years, with the TTIP and the TPP.

For the good or the bad, the PTAs, and especially the last two mega deals, have put in check the international integration strategy of the Brazilian economy. The Brazilian foreign policy has always favored the multilateral negotiations in the WTO. So far, this strategy has been justified by the understanding that negotiating in bloc allows greater bargaining power for developing countries, which are relatively closed and have large and coveted domestic markets, such as Brazil and India. However, multilateral negotiations have been exhausted by the developed countries, in favor of the mega agreements. In her article, Beky Moron de Macadar explores the challenges that these mega agreements represent for the Brazilian foreign policy. In practice, the country is likely to face higher tariffs than its competitors in the markets of the U.S. and the European Union, at the same time that it may witness the undermining of its trade preferences with South and Central America. On the other hand, the possible accession of Brazil as a member would take place with "the scarce space to negotiate [its] interests" (p.29). For Macadar, despite the challenges, which are not few, the mega agreements are an opportunity for Brazil to review its strategy and to adopt measures that may contribute to increase productivity.

Still on the challenges that mega agreements inflict on Brazil, in his text, Tomás Amaral Torezani seeks to evaluate their potential effects on the sectors of the Brazilian economy in terms of both trade diversion and the possibility of the


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erosion of the preferential access obtained in previous negotiations. For Torezani, commodity trade diversion may occur from Brazil to Asia in favor of competitors such as the U.S., Canada, Australia and New Zealand. Also, there can be diversions in the Brazilian markets of goods manufactured in the U.S. and in South America. In terms of economic growth, the effects may not be significant, given that Brazil is still a relatively closed country. However, such moves can reinforce the Brazilian deindustrialization process, affecting, in particular, the automotive industry. For the author, the emergence of mega agreements and the nonparticipation of Brazil tend to reinforce both the fact that Brazil is a commodity exporter and its ties with China, both taken as outsiders.

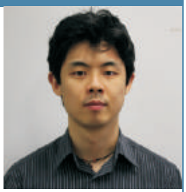
The current issue's interviewee is Prof. Jorge Arbache, from the University of Brasilia (UnB). The interview tackles not only the challenges that mega agreements represent for Brazil, but also some broader issues behind those agreements, especially the increasing integration of services markets, which has been his latest research area.

Enjoy your reading! P

ARTICLE

Trade protection: an endless debate

Thomas H. Kang *



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When the Presidential Decree No. 7567 of September 15th, 2011 imposed discriminating tariffs on imported cars, except for cars manufactured in Mexico and countries of the Southern Common Market (Mercosur), the old debate on protectionism versus free trade resurfaced in Brazil. The target of the decree at the time was mainly the cars produced in Asian countries, in a context of rising nationalist industrial policies. Thereafter, the mounting fiscal deterioration and political instability in Brazil made the controversy over trade protection lose prominence. However, the debate is recurrent in Brazil and the arguments used are often based on fragile empirical evidence, if not upon dogmatic assertions. In order to clarify the issues at stake, it is once again worth asking: what are the benefits and costs of a protectionist trade policy?

The mainstream theoretical models point out to the negative effects of protection for the country as a whole, as tariffs make consumers face higher prices. On the other hand, besides saving some domestic firms and jobs, government revenues increase according to the same models. In the end, the losses are greater than the gains. There is evidence of such losses in the literature: Douglas Irwin (2005) estimated the losses caused by the trade embargo levied by the United States against British products between 1807 and 1809[1]. Another study undertaken by Bernhofen and Brown (2005) stated that the rapid and unilateral trade opening in Imperial Japan after

* I thank Thales Zamberlan Pereira for the comments — especially for calling my attention to footnote 14 and its reference —, Ana Clara Lima, Tomás Torezani and other members of the Editorial Board. The usual disclaimers apply.

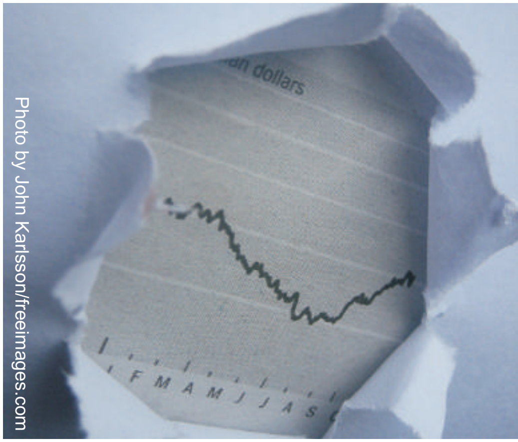
1 IRWIN, D. The welfare costs of autarky: evidence from the Jeffersonian embargo, 1807-1809. **Review of International Economics**, v. 30, p. 345-358, 2005.

the arrival of the U.S. navy generated a gain of 5.4% to 9.1% in the Gross Domestic Product (GDP).[2] The economic historian Jeffrey Williamson (2011) agrees with the general rule that there are static gains from trade in the short run.[3] The idea that comparative advantages in international trade generate more gains than losses, as traditional models conclude *à la* David Ricardo or Heckscher-Ohlin, is not in check for the author. The point of the dispute is elsewhere.

Williamson (2011) then underlines that it is a long-run problem: what are the effects of free trade or protection on growth? The issue of growth is distinct from the traditional welfare analysis, which compares a state of affairs before and after trade liberalization. Bearing that question in mind, Williamson presents the responses found in the most recent literature. The author raises three possible effects of free trade and productive specialization that could be detrimental to countries seeking the path of long-run growth: (a) the "Dutch disease", (b) commodity price volatility, and (c) the curse of natural resources. Perhaps these three effects could justify a protectionist policy that changes relative prices in order to bring about changes in the productive structure. But even if the importance of these three effects were recognized, protection would only make sense if "government failures" were smaller than "market failures", such as spillovers or capital market imperfections. The possibility of "government failures" is probably the main reason underlying the research agenda on the political economy of protection.

Besides the theoretical question, there is an empirical problem: it is not clear in which conditions protection could work. In economics, there are still a number of empirical difficulties in some specific areas, which makes room for disputes. Some claim that the infant industry protection is an important tool for industrialization: the tradition is long, dating back to the founding father, Alexander Hamilton, and the creator of the Zollverein, Friedrich List. These authors inspired the Economic Commission for Latin America (ECLA) in the mid-20th century as well as contemporary authors, such as Ha-Joon Chang. Others, including Douglas Irwin (2001)[4] and John Nye (2007)[5], tried to show how certain countries, among which are the United States and England, have grown despite protectionist policies in the 19th century. Regarding the 20th century, the comparison between Latin America and East Asia is well--known, since the two regions adopted

2 BERNHOFEN, D.; BROWN, J. An empirical assessment of the comparative advantage gains from trade: evidence from Japan. **American Economic Review**, v. 95, p. 208-225, 2005.
3 WILLIAMSON, J. **Trade and poverty:** when the third world fell behind. Cambridge, MA: MIT, 2011.
4 IRWIN, D. Tariffs and growth in late nineteenth-century America. **The World Economy**, v. 24, n. 1, p. 15-30, 2001.
5 NYE, J. **War, wine, and taxes:** the political economy of Anglo-French trade, 1689-1900. Princeton: Princeton University, 2007.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active trade policies. The first group of countries seemingly performed below expectations, although some countries, such as Brazil and Mexico, were able to reach an advanced level of industrialization. On the other hand, East Asian countries were more successful in their interventions.[6] One should not forget that, despite having features in common, the East Asian strategy of export promotion, combined with high-level educational policies, was distinct from the Latin American strategy.

Part of the answer to the ambivalent evidence might be found in politics, not in economics. As mentioned earlier, if government failures are greater than market failures, either by clumsiness, misinformation or capture, at least some of the disappointing results can be explained. This makes room for the research program in political economy. A review written by Renato Colistete and Jarbas Menezes (2004) categorizes this literature into two lines of research: “historical” political economy and “positive” political economy.[7] The first school is represented by the successors of Alexander Gerschenkron, a well--known Harvard economic historian in the mid-20th century. This line of research highlights the fact that the political fragility of governments increases its incentives to protect certain groups, while economic crises may give rise to increased demand for protection.[8] On the other hand, the "positive" school develops formal models whose origins date back to the electoral competition model of Downs (1957). In this line of research, the work of Grossman and Helpman (1994) on the political economy of protection is perhaps the most influential. The authors present a model in which lobbies make contributions on account of trade policies, a kind of "protection for sale".

The dichotomous debate between protecting or liberalizing tends to leave the "gray" area aside: maybe the question is about how and how much to protect. Santiago Macario (1964)[9], an economist from ECLA, had already

6 FEENSTRA, R.; TAYLOR, A. **International economics**. 3 ed. New York: Worth, 2014.
7 COLISTETE, R.; MENEZES, J. D. Modelos de proteção comercial - uma resenha. **Revista de Economia Política**, v. 24, n. 2, 2004.
8 SIMONS, B. **Who adjusts?** Domestic sources of foreign economic policy during the interwar years. Princeton: Princeton University, 1994.
9 MACARIO, S. Protectionism and industrialization in Latin America. **Economic Bulletin for Latin America**, v. 9, p. 75-83, 1964.

"The dichotomous debate between protecting or liberalizing tends to leave the 'gray' area aside: maybe the question is about how and how much to protect."

drawn attention to the excesses of indiscriminate protectionism in the region long before the "market critics" — such as Anne Krueger[10], Bela Balassa[11] and Jadgish Bhagwati[12] —, who criticized the trade policies carried out by the developing countries from the 70s onwards. According to Macario (1964), the average effective tariff for manufacturing sectors in Latin America was 165%, an obvious excess even for the standards of the time. Colistete (2010) highlights this point: it is possible that the indiscriminate protection has generated almost autarchic economies without incentives to achieve high productivity levels, with some exceptions in some sectors. However, the author acknowledges that the crises of the 70s hinder better assessments of the policies of that period. Anyway, in this "gray" area, explanations based on political economy issues may be even more important.[13]

The case of the Brazilian automotive industry is an excellent example of trade policy dilemmas. The industry is not competitive yet and has been supported by protectionist policies for more than half a century, but its importance in the production chain and labor absorption is far from negligible. The auto industry has not been considered "infant" for a long time, which compromises the defense of its protection in terms of long-run growth. On the other hand, the immediate social consequences of a sudden end of protection could be disastrous in terms of unemployment in the sector and its ramifications — the well-known Stolper-Samuelson theorem points out the risks of trade liberalization in terms of losses for certain segments of the economy, although liberalization continues generating net gains as a whole under the assumption of full employment. The question is how to "disarm the bomb without destroying the entire building", particularly taking into account the significant political power of the manufacturers and the labor unions of that category and the need for thinking of compensatory policies. In this regard, there are pessimistic studies, such as that of Autor (2014), which estimate the effects of labor market adjustments triggered by the U.S. trade integration in recent decades.[14] It is hard to believe that there

10 KRUEGER, A. **Liberalization attempts and consequences**. Cambridge: Cambridge University, 1978.
11 BALASSA, B. **Development strategies in semi-industrial economies**. Baltimore: Johns Hopkins University, 1982.
12 BHAGWATI, J. **Protectionism**. Cambridge: Cambridge University, 1988.
13 COLISTETE, R. **Revisiting import-substitution industrialization in post-war Brazil**. Munich: University Library of Munich, 2010. (MPRA Paper, n. 24665).
14 AUTOR, D. et al. Trade adjustment: worker level evidence. **Quarterly Journal of Economics**, v. 129, n. 4, p. 1799-1860, 2014.

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would be no similar problems in Brazil, and the solutions are not that simple.

Despite the advances in the research, more definitive solutions to the debate seem distant. Practical problems in testing the effects of trade policies are not the only obstacles. Measuring the effects of certain trade policies can help, but does not solve the disputes. Disagreements in the field do not comprise only utilitarian considerations, in which only economic costs and benefits are taken into account. Fundamental questions about the limits of the government or the private actors in the economy and in the society are at the heart of the discussion. This kind of debate transcends traditional cost--benefit assessments, sometimes reaching almost a dogmatic character. Therefore, the advances made in the research on protectionism can support debates, but hardly solve the disputes — actually grounded on political or moral perspectives — between the most ardent supporters and the detractors of each view. In fact, there is no way out of the moral discussion in Economics, but it can become a problem when the prevailing attitude is based on "*fiat justitia, pereat mundus.*"[15]

15 Let justice be done, even if the world perishes (Translation mine).

Brazil and the mega-trade agreements: principles, history and challenges

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Non-discrimination is the basic principle of international trade. Under the World Trade Organization (WTO), non-discrimination gives rise to two important pillars, national treatment and the most-favored-nation clause. This clause requires that any commercial advantage offered to any country, member or not of the WTO, be also offered to other nations of that organization. The national treatment principle, on the other hand, ensures that imported products must receive the same treatment given to domestic products. Based on these principles, which seek to prevent discrimination on the origin and between products, the WTO aims to promote trade liberalization globally. Moreover, the WTO offers its members a number of trade defense measures against dumping (anti-dumping measures), against subsidy (countervailing measures) and against import surges (safeguards).

However, the international trade complexities and disparities that hinder the process of trade liberalization led the 1979 Tokyo Round of the Organization to establish the

Photo by World Trade Organization/Flickr enabling clause. This clause aims to create a legal framework, parallel to the multilateral negotiations, to promote the gradual advance of free trade through trade preference systems: the Generalized System of Preferences (GSP) and the Global System of Trade Preferences (GSTP).

Both the GSP and the GSTP are ruled by the United Nations Conference on Trade and Development (UNCTAD). While the GSP deals with unilateral tariff concessions from developed to developing countries without the need for extending them to other WTO member states, the GSTP regulates tariff concessions between developing nations. Thus, both the GSP and the GSTP have consolidated themselves as exceptions to the basic principle of non--discrimination.

Regarding the recent historical dimension of the trade agreements, it is possible to identify three great waves of trade regionalism.[1] The first one was marked by the beginning of the process of unification of Europe through the creation of the European Coal and Steel Community (ECSC) in 1951, followed by the formation of the European Economic Community (EEC) in 1957. These experiments influenced, for example, the creation of the Latin American Free Trade Association (LAFTA) in 1960.

During the second wave, more countries joined the EEC, which, in 1993, with the signing of the Maastricht Treaty, was renamed the European Community (EC). The EC progress towards the countries of Eastern Europe (satellites of the former Soviet Union) led the United States to abandon its traditional appreciation for multilateral negotiations under the General Agreement on Tariffs and Trade (GATT), of the WTO, and to sign a bilateral agreement with Canada (1988), which was then extended to Mexico in 1990, thus consummating the creation of the North American Free Trade Agreement (NAFTA). In the same period, the Southern Common Market (Mercosur) and the Andean Community were created in South America, while in Africa and Asia many other similar agreements were signed.

Finally, the third stage has been characterized by the influence of the

“However, the international trade complexities and disparities that hinder the process of trade liberalization led the 1979 Tokyo Round of the Organization to establish the enabling clause.”

1 ORGANIZACIÓN MUNDIAL DEL COMERCIO. La OMC y los acuerdos comerciales preferenciales: de la coexistencia a la coherencia. **Informe sobre el Comercio Mundial 2011**, Ginebra, 2011. Retrieved from <https://www.wto.org/spanish/res_s/booksp_s/anrep_s/world_trade_report11_s.pdf> on Mar. 9, 2016.

Photo by World Trade Organization/Flickr

United States and the European Union. However, the peculiarity of this present moment lies precisely in the participation of the Asian countries, traditional supporters of the multilateral trade negotiations under the WTO. In addition to the 1997 financial crisis and the failure of the 1999 WTO negotiations in Seattle (USA), the proliferation of regional agreements in Asia was also due to the intense productive integration process that has taken place in the region in recent years.

The multilateral WTO agreements are characterized by their amplitude, by their binding effects and for incorporating complex issues, such as the service sector, foreign investment and intellectual property. This scope is a result of the global productive system rearrangement in recent decades, which demands an increasingly more open and less discriminatory trade.

With regard to market access, the Preferential Trade Agreements (PTAs) aim at the reduction and/or elimination of import tariffs and the elimination of nontariff barriers. As for the regulation of international trade, it deals with the incorporation of international trade rules under the WTO (WTO-in), the deepening of these very same rules (WTO-plus) and the incorporation of rules not yet covered by the WTO (WTO--extra). This way, it is possible to perceive the regulatory dimension of the PTAs as a necessary condition or even as a deliberate strategy for the countries' integration into the global production chain.[2]

In this context, the WTO's **World Trade Report 2011** points out that the Regional Trade Agreements involving two or more countries from different geographical regions have become known as Preferential Trade Agreements. This is due to the fact that the unilateral preference systems (GSP

2 THORTENSEN, V.; FERRAZ, L. O isolamento do Brasil em relação aos acordos e mega-acordos comerciais. **Boletim de Economia e Política Internacional**, Brasília, n. 16, p. 5-17, jan./abr. 2014. Retrieved from <http://repositorio.ipea.gov.br/bitstream/11058/3762/1/BEPI_n16_isolamento.pdf> on Mar. 10, 2016.

and GSTP) and other nonreciprocal agreements fall within the concept of Preferential Trade Agreements. In February 2016, the WTO registered 284 trade agreements on goods and services involving countries from different regions of the world.

Finally, it must be stressed that the PTAs are agreements that also occur in the legal framework of the WTO, thus counteracting the argument about a possible weakening of the Organization. Actually, the PTAs stand out as a world trade liberalization strategy that takes place along with the multilateral negotiations of the Doha Round. Thus, the WTO now offers two negotiation channels for international trade liberalization: a multilateral one, which grants greater bargaining power to developing countries (Doha Round); and a plurilateral one, which grants greater bargaining power to developed countries.

The current international trade scenario poses, then, a serious challenge to Brazil, to the extent that multilateral negotiations within the WTO, the traditional strategy for the Brazilian diplomacy, have been abandoned by some of the world's major commercial powers: the United States, the European Union and Japan. In 2013, President Barack Obama argued for the creation of the Transatlantic Trade and Investment Partnership (TTIP), involving the United States and the European Union. Last year, 2015, the United States, Canada, Mexico, Chile, Peru, Japan, Vietnam, Brunei, Singapore, Malaysia, Australia and New Zealand signed the Trans--Pacific Partnership (TPP).

"The current international trade scenario poses, then, a serious challenge to Brazil, to the extent that multilateral negotiations within the WTO, the traditional strategy for the Brazilian diplomacy, have been abandoned by some of the world's major commercial powers."

It is important to remember that even the negotiation over the TTIP between actors of the same relevance in terms of economic and social development, such as the United States and the European Union, has been quite complex. Regarding the TPP, the conditions are asymmetric. There are two major trading powers (NAFTA and Japan) negotiating a mega-trade agreement with countries whose domestic markets are reduced, with few alternatives from the point of view of their economic growth policies, except the production for foreign markets — a situation that is diametrically opposed to that of Brazil, which has a vast and coveted domestic market.

Photo by World Trade Organization/Flickr

With regard to Brazil, its possible adherence to mega-trade agreements brings to the debate the discussion of the flexibility of its labor laws, the impact of international competition on the various industrial segments in Brazil and the loss of market for the Brazilian manufactured goods in Latin America, especially in South America. In addition, the exchange rate issue is a central — though little discussed — variable in this process. What would be the impact of an agreement of this magnitude on a context of overvaluation of the real on the national economy as a whole?

In this sense, the main question to be answered is whether the country is able to engage itself into international trade via adherence to mega-trade agreements. Further questions regard the national entrepreneurs' cohesion around a national policy regarding the commercial insertion of Brazil, which traditionally includes, for example, federal subsidies, openly countered in international trade.

It is clear, therefore, that Brazil's adherence to a wide range of trade agreements involves, among other arguments, the reevaluation of its domestic and external priorities. Domestically, the impact of these agreements on the country's external accounts, on the political friction among different business groups with conflicting interests in the implementation of the country's foreign policy and on the interests of workers and consumers is noteworthy. Internationally, Brazil seeks a

Countries with which Brazil maintains preferential trade agreements

COUNTRIES	INSTRUMENTS	SITUATION
Chile, Bolivia, Guiana, Suriname (rice), Mexico (including the automotive sector), Peru, Ecuador, Colombia, Venezuela and Cuba	Mercosur Economic Complementation Agreements	In force
India, Israel and Southern Africa Customs Union (SACU) — South Africa, Namibia, Botswana, Lesotho and Swaziland	Mercosur Preferential Trade Agreements	In force
Palestine and Egypt	Mercosur Preferential Trade Agreements	In force
European Union	Mercosur Preferential Trade Agreements	Under negotiation

SOURCE: BRAZIL. Ministério do Desenvolvimento, Indústria e Comércio Exterior (MDIC). **Acordos dos quais o Brasil é parte.** Retrieved from <http://mdic.gov.br//sitio/interna/interna.php?area=5&menu=405> on Mar. 30, 2016.

compromise with Argentina in order to reach a trade agreement with the European Union without jeopardizing its goals related to Mercosur and South America, a strategic area of influence within its foreign affairs.

PANORAMA INTERVIEWS
Jorge Arbache

WORLD TRADE and the commoditization of Brazilian exports

By Tomás Torezani

Jorge Arbache, a Professor of Economics at the University of Brasília, is the former chief economist of the Brazilian Ministry of Planning, Budget and Management. His previous positions also include senior economic advisor to the President of the National Bank for Economic and Social Development (BNDES) and senior economist at the World Bank in Washington, D.C. Arbache holds a Ph.D. in Economics and a B.A. in Economics and Law. His main current research interests are sectorial competitiveness, investment, productivity, technology and trade.

In an interview to **Panorama**, Jorge Arbache evaluates the challenges for foreign trade and points out that the costs are no longer what determines the competitiveness of nations and enterprises. He comments on the obstacles faced by developing countries for their integration into the international trade and argues that Brazil's focus on the production and export of commodities traps the country in a backward situation. Arbache explains the weakening of multilateral agreements, positions himself on the challenges that mega-deals represent for Brazil and evaluates the productivity of the Brazilian service sector.

Image: Freepik

Panorama: In recent decades, several processes have decisively changed the configuration of the international economic order, especially the fragmentation of production in global value chains, the role of multinational companies and the growing importance of China. Do these movements bring new challenges to foreign trade in the 21st century?

Yes, many new major challenges, particularly for developing and emerging countries that are still looking for a "place in the sun" in the twenty-first century. Costs are losing relevance in determining the competitiveness of nations and enterprises. Robots, the "Internet of things", artificial intelligence, 3D printers, manufacturing 4.0, new energy, nanotechnology, etc. reduce part of the conventional production costs of the final value of products. Yes, they still are and will be very important for a long time, but what increasingly determines competitiveness is the ability to produce value added to things. "Commoditized" goods and services will be less and less able to promote the full and inclusive economic development.

Panorama: With the weakening of the multilateral agenda of the World Trade Organization (WTO), preferential trade agreements have been signed. Can recent mega deals that begin to take shape be considered a new stage of globalization?

The weakening of multilateral agreements is due to the change in orientation of the United

"Costs still are and will be very important for a long time, but what increasingly determines competitiveness is the ability to produce value added to things."

States and other countries in favor of the plurilateral agenda, letting the multilateral agenda die of inaction. Plurilateral agreements, such as the TPP and the TISA, are already tacitly replacing multilateral agreements and, later, will expressly replace them. The problem is that the plurilateral agreements are neither concerned with the development agenda nor consider the huge inequality between countries in terms of their technological *status quo*, innovation, *per capita* capital inventory, access to credit capacity, intellectual property, whether or not they host global corporations, etc. Virtually the whole digital economy is in the hands of a few giant firms, and almost all of them are in the U.S. and a few are in Europe. It is an agenda that basically aims to extend the benefits of those who already have an advantage. Maybe it's the globalization in its most questionable step from the point of view of access to productivity, growth and prosperity convergence opportunities for all.

"The weakening of multilateral agreements is due to the change in orientation of the United States and other countries in favor of the plurilateral agenda, letting the multilateral agenda die of inaction."

Panorama: What are the major obstacles that emerging countries are facing in order to assertively integrate themselves into the international trade? And, in the case of Brazil, how does the country position itself in the trade negotiations?

The major obstacles are associated with the inability, in the foreseeable future, to reduce the knowledge and technology gaps, which keep expanding. Yes, in part, the gap increases due to the ultra-mercantilist posture of the advanced countries. But in large part it is due to ourselves, because we insist on confronting the relevance of knowledge agendas in their various dimensions: basic education, science and technology, innovation, professional education, production management, cooperation between universities and companies. As for the position of Brazil in the negotiations, we have focused on agendas that favor the production and export of commodities, which can be good in the very short term, but which worsens even further our situation of backwardness and increases our detachment from the countries that develop and produce high value added goods and services.

Panorama: The attention given to the role played by services produced and marketed globally has been increasing lately. What is your opinion about the real importance of the sector for international trade and the growth prospects in the current world economic order?

One of the characteristics of globalization is the consolidation of markets, namely, the reducing number of players in the segments that matter the most. This is already happening before our eyes in the food, automobiles, processors, glass, aircraft, supermarkets and insurance markets, and so on. In some markets, it is now more difficult for a company that operates only nationally to compete with companies that operate globally, let alone companies at state and municipal levels.

Panorama: The services' share of value added of global exports is increasing. However, the weight of the sector in Brazilian exports and its productivity in the economy as a whole are still low. How much can services represent for the country's trade, investment and technology flows?

Services now account for 54% of global trade, when counted in Value Added. It is estimated to be 75% by 2025. Therefore, exported final services, such as insurance policies and, more importantly, services "embedded" in the production of industrial,

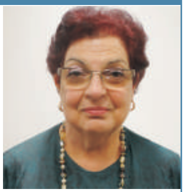
"Services now account for 54% of global trade, when counted in Value Added. It is estimated to be 75% by 2025."

Image: Freepik

agricultural and mineral goods are simply crucial to the competitiveness of enterprises and the prosperity of nations. In Brazil, services are the main component of the gross value of industrial production. Their share is high among exported products. The more elaborate the product, the larger that share can be, which is not our case, because we export many commodities and commoditized industrial goods, such as cellulose and sugar. Finally, as the productivity of our service sector is very low and has stagnated, services "intoxicate" the other sectors, undermining their competitiveness. This helps to explain inflation, in general, and our low international competitiveness.

Preferential Trade Agreements: Brazil at a crossroads

Beky M. de Macadar



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In general, emerging countries such as Brazil, China and India, which trade with all regions of the world, prefer to maintain their international trade negotiations within the framework of the World Trade Organization (WTO), in which multilateralism ensures a more equitable treatment for its member countries when defending their interests. Thus, in the case of Brazil, the few Preferential Trade Agreements (PTAs) signed by the country have a very limited scope and focus on negotiations with neighboring countries or with other countries of the South. Brazil is noteworthy for its closed economy, even when compared with other large nations, because it maintains low levels of trade with the rest of the world, imposes trade restrictions, creates nontariff barriers, especially certifications, and also for the level of its tariffs, which still are relatively high and subordinated to powerful economic interests.

Although the country stands as the 7th world economy, its trade with the rest of the world represented, in 2014, only 1.2% of the global exports (25th place) and 1.3% of the imports (22nd place).[1] In the same year, the ratio between the total merchandise trade and the Gross Domestic Product (GDP) reached 19.4%, while in countries such as China, Russia, South

1 WORLD TRADE ORGANIZATION. International Trade Statistics 2015. [2016]. Retrieved from <https://www.wto.org/english/res_e/statis_e/its2015_e/its15_world_trade_dev_e.htm> on Mar. 03, 2016.

Africa, Chile, Mexico, South Korea and Turkey this ratio was above 50%. The latest data from the Organisation for Economic Cooperation and Development (OECD), in joint work with the WTO[2], indicate that, in 2011, the foreign content in the Brazilian gross exports reached 10.8%, while the average for 61 countries studied, including all OECD members, was 28.5%.

The Doha Development Round of the WTO negotiations, which started in 2001, has been the main recent Brazilian bet regarding its integration into the international trade, but progress has been unsatisfactory to date. For years, the European Union and the United States strived to impose, in the WTO, their interests over those of the emerging countries, but their attempts were unsuccessful. For this reason, they have chosen to create PTAs that reflect their interests and impose their own rules, thus weakening the WTO and everything it represents in terms of multilateralism. Consequently, as the developed countries have failed to co-opt the developing countries into adopting the trade rules which would lead to a deeper integration in the WTO, we can see, in recent years, an intensified activism concerning the PTAs.

"The Doha Development Round of the WTO negotiations, which started in 2001, has been the main recent Brazilian bet regarding its integration into the international trade, but progress has been unsatisfactory to date."

However, what can really affect the functioning of the multilateral trading system radically are the so-called mega-trade agreements. Two negotiations call attention: (a) the Trans-Pacific Partnership (TPP)[3], which gathers 12 countries of Asia and the Americas (the United States, Japan, Australia, Brunei, Canada, Chile, Malaysia, Mexico, New Zealand, Peru, Singapore, Vietnam); and (b) the launching of the Transatlantic Trade and Investment Partnership (TTIP) between the United States and the European Union. Thus, and after Japan's admission to the TPP negotiations, all developed countries are included in some mega-agreement that will dictate the rules of international trade to be followed by a large number of countries.

The agreements between the developed countries can also be seen as a way to deal with the rise of large economies of average or low income,

2 ORGANISATION FOR ECONOMIC CO-OPERATION AND DEVELOPMENT. Measuring trade in value added: an OECD-WTO joint initiative. 2015. Retrieved from <http://www.oecd.org/sti/ind/measuringtradeinvalue-addedanoecd-wtojointinitiative.htm> on Mar 03, 2016.

3 Agreement signed in February 2016, but not yet ratified by the countries and, therefore, not yet in force.

such as China and India, diverting the trade and investments directed to them to the countries which participate in such agreements. These negotiations allow not only to deal with the issues under discussion in the Doha Round, but also to advance on regulatory issues that affect the functioning of the global value chains (GVC), such as labor relations or environmental certifications. The consolidation of these agreements will limit Brazil's ability to benefit from the opportunities that the fragmentation of the production process can offer and may further restrict its participation in global production chains. This is because the mega preferential trade agreements which emerged in the 21st century differ from the previous PTAs in many ways. Previously, the purpose was to obtain tariff reductions; currently, the PTAs have more ambitious goals. The countries that are part of these agreements represent a significant portion of the international trade and intend to establish a new system of rules that are both deeper than those in force in the WTO, such as, for example, in services and in intellectual property, and more comprehensive, involving themes that have not yet been incorporated, such as the environment, climate change, labor, investment and competition.

The expectation of the developed countries and the transnational corporations attached to them is that through the deep integration of this new generation of PTAs, including the mega

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agreements, many trade barriers between the member countries will be eliminated, leading to regulatory harmonization or, at least, to the acceptance of regulatory equivalence, thereby expanding the freedom for the functioning of the global production chains. This whole new configuration may adversely affect the non-member countries, not only in trade participation, but also in terms of growth prospects.

On the other hand, the multilateral trading system is under tension given the amount of rules that affect not only the trade in goods and services but also the production methods, the labor standards and the impact on the environment and climate. As a result, the developing countries face a multiplication of new barriers to their products. Thus, the diversity of regulations, standards and certifications can turn into barriers to trade which are even more significant than the old tariff barriers.

Photo by World Trade Organization/Flickr

The WTO is facing major challenges due to the proliferation of PTAs and the new paradigm of production of goods and services of global value chains. Both issues bring concerns about the multilateral trading system, its possible exhaustion and the necessity for reforms. On the other hand, developing countries, including Brazil, which do not often participate in GVCs, but wish to do so, should review their trade policy and accept changes in the WTO.

Evidently, the geographical location of the countries and the profile of their industrial structure may restrict some of them from joining this pattern, as the GVCs are concentrated in Asia, Europe and North America. But Brazil has sufficient conditions to take advantage of the new pattern of international trade, such as: a strong technological base, as compared with other countries, and areas of excellence; a very significant stock of foreign capital and a fairly diversified sectoral distribution of foreign investment; cultural proximity to Europe and the United States; the possibility for developing its own value chains at the regional level; successful experiences in setting up GVCs in aeronautics and in the food industry.[4]

Not participating in the current outbreak of PTAs has several consequences, such as for example the fact that Brazilian exporters will face higher tariffs than their competitors in the markets of the U.S. and the E.U., since several Latin American economies — Mexico, Peru, Chile, Central American countries, etc. — have already signed PTAs with that country and that region. A predictable consequence is the erosion of the preferences obtained by Brazil from

4 MARKWALD, R. Inserção do país na economia mundial: qual a singularidade do Brasil? **Revista Brasileira de Comércio Exterior**, Rio de Janeiro, n. 118, jan./mar. 2014. Retrieved from <http://www.funcex.org.br/publicacoes/rbce/material/rbce/118_RM.pdf> on Mar. 23, 2015.

these and other nations in South America and Central America, as they are increasingly active, signing PTAs with developed countries and emerging economies. Moreover, the lack of preferential access to markets of the North hinders the competition of the Brazilian goods with exports from countries such as China and India, which, despite lacking preferential agreements signed in these markets, have advantages of scale and lower labor costs. But even if Brazil wished to change the current trade policy, an obstacle that the country faces to advance individually towards new trade agreements is the commitment made by the member states of Mercosur in 2000 to jointly negotiate trade agreements with third nations or blocs.

As already noted by Thorstensen[5], due to the changes in the framework of international trade, there are three options left for the countries not included in the new generation of PTAs: (a) following the negotiations passively and accepting what is imposed to them, since they did not make the rules; (b) accepting the new reality and deciding to participate as members of these new blocs while they are not fully consolidated, though recognizing the scarce space to negotiate their interests; (c) continuing to keep a limited number of deals and trying to boost the WTO as the main regulatory institution of international trade.


Photo by World Trade Organization/Flickr

For all these reasons, Brazil is at a crossroads, because if, on the one hand, it fears to open its market to foreign competitors, on the other hand, joining relevant PTAs may have the advantage of fostering an increase in the foreign content of the exported products and enhancing the country's competitiveness, facilitating its integration into the GVCs. The Brazilian participation in international trade is not on a par with the importance of its economy, and the erosion of its tariff preferences among trade partners in its region, which are the main purchasers of

5 THORSTENSEN, V. WTO – Challenges for the next 20. **Mural Internacional**, v. 6, n. 1, jan./jun. 2015.

Brazil's manufactured goods, will bring, as a result, a deeper reduction in exports in this category, strengthening its primary exporter profile. The current strategy of maintaining the preference for multilateral negotiations, and the restraints of Mercosur, limits Brazil's activities in the scenario of international trade, so its costs and benefits should be examined more closely.

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ARTICLE

The possible outcomes of the mega-trade deals in Brazil's exports

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Whatever the extension or the depth of a debate on trade deals, even in the 21st century, the duality between free trade and protectionism gains ground. While the advocates of the first one identify potential gains and opportunities for those involved in an agreement of this scope, from the perspective of comparative advantages based on traditional models of international trade, others argue that trade liberalization changes the composition of employment and its level, as well as other variables, such as wages, income and the trade flows themselves. The advances of the last global trade and investment deals have invigorated this debate. However, what is at stake in these deals surpasses this false dichotomy when we start to understand what is really being defined in these negotiations.

The Trans-Pacific Partnership (TPP) and the Transatlantic Trade and Investment Partnership (TTIP) are mega-regional trade agreements formulated under the leadership of the United States, to the detriment of the multilateral negotiations under the World Trade Organization (WTO). The TPP consists of a partnership between 12 countries of the Pacific coast[1], which

1 Besides the U.S., the other TPP members are Canada, Mexico, Peru, Chile, Japan, Malaysia, Vietnam, Singapore, Brunei, Australia and New Zealand..

together account for 25% of world exports, about 40% of the global Gross Domestic Product (GDP) and over 800 million people. It is an American prerogative to increase its influence in Asia at the expense of China's advance on the continent. This is reinforced by the fact that the United States already has trade agreements (low tariff barriers) with some of the countries involved, although these barriers are still high between the other members of the TPP. The TTIP, on the other hand, is a more thorough proposition of a trade and investments agreement between the United States and the European Union, bringing together 60% of the world's GDP, one third of the world's trade in goods and more than 40% of that of services.

In common, these two mega deals go beyond the barrier of trade in goods and services, emphasizing issues such as the reduction of nontariff barriers, dispute resolution mechanisms[2], intellectual property rights, labor standards, currency manipulation, government procurement, the environment, etc., that is, these mega-deals inaugurate a new regulatory framework for international trade within the deepening of the current logic of production fragmentation and the global value chains.

"From the establishment of these partnerships arises a natural discussion about their potential effects (direct and indirect, positive and negative) on the countries (independently of their being or not being members of the partnerships)."

From the establishment of these partnerships arises a natural discussion about their potential effects (direct and indirect, positive and negative) on the countries (independently of their being or not being members of the partnerships). However, a more accurate and thorough investigation has been made impossible due to the lack of access to the terms of the agreements, a behavior that has been widely criticized. In spite of the legitimate concerns caused by the lack of knowledge of the full texts of the agreements, it is clear that there will be winners and losers and benefits and drawbacks unevenly granted to the world economies. At the same time, challenges will be presented and opportunities will be created for every country.

2 In this respect, in **The secret corporate takeover**, published in Project Syndicate, on May 13th, 2015, Stiglitz draws attention to the fact that mega deals consist of managed trade agreements, tailored to the corporate interests of the U.S. and the European Union, requiring fundamental changes to the legal, judiciary and regulatory frameworks of the nations involved. By allowing foreign investors to sue countries, it opens up the possibility of the latter indemnifying the former for losses on expected profits even in cases in which profits are made from public damage.

The possible outcomes of the mega-trade deals in Brazil's exports

Image: Freepik

Undoubtedly the mega deals will profoundly affect the trade relations and the flows of goods and services across national economies. At first, we can anticipate the potential outcomes for both the participating and the nonparticipating countries. Among such outcomes are: (a) trade creation and/or diversion; (b) deepening or isolation of global value chains; (c) erosion of special and differential provisions of previous bilateral negotiations; and (d) the effects on income and employment throughout the world.

For Brazil, it is understood that the intra-regional trade liberalization of the TPP and the TTIP countries, as well as the alignment of their regulatory frameworks, will affect their trade flows in all product categories (basic and industrial). As we can see in the table, most of the products that Brazil exports (47% of the total) are not highly significant in these markets. Nonetheless, the nations that participate in these partnerships are major exporters or importers of many of these products, which can generate negative indirect effects on Brazilian exports. Moreover, regarding the other 53%, the foreign sales of some products are largely dependent on the markets covered by the partnerships. At the same time, there are, in these regions, potential competitors to Brazil and expectations of a growing intra-regional trade, which could result in negative direct effects to the country's exports.

In the case of the primary sector, the TPP may cause trade diversions between Brazil and Asia in favor of competitors such as the United States, Canada, Australia and New Zealand, specifically in the sectors of grains, milk, meat and sugar. Manufactured products sales may also undergo some adaptions, once some European markets and the United States are important destinations of these Brazilian products. On the other hand, the participation of countries such as Mexico and, most of all, Peru and Chile can create an open door for industrial products in South America, at Brazil's expense. In addition, the granting of preferential tariff quotas by the European Union to the U.S. could also reduce Brazil's access to European markets.

Some previous studies have estimated the effects of the TPP and the

Participation of the 10 main products exported by Brazil and major source and destination markets — 2012-15

(%)

PRODUCT	PRODUCT/ TOTAL BR	PRODUCT TPP/TOTAL BR	PRODUCT TTIP/ TOTAL BR	MAJOR WORLD EXPORTERS	MAJOR WORLD IMPORTERS
Iron ore	11.5	1.4	2.1	Australia (52%), Brazil (25%), South Africa (6%)	China (65%), Japan (12%), South Korea (6%)
Soybeans	9.4	0.4	1.3	U.S. (42%), Brazil (38%), Argentina (7%)	China (64%), Germany (3%), Spain (3%)
Crude oil	6.8	2.4	2.3	Saudi Arabia (20%), Russia (17%), United Arab Emirates (9%)	U.S. (19%), China (15%), Japan (9%)
Sugar	4.6	0.5	0.3	Brazil (40%), Thailand (11%), France (5%)	China (8%), U.S. (8%), Indonesia (7%)
Broilers	3.0	0.6	0.1	Brazil (26%), U.S. (18%), Netherlands (10%)	Germany (8%), Hong Kong (7%), UK (7%)
Soybean meal	2.9	0.1	1.9	Argentina (37%), Brazil (23%), U.S. (13%)	Netherlands (8%), Indonesia (7%), France (6%)
Coffee	2.4	0.8	1.8	Brazil (19%), Vietnam (11%), Germany (9%)	U.S. (20%), Germany (14%), France (8%)
Corn	2.3	0.6	0.2	U.S. (29%), Brazil (17%), Argentina (15%)	Japan (15%), South Korea (8%), Mexico (8%)
Cellulose	2.2	0.5	1.3	Brazil (17%), Canada (17%), U.S. (16%)	China (30%), U.S. (10%), Germany (9%)
Meat	1.9	0.0	0.1	Brazil (21%), Australia (18%), India (15%)	Russia (16%), U.S. (15%), Hong Kong (9%)
Subtotal	47.0	7.3	11.4	Australia (29%), Brazil (25%), U.S. (8%)	China (42%), Japan (10%), South Korea (6%)
TOTAL	100.0	22.9	30.6	China (16%), U.S. (15%), Germany (9%)	U.S. (14%), China (11%), Germany (7%)

RAW DATA SOURCE: BRASIL. Ministério do Desenvolvimento, Indústria e Comércio Exterior. **Aliceweb 2**. 2016. Retrieved from <http://aliceweb.desenvolvimento.gov.br/> on Mar. 8, 2016.
UNITED NATIONS. **United Nations Comtrade Database**. [2016]. Retrieved from <http://comtrade.un.org/data/> on Mar. 8, 2016.

TTIP on the Brazilian economy. Simulations made by Thorstensen and Ferraz (2014)[3] indicate a reduction of the Brazilian trade with the TPP and the TTIP countries and Brazil's participation in international trade as a whole, with more significant retractions when they simulate reductions in nontariff barriers — in addition to tariff barriers —, which is precisely the case of these mega deals. As the tariff barriers between member countries are already relatively low, the reduction of nontariff barriers would bring major negative effects to Brazil. With the adoption of the TPP, the most affected sectors in Brazil would be meat products, animal products, fruits, vegetables and coffee. On the other hand, the most benefited sector would be silviculture. With the TTIP, there would be even more deleterious effects on Brazilian trade: in the agricultural sector, most of the losses would be in the same sectors of the TPP. In the industrial sector, however, the most benefited segment would be wood products, while the most damaged would be the ones related to transports equipment, vehicles and parts, leather and nonmetallic minerals.

Another study, conducted by Fleischhaker *et al*. (2016)[4], simulates that the mega deals would have a limited effect on Brazil's growth rate — for the

“Nonetheless, the nations that participate in these partnerships are major exporters or importers of many of these products, which can generate negative indirect effects on Brazilian exports.”

country has a relatively closed economy —, but its trade structure would be severely compromised. Overall, the country would be even more isolated from the global trade and increasingly characterized as an exporter of commodities. Regarding the TPP, a trade growth with China is expected, strengthening the ties between two great outsiders. However, gains in exports to China would be counterbalanced by even greater losses in exports to the TPP members, especially the U.S. and Mexico. When it comes to the TTIP, even with the relative increase in exports of mineral raw materials for the European automotive industry, this would come as a cost for exports in other key markets for Brazilian products, with overall negative results in terms of trade and growth. The only sector that would not lose is mining, but

3 THORSTENSEN, V.; FERRAZ, L. Brasil: entre acordos e mega-acordos comerciais. **Revista Brasileira de Comércio Exterior**, Rio de Janeiro, n. 120, Jul./Sep., 2014.

4 FLEISCHHAKER, C.; GEORGE, S.; FELBERMAYR, G.; AICHELE, R. **A chain reaction?** Effects of mega-trade agreements on Latin America. Gütersloh: Bertelsmann Stiftung, 2016.

not even other commodity-based industries would benefit due to the presence of other agricultural powers, such as Canada and Australia, which would have preferential access to important markets for these products, among which are Japan and the E.U. Moreover, the authors argue that the progress of these mega deals could aggravate the deindustrialization process of the Brazilian economy, making the manufacturing industry shrink in almost all its segments, starting with the automotive industry.

In times of increased interdependence of national economies, lower growth in world trade and fiercer foreign competition, the consummation of the mega deals may pose further challenges to a good integration of the Brazilian economy in the international arena and to a greater integration in the global value chain, especially in a downward period in the cycle of commodities, with unfavorable terms of trade and a rebalancing of the Chinese economy. In this sensitive scenario for Brazil, even with a large domestic market, advantages in some agricultural and mineral sectors and demand for its manufactured products from its strategic neighbors, it would be desirable that the country should adopt a strategy to at least reduce its relative isolation in terms of international trade and global value chains. While the TPP and the TTIP seem to represent serious threats to Brazil's interests, with


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potential effects on the composition and the direction of its trade flows, these effects may worsen the Brazilian situation even more, by increasing its dependence on the exports of only a few commodities. P