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THE IMPACT ON CARIBBEAN BASIN TRADE AND FINANCE OF THE NAFTA

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The Impact on Caribbean Basin Trade and Finance of the NAFTA

by

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1) Introduction

The Caribbean Basin has to adjust quickly to the events happening in North America. The environment has already changed with the expectations of a North American Free Trade Agreement (NAFTA) becoming a reality in 1993. Policies will have to be implemented that would lead to actions by the rest of the Caribbean Basin nations to react to one of its members (Mexico) signing this special pact.

More than ever the trade and financial policies of the Caribbean Basin countries will have to adjust. To expect the extension of the Enterprise for the Americas Initiative (EAI) of the Bush Administration to reach them, rather than grasping for it, may be disastrous. Expecting that Mexican leadership will provide an integration of the whole area into NAFTA will also be courting disaster. Notwithstanding the lip service being provided for Mexico's connection with an expanded Central American Common Market, or the motions of that country with Venezuela and Colombia (known as the G-3) to come closer to the Caribbean Islands, concrete actions are of the essence.

Thus, a review is needed of the form and substance in which the freeing of trade and financial services in NAFTA is going to impinge on the relevant policies in the Caribbean, Central America and Colombia and Venezuela. A book will be prepared later based on papers and discussions taking place in seminars addressing these issues. Statements by distinguished economists from the region will be woven into a common response to these problems. The IESCARIBE network will be used as the infrastructure of institutions backing this effort, because as the Spanish acronym suggests, it is composed of the leading institutes of economic and social research for the Caribbean Basin.

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2) Conceptual Framework

The impact of economic integration had traditionally been measured according to partial equilibrium, comparative statics analysis. The usual concepts considered involved trade creation and trade diversion, and the impact they would have upon costs and prices (including the terms of trade). The outcome of these primary effects would determine the changes in trade, production and expenditure flows for each country involved, the rest of the world and the region being integrated as a whole. Many studies have been done along these lines and only exceptionally have their measurement shown significant impact to the parties affected.

Since these measurements have been disappointing, an attempt has been made to introduce dynamic factors into the analysis. The first one to be considered was that of economies of scale. However, not much was gained from it since the practical significance of its application was a once-over change in costs resulting from serving a larger market. These in the large majority of instances do not bring substantial reductions in costs and prices, given national market sizes and the characteristics of the cost functions of tradable goods. This is also the case when the firms involved have already chosen larger economies of scale options by selling outside their national markets.

Since the successes of the integration movement of the Post World War II era seemed to belie such meager gains, economists explored other sources. The first to be considered was that of competition. The seemingly contradictory results that economic unions among countries that produced, not complementary, but competitive products were expected to be more successful, actually was argued in the 1950s. However, how it would work was not altogether spelled out, and thus its implications for placing integration theory squarely in the realm of economic dynamics were not clearly perceived. As the companies in different lands competed to hold and possibly expand market share, new techniques, know how, product marketing, etc. would be required for efficiency gains. This meant not moves along the curves, as had been considered before, but downward shifts in cost functions. It was increasingly realized that in order to compete the firms would have to invest in physical, technological, innovational and human capital. This would not only spur the growth of the integrating economies, but it would generate externalities in other sectors, which would in turn necessitate a general equilibrium approach to be understood.

Other insights came as a process of induction. Trade in Europe and Central America after integration, became more specialized, not in terms of industries as traditional trade theory had conceived, but with regards to lines within them. This came to be known as intra-industry trade. It showed that tastes, quality of goods, variety and availability had more to say in determining trade flows than had been accounted for. Such specializations led to economies of scope as the management of an enterprise could efficiently be spread thinner along multi-product activities, and concurrently to production runs that would be longer and less costly as the range of the products within an industry would be further concentrated. Management would be handling more products, sometimes from several industries and markets. The implications of all this led to higher investments to develop new brands, organize franchises, gain technological advantage, etc.

Competition, specialization and economies of scope justified why integration would uplift the economies involved, particularly for advanced country economic integration. Every further perfection of a scheme, which would mean greater liberalization of trade, factor movements, policy coordination, etc. would bring with it a bout of investment, innovation, skills, upgrading and entrepreneurial dynamism that would last several years. Ceteris paribus, the economies involved would grow faster and income per head of population would increase. But what about developing economies? Would the same dynamism be expected to result given the market imperfections, lack of modern entrepreneurship, limited mobility and other similar characteristics shared by these economies? Hardly.

However, the analysis of economic integration among the less fortunate members of the world economy also felt the insights of new approaches. Incursioning directly into growth theory for their support when evaluating economic integration, analysts agreed that productivity gains would be derived by drawing into the modern sector of these economies those which more fully reflect the activities to be favored by the expansion of tradables (largely industrial goods) within a growing interregional trade. Since such productivity gains would be multiples of the traditionally ascertained gains from trade described earlier, if part of them are devoted to savings and investments, the calculated returns would make integration as favorable to and probably more so than competition, intra-industry specialization and economies of scope determine it to be in developed countries. In addition, some developing economists have used the concept of economies of scale in a novel manner by considering the economizing of crucial factors, such as foreign exchange, and valuing these at shadow prices dictated by general equilibrium benefit-cost calculations. Again, major gains are derived from economic union through this approach, especially if the connection is established with saving and investment[2].

All of the above seem to distill a success story for integration: what is needed is a spurt of investment, productivity and savings. Whether investments for competition, specialization, etc. in advanced countries, or in the modern sector in developing ones, this mechanism constitutes a virtuous cycle of growth and positive spread-effects throughout other activities in integrating economies. This impact could be called the investment-creation effects of integration. Unfortunately in those countries that are left out, it usually produces an investment-diversion impact, which constitutes its backwash twin. This concept will be crucial in the following sections.

3) Regionalism in a World Economy

No decision, whether by fiat or the market, can ignore the broad trends in the aggregation of the major economies in the world. At present there are two forces being played out, not necessarily in opposition. The dominating one to the present has been internationalism. It started after World War II with the development of the appropriate institutions, and attained momentum when the growth in foreign trade overtook by a significant margin the expansion of the national economies (particularly their non-tradable sectors). This trend did not reach the developing economies until the 1970s, but is now mostly accepted.

The above notwithstanding, some regional trends became noticeable in the 1960s. This was a key characteristic of the European economies, although in Latin America and Africa there were some mildly successful experiments here and there. For a decade and a half these experiences were not majorly discriminatory against the rest of the world given the degree of openness of the European nations, and the dismantling of barriers to trade and finance within Europe. Yet, after the oil crisis of the early 70s all this began to change, as

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[2] On these points see Antonio Jorge and Jorge Salazar-Carrillo, (eds.), Integración y Cooperación en América Latina, University Presses of Florida and ILDES (Friedrich Ebert Stiftung), Gainesville - Rio de Janeiro, 1982 and Jorge Salazar-Carrillo, Industrialización y Empleo en el Contexto de la Integración Latinoamericana, Organization of American States and Estudios Conjuntos para la Integracion Economica Latinoamericana (ECIEL), Washington D.C., 1976.

protectionism became the order of the day in the advanced countries[3].

The tendency toward regionalism was further strengthened by the definition of a Europe 1992 in terms of a confederation of states, stopping just short of one country, with free movements of goods and factors of production and the coordination of government policies. With the forthcoming agreement of the European Community and the European Free Trade Agreement (EFTA) for the incorporation of the latter into the Europe 1992 economic provisions, beginning some time in the middle nineties, plus having other nations in the continent (mostly from Eastern Europe) knocking at the door, the sheer size and the spread of income levels of the European bloc will certainly tilt the balance towards greater protectionism. It is hard to ignore that European countries have established preferences which facilitate dealing with each other, and exclude third parties through common agricultural policies, external tariffs and non-quantitative barriers that hinder access to their markets.

The movement towards greater integration in Europe has coincided with the crisis in the last trade liberalization round organized by GATT, and known as the Uruguay Round. Additionally, the United States and Canada jumped on the bandwagon of regionalism and signed a free-trade agreement in 1988, which eventually led to the idea of the North American Free Trade Agreement (NAFTA). There is very little doubt that the latter will be signed into law in 1993. Should it be concluded that the forces of regionalism will overpower the Uruguay Round and the major trend towards internationalism that has existed for more than four decades?

This is not to be expected because of four factors:

a) the Asian region, which altogether approaches the economic size of the twelve of Europe 1992, has remained mostly clear of regionalism;

b) there would still be a lot of room for trade among blocs, even after they are strengthened;

c) the blocs themselves have kept striving towards internationalism, even while strengthening their own regions;

d) financial and currency internationalization is a mighty force leading trade in the same direction.

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[3] Oddly enough when the developing world, at the behest of the developed nations, began to join en masse the movement towards world trade.

Thus, the major and older trend will coexist with the minor and younger tendency into the 21st century. However, the danger of being hurt by these trends is greater for developing economies, particularly those that inhabit the backwaters of the meshing international and regional forces. As Paul Krugman has adeptly put it at the conclusion of an article considering similar questions: "The main concern suggested by this economic analysis is distributional: inward-turning free trade areas, while doing little damage to themselves or each other, can easily inflict much more harm on economically smaller players that for one reason or another are not part of any of the big blocs"[4].

4) The State of the Economy in Latin America and the Caribbean Basin

How is Latin America doing? Has it been integrating with the rest of the world? The same questions should be asked about the Caribbean Basin.

Since 1991 the Latin American economy has been growing somewhat faster than the average for the decade of the eighties. The growth rate in constant prices has been 3.2 percent per year, slightly one percentage point over the expansion of population (about 2.0 percent yearly). This performance follows three years of expansion at an annual average just above 0.8%, quite below the growth of population. Although it may appear that Latin America may be out of its slump of the eighties, actually the better interpretation is that these economies are simply in the prosperity phase of a cycle about a declining trend, which has been played out in the eighties, with a depression in 1982-84 and a recovery in the middle eighties.

With regards to its participation in the international economy, in 1980 Latin America exports hovered about the $100 billion mark. In 1992 they are expected to be around $130 billion. The rate of growth implicit in these numbers is clearly under 3% a year in nominal terms, well below the rate of expansion of world trade. Similar figures apply to imports, although their expansion has been of recent origin (18 percent per year in 1991 and 1992). Thus, the situation does not appear to show that this region has been integrating with the

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[4] See for this view Paul Krugman, "The Move Toward Trade Zones" in Federal Reserve Bank of Kansas City, Policy Implications of Trade and Currency Zones, Kansas City, Kansas, 1991. Other chapters in the same volume should bear reviewing as well.

world economy.

Yet, one facet of the expansion in trade of the Western Hemisphere is very noticeable: its increasing trade ties with the U.S. The Americans have been winning back their market shares in the seventies and eighties, and in many cases these are close to historical highs. With few country exceptions, they represent the principal trading partner of Latin America. To cite an indication, U.S. exports to Latin America expanded from $44 billion in 1988 to $63 billion in 1991, almost a 50 percent increase. It should be noted that U.S. imports from the region are even larger, although not expanding as fast lately. Therefore, the Latin American economies have been informally (without any agreement backing it) integrating with the U.S. economy at an increasing velocity in the last two decades. Yet the same cannot be said of the U.S.A., whose imports and exports from and to the Latin American nations have been just above 15 percent of the former's totals.

With respect to the Caribbean Basin its overall rate of growth in 1991-1992 appears to have been somewhat higher than for Latin America as a whole, even though this was countermanded by a higher demographic expansion. Yet, the perception that this is just a reflection of the cyclical phases being experienced by these countries is akin to the noted above for the region as a whole.

Indeed the Caribbean Basin has done slightly better than Latin America as a whole with respect to its trade performance. It is perhaps not realized that the overall trade figures for the Caribbean Basin are larger than those of the Latin American region as a whole, expurgated of the Caribbean Basin itself, which is a measure of its greater trade orientation[5]. But still the combined export and import expansion of this sub-region during the 1980-1992 period fell quite below the expansion of world trade, signalling that commerce is lagging behind the expansion in the non-tradable part of the economy.

Again, the most noticeable pattern in the international economic relations of the Caribbean Basin is the very strong trading partnership that has emerged with the U.S.A. In the case of the Caribbean Basin it is bolstered by formal agreements. The first to come was the Caribbean Basin Initiative (CBI)[6] which favored practically all of the politically

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[5] If this is taken in per capita basis the difference would be even more remarkable, as the Caribbean Basin has significantly less than half the total population of Latin America.

[6] Also called the Caribbean Basin Economic Recovery Act (CBERA).

independent and democratic countries in the Caribbean and Central America, with the exception of the large continental countries of Mexico, Colombia and Venezuela[7]. Although to a large extent its advantages for the Caribbean Basin largely overlap with the Generalized System of Preferences (GSP) provided to developing countries by the advanced nations of the world, it does not include graduation and is a U.S. law that has been recently made a permanent act, while restricting even more the handful of products to which it does not apply[8].

More recently a new Act has been approved as law by the American government which practically extends the privileges of the CBI, with some limitations (e.g., only for a ten year period), to all of the countries of the Andean Group. Two of the countries are situated also in the Caribbean Basin, and will now be eligible for privileges similar to the CBI, namely Colombia and Venezuela. If the puzzle is completed by reminding the reader of the NAFTA agreement with Mexico, it is clear that like Latin America, but more so, the Caribbean Basin is increasingly integrating with the U.S.A., while the same cannot be said when considering the rest of the world as trading partners[9].

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7 The date of initiation of the CBI was 1983. For further information on the Initiative and the concept of the Caribbean Basin see Antonio Jorge, Jorge Salazar-Carrillo and Irma Alonso, "In Search of an Optimal Economic Development Strategy for Maximal Growth in the Caribbean" in Edgar Ortiz (Ed), Current Economic and Financial Issues of the North American and Caribbean Countries, Centro de Investigacion y Docencia Economica (CIDE), Mexico, 1990.

8 Perhaps the most transparent way of looking at the CBI is by realizing that it is practically a one-way free trade agreement by which the United States offers free entry to its market by the signatory countries, without any countervailing demand of the same kind. It also facilitates tourism and investment in the signatory countries, while requesting tax information on U.S. tax payers and the abolition of secret banking.

9 Exceptions may be the now politically independent former colonies of the European Community members. These have kept stronger ties with Europe through the Lome Convention, which are similar to the CBI provisions. Yet, the former is a small club of nations in the Caribbean Basin with even less importance in terms of economic weight, although Haiti and the Dominican Republic have recently acceded to the framework.

5) Trade and Financial Reform in Mexico

When Mexico decided to join the General Agreement on Tariffs and Trade (GATT) in 1985, some of its tariffs were as high as 200 percent. In 1992 the average tariff rate in the nation is around nine percent. When the country joined GATT it made a commitment to abide by the rules of international trade that the institution, one of those created after the Second World War to foster internationalism, had established over the years, and which it polices. This first but major step taken by the Mexicans led to a liberalization of foreign commerce that has been steadily transforming the economy into an increasingly open one, which has had important implications for a the reform of financial policy as well.

From 1985 onwards the imports and exports of Mexico began to expand at a torrid pace. If the attention is focused on Table 1, it can be seen that imports of goods grew three and one half times over five years, at an annual percentage rate of 28.0 percent. Exports of goods expanded less, but still at a yearly rate of 13 percent.

TABLE 1

Mexico's Foreign Trade in Goods

(in millions of US$)

Year	Imports	Percentage	Exports	Percentage
1986	11 432	--	17 326	--
1987	12 223	6.9	22 254	28.4
1988	18 898	54.9	22 902	2.9
1989	25 438	34.6	25 889	13.0
1990	31 090	22.2	30 585	18.1
1991*	38 357	23.4	31 292	2.3

* preliminary

Source: Instituto Nacional de Estadisticas, Geografia e informatica and Banco de Mexico

To a large extent, as pointed out in the previous section, total trade has enlarged the most with the United States. Mexico is now the third largest trade partner of the U.S. after Canada and Japan, in that order. This is already influencing many of the statistics of economic interaction between the U.S. and Latin America, and even more so for the Caribbean Basin. To exemplify consider the following fact for 1990: "Mexico's share of U.S. total exports to Latin America ... reached 52%, the highest level on record"[10].

In fact, if services are considered as well as goods, Mexican exports to the U.S.A. grew from $23 billion in 1988 to $30 billion in 1990, about a 30.0 percent increase in two years. In turn American exports into Mexico went from $21 billion in 1988 to $28 billion in 1990, a 33.3 percent expansion. It should be noted in passing that the trade deficit of the U.S. with its immediate neighbor to the South was much smaller than that with Latin America as a whole.

Financial reform in Mexico was spurred by its commercial revolution which has been exposed above, because of the increasing importance of trade in services in the world. Financial services commerce being an important part of the latter, and indirectly influencing other components like information, communications, insurance, etc., requires a minimum of barriers and controls. Certainly this has been provided by the Mexican authorities and more, since their involvement in negotiating NAFTA presumed a degree of field levelling and transparency comparable to the U.S. position at the Uruguay Round now being negotiated.

Clearly another important portion of commerce in services involves foreign exchange operations. It is of the essence to have a unified rate and a convertible currency to join the largest market in the world and its sizable commissions. Mexico has achieved an increasingly transparent system and with a predetermined daily mini-devaluation of its peso. So much in fact that another major component of services trade, foreign investment, part of which is short term and very sensitive to foreign exchange muddles, has boomed in Mexico. "Since 1988, global corporations have invested some $80.8 billion in Mexico and are now investing at a rate 25% higher than just two years ago"[11]. In addition Latin America is experiencing a two-year record capital inflow in 1991-92, with a total magnitude estimated approximately

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[10] United Nations Economic Commission for Latin America and the Caribbean (ECLAC), CEPAL News, Vol.XI, Nr.11, November 1991, p.2.

[11] See Susan Walsh Sanderson and Robert H.Hayes, "Mexico Opening Ahead of Eastern Europe", Harvard Business Review, September - October, 1990, p.4.

at $80 billion. Half of these flows are going to Mexico.

6) Trade and Financial Reform in the Rest of the Caribbean Basin

The nations of the Caribbean Basin have the highest import/GDP ratios in Latin America, if Colombia, Mexico and Venezuela are excepted. No country in this group has a ratio below 23 percent, and ignoring the smaller countries like Barbados and Bahamas which are even higher, typical ratios are in the 45 to 50 percent range, like those for Honduras, Jamaica and Costa Rica. For all the nations in the Basin the principal trading partner is the U.S. In fact, the latter country was more important in the commerce of the Caribbean Basin than the catchall category named "the rest of the world", which only excludes Latin America and of course the U.S.A. The single exception to this rule was Nicaragua (in 1990)[12]. The exchange among the Latin American nations themselves, including those of the Caribbean Basin, comes in third.

Additionally, the large majority of the countries of the Caribbean Basin are heavily indebted internationally. The lion's share of their foreign debts are owed to O.E.C.D. governments and multilateral lending institutions, thus being of a public nature (the exceptions to this rule are the continental nations: Colombia, Mexico and Venezuela). In order to handle the service of their debts, avoid default, and not risk being ostracized from the reschedulings, debt-equity swap operations and debt-reduction plans, these countries agreed to policy-reform packages presented by their creditors. The key creditor country involved in all the above is the U.S.A., which has put forth different schemes to solve the dilemma of the foreign debt, namely the Baker and Brady Plans.

The situation they face has pressed the Caribbean Basin nations to adopt trade and financial reforms along the liberalizing lines being suggested by developed country governments and multilateral institutions (which are as well dominated by those governments). This is not to say that at this moment in the Caribbean Basin a large number of public leaders, their policy-makers and many researchers and academicians, also espouse similar lines of thought. The end result is the establishing of policies which remove tariff and

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[12] Since then Nicaragua's circumstances have changed, and the country is now a signatory of the Caribbean Basin Initiative, so this exception is in the process of conforming to the rule.

non-tariff (quantitative) barriers, allow the determination of market-determined exchange rates and in general try to attain neutrality between export, import-substituting and non-tradable activities. This would result in an expansion of exports which remain essential to maintaining the import levels required by these open economies, while facing the obligation of managing their debt service. Given their intricate relations with the U.S., it also remains necessary to toe the line not to offend the government of its principal export market, and its main supplier of credit, as well as goods, foreign investment, technology, know-how and last but not least, aid. Notice that it is the effort and the public agreement to attain these reforms that are important here, as many nations in the Basin have not been nearly as successful as Mexico in implementing these policies, perhaps because the general conviction of their electorates is not that strong.

With regards to financial liberalization, it has not been the strong suit of the policy reforms suggested as conditions by the creditor nations and institutions. But as noted above, the liberalizing of trade implies some efforts along the same lines in exchange rate determination, so strongly linked to financial markets and interest rate and monetary policies, in conjunction with the removal of obstacles to foreign investment. It is also realized, furthermore, that the control of inflation is a *sine qua non* for stable rates of exchange, and that in addition to control of monetary policy, fiscal balance has to be achieved. Finally, if the economy is to grow interest rate subsidization has to be prevented, so that rates paid on deposits stimulate private savings and the selective credit controls usually related to subsidized rates give way to a neutral allocation system. It is well understood, but left toward the tail end of policy reform, that the opening of the financial markets to the free flow of capital requires a solid economy backed by substantial foreign reserves.

As an illustration of how far reform has gone in the Caribbean Basin some excerpts can be taken from a representative case, as expressed by President Callejas of Honduras (the same words could have been written by formerly socialist leaning Prime Minister Manley of Jamaica)[13]: "we have opened our market dramatically, reducing import tariff rates from a maximum 135% in 1989 to a current maximum of just 20%. Price subsidies have been eliminated. Foreign-investment regulations are being liberalized. Interest rates and the value

[13] Prime Minister Manley recently left his post because of health reasons, after being returned to office three years ago. His party remains in power.

of our currency are now set in response to market forces. Government spending has been brought under control: The fiscal deficit declined to an estimated 4% of gross national product in 1991, from 9.2% of GNP in 1989"[14]. Yet, such achievements pale when compared to the unwavering, mostly popular and wide-ranging changes in policy and obtained results of Mexico.

7) NAFTA and its Consequences

The addition of Mexico to the existing Canada-U.S. Free Trade Agreement has captured the attention of many all over the world. To some extent it shows how the media can hype a happening into something larger than it actually is. It is true that the free trade area[15] will be the largest market in the world, surpassing 1992 Europe in every sense, but this can be attributed primarily to the gigantic economic size of the U.S.A.[16].

Looking at the impact of NAFTA it is useful to point out that there are a few important steps to be taken before it is assured passage, even though it is expected that the Agreement will go through. In Graph 1 the various elements involved in achieving the final accord are depicted in ways that resemble a computer flow chart, a stop-go board game or an organizational chart, depending on your perception. To reach home on January 1, 1994, the three nations must move from presidential signatures of the Agreement, to two difficult down moves called "implementing legislation" and "congressional approval". The latter has

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[14] Rafael Leonardo Callejas, "Extend Free-Trade Accord Southward", Wall Street Journal, January 31, 1992, p.A15.

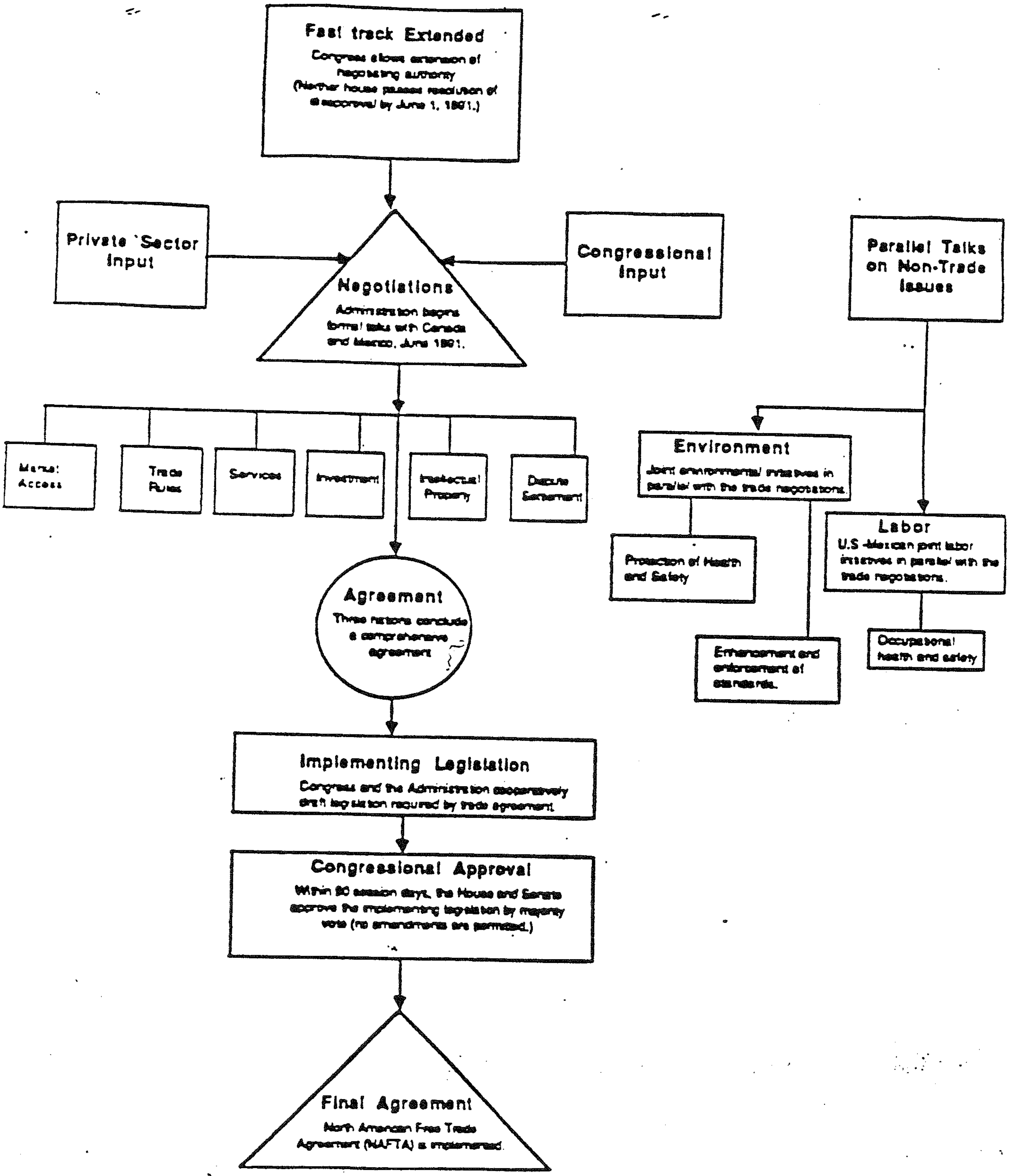
[15] It should be clarified that what has been underemphasized is that NAFTA is much more than a trade agreement. It is an investment agreement as well, and includes everything that a unified market provides except totally free movement of labor. It is also the most sophisticated and extensive treatment of trade in agriculture, services, finance, technology, copyrights, patents, etc., following the principles innovatively introduced in the Uruguay Round. The fact that there is no coordination of external tariffs or policies is largely inconsequential because the U.S. leadership is accepted even without agreements, with the region constituting an optimum currency area, where tariffs and other barriers differ very little among the three nations.

[16] The slow growth of the U.S. economy which many decry can be misconstrued. A 1 percent growth in the American economy signifies adding more than $50 billion in output to the world in one year, a figure that is larger than the whole gross domestic product of the large majority of world nations.

to take place before May 31 of 1993 and the U.S. will be in political transition until then with a new President and Congress.

GRAPH 1

The U.S. Negotiations and Approval Process for a North American Free Trade Agreement (NAFTA)



To consider the consequences of NAFTA please refer to Table 2. The wide gap between Mexico and the other two countries is appalling. If the four poorest countries in the Community were put together (Portugal, Greece, Ireland and Spain) they would economically add up to something similar to Mexico. As a proportion of the European Community of January 1 of 1993 these four countries would represent a similar share as Mexico to NAFTA in January 1994. So there is no novelty here. Moreover, since the U.S.-Canada Free Trade Agreement is already in place, the addition of Mexico, with a total G.D.P. of approximately $275 billion a year, would increase total market power in about 3.5 percent to the previously existing market. This is tantamount to adding just one large state to the American Union, and some may recall that when Alaska fully became a member of the United States of America, nobody paid much attention. Finally, as well shown in preceding pages, Mexico is already informally integrated into the U.S. similarly to the way in which many Asian nations are already well advanced into a symbiotic relation with Japan. Thus, not much further impact would the new NAFTA have on the international economy than it has already had.

TABLE 2

Key indicators in the NAFTA countries	**US**	**CANADA**	**MEXICO**
GDP per capita 1988 (US$)	19,678	18,747	2,116
Population mid-1988 (mil)	246.33	25.95	82.73
Employment (mil), 1988 % in services % in agriculture	118.0 69.6 3.0	12.4 69.8 4.9	7.4 31.3 33.1
Industrial Production as % of GDP, 1987	30	35	34
Capital goods as % of ind. production, 1987	35	25	14
Labor compensation per employee (wages plus fringes), 1988 (US$)	13.92	13.58	1.57
Per capita public expenditure on education (US$)	1,126	1,171	59
Productivity, GDP/employee, 1988 (US$)	42,161	39,733	7,935
Gross domestic investment as % of GDP, 1986-88	17.3	20.9	19.1
Expenditure on R&D as % of GDP, 1988	2.7	1.3	0.5

Clearly the major impact of NAFTA will be upon the Mexican economy, which stands the most to gain (according to practically all simulations) or to lose (following a few critics). And then upon the other countries in the Americas, particularly those that have achieved a special status with the "Giant to the North", and for the longest time. Of course, there will be trade diversion in their exports to the U.S.A. most importantly, but also of those lines of products that these countries were exporting to Canada and Mexico. But most importantly there will be investment diversion, principally affecting the nations of the Caribbean and Central America, which are already seeing a significant number of investors preferring a locality like Mexico, rather than the Caribbean Basin, as a production point from where to enter the U.S. and Canadian markets.

8) Expanding NAFTA to the Caribbean Basin and Beyond

Official statements by the American government are loath to admit that by helping Mexico through NAFTA, they are hurting other neighbors to the South. In fact they have put their negotiations behind their words as they have signed framework agreements with practically every country, or group of countries (like the MERCOSUR composed of Argentina, Brazil, Paraguay and Uruguay). Even before, President Bush had launched the Enterprise for the Americas Initiative, whose ultimate objective is to create one market from Alaska to Tierra del Fuego. But these plans are moving slowly. Supposedly a free-trade agreement with Chile is in the works, yet the signal is clear that first priority is turning NAFTA into law, and the rest will follow. However, it is increasingly clear that anything else is based on the presumption of a continuation of President Bush's programs.

Although analysts concur that the Caribbean Basin, and Latin America as a whole, will suffer from trade and investment diversion, it is the most dependent and closer neighbors of the U.S. that have the most to lose. They had been favored by the CBI, and had weathered the complaints of other countries in the Western Hemisphere to the Americans, that the agreement was discriminatory toward those nations which had been excluded[17]. Tables have turned, and now the CBI members have to complain about the preferential treatment afforded to Mexico.

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[17] Actually the Andean Trade Preference Act is in part a response to such clamor.

Even though the countries in Latin America not included in any agreement are those that will bear the brunt of the diversionary forces, the Caribbean Basin countries will probably attract more supporters in the U.S.A. They are strategically located at the underbelly of America and present the most immediate dangers (certainly as much if not more than Mexico) to the immigration and drug concerns of the U.S. They are economies presenting the greatest opportunities, given their size and that they are economies at risk, for Americans to indulge as well in tax evasion, financial scams, frauds and money laundering. Although, perhaps with coercion from abroad, these countries have complied with the policy reforms requested from them, at least formally having undertaken the trade and financial liberalizations that stand at the center of the structural changes harped by the Washington Consensus[18]. They have also achieved other important goals like political democracy, demilitarization and (attempts at) privatization and reducing the role of government, that has allowed the U.S. to deactivate the crisis status of the region and reassign its aid resources elsewhere. For an area that economically represents less than one percent of the combined economies of the U.S.A. and Canada, their incorporation into the North American Market would cost very little to these two major economies and even to Mexico. Finally, it would serve to indicate that the movement of the free market towards Patagonia has begun[19].

Still, at the moment the C.B.I. lobbyists have been asked to hold their guns, as nothing should be allowed to arouse Congress and endanger its passing of the NAFTA legislation. However, another gambit may be in the offing here, which assigns to Mexico a special role in extending the North American Free Trade Area southward. Certainly Mexico has been very busy itself negotiating free-trade agreements with Chile and the Central American Common Market, and its partners in the so-called G-3 countries of the Caribbean Basin, namely Colombia and Venezuela. It may be in the cards that Mexico would become a corridor that in compliance with the rules of origin limitations, could constitute not only an entry for the Caribbean Basin countries to the North American market, but also to

[18] This is a term reflecting the thinking with one mind and speaking with one voice of all the U.S. agencies and multilateral institutions located inside the Washington D.C. Beltway.

[19] Not to be lost in the shuffle is the fact that the Caribbean Basin is rich in energy.

southern markets for the U.S. and Canada[20]. However most Caribbean and Central American leaders are skeptical, and even many Mexican analysts share their sentiments.

Given the above considerations, it is not difficult to be in sympathy with the ideas of President Callejas, which reflect the First Ministerial Conference for Central America and the Caribbean, hosted by his country of Honduras. It is, he writes: "necessary to ensure that the expanded NAFTA does not put the CBI countries at a comparative disadvantage with Mexico attracting trade and investment. Consequently, as the NAFTA negotiations proceed, a bridging mechanism for the CBI countries should be developed. Such a mechanism would solidify the reforms carried out thus far and strengthen the positive economic and political trends taking place in the region"[21]. Hopefully, this bridging will sooner or later be applied to Colombia and Venezuela, and in the not too distant future to the rest of Latin America, to make valid the goal of one market from Alaska to Antarctica.

9) The Role of the United States

The American position has, at least during the 20th century, been key to the world's international stance. The Smoot-Hawley Act of 1932, supported by then President Herbert Hoover, gave rise to a sequel of retaliatory measures that ended up drastically reducing world trade for the rest of the decade. The multilateralization of the trade agreements subscribed between the U.S. and several nations on a bilateral basis, were the harbinger of the Bretton Woods Agreements and the creation of the GATT in the Post-War World. The position of this leading country now seems to be stradled between its present long-standing free trade position, and its recent bent toward regionalism. Given the uncertain results of the Uruguay Round, the path toward a free-trade area joining all of the Americas may end up being the one of less resistance. Nevertheless, as pointed out in the earlier sections of this paper, it is doubtful that the U.S. would abandon its promotion of world trade to any other multicountry objective. In the end, and particulary at this moment, it may not consider it contradictory to pursue both objectives simultaneously.

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[20] For an elaboration of some of these views see Sharon Belluca, "Mexico is the Door South to Latin American Trade", in Foreign Trade, September-October 1992, p.10.

[21] Refer to Rafael Leonardo Callejas, loc. cit.

Within the above setting, a particular change in the foreign trade position within the United States of its various interest groups, is not well-known and is well worth exploring at this juncture. The various States of the Union have become increasingly interested in promoting international trade[22]. In many cases they do not distinguish between exports and imports, although some unknowingly consider that if they emphasize exports their balance of trade would improve[23]. The governments of states, a good number of counties, and even some municipalities have been increasing substantially the expenditures devoted to commerce and other economic exchange with other nations. In fact, referring just to the states plus Puerto Rico, the total budget for these activities reached $110 million in 1990, and has doubled since 1986[24].

It should be noted that some of these states are large enough to be among the top twenty biggest economies in the world if they were separate countries. California would be in the top five, and New York and Texas among the ten largest nations. If they promote international trade certainly by their sheer weight the U.S.A. is going to end up doing the same. Additionally their legislators have a major influence over the enacting of laws which must emerge from Congress in the American political system[25]. If only the 15 largest states were strongly in favor of relaxing trade barriers, it would practically be assured of a majority in the House of Representatives which, because of its better representation of the overall population, has a crucial role to play in drawing up and enacting bills in the legislative branch of the American democratic system. Thus, it seems that such a major force would ensure a favorable posture for international exchange by the U.S., that would preserve a balance among commercial ties with the Atlantic Alliance, the Pacific Rim and the American Continent.

All of the above is not to depreciate entirely the new leaning of the U.S. toward

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[22] And also a special form of trade in services, namely, tourism. They are promoting as well foreign investment within their own political entities.

[23] The balance of trade of any state of the Union is substantially determined by their economic exchange with each other, rather than with foreign nations.

[24] The National Association of State Development Agencies (NASDA) reports on these numbers. They compile the NASDA State Export Program Database.

[25] The President of the United States can only sign or veto these bills. In the latter case it may be overridden by a two thirds majority of Congress.

regionalism, but to put it in the proper perspective. In fact, the interests of local governments in the United States also favor inter-American trade: the statement about the fifteen states could also be applied to Mexican trade. Considering the twelve states that export more than $400 million a year to Mexico as depicted in Table 3, and the three whose percentage rate of exports to that country had exceeded 500 percent between 1987 and 1990 (in the same Table), it follows why NAFTA is practically assured passage in Congress. It should be also noted that the four largest states in the Union (California, New York, Texas and Florida) are among the ten largest states in exports to Mexico.

Paradoxically, for the same reasons it is difficult to foresee that the trade and (most importantly) investment diversion that NAFTA is already causing in the Caribbean Basin, will not create countervailing forces by the states that are most closely tied to the latter. This is especially the case when Mexican trade with the States of the Union is concentrated heavily in Texas and California, while that having to do with the Caribbean Basin is more widely spread[26].

10) Conclusions

This paper links the trade and financial reforms that have been occurring at a rapid pace in the Caribbean Basin, to the consequences of the North American Free Trade Agreement (NAFTA), which is considered certain of approval. In turn this requires an examination of trends in world trade and finance, and a conceptual apparatus for the evaluation of the main impacts of NAFTA on the region in question (of which Mexico is itself a member). The economic situation of Latin America also constitutes a required backdrop to such analysis. The major conclusions of this essay are the following:

a) Unless the Caribbean Basin participates in a free-trade agreement involving its principal trading partner, the U.S., it will suffer a drop in foreign and domestic investment coming from the diversion of the former fundamentally to Mexico. This will in turn have deleterious consequences for savings and development in the region, per contra enhancing principally those of Mexico.

[26] With New York and Florida, the other two of the four largest states, being in this latter group.

TABLE 3

STATE EXPORTS TO MEXICO: 1987–90

	(Thousand $)				(Percent Change)		
	1987	1988	1989	1990	1988-89	1989-90	1987-90
ALABAMA	$80,551	$114,216	$156,037	$160,335	36.6	2.8	99.0
ALASKA	5,293	2,678	9,942	4,724	271.3	-52.5	-10.7
ARIZONA	644,677	761,786	759,494	850,613	-0.3	12.0	31.9
ARKANSAS	37,710	42,664	80,519	46,752	88.7	-41.9	24.0
CALIFORNIA	2,257,263	3,241,765	4,172,918	4,670,518	28.7	11.9	106.9
COLORADO	69,290	79,955	96,398	113,553	20.6	17.8	63.9
CONNECTICUT	115,378	160,174	182,953	175,896	14.2	-3.9	52.5
DELAWARE	28,033	38,900	51,414	117,121	32.2	127.8	317.8
DIST. OF COL.	4,932	7,063	6,627	8,464	-6.2	27.7	71.6
FLORIDA	218,998	326,336	424,199	494,089	30.0	16.5	125.6
GEORGIA	108,097	157,208	232,017	435,118	47.6	87.5	302.5
HAWAII	61	216	22	37	-89.9	68.2	-39.0
IDAHO	11,238	36,331	22,652	31,075	-37.7	37.2	176.5
ILLINOIS	278,373	448,166	569,203	880,814	27.0	54.7	216.4
INDIANA	270,929	155,910	203,961	219,211	30.8	7.5	-19.1
IOWA	66,084	93,773	116,720	87,983	24.5	-24.6	33.1
KANSAS	124,979	279,445	221,210	186,791	-20.8	-15.6	49.5
KENTUCKY	43,266	86,127	99,428	113,165	15.4	13.8	161.6
LOUISIANA	377,426	530,149	671,019	735,554	26.6	9.6	94.9
MAINE	2,685	10,858	11,237	14,846	3.5	32.1	453.0
MARYLAND	17,044	33,212	25,262	53,377	-23.9	111.3	213.2
MASSACHUSETTS	100,117	116,530	155,449	184,667	33.4	18.8	84.5
MICHIGAN	1,077,870	1,317,396	1,720,558	1,432,058	30.6	-16.8	32.9
MINNESOTA	89,975	135,383	162,847	162,680	20.3	-0.1	80.8
MISSISSIPPI	52,510	69,557	97,460	80,390	40.1	-17.5	53.1
MISSOURI	198,713	312,727	322,043	273,534	3.0	-15.1	37.7
MONTANA	1,219	2,255	19,948	9,661	784.6	-51.6	692.5
NEBRASKA	44,546	52,275	50,581	33,514	-3.2	-33.7	-24.8
NEVADA	2,706	5,476	22,207	32,348	305.5	45.7	1095.5
NEW HAMPSHIRE	9,790	14,280	18,316	23,379	28.3	27.6	138.8
NEW JERSEY	189,209	266,749	390,817	417,009	46.5	6.7	120.4
NEW MEXICO	9,058	15,968	14,479	17,217	-9.3	18.9	90.1
NEW YORK	512,368	827,931	834,284	801,299	0.8	-4.0	56.4
NORTH CAROLINA	94,670	137,110	190,184	228,485	38.7	20.1	141.3
NORTH DAKOTA	39,886	37,483	51,651	46,897	37.8	-9.2	17.6
OHIO	245,232	381,331	464,034	444,690	21.7	-4.2	81.3
OKLAHOMA	44,248	97,769	62,369	55,839	-36.2	-10.5	26.2
OREGON	19,477	23,453	38,067	42,986	62.3	12.9	120.7
PENNSYLVANIA	181,126	337,393	474,687	582,604	40.7	22.7	221.7
RHODE ISLAND	14,664	23,941	32,108	41,011	34.1	27.7	179.7
SOUTH CAROLINA	32,350	54,853	59,751	52,536	8.9	-12.1	62.4
SOUTH DAKOTA	5,358	4,760	5,251	5,722	10.3	9.0	6.8
TENNESSEE	100,938	141,177	244,237	283,176	73.0	15.9	180.5
TEXAS	6,465,123	9,334,029	11,010,627	13,287,718	18.0	20.7	105.5
UTAH	37,088	50,985	31,758	40,082	-37.7	26.2	8.1
VERMONT	2,570	16,351	11,550	16,581	-29.4	43.6	545.3
VIRGINIA	41,056	63,513	85,743	108,444	35.0	26.5	164.1
WASHINGTON	83,382	90,990	119,270	91,641	31.1	-23.2	9.9
WEST VIRGINIA	43,988	18,567	26,273	30,516	41.5	16.1	-30.6
WISCONSIN	77,322	83,188	135,217	136,880	62.5	1.2	77.0
WYOMING	3,374	3,055	3,824	11,868	25.2	210.4	251.7
TOTAL U.S.	$14,582,239	$20,643,408	$24,968,823	$28,375,468	21.0%	13.6%	94.6%

Source: U.S Department of Commerce, International Trade Administration (ITA), U.S *Exports to Mexico: A State - By - State Overview, 1987-90*, Washington D.C., 1991, p.3

b) Internationalism and regionalism will constitute in essence the non-contradictory milieu of the nineties and the early years of the next millennium. It is felt that trade within major blocs will not impede the growth of world trade, and the U.S. is committed to free trade at the international level, while it pursues the Americas concept.

c) Even without one free-trade agreement signed with any Western Hemisphere country, save for the market access ceded to the Caribbean Basin Initiative (CBI) signatories for economic recovery purposes (as stated in the name of the Act), and the drug eradication and control inspired Andean Trade Preference Act (ATPA), the U.S. has become the major trading partner by far, of the Latin American economies. Thus, in a deeper sense, the area is already an informal free-trade region with low tariffs and non-tariff barriers in practically every country and with the U.S. being the principal commercial ally of each nation. This does not apply in reverse given the previous point and the size of the American economy.

d) Given the decline of the Latin American and Caribbean Basin economies in general, such informal or formal trade enhancement agreements are a sine qua non for a reversal of these trends. Therefore, these countries must use every means necessary to ensure inclusion into any free trade area in the Americas when it comprehends the sizable import markets of the U.S. and Canada, which combined constitutes the largest in the world.

e) The trade and financial reforms of Mexico have been the most substantial in the Western Hemisphere, and have made it worthy to be first to join the U.S. and Canada in a regional market. The policy measures in question, even before considering NAFTA, have already meshed the Mexican and the U.S. economies to such a degree, that for all intents and purposes they already constitute one economic region. The formalization of NAFTA will represent to a large extent a rubber stamp of trends of the past that shall continue into the future, but it does not add significantly to the behemoth consisting of the American and Canadian economies, which already signed their one-market pact some years back. Although a possibility, Mexico is not likely to provide access to the NAFTA for its Caribbean Basin neighbors on its own.

f) It encumbers the Caribbean Basin countries, which will experience the erosion of the advantages achieved by their special CBI and ATPA agreements by NAFTA, to pressure the United States for parity with the latter. This is especially the case since the Agreement is wider than just trade, including foreign investment, services, technology, finance and intellectual property rights. In attaining such objective the Caribbean Basin nations will find much solace of a common purpose with many States of the Union, which have a good chance of increasingly forcing the extension of NAFTA to the closest neighboring nations. This was originally the intention of the Enterprise for the Americas Initiative, but this venture at the moment lacks the commitment of the future American government.

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