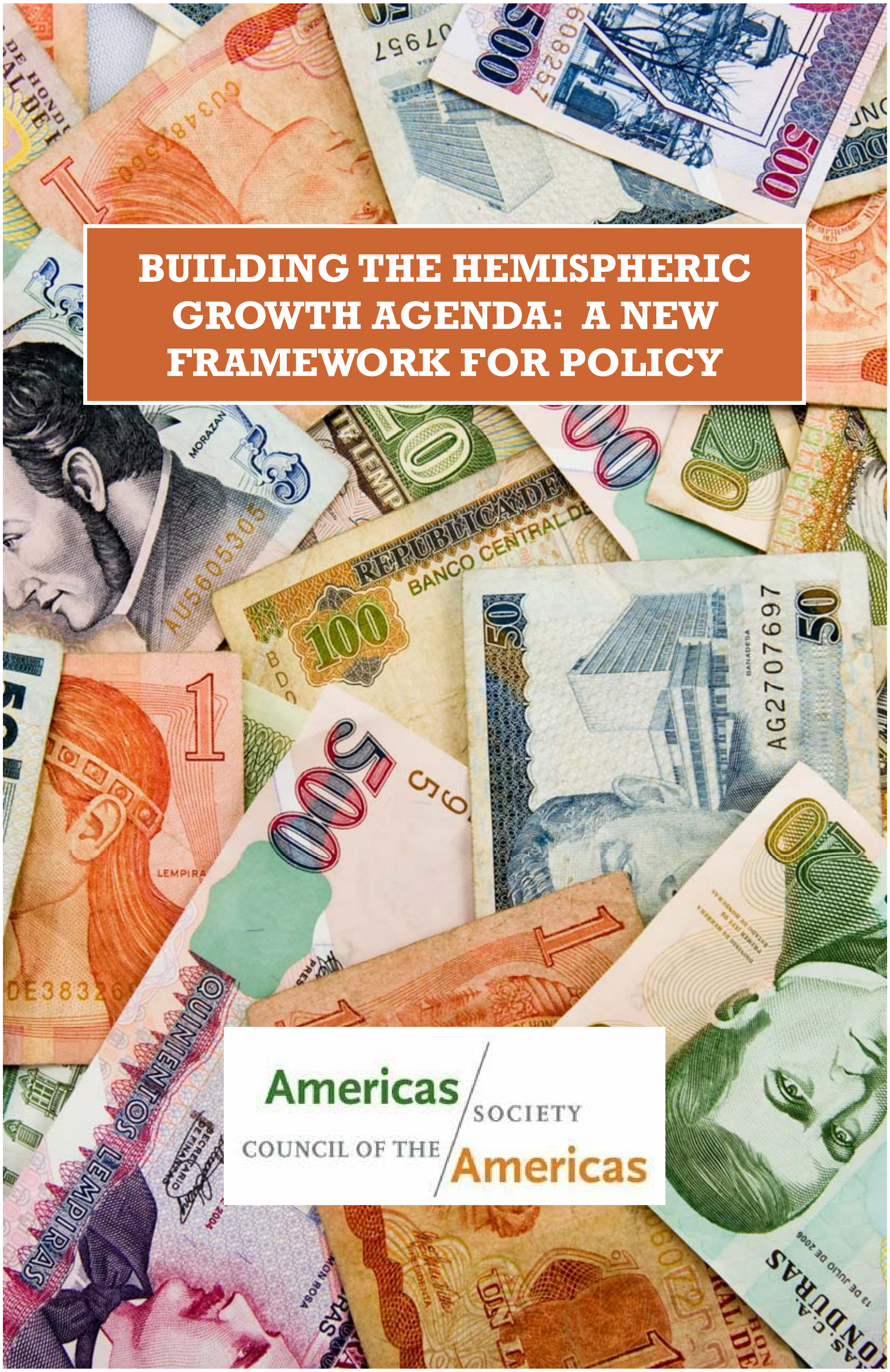
BUILDING THE HEMISPHERIC GROWTH AGENDA: A NEW FRAMEWORK FOR POLICY



Americas Society
Council of the Americas

BUILDING THE HEMISPHERIC GROWTH AGENDA: A NEW FRAMEWORK FOR POLICY

Report of the Trade Advisory Group
Americas Society and Council of the Americas

FOREWORD

As leaders prepare to gather at the next Summit of the Americas in Trinidad and Tobago in April 2009, they will be faced with the challenge of how to recharge a hemispheric growth agenda within the reality of global economic turbulence, even as regional politics have become less predictable. The agenda must be focused, achievable, and based on mutual self-interest. At the same time, the Summit will be the first opportunity most hemispheric leaders will have to meet and take measure of the new US president, providing the White House with an important opportunity to signal the tone and substance of its evolving hemispheric plans.

With this in mind, the Americas Society/Council of the Americas has brought together leading trade policy experts to come up with ideas on how the incoming administration and Congress can use trade expansion as a tool to build the hemispheric growth agenda. Throughout 2008, the Americas Society/Council of the Americas held a series of focused, by-invitation roundtable policy discussions which explored specific topics with the potential to broaden thinking about what constitutes a hemispheric growth agenda. These discussions sought to move beyond the existing trade and investment agenda while looking to pinpoint sectors where further integration would provide the greatest impetus for growth with equity.

The following document is intended to give policy makers a head start on the issues that will face them and to suggest effective ways to address these issues. It is designed for the most senior policy makers in both the executive and legislative branches, and is offered in hopes of contributing to a positive hemispheric agenda based on pragmatism, shared values, and mutual respect.

Special mention for this report should go to the members of the working group, listed separately, as well as to A. Michelle Morton of the Council, who served as the primary project coordinator. Special note must also be made of documents and statistical information that the UN Economic Commission for Latin America and the Caribbean provided. Finally, we wish to thank the Board and members of Americas Society/Council of the Americas for their continued support, and President and CEO Susan Segal for her outstanding leadership and wise counsel in the production of this report.

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Vice President
Americas Society/Council of the Americas
January 2009

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"There is always one moment...when the door opens and lets the future in."

Graham Greene
The Power and the Glory

"When goods don't cross borders, armies will."

Attributed to Cordell Hull
US Secretary of State 1933-1944

EXECUTIVE SUMMARY

The global economic downturn, the pending Fifth Summit of the Americas in April, and the US presidential transition and new Congress all suggest that now is a propitious time for a re-evaluation of hemispheric trade policy and broader US relations in the Americas.

Circumstances have changed dramatically since the last US presidential transition in 2000. Economically, much of the hemisphere is better prepared to weather the severe financial crisis as reforms have taken hold and commodities exports, at least until recently, supercharged growth. The rise of China, India, and other emerging markets has forged a secular change in regional trade and investment dynamics. Democracy remains the accepted organizing framework for hemispheric governance, even as anti-democratic steps in some countries argue against complacency.

"Circumstances have changed dramatically since the last US presidential transition."

Unfortunately, the comprehensive, consensus-based Summit of the Americas agenda has long since broken down, a reality ratified in 2005 at the last Summit in Mar del Plata. Much of Latin America is now attempting to forge its own path in the global economy. At the same time, the United States' ability to drive hemispheric trade expansion has become more difficult as the US electorate turns increasingly inward. More broadly, the United States, preoccupied with a post-9/11 security agenda, has seen much hemispheric goodwill dissipate, though countries remain hungry for access to the US market and flows of foreign direct investment (FDI).

With roughly 33 percent of the regional population continuing to live in poverty, the need for a broad hemispheric growth agenda is critical, even more so during a time of economic uncertainty and stress. Trade expansion remains a critical tool to promote growth. While other nations have stepped in to fill the void on certain issues, nuanced US leadership remains essential.

Trade expansion does not occur in a vacuum, nor is it sufficient in and of itself. A spirit of goodwill and mutual interest must first exist, and the new administration should consider several steps early on that will build a positive atmosphere prior to the Summit. Among them: the naming of a Special Envoy for the Americas, support for Brazil and Mexico (and Spain) to join the G8, passage of pending trade agreements with Colombia and Panama, support for additional recommendations to reduce the effects of financial shock across the region, and a softening of the most punitive measures targeting Cuba, including visits, exchanges, and remittances.

The Summit agenda should focus on specific priorities, including energy security and climate change, financial well-being, microeconomic reforms, and capacity building and workforce development. All of these must go hand-in-hand with trade expansion as part of a longer term growth agenda, as must an effort to engage more actively with Brazil. Efforts on climate change and energy security, a game changer in the context of hemispheric relations, should be led initially by a subgroup of willing nations.

The trade agenda itself must also be reconsidered. As a practical matter, competitive liberalization has reached a point of diminishing returns. Nonetheless, given the importance of trade expansion to a successful growth agenda, momentum must be restored. Other nations are moving forward aggressively, expanding market opportunities for Asia, Canada, and Europe often at the expense of the United States.

Although the Free Trade Area of the Americas (FTAA) proved too ambitious for its time, it should remain a longer-term goal of the United States. In the meantime, the harmonization of the rules of origin within existing US trade agreements would be a useful place to concentrate trade expansion energies, and existing efforts to increase global competitiveness such as the Pathways to Prosperity in the Americas and the North American Security and Prosperity Partnership should be broadly continued. As well, given the growing promise of Asian trade with the Americas, the Trans-Pacific Strategic Economic Partnership is an exciting initiative that the Council has strongly advocated. It is perhaps the most promising recent initiative to kick start *hemispheric* trade expansion and should be prioritized by policy makers.

Additional comprehensive bilateral trade negotiations are unlikely to prove successful in the near term given prevailing political and economic conditions. A new path forward must be found. Nonetheless, trade remains a critical tool to promote a regional growth agenda, and numerous alternative areas of promise can be pursued. With a new US administration and Congress and the Fifth Summit of the Americas in April, now is the best time to begin.

BUILDING THE HEMISPHERIC GROWTH AGENDA

The Fifth Summit of the Americas, to be held in April 2009 in Port of Spain, Trinidad and Tobago, provides an important opportunity to build on a generation of enormous progress in hemispheric development. Although anti-democratic actions in some countries argue against complacency, democracy remains the accepted organizing framework for hemispheric governance. After years of economic stagnation and questionable policy choices, much of the region has begun to emerge as a stronger player in the global economy. Numerous countries have taken real steps to stabilize inflation and reduce official debt, diversify exports, and promote investment while attacking poverty head on. Growth has been steady. Citizens' lives have improved.

> *"If expectations are kept realistic, the agenda is focused, and the approach is collaborative, the Summit could very well become the foundation upon which a revitalized hemispheric policy is built over time."*

Nonetheless, the future is not guaranteed, especially given the global financial downturn. Initially, many in the Americas thought they might escape being drawn into the vortex of the financial crisis. Despite being better prepared in some cases than ever before, they too have now been affected. All too real is the risk of retrenchment, mounting anti-globalization sentiment leading to protectionist measures, and, in some countries, additional pressure for populist change as growth stagnates.

Significant thought must be given now to building a regional agenda that reflects these new challenges while seeking to take advantage of the opportunities they present. If expectations are kept realistic, the agenda is focused, and the approach is collaborative, the Summit could very well become the foundation upon which a revitalized hemispheric policy is built over time. The time is ripe for a review of where we are and where we need to go next.

> *"Significant thought must be given now to building a regional agenda that reflects these new challenges while seeking to take advantage of the opportunities they present."*

Changed Circumstances Require a Revised Approach

Nearly two decades after the launch of the Enterprise for the Americas Initiative (EAI) and 15 years after the first Summit of the Americas in Miami, the hemisphere is divided, the global economy is troubled, and the ability of the United States to exercise leadership, while significant, is reduced. In its original form, the EAI had three main components: the negotiation of free trade agreements in the hopes of establishing an FTAA; the adoption of measures to increase capital flows to the region; and a conditional debt-relief program. The EAI was essentially incorporated into the expanded Summit of the Americas agenda. The FTAA, which sought to join 34 countries of greatly diverse levels of development into a reciprocal agreement, proved to be overly ambitious. To keep the hemispheric trade agenda moving forward, the United States pursued a strategy of competitive liberalization by negotiating bilateral free trade agreements. Without finding a way to attract Brazil, this strategy has now reached a point of diminishing returns, and few additional countries seek to join the FTA queue.

A palpable discomfort with global economic change has the US and hemispheric electorates on edge, reducing political desire for additional trade expansion efforts. Where once the United States was able to ignite the hemispheric imagination by concluding the North American Free Trade Agreement (NAFTA), now the idea that NAFTA is to blame for much US economic frustration has become conventional if misguided wisdom. Other agreements, including those with Colombia and Panama, both of which serve the strategic and economic interests of the United States, have been sidetracked. US credibility and economic and security interests have suffered as a result. Beyond trade relations, the United States has seen much hemispheric goodwill dissipate given its preoccupation with a post-9/11 security agenda. Though most countries remain hungry for access to the US market and flows of FDI, they have also sought to diversify their options.

The broader world has also changed dramatically since the launch of the EAI and the first Summit in Miami. The explosive rise of China, India, and other developing nations has fundamentally changed global finance and patterns of trade. Commodities producers, particularly in South America, have benefited handsomely. At the same time, some nations, enjoying historically high prices for their products, remained complacent, unable, or unwilling to take additional steps that would more effectively prepare them for the inevitable economic downturn that has now arrived. They preferred the politically less costly course, a bet on a continued secular rise in the commodities trade.

Yet even when times are good, no successful international development strategy has ever emphasized long-term reliance on primary goods rather than a concerted effort to move up the value-added production chain. Global supply chains are a key to growth in modern business operations, and within this context Latin America and the Caribbean are competing not just among themselves but also with the most competitive producers globally. Hemispheric growth thus requires attention to domestic factors that build national capacity beyond the export of primary commodities. Nations are finding that in order to succeed in the global economy they must also do more. Reforms in areas such as tax policy, market regulation, infrastructure, education, climate change and energy policies, and effective application of the rule of law are also critical to their ability to compete.

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Development Remains the Goal

Arguably, trade expansion and enhanced access to the US market—while vitally important—are no longer sufficient political catalysts to promote such a comprehensive hemispheric growth agenda. Yet these issues are of pressing concern because Latin America still has about 182 million people living in poverty, roughly 33 percent of the population. The global financial crisis will exacerbate their plight, which could well have broader political implications.

Hoping to spur growth for the impoverished even before the financial crisis, several countries have returned to the intellectually comfortable but discredited models of the past that emphasize resource nationalism, import substitution, and a populist, state-centered approach to development. Political radicalization in the hemisphere, even among some countries with which the United States maintains formal free trade agreements, means that hemispheric policies built on expanding trade and investment—no matter how well-designed or worthy—will not likely succeed absent a broader approach to development. A pragmatic approach must therefore be found that takes into account hemispheric realities as they are, rather than default to an abstract idea of how we would envision a perfect hemisphere to be. It is time to develop a new vision and to focus US policy efforts on building broader consensus in the promotion of a "trade-plus" hemispheric growth agenda.

Getting Started: Revitalizing US Engagement in the Americas Even Before the Summit

Nuanced leadership on the part of the United States remains essential for the hemisphere to address the challenges it now faces, no matter how much the US "brand" may have been sullied. That said, leadership should be softer spoken, with an emphasis on listening and partnership, and should seek to incorporate the legitimate priorities of the hemisphere.

With this in mind, the new US administration could take several actions as an early gesture of goodwill prior to the Summit that would create a more positive atmosphere for the Summit itself. For example, during the transition the US president-elect should name a new White House Special Envoy for the Americas. In the wake of the G20 meeting in Washington, he should announce that the United States would support the inclusion of Brazil, Mexico, and Spain in the G8. The new president will not want to arrive at the Summit empty handed; he should ask Congress to pass pending trade agreements with Colombia and Panama by the time of the Summit. He should ask his Treasury Secretary to develop specific recommendations to mitigate the effects of financial shock in the region. Finally, the clearest way to electrify the hemispheric community in advance of the Summit—the first to be held in the Caribbean—would be to soften the most punitive measures targeting Cuba, including visits, exchanges, and remittances.

> *"The new president will not want to arrive empty-handed; he should ask Congress to pass pending trade agreements with Colombia and Panama by the time of the Summit."*

<u>The Summit Agenda</u>

At the Summit itself, several productive actions could usefully be pursued by the new US administration, even under difficult global economic conditions. Building on the draft documents prepared for the Summit, the United States should promote a hemispheric agenda focused on energy security, climate change, financial regulation, and workforce development. A number of these issues will have to be dealt with in a global context, but moving forward within a regional context consistent with the Summit agenda can nonetheless be an important means to advancing global discussions.

Energy Security and Climate Change

Energy security and climate change are a game changer. Among existing energy partnerships in the region, the most significant for the United States are ties with its NAFTA partners Canada and Mexico, and also Venezuela and Trinidad and Tobago. At the same time, development of new deepwater oil and gas resources could confirm a global leadership role for Brazil in traditional energy supplies. Brazil is already a global leader in biofuels. As a starting point to greater regional integration, the United States and other willing partners across the hemisphere, perhaps as an E4 or E5, should join together to formulate a mutually beneficial hemispheric energy agenda roughly analogous to the original European Coal and Steel Community. Technical assistance, technology transfer, capacity building, and infrastructure development financed in part by the Inter-American Development Bank (IDB) could be a means to generating a regional energy agenda.

Energy and climate change cooperation may in fact be one of the most effective issues on which to successfully expand engagement with Brazil, Latin America's largest economy. Bilaterally, the United States and Brazil are already working to address energy security and decrease their dependence on traditional fuels by promoting ethanol markets and refining capacity in the region, beginning with Central America and the Caribbean. A natural policy for the new administration would be to seek the gradual elimination of the 54 cent per gallon secondary tariff on imported ethanol. Another might be consideration of a civil nuclear deal with Brazil similar to the one the United States has with India. Brazil is one of a handful of nations that voluntarily abandoned the development of nuclear weapons, yet it maintains an active nuclear program for peaceful purposes. Cooperation here could also have broader national security implications, possibly leading to a next generation "atoms for peace" program for the hemisphere, and proving to be a positive model for hemispheric energy aspirations.

The new US administration should also announce its desire to seek a common agenda on climate change through active consultations with Western Hemisphere nations prior to the December 2009 global climate change meeting in Copenhagen. A hemispheric approach to climate change that includes Brazil might also encourage other carbon-emitting nations, such as China and India, to make appropriate commitments.

Financial Well-Being

Undoubtedly, the Summit will also need to address the hemisphere's financial well-being. As new regulations are developed in the midst of the ongoing global financial crisis, the United States must show a willingness to consult and cooperate with its partners in the Americas. Principles must be developed for a strategy to manage future financial market disruptions. The following should be considered: increased policy coordination among central banks; an early warning system for financial difficulties; appropriate standards for capital liquidity in financial institutions; and regular hemispheric ministerial consultations at the margins of the IMF/World Bank meetings.

> *"A hemispheric approach to climate change that includes Brazil might also encourage other carbon-emitting nations, such as China and India, to make appropriate commitments."*

At the same time, broader hemispheric integration and a growth agenda depend on the seamless flows of capital to their most productive uses. Market signals are critically important to those making the innumerable private decisions to deploy capital, or not, that occur every day in the hemisphere. Increasing the number of high standard dual-tax treaties, particularly a long-discussed treaty between the United States and Brazil, should be prioritized. The further harmonization of accounting standards and corporate governance rules would also encourage hemispheric economic integration, and would serve as a broader catalyst for the growth agenda.

Microeconomic Reforms

Even as the financial crisis plays itself out over time, attention must also be paid to the microeconomic climate in Latin America and the Caribbean, which continues to pose a significant constraint on regional growth. Companies in the region cite informality and corruption as two top obstacles to doing business. The creation of transparent regulatory and simplified tax systems would do much to reduce these obstacles. Updating economically stultifying labor codes and moving more workers into the formal sector would help provide stability, job security, and the protections of the state to those at the bottom of the pyramid. Common standards for key microeconomic policies affecting both domestic and foreign companies should be designed. Such an approach could bypass the current debate on the merits of trade liberalization and may offer one of the best opportunities to stimulate regional growth.

> *"Even as the financial crisis plays itself out over time, attention must also be paid to the microeconomic climate in Latin America and the Caribbean, which continues to pose a significant constraint on regional growth."*

An agenda for action at the Summit would identify microeconomic policies that should be targeted for improvement, including those for which objective data now exist such as starting a business, obtaining proper licenses, registering property, paying taxes, and accessing credit. Incentives to undertake these reforms could include capacity-building assistance for governments and streamlined access to international loans for the private sector. Such an approach is particularly appealing to smaller countries in the region, countries with large informal sectors, countries interested in expanded supply chains, and countries seeking FDI in manufacturing and services.

Along with bilateral donors, regional institutions such as the IDB, the Andean Development Corporation (CAF), and the Central American Bank for Economic Integration (CABEI) can and should be encouraged to play an enhanced role in these efforts.

Capacity Building and Workforce Development

In addition to microeconomic reforms, enhancing science and technology capacity and related workforce development must be a priority in Latin America and the Caribbean. To remain competitive in the global economy, countries in the region will ultimately have to move beyond commodities-based growth to a knowledge-based economic model. Structural barriers to innovation in the region include poor basic and technical education and lack of public support for private sector research and development. Research and development spending in the region remains strikingly low, particularly in comparison to Asian nations. Domestic incentives including tax relief for basic research, assistance in the commercialization of discoveries, appropriate protection of intellectual property, reduction of barriers to imported technology, and development of domestic venture capital resources could help build a culture of innovation in the region that, to date, has not widely existed. Technical assistance from the United States and elsewhere would be catalytic as a means to address these issues.

Rebuilding the Hemispheric Trade Agenda

All of which brings us to the trade and investment agenda itself. Despite hemispheric currents that hinder forward momentum, trade remains one of the most effective tools available to build and support economic development and growth with equity. Freer trade is one of the strongest tools available to promote regional development, and a critical means to encourage and underwrite political, economic, and social reforms. Limiting trade is certainly an option, but it is not a good option. Backpedaling from the broader trade agenda would encourage protectionist forces from all sides, including the business community, to reassert monopolistic positions in local markets. (Similarly, backpedaling by some nations on investor rights, including access to neutral international dispute resolution mechanisms, would raise investor risk significantly and reduce trade and capital flows—the lifeblood of development—in an already capital-restricted global marketplace.)

At the same time, even as public enthusiasm in the United States for trade has waned, other nations continue to move ahead. For example, some 15 trade agreements will link five Latin American countries with 11 Asian economies by 2010, in addition to the 10 hemispheric nations that have already implemented agreements with the United States (not counting Colombia and Panama). A group of Latin American nations calling themselves the Arc of the Pacific has also banded together to develop a joint strategy for approaching Asia. The United States is not a party to many of these negotiations, and each new agreement provides preferential access to Latin American markets for nations competing directly with the United States, including China, the European Union, and Canada.

With this in mind, the new US administration should continue to pursue trade facilitation initiatives to keep the agenda moving forward while side-stepping political land mines where possible. Within existing processes, trade liberalization in areas that support the broader hemispheric development agenda, including, for example, green technologies, alternative energies, energy infrastructure and services, and education services, should be fast-tracked.

> *"Freer trade is one of the strongest tools available to promote regional development, and a critical means to encourage and underwrite political, economic, and social reforms."*

The FTAA proved too ambitious initially but should remain a longer-term goal of the United States. In the meantime, a useful place to concentrate would be in pushing hard for the harmonization of rules of origin contained in US agreements with Latin American countries and Canada. Existing trade preferences programs might also usefully be harmonized. Efforts to increase global competitiveness such as the Pathways to Prosperity in the Americas and the North American Security and Prosperity Partnership should be broadened.

Additional initiatives to include appropriate Asian nations must also be considered. The 21 member economies of the Asia-Pacific Economic Cooperation (APEC) forum have agreed to study prospects for a Free Trade Area of the Asia Pacific as a long-term goal, and Colombia should be permitted to join the group as Canada, Chile, Mexico, and Peru already have. A promising step to advance this vision was the announcement that the United States will enter negotiations to join the Trans-Pacific Strategic Economic Partnership, including the P4 nations of Brunei Darussalam, Chile, New Zealand,

and Singapore. Australia and Peru made commitments during the 2008 APEC Leaders' Meeting in Lima in November to participate in negotiations to expand the agreement. Vietnam has also expressed an interest in joining but has not yet committed to do so. Additional APEC countries have been invited to participate as well.

"The Trans-Pac could well be the most promising future driver of hemispheric trade expansion, given the desire of many nations in the region to link more closely with Asia, the coincidence of interests with the United States and Canada, and the high-standards approach that the original parties have promoted through the agreement."

In fact, the Trans-Pac could well be the most promising future driver of *hemispheric* trade expansion, given the desire of many nations in the region to link more closely with Asia, the coincidence of interests with the United States and Canada, and the high-standards approach that the original parties have promoted through the agreement. By engaging with those parties in the pan-Pacific region who truly want to expand trade and investment in a forward-looking manner, this vehicle provides an outstanding opportunity to build the hemispheric trade and investment agenda as additional countries seek to be included. It should be given priority in the advancement of hemispheric policy.

Conclusion

Hemispheric trade expansion must be seen to be and must in reality be a tool that supports a broader growth agenda. Despite the considerable merits of trade expansion, the political reality is that in the aggregate, people in the Americas, including the United States, must perceive that trade expansion is in their interest or else such efforts will be unsuccessful. To keep the momentum going, a new path forward must be found. With a new US administration and the next Summit of the Americas in April, now is the right time—beginning with the recommendations in this report—to begin.

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Council of the Americas (COA) is the premier international business organization whose members share a common commitment to economic and social development, open markets, the rule of law, and democracy throughout the Western Hemisphere.

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