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Brazil's Foreign Economic Policy: South – South, North – South or both?

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1 Introduction

Since he came into office on 01 January 2003, the new Brazilian president Luiz Inácio "Lula" da Silva has promised continuity in his foreign policy objectives and priorities while setting some different emphasis than his predecessor Fernando Henrique Cardoso. Seeing foreign trade as an essential instrument for economic development and the reduction of external vulnerabilities, Lula's main concern is to achieve a more equitable international order through an active engagement in regional and global partnerships. He wants trade liberalisation to go hand in hand with social justice. Trade should not only be free, but also fair.

This paper examines Brazil's foreign economic policy under president Lula da Silva and pays special attention to Brazil's role within a changing international context of new constellations in North-South and South-South economic relations. [1] These new elements became obvious through active players in the World Trade Organization (WTO) like China, India, Brazil and South Africa, who established the G-20, a group of developing countries that insists on becoming more involved in setting the rules of world trade. Especially since the collapse of the 5th WTO Ministerial in Cancún in September 2003, there is a new capacity and willingness amongst countries of the Southern Cone to form a united front based on coalitions or joint actions. Brazil is actively involved in those efforts. "The emergence of the G-20 […] has demonstrated that the time of deals negotiated between the major powers and then passed on to the rest of the membership for minor adjustments is past", said Luiz Felipe de Seixas Corrêa in his candidate statement during the WTO Director-General selection process. But can intensified South-South cooperation enhance trade and even the negotiating weight of the states involved? And how do Brazil's traditional trading partners, the European Union (EU) and the United States, react to those ambitions?

Brazil faces a very difficult challenge in negotiating simultaneously on several international fronts: at the WTO, the Free Trade Area of the Americas (FTAA), an Association Agreement between Mercosur and the EU and within Mercosur itself. The overlap of various agendas for parallel negotiations means an uncertainty of results. Apart from the analysis of those negotiations, some special aspects of Brazilian domestic policy have to be examined in this paper as well in order to see if Brazil's foreign trade policy is integrated into a sound domestic policy framework and follows a coherent national strategy.

As the title of this paper already indicates, this study will have two parts: Brazil's relations with the South, i.e. to the developing world, and Brazil's relations with the industrialized countries of the North.[2] The next chapter will include an overview of some possible strategies a country can pursue concerning its foreign economic policy.

2 The options: bilateral, regional and multilateral trade negotiations

After the collapse of the 5th WTO-Ministerial in Cancún, bilateral free trade agreements (FTAs) have expanded exponentially. The number of FTAs will continue to rise simply because the economies concerned want to move quicker than in the WTO-framework. On the other side of the argument, the question of exclusion is raised because the faster bilateral trade deals render irrelevant the most-favoured-nation-clause (MFN), the basic principle of the World Trade Organization, under which the conditions granted to one country apply equally to all member states. Therefore, FTAs are by definition discriminatory. Furthermore, there are asymmetries if a developed and a developing country negotiate a FTA because of the often substantial differences in bargaining power. In particular, the United States are pushing forward bilateral trade agreements. There is a serious desire by the US to have access to the services markets of developing countries, and also to get those countries to agree to rules favouring the protection of intellectual property and rules covering foreign direct investment. Developing countries for their part want to secure market access to the large industrialized countries' markets. They

[1] South-South trade is increasing at an annual rate of 10 %, more than twice the rate of expansion of world trade in 2003. Especially in Asia South-South trade is moving at full speed.

[2] Following UNCTAD's definition, "developed or industrialized countries" are: the countries members of the OECD, "transition economies" are: the countries of Central and Eastern Europe, the Commonwealth of Independent States (CIS) and the Baltic States and "developing countries" are: all countries, territories or areas not specified above. See definition of UNCTAD in *Trade and Development Report 2004*, p. xi. Although not all OECD countries are in the northern hemisphere (i.e. Australia) and not all developing countries are on the southern part of the globe, the OECD-countries are in this paper referred to as "the North" and developing countries as "the South". This simplification is undertaken to underline the Brazilian president's ideological element in his foreign economic policy.

also see an opportunity for increasing foreign direct investment in their respective countries.

Apart from the more recent phenomenon of bilateral trade agreements, the last decade has also witnessed a spectacular increase in the number of Regional Trading Agreements (RTAs). However, it is still unclear whether those represent "building blocs" or "stumbling blocs" in the development of a more globally integrated market economy. The proliferation of regional trade agreements is fundamentally altering the world trade landscape. The number of agreements in force nowadays surpasses 200 and 40 percent of global trade takes place among countries that have some form of reciprocal regional trade agreement. RTAs imply new trading opportunities for developing member countries and they can complement unilateral and multilateral policies. But one should not overlook the effects RTAs can have on excluded countries because preferences for some countries mean discrimination against others who are not members of those "exclusive commercial clubs". This can even result in a disadvantage for a member country of a RTA: Many regional agreements cost the economy more in lost trade revenues than they earn, because they discriminate against efficient, low-cost suppliers in non-member countries. The World Bank's report on "Global Economic Prospects 2005" states that not all regional agreements create new trade and investment.[3] Especially those with high external border protection are particularly susceptible to the adverse effects of trade diversion.

The average Latin American country belongs to eight agreements. This creates a "spaghetti bowl" of overlapping arrangements with little transparency and coherence. Each agreement has different rules of origin, different tariff schedules, and different periods of implementation, which complicates customs administration.

The report states further that in general, North-South agreements score better on implementation than South-South agreements. This is because North-South agreements can integrate economies with distinct technological capabilities and other different factor proportions and therefore the potential gains are usually greater. This does not mean, however, that there are no potential win-win situations in FTAs and RTAs being negotiated amongst developing countries.

To sum up, RTAs are proliferating and now cover one third of world trade, but their liberalizing effect has often been modest. RTAs accounted for only about 10% of the fall in developing countries' average tariffs in the past 20 years. RTAs and FTAs have not benefited all their signatories. Although preferential trade agreements could in theory help developing countries to expand their export markets, to raise economic efficiency and to deepen regional policy co-operation, poorly conceived deals have often prevented those gains from being realised. Positive results are not automatic and depend critically on the design of each treaty.

Parallel to FTAs and RTAs, 148 member countries of the World Trade Organization are involved in the Multilateral Trading System. The WTO, an intergovernmental institution, is the only negotiating forum in which the needs of developing countries can be given full weight. Every country, no matter how small or poor, has a veto. The Doha Development Round was launched in November 2001 specifically to help poor countries. They will be the biggest victims if the negotiations do not lead to results. However, the Multilateral Trading System can only provide frameworks and opportunities for development. Other important conditions have to be met domestically. This means that even if the system worked perfectly, it would still require the right domestic policies to take advantage of the opportunities offered.

The World Bank report states that RTAs are no alternative to multilateral liberalization because gains for developing countries are usually only a fraction of those from full multilateral liberalization. Therefore, developing countries have a powerful collective interest in an effective and successful Doha Development Round. A successful Round would lower the risk of trade diversion for members and eliminated the negative effects on excluded countries from bilateral or regional deals. Therefore, the report suggests that developing countries should see regional integration as one element in a three-pronged strategy that includes unilateral, multilateral, and regional liberalization.

The important question in this context is in favour of which options Brazil decides concerning its foreign economic policy: How much importance does Brazil give to multilateral negotiati-

[3] See "Global Economic Prospects – Overview and Global Outlook 2005", edited by *The International Bank for Reconstruction and Development / The World Bank*.

ons and which aims does it pursue within its institution, the WTO? Brazil is involved in the preferential regional agreement Mercosur and is currently negotiating an inter-regional agreement between Mercosur and the European Union. Therefore the question about Brazil's role within those negotiations arises. Is Mercosur adequate to push Brazil's trade forward and to strengthen its negotiating power with respect to the North?

3 Brazil's foreign economic relations

While Brazil's export performance was disappointing during the 1990s this trend was reversed after the major devaluation in January 1999, which marked the start of a period of sustained currency weakness. The trade balance swung back into surplus in 2001 for the first time since 1993 and record export earnings were achieved in 2002-2003.[4] In 2003 primary products performed strongly, boosted by robust Chinese demand for soya and iron ore, but exports of manufactures also recovered, led by cars. Between 2002 and 2004 the main industrial items exported by Brazil were civil aircraft, vehicles and parts, steel, chemicals, machinery, electric equipment, paper, pulp, and footwear. As for commodities, soybeans, ores, oil, meat, coffee, sugar and tobacco maintained a leading share. Fruits, maize and cotton have raised their share in the total exported.

Lula's fiscal restraint has not only produced a healthy current account surplus, but also encouraged investment to flow back into the country. In the second quarter of 2004, Brazil's economy grew by 5.7 percent compared with the same period last year – the third successive quarter of strong growth.[5] This provides Brazil with more possibilities to pay its external debt, which in turn would lead to a higher credit rating, lower interest rates, faster economic growth and eventually more jobs and higher wages.

An essential part of Brazil's economic policy strategy is to fight hunger and poverty in the country itself and worldwide. Lula's programme "Fome Zero" (Zero Hunger) aimed at eradicating hunger and social exclusion, wants to tackle fundamental social rights such as access to food, education, social welfare, and employment protection.[6]

The Brazilian government sees the active use of trade policy as a means of fostering sustainable economic growth, fighting hunger and poverty and reducing the country's vulnerability with respect to global financial markets. Regional economic integration and export diversification are therefore considered important policy targets. Brazil's essential goal is to obtain enhanced market access for its agricultural products through multilateral and regional negotiations while at the same time developing its manufacturing sector. The country has the potential to become a giant in industry and agribusiness, in the technology of uranium enrichment, and in biotechnology since it has immense biological reserves and an extremely mineral-rich soil.[7] According to the WTO's Trade Policy Review "Brazil", further liberalization would promote greater competition and efficiency and help ensure sustainable growth.[8] Brazil would gain by addressing remaining economic distortions and barriers to market access. The tariff continues to be Brazil's main trade policy instrument. The average applied MFN tariff decreased from 13.7 percent in 2000 to 10.4 percent in 2004.

In parallel to the growth in export volumes, Brazil has diversified its trading partners. While Brazilian exports between 2000 and 2003 to its traditional trading partners the USA and Europe rose by 26.4 percent and 24.9 percent respectively, regions with a hitherto small share in Brazil's trade were significantly higher: exports to Africa increased by 112.3 percent, the Middle East, 109.7 percent, Eastern Europe 108.6 percent and Asia 84.6 percent.[9] While in 2003 Brazil exported to Mercosur and the US mostly manufactured goods, the European Union and Asia

[4] That helped to turn a current account deficit, which had peaked at $ 33 billion in 1998, into a surplus of $ 4 billion in 2003.

[5] See "To Lula's credit", in: *The Economist*, September 2nd 2004. For 2005, an economic growth between 3.5 percent and 4 percent is being projected by Bloomsberg.

[6] In the long run 46 Million Brazilians are to be relieved from hunger. Social programmes with a view to attain reduction of poverty and social inequalities and a reallocation of public expenditures have been put into practice.

[7] See Tachinardi, Maria Helena: Brazilian Food Needs Only a Chance, Globalization Insights 2005, FES Berlin.

[8] See Trade Policy Review "Brazil", http://www.wto.org/english/tratop_e/tpr_e/-tp239_e.htm from December 2004.

[9] See *WTO-Trade Policy Review, Government Report by Brazil*, November 2004.

absorbed mainly primary products. The expansion of Brazil's foreign trade has helped the country to better integrate into the global economy, although Brazil still accounts for only 1 percent of world trade. Therefore better market access, especially for agricultural products, is Brazil's priority.

Brazil looking South

Deeper integration in South America?

In South America, the Brazilian president Lula da Silva explicitly wants to assume and exercise political leadership and strengthen Mercosur. This regional integration initiative, launched in the early nineties by Brazil, Argentina, Uruguay and Paraguay, is perceived as the platform from which regional leadership must be further built and exercised.[10] Mercosur has preferential trade agreements[11] with its associate members Chile, Bolivia, Peru, Ecuador, Columbia and Venezuela.[12] In October 2004, Mercosur has signed an agreement with the Andean Community of Nations (CAN)[13], which has the potential to become the world's fifth largest trade bloc. Furthermore, in July 2002, a partial scope agreement providing for free trade in the automotive sector was signed between Mercosur and Mexico, which also announced its intention to apply for becoming a Mercosur associate member. It seems that Brazil's relations with Chile are developing particularly well. At the end of August 2004, Lula signed a number of agreements in Santiago de Chile increasing Chile's access to the Brazilian agricultural and agro-industrial market.

Apart from those new trade deals, Brazil's intentions to push forward and strengthen Mercosur became obvious through financing projects of the *Banco Nacional de Desenvolvimento Econômico e Social (BNDES).* Furthermore, Brazil tries to achieve more convergence regarding Mercosur's Common External Tariff (CET). These efforts are undertaken to achieve a deeper regional integration – especially in the fields of infrastructure, transport, energy and telecommunication. More integration – so the Brazilian strategy - should then result in enhanced power in the negotiations with the European Union and the United States. But Mercosur is accompanied by setbacks and many difficulties. It is still an "imperfect customs union", no real free trade zone and it has no common market. The "Common" External Tariff has 800 exceptions and exporters to Mercosur often pay double-tariffs: once on entry into Mercosur and again at the border with the destination country.

In 2004, relations between Brazil and Argentina worsened because Argentina protected its domestic production from some Brazilian imports through special safeguard mechanisms. Brazil itself provides cheap finance to its own exporters and has a system of trade and investment incentives, a practise that adversely affects Argentine industry.[14] Most probably the solution to this conflict will be the introduction of quotas and limits for imports of "sensitive" products. The problems with Argentina have aroused a lot of criticism in Brazil's business community calling Mercosur a "suitcase without a handle" – because a suitcase that has no handle is obviously very difficult to carry around.[15]

Apart from Mercosur, Lula tries to strengthen its own sub-continent in an initiative which aims at building a new political union, the "South American Community of Nations". On 08 December 2004 twelve Latin American countries established this union in Cuzco, Peru. This Community has ambitious aims: it wants to follow the European Union and its process of establishing a single market and currency along with a common parliament. A first concrete signal towards more integration is the project for the 1200 km long highway "Transoceánica" linking Brazil to the pacific through Peru. But not all Latin American governments seem to give the same importance to the Community as Brazil does: three of the four Mercosur presidents did not come to Cuzco

10 See Costa Vaz, Alcides: Brazilian Foreign Policy under Lula: Change or Continuity?, Friedrich Ebert Foundation Briefing Paper, April 2004.

11 Since June 2001 Mercosur member countries are no longer allowed to sign individually trade preference agreements with third parties, according to a Common Market Council Decision.

12 On 17 December 2004 at the "Summit of Ouro Preto", Ecuador, Columbia and Venezuela became new associate members with a similar status as the three already existing.

13 The CAN is made up of Bolivia, Colombia, Ecuador, Peru and Venezuela.

14 Brazil protects its beverages, transport equipment, clothing and footwear against import competition and specific financing support programmes have benefited the automobile, shipbuilding and aircraft industries.

15 See Jank, Marcos: "'Suitcase Without A Handle': Brazil's Expression, Mercosur's Fate?", in: *InfoBrazil*, 14 October 2004.

and not everyone is in favour of Brazil's self-imposed leading role.

Economic relations to Asia and Africa: a new geography of world trade?

***China* –** As there is hard competition between the newly industrializing countries of the South, China is a strong competitor for Brazil's manufacturers. On the other hand it is a promising market for its commodities. Trade between Brazil and China has been growing significantly, making China Brazil's third biggest trading partner after the EU and the US, especially for exports as soya beans, iron ore and steel. In May 2004 Lula paid his first presidential visit to China. The meeting of the two giants aimed at searching for a "new geography of world trade". During President Hu Jintao's November 2004 visit to South America, China signed a number of deals with Brazil increasing their already rapidly growing bilateral trade. The Brazilian-Chinese relationship could mark an important shift in world trade, as emerging market economies substitute imports from rich industrialized nations with cheaper products from other developing countries. In the case of Brazil and China this procedure is being simplified by their complementary economies. China's appetite for natural resources and farm products seems insatiable and Brazil can offer both. But there are fears in Brazil that a closer relationship will simply help the Chinese to compete in the world market in manufactures, especially in textiles and the car sector, without bearing the same advantages for the South American country.

India and South Africa - Because of Brazil's leading role within Mercosur, it could play a key role as a link between fast growing India and Latin America. India and Mercosur have already signed a framework trade agreement in January 2004, the first trade deal between Mercosur and an Asian country, which later could lead to a free trade agreement. This is especially important for Brazil as India is one of the world's most protected economies. For Brazil there is the chance to export its huge abundance of primary products that India needs.

Apparently India, Brazil (through Mercosur) and South Africa are confident in leading South-South cooperation. The three have formed the India-Brazil-South Africa Forum (IBSA) since September 2003. A Trilateral Business Council will create the framework under which business people from the three countries can get together and use synergies with the existing Preferential Trade Agreements that Brazil has initiated with India.

In December 2000, Mercosur and South Africa had already signed a framework agreement to negotiate a free-trade agreement. In 2003, the other South African Customs Union members[16] joined the negotiations.

The two previous chapters have shown Brazil's recent initiatives with countries of the South - in Latin America, Asia and Africa. South-South trade has been increasing well above world trade average growth and is becoming a significant source of dynamism for the global economy. There are some initial results in South-South trade with global trade flows reorienting themselves as emerging market economies substitute imports from rich industrialised nations with cheaper products from other developing countries. But the increasing number of South-South agreements does not always necessarily mean an increase in trade flows. Therefore it is very important to examine the trade creating capacity of each new agreement. Brazil's president Lula da Silva emphasized that North-South trade should not be diminished by these initiatives - trade with Europe and the USA absorbs almost half of Brazil's exports - but that new alternatives are necessary to reduce dependencies and to forge an alliance of developing countries which would help them to increase their bargaining power in international and regional organisations.

Critics of South-South cooperation, amongst them many Brazilian business men, accuse the Brazilian government of pursuing deals with other developing countries at the expense of trade with the European Union and the United States. Celso Lafer, professor and ex-Minister for Brazil's foreign relations, made some critical remarks on the present government and its "política-espetáculo".[17] He criticizes especially the creation of an image of radical new beginning in foreign policy. In his book *A Identidade Internacional do Brasil e a Política Externa Brasileira* he attacks the government's rhetoric and the use of the external politics for the internal ideological

[16] SACU members are Botswana, Lesotho, Namibia, South Africa and Swaziland.

[17] See Kuntz, Rolf: "O ex-chanceler e a diplomacia", in: *O Estado de São Paulo* of 05 December 2004.

satisfaction.[18] Lafer argues that many positive achievements credited to Lula's government had already been priorities under ex-president Fernando Henrique Cardoso as, for example, the main concern for the South American integration, for multilateralism and even the emphasis on China, India, Russia, South Africa and on Portuguese speaking countries as Angola and Mozambique. Lafer further criticizes the current government's ignorance of the costs for Brazil from missed export opportunities and markets.[19]

Brazil's engagement in the WTO

Brazil is one of the WTO's most active participants and its actions are geared towards building consensus and preserving the integrity of the mandate agreed to in Doha, while at the same time emphasizing and promoting the shared interests of developing countries. As the third largest exporter of agricultural products worldwide,[20] Brazil has played a leading role in the agriculture negotiations, since the sector remains subject to wide trade distortions and protectionism that hinder Brazilian trade.

The country supports the strengthening of Special and Differential Treatment (S&DT) for developing countries and considers it to be an essential part of an agreement on agriculture in particular to cover food security and vital concerns of rural populations. Brazil is also an active user of the WTO dispute settlement mechanism. This mechanism has become an essential instrument for Brazil to address worldwide market distortions, which affect Brazil's exports and is one important reason for Brazil to further strengthen the WTO. The country has recently reached a victory in a dispute over American cotton subsidies, which were higher than the agreement allowed and thus harmed Brazilian exporters. In 2003, Brazil together with Australia and Thailand, filed a complaint at the WTO against the European Union's subsidised sugar production. The WTO Panel ruled recently in favour of the complainants, concluding that the EU contravened its WTO commitments by subsidising its excessive sugar re-exports of an amount equivalent to imports of sugar from the ACP countries and India (1.6 million tons). Brazil is the largest sugar producer in the world accounting for 16.6 percent of world production in 2002. The subsidised production of sugar by the EU depresses the world market price, which has severe consequences for Brazil. Foreign exchange losses for Brazil as a result of EU sugar subsidies are estimated to be around 500 million US$ per year. In both cases – cotton and sugar – there is still no final ruling. Should the final decision be in favour of Brazil, which is a very probable outcome, Brazil might soon continue using the dispute settlement mechanism - this time against US' subsidies for soybeans.

A very important forum for Brazil is the G-20, a group which was established in August 2003 in the final phase of the preparations of the 5th WTO Cancún Ministerial.[21] Led by Brazil, China, India and South Africa, the G-20 became a powerful voice and a distinctive and new element in the scenario of trade negotiations. Its objective was, and still is, to reach an outcome in the agricultural negotiations which would reflect the level of ambition of the Doha mandate and the interests of developing countries. The G-20 addresses export subsidies, trade-distorting domestic support and market access for developing countries' products. It takes its legitimacy out of the importance in the agricultural production and trade, as it represents almost 60 percent of the world population, 70 percent of world's rural population and 26 percent of world's agricultural exports. Furthermore, the G-20 has the capacity to translate a vast range of developing countries' interests into concrete and consistent proposals. It has developed skills in coordinating its members and interacting with other groupings in the WTO.[22] However, due to the great differences of the leading states Brazil, China, India and South Africa, common positions are not easily reached. India, for example, is more defensive than Brazil concerning "Agriculture" and "Market Access" because it wants to protect is own internal market and is not ready to

[18] See Lafer, Celso: A Identidade Internacional do Brasil e a Política Externa Brasileira, São Paulo: Editora Perspectiva 2004.

[19] The FTAA and an EU-Mercosur trade deal could allow Brazil to increase its exports by 20 percent a year.

[20] Brazil is the leading exporter of soybeans, coffee, orange juice, sugar, beef and chicken.

[21] Today the G-20 is integrated by 19 members: 5 from Africa (Egypt, Nigeria, South Africa, Tanzania and Zimbabwe), 6 from Asia (China, India, Indonesia, Pakistan, Philippines and Thailand) and 8 from Latin America (Argentina, Bolivia, Brazil, Chile, Cuba, Mexico, Paraguay and Venezuela). Colombia, Costa Rica Ecuador, El Salvador, Guatemala and Peru had left the group because of incompatible negotiations with the USA in the frame of the FTAA-negotiations.

[22] See http://www.g-20.mre.gov.br/

make major concessions in these regards. While South Africa has similar offensive positions like Brazil, China differs from those two. China is not as in favour of liberalization as Brazil and South Africa and as a recently acceded member country of the WTO it wants to avoid further obligations and is thus less involved in the G-20 discussions.

Brazil has a large, modern and competitive agricultural sector, but at the same time there are widespread areas of poverty and millions of small farmers living at a subsistence level. Therefore, Brazil has proposed a free-trade agreement among the G-20 developing countries and will continue to press for concessions by rich countries at global trade negotiations.[23] However, there are limitations: Brazil cannot continue fighting against Europe if it becomes its partner through an Association Agreement between Mercosur and the European Union.

The July Package and the Framework Agreement of 01 August 2004 would not have been possible without the active participation of Brazil in the G-20, which contributed greatly to the success in harmonizing conflicting interests in agriculture. On farm trade, the giants USA, EU, Brazil, Australia and India are inching towards compromise. New guidelines were established which might lead to good solutions although the original Doha mandate was more ambitious than the July package. Negotiators agreed to eliminate export subsidies, but they failed to set a date certain. They also committed themselves to substantial reductions in trade-distorting domestic subsidies, but there are no time frames either and no definition of "substantial". Tariffs and other impediments to imports are to be reduced as well, but with the right to declare products as "sensitive" and thereby protect them. The Agreement is important in the sense that it gives the Doha Round-negotiations new drive. It has shown the member countries' willingness to commit and engage in the forthcoming negotiations, especially in "Agriculture", as said by Ambassador Luiz Felipe de Seixas Corrêa.[24]

The Global System of Trade Preferences

Another element in South-South cooperation is the *Global System of Trade Preferences among Developing Countries (GSTP)*, whose third round has been launched at the UNCTAD XI meeting in São Paulo in June 2004.[25] The GSTP is a multilateral trading system which was established in 1988 as a framework for the exchange of trade preferences among developing countries in order to promote intra-developing-country trade. The basic idea was that member countries make concessions - such as the reduction of trade barriers - that they do not have to extend to developed countries. Negotiations are dealing only with non-agricultural goods. It is important to note that UNCTAD, and not the WTO, services the Committee of Participants and provides technical and administrative assistance in setting up the GSTP. There are currently 44 participants and approximately 900 products are covered by the tariff schedules of the participants. All members of the Group-77 are invited to join including China, which is not yet a member of the GSTP. Trade amongst GSTP members between 1960 and 2003 increased from 24 percent to spectacular 43 percent of the world's total trade.[26]

Brazil has taken a leading role within the GSTP as an answer to developed countries' demands that the more advanced developing countries are to take their responsibilities for a fairer international trading system as well helping less and least developed countries to improve their trade performances. Industrialized countries demand that trade between southern countries should be

[23] The Group – despite its prophesized early end of some industrialized countries – still exists: it held two Ministerial Meetings and meets frequently at the level of Heads of Delegation in Geneva. Within the G-20 a group of five countries, Argentina, Brazil, China, India and South Africa, meets at technical level to discuss the WTO-agriculture negotiations.

[24] At the conference "Multilateralism and its Options – A Multi-Stakeholder Approach", 26 November 2004 in Lausanne (co-organized by the Friedrich Ebert Stiftung Geneva Office and the IMD Lausanne, Evian Group).

[25] The second round of the GSTP was concluded in 1998, but the first and second round did not fulfil their expectations. In 2004, two negotiating groups, "market access" and "trade rules", were established to develop negotiating plans in their respective areas. The completion of the third round is foreseen for November 2006.

[26] Cp.: Khor, Martin: "South Leaders launch GSTP new round in optimistic mood", TWN Report São Paulo, 17 June 2004, in: *South North Development Monitor*, 18 June 2004.

more evenly distributed: today only ten developing countries account for 70 percent of south-south trade between themselves.

For Brazil, the GSTP is an opportunity to promote new markets. Yet there are still many constraints on a boost in trade among developing countries: apart from high tariffs, practical constraints such as institutional problems, procedural issues (no transparency of rules and procedures), long customs clearance and a often poor financial and physical infrastructure are considerable.

Brazil looking North

FTAA – negotiations: a lighter version?

In 1994 at the Summit of the Americas in Miami an effort began to unite the economies of the Americas into a single free trade area. The Heads of State and Government of the 34 democracies in the region agreed to construct a Free Trade Area of the Americas (FTAA) reaching from Alaska to Cape Horn[27]. Initially Brazil took a favourable position towards the FTAA-negotiations because it expected substantial gains through access to the US-market. But now negotiations are practically stalling. Apart from the fact that the FTAA-negotiations are not on the US' top priority list at the moment, the US government has made some demanding claims on Brazil. The USA wants to secure strict intellectual property rights (Trips+) and full liberalization in the service sector. Brazil does not want to accept these demands and promotes a "FTAA-light", a flexible 34-country agreement of two speeds allowing the members to assume different levels of commitment in the agreement. The members will agree on a minimum consensus of commercial opening and those who want to go beyond this can sit voluntarily at a parallel table. There are now few obligations to open up areas such as government procurement, services, investment or tougher rules on intellectual property rights, the issues the US wants to see included in the negotiations and not waiting to be dealt in the WTO. Brazil, on the other hand, cares most about farm subsidies, market access and anti-dumping measures, issues the US wants to be excluded from the FTAA negotiations and be dealt with by the WTO talks.[28] This means that the current joint presidency of the final negotiations to conclude the FTAA-negotiations taken by Brazil and the United States has very asymmetrical and polarized positions. Therefore, the United States have offered various countries, amongst them many Latin American countries, bilateral trade deals. With this strategy the USA want to put pressure on Brazil. However, for Brazil there are very practical reasons to prefer multilateral negotiations to those in the frame of the FTAA: in the multilateral context the same results can be achieved without bearing costs that regional agreements like the FTAA would imply because of higher negotiation power on the side of the United States. The other reason why Brazil has an interest in "light" FTAA negotiations is because standing up to the United States' vision of pan-American free trade "compensates" for Lula's own tight economic policies and therefore can be seen as a populist reaction to domestic developments in Brazil. For now, the "FTAA light" is a convenient solution for both, Brazil and the United States, because none of them is obliged to make major concessions in their respective sensitive fields (Brazil: "Intellectual Property" and "Services" and USA: "Agriculture"). Although the negotiations are stalling, the parties have left open the option to take up talks again at a later point. The deadline for the creation of the FTAA was January 2005, a timeframe which could not be met. Now the parties are trying to reach an accord before the next *Summit of the Americas* in November 2005 in Argentina. This will still be a difficult task keeping in mind that Lula will fight for his re-election in 2006 and therefore might not be ready for bigger compromises.

Brazil and the European Union: towards an EU-Mercosur Association Agreement

Brazil's relations to the European Union, its main trading partner, are carried out through Mercosur.[29] Mercosur has been trying to reach the so-called Bi-regional Association Agreement EU-Mercosur for five years since the negotiations were launched officially in June 2000. This agreement is a comprehensive agreement encompassing political dialogue and cooperation aspects apart from commercial issues. For Mercosur, a trade deal with the EU would be very

[27] See http://www.ftaa-alca.org. Spanish: ALCA – Área de Libre Comercio de las Américas.

[28] See Vigevani, Tulio / Passini Mariano, Marcelo: El ALCA Light y el Gobierno Brasilero, Estudios sobre el ALCA No. 20, Friedrich Ebert Foundation Chile, July 2004.

[29] For the EU, Brazil only represents its 11th trading partner worldwide.

valuable because of access to its highly protected agricultural market.

In October 2004, the European Union and the four-nation South American customs bloc failed to reach a deal to create the world's biggest free-trade area embracing nearly 680m European and Latin American consumers, and 11.6 trillion US$ of GDP.[30] A deal would have given a huge boost to trade between the EU and Mercosur from the present 43 billion US$ a year.[31] EU and Mercosur are planning to set up ministerial talks in March 2005 to proceed with the negotiations. At the last negotiations meeting, Mercosur had presented a more restricted and sophisticated offer to the EU than in other negotiation rounds hoping the EU would accept those conditions. In the case the EU did not (as indeed occurred), Mercosur would obtain a delay during which it could realize its other priorities, for example deepening integration in South America. Mercosur's demands for greater access to Europe's beef, poultry and services markets have continued to be stumbling blocks for the negotiations. At the same time the Europeans had offered less liberalisation of agricultural trade than Mercosur had hoped for. Furthermore, the EU's requests for expanded access for industrial goods, services and investment, as well as greater opportunities for European firms to compete for public procurement contacts in Mercosur countries have been an obstacle for the negotiations. The EU pressed for its goods to circulate freely within Mercosur. This would have given the bloc an impulse to finally free trade completely among its own members and by this push Mercosur forward making its own members fulfil their commitments to integration.

Reaching an agreement with the EU could bolster Mercosur's bargaining position with the US in the negotiations for a Free Trade Area of the Americas. There are important political reasons for Brazil to conclude the negotiations showing hereby that Brazil is "closer" to the EU than to the US and the FTAA. Mercosur's trade with the US is 20 percent smaller than with the EU, but it is growing faster. When the US takes up the FTAA talks again, pressure on the EU and fears to lose commerce to the US will rise again.

It is difficult to foresee how the negotiations will develop and when they will be concluded. There are still very high technical difficulties. Next steps might become clearer at the upcoming ministerial conference between the EU and Mercosur in April 2005.

4 Conclusions

Amongst North-South, South-South or both, the answer has to be: both. Having concentrated on South-South relations in 2003 and 2004, the Brazilian president Luiz Inácio Lula da Silva might have to look further North in 2005 as there are unfinished negotiations waiting for results, both within the USA as with the European Union.

The Brazilian administration following Fernando Henrique Cardoso has maintained a position in further opening international commerce and a generally positive attitude towards the industrialized world, but at the same time Lula has been critical towards the developed North and is self-confident in defending Brazil's interests and those of the developing world. This has contributed to the difficulties in the negotiation processes with the EU and the US. While relations both with the United States and the European Union are not very dynamic at the moment, Brazil is not merely "waiting" for the North to move, but on the contrary has been very actively engaged with countries of the South. In South America, Brazil is seeking a leading role. The country has a strong interest in deepening South American integration through two platforms: firstly Mercosur and secondly the newly created South American Community of Nations. Brazil's priorities have shifted from inter-regional interests (Mercosur – EU, Mercosur – USA) to intra-regional priorities within South America. Those options do not exclude each other and Brazil's ideal seems to be to negotiate with the EU and the USA with an expanded and deepened Mercosur bloc.

Mercosur is - despite its problems - a trade creating bloc and only to a small extent trade diverting.[32] It facilitates dealing with region-specific issues – such as transit, water, energy, migration, movement of labour, customs and standards – that are difficult to broach at the global level. Mercosur is therefore seen by Brazil as a useful complement to the multilateral system. But in order to be successful, Brazil should not only

30 See "Still prickly – Mercosur and the EU", in: *The Economist*, 29 April 2004.

31 See "EU-Mercosur: EU presents its completed offer to Mercosur in on-going trade talks", Brussels, Press release from 29 September 2004.

32 Richard Newfarmer at the *Global Economic Prospects 2005 Press Briefing* in Washington D.C. on 16 November 2004.

include new members as recently has happened with Columbia, Ecuador and Venezuela, the new associate members of Mercosur, but build up further pressure on establishing a new paradigm of regional development based on coherent policies agreed by the involved countries. A regional approach could help build policies that promote growth and regional development on a more sustainable basis.

Besides this regional initiative since the early 90s, there can be seen a new and very recent phenomenon: Lula has been carving out a role for Brazil as spokesman for poor countries. Brazil is trying to unite countries of the South to give South-South trade and cooperation new impulses. This grouping together of like-minded countries aims at enhancing negotiating power of the South towards the North and at pushing forward trade amongst developing countries. The Brazilian government has tried to strengthen relations with Asian and a few African countries[33], whose concerns and perspectives regarding the present international scenario are seen as convergent. For Lula there are three different playing fields for pushing forward South-South cooperation:

1. multilaterally within the G-20 principally to gain market access for Brazilian and other developing countries' agricultural products;
2. regionally through Mercosur to deepen integration in South America and to enhance the region's negotiating power and
3. within the GSTP trying to deepen an existing network and hereby enhance trade in non-agricultural goods amongst its members without having to extend those concessions to developed countries.

South-South cooperation from the Brazilian perspective has various aims: firstly, there are trade interests to achieve a diversification of Brazil's export markets. Lula is promoting third world solidarity because developing country markets are increasingly important to an export boom that helps recover the Brazilian economy. Lula needs to fight large income inequalities in his own country by increasing Brazil's GDP. Therefore, he needs more gains from foreign trade. At the same time, he needs to pay Brazil's substantial debts. Although fiscal targets are set and the economy grows, in 2003 and 2004 the surplus of the non-financial consolidated public sector has not been sufficient to cover the increasing debt interest payments. The public debt to GDP ratio increased to 56 percent in mid 2004, from some 49 percent in 2000, which has constrained policy choices.[34] Lula's foreign economic policy is therefore a reaction to the country's growing external vulnerability by trying to diversify trade and secure high export revenues.

There is secondly the aim of strengthening multilateralism by forging new international alliances and coalitions to support development and developing countries. Lula wants to move forward the Doha Development Agenda while trying not to make too many concessions to the North. Tireless he has tried to show the industrialized countries the original aim of the Doha Round, which was initiated to respond to the needs of developing countries.

A third important objective of Brazilian Foreign Economic Policy is to achieve greater negotiation weight and more balanced relations with the great powers EU and USA.

South-South cooperation cannot be a substitute for freer trade with rich countries and is unlikely to pay off very soon. There are still many obstacles to overcome as the lack of interest within the southern countries to trade amongst themselves, preferring instead to build economic bridges with lucrative markets like the United States or the European Community. Weak implementation often afflicts South-South agreements as well as infrastructural problems and hard competition amongst the developing countries. However, for more advanced developing countries like Brazil, South-South trade can be a supplement because those countries find more complementarities in trade with other developing countries. If South-South cooperation is to include a gesture of solidarity and to help least developed countries, bigger developing countries like Brazil have to

[33] Trade negotiations with Morocco and Egypt are to start early this year.

[34] A danger is banks and foreign creditors siphoning off funds as happened in the months before the Brazilian election in 2002 as foreign investors feared a social president Lula. The real crashed down and Brazil got at the fringe of a crisis. A mount in US-interests, falling prices for raw materials and signs that Brazil could leave its careful spending policies and 2002 could be repeated. Other problems are high costs of credits, inefficiencies on the bureaucratic level, corruption, unemployment and a poor infrastructure, which hinder the country to fulfil its potentials. See Henkel, Christiane: "Träum weiter, Brasilien", in: Die Zeit No. 31, June 2004.

take their responsibilities and make their contribution by opening their markets to poorer countries. It will be interesting to observe if concrete preferential measures in favour of LDCs, as foreseen in the GSTP, will be taken.

Lula has raised very high expectations especially in the poor part of the Brazilian population and is in a difficult position in a very heterogeneous country with large income inequalities. He has made many promises he now needs to fulfil if he wants to be re-elected in 2006. In his ardent intent to promote the old idea, fashionable in the Non-Aligned Movement in the 1970s, that poor countries can stand up to rich ones and achieve development by co-operating with each other, Lula hopefully does not achieve the contrary of what he intended: less possibilities to move international trade forward because of hardened fronts, deeper conflicts and hereby blocked negotiations. It will be extremely important to maintain a balance at the different negotiation levels.

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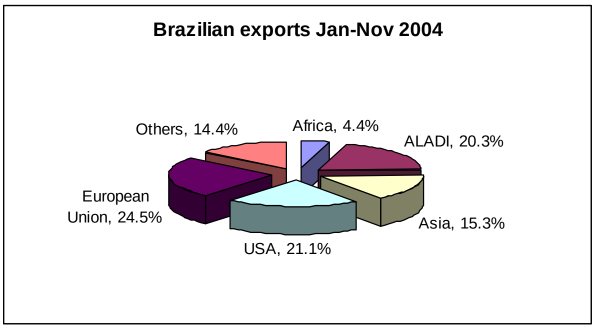
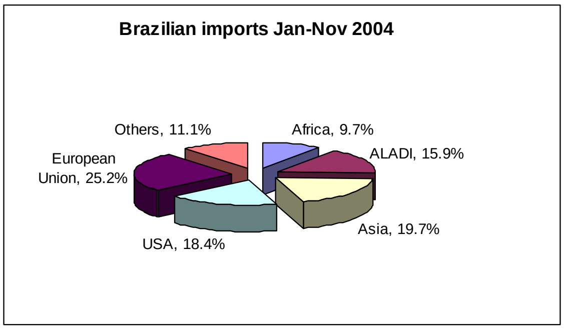
6 Appendix

	Exports		**Imports**	
	Jan – Nov 2003 in million US$	**Jan – Nov 2004 in million US$**	**Jan – Nov 2003 in million US$**	**Jan – Nov 2004 in million US$**
EFTA states	542	636	1120	1237
Africa	2587	3816	3083	5526
ALADI*	11583	17753	7500	9096
Mercosur	*5075*	*8072*	*5183*	*5800*
Asia	10772	13375	8251	11239
China	*4253*	*5075*	*1950*	*3378*
Canada	893	1107	654	789
USA	15399	18453	8827	10506
European Union	16464	21414	11635	14380
Other	8096	10726	3221	4307
Total	**66336**	**87280**	**44291**	**57080**

** Argentina, Bolivia, Brasil, Chile, Colombia, Cuba, Ecuador, México, Paraguay, Perú, Uruguay and Venezuela*
Source: Boletim do Banco Central do Brasil, http://www.bcb.gov.br/?BOLETIMEST





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