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Argentina

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The land and its people

Argentina has a total population of 36,260,130, a total surface area of 3,761,274 square kilometers (continental Argentina: 2,791,310 square kilometers and Antarctic Argentina: 969,464 square kilometers), and a density of 13 inhabitants per square kilometer. It is surrounded by Chile to the west; the Atlantic Ocean to the east; and Peru, Bolivia, Paraguay, Uruguay, and Brazil to the north (see Figure 3.1). Argentines' ancestors mostly came from Europe, and were mainly Spaniards and Italians. There were also, in smaller numbers, German, French, and English immigrants. In 2004–2005 a national survey revealed that a total of 600,329 people recognized themselves as being pure aboriginals or descendants of the first generation. There is freedom of religion but Argentines are for the most part Roman Catholic. However, Jews, Protestants, Muslims, and many other religions live together peacefully. Since the adoption of the 1853 National Constitution the form of government has been representative, republican, and federal. The country is divided into 23 provinces and the federal capital, which has been an autonomous city since a modification of the Constitution in 1994.

The government is divided into three branches: the Executive, formed by the President and Ministers; the Legislative, with two houses – the Senate and the House of Representatives; and the Judicial, with a Supreme Court of Justice and different jurisdictions.

Taking advantage of the good climatic conditions of the temperate pampas, the main economic activity in Argentina is agriculture and food processing industries. Other important activities are livestock raising and fishing. As in many developing countries, the nonagricultural industrial sector is of moderate size and has been influenced by periods of protective measures and periods of free trade policies.

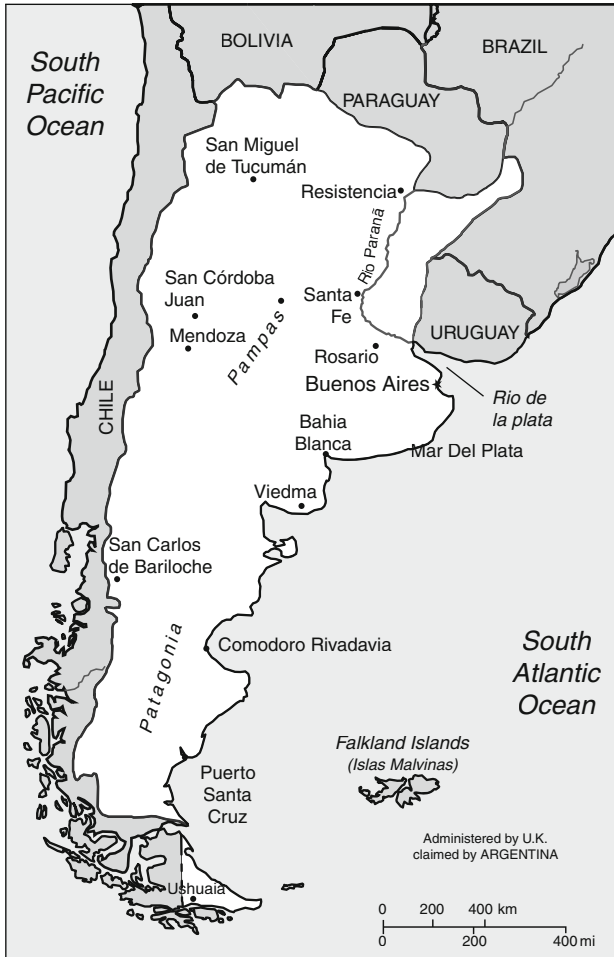


Figure 3.1 Map of Argentina

Cultural and economic history

The beginnings

The survival of many heterogeneous aboriginal groups has shaped the culture in Latin America. Argentina has incorporated many characteristics of European culture, introduced mainly by conquerors and afterward by immigrant streams mainly from European countries at the end of nineteenth and beginning of the twentieth centuries.

Many indigenous groups from different cultures occupied the Argentine territory before its colonization. The Diaguitas and Comechingones from the middle-west territory domesticated animals, wove and hunted. The Querandies, Patagones, and Onas inhabited Patagonia, the Litoral and Pampa regions. These people were nomads and lived by hunting and fishing. The Calchaquies and Maticos inhabited the north region, cultivated the land and domesticated animals.

Juan Díaz de Solís, a Spanish colonist, discovered the River Plate in 1516. Sebastian Cabot first penetrated the territory in 1526 and established the first Spanish colony in the region. In 1536, Pedro de Mendoza founded Santa María del Buen Ayre, but the rebellious natives, who refused to provide food to the Spaniards, burnt down the city.

However, Domingo Martínez de Irala is considered the first colonist, since he was able to approach the indigenous groups peacefully, achieving the unification between Spaniards and natives. Colonizing streams from Peru, Chile, and Spain he started penetrating Argentine territory in 1560, populating the region and giving birth to new cities. Jesuit missionaries also began to make their way into the area during this time.

In 1776, the viceroyalty of the Río de la Plata was created, integrating Argentina, Bolivia, Uruguay, Paraguay, and southern Brazil. Buenos Aires was its capital. In 1777, the Port of Buenos Aires began free trade with ports in Spain.

The road to independence

In 1810, the viceroy was replaced by an open city council (*cabildo abierto*). The development sprang from popular beliefs influenced by emancipating ideas from the French Revolution and North American independence. Liberating armies propagated the revolutionary doctrine in neighboring countries, trying to evict the Spaniards from their territories.

General José de San Martín, one of the nation's most important historical characters, contributed to freeing Chile and Peru, thus assuring the independence of the south of the continent. In 1816, independence from Spain was declared. In 1853, the National Constitution was created, establishing a republican, representative, and federal form of government.

The economic culture in Argentina was greatly influenced by figures such as the Frenchman Quesnay who favored wealth creation through work on the land, that is, developing agriculture. Influence also came from the British, through the ideas of John Locke and Adam Smith, favoring freedom and private property, as basic human rights, and free trade.

One major exponent of these economic principles during the viceroyalty period was Mariano Moreno, who defended the farmers' interests. He strongly defended free trade and counseled the viceroy against monopolies that tended to generate contraband. He confronted Spanish public officials who denied the Spanish colonies the right to trade directly with London merchants. However, Spain's attitude became more flexible due to its economic decadence (the result of debilitating wars with other European countries) at the beginning of the 1800s.

Releasing the constraint on foreign trade established the basis for free trade with Europe after the country's independence in 1816, and shaped Argentina's attitude until the First World War. Consequently, the trade derived from cattle and sheep – such as leather, wool, and frozen beef – began shaping external trade. Of course, the other side of the coin was the importing of manufactured goods, mainly from Britain. These imports enhanced competition and produced discomfort for the Argentines involved in businesses competing with them. Although some protectionist policies were set in motion to protect certain industries, free trade was the general policy thanks to the revenues stemming from customs duties. This policy favored internationally competitive sectors such as agricultural production.

At the beginning of the 1800s, agriculture played a subordinate role to cattle. Much of the country's interior, where agricultural conditions were optimal, had not been extensively populated. However, this tendency started to reverse in the 1820s with the stimulation of export policies for fruit and other agricultural products.

The country tried to develop mining activity, but with no success. The goal was to supplement the wealth generated by stock exports and to attend to the great financial needs of the revolution for independence. The people's lack of knowledge on how to exploit mines destroyed this dream and made the economy dependent first on cattle, second on agriculture, and lastly on manufactured goods. The direct consequence of the lack of mineral wealth was a shortage of coins to back up commercial transactions. Thus, paper money was printed with a set conversion rate to gold and silver, to substitute for the lack of coins.

After achieving independence from Spain with much effort, the young Argentine republic enjoyed a unique place in the world. It had vast natural resources, a huge internal market, and direct access to the sea. Again, derivatives from cattle easily found eager importers such as Brazil, North America, Europe, and Cuba. The following decades, however, were tainted by imbalances between Buenos Aires – the center

of commercial activity due to its proximity to a port, as well as of financial, political, and economic activity – and the other provinces. Nevertheless Argentina began to position itself as one of the most powerful countries in Latin America.

The see-saw century: dealing with populism and coups d'état

In 1904, the working class party gained representation in the government. H. de Yrigoyen assumed the presidency in 1916, maintaining the country's neutrality during the First World War. A succession of military coups took place from 1930 until 1946, replacing the elected democratic governments. In 1944, diplomatic relations were broken with Germany and its allies, and war was declared on them.

In 1946, General Juan Domingo Perón was elected president with massive support from the working class. His government was characterized by populist measures. Perón and his wife, Eva Perón (who died in 1952), favored policies to enhance social welfare. However, these policies produced unsustainable macroeconomic pressure and social unrest that ended with Perón's exile in 1955. A new succession of democratic governments and coups d'état characterized the period from 1955 to 1973.

In 1972, Perón was reelected with substantial popular support, but he died the following year. His widow, María Estela de Perón, the vice-president, succeeded him. But the period was characterized by waves of violence due to the lack of economic policies to support the nation's development and control the fiscal deficit and inflation. A new military coup again ended the democratic government.

The period called the Proceso Nacional de Reorganización (National Reorganization Process) was characterized by a sort of civil war with massive violation of human rights. The results of this era were thousands of missing people, a great increase in the external deficit, a deep recession, and the closure of many private firms, as well as the military occupation of the Malvinas Islands in 1982. The islands had been seized in 1833 by the United Kingdom.

The leader challenged: gaining stability

This last phase of Argentine history culminated in the lost war in the Falklands (Malvinas). Democratic elections were reestablished in 1983. New president Raúl Alfonsín, from the Radical Union Party, was elected for a six-year period. He worked hard on establishing and protecting the basic pillars of democracy and institutional stability. However, he was not successful in controlling the constant increases in prices that finally led to hyperinflation. As a result, a few months before the end of his

mandate Alfonsín surrendered the presidency to Carlos S. Menem, from the Justicialist Party who had won the presidential election.

Menem was reelected for the period 1995–1999. During his decade of administration, he achieved price stability by creating the Convertibility Plan, based on a fixed exchange rate (under which one Argentine peso equaled one dollar). He also privileged free trade and capital mobility. The outcome of these policies was an increase in gross national product (GNP) that made Argentina the second largest economy in Latin America after Brazil. However, a succession of balance of payment crises in the developing countries of South-East Asia in 1997, and the Russian debt default in the second half of 1998, forced Argentina into a period of recession, which was worsened by the Brazilian devaluation of the Real at the beginning of 1999. The economy started to recover in the second half of 1999. In 2000, the Alliance Party (named after the alliance of the Radical Union and Frepaso parties) won the presidential elections under Fernando de la Rúa. A combination of major tax increases, adverse terms of trade, and capital outflows aborted the recovery and a new period of recession began. These developments, together with the lack of attention to badly needed structural changes, produced social turmoil that ended with de la Rúa's resignation in December 2001, plunging the economy into an even bigger crisis. A new provisional government, under the Justicialist Party, declared, with the approval of the National Congress, defaults on the national debt, and later assigned the presidency to Eduardo Duhalde. One of Duhalde's first actions as president was to pass two other controversial laws: the abolition of the Convertibility Law, producing a devaluation of the Argentine peso; and the "pesofication" of dollar-denominated contracts in the banking sector. This meant that every dollar deposit in the banks was converted to \$1.40 (Argentine pesos), whereas at the time, the price of the dollar in the exchange market had reached approximately \$4 (pesos). At the same time, the loans in dollars that banks had made to the public were converted to Argentine pesos at the official conversion rate, that is, one dollar for one Argentine peso. That is why the process was referred to as asymmetric "pesofication": Banks' dollar assets and liabilities were converted to pesos at different exchange rates, producing a massive redistribution of wealth from lenders to borrowers. For example, a borrower holding a liquid position in US dollars was able to convert that position at an exchange rate of four pesos for each dollar in the unregulated open exchange market, canceling his previous debt converted at an exchange of one peso to one dollar. To be precise, this process represented a nominal debt reduction of 75 percent.

These policies immediately produced high country risk; the default was interpreted by the international community as a lack of willingness to pay. Moreover, the above policies also produced vast social discomfort, political uncertainty, and the deterioration of institutions. Consequently Duhalde called for anticipated elections, without primaries, an election that was won by Carlos Menem, but as he obtained fewer than 40 percent of the votes, the law required a second election. In the runoff election, Carlos Menem and Nestor Kirchner (second in number of votes), would be allowed to compete. As Carlos Menem decided not to compete in the second round, Nestor Kirchner was elected president with just 22 percent of the votes.

Although he started with weak support from the population, he was able to complete his four-year appointed term. At the end of his presidency, the high growth rate in GNP, the low unemployment rate, and the relative stability in the value of the Argentine peso, contributed to a certain period of peace among the citizens of Argentina. These positive indicators of the economy can be largely explained by the very favorable terms of trade and abundant international liquidity during Kirchner's term. However, certain manipulations of core macroeconomic indices, such as the inflation level and the amount of foreign reserves, and an increasing concentration of power in just a few people's hands – "crony capitalism" – started to undermine the confidence of the population in the real strength of the economy and its institutions.

After his first mandate, Kirchner appointed his wife, Cristina Fernandez, to compete for the elections in 2007, thus again avoiding the normal procedure of primary elections within the party. Cristina Fernandez won the elections and assumed the presidency in December 2007. Unfortunately, her term had a rough start: immediately after she gained power, a corruption case put the financing of her campaign under the magnifying glass. Her campaign was presumed to have been financed with illegal money from Venezuela. After that, she tried to pass a controversial resolution raising the tax on exports of agricultural products, thus fomenting a tax revolt by farmers. The farmers tried to reverse the situation through public demonstrations, which involved blocking traffic on the roads. They also sought support, which they successfully gained, from people not directly involved in agricultural activity. Cristina Fernandez decided to end this civil revolt by sending the resolution for approval by the National Congress. In a heated debate with tied votes for and against the law, the vice president, Julio Cleto Cobos, had to make the deciding vote. He voted against the tax hike. This represented a huge loss of power for the president and a steep fall

in popularity from an original 60 percent to a low of 20 percent in just a few months in power.

Also, the world financial situation after the subprime crisis affected the Argentine economy by diminishing the price of food commodities which had greatly contributed to Argentina's recovery after the 2002 crisis. After the default in 2001, Argentina was not able to access the international financial markets. The combination of these adverse factors (high inflation rate, loss of access to capital markets, and worldwide decrease in growth at the end of 2008) has put pressure on the fiscal accounts. This phenomenon produced a sharp increase in country risk and consequently the pursuit of desperate measures by Argentina to attract foreign capital. To address this matter, the president passed a law in November 2008 that enabled capital from abroad to return to Argentina with very flexible prerequisites. The opposing parties accused the government of permitting the laundering of money. Another drastic measure was the nationalization of the private funds that workers used to save money to finance their retirement. After the law was passed through Congress (where Cristina Fernandez had a majority) these funds were automatically transferred to the national social security administration.

This and many other policies contributed to making the opposition complain, over the past few years, against policy actions which undermined the basic institutional framework of Argentina: the defense of property rights and the balance of power among the legislative, judiciary, and presidential branches of government. The years to come will surely be difficult. The national leadership will certainly be challenged.

World economic organizations: trade and growth

As mentioned earlier, Argentina enjoyed a comfortable position in world trade at the end of the 1800s. However, the country became progressively poorer compared to other nations from the beginning of the last century. For example, Argentina's output grew by 157 percent from 1900 to 1997, whereas Canada's output grew by 603 percent over the same period. The explanation for this very low growth rate seems to be an inward orientation and macroeconomic instability. President Juan Perón's administration particularly favored import substitution policies over export policies in order to encourage domestic industrial development. He also favored an expansionary fiscal policy. However, empirical evidence (Díaz A., 1970) shows that output grew 5.6 percent annually between 1900 and 1930, whereas from 1930 to 1965, output grew by

only 3.7 percent, thus putting into question the success of import substitution measures. When barriers to growth were eliminated under Menem's administration, output experienced a higher annual growth rate of 6 percent. This tendency decreased as other developing countries' crises spread around the globe.

In 2002, an import substitution policy was pursued again, strengthened by a major devaluation of the Argentine peso, which has remained undervalued in the past few years. This type of policy, together with a strong increase in the price of commodities that Argentina exports has produced high growth rates, but many suggest this type of growth will not lead to development in the long run. Several export taxes and import restrictions in the past few years on products such as petroleum, meat, and agricultural goods, and the strong intervention by the government to control prices – applying cross subsidies between sectors and expropriating companies and retirement funds – have resulted in a lack of investment and the consumption of the capital stock accumulated during the freer decade of the 1990s, thus compromising growth in the long run. These results suggest that when Argentina follows relatively free trade policies, it tends to produce more sustainable growth than during periods of protectionism.

Trade liberalization: the birth of Mercosur

The recent attempts by Argentina to liberalize trade started at the end of the 1980s. The first attempt at free trade started in 1988, unilaterally, by abandoning the previous protectionist policies that tended toward autarky, import substitution, and exchange rate and price controls.

There were also efforts to open trade multilaterally by deepening the country's compromises with GATT (General Agreement on Tariffs and Trade) and the WTO (World Trade Organization) and by lowering tariffs and quota restrictions.

Regional openness started with Brazil in 1986 with the signing by both countries of the Programa de Cooperación y Integración Económica Argentina-Brasil (Argentina-Brazil Integration and Economics Cooperation Program). In November 1988, a new treaty – the Tratado de Integración, Cooperación y Desarrollo – (the Treaty in Integration, Cooperation and Development) was signed, whereby both countries agreed not only to a free trade union but to recognize the importance of coordinating monetary, fiscal, and exchange policies.

Later, in 1991, the Tratado de Asunción (Treaty of Asunción) was signed, which gave birth to Mercosur (Mercado Común del Sur). A 40

percent tariff decrease was agreed upon among the participating countries – Argentina, Brazil, Uruguay, and Paraguay – starting June 1991. The remaining tariffs would gradually decrease to zero tariffs in 1995, thus establishing a free trade area and a new external common tariff for other nonmember countries. However, the members of Mercosur agreed to keep certain products under a specific tariff. Such was the case for Argentine products related to the steel, textile, paper, and shoe industries. Moreover, the sugar and automobile industries were given special treatment ad hoc due to divergences in policy among the countries regarding the protection of these vulnerable sectors. Still, the main objective was to move to a customs union by 2001 by gradually eliminating these restrictions on trade.

Chile, Bolivia, Ecuador, Colombia, and Peru were included in the Mercosur treaty as “associate economies”, which meant that they could negotiate bilaterally with Mercosur, whereas Venezuela requested to be fully incorporated as a new member in 2006 but has not received ratification from all member countries yet.

Mercosur has also served as an enforcing mechanism. Due to the international commitment among countries, the task of local lobbyists to press the government for protection for certain industries was made more difficult. This mechanism is particularly valuable for a country like Argentina, accustomed as it is to protectionist policies. In this area in particular, regionalism is preferable to unilateralism.

What is behind the trade agreement?

Many authors have analyzed the determining factors of regional trade (Sanguinetti and Garriga, 1995). Unilateral liberalization – together with geographic features – seems to be an important factor in determining intra-regional trade among countries. There appears to be a concept of a “natural bloc”, drawn from common frontiers, similar cultural inheritance, and similar languages, that reduces the costs of transactions between these related countries compared to others. There is empirical evidence suggesting that Mercosur is such a natural bloc.

Although the first four member countries are neighbors with markets close enough to lower transaction costs, there are different national interests. Argentina, Paraguay, and Uruguay are economies that view integration as a way to increase trade. These nations look at Mercosur as a stage in opening commerce to other countries outside their current trading bloc. However, Brazil’s economy is the largest of the bloc partners. As a result, membership in Mercosur seems to have an additional geopolitical interest: to generate a very large economic area so as to

increase negotiating power relative to other trade areas in Europe, Asia, and the United States.

Thus, Mercosur's pitfall is differing interests. In Argentina's case, the country would obtain more benefits by opening up to the rest of the world than by belonging to a bloc in which Brazil's economic leadership leads to higher tariffs for countries outside the bloc. Chile's reluctance to adhere to Mercosur might be taken as proof of the advantage for this country to function as a small world economy rather than as a member of a group of countries not offering all the advantages of trade creation and suffering from trade diversion within the region, as well. Despite the different interests among member countries, Mercosur is a useful tool for all of them since it can be used as a transitional stage to greater global integration and as leverage during negotiations. As a result, the member nations are more powerful as a bloc than individually.

Trade development

Table 3.1 gives some insight into the trade statistics of the Mercosur bloc. As can be seen from the information in the table, trade within Mercosur has grown much more quickly than trade outside the bloc. However, the balance of trade accounts moved from an initial surplus to a deficit starting in 1995. This phenomenon can be explained by the underlying macroeconomic movements that members of the bloc have experienced in opening their economies and abolishing external capital rationing.

These movements also explain why the balance of trade deficit has produced discomfort for those who favor protectionist policies. Nonetheless, the trade balance reverted to a surplus in 2001. This seemingly happy turn of events was due at first not to an increase in competitiveness but to an ongoing recession.

However, in 2002, the devaluation of the peso in Argentina helped to bring about a trade surplus. At present, inflation in Argentina has been eroding the real exchange rate, which has encouraged lobbyists from the industrial sector to push for an ever-greater depreciation of the peso.

Clearly then, in most sectors of the economy, Argentina is not gaining in competitiveness due to an increase in its productivity (that is, using new technologies that help reduce the costs of production) but due to continuous intervention by the central bank to maintain the exchange rate at an artificially high level.

Table 3.1 Foreign trade, Argentina, 1990–2006

Year	Exports within Mercosur	Exports to the rest of the world	Total exports	Imports within Mercosur	Imports from the rest of the world	Total imports	Balance with the rest of the world
(a) Trade statistics (US\$ millions)							
1990	4228	42,191	46,419	3606	23,642	27,248	18,548
1991	5243	40,699	45,912	4789	27,357	32,146	13,312
1992	7369	42,872	50,241	7108	31,564	28,673	11,308
1993	10,057	44,018	54,075	9024	36,846	45,869	7172
1994	12,049	50,066	62,115	11,622	46,459	58,082	3607
1995	14,444	56,066	70,059	13,928	61,829	75,758	-5763
1996	17,034	57,965	74,999	17,112	66,169	83,281	-8204
1997	20,758	62,796	83,555	20,483	77,021	97,504	-14,225
1998	20,507	61,098	81,605	20,935	75,848	96,783	-14,750
1999	15,399	59,176	74,576	15,845	64,953	80,978	-5777
2000	17,697	66,901	84,598	17,431	69,191	86,622	-2290
2001	15,214	72,671	87,885	15,331	66,294	81,625	6377
2002	10,214	78,669	88,883	10,665	49,036	59,702	29,663
2003	12,631	93,467	106,097	13,059	53,083	66,143	40,383
2004	17,192	118,396	135,588	17,601	73,388	90,989	45,007
2005	21,105	142,700	163,805	21,323	88,020	109,343	54,680
2006	25,629	164,527	190,156	25,533	110,069	135,601	54,459
(b) Trade statistics (percentage change)							
1990							
1991	24	-3.6	-1.1	32.8	15.7	18.0	-28.2
1992	40.5	5.4	9.4	48.4	15.4	20.3	-15.1
1993	36.5	2.7	7.6	26.9	16.7	18.6	-36.6
1994	19.8	13.7	14.9	28.8	26.1	26.6	-49.7
1995	19.9	12.0	13.5	19.8	33.1	30.4	-259.8
1996	17.9	3.4	6.4	22.9	7.0	9.9	42.3
1997	21.9	8.3	11.4	19.7	16.4	17.1	73.4
1998	-1.2	-2.7	-2.3	2.2	-1.5	-0.7	3.7
1999	-24.9	-3.1	-8.6	-24.3	-14.4	-16.5	-60.8
2000	14.9	13.1	13.4	10.0	6.5	7.2	-60.4
2001	-14.0	8.6	3.9	-12.0	-4.2	-5.8	-378.5
2002	-32.9	8.3	1.1	-30.4	-26.0	-26.9	364.7
2003	23.7	18.8	19.4	22.4	8.3	10.8	36.3
2004	36.1	26.7	27.8	34.8	38.3	37.6	11.5
2005	22.8	20.5	20.8	21.1	19.9	20.2	21.5
2006	21.4	15.3	16.1	19.7	25.0	24.0	-0.4

Sources: Centro de Economía Internacional en base a Indec, Secretariat of Foreign Trade, Brazil (SECEX), Banco Central de Paraguai, Banco Central del Uruguay, and International Monetary Fund (FMI).

The present and future of trade

Mercosur at present

Mercosur has remained relatively stable despite changes of government and economic crises. There is an ongoing debate as to whether Mercosur has been trade creating or trade diverting. There is empirical evidence that supports each position. In 1997, an economist at the World Bank released the first publicly available document that suggested that Mercosur was trade diverting (Yeats, 1997). This document produced justified discomfort for all bloc members and prompted many responses suggesting that overall Mercosur had been trade creating (Bohara, Kishore, and Sanguinetti, 2001).

Before Mercosur was founded, many of its members – especially Argentina – had relatively closed economies. So, it is not wide of the mark to consider that any degree of opening to commerce is trade creating, at least at the beginning of the agreement. Indeed, Mercosur produced a strong initial expansion and encouraged trade and investment. Nevertheless, policies that protect vulnerable industries still remain. There are tariffs, nontariff restrictions, export subsidies, and production subsidies that distort trade. This state of affairs has also produced decreased exports to both NAFTA and the European Union.

These protectionist policies have prevailed due to lobbying by different sectors of the economy. The power of these lobbyists has had considerable influence and has coddled the so-called “infant industries” in Argentina to the ripe old age of 50 years! These small business groups, which hold a more protectionist view, are suspicious of economic integration programs. They try to maintain a system of protection of the products they represent. Such is the case, for example, of industrial products represented by the Industrial Union. Nevertheless, these goods do not represent a large proportion of GNP.

On the whole, the business community has accepted Mercosur and supranational organizations as a good plan for growing international trade, and as growth enhancing. Yet they do not enjoy 100 percent public support; most of the Argentine people are strong supporters of nationalism and are accustomed to populist measures to protect them. There has also been some discomfort about the opening of the economy due to such external shocks as Brazil’s devaluation in 1999. However, as mentioned earlier, in January 2002, Argentina abandoned the convertibility plan by devaluing its currency and moved to a floating exchange rate, which improved its terms of trade. Exporters received Argentina’s devaluation of the peso with great relief. They felt that the rule one

peso = one dollar had made tradable products less competitive, due to the artificially appreciated value of the local currency that was pegged to the dollar.

In the past few years there has been some complaint from the smaller countries – Uruguay and Paraguay – due to the protective restraints that still prevail in the bigger countries like Brazil. For example, Paraguay considers there has not been a significant increase in the living standards of its citizens since it joined Mercosur. As a result, the country might pursue bilateral agreements with other countries like the United States; Uruguay might follow this same path.

This type of macroeconomic conflict within Mercosur has caused intraregional relations to deteriorate and has produced a negative impact on direct investments from countries that could have taken advantage of the enlarged trade area. There is an urgent need to deepen international policy coordination in order to avoid these hurtful consequences.

Mercosur's future

Sadly, in the past few years, controversial policies that limit access to foreign markets by prohibiting exports of certain goods and imposing high tariffs and quotas on many exports products have produced discomfort among the exports' producers. Many foreign markets that were gained during the opening of trade during the 1990s are now closed to Argentine exporters mostly due to export tariff and export quota. This tendency, together with policies biased against international companies, has left Argentina in an uncomfortable state, isolated from the rest of the world.

Despite these last developments, many simulations have been run to determine the impact of eliminating barriers to agricultural goods – a field in which Argentina has a comparative advantage (Fundación Mediterránea, 2000). In particular, this exercise has been run for the United States and the European Union. The results for the latter are very favorable, suggesting that if barriers are eliminated for this type of produce, meat exports to the EU will increase by 350 percent and sugar exports by 143 percent, for example. This result is a direct consequence of the European Union's distorting measures toward agricultural goods. Argentina already exports this type of goods despite the European Union's policies.

If the United States eliminates agricultural trade barriers, the results are more modest compared to those for the European Union. For example, sugar exports would increase 60 percent and dairy products 20 percent. The explanation for these modest increases in exports is that there

are fewer barriers and distortions to these goods and that the United States is more efficient in producing its own.

Although negotiations regarding tariff reductions and/or elimination have started among these countries, Argentina, like many other developing countries, faces additional costs when settling multilateral agreements. Due to poor management infrastructure, in order to comply with standards and technical norms, many countries require expensive tests and certificates for exporters. One example of this kind of cost was the outbreak of *aftosa* (foot-and-mouth disease) in the country. Argentina's ineffectiveness in controlling this type of virus resulted in the closure of the meat market by almost all importers for a very long time. Despite this incident, the country's agricultural and cattle industry is considered competitive relative to the United States. So, it might be better to improve trade with those countries that do not have a comparative advantage in this particular market segment.

There is a new debate on whether the country should try to separate itself from its present bloc and search for other markets unilaterally. Currently, given market conditions, there might be more trade creation if the country entered NAFTA directly, even if it meant abandoning Mercosur. One of the advantages of entering NAFTA is the possibility of using the fast track policy of the United States in order to negotiate tariffs more easily. The reduction of transaction costs is a valuable tool in trying to reach an agreement with NAFTA. At present, Brazil's reluctance to lower the Mercosur external tariff is unfavorable to the other members who wish to have greater trade gains.

Culture versus globalization

There is an ongoing debate as to whether the growth in globalization has been detrimental to culture and tradition within a given country. The different ethnic groups in Argentina have integrated perfectly well into the democratic system. As was previously mentioned, there is a very small indigenous ethnic population in the country. These peoples' claims concerning their territory and culture are always heard. Moreover, they have been protected by specific legislation. International agreements such as Mercosur, NAFTA, and the Andean Pact are recognized by the ethnic groups and are considered to be a normal process of integration among nations. The indigenous tribes do not believe that their cultural features are threatened since they are well protected by specific laws. Moreover, they have greatly benefited from the sale of their handicrafts and services (for example as ski instructors or tourist

guides) to tourists, especially in the north of the country where these groups are mostly found.

Trade is definitely a factor of cultural integration in many other ways. Argentina has incorporated many modern practices, such as marketing structures and the development of economies of scale for mass production. All these practices are sooner or later translated into the educational or business culture. Buying bread at the bakery, meat at the butcher's shop, and then vegetables at the grocer's is, for many Argentines, the culture of the small merchant. So, when large companies enter the country with big, efficient supermarkets, with better prices, higher quality, and mass production, people argue that such behavior destroys culture.

The argument is accurate from that point of view. That is, in a competitive system, the more efficient baker will compete successfully in the market, and the inefficient baker might find himself arranging bread on the supermarket's aisles. Thus, small merchants might argue that life was better before globalization. However, as consumers wish to optimize price and quality, this argument is not true for them.

Should consumers sacrifice themselves for culture's sake? In Argentina, although the small merchant culture still exists in some places, especially in the most rural regions, the more traditional political parties, such as the Radical and the Justicialist Parties, do not reject globalization. Moreover, they tend to promote economic integration with other countries.

Free markets and democracy were at the origin of the Argentine republic as established in the 1853 Constitution, but were gradually abandoned through time; however these principles have resurfaced in the past three decades. Freedom and democracy restarted in 1983, and freedom of the press restarted in the 1990s. Political competition is relatively new for most of the present generation.

There has not yet been enough time to allow the system fully to work in favor of efficient allocation of resources and strong monetary, fiscal and political institutions.

Conclusion

Argentina has been able to improve its terms of trade by becoming an important participant in the Mercosur trade agreement. Yet there is an urgent need to coordinate macroeconomic policies in order to minimize negative external shocks to the bloc. Until the major peso depreciation at the beginning of 2002, the debate in Argentina was

whether the country should separate from the other bloc members that had previously depreciated their own currencies without allowing for compensatory measures to absorb short-run disequilibrium. An alternative proposal was to negotiate unilaterally with the United States or the European Union, or to enter NAFTA, by which means Argentina could benefit by penetrating these markets. This strategy could have also been useful to all the members of Mercosur affected by trade diversion. On the one hand, it could be stated that real exchange rate volatility has affected, and will continue to affect, regional economic integration in the future. On the other hand, culture and tradition have integrated well with globalization. The country's ancient and rich culture is maintained by the prevailing ethnic groups, which have accepted the challenge of an integrating world.

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