

The FTAA as a Two-Level Bargaining Game

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Abstract

This paper applies Putnam's (1993) seminal work on negotiations as "two level games," to the FTAA (Free Trade Area of the Americas) negotiations process. The paper compares the treaty ratification processes and the existing web of regional and bilateral trade agreements for insights into the relative bargaining strength and key issues for the most important economies in the hemisphere: the U.S., Canada, Brazil, and Mexico. By laying out the possibilities for domestic interest groups to gain access to trade negotiators, we can better understand the dynamics of the negotiation process. For example, how does the awarding of fast track authority affect the U.S.'s relative bargaining strength? How does the greater influence of the provincial level in Canada on federal negotiators affect Canada's bargaining position vs. the U.S.? How does the MERCOSUR agreement affect the positions of the member countries? How do the large number of bilateral agreements, e.g., Chile-Canada, affect the possibilities for bargaining coalitions among non-U.S. countries? This paper will deliver some important insights into how the existing international and domestic legal context will affect the dynamic shape of FTAA negotiations.

Introduction

Much of the critique lobbed at a possible Free Trade Agreement of the Americas (FTAA) pictures a behemoth U.S. demanding conditions from other countries of the hemisphere in return for a limited increase in access to the world's largest market.¹ The reasons for this fear are the regional asymmetries demonstrated below:

Table 1: Largest Countries in the FTAA Region:

	GDP		Population
United States	9837.4	United States	281.6
Canada	687.9	Brazil	170.4
Brazil	595.5	Mexico	98.0
Mexico	574.5	Colombia	42.3
Argentina	285.0	Argentina	37.0
Colombia	81.3	Canada	30.8
Chile	70.5	Peru	25.7
Peru	53.5	Venezuela, RB	24.2
Uruguay	19.7	Chile	15.2
Costa Rica	15.9	Ecuador	12.6
Ecuador	13.6	Cuba	11.2
Bolivia	8.3	Bolivia	8.3
Paraguay	7.5	Paraguay	5.5
Nicaragua	2.4	Nicaragua	5.1
units	\$billions, current		millions

Notes: Source: World Bank, year = 2000

However, this analysis would miss a much wider picture of the true scenario for the FTAA negotiations. A proper analysis should consider, for example, that FTAA negotiations occur among partners with different negotiating organizations and

¹ See, for example, Grinspun and Cameron (1994).

procedures; among negotiators representing diverse and sometimes conflicting domestic interests; and within a web of pre-existing multilateral and bilateral agreements both within the region and between regional countries and extra-regional partners. We explore these complications in the following sections.

Putnam's Two Level Bargaining Game

Robert Putnam's classic 1988 article represents a seminal step forward in the theory of international bargaining. At the heart of Putnam's theory is that international negotiators must satisfy diverse sets of domestic interests while at the same time pushing forward their view of the national interest in light of what is available to other negotiators. Putnam terms "win sets" the various stances that a negotiator can adopt and still win domestic ratification. Therefore, the key is to try to maximize one's national gains within one's win set.

This implies a secondary level of complexity, namely that the knowledge of negotiating partners' win sets can be used as strategic information. Thus, a negotiator with a limited win set can claim to his/her negotiating partners that they really have little room to compromise. In a sense, therefore, the negotiator naturally has an interest in exaggerating the tightness of the win set.

We can add several other layers of complexity to Putnam's basic model by borrowing from insights from other political theories. Graham Allison's classic article on bureaucratic decision making during the Cuban missile crisis suggests three basic analyses. The first mode of decision-making is to look at unitary decision-making by the executive. That is, the chief executive ultimately makes a decision about whether a step (or treaty) is in the national interest, using a basic cost-benefit analysis. The second mode would be to look within the government apparatus as a competition among different ministries for their own particular interests. Thus, the defense establishment may have quite different interests from commerce, agriculture from industry, etc. For our purposes, we might expand this to include well-organized interest groups in society with an interest in trade. The third mode of decision-making would be to look at the "standard operating procedures," or the ways in which decisions are routinely made in the government. For example, the level and amount of public hearings on an issue can strongly affect its outcome.

Finally, a number of authors who have written in international regime theory, such as Keohane, point to the importance of issue linkage. Issue linkage, in a sense, involves both quid pro quo, or concessions on different issues in order to reach an agreement. Issue linkage can also be thought of as the ways to create a winning coalition through an agreed-upon platform amongst different interests.

In the next section we will analyze the contours of an FTAA negotiations along the lines of these three basic perspectives. Given the nature of both the NAFTA and MERCOSUR to preserve national autonomy, and to create instead coordinating or, at most, in the case of NAFTA, arbitral bodies, we do not examine the idea of regional bargaining. Similarly, the proposed South American Free Trade Area (SAFTA) has not really emerged as an alternative. Nor have the various other alternatives, such as the Central American, Caribbean, and Andean Pact free trade areas developed into anything resembling independent foreign policy making regional institutions. Instead we argue

that existing regional and sub-regional agreements will still work ultimately through the national lens. We will outline the treaty ratification procedures for each country in order to see how those shape the possible win sets of the negotiators and the potential influence of these standard operating procedures. We will look to the most sensitive national industries to attempt to discern the key interest groups that will strongly influence both the win set and the possibilities for issue linkage. We will then look to the series of bilateral and multilateral existing agreements for each country to determine if their win sets are also comprised at the sub-regional level. Finally, we will turn to the role of environmental and labour groups at the domestic and international levels. This picture will then give us an interesting idea of how the bargaining over an FTAA might play out.

Treaty Ratification Procedures

Treaty ratification procedures are key to international negotiating outcomes because they affect the possible size of the win set. Procedures can also delay and/or open up the treaty to various degrees to domestic interest groups. In the case of the FTAA, treaty ratification procedures will be particularly important from the point of view of the degree or amount of modifications that could occur, and potential stall, the treaty's adoption once a working document is created. Moreover, the domestic authority of the executive branch to sign a treaty and implement it could potentially limit the jurisdiction of any international bodies created to arbitrate, mediate, or even legislate the treaty.

U.S.

The granting of fast-track authority to Pres. Bush in 2002 completely changes the dynamic for trade negotiations in terms of the ability of special interests to affect the outcomes via the U.S. Congress. In the U.S., the Executive takes the lead in negotiations via the office of the U.S. Trade Representative. Informal negotiations also take place with industry associations and, to a lesser extent, with non-governmental organizations, particularly those concerned with environmental and labor standards. A variety of executive agencies also create fact-finding missions and reports. The advantage of fast track authority is that the U.S. Congress is not able to amend an agreement. Therefore, most special interest pressure will be on the executive branch in the negotiation stage. A key aspect for the U.S. will be to gauge the extent to which the U.S. is willing to concede the special interventions and degrees of autonomy that it uses to insulate its economy from trade impacts. These include anti-dumping measures and submission to international dispute resolution, both recurrent issues in international trade negotiations.

A key legislative election was held in 2002 that could affect the passage of trade negotiations in favor of passage. The Republicans were able to increase their control over the House, but they are at a deadlock in the Senate. The table below summarizes the current membership of the U.S. Congress:

U.S.	House of Repr.s	Senate
Republicans	223	49
Democrats	208	49
Indep.s	1	2

The Democratic Party has long-standing stronger ties to organized labour and to environmental groups, so that if the increase in support for Republicans continues, the special interests that most impeded the passage of the NAFTA treaty would be more impeded. However, we should also keep in mind that the more important political key to the FTAA from the point of view is the question of whether Mr. Bush will be re-elected in 2004. While even the Democratic Party beginning with Clinton supported free trade, their ties to the special interests mentioned above could complicate the treaty's passage. The President's ability to appoint the heads of the Dept. of Commerce, the Dept. of State, and the U.S. Trade Representative undoubtedly will mark the final shape of the FTAA agreement.

The U.S. government relies upon executive leadership to help decide the bulk of trade strategies, with the U.S. Trade Representative (USTR) acting as the right hand of the President. Within the executive branch, both ad hoc and formal inter-agency committees," usually led by the USTR, attempt to hammer out differences within the public sector. Members may all include Congresspersons and congressional staff. The U.S. International Trade Commission (USITC) acts as a neutral fact-finding arm for trade matters. Under the guise of the "official advisory committee system, inter-branch committees and members of interest associations are brought together for consultation. Members are selected for the committees on the basis of qualification, geography, and need. There are 33 committees with approximately 1,000 members. The committees system is organized into three basic levels: the President's Advisory Committee for Trade Policy and Negotiations (ACTPN); six policy advisory committees; and 26 technical, sectoral and functional advisory committees. Most of the committees are organized along sectoral lines, with industry and agriculture being the primary focal areas. In addition, environmental and consumer organizations are represented in the Trade and Environment Policy Advisory Committee (TEPAC). Trade matters are brought to public attention through public hearings.² One of the key points of contention here is that environmental and other civil society groups are kept in separate committees. This may improve the quality of the information given by each group, but it also allows the Executive to act as a deliberative body in determining national interests. It may also prevent both open conflict and the possibility for longer-term compromise among the different interests through social interaction and discussion.

Canada

The Canadian domestic policy environment for international trade is shaped by a number of internal and external factors. Historically, negotiating international trade agreements was a relatively simple process. The Imperial Preference System prior to World War Two guaranteed markets for Canadian goods and the post-war General Agreement on Tariffs and Trade (GATT) focused solely on tariff barriers, which were

² Jon E. Huenemann, "On the Trade Policy-Making Process in the United States," pp.67-73 in in Inter-American Development Bank, Intal Division. 2002. *The Trade Policy-Making Process, Level One of the Two Level Game: Country Studies in the Western Hemisphere*. Occasional Paper 13.

strictly areas of federal jurisdiction. During the past two decades, however, the intrusiveness of international commitments such as the GATT, the new World Trade Organization (WTO), and the North American Free Trade Agreement (NAFTA), have increasingly expanded into areas of domestic jurisdiction. Moreover, judicial interpretation of the Constitutional implications of these and previous trade commitments would appear to grant provincial governments increasing legitimacy in matters related to international trade. Therefore, as we see with the present impasse over adoption of the Kyoto Agreement, Canadian ratification of the FTAA will involve a strong level of provincial discussion.

There are several formal methods of consultation set up by the Canadian government. The Continuing Committee on Trade Negotiations is a forum for federal-provincial consultations. In terms of non-governmental participation, there are the Team Canada Inc Advisory Board and the Special Advisory Committee on International Trade (SAGITs). All members of both the ITAC and the SAGITs are appointed by the Trade Minister. There are 12 SAGITs, with membership from industry associations, environmental groups, and academia, each serving a two year term. The 12 SAGITs are organized along sectoral lines:

- | | |
|---|--------------------------------|
| Agriculture, Food and Beverage | Apparel and Footwear |
| Cultural Industries | Energy, Chemicals and Plastics |
| Environmental | Fish and Sea Products |
| Forest Products | Information Technologies |
| Medical and Health Care Products/Services | Mining, Metals and Minerals |
| Services | Textiles, Fur and Leather |

In both cases, members are expected to act with personal independence from their interest group organizations. In addition, there is an Academic Advisory Committee that includes 15 senior academics from a variety of disciplines. There are a variety of informal consultation efforts, including public hearings, as well.³

As a parliamentary system, once a treaty is adopted by Canadian negotiators, the passage should be much easier than in the U.S. case. The Prime Minister, by definition controls the legislature, and in Canada, the Senate is appointed by the PM. The Canadian Senate operates more as a body for reporting and hearings rather than as a legislative body. Moreover, the parliamentary system seems to allow for greater control of the bureaucracy and negotiations. However, the outcry over the adoption of the NAFTA treaty has made subsequent Canadian governments much more aware of the long-standing Canadian sensitivity towards U.S. domination. The current make-up of the Canadian House of Commons is:

Canada House of Commons

³ William A. Dymond and Laura Ritchie Dawson, "The Consultative Process in the Formulation of Canadian Trade Policy," pp. 23-30 in Inter-American Development Bank, Intal Division. 2002. *The Trade Policy-Making Process, Level One of the Two Level Game: Country Studies in the Western Hemisphere*. Occasional Paper 13.

Bloc Quebecois	35
Canadian Alliance	63
Liberal	169
New Democratic Party	14
Progressive Conservative	14
Independent	3

Bloc Quebecois has historically played an independent role in the Parliament, pushing for greater autonomy for Quebec. In recent years, Quebec has become a successful exporter in a number of industries, such as Bombardier airplanes and HydroQuebec energy, thus, the BQ would most likely be active in these specific sectors in regard to an FTAA. While the Progressive Conservatives and Canadian Alliance would potentially make for a formidable opposition party against the dominating Liberals, they historically have not been able to form any united opposition front. Moreover, both parties are more conservative, with the Alliance making its stronghold in resource rich Alberta and British Columbia, thus, they are not likely to present any real challenge to FTAA passage. Moreover, it appears now that Paul Martin, a Liberal leader, will be the next Prime Minister, so that FTAA passage should not encounter any problems via formal Canadian institutions. The important discussions in Canada are likely to take place along two lines:

- a) The core minority opposition to free trade and the anti-globalization movement that is able to take advantage of latent Canadian anti-Americanism.
- b) On the sectoral level, the need for the federal and provincial governments to hammer out agreements. For example, Alberta will likely push for greater liberalization of the energy sectors, while BC will be more interested in forestry sector provisions.
- c) The Canadian desire to keep health care and cultural industries out of negotiations.

In terms of the former factor, the present Canadian government seems well-insulated from political scandals. Moreover, the argument can be made that an FTAA will actually help to dampen or reduce U.S. domination as well as to help out the developing countries to the South. Still, the anti-globalization movement is well-organized in certain areas of Canada, and undoubtedly will make its presence felt. In terms of the latter factor, the federal government will have a much more difficult position to manage. The federal government will want to maintain its ability to use issue linkage, thus trading off concessions on one sector for those in another, but its ability to use this most important negotiating tool will be conditioned by the need to placate provinces.

Brazil

Brazil represents the greatest single challenge to U.S. domination of FTAA talks. Brazil is the 10th largest economy, and boasts a population of 170 million. More importantly, Brazil has a long history of industrial policy and protection of sensitive industries. Indeed, Brazil has had recent disputes with Canada (over aircraft production,

and the U.S. over steel and orange juice. Brazil will likely use its strong influence in MERCOSUR to try to create coalitions to block the U.S. on key issues.

Before 1992, the Ministry of Economy, Finance and Planning carried out trade negotiations in cooperation with the Ministry of External Relations.⁴ Since late 1992, the Ministry of External Relations is responsible for bilateral, regional and multilateral trade negotiations as well as for representing Brazil, and coordinating the country's participation, in international trade-related forums. The Ministry is the only entity with authority to sign international agreements on behalf of the Brazilian Government. The Brazilian Congress then has to approve the treaty by a simple majority. However, the Brazilian Congress has always been highly fractionalized, with inconsistent party discipline. This raises some considerable potential obstacles to ratification.

The Chamber of Foreign Trade (CAMEX) was created in 1995 to formulate and evaluate policies and co-ordinate activities related to foreign trade. It also serves as a forum for discussion between the authorities and sectors directly interested in the conduct of foreign trade policy. The Chamber consists of: the Head of the Presidential Office (Casa Civil) who chairs its meetings, and the Ministers of Agriculture, Finance, External Relations, Planning and Budget, and Industry, Trade and Tourism; the President of the Central Bank also attends the meetings. The Chamber co-ordinates the implementation of its decisions through its Executive Secretariat, but each Ministry remains responsible for matters within its competence.

In terms of the FTAA, the public sector's efforts are being coordinated through the National FTAA Secretariat (*Secretaria Nacional da ALCA*, or SENALCA), under the auspices of the Foreign Ministry. SENALCA holds monthly meetings attended by ministerial representatives, CAMEX, and the Central Bank. Civil society, business, and labor representatives may attend the meetings as guests. The Brazilian Business Coalition (*Coalizão Empresarial Brasileira*) within the long-standing business association, the CNI to coordinate industry, agriculture, and service interests on the FTAA.⁵

In Brazil, the election of President Lula has tremendous implications for the future of the FTAA. Lula has publicly criticized the FTAA as an example of American domination, with strong support in the polls. However, Lula has also agreed to adhere to the rules of the recent \$60 billion loan from the International Monetary Fund, and has made overtures to the Brazilian military. Lula seems to be more pragmatic than his campaign rhetoric would have us believe. More importantly, Brazilian politics is famous for the high level of party fragmentation, and lack of party discipline. The political system is fragmented structurally by the proportional representation voting system. The Brazilian government is also tied financially by the requisite fiscal transfers from the federal level to the states as required by the 1988 Constitution. As the following tables

⁴ See World Trade Organization (WTO) Report WT/TPR/S/75, Sept. 27, 2000.

⁵ Pedro de Motta Veiga, "Trade Policy-Making in Brazil: Transition Paths," pp. 13-21 in Inter-American Development Bank, Intal Division. 2002. *The Trade Policy-Making Process, Level One of the Two Level Game: Country Studies in the Western Hemisphere*. Occasional Paper 13.

demonstrate, Lula's PT (Worker's Party), has nowhere near the required votes to pass either any strong trade or domestic reform legislation.

Brasilian Legislature

2002 Chamber of Deputies	Number of Seats		2003 Senate	Seats
PFL	97		Partido do Mov. Democrático Brasileiro (PMDB)	19
PMDB	87		Partido da Frente Liberal (PFL)	19
PT	58		Partido dos Trabalhadores (PT)	14
PSBD	95		Partido da Social Democracia Brasileira (PSBD)	11
PPB	53		Partido Democrático Trabalhista (PDT)	5
PTB	33		Partido Socialista Brasileiro (PSB)	3
PSB	17		Partido Liberal (PL)	3
PL	22		Partido Trabalhista Brasileiro (PTB)	3
PDT	16		Partido Popular Socialista (PPS)	1
PPS	12		Partido Social Demócrata (PSD)	1
PC doB	10		Total	79
PV	1			
Prona	1			
Outros	11			
sem definição				
	513			

Source: Georgetown University's *Political Database of the Americas*

As we can see from the tables above, the PMDB and PSDB, centrist parties set up back in Vargas' time, and the mainstays of the Cardoso Administration, continue to be the most important parties in the Brazilian legislature. Moreover, the PFL, the conservative party with strong roots in the Northeast, occupies a significant presence in both houses, but has had an especially strong effect in the Senate in terms of being able to block agrarian reform. However, we should note that there is no tradition of party

discipline in Brazil. Politics often tend to follow particular leaders, and parties themselves are not so set ideologically. The PT is the only party with clear ideological and consistent organizational traditions.

Mexico

In Mexico, the President has negotiating authority over international trade treaties. Treaties must then be approved by the Senate. Following such approval, they are considered part of the law of the land. For many years, the PRI (Institutional Revolutionary Party) dominated Mexican politics. Changes by leadership within the party led to the present encouraging attitude towards trade liberalization, and was highlighted by the NAFTA treaty in 1994. Since then, Mexico has continued to pursue a vast array of free trade agreements internationally. However, at present there is some degree of tension between the new President, Fox, who is a member of the PAN (National Action Party), and the Mexican Senate, which is split almost evenly between the PAN and the PRI.

Mexico 2000 Legislature

Political Party or Coalition	Senate	House
	Total	Total
Partido Revolucionario Institucional	58 45.31%	210 42.00%
Alianza por el Cambio	53 41.40%	224 44.80%
Alianza por México	17 13.28%	66 13.20%
Total	128 100%	500 100%

With the PRI's long history of developing the Mexican bureaucracy and state institutions, it has been able to block Vicente Fox's main initiatives towards changing the nature of the Mexican state. Moreover, the PRI has a potential ally on the domestic side with Alianza por Mexico, which is an alliance of leftist and nationalist parties, led by the PRD. However, the PRI itself chose to push through the NAFTA accord, therefore they would be unlikely to block the passage of an FTAA. However, there remain strong elements of nationalism within the PRI as well as support within the bureaucracy and state-owned companies (such as Pemex), so that they could constrain Fox's negotiating strategy. Already, Fox's attempts to open up the energy sector have been slowed down.

In terms of formal consultation, the Mexican government relies upon the Advisory Council for Trade Negotiations, and the Coordinating Body of Foreign Trade Business Associations (*Coordinadora de Organismos Empresariales de Comercio*

Exterior, or COECE), which represents large businesses with an international orientation. The Advisory Council was set up in 1990 in preparation for the NAFTA negotiations and includes representatives of the private sector, academia, labor and the agricultural sector. COECE has 140 working groups, organized by sector. In addition, informal consultations were held during the NAFTA negotiations with members of civil society. In Mexico, the government Ministry of Trade and Industrial Production (SECOFI), seems to have the dominant hand in terms of the trade agenda.⁶

Environmental, Labour, and Anti-Globalization Movements

The environmental and labour groups of the U.S. successfully put pressure on Pres. Clinton during the ratification process of the NAFTA treaty. The results was the side agreements (or side payments, if you will) that established the separate agreements on environment and labour standards and created the North American Agreement on Environmental Cooperation and the North American Agreement on Labor Cooperation. However, the resulting commissions and policies have remained under fire by activists in the U.S.

Since the NAFTA agreement, protests at the meetings of various international forums, such as the World Trade Organization, the World Economic Forum, and the G-8, have witnessed increasing waves of anti-globalization protests. Yet, by most accounts, the movements remain quite fragmented and diverse, including elements of anarchists, Trotskyites, socialists, and more mainstream activists. One of the central claims of the movement is that international trade agreements and decisions are neither transparent nor participatory. The pressure from such groups has led governments internationally to take steps, such as increasing participative consultation, to defuse such challenges.

For the purposes of this analysis, it is important to note that the pressures from such groups are much more powerful and better organized in the North rather than the South. Thus, on the one hand environmental, labor, and to a lesser extent anti-globalization groups will have a great effect on the ratification process, levels of participation, and particularly the public discourse at the domestic level in Canada and the U.S. On the other, U.S. and Canadian policymakers will use the strength of these domestic groups to possibly leverage in concessions from their Latin counterparts. We should note that there is a budding industry of environmental equipment manufacturers in the U.S. that could also add some weight to this effort. However, in multilateral forums, Southern governments have maintained a strong and consistent position that neither environmental nor labor standards are open for negotiation in trade liberalization talks.

Conclusion on Treaty Ratification Procedures

On the basis of ratification procedures alone, we can make some interesting observations. Ironically, one of Putnam's observations is that if there are heavy domestic constraints, a negotiator at the international level can claim that he has less room for compromise to his colleagues. On the other hand, the size of the win set in terms of the

⁶ Carlos Alba V. and Gustavo Vega C., "Trade Advisory Mechanisms in Mexico," pp.55-64 in Inter-American Development Bank, Intal Division. 2002. *The Trade Policy-Making Process, Level One of the Two Level Game: Country Studies in the Western Hemisphere*. Occasional Paper 13.

ease of domestic passage allows negotiator greater leeway in reaching an acceptable agreement.

We can summarize our observations in terms of the following categorization. Mexico seems to have the easiest domestic situation for passage, followed by the U.S. In both cases, while there are divisions within the appropriate legislative branch, both major parties are pro-free trade. Canada and Brazil are much more problematic. In the Canadian case, diverse provincial interests weigh in on the present federal government's ability to negotiate international agreements, though there seems to be general support for free trade. Thus, Canada faces considerable domestic pressures in ratification. In Brazil, while the action will be focused in the domestic arena, there is a strong political sentiment against the FTAA already, reinforced by Brazilian President Lula of the PT (Worker's Party). Moreover, the lack of party discipline further complicates any easy ratification. Therefore, the U.S. and Mexico have the widest domestic win-sets, and Canada and Brazil the narrowest. It remains to be seen whether Canada and Brazil can use these facts to argue for better terms from an FTAA. As we discussed earlier, we should be careful with our conclusions in the sense that a known narrow win set could be used as a bargaining chip in negotiations.

From Allison's model, we must modify these conclusions. Mexico and Brazil seem to be highly insulated negotiating teams within the executive branch. The U.S., while also highly concentrated in the executive branch, must deal with intra-bureaucratic rivalries, such as differences between State, Commerce, and the U.S. Trade representative, and inputs from the business and labor committees. In Canada, with the parliamentary system, and the dominance of the Liberal Party, there is more likely to be a strong international negotiating team, but that team must coordinate with the provincial premiers, resulting again into more of a negotiating posture by consensus rather than the cost-benefit analysis implied by the unitary decision-maker model.

Once a treaty is negotiated, it must still be ratified by the legislature. On this front, the U.S., Mexico, and Canada all seem to have a strong position for passage of an FTAA, though sectoral elements will remain for negotiation. In Brazil, the history of party factionalism and lack of party discipline could make things difficult. However, if the PT can reach an agreement, it is likely that passage would be relatively smooth given that the centrist and rightist forces control most of legislative seats. As we have discussed, only in the U.S. and Canada are groups other than businesses, including labor, environment, and other civil society interests, a clear part of the consultation process.

Sensitive National Sectors

Perhaps one of the most important aspects of the negotiations for free trade is the effect that free trade will have on particularly important economic sectors. International trade theory, going back to the Stolper-Samuelson theorem on relative factor price equalization, has long been concerned with the distributional effects of trade. Free trade should theoretically increase the possibilities for competitive exporting products and

damage industries that are not internationally competitive or that compete with imports. While the net gains may be positive for consumers as a whole, furthermore, the losses from free trade will be more concentrated. Moreover, in political terms, those who benefit from the status quo are naturally better organized than those who might experience potential gains. In both the European Union (EU) and the NAFTA negotiations, sectoral issues are among the most difficult aspects of the negotiations, and gradual or permanent protection for sectors is at the heart of every free trade agreement, reflecting the domestic parameters of each negotiator's win set.

The key common sectors for negotiation in the NAFTA negotiations were agriculture, automobiles, and textiles.⁷ These were distinct from some of the issues that were tackled between the U.S. and Canada in their preceding agreement, where energy, culture, fishing, lumber, and liquor also counted.⁸ The MERCOSUR agreement's main sectors of contention were automobiles, textiles, footwear, and sugar. The agreement has provisions explicitly protecting Argentine and Brazilian interests in this area. We will identify the key sectors for each country which might be affected by a free trade agreement, both in terms of overall gains and in terms of losses due to competition.

The second line of analysis is to look at sectoral promotion policies, namely subsidization, anti-dumping provisions, and non-tariff barriers, and the related issue of rules of origin. Subsidization is a particularly hot issue, given the agricultural dominance of many of the smaller nations in the hemisphere, and the level of subsidies and protections for U.S. and Canadian farmers. An ongoing dispute between Canada and Brazil over subsidies to airplane manufacturers, combined with recent U.S. anti-dumping protection placed on Canadian lumber and Brazilian steel, reveals that manufacturing generally, and not just automobiles, will be a bone of contention. Rules of origin are key in terms of the U.S.'s fear that East Asian manufacturers will simply use Mexico or another country in the hemisphere to dump their own goods on the market. We will attempt to touch on some of these at the end of the section.

U.S.

The U.S. is the largest and most diversified economy in the world. However, the record of trade disputes and political activity indicates that there will be key sectors for negotiation in an FTAA. We can furthermore look at the areas of the U.S. economy that are most likely to be impacted as the ones that will be negotiated most stressfully. Given that most Latin American countries are primary product producers, a free trade agreement could have significant impacts on U.S. agriculture. While U.S. agriculture is not a large employer, it is geographically concentrated in the Midwest and Southeast, which gives the lobby strong numerical support in the Senate. Moreover, on the import side, the impacts on the automobile industry, which is a very strong lobby from the Midwestern

⁷ A good analysis of the NAFTA auto negotiations is found in David A. Lynch, "Negotiating with Goliath: Cross-national and Cross-level Interactions in NAFTA's Auto and Textile Sectors," in Bart Kerremans and Bob Switky, eds., *The Political Importance of Regional Trade Blocs*, Burlington: Ashgate, 2000, pp.241-75.

⁸ For an interesting study of the Canada-US free trade agreement, see Mordechai Kreinin, ed., *Building a Partnership: The Canada-United States Free Trade Agreement*, E. Lansing: Michigan State U. Press, 2000.

states, could be quite important, given the growing size of operations in both Mexico and Brazil. Given the recent anti-dumping findings in regard to steel, which affected Brazil, that could be another important issue for discussion. On the export side, the U.S. seems particularly keen to promote high technology, entertainment, financial, and related high revenue services. Therefore, intellectual property rights, investment, and dispute settlement will be key issues. We can also anticipate that the perennial issues of skilled labor and environment to be raised by unions and activists. Last but certainly not least, the California energy crisis as well as the continuing uncertainty in the Middle East mean that the U.S. has a strong interest in increasing energy exports from the hemisphere, and particularly from neighbors Canada and Mexico.

Canada

Canada is a diverse economy, but one in which industries are geographically concentrated, which highlights even more the importance of provincial-federal relations. Heavy industries and high technology companies are concentrated in Ontario and Quebec, though there are some other isolated areas of high tech activity such as the cities of Vancouver and Halifax. Most of the agricultural production, particularly in terms of grains, is concentrated in the prairie provinces of Saskatchewan, Manitoba, and Alberta. Alberta is also the center of the energy industry, including major exports of oil and natural gas, though many provinces retain public control over the electricity sector. British Columbia has been hard hit recently by softwood lumber tariffs imposed by the U.S. Both British Columbia and the Atlantic provinces also have strong interests in fishing exports. For Canada, then, both agriculture and natural resources, particularly energy, will be key issues. In particular areas, such as automobiles, telecommunications (Nortel), airplane manufacturing (Bombardier); and high technology, Canada will also have strong negotiating interests. Like the U.S., Canada will also be anxious to obtain investment security, particularly in the areas where it has a strong position, such as energy development (TransAlberta, QuebecHydro). For Canada, health care remains the most important national anxiety. With a strong and completely public health care system, Canada will undoubtedly protect this sector from the negotiations as it has in previous agreements.

Brazil

Like Canada, Brazil is also a diverse economy with geographic concentration. Northeastern Brazil is the center of fast growing commercial tropical agriculture, including cattle, orange juice, coffee, and nuts. Brazil's large and diverse industries are concentrated in the Southeast, particularly in the states of Minas Gerais, Sao Paulo, and Rio de Janeiro. Some parts of the Southern Brazil also contain coffee, cattle, and grain producers. In recent years, Brazilian heavy industry has been involved in a number of international trade disputes, such as steel, airplane manufacturing, and high technology. Brazil could make major gains in labor-intensive exports, such as shoes and sugar, but might be hard hit in the areas of industrial policy focus, such as energy and high technology. The energy sector is still dominated by the state company Petrobras, and high technology, such as computer manufacture has been heavily protected. Brazil also has a well-developed auto industry, though focused more on auto assembly. Because of its long tradition of industrial policy protection, dating back to the Vargas years of the

1950s, Brazil is unlikely to completely open its industrial sector. As in the case of Mercosur, Brazil will probably demand gradual or restricted opening for sensitive sectors.

Mexico

For Mexico, both agriculture and the maquiladora industry are key aspects to the FTAA negotiations. In terms of agriculture, Mexico should be competitive in terms of tropical agricultural products, like sugar and oranges, as well as selected grains (corn) and vegetables, such as tomatoes. On the other hand, other Mexican products, such as wheat and cattle, might be hard-hit by competition from U.S., Canada, and Argentine exporters. In terms of industry, Mexico has a high degree of vertical integration through the maquila system with U.S. multinational corporations, such as the large automobile companies. The maquila system, presently under pressure by lower Chinese wages, therefore ironically has a strong interest to prevent free trade which would mean the end of its privileged position in terms of access to the U.S. market. As in the NAFTA negotiations, the energy sector is highly sensitive for Mexico. The state oil and gas company, Pemex, continues to enjoy privileged monopoly status. Mexico's electricity sector is also highly limited in terms of foreign investment, though a domestic shortfall is expected.

Conclusion- Key sectoral issues

In terms of sectoral issues, we can use our concept of issue linkage to attempt to anticipate the possible trade-offs and quid pro quos that could be embodied in an agreement. Clearly, in regard to agriculture, Brazil, Argentina and a number of other producers in specific products and countries will be pushing for liberalization. A key issue will be the massive subsidies going to U.S. and Canadian farmers. Moreover, highly protected sectors such as sugar and oranges/orange juice will be important topics. In certain niches, such as possibly wheat and corn, the U.S. will, on the other hand, push for greater liberalization. In terms of heavy industry, the U.S. and Canada will likely seek to halt or condition liberalization, while Mexico and Brazil will push for liberalization. On the other hand, the U.S. and Canada will be heavily in favor of energy liberalization, while the larger Latin American countries will seek to protect their state-owned industries. The U.S. will push particularly hard for intellectual property rights and high technology industry liberalization, while other countries will seek to preserve their protection and subsidies of the same. We can predict, therefore, that the main general axis of issue linkage will be agriculture and heavy industry vs. energy, high technology, and services, including investment. The most interesting role will be played by Mexico, with its obvious close ties to U.S. interests on the one hand, but with other areas of its economy, such as certain sectors of agriculture and energy, more closely following the lead of Brazil.

Existing Bilateral and Multilateral Agreements

Having identified some of the initial elements of each major country's win-set, we can turn to sub-regional level agreements. Naturally, existing bilateral and sub-regional

agreements such as NAFTA and MERCOSUR have to be harmonized with an FTAA. By detailing the agreements here, we can take a first step towards estimating how the agreements will affect FTAA negotiations. For example, sub-regional groupings such as MERCOSUR, or bilateral agreements such as Mexico-Brazil, could aid the process of building together sub-regional coalitions that could then increase their leverage vis a vis the U.S. or other partners. In the same way, the U.S. could find allies through issue linkage in bilateral agreements to possibly block the formation of such coalitions.

U.S.

The U.S. is the main architect of the multilateral trading order in the world. It is the key player in the G-8, the WTO, and the OECD. In the Western Hemisphere, the U.S. has been hesitant to sign further trade agreements, perhaps in part because it prefers a multilateral approach that would make harmonization with its multilateral role easier. Moreover, by negotiating an FTAA altogether, the negotiation process is likely to be not only much easier, but also reduce the amounts and types of concessions that might occur if the U.S. negotiated with each country separately. On the other hand, the U.S. would like to keep the rest of the countries from creating a negotiating bloc, which would change its level of leverage, and so concessions to each country. With the largest market in the world by far, the U.S. should be able to gain highly favorable terms in return for market access. The U.S.'s primary agreement is NAFTA, though it does also provide privileged access to the Caribbean through the CBI program. The U.S. has also been involved in ongoing negotiations with Central America and the Andean Pact on free trade.

Canada

Besides NAFTA, Canada has signed free trade agreements with Chile (1997) and Costa Rica (2001). Canada is also a member of the WTO, the OECD, and the G-8 so it also has a strong hand in multilateralism. Like Mexico, Canada feels a very heavy dependence on the U.S., and sees an FTAA as one of the most plausible ways to reduce it. Canadian exporters are also keen to gain market access to Latin America. Canada's strategy seems to be, like Mexico's, to attempt to ally itself with some smaller partners to gain leverage.

Brazil

As a founding and key member of MERCOSUR, Brazil has a strong interest in creating an anti-U.S. bloc during FTAA negotiations. However, its production profile and interests are different from many of the other nations in the hemisphere, and the U.S. may be able to reach smaller concessions with key countries on separate side agreements in order to prevent such a large alliance from taking hold. Within MERCOSUR, Chile as an associate member has left its options open, signing free trade agreements with various regional partners, including Canada, Mexico, Bolivia, and most recently, outside the region with the European Union. Secondly, Argentina, has more recently, especially under Menem in the 1990s, flirted with a more pro-U.S. and independent foreign policy than Brazil would like. Still, with the recent economic meltdown in Argentina and the devaluation of the peso, there seem to be possibilities for greater rapprochement between the two giants of the Mercosur.

Mexico

Besides NAFTA, Mexico has signed a myriad of bilateral agreements, including ones with the European Union; with Chile; with a number of Central American states; with Group of 3 partners Colombia and Venezuela; and with Bolivia. Mexico has also just reached an “economic complementation” agreement with MERCOSUR and separately with Brazil. Mexico therefore clearly seems to be following a strategy of attempting to reduce its heavy dependence on the U.S.

Conclusion- Existing Agreements

The U.S. has an interest in having a short and clear FTAA negotiating process in which it is the dominant partner dictating terms to smaller countries. Brazil and Mexico’s recent trade facilitation agreement, however, indicates, that large Latin American countries recognize the benefits of a united negotiating posture. This might explain the recent progress in both the Caribbean and Central America towards further trade agreements with both the U.S. and other Latin American countries. Moreover, to the extent that Canada is able to link up with her Southern neighbors, she can also create more leverage to try to balance the U.S.’s terms. This helps us to explain her recent agreements with Chile and Costa Rica. The “middle level” players, such as Venezuela, Colombia, and Peru, are therefore key to the outcomes of this shuffling process. Venezuela under Chavez has come out strongly against the FTAA, which hurts the process generally, but also the chances for Latin American solidarity. On the other hand, the Andean Pact has attempted to reach an agreement separately with the U.S. Similarly, the U.S.’s movement towards free trade with Central America could be interpreted as a way to “pick off” possible partners for an anti-U.S. coalition during negotiations. Last but not least, the dalliance of the Latin American countries with the European Union is another interesting strategy to try to counterbalance U.S. presence. Recent E.U. agreements with Mexico and Chile demonstrate the promise of this approach for Latin American countries. However, because of its social welfare programs and its heavily protected agricultural sector, the EU is unlikely to act as a true alternative to the U.S. Ongoing negotiations with the MERCOSUR seem to have borne little real fruit, for example.

Conclusion

While acknowledging that the dominating size and diversity of the U.S. economy give it strong leverage in the FTAA negotiations, we have demonstrated in this paper that there are a number of avenues open to the other countries in the hemisphere to attempt to counter-balance this asymmetry. We have also demonstrated that the domestic, the regional, and the international political economies are inextricably inter-woven, allowing for not only domestic, but also international coalitions for and against free trade. The real trick of the negotiators will be to create an adequate win-set for the agreement both on the domestic and international levels. Using issue linkage and the insulation sometimes provided by differences in domestic ratification procedures and norms, negotiators will seek to maximize national gains while ensuring that the other states have an equal interest in preserving the long-term viability of an agreement.

Still, we must recognize the staggering complexity of such a bargaining process. Not only are there a wide asymmetry of power variables, including population, economic, territory, and military size, from small Caribbean islands to middle-level countries like Colombia to the powers Brazil, Mexico, and Canada, before we reach the U.S., but there are a huge number of factors that could create potential coalitions, including common sectoral concerns, anti-imperialistic political traditions and domestic constituencies, regional rivalries and commonalities, such as Ecuador and Peru (both members of the Andean Pact with a border dispute). Moreover, as Moravcsik points out, domestic leaders will likely seek not only to influence negotiating partners' positions, but also to dynamically shape their domestic win-sets. They may

“shape the formal and informal ratification procedure (e.g., voting rules, status of the agreement under separation of powers, party discipline, agenda-setting, issue linkage) or alter the domestic balance through side-payments, enforcement of party discipline, selective mobilization of political groups, or manipulation of information about the agreement. (More radically, they may seek) to implement a broad program of social or institutional reform.”⁹

The international bargaining literature also points out that state negotiators also have the ultimate tool of the threat that the treaty will not pass both on the international and domestic level, however the threat must be credible and therefore is unlikely to be effective if used often. More importantly, on the international level, the value of such a threat will be commensurate with the relative power of the country. That is, the relative value of having that country included in the agreement will determine the level of its veto power. Thus, the more important negotiations during most of the period will be in terms of sectoral and issue linkage. As collective action theorists such as Mancur Olson and interest group theorists such as Helen Milner, Robert Rogowski, and Peter Gourevitch have pointed out, the level of organization, the salience of the issue, and the amount of resources that an interest group controls will have major impacts on its power to shape foreign economic policy. Thus, a statesman can use a well-organized private interest in as a semi-veto threat, that is, he/she can use the need to placate or feed a powerful domestic interest group who support is supposedly needed for passage to wring concessions from trading partners. To the extent that those trading partners have a common production profile but face powerful domestic interests in different sectors, issue-linkage and side-payments (partial or full concessions, such as gradual liberalization) can take place. As noted above, the emerging areas of issue linkage on an international level are likely to take place among the non-US countries' interests in natural resources (mining, energy), agricultural, and heavy industries (steel, automotive) sectors on the one hand, and the U.S. interests in investment, financial services, and intellectual property issues on the other. We should not discount either the “wild card” variable in the FTAA negotiations process- namely the push of anti-globalization, labor, and environmental activists in the U.S. and Canada to reform both the participatory

⁹ Andrew Moravcsik, “Introduction: Integrating International and Domestic Theories of International Bargaining,” p.27, in Peter B. Evans, Harold K. Jacobson, and Robert D. Putnam, *Double-Edged Diplomacy: International Bargaining and Domestic Politics*. Berkeley: U. of California Press, 1993.

process and to include their issues in the discussion. While transnational linkages are more likely to form along business lines, given the fragile state of many Latin American economies, international synergies along the lines of protest of an FTAA, with the FTAA becoming a proxy scapegoat for general economic unhappiness, should not be surprising.

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