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TRADE POLICIES IN A HEAVILY INDEBTED ECONOMY: BRAZIL, 1979-1990

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Trade Policies in a Heavily Indebted Economy: Brazil, 1979-1990[1]

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The main objective of this paper is to consider the formulation and implementation of trade policies in Brazil during the 1980s, a period marked by overall balance of payments vulnerability due to heavy foreign indebtedness accumulated before 1982 and by very poor economic performance if compared to the long term trend. An effort is made to understand how distinct and changing vested interests affected negotiating stances as well as the links between trade developments in the bilateral level and stances in multilateral trade negotiations. The increased leverage of multilateral financial agencies as a factor to explain shifts in trade policy is also considered. The recent overhauling of decision-making arrangements in the trade policy area and liberalizing moves are assessed in terms of policy sequencing, coherence and sustainability in the longer term.

The paper is divided in four sections besides this introduction. Section 1 considers trends in trade performance and evidence on the obstacles which have constrained access of Brazilian exports to developed markets since the early 1980s. The next section deals with negotiations in the GATT, especially in connection with the Uruguay Round of Multilateral Trade Negotiations. Section 3 examines relations with multilateral financial agencies, especially the World Bank and the IMF, and implications for trade policy. The final section considers recent liberalization in Brazilian trade policy in the context of policy trends established in the past and presents conclusions.

1. Trade Performance and Market Access in Developed Countries in the 1980s

The 1980s are commonly referred to as the lost decade in Brazil as GDP per capita actually fell, in sharp contrast with long term trends. GDP in 1980-89 increased at the yearly rate of 2.2% whereas it had increased at 7.1% yearly in 1973-1980 and 11.2% in 1967-1973 (see table 1 for data on GDP in the 1980s). In 1990 it decreased by a further 4.6%. International economic policy was based on a blend which included export promotion, import substitution and foreign indebtedness. Mediocre growth performance resulted from a particularly destructive combination of high inflation and foreign exchange constraints related to the reversal of Brazil's role as an importer of real resources after 1982. This is not the place to delve into the main causes of the deterioration of the Brazilian growth performance, but a balanced view of the process would certainly require a mix of arguments related to the structural inability to finance public expenditure and the generalization of indexation rules which made inflation at least partly an inertial phenomenon (see table 1 for data on inflation, foreign debt and the flow of real resources)[2].

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2 Those interested in a full treatment of Brazilian economic policy in the 1980s should consult Carneiro and Modiano (1990) and Modiano (1990).

Attempts to face the debt crisis in the early 1980s led to the adoption of recessive policies together with a realignment of the real exchange rate in relation to the US dollar of around 40% in 1983-86. This was, however, followed by appreciation of the domestic currency against the dollar: in 1989 the average real exchange rate was back to its 1981-82 level. It has fluctuated significantly in the recent past as a result of successive failures of stabilization efforts in 1990-91.

Table 1

Brazil: Main macroeconomic indicators, 1980-1990

	GDP Yearly Rate of Change (%)	GDP Deflator Yearly Rate of Change (%)	Foreign Debt (US$ billion)	Balance of Trade and Non-factor Services (% GDP)
1980	9.3	90.3	64.2	-2.5
1981	-4.4	107.0	74.0	-0.4
1982	0.6	105.0	85.3	-0.7
1983	-3.4	140.0	93.6	2.4
1984	5.3	213.0	102.0	5.7
1985	8.0	232.0	105.1	5.2
1986	7.5	146.0	111.0	2.5
1987	3.6	204.0	121.2	3.3
1988	-0.1	648.0	113.5	5.2
1989	3.2	1323.0	115.1	3.2
1990	-4.6	2848.9	121.0	1.6

Source: Central Bank of Brazil.

Export performance was outstanding between 1979 and 1984, but less so since the mid-1980s (see export values in table 2). There was a marked product diversification away from raw materials or semi processed goods in favour of manufactures (see table 2). Manufactured export prices fell until the mid 1980s as a result of the vent for surplus stance of domestic producers[3]. Brazilian exports remained small both as a proportion of world total exports (around 1.1%) and of GDP (around 10%).

Table 2

Brazil: Exports and Imports, Selected Years, 1964-1989 (US$ million)

	Total Exports FOB	Manufactured Exports (Braz.def.) FOB	Total Imports FOB	Mineral Fuel Imports FOB
1979	15,244	6,645	18,083	6,773
1981	23,293	11,883	22,091	11,340
1982	20,175	10,253	19,395	10,623
1985	25,639	14,063	13,153	6,176
1986	22,348	12,404	14,044	3,541
1987	26,224	14,839	15,052	4,709
1988	33,787	19,188	14,605	4,136
1989	34,383	18,634	18,263	4,430
1990	31,391	16,988	20,593	5,288

Sources: Central Bank of Brazil.

Export product diversification was matched by market diversification until the early 1980s as the shares of Latin America, Africa and the Middle East in total exports increased significantly. This was partly explained by the growing importance of barter trade with the Middle East, as Brazil was severely hit by the rise in oil prices. After the debt crisis and with the fall in oil prices these trends were reversed and markets in developed countries partly regained their former importance, especially in the case of the USA as its economy recovered from the recession in the early 1980s and the dollar was overvalued in relation to other key currencies. These trends were even more marked for manufactured exports[4].

The sharp reversal of Brazil's trade balance in the early 1980s is explained not only by the rise in exports but also by a significant contraction of imports, initially as a result of a strengthening of controls under the provisions of GATT article XVIIIb and other protective policies, then mainly by the reduced rate of growth of GDP. Import volume by 1989 was still almost 20% below its 1979 level in spite of a GDP growth over the decade of more than 30%. Much of this is explained by the initial reliance on imported oil and its sharp reduction by a combination of substitution in consumption and increased domestic production. This led to the reduction of the share of oil in total imports from more than 50% to about 25% between 1981 and 1990. Non-oil imports were also significantly reduced. The geographical origin of imports reflected the importance of oil imports. Indeed, the non-oil import shares of the US and the EC in Brazil are similar and stable since 1979.

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3 Subsidies and exemptions (fiscal and credit) declined from 28.8% of the value of exports in 1979 to 3.9% in 1980 then rose back to almost 30% and fell rapidly to around 5% in the mid-1980s. See Baumann and Moreira (1987).

4 The US share rose to almost 30% of total exports in the mid-1980s but was in 1989 down to 23.3% in comparison to an EC share of 28.9%. The combined Middle East-Africa-ALADI share, which reached more than 26% in 1982 was around 17% in the end of the 1980s. The US was, however, absorbing 35% of manufactured exports as compared to 21.5% by the EC and 23.2% by the new markets. These had bought more than 40% of Brazil's manufactured exports in the late 1970s.

Brazilian exports faced severe restrictions of access to the markets of developed countries. Evidence on this is notoriously difficult to interpret: data on the proportion of trade affected by non tariff barriers (NTBs) suggest that barriers to Brazilian exports to developed countries in 1986 were relatively more important than those faced by exports from Latin America as a whole or from all developing countries, especially in the US market, which was however significantly less protected than the EC. These obstacles affected especially exports of processed tropical products, certain temperate climate agricultural exports, iron and steel products, textiles and clothing, and shoes[5]. There is evidence that these restrictions have been reduced since 1986 as data presented in Table 3 suggest.

Table 3

Brazil: NTB Coverage Ratio by Exported Product in the Main Developed Economies, 1986-1989

	USA		Japan		EC	
	1986	1989	1986	1988	1986	1988
Food Products	25.5	16.9	96.4	99.0	13.6	12.2
Agricultural Raw Materials	1.8	0	14.7	14.9	5.1	6.3
Minerals and Metals	37.1	46.3	0.1	0	11.7	16.7
Iron and Steel	81.9	81.9	0	0	74.2	88.0
Fuels	92.0	97.9	0	0	0	0

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5 See Tables 10.1 and 10.2 of Abreu and Fritsch (1989) which also presents a discussion of obstacles to Brazilian exports in relation to graduation in the Generalized System of Preferences, tariff escalation, agricultural products, textiles and clothing as well as subsidy countervailing duties (CVDs), antidumping duties (ADs) and gray area measures such as voluntary export restraints (VERs).

Chemical Products	37.6	3.3	100	92.8	2.2	1.5
Manufactures	19.5	7.3	62.7	56.3	22.9	32.6
Leather	0	0	20.6	13.6	24.4	99.6
Textiles	74.6	71.1	50.3	37.8	90.8	86.5
Clothing	96.7	97.0	0	0	92.6	96.6
Shoes	0	0	79.1	0	100	100

Source: computations based on Smart data base. EC ratios concerning food products may have been affected by incomplete information.

Bilateral trade disputes especially with the US but also with the EC have affected the growth of Brazilian export trade in many products in the recent past. Barriers take the form of ADs and CVDs, the imposition of VERs by importing countries and actions under the US Trade Act to redress alleged injury to US interests.

Brazil faced more countervailing subsidy initiations than any other developing country in 1980-86. After Mexico, Brazil also led the list of countries affected by provisional measures and definitive duties. Similarly, with the exception of initiations -- in relation to which it has suffered marginally less than South Korea -- Brazil was the developing country which led the table of developing countries subject to anti-dumping actions concerning the imposition of provisional measures and definitive duties as well as price undertakings[6].

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6 GATT, set of tables, Committee on Subsidies and Countervailing Measures and Committee on Anti-Dumping Practices, [1986], data provided by CTT/Brazilian Government and GATT (1990). The argument that it is natural that the countries which dump and subsidize more should suffer more actions fails, of course, to cope with the fact that ADs and CVDs are misused to unfairly dissuade new suppliers, which are more competitive, from entering the markets

In the US market, AD and CVD actions have affected Brazilian exports such as airplanes, iron and steel products, paper products, plywood, tools, cotton yarn, chemical products (ethyl alcohol, fatty acids, oxalic acid and cyanuric chloride), petrochemical products, orange juice, castor oil, and footwear. EC actions have affected mainly steel products, paper products, textiles, pig iron, footwear and soybean products[7]. Bilateral negotiations aiming at the suspension of AD/CVD duties usually result in the introduction of voluntary export restraints (VERs). In the case of Brazil they mainly affect steel and iron products both in the US and EC markets.

There are indications that after 1986 Brazil was relatively less affected by AD and CVD actions at least in part because of the use of other instruments. Thus Brazil has faced US actions under Sections 301 of the Trade Act of 1974, as amended, and "Super 301". Of 79 investigations under Section 301 between 1975 and the end of 1989, 29 were against developing countries of which 5 against Brazil (Republic of Korea 8, Taiwan 6, Argentina 5 and India 3)[8]. Brazil was the only developing country which suffered retaliation as in October 1988 action was taken by the US

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of developed countries.

7 UNCTAD NTM inventory, IPEA/CEPAL (1985a) and (1985b) as well as data supplied by CTT/Brazilian Government.

8 GATT (1990), pp. 262-5.

imposing tariffs of 100% on Brazilian paper, pharmaceutical and electronic products entering the US market. This resulted from a complaint by the Pharmaceutical Manufacturers Association that the Brazilian intellectual property legislation did not provide adequate protection for US pharmaceutical patents. This case prompted Brazil to ask for the establishment of a GATT panel (see section 2 below) and was concluded only in June 1990 as Brazil provided assurances that it would change its legislation so as to increase the protection of process patents.

The other notorious 301 case affecting Brazil was related to the informatics policy, in particular concerning software legislation. The case was initiated by the United States Trade Representative (USTR) in 1985 based on grievances concerning access to the Brazilian software market, protection of intellectual property in relation to both software and hardware and administrative procedures adopted by the Brazilian authorities in the informatics sector. The case was only concluded in October 1989 after changes in the relevant Brazilian policies[9].

Brazil was designated in May 1989 with Japan and India as one of the priority countries for possible application of retaliation under Super 301. Investigations should start in relation to the Brazilian import licensing system. The striking

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9 See SELA (1987), pp. 15-28 for details.

feature of this decision is that by concentrating its attention on the trade surplus it made explicit the contradictory aims of US foreign economic policy in Brazil as it is difficult to see how foreign debt could be serviced - even at a much reduced level in relation to initial contractual terms - without the generation of trade surpluses with developed countries. The controversial first application of Super 301 was suspended in May 1990 in the wake of Brazil's decision to significantly liberalize its import licensing procedures. While Brazilian good behaviour may have helped to avoid statutory retaliation it may be noted that other countries have escaped until now Super 301 retaliation without making substantial concessions[10]. New American goodwill in trade matters towards a more liberal Brazil was also expressed by the reversal of a long standing policy concerning graduation of products enjoying preferential treatment under GSP as preferences were restored in 1990 for products whose trade covered about US$ 0.5 billion.

2. Brazil in the GATT

Brazil is a poor but active GATT founding father[11]. Involvement before the early 1960s was mainly related to the renegotiation of tariff schedules and the Brazilian-Uruguayan

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10 See GATT (1990), pp. 264-5.

11 For a detailed account of Brazilian experience in the GATT see Abreu (1991).

initiative concerning nullification or impairment of obligations (article XXIII) which proposed the principle of financial payments by developed to developing countries for violations of the General Agreement[12]. The best efforts of Brazilian commercial policy diplomacy until the Tokyo Round, however, were to be devoted to the negotiations in UNCTAD, in particular in connection with GSP.

Brazilian trade policy to the 1960s was to a large extent that of a commodity exporter with a fragile balance of payments and an industrial policy based on import substitution. Import substitution policies have had a long, and until the early 1980s, extremely successful history in Brazil[13]. "Modernization" entailed by the change of political regime in the mid-1960s included the strengthening of links with the international economy but this was a rather asymmetrical affair as more liberal policies concerning direct foreign investment, less distorted foreign exchange policies, and export promotion policies were not matched by a significant reduction in barriers to imports[14]. Quite on the

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[12] See Dam (1970), pp. 368-70. See also Hudec (1975), p. 222, and GATT (1966), p. 18.

[13] This contrasts with the experience of other Latin American countries such as, notably, Argentina, but also Chile and Mexico. Brazilian GDP per capita stood in 1913 at 10% of the level of Argentina's, 30% of Chile's and 40% of Mexico's. In 1989 Brazilian GDP per capita was considerably above the level of these other countries (World Bank data).

[14] Import liberalization was an important element of the policy package introduced in the mid-1960s but for reasons not entirely clear the move towards tariff reduction in 1967 was clearly reversed in the end of 1968, see Coes (1991),

contrary, balance of payments difficulties in the 1970s served as argument for the imposition of severe quantitative import controls.

In the 1970s, during the Tokyo Round, the issue, besides the GATT codes, which involved closer Brazilian involvement was the reform of the GATT system. Negotiations within the so-called Framework Group originated with a Brazilian proposal which included: the provision of a standing legal basis for GSP so as to make the preferences legally binding and their withdrawal subject to compensation; greater flexibility in the use of article XVIII for balance of payments and development purposes; improvements in dispute settlement; the right of developing countries to non-reciprocity. Developed countries were mainly interested in dispute settlement matters and in the limitation of the use of export controls by developing countries. The US initial stance was to stress the American unwillingness to relegate the MFN clause to a residual role and that developing countries should be prepared to forego special treatment as they achieved their development goals[15].

The Framework negotiations resulted in four agreements. An enabling clause consolidated the waiver allowing non-reciprocity based on differential and more favourable treatment for developing

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15 See Maciel (1978) and Winham (1986), pp. 144-146.

countries and as a quid pro quo a general statement was included on the principle of graduation of developing countries and their fuller participation concerning obligations as they reached higher levels of development. Resort to article XVIII for both balance of payments and development purposes was made easier or more expedite but there were no fundamental changes. On notification, consultation, dispute settlement and surveillance the US pressed for a more automatic process based on majority vote but EC support for a consensus approach was important to avoid a backfiring of the Brazilian initiative. No agreement was reached on export controls[16]. The concessions made by developing and developed countries were thought to have been more or less equivalent. The initial Brazilian objective to try to compensate the inherent disequilibrium of retaliation power due to differences in size was certainly contained by the counterproposals of developed countries.

In the period before the launching of the Uruguay Round Brazil took a markedly defensive stance in the discussions which preceded the 1982 GATT Ministerial Declaration as occurred with several of the more advanced developing countries. They resisted the introduction of "new issues" related to Trade-Related Intellectual Property, Trade-Related Investment Measures and, especially, trade in services, in the draft agenda for the next

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16 See Winham (1986), p. 274 ff.

multilateral trade negotiations. The main objection of developing countries to the inclusion of trade in services in the GATT framework was that negotiations in services would tend to diminish the importance of the traditional GATT issues which composed the backlog of unfinished business from the past which was of great importance for them. There were, moreover, doubts, shared by some developed countries, on whether this new issue should be treated in a multilateral framework and within the GATT in view of the large number of sector specific issues involved and of the work of other specialized international organizations.

In several instances in the history of multilteral negotiations in the GATT Brazil was vulnerable to bilateral pressures, especially from the US, to modify its stance. The most important code negotiated in the Tokyo Round from a Brazilian point of view was the one on subsidies. This was basically a negotiation between the EC and US but it had great importance for Brazil, as for code signatories US countervailing actions had to be based on material injury findings and the US market was relatively more important for Brazilian manufactured exports than for Brazilian total exports. The quid pro quo was a commitment by Brazil to abolish by June 1983 the subsidies entailed in the credit premia system which allowed tax credits over and above export tax exemptions, as well as freeze levels of subsidy. Brazil's new position resulted from the assessment by the Ministry of Finance that the bilateral Brazilian position in relation to the US was untenable and some concession had to be made. This was a low ebb in the relations between the Brazilian Ministries of Finance and Foreign Affairs[17].

In 1982, trade and debt negotiations were linked in a very peculiar form. The 1982 GATT Ministerial Declaration included an explicit statement about some of the new themes. This was at least partly related to a wavering in the stand of some of the more active developing countries as was the case of Brazil which agreed with such an inclusion while at the same time stressing that this did not affect its substantive stand in favour of a backlog-based agenda. In the second semester of 1982 Brazil was in an extremely fragile external financial position following the Mexican debt crisis. A bridge loan by the US Treasury was an important source of foreign exchange while the IMF considered the Brazilian position. Also in November 1982 the US agreed to a two-year extension of the time span defined in 1978-79 for Brazil to discontinue payments related to the export credit premia scheme. It is difficult to see all these questions as unrelated[18].

The long negotiation process in the GATT which preceded the launching of the Uruguay Round in September of 1986 was marked by the continuous friction over the agenda between a small group of developing countries -the so-called G-10 formed by Argentina,

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17 See Lima (1986), pp. 330-336.

18 See Lima (1986), pp. 338 and ff.

Brazil, Cuba, Egypt, India, Nicaragua, Nigeria, Peru, Tanzania and Yugoslavia - and the developed countries[19]. The frictions continued to center on the new issues and especially on services.

Two agenda proposals were presented at Punta del Este: one, by Colombia and Switzerland, initially supported by the developed countries and many developing countries, included all the new themes; the other, by the G-10, which included only the backlog. The Colombian-Swiss draft, however, could not resist the EC's dissatisfaction with its wording on agriculture. EC's role was also important in supporting the consensus unwritten rule thus avoiding that the US view prevailed on bringing matters to a vote and breaking more effectively the resistance of the G-10 on the new themes[20].

The Uruguay Round declaration formally reflected a compromise as new themes other than services were included in the undertaking to enter into the general negotiations according to the General Agreement and separate negotiations were launched for trade in services. It was decided to create a Group on Negotiations on Services - outside GATT but with GATT support and

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19 See Kumar's chapter in this book on coalitional behaviour of developing countries since the 1960s.

20 Frictions between the US and the EC included US dissatisfaction with EC behaviour in vaguely supporting the G-10 in exchange for a softening of commitments on agricultural liberalization. EC support of the consensus rule and of the two-track compromise are consistent with such understandings.

applying GATT procedures and practices - a decision on the implementation of its recommendations being postponed.

The agenda of Brazilian active interests in the Uruguay Round can be summarized as consisting of tariff matters, temperate agriculture products, textiles and clothing, as well as "rule making" issues, such as anti-dumping, subsidies countervailing as well as safeguards. In relation to the new themes the natural stance was defensive, especially so in the case of intellectual property (TRIPS) and trade related investment measures (TRIMS)[21].

Tariff matters include graduation under GSP schemes, tariff escalation and tariff preferences. Tariff graduation under GSP may affect harshly some specific products but is not an overall important issue as trade gains entailed by GSP are thought to be around 1% of total exports. Tariff escalation affects a high proportion of Brazilian exports of primary and semi-manufactured products especially in the case of coffee and cocoa product chains. Brazilian interests are also unfavourably affected by the continuation and/or expansion of such preferential trade arrangements as those entailed by the Lomé Convention and the US Caribbean Basin Initiative. But to press for the elimination of

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21 For a detailed discussion of Brazil's concrete interests in the several negotiating groups see Abreu and Fritsch (1989). For an overall assessment of the interests of developing countries in the negotiations see Abreu (1989).

these would involve large political costs and would undermine relations with a large number of developing countries.

Brazil was an early member of the Cairns group of countries that was formed to counter protectionist trends which affect agricultural products[22]. The initial motivation was political as it was not a priori clear cut whether Brazil was to gain from the dismantlement of temperate agriculture protectionism. Estimates of the impact of the removal of all barriers on this trade suggest that Brazil gains in relation to sugar and beef would more than compensate the losses related to higher wheat prices and decreased soya exports as inefficient purchasers of feed stuff such as the EC are superseded by more efficient meat producers using more land-intensive technologies[23].

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22 See Tussie's chapter in this book on the role played by the Cairns group of countries since 1985.

23 See Abreu and Fritsch (1989) for rough estimates of the impact on the Brazilian trade of main temperate food commodities of a liberalization of protectionism in the developed countries. More recent estimates by Anderson and Tyers (1990) suggest large Brazilian gains, from both welfare and balance of trade points of view, with liberalization in the developed countries and also with the removal of all food price distortions in all countries.

During the Uruguay Round negotiations it became increasingly difficult for the small group of developing countries to maintain their stance of opposition to the consideration of new themes before the backlog had been given adequate consideration. Political support in the capitals flagged as some of the more important developing countries faced severe macroeconomic difficulties and became more vulnerable to pressures to yield. There was a growing sense of isolation. The heterogeneity of negotiating basic interests of different developing countries became clear not only in relation to trade-debt links but also in relation to trade matters: the importance of agricultural issues for Argentina, for instance, became an increasingly dominant factor in shaping her stand in relation to other issues. So the difficulties which had plagued the working of a G-77 style coalition of developing countries started to become explicit also in the case of the G-10.

Even before the change of course of economic policy towards trade liberalization, when the Collor administration took office in early 1990, Brazil's stance in the GATT became less visible, objections were toned down, positions reversed. Membership of the Cairns group, which had been initially seen with mixed feelings, became increasingly important as the emphasis of Brazilian policy in the GATT singled out agricultural liberalization as the most important issue in which Brazil could be a demandeur. So Brazil played a crucial role in Montreal's 1988 GATT Mid-Term Review in turning Argentina's strong reaction to the lack of results in agriculture into a position of all the Latin

While the former qualitative assessments of the impact of a dismantlement of MFA on Brazilian textile exports suggested that Brazil would lose from it, these estimates have been reversed by more recent research work which includes Brazil among the big gainers with textile and clothing trade liberalization [24].

The importance of ADs, CVDs and VERs has already been noted in section 1 but it is extremely difficult to assess the concrete losses entailed by such actions given the importance of export dissuasion[25].

Given supply response difficulties in developing countries it is unlikely that they would be significant <u>demandeurs</u> in services. It is, of course, true that liberalization of services shall improve the competitiveness of developing country exports, as it would enhance economic efficiency, but this an altogether different argument which has to do with economics and not with negotiations in the GATT which are based on the exchange of "equivalent concessions". It is also hard to see developing countries as <u>demandeurs</u> in TRIPS and TRIMS.

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24 See Trela and Whalley (1988).

25 Very rough estimates of impact on exports of VERs can be found in Abreu and Fritsch (1989).

American members of Cairns. This obstruction, counting with US support, made possible to put results "on hold" until more acceptable drafts could be negotiated in Geneva in April 1989. Brazil's newly found agricultural enthusiasm led to a still clearer stand in the ill-fated Brussels meeting of the GATT in the end 1990 as Brazil once again played a significant part in refusing to proceed with the negotiations while results where not obtained in agriculture. These new stances have to be understood in the context of fatigue of obstructive policies concerning the new issues, of the change of course in economic policy and of the importance ascribed by the Brazilian new administration to improvement of relations with the US government and consequent support in the foreign debt negotiation.

There were in the 1980s many instances of consultations and panels of Brazilian interest in the GATT, both as a complainant (the Brazil-Spain 1980 panel on the tariff treatment of unroasted coffee, the consultations held in 1982 on the EC sugar export refund system in which Brazil was one of the ten countries involved, the 1986 Brazil-US consultations on US tariff on ethyl alcohol, the protracted Brazil-US dispute on CVD duties charged on non rubber footwear, the 1988 Brazil-US consultations on the unfavourable impact of US ubsidies under the Export Enhancement Program on Brazilian exports of soya bean oil) and as a defendant (the US 1983 complaint on Brazilian violation of Code of Subsidies in relation to poultry exports, the US-Brazil 1987 aborted consultations on restrictions on micro electronic products and the US 1989 complaint on the Brazilian quantitative import control regulations)[26].

But by very far the most significant issue of Brazilian bilateral interest to be discussed in GATT in the 1980s was related to retaliatory action taken by the US in 1988 by imposing tariffs of 100% on selected Brazilian paper, pharmaceutical and electronic products entering the US market as result of a complaint on the inadequate protection provided by Brazil's intellectual property legislation on pharmaceutical products. Brazil asked for the establishment of a panel to consider the questions of principle involved in the American action. The US footdragged but the nel was eventually established early in 1990. There was no agreement on its terms of reference as the US insisted that the substantive Brazilian legislation should be examined while Brazil centered its case on the conflict between the American action and GATT rights and obligations. Terms of reference limited the panel to examination of compatibility of action with GATT. The US faced much criticism of their action in the GATT as its action was not preceded by any effort to settle the dispute using GATT machinery. The dispute was solved bilaterally as US retaliatory tariffs were withdrawn following Brazilian assurances on changes in the relevant intellectual

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26 See GATT, GATT Activities, several issues.

property legislation. These changes were still being discussed in the Brazilian Congress in the end of 1991.

More recently the old Brazil-US dispute on CVDs on non-rubber footwear Brazilian exports has flared up as Brazil has blocked, with support of other contracting parties, the adoption of the panel's report in favour of the US.

3. Trade and Debt Vulnerability

Balance of payments provisions have traditionally played a major role in GATT from the point of view of many developing countries and certainly also in the case of Brazil: article XVIIIb provided a sound legal basis for effectively closing the domestic market to imports. Barriers which would be better explained by infant industry or national security were presented as necessary because of balance of payments difficulties since it was traditionally easier to successfully invoke Article XVIIIb than other GATT articles.

Indebted countries had originally hoped that their need to generate trade surpluses could be taken into consideration by creditor countries in trade negotiations by improving the access for their exports in developed markets. But in spite of the pious words of the Leutwiler Report back in 1985 that "the health and even maintenance of the trading system ... are linked to a satisfactory resolution of the debt problem" there is no sign that the trade-debt link had or is going to have any concrete implications in multilateral trade negotiations. In fact not only commercial banks abstained from any lobbying to improve market access of debtor countries' exports to their respective markets but turned initial ideas about the trade-debt link upside down by supplying political backing for the US insistence in obtaining right of establishment for services industries in developing countries. Deterioration of the balance of payments entailed, moreover, increased vulnerability in relation to conditionalities imposed by international financial agencies as foreign exchange starved debtors have been pressed by agencies such as the IMF and the World Bank to adopt unilateral trade liberalization as part of a deregulation/liberalization package[27].

An important trade-debt complication is the contradiction between GATT's traditional reciprocal basis of negotiation and unilateral liberalization as a result of conditionalities imposed on borrowers of funds of multilateral financial agencies. To the extent that there is no equivalent pressure on other GATT contracting parties to reform unilaterally their trade policies a perverse asymmetry is created penalizing developing countries and in particular indebted countries[28]. As these tariff reductions are unlikely to be taken into account as concessions in the future as they are not bound and financial vulnerability will assure in any case that they are permanent, even if not bound in the GATT, it would make all the sense to bind them and try to extract counterconcessions as soon as possible[29].

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27 It is interesting to note that historically the trade debt link tended to be made explicit by the use of trade bargaining power, defined on the basis of the size of the trade balance, to establish a preferential position for debt repayment of certain loans. See Abreu (1984) where the use of such links by the British in Argentina in the 1930s is compared to the US self discipline in Brazil imposed by its strategic aim of reinforcing the multilateral trade system after 1934.

28 Supposing that at least in relation to certain issues certain developing countries or coalitions of developing countries are not "small" from a technical viewpoint.

29 Whether developing countries will have the bargaining power to make sure that these tariff reductions are taken into account by developed countries is open to question.

Trade policy conditionalities were included rather loosely in the letters of intent to the IMF signed by Brazilian authorities during the 1980s. Initially vague commitments in early 1983 to reduce quantitative restrictions "after the economy adjusts" were followed by commitments in 1983-88 to substitute tariff for import licenses, to reduce controls of imports of agricultural commodities, to reduce tariff levels and to reduce certain types of quantitative restrictions[30]. Similarly the Brazilian government was reluctant to agree with World Bank proposals to eliminate NTBs - in particular licensing or prohibition of imports -, reduce tariffs, eliminate export incentives and devaluate the exchange rate to the extent proposed[31]. From the mid-1980s modest trade reform took place involving a reduction in the more lavish export promotion schemes and some import liberalization, through a reduction of tariffs and of the number of items subject to licensing and prohibition. This was partly a result of some trade conditionalities which were included in agricultural sector and "export development" World Bank loans and of IMF conditionalities. But negotiations on a trade reform loan remained deadlocked.

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30 For the successive Brazilian letters of intent and memoranda of understanding see Brazil Economic Program: Internal and External Adjustment, several issues.

31 See World Bank (1989).

Differing views on liberalization policies tend to concentrate on timing and the sectoral distribution of the consequences of liberalizing efforts rather than on their inherent validity. The sequencing of policies acquires crucial importance in the context of stabilization programmes designed to control high inflation. The crucial question to answer is whether the simultaneous adoption of trade reform, foreign exchange devaluation and tighter fiscal and monetary policies is to be preferred to a sequencing of reforms which would improve their chances of success.

Those in favour of the shock approach as opposed to a more gradual approach[32] emphasize the credibility argument as with immediate commitment to reform economic agents are less likely to believe that the reforms are not to be sustained. Political costs of implementing reform over a longer term are also thought to be higher as economic agents tend to use breathing space to preserve their privileged positions. The gradual approach suggests, more convincingly, a stabilization strategy in which fiscal adjustment policies should precede other policies such as foreign exchange devaluation and trade liberalization and underlines the need of new foreign finance as the exchange rate is targeted on inflation and not on external balance[33]. Based on the experience of Latin

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[32] See, for instance, Rodrick (1990) and World Bank (1989).

[33] See Sachs (1987).

American countries it would seem that those proposing a shock approach tend to underestimate the difficulties of formulation of a comprehensive reform package with the adequate timing and, more importantly, that while there could be in principle some merit in a shock strategy this is less likely to be the case when previous shocks have already affected expectations of economic agents.

There is no crude trade-off between increased imports prompted by liberalization and the level of payments entailed by debt settlements since exports would also increase. It is clear, however, that trade liberalization without a corresponding liberalization by developed countries requires bigger devaluations than would be required by a concerted move to reduce protection in developing and developed countries since exports are to some extent constrained by barriers in developed countries. This further strengthens the argument for multilateral rather than unilateral liberalization. Alternatively, the reduction in trade surpluses can be compensated by large transitory financial facilities to support liberalization reform.

4. Towards Trade Liberalization

Brazilian economic diplomacy in multilateral trade fora has traditionally been a direct responsibility of the Ministry of Foreign Affairs. Policy formulation has been basically the responsibility of the Ministry of Finance which to a large extent acted as an interface with the private sector. Brazilian interests until the 1980s have been classically concentrated in access for commodity exports and keeping the domestic market for manufactures protected from foreign competition. These interests were in common with the bulk of other developing countries and are important to explain the developing country coalition of the 1960s in UNCTAD, especially in relation to the adoption of a Generalized System of Preferences for their exports. Export diversification and fast growth since the early 1960s made Brazilian concrete interests in the global trading system more complex and questions such as market access for exports of manufactures and, to a lesser extent, some of the new themes, especially services and intellectual property, became part of the relevant agenda in the 1980s. As import substitution remained a pillar of trade policy, Brazil played as if the interests of developing countries had not significantly diversified in the 1970s and, particularly, in the 1980s. Negotiating stances in the GATT until the late 1980s tended to stress the desirability of dealing with the "backlog" of themes, in relation to which "developing countries" had special interests, and to be defensive or even obstructive in relation to initiatives which would have resulted in opening up the domestic market to foreign competition.

Domestic lobbies with interests targeted in trade policy included until the mid-1960s commodity exporters, mainly interested in exchange rate policy, as well as domestic producers of manufactured goods (both domestic and foreign firms) interested in a high level of protection affecting competitive imports and access to cheap imported inputs and capital goods. As the export structure diversified, the domestic industrial sector became increasingly concerned with export promotion through access to fiscal and credit incentives. Concern with foreign exchange policies ceased to be restricted to commodity producers as the export lobby diversified. Commodity producers as well as producers of temperate agricultural products tried to maximize their extraction of subsidized credit from the government and in the latter case also lobbied for import substitution. There was full appropriation by the private sector of rents related to export quotas due both to domestically defined export restrictions and to the imposition of restraints by importers, notably the case of textiles and clothing exports restricted by quotas negotiated under the Multifibre Arrangement and of steel exports regulated by VERs.

Brazilian foreign economic policy in the 1980s, with its combination of export promotion and import substitution, can be better understood in a context which made possible to think that a relatively large (in a technical sense), politically relevant and rapidly growing developing country could effectively exchange trade concessions with the major developed blocks. It could not be anticipated that at least some of the underlying assumptions supporting this strategy would prove to be wrong. The Brazilian policy stance cannot be analysed in the same perspective as, say, the case of Chile, a small economy with a comparatively rather unsatisfactory growth record after insisting on an import substitution strategy which could not be sustained by the size of the domestic market[34]. A long history of success of import substitution was also a powerful factor to explain the reluctance to adopt liberalizing packages in the 1980s as opposed, for instance, to the stand of Chile and Mexico. It does not seem a particularly interesting angle of analysis to stress, with the help of hindsight, the shortcomings of Brazilian policy in postponing the opening up of the Brazilian market and consequently not reaping the advantages of liberalization.

Important changes of policy occurred in Brazil since March 1990 as a new presidential term of office started with the introduction of a new stabilization plan. An initially reluctant withdrawal of import prohibitions was followed by tariff reduction for a wide range of products, in particular textiles and agricultural inputs and capital goods, as the possible role of increased imports in dampening domestic price increases became a tenet of decision-makers having stabilization as the primary target. There was also the hope that trade policy changes would help in convincing the US Government to support Brazil in its debt negotiations. Strictly industrial or trade policy considerations receded to a secondary position among the arguments favouring trade liberalization. World Bank conditionalities had no major

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34 Chile's GDP was equivalent in 1990 to 7% of the Brazilian GDP. It is of course true that the Brazilian economy is more closed than the Chilean but, on the other hand, the rising importance of investment-related as opposed to purely trade issues, tends to weaken this classic qualification.

direct influence on these decisions. These moves were among a massive effort - not necessarily coherent or comprehensive - to deregulate the economy and reduce the role of the State as a producer of goods and services. A significant additional import liberalization programme which will reduce the modal and average tariffs to 20% and 14.2% respectively in 1994 (as compared to 40% and 32.2% in 1990) was introduced early in 1991[35].

The Brazilian stabilization programme does not fit either the shock or the gradual reform paradigms. The major difficulties faced on trade policy involved the overvaluation of the exchange rate and its impact on the trade balance. Hopes that imports would contribute to lower domestic prices were rapidly disappointed as the introduction of automatic import licensing, by initially restricting the access of economic agents to a list of approved firms, only transferred rents from import-substitution to import trade activities. This has been recently changed to allow access by final importers but commercialization margins show downward rigidity. Import volumes have not increased significantly due to severe recession.

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35 It is, however, important to stress that nontariff barriers such as minimum national content requirements to qualify to long term credit remained significant, see Fritsch and Franco (1991). These NTBs are likely to be of special relevance to block imports of electronic products.

There was initially, as mentioned above, a visible improvement in the rather tense bilateral relations with the US in line with the adoption of trade policies which had long been promoted either directly by the US authorities or indirectly through the efforts of the IMF and the World Bank.

An extremely powerful new Ministry of the Economy concentrated in principle much of the decision-making in the trade area. A Department of Foreign Trade was made responsible for tariff reform - theoretically in coordination with industrial policy - and for implementation of trade policy. Actual decision-making seems to be rather fragmentary and lines of command are hazy. While on paper there was further weakening of the influence of Ministry of Foreign Affairs, the secondary position of trade matters in the priorities of decision-makers in the economic departments, contributed to maintain the influence of Foreign Affairs on trade matters. More recently diplomats have increased the scope of their influence by occupying key positions in the economic decision-making agencies.

It is not surprising that Brazil should seek to improve its position in the debt negotiations even if at the expense of some traditional objectives of trade policy as debt service is substantial in relation to prospective trade liberalization "gains"[36]. While towards the end of 1991 there has been a clear

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36 Potential gains generated by trade liberalization would be of

change of attitude by US authorities, as well by the IMF, on cooperation with Brazil, there is still, however, a feeling that good behaviour has been until now unrewarded. Brazilian changes in trade policy may have countered US retaliation menaces in the bilateral context but these are meagre rewards.

The most recent and significant US minilateral initiative, even if sustained, is unlikely to provide substantial relief for a country such as Brazil at least in a mid-term perspective. In June 1990 President Bush launched the Enterprise for the Americas which contained proposals on trade, foreign investment and foreign debt. Potentially the trade proposals seem to be more significant than those on investment and debt. The US$ 500 million mentioned as a contribution over 5 years to IBD to foster investment is unlikely to make much impact if there is no change in macroeconomic conditions in Brazil. The reduction in debt service is unlikely to provide much relief in the case of Brazil: the Overseas Development Council suggested US$ 286.9 million of debt service over 1991-1994 as the likely relief. It is difficult to see Japan, and especially the EC, enthusiastically cooperating in the provision of additional funds to a project which is clearly a

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the order of US$ 4 billion yearly of additional Brazilian exports (see Laird and Nogués (1989), p.255). If account is taken of the fact that the present value of the Brazilian commercial foreign debt is much lower than the nominal value outstanding, interest payments if accordingly adjusted are likely to be at least of the same order of magnitude of liberalization export "gains".

counterbalance to their initiatives in the respective areas of main economic influence.

In the commercial field the proposal considers the creation in the long term of a Free Trade Area particularly with those countries which have associated to liberalize their trade. As a transitory step the US would negotiate framework agreements with countries which felt unable to consider joining the FTA. A Free Trade Area is more interesting for Mexico, which has the bulk of its trade with the US, or for Chile, whose tariffs are already low. For Brazil, due to its higher tariff and the importance of non-US trade, joining an FTA would have costs similar to a non-discriminatory unilateral liberalization since the US is a potential supplier of the bulk of Brazilian imports and export benefits are restricted to the US market. A major obstacle to success is that the US is unlikely to include in its offers a significant reduction of NTBs in those sensitive sectors in which Brazilian interest is concentrated. There would be in principle certain advantages for Brazil in negotiating a framework agreement with the US jointly with other Latin American countries but to do this the present plans for a FTA in the Southern Cone must be transformed into plans for a customs union[37]. There are, however, important difficulties in relation to the latter, as illustrated by Mercosul, in particular the conflict of interests on the

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37 See Fritsch (1990).

desired level of the common tariff between Brazil and the more open and smaller economies. Brazil's basic main trade interests seem very much to lay with multilateral liberalization rather than with any trade bloc formation.

Trade liberalization in Brazil has partly subverted the equilibrium previously reached in the size and distribution of trade-related rents. Other likely developments such as a foreign debt settlement, additional sales of public assets and further trade liberalization including services should also contribute to give shape to a new distributive equilibrium. Until now the widespread expectations of gains have made possible reforms to advance even if somewhat slowly and with a far from comprehensive scope. But as the liberalization process advances political obstacles are likely to become harder to surmount as losers face increasing (real and perceived) difficulties to adjust to new conditions.

Debt negotiations remain crucial as together with a deep fiscal adjustment they could provide a significant basis for the beginning of a lasting stabilization in Brazil in a context marked by the continuously advancing trade liberalization and other structural reforms. The obstacles in the path of such an adjustment look formidable as political constraints on the Collor government tend to become increasingly effective .

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