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Determinants of Sustainability of Trade Liberalization: Export Diversification

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Section I: Introduction

Economists tend to agree that the formation of free trade agreements is beneficial to all, citing that each individual country is better off if it specializes in production and trade of goods in which it has a comparative advantage relative to other nations.[i] Despite this general consensus, the ideal way for a country to overcome political obstacles and achieve integration into the international economy is still debated. Additionally, the reason why some countries sustain their momentum for liberalization while others falter remains a pertinent topic of scholarly research. These issues have become especially important in light of recent setbacks in the international trade arena, such as the collapse of the WTO talks and the loss of momentum towards liberalization in several Latin American and East Asian countries.

Since the end of the World War II, countries have been increasingly pressured to lower their trade barriers as the world becomes more integrated. Many countries have followed the lead of the United States and other industrialized countries by participating in successive 'rounds' of trade liberalization organized under the auspices of the General Agreement on Tariffs and Trade (GATT) and its successor the World Trade Organization (WTO).[1] Other countries, however, have questioned if the terms offered by these organizations are in their best domestic interests or provide a disproportionate and unfair share of the benefits to wealthier nations. Each WTO meeting has become increasing complex with a multitude of country-specific agendas; the scope of these inequities was illustrated in 1999, when the Seattle Round ended without the formation of a new agreement. Again, in September 2003, talks in Cancun collapsed as over 20 developing countries walked from the negotiating table.

While these two WTO rounds ended without new agreements, in the overall trade frontier during the late 1980s and early 1990s there has been a growing abundance of newly formed overlapping regional trade agreements (RTAs) worldwide. These agreements have ranged from highly integrated customs unions such as the European Union to more modest free-trade

initiatives throughout the world. According to the WTO, 181 regional trade agreements existed worldwide as of year-end 2002, substantially more than the 43 RTAs that existed in 1992. Chart 1 illustrates the rapid increase of these regional trade agreements since 1948. In December 2003 the United States concluded talks with four Central American countries -- El Salvador, Guatemala, Honduras and Nicaragua – signing a Central American Free Trade Agreement (CAFTA). The agreement must still be ratified by each country (and is not included in Chart 1), but is exemplary of the types of RTAs that are being formed throughout the world. Other agreements gracing the headlines of world newspapers throughout recent months include the Free Trade Agreement of Americas (FTAA), South Asian Free Trade Area (SAFTA), and the Common Market for Eastern and South African (Comesa) Free Trade Area (FTA).

If economists are correct in stating that trade is beneficial to all countries, then it is imperative to understand why certain countries have refused to partake in liberalization efforts or ratify RTAs throughout the world. If a country expands regionally rather than unilaterally or multilaterally, will it be more likely to continue opening to both trade and foreign direct investment? Will it become more or less integrated into the world's trading system? Is there a causal link between the method of expansion and the integration of its regional and multilateral trade? Is choice of trade partner relevant to the durability of the agreement; will a country continue to expand its trade throughout recessions, will the policy withstand the stand the test of time, and a even political transition depending upon its initial liberalization scheme?

My research attempts to answer some of these questions and contributes to the burgeoning literature on the political economy of trade liberalization. I argue that regional versus multilateral trade liberalization is actually extraneous when looking at commercial openness, and instead export diversification is the topic that necessitates further exploration. It differs from previous literature because it links export diversification with the sustainability of trade liberalization. Each topic has been explored in depth individually, yet they have not been linked

[1] Goals of the WTO include the promotion of international trade through the reduction of tariffs.

together. In my argument, diversification is defined with respect to the heterogeneity of products that a country exports. While export diversification is not the panacea for sustainable commercial openness, I have compiled case studies and empirical data to support the argument that it does contribute substantially to the durability of trade liberalization. There are two main theoretical frameworks that support my argument that greater diversity in exports generates more sustained openness. The first framework stems from the effect of fragmentation on the determinants of policy, and hypothesizes that a more diverse set of exports leads to greater support among important constituents, which in turn pressures policy-makers to maintain liberalization. I will refer to this as the "policy approach" throughout the paper. The second model is an extension of modern portfolio theory, adding to it the idea that constituents will desire less volatility and more stability in exports and overall earnings, which is achieved by having diverse exports and continual opening. This will be referenced as the "portfolio approach."

The breakdown of the paper is as follows: Section II discusses pertinent research in regards to regionalism versus multilateralism, and concludes that it is an immaterial factor in sustainability of liberal trade policy. Section III highlights current literature to support my theoretical idea that diversity of exports will lead to policy-makers' sustaining liberalization. Section IV explains the traditional idea of 'portfolio theory' as applied to trade and extrapolates from it that a more diverse export base will generate greater sustainability of commercial openness. Section V presents in depth case studies of four Latin American countries' trade history. Section VI analyzes these studies in order to solidify the arguments outlined in Sections II, III, and IV. Section VII discusses the empirical study conducted with the research and its results. Section VIII addresses the limitations of this argument while Section IX contains concluding remarks and future research possibilities.

Section II: Regionalism vs Multilateralism

The changing face of trade agreements throughout the world has also been at the forefront of recent scholarly discussion. Researchers have asked new questions such as "Do WTO Members have a more liberal trade policy?" Exploration of several measures of trade liberalization has shown that membership in the WTO has had a statistically insignificant impact on a country's trade openness. (Rose, 2004a) A pertinent and much-debated topic has been whether the WTO or multilateral trade has been hindered or assisted by the new proliferation of RTAs. Some scholars argue that the pursuit of regionalism has acted like a stepping stone in multilateral negotiations, ironing out a plethora of difficult issues among smaller contingencies. (Salazar-Xirinachs, 2002) It has been argued that RTAs are building blocks of multilateral trade that strengthen exports and favorable trade policies. (Lawrence, 1999) Benefits from RTAs include the creation of trade that is consistent with further global liberalization and the expansion of individual nations' market-size and stability. (Robinson and Thierfelder, 2002)

However the opposition claims that "stepping stone" evidence is inconclusive, problems are caused by the RTA overlaps and regional agreements are "stumbling blocks" weakening the multilateral trade. (Sampson and Woolcock, 2003) (Crawford and Laird, 2001) (Winters 1996, 1998) (Bhagwati, 1993). Times-series evidence has also been presented suggesting that broad liberalization is a more favorable policy in both the long and short run; economies grow faster and have higher investment shares with this strategy than through RTA formation. (Vamvakidis 1999) Finally, proponents of multilateral trade say that the establishment of RTAs creates more powerful coalitions that make changing international trade policy toward multilateralism at WTO rounds more difficult. (Krueger 1995) Still others stress that regionalism has been a consequence arising from the success of the multilateral trading system and scholars have causation backwards. (Either, 1998) (Freund, 2000)

The recent problems at WTO meetings and the wave of regional integration throughout the world have placed increased importance on this question. In this paper, I explore the effect

diversity in trading partners has on the sustainability of a country's commercial openness as well. The argument follows: a nation with large percent of exports going to only one country becomes heavily tied to that importing country's economy. If the importing country falls into a recession or has a crisis of some sort, contagion is much more likely to occur, with the home country experiencing a recession as well. For example, Mexico relies heavily on the US to buy its exports. The recent US recession as well as increased imports from China, has hurt Mexico's currency, exports, and overall earnings. A country that liberalized regionally may have similar problems; financial crisis may spread throughout the region, political instability may be more likely to occur in its neighborhood, or historic rivalries may influence its policies. Diversifying in partners not only permits less dependency on the economic environment of any one country but also allows more political, financial and social independence for the home country. A country with a large number of partners will be more likely to sustain a liberal trade policy due to mitigation of adverse economic shocks caused by the external sector.

Despite this framework, the case studies in this paper do not provide conclusive results of these ideas, suggesting instead that sustainability of liberalization is a consequence of a combination of other factors. Empirical evidence was insignificant as well; backing the case studies in saying that trade concentration in partners is immaterial for sustainability of commercial openness. Mexico, with high trade concentration in regional agreements, has maintained an open policy similarly to Chile, a country with a diverse set of trade partners. Mexico's trade benefited initially from partnering with the United States under NAFTA. As former President Carlos Salinas illustrates, "NAFTA took effect in 1994, when the North American economy began the longest economic expansion of its [recent] history. It arrived just in time [for Mexico] to be a part of that expansion." However, recently it has felt the pressures of China and has lost ground in the trade arena. Both Chile and Mexico, however, have focused on export-led growth and diversification, which was found empirically significant. Another example of the regional versus multilateral argument is found in Bolivia and Venezuela. Bolivia opened

relatively unilaterally while Venezuela opened to trade relatively regionally. Both have seen recent problems on the liberalization front, combined with pressures to re-close their borders. This suggests that something other than method by which a country liberalized or whom a country trades with is relevant in trade liberalization discussion. I suggest that the "missing link" is an export diversification strategy.

Section III: Policy Approach

While some authors have questioned whether trade liberalization is a necessary component of successful outward oriented strategies (Sachs 1987), most accept that trade liberalization is beneficial. With that assumption in mind, scholars have set out to provide a set of clear policies and attributes that allow sustainability of commercial openness in individual countries. On the political front, some scholars have explored the influence of state regime type on economic reform and trade liberalization. Henisz and Mansfield have illustrated that deteriorating macroeconomic conditions impede commercial openness but are more influential on trade policy in democracies than in non-democratic countries. They assert that as fragmentation increases, it becomes more difficult to change an existing liberal trade regime due to an increase of "veto points" that reduce societal pressures on political actors. (Henisz and Mansfield 2003) This argument expands upon previous literature explaining that policy makers respond to voters' demands due to pressure of re-election. Assuming trade is an issue that voters care about, politically powerful coalitions can then influence politics and thereby have the potential to influence commercial openness and policy. (Thornberg and Edwards, 2001) The more voters that support liberalization, the harder it will be to close a country's borders once it has liberalized.

From this foundation I assert that as the variety of exports increases in a nation the support for further trade liberalization will subsequently grow as well. In a country with one export, the pressure on the government to liberalize will be concentrated in one actor. If not well connected politically, the exporter will not have much influence and policy will be formed

irrespective of that exporter's views. With strong political ties, several possibilities may occur. In order to minimize competition and maximize its marketplace, the exporter may push for subsidies, higher tariffs, and industry specific export-oriented policies. This will protect the exporter, but not encourage trade liberalization or send positive signals to the international community. In a second situation, a case where a country has a relatively liberal policy already, a negative shock to the economy leaves the single exporter with greater difficulty in trying to sustain this policy of overall openness. Large support for protectionism will be generated by the negative shock, and policy makers fearing loss of re-election will pass retrenchment measurements that adhere to these powerful constituents' demands.

As the country expands its exports by diversifying across industries, more groups will have an interest in an overall open trade regime. They will form their own powerful collation to pressure policy makers to act in their favor, by either liberalizing trade or maintaining a liberal trade regime. Each exporting business' desire of larger international marketplace and lower tariffs abroad will lead to pressuring policymakers into signing of trade agreements with foreign countries. As these agreements call for reciprocal measures, the domestic country will be forced to lower tariff and non-tariff barriers as well. Economically as more competition floods the marketplace, prices will fall and consumer demand will increase, passing the benefits of trade to another group of constituents. Policy makers will also become more susceptible to international pressures of liberalization as more products are imported to and exported out of the country. As the number of influential actors in favor of liberal trade continues to increase, it will become more difficult for the country to revert back to a protectionist policy. The consumer, exporter, and international "veto points" should be able to combat retrenchment pressures from liberalization opponents.

Section IV: Portfolio Theory Approach

The development of modern portfolio theory in the field of finance by Harry Markowitz has stimulated much parallel literature devoted to applying the idea of diversification to the realm of trade. Brainard and Cooper first applied Markowitz's portfolio theory to trade, with the basic argument that an optimal export portfolio is achieved by exporting a set of products that together minimize the risk of export earnings instability, while achieving the maximum level of export earning returns.[ii] The goods selected in each portfolio are measured in terms of return and variation in return, or risk, and then the overall portfolio is assessed. An optimal portfolio is results the highest return and lowest risk, and can be used to maximize and stabilize export earnings. (Brainard and Cooper, 1968) Research has primarily focused on diversification away from primary commodities and many scholars have concluded that a portfolio optimization strategy is a valuable tool to mitigate risk and increase return. (Dawe 1996) "Export diversification offers a means by which countries can combat earnings uncertainty, when these earnings derive from a few primary commodities and, at the same time, can increase their revenues from investment in the production of products with market growth potential." (Laby and Lord, 1990) However, diversification does not always mitigate fluctuations in export earning, and a country sacrifices some of the benefits of specialization in exchange for increased stability in export earnings. (Love, 1979a) Price-based portfolios are incomplete and often inaccurate in scope because export quantities vary by more than simply prices. Additionally, export assets are not as liquid as financial assets discussed in Markowitz's original theory. While diversification may not be a cure-all for less volatility, a portfolio approach can assist in designing appropriate export policies that enhance a country's earnings. (Alwang and Siegel, 1991)

Studies have been also been conducted demonstrating that export concentration hampers economic growth. (Lederman and Maloney, 2003) According to Maizels, "unstable export earnings make it difficult for a country to plan capital imports, destabilize consumption, and can adversely affect export earnings trends." (Maizels, 1987) Trade thereby affects overall economic

growth, and when the balance is volatile there becomes a necessity to act in order to avoid financial crisis. This is of utmost priority for home-country constituents; therefore they are willing to give up a volatile high-growth and high concentration approach to trade for more diverse export strategy that leads to lower growth and less volatility. Additionally, by diversifying into other goods, the country's economy becomes less susceptible to a drop in international prices for individual commodities and more stable overall. Conversely, in a concentrated export environment, the dependence on one good to generate export earnings can lead to great economic instability, especially in LDCs with high percentages of GDP dependent upon trade. If adverse events occur in a country with volatile earnings, protectionism will be sought after and the liberalization cycle reversed. Foreign investment and trade will fall, resulting in deteriorating economic, financial and social conditions all in turn further impeding commercial openness. Therefore, if WTO policies suggest excessive concentration because textiles and agriculture are not opened to LDCs, then these countries will opt-out in order to achieve greater stability.

Section V: Case Studies

Support for the policy and portfolio theories previously outlined theories comes by examining four Latin American countries. While data suggests that export diversification helps sustain trade liberalization worldwide, this region has many historical, cultural, economic, social and political characteristics in common[iii] thereby making it easier to assess the consequences of the trade liberalization durability depending upon exportation strategies. Through looking at several statistical sources as well as historical reports on each country's trade policy, four countries were selected: Chile, Mexico, Venezuela and Bolivia. In all four cases there were distinct periods where policy focused on export diversification as part of a liberalization strategy, but each country has had varied success in the sustainability of these open policies. Chile and Mexico are two examples of countries that have been able to maintain a liberalization policy to date. On the other hand, recent setbacks or backlashes in the international trade arena have

followed Bolivia and Venezuela's commercial openings. In the case of Venezuela, the country did not diversify exports into an optimal portfolio and are still overly dependent on petroleum revenues. A high-level of state-involvement in the private sector has additionally prohibited the formation of strong coalitions to combat retrenchment. Failure to implement the "portfolio" and "policy" approaches has led the country to continue experiencing rocky export earnings and overall growth patterns, as well as intense pressure for closing borders to trade. Bolivia is a case where exports are no longer concentrated, but the support of political actors was not effectively garnered. This case highlights that an export oriented growth policy has limitations, unless the country has strong institutions, the support of the public, and an element of luck, then it may not be successful in maintaining liberalization. The recent retrenchment issues in Bolivia and Venezuela also illustrate that export diversification must provide a broad base of support and increase productivity in order for the country to sustain commercial openness.

Building from several books, research papers, and WTO reports, an in-depth case study of each country has been formed, illustrating their liberalization policies and the events that have since transpired. Articles from local newspapers and magazines assisted in providing first-hand accounts of the occurrences during the liberalization and concluding whether it may have influenced the continued success or closing of the country's trade.

Chile depicts a country that liberalized unilaterally/multilaterally, by decreasing tariffs to all trading partners in a nondiscriminatory fashion. The country was the Latin American pioneer of trade liberalization during the mid-1970s and has maintained a relatively open trade policy ever since, with a brief period of increased tariffs during the 1980s. In part due to the country's unilateral opening, they have had an overall durable trade policy that has survived recessions, financial crisis, and political transitions.

Throughout the 1940s and 1950s Chile had a protectionist trade policy with the government interfering in the marketplace through high tariffs, subsidized credits and price controls. During the late 60s the government slowly started to adopt a more export-friendly

strategy; however import-substitution was still a cornerstone of external policy. Certain tariffs were over 700%; there were 187 import prohibitions and a plethora of other quantitative restrictions.[iv] The Minister of Labor and Social Security from 1978 to 1980, Jose Pinera, summed up the situation saying that prior to the 1970s it was "as easy for an industry to obtain tariff protection as to mail a letter." Local businessmen asserted that it would take another generation to make their industries competitive in the world market.[v] Protective measures combined with a deceptive multiple exchange rate system consisting of fifteen different rates further obstructed the external sector. During Allende's *Unidad Popular* from 1970-1973, in order to avoid a collapse in the external sector and a balance of payments crisis, the government continued to impose layers of regulations upon previous layers. The long tradition of trade restrictions generated large inefficiencies in the manufacturing sector as well as the stagnation of non-copper exports.

In the aftermath of overthrowing Salvador Allende, the newly appointed Minister of Finance Admiral Lorenzo Gotuzzo, stated that Chile's best growth prospects were gradually opening to international trade. His views were generally in line with those of the "Chicago Boys," a group of Chilean economists educated in the United States that advised the government in the structuring of a neoclassical market-economy model. Tariffs at this time averaged 94%; the Minister of Finance reduced the maximum tariff to 220% and lower duties that were between 50-220% by 10%. The majority of these reductions implemented had little effect on relative prices and foreign competition, as they merely involved redundant levels of protection that still remained at "prohibitive" levels.[vi]

From 1974 to 1976, the country focused on trade liberalization through both sides, centering policy on expanding the export sector with the continual decreasing of tariff rates. Sergio de Castro, replacing the previous Minister of Finance, announced that by early 1978 the nominal rates would be between 10-35%. He argued that this schedule was "perfectly adequate for the Chilean economy since it provide[d] reasonable levels of protection for the nation's industrial activity." In 1976, prohibitions numbered only at 6, and import deposits were phased

out. By mid-year, the average tariff had fallen to 34%, with the maximum tariff not exceeding 60%. In respect to exports, policy was aimed toward raising the percentage of exports in GDP (13% 1971-1973 to 30% in 1976) which had been growing slowly. The increase in exportation volume focused on nontraditional exports, whose value quadrupled in the three years.[vii] Pinochet himself acknowledged the focus on exportation through maintaining a high real exchange rate, "We shall continue to encourage nontraditional exports… the Minister of Finance will announce the manner in which the exchange rate shall be established in order to guarantee a viable and permanent value for foreign currency." The real exchange rate rose sharply between 1973 and 1976, not only helping spur exports but also mitigating the loss of competitiveness for domestic output. From 1976 to 1981, the key instrument became the exchange rate. After a brief appreciation in March 1977, the government scheduled monthly deflations with the objective of lowering inflation.

Chile had previously entered into the Andean Pact during 1969 with Bolivia, Colombia, Ecuador and Peru. In 1976, however, the country withdrew from the Pact due to opposition of Decision 24[2] and the desire to pursue aggressive economic policies that clashed with the generally protectionist, state-led industrial development philosophy of the Andean Pact scheme.[viii] Minister de Castro alluded that the tariff policies of the Pact constituted a threat to Chile's sovereign right to establish its own exchange rate policy." [ix] A year later, the Minister announced its final goal of a uniform 10% tariff rate by mid-1979. In two speeches he stated:

> "We have decided to eliminate the distortions generated by the discriminatory tariff structure and to establish a uniform tariff; this way all activities producing

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[2] Decision 24 forbid foreign investments in activities presently being carried out by firms from the Andean countries and prohibited foreigners from buying stock in Andean firms. Twenty percent was set as the maximum amount of yearly profits a foreign corporation could repatriate abroad and required future foreign companies to sell at least 51 percent of its shares to Andean Pact nationals to be considered a "mixed company" thereby allowed to utilize the Pact's intraregional free trade scheme. Decision 24 also prohibited member states from granting licensing contracts to foreign companies that contained restrictive noncompetition clauses.

for the domestic market will be on an equal footing regarding foreign competition.

The lower the tariffs, the higher the exchange rate should be… compensation for the tariff reduction corresponding to the current month, we have decided to devalue by 4.3%… for the following months the exchange rate adjustment will correspond to inflation in the preceding months plus an additional amount to compensate for the tariff reduction."

In mid-1979 the tariff rate was successfully established at a uniform rate of 10%, with the sole exception of automobiles, and tariff differentiation of goods regardless of whether final, intermediate or capital was eliminated. From 1976-1981 the volume of imports increased 2.25 times and imports of consumer goods increased 4 times; however, eventually certain national industries began to lose competitiveness with the flood of newly import goods.

In the 1980s the country suffered through a debt crisis alongside most other Latin American countries. The transformation of the country from a highly closed market to an open economy had severe effects on firms and the economy as a whole. With a recession in the US, Chilean products lost their major market and with a tight money supply at home, several Chilean industries went bankrupt. In November 1981 four banks and four major finance corporations went under, obliging the government to move away from its emphasis on private enterprise.[x] A number of firms that had been subsidized through high import tariffs shut down, while others embarked on reorganization processes to increase their efficiency and productivity. In the first few years of the decade, there was a sharp fall in output as well as value and volume of exports. There was a collapse in the external markets and a sharp devaluation of the currency. As other economic activity deteriorated, firm's debt-to-equity ratios and financial soundness eroded and the economy collapsed.

Against the growing concern over the poor health of the Chilean economic model, all of Pinochet's ministers resigned permitting him the freedom to reshuffle his cabinet. Finance Minister de Castro was one of the strongest supporters of existing policy, insisting that the economy was experiencing an 'automatic adjustment' to the international recession. According to the newspapers, he was prepared to concede some 'compensatory action': the 'anti-dumping' clause to protect against unfair import competition, which had already been announced, plus some help for exporters.[xi] Minister de Castro's resignation was demanded and he was ousted from the finance ministry. The appearance of continuity in economic policy was maintained by the appointment of Sergio de la Cuadra, a Chicago graduate who shared de Castro's monetarist convictions, to the finance ministry. But the real challenge to policy makers at the time, according to local press, came from the appointments of General Luis Danus to the economy ministry and General Gaston Frez to the planning agency, both military nationalists who both were intensely critical of the free market model. One of these new ministers alluded to the strengthening of the economy ministry, while the finance ministry was to be reduced to a more 'technical' role.[xii]

The government eventually enacted a hike in the lowered tariffs; in 1982, import surcharges of 4-28% were implemented on more than 30 items. In 1983, import tariffs were temporarily increased to a uniform 20% and domestic products began to substitute imports once again. The value of exports continued to be limited by lack of capital, constraining the typical improvement in exports associated with a real depreciation of the currency. A year later, the tariffs were temporarily raised to a uniform 35% rate. Many considered the events that transpired during this period as signaling the end of "the experiment initiated by the Chicago economists." [xiii]

But in February 1985, Chile's Finance Minister, Hernan Buchi, announced legislation to help kick off a seven-year, export oriented growth drive. In 1987 the economy finally started showing signs of recovery since the drastic collapse in 1982 and 1983. Once Chile's only significant export, copper made up less than half the value of all exports with most growth coming from the exportation of fresh fruit and other farm and fisheries products. [xiv] Raimundo

Correa, the vice president of the association of Chilean fruit producers represents the thought of exporters: “Whenever people in other countries ask me for advice on how to do what we've done, I recommend three things. First, guarantee private property; second, guarantee free trade; and third, be sure the government does nothing else to interfere with private enterprise.”[xv]

Since the 1990s, the country has re-implemented its policy of low import tariffs. The return to the world’s capital markets helped to stabilize the currency and the country has returned to democracy. In 1991, President Aylwin and the Chilean congress lowered all tariffs on imports to 11% from an already low 15% with hopes to negotiate a free trade agreement with the U.S. under the fast-track process. An interview with a local investment banker suggested that Chilean businessmen were upset with the new ruling, “The problem is, the new tariff rate may still be too high.” The article concluded that Chile has defeated the protectionist business class that many of its peer countries have, and has “shown consumers the benefits of access to the global market. But… the development of a free market is a dynamic process that must be continually encouraged among every sector -- from wage earners to world-class industrialists. Otherwise, the tendency for vested interests to arrange for protections from competition can reappear.”[xvi] However, El Popular headlined biweekly articles with "The Chicago Boys are still in La Moneda (the presidential palace)," describing union dissatisfaction with Aylwin's economic policies.[xvii]

Since the country’s economic strategy is largely based on export-led growth, and it has enacted measures to aid exports including faster return of value-added tax overpayments, creation of in-bond warehouses, and market intelligence and support through ProChile, the government export-promotion agency linked to the Ministry of Foreign Affairs. The government has emphasized the formation of trade agreements as well. Throughout the decade, Chile formed trade agreements with other countries including Mexico (1991), Venezuela (1993), Colombia (1993), Ecuador (1994), Canada (1997), and Peru (1998). It also became an associate member of MercoSur (1996), signed a free-trade agreement with five Central American countries (2001) and is in the continual process of signing one with South Korea (2003). Additionally, in 2002, Chile

signed a comprehensive economic, political, technological, and cultural co-operation agreement with the EU that grants immediate tariff-free access for 85% of Chilean exports and signed a free-trade agreement with the United States. By year-end 2002, Chile had 37 bilateral investment treaties in operation, 14 awaiting ratification and 4 being negotiated. It is an active participant in the negotiations for the Free-Trade Area of the Americas (FTAA) and the Asia-Pacific Economic Co-operation (APEC) group. The country cut the general import-tariff rate from 7% to 6% at the beginning of 2003, which had been at 10% in 1999.[xviii]

Mexico is a country that experienced a relatively regional liberalization, signing the North American Free Trade Agreement (NAFTA) which served as a model for future Latin American free trade agreements. The country has become one of the most prolific signers of free-trade agreements in the world, superficially continuing to liberalize and decrease tariffs. While non-tariff and tariff boundaries have been eliminated within formal trade agreements, trade barriers have increased for all other countries highlighting an increasing disparity in the degree of Mexico's openness. The country illustrates a durable regional approach that has survived recessions, financial crisis and political transitions, yet has seen limitations on the overall expansion of its trade worldwide.

Comparable to most Latin American countries, from 1940-1985 Mexico essentially operated as a closed economy. In the 1940s the country operated under an import substitution industrialization policy, promoting new domestic industries and allowing unrestrained development of existing industries through a set of tariff and non-tariff barriers. Due to its large internal market import substitution was maintained throughout the decades, leading to a high cost structure and internal prices domestically in comparison to those of the rest of the world.[xix] From the 50s to the 70s the "Mexican Miracle" took place; the country grew at an average of over 6% per year while inflation remained relatively low. In the 1970s Mexico obtained unwarranted and excessive lending by foreign banks and investors, on par with many of its neighbors in Latin America. The country began appointing professional economists, most with graduate degrees

from foreign universities and ties to multilateral institutions and foreign banks, into high-level policy position during this time.

Under President Echeverrya (1970-1976), government spending increased enormously while problems with the import substitution method began to appear.[xx] The peso became overvalued and the country's industrialization process, which had a built-in need for increasing imports, could no longer be met by the export of primary products. Despite a large public deficit and high inflation the import substitution policy did not collapse primarily due to the discovery of oil that opened unprecedented international financing.[xxi] After the 1976 elections, President Jose Lopez Portillo invested ardently in Mexico's state-owned petroleum industry and increased government spending. During the last few years of the decade growth of oil exports and credits induced industrial sector expansion and increased consumption. In 1980 exports, of which petroleum accounted for more than 80%, were 11% of Mexico's GDP.[xxii] The economy began unraveling against a background of enormous debt, high inflation, a rise in interest rates and a decline of international oil prices.[xxiii] Investors withdrew capital as speculation about the devaluation of the peso increased. In 1982, when President Miguel de la Madrid took office, he inherited US$92.4 billion of debt, or 36% of Mexico's GDP. Later that year, the Finance Minister informed the world financial community that Mexico was unable to meet its debt payments.

The debt crisis was the spark for Mexico's change to free-market reform, and domestic businesses mobilized in support of the government's liberalization program. A new team of US-trained economists that believed in the efficiencies of liberalization was appointed responsible for Mexican economic policy. The President himself had been educated at Harvard and he appointed two Yale-trained economists to head the Finance Ministry and the Central Bank. Together they negotiated settlements with the IMF, the US Treasury and international banks. In return for the support of these external organizations, Mexico promised to implement structural adjustment measures proposed by the IMF: to practice fiscal and monetary austerity and to gradually open to trade and other market mechanisms. Economists whose views emerged during the de la Madrid

administration were promoted to top policy positions during subsequent administrations, thus ensuring the continuance of free-market policies.[xxiv]

The country experienced a relatively rapid unilateral shift to free trade agreements that began in 1985 and was completed by 1988. Trade liberalization, mostly through multi-national corporations, was a requirement to boost export-led growth as well as to reduce inflation by introducing import competition to control prices. In 1984, Mexico obtained the World Bank's first Trade Policy Loan which stipulated that the country liberalize trade policy in exchange for a series of loans. Development plans changed from import substitution to export promotion under the National Program of Industry and Trade.[xxv] The fiscal and monetary austerity program was expanded to become a full-fledged neoliberal program, complete with widespread privatization and the lifting of several tariff barriers. Debates over how fast and how far to decrease tariffs surrounded the trade liberalization. On one side were fiscally conservative developmentalists within the Ministry of Commerce; on the other were the "free traders" of the Central Bank. [xxvi] In 1985, import permits covered 92% of domestic products and foreign trade was approximately 26% of GDP. Over the next two years, import licensing was cut to a quarter of previous levels and the maximum import tariffs became more unified by falling 50%.[xxvii] The country sought a bilateral agreement with the US on subsidies and countervailing duties and announced its intentions to participate the following year in the GATT.[xxviii] In 1986, 1987, and 1988 exports continually expanded at 43%, 40%, and 17%, respectively, due to the recession, the devaluation of the peso, government control over wages and excess manufacturing capacity.[xxix] The financial system continued to liberalize, policy toward foreign investors was favorable modified and Mexican lands were opened to purchase by private investors.[xxx]

In 1987, Mexico introduced a trade liberalization program that went beyond GATT and World Bank requirements as a prelude to NAFTA. After a new devaluation of the peso, the country underwent a period of domestic growth and modernization driven by trade, but cuts in public expenditures due to the fiscal austerity imposed by the IMF led the middle class to show

signs of political discontent. A *Financial Times* correspondent cited, "Mexico went much further in reducing its trade barriers than the World Bank required… The two sides agree on almost everything… World Bank economists and Mexican officials often spend weekends together brainstorming on policy issues. Many are graduates of the same US universities, and friends."[xxxi] When Salinas was (fraudulently) elected in 1988, his administration enacted new social programs, economic restructuring, and political reforms to mitigate the continuing hardships that the neo-liberal economic agenda had inflicted. He continued to deregulate markets, privatize state-owned enterprises, and fight inflation. On the trade frontier, Salinas presided over a second wave of unilateral trade liberalization that deepened import quotas and permits, dismantled other non-tariff barriers to trade and further opened the country to foreign investment participation.

The decision to enter into a free-trade agreement with the United States and Canada came in 1989.[xxxii] The following year witnessed the first attempt of a free-trade agreement between the Salinas and Bush administrations. For Mexico, the main objective at this time was to expand trade and investment while improving the country's risk assessment and visibility. The negotiation process occurred in earnest from mid-1991 to November of 1992. Much was taken from the US-Canada trade deal of previous years, but NAFTA was more extensive with the ultimate goal the removal of restrictions on free trade of goods between its partners. In addition to a staggered 15-year maximum phase-out period for tariffs,[3] the agreement included mechanisms for dispute resolution and import-surge protection and two parallel agreements on the environment and labor rights. The United States immediately removed tariffs on 75% of Mexican products (many of which already had preferential treatment) in the first year, while only about 55% of Mexican tariffs on US and Canadian goods were immediately removed. By year-end 2003, 99% of NAFTA goods were scheduled to have no tariffs, while the remaining 1% were to remain until 2009. For Mexico, NAFTA marked the end to its import substitution strategy but severely restrained the capabilities of the government to pursue target-oriented policies.

During the NAFTA negotiations, Mexico was also in the midst of forming an Economic Cooperation Agreement with Chile. The agreement encompassed several aspects, including tariff scheduling and investment liberalization, and was implemented in 1993. After NAFTA was signed in 1992, Mexico enacted a Foreign Trade Law establishing the Foreign Trade Commission in preparation for NAFTA's implementation. During the Uruguay Round, however, it was established that Mexico's phasing out of tariff and non-trade barriers with non-NAFTA partners would be done at a slower speed than with NAFTA partners,[xxxiii] setting precedent for the country's continual separatist policy today. In 1993, domestic product covered by import permits had shrunk to 16.5% and foreign trade had rebounded to 38% of GDP by 1994 – post-NAFTA implementation. [xxxiv]

NAFTA has restricted the Mexican government's ability to apply domestic policies that promote social, health and educational programs due to fiscal austerity pressures, however. Large capital inflows and trade liberalization since the agreement contributed to the appreciation of the peso, causing a large increase in imports to Mexico and a record current account deficit. In December 1994, the government signaled its inability to support the value of the peso by allowing it to drop from 3.5 to over 4 pesos to the dollar. Investors once again removed capital from the market, starting a collapse that carried into 1995.[xxxv] Since the correction in the market, Mexico has continued to grow rapidly; from 1997-2000 Mexico's trade attained the fastest growth rate among the WTO's twenty largest single members. Through the directives of the WTO, the country has eliminated most export permits, substantially reduced export taxes and direct export subsidies, and eliminated fiscal incentives for exports. The government has reduced the list of imports requiring licenses, increasing competition that has lowered domestic prices. More than 300 products still require either import permits or license, with NAFTA countries and Chile exempt from 22 of them. By the year 2000, foreign trade was 65% of GDP[xxxvi] and trade has grown 135% and 145% with the US and Canada, respectively, between 1994 and 2001. But in the

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[3] Mexico's car industry obtained a significant extended protection under the tariff phase out.

wake of falling US demand and declining international oil prices, trade and GDP growth for Mexico slowed in 2001. The composition of exports have changed drastically since the 1970s; in 2002 manufactured goods account for 89.5% of revenues, petroluem products account for 9%, agricultural goods, 2.8% and mining products, 0.3%.

As previously stated though, Mexico's tariff regulation and growth has been asymmetrically distributed. Mexican tariffs at implementation of RTAs vary, from 4.9% weighted inside NAFTA to 13.4% in the EU. Outside the free-trade agreements, Mexico's duties range from zero to 35%. In 1999, Mexico escalated tariffs by 3 percentage points for capital goods to 16.5% and by 10 percentage points for consumer goods for all nations with which Mexico does not have a trade agreement. The move was to be a temporary measure to compensate for the East Asian Crisis and low oil revenues, but a reversal has yet to be put into effect.[xxxvii] The increase in rates and reductions in preferential tariffs has widened the gap between treatment granted to imports from MFN and preferential sources.

By September 2003 Mexico had trade pacts with 32 countries, including Argentina, Bolivia, Brazil, Chile, Colombia, Costa Rica, El Salvador, the European Free-Trade Association, the European Union, Guatemala, Honduras, Israel, Nicaragua, Uruguay and Venezuela, representing an overall market of 870m people. The country has tried to consolidate its position as a hub in the network of trade arrangements and will be hosting the negotiations for the Free-Trade Area of the Americas (FTAA) until 2004. The Fox government has continually tried to expand trade with the EU, seeking to lessen Mexico's dependence upon trade with the US, but the investor and exporter privileges established in NAFTA plus poor economic conditions worldwide have made this goal difficult. Pressure is building within Mexico for Fox to re-work the agricultural component of NAFTA, however this will prove hard as the country is so reliant on Canada and the US as trading partners. Outside of NAFTA, no individual country absorbed more than 1% of total Mexican exports.

Venezuela's trade liberalization occurred largely regionally, as the country formed influential trade agreements such as the Andean Pact. During the late 1980s/early 1990s, the country went through a period of commercial opening, which survived crises and falling oil prices. While the country has continued to expand on certain trade fronts, it has been very vocal recently in the rejection of others.

Venezuela's economy is largely dependent upon petroleum exports, making foreign trade essential to the country's prosperity. Not only is oil the country's largest export, but it also provides an abundant source of inexpensive energy for domestic industries, generates large amounts of revenue for the government, and is used to finance advances in education and public welfare. [xxxviii] In the 1970s, the country benefited from extremely favorable terms of trade in oil and was considered by the World Bank as one of the four Latin American countries with an upper-middle-income economy.xxxix In 1973, the quadrupling of oil prices afforded the country new wealth and citizens demanded imported luxury goods. The same year, Venezuela joined Chile, Ecuador, and Bolivia in forming Ancom – a short lived trade agreement that diminished in importance during the late 1970s/early 1980s. In the early 1980s though, oil prices fell on the international market, leading to a massive decline in exports (US$20.1billion in 1981), which accounted for about 90% of total export value at the time. The country continued to demand luxury goods, despite the falling oil prices and imports peaked at US$11.7 billion in 1982. The same year Venezuela joined the Latin American Free Trade Association. During the remainder of the decade, Venezuela experienced a severe economic crisis. The government imposed multiple exchange rates, higher tariffs and greater nontariff barriers as measures to stimulate the economy, but they stifled new imports, which fell by 43% from 1983 to 1986. In 1986, there was a 50% reduction in world oil prices, which further exacerbated the country's internal weaknesses.[xl] During the late 1980s, the country's exports recovered slightly yet did not reach the highest levels from 1981.The state was responsible for exporting as much as 66% of all non-traditional goods. On both the import and export front, the US was Venezuela's main trading partner. Imports

totaled US$10.9 billion, and the country ran its first trade deficit since 1978. The country employed an import-substitution policy to protect local industry and agriculture from foreign competition. The government accomplished this policy through exchange rate manipulation, the imposition of tariffs and through import licensing restrictions. In 1988 there were 41 different rates on more than 6,000 goods. Tariffs were sometimes in excess of 100%, with the average rate at 37%. Both export and import figures excluded substantial illegal trade that occurred along the Colombian border.

At the end of the decade, trade liberalization began as the Carlos Andres Perez retook office (he served as President from 1974 to 1979). During his presidency, he promoted free-market economic reforms, including a plan to encourage economic austerity to deal with foreign debt and secure a loan from the International Monetary Fund.[xli] Liberalization measures also included steps to attract private investment. The reforms were in response to a deteriorating trade balance and major foreign exchange problems and entailed fiscal adjustments, tightening of monetary policy and a lifting of controls on prices and interest rates. A unified, flexible exchange rate was adopted.[xlii] Massive rioting and looting occurred in 1989 killing between 300 and 2,000 people, provoked by a raise in bus fares. Despite a strike called in opposition to Perez's presidency, he continued forward with his economic reformation plan.[xliii]

The government devalued the bolivar thereby making Venezuelan exports cheaper and imports more expensive, a change from the previous import-substitution policies of earlier years. Trade policy changed to focus on making national exports more competitive, to diversify away from the large dependence on petroleum, to reduce the anti-export bias and to integrate the Venezuelan economy more closely into world markets.[xliv] The import policy became more liberal as well in order to comply with GATT requirements. The government reduced the maximum tariff to 80% in order to simplify the tariff structure and set a maximum tariff of 20% and a minimum tariff of 10% by 1993. Import liberalization also addressed nontariff barriers, by abolishing most import licenses, which had dampened the flow of imports and bred corruption.

The changes forced the local industries and farms to be more competitive with international industries, to the displeasure of local businessmen, but the improved access for imports were expected to increase trade flows from within the Andean region. Agriculture remained relatively protected and local content requirements were imposed on imported inputs for automobile assembly.[xlv]

During this period, the country entered into several bilateral and regional trading arrangements with other countries in Central and South America. Trade policy revolved around its accession into GATT in 1990, for which Venezuela bound its tariff at a ceiling level of 50%.[xlvi] Many government subsidies were in violation of GATT regulation, so the amount of subsidized credit offered to merchants for financing exports was curtailed. Likewise, by the early 1990s exporters were no longer eligible to receive tax rebates.[xlvii] From 1990-1992, the reforms showed moderate signs of success as GDP grew and inflation fell. The recovery of oil prices on the world markets contributed as well. Both government finances and the trade account returned to surpluses and external debt was completely restructured. However, the stringency of the fiscal measures contributed to a serious political crisis, and the pace of adjustment slackened. [xlviii] In 1991, Hugo Chavez became a national hero after leading a failed military coup against the government.[xlix]

In 1993, Perez was forced from office due to corruption charges. At this time, the US was Venezuela's most important trade partner, with the EU as second. Imports from other Latin American countries grew to about 18%, however exports within the region fell to 32%. Merchandise trade with MercoSur and Colombia in particular has grown.[l] Rafael Caldera replaced Perez as president, and embarked upon a privatization program, continuing the reforms started in 1989, following a weakening of reformation efforts in 1992-93. The reforms included liberalization in a regional context as well as the entry into the WTO in 1994. However, during 1994, the country experienced a banking crisis that spread to the insurance industry. The government had to re-acquire a large number of companies and eventually liberalized the sector

resulting in significant changes in its operations and structure. This crisis combined with other serious economic problems resulted in a loss of momentum in Venezuela's trade and economic reform, but the country avoided reversing the most of the reforms. The initiation of foreign exchange controls to overcome capital flight and large reserve losses during the political crisis of 1992 had detrimental effects on foreign investment, capital inflows and trade due to a lack of transparency. [li] The controls also led to a real appreciation of the bolivar, and the loss of competitiveness for many Venezuelan exports. [lii] At the end of 1994, Caldera proposed a new Stabilization and Recovery Program that proposed the reduced role of the state in the petroleum and financial sector, among others, and restarted the liberalization program.[liii] In 1995, inflation reached 6%, and to counteract inflationary pressures, the bolivar was devalued approximately 70% against the US dollar.[liv]

In 1995, the Andean group was consolidating free trade and moving towards a full customs union, in which the establishment of a common external tariff was the first step. [lv] The Common External Tariff of the Andean Group, to which Venezuela adheres, is an applied tariff schedule with most rate ad valorem at 5, 10, 15, and 20%. Specific and compound duties are levied on certain items and reduced or zero tariffs apply to inputs, raw materials and capital goods not produced or available in the Andean sub-region. Venezuela implemented the Andean Community's price band system in 1995 to replace a similar national scheme in place since 1991. The price band system makes floor and ceiling prices linked to the moving average and spread over the previous five years of world prices. The system raises questions about the predictability of such a form of border protection that exhibits many of the properties associated with variable levies. Venezuela adopted this system for several agricultural products, including feed grains, oilseeds, oilseed products, sugar, rice, wheat, milk, pork and poultry. Tariff escalation was intended to promote industrial development, encouraging further processing of regional raw materials in Andean countries. [lvi] Under the Andean Community's Common Automotive Policy (CAP), assembled passenger vehicles constitute an exception to the 20% maximum tariff and are

subject to 35 percent import duties. Venezuela maintains special safeguard provisions for 76 agricultural products. However, the country reduced tariff peaks affecting certain automotive items from 40% to 35%[lvii] and created the Ministry of Industry and Trade. Eventual integration between the Andean Group and MercoSur was being promoted, and Venezuela was actively participating in the negotiations of a Free Trade Area for the Americas. [lviii] In 1996, the country eliminated the foreign exchange controls.

In 1998 Hugo Chavez ran for president and began his term in 1999. He campaigned for large-scale political change on an anti-corruption platform, appealing to the impoverished, politically inarticulate yet clearly powerful electorate of Venezuela. His interests were squarely contradictory to the old Venezuelan political and cultural elite.[lix] During his first year of presidency, the Andean Automotive Policy Council determined that it would not eliminate the local content requirement as it had initially indicated, but instead decided to increase it gradually to 34% by the year 2009. This automotive policy was inconsistent with Venezuela's WTO obligations under the TRIMS Agreement and the countries were forced to lower requirements to 24% the following year, and eliminate them entirely by year-end 2000. [lx] In December of 1999, the country entered into an economic recession, but growth returned the following year under the influence of strong global oil prices. The inflation rate was stabilized due to the continuation of a foreign exchange policy that maintains a 7% annual depreciation of the bolivar and the Central Bank's determination to control inflation despite its negative impact on non-oil exports. Foreign investment improved, but investors remained cautious due to Chavez's expressed desire for a "multipolar" political and economic world. His presence has caused uncertainty about the country's long-term political and economic stability, and trade policy has changed as he has expressed concerns over the Free Trade of the Americas Agreement (FTAA). While much of President Chavez's legislation is positive, his frequent verbal attacks on U.S. "economic hegemony" and criticism of globalization have dampened the previously encouraging climate for US exports. [lxi] U.S. goods exports to Venezuela were approximately $5.7 billion, an increase of

$134 million (2.4%) from the level of U.S. exports to Venezuela in 2000. U.S. imports from Venezuela were about $15.2 billion in 2001, decrease of $3.4 billion (18.2 percent) from the level of imports in 2000.[lxii]

In November 2001, Chavez's administration passed a hydrocarbon law that caused further hesitation on the part of foreign companies. The law increased royalty payments owed by investors and required that the state control at least 51% of each joint venture in this sector.[lxiii] Chavez also announced 49 reform laws, prompting a protest of the business community in the form of a one-day strike. The laws include land and oil reforms that were enacted without the approval of the National Assembly. In early 2002 the government ended exchange rate controls on the Bolivar, causing it to drop 25% against the U.S. dollar. Opposition to Chávez, comprised of political parties, powerful business groups, trade unions, and other sectors of civil society, began to become more vocal, staging protests and mass demonstrations. In April 2002, the pro- and anti-Chávez groups clashed violently during a general strike, which had been called in protest of his economic reforms, among other objections to Chávez's rule. 150,000 people came out in support of the strike, of which 10 were killed and another 110 injured. Military factions attempted a coup against Chávez's government, which failed within two days and Chávez returned to power. After the coup attempt, Chávez promised to cooperate with his opposition, but the increasingly desperate economic turmoil within Venezuela energized the opposition once again. In December though, a general strike was called, which included many workers in the state oil company. Shops and universities closed, and shipments and oil production came to a standstill, further endangering the Venezuelan economy. The opposition hoped to topple Chávez's government with the work stoppage, and Chávez chose to ride out the storm, which ended after 9 weeks. The opposition accepted Chávez's proposal of a recall referendum.[lxiv]

Chávez has steered the country towards protectionism and made few market reforms. Still, the government has maintained a number of free-trade zones and tax incentives for foreign investors. Incentives include tax holidays, usually lasting for five years.[lxv] In April 2001,

Venezuela, Colombia and Mexico re-launched the practically defunct Group of Three Accord (G3) that had originally taken effect in January 1995, with pledges for greater political co-operation and a firmer commitment to fighting regional poverty. In January 2002 the country joined Bolivia, Colombia, Ecuador and Peru to expand the 1996 Andean Pact into a free-trade zone and to adopt common import tariffs from January 2004. The country has formed bilateral investment protection and promotion agreements with 20 countries and bilateral tax treaties with 18 nations, including the United States. In 2002, as part of the Andean Community Venezuela agreed to establish an Andean free trade zone, a common external tariff (CET), and a customs harmonization policy by January 2004. The CET agreement establishes a unified tariff schedule that will come into effect at the end of 2003. The CET reportedly will be zero duty on capital goods, five percent on industrial goods and raw materials, ten percent on manufactured goods with some exceptions, and twenty percent on "ultra-sensitive goods." [lxvi]

However, when all finance ministers of Latin American countries signed a resolution to join the Free Trade Area of the Americas (FTAA), Venezuela said "no thanks." The country's chief FTAA negotiator Victor Alvarez noted that the US was preaching free trade while facing an enormous penalty from the WTO for raising steel tariffs. President Chavez, in an interview, was quoted as being less subtle: "the FTAA is the path to hell." He does have an alternative to FTAA, ALBA, standing for the Bolivarian Alternative for America. Chavez wants to create a "compensation" fund, in which the wealthier nations of North and South America would fund development in the poorer states.[lxvii] Also recently, Venezuela has been reluctant to implement directives from the Andean Community, straining its relations with its Andean trade partners. Ill feelings are exacerbated by the government's unilateral overtures towards the MercoSur, which Mr Chávez would like Venezuela to join, and for restricting imports or imposing tariffs on garlic, wheat, potatoes, sorghum and yellow maize. The signing of the Andean Community of Nations (CAN) ended without Venezuela signing the document of the sixth regular meeting of the Advisory Council of Finance Ministers of Central Banks. The agreement includes a clause stating

that the authorities urge Venezuela to “give priority and automatic treatment to community imports which are channeled through the reciprocal payments and credits agreement of the Latin American Integration Association.” The country has failed to pay debts relating to imports from Colombia, Ecuador, Peru and Bolivia. Additionally, Venezuela was among the countries that walked out of the WTO trade negotiations in September 2003. The government imposed tariffs of 10–30% on a variety of steel products in April 2002 after the US announced similar measures. The tariffs were set to expire on June 11th 2002, but the government extended them for an additional 15 months. The average tariff in 2001 rose to 11.8% from 9.7% in 2000. The Chávez administration also wants to support import substitution; it is willing to impose import controls and some price restrictions to protect domestic agriculture and industry. Since 1999 the government has required importers of agricultural products to register with the Ministry of Production and Commerce, establishing another bureaucratic barrier to imports.[lxviii]

Bolivia depicts a country that liberalized relatively unilaterally/multilaterally through decreasing tariffs to all trading partners in a nondiscriminatory fashion, but also has had regional and multilateral agreements play influential roles in its liberalization. Throughout its history, the country has depended on a few exports such as tin and natural gas to generate foreign exchange and import the goods and services it was unable to produce.[lxix] After the collapse in the world tin markets in 1985 a distinct period of liberalization and commercial opening occurred, but recently the country has faced setbacks and backlashes in the international trade arena.

Since the 1500s to present day, the mining industry has dominated Bolivia’s economy. In 1952 a five-year long revolution led by the Central Obrero Boliviano (COB) consisting primarily of native Indians, led to the nationalization of the country’s tin mines.[lxx] Due to the country’s large stock of natural resources, during the 1970s, its future looked bright. The world market for mineral exports was strong, and gas and oil reserves made it appear that the country would be a net exporter for time to come. The Banzer presidency in the mid-1970s enjoyed a spending and borrowing spree, but towards the end of the decade commodity prices fell, rapid growth of local

oil consumption eroded the exportable surplus, and gas exports ran into trouble.[lxxi] Despite being one of the world's leading producers and exporters of tin, by the early 1980s the industry faced numerous structural problems. The cost of underground mines were among the highest worldwide, transportation was difficult due to poor infrastructure, high-grade ore had become largely depleted, and continual labor problems were some issues that the nation's most important export faced. Between 1978 and 1985, Bolivia fell from second to fifth position among tin producers.[lxxii] The falling demand for tin on the world market began to decrease forcing many Indian producers to turn to the production of coca to earn income. Natural gas, the country's most lucrative export after tin, became jeopardized in late 1970s and early 1980s by payment difficulties and the discovery of gas deposits in its major market, Argentina.[lxxiii] However, in 1977 the mining sector still accounted for 8% of the country's GDP and 65% of its exports. [lxxiv]

In 1980, registered exports exceeded $1 billion. That year a military coup led by General Luis Garcia Meza, allegedly financed by cocaine traffickers, overthrew an already fragmented government. Due to government involvement in drug trafficking, Bolivia's international reputation started to deteriorate. Meza abandoned the IMF's stabilization plan and instead invested largely in coca growth. Cocaine exports during the 1980-1981 period were estimated to be $850 million, rivaling total reported registered exports of $908.5 million.[lxxv] Imports for the year were estimated to be $918 million.[lxxvi] As foreign debts came due and prices for mineral exports fell, the government corruptly plundered the country's central bank of its dollar reserves. In one year, the deficit of government revenues in relation to spending nearly doubled. Due to the coup along with other domestic policy changes the IMF, creditor banks and the World Bank blocked credit to Bolivia and placed an embargo on its international trade. [lxxvii] These measures provoked a financial crisis and the government printed money to finance the deficit. Hyperinflation resulted, terms of trade declined, and the country's average wage fell to $13 a month. Meza eventually faced repeated coup attempts and resigned during 1981. In Feb 1982, President Celso Torrelio Villa announced the devaluation of the peso to 44 pesos per dollar from

24.51 to the U.S. dollar. However after years of mounting debts**,** unstable governments, high inflation, and falling industrial production the economy entered into a severe recession.[lxxviii] In 1982, the combination of depressed international tin prices and Argentina's debt problems leading to sporadic payment of natural gas exports (40% of exports) exhausted Bolivia's foreign-exchange reserves. In 1983, the country stopped making repayments of principal on foreign debt and in 1984 it announced that it would not be able to make interest payments either "for the time being."[lxxix]

In 1984 elected-President Hernan Siles Zuazo tried to regain control of the situation by implementing exchange controls, raising export taxes and converting all dollar-denominated contracts to Bolivian pesos. Labor groups frustrated attempts at economic reform by striking and closing the Central Bank. As inflation reached almost 1,500%, the President called his mandate short by 1 year and declared elections in 1985.[lxxx] Since no candidate received over 50% of the vote, the congress appointed on Paz Estenssoro as president. Estenssoro entered into an economy with inflation of 4,000%, outputs and exports had been declining for years, many financial institutions were insolvent, and there was widespread social unrest and drug trafficking. He implemented his presidential-competitor's economic recovery program under the name of the New Economic Policy (NEP). The policy called for the stabilization of the exchange rate with a "dirty float," the reduction of government deficits to reduce the growth of the money supply, and the liberalization of exchange operations to re-attract capital into the country. Additionally, it called for cuts in real wages and the suppression of the powerful labor movement and negotiations with international creditors. The NEP's decision to float the peso against the dollar caused an immediate devaluation. Three months of stability ensued but tin prices collapsed and inflation once again rose. Estenssoro followed the advice of a US economist, Jeffery Sachs, by supporting the peso through buying peso in international markets with Bolvia's foreign exchange reserves. This resulted in an appreciation of the peso by 10% and monthly inflation quickly fell to

zero. Furthermore, the black market was legalized in order to keep the currency at market rates.[lxxxi]

Trade policy was focused on diversifying the export base as well as making the external sector more market oriented. After 1985, all export taxes were abolished and constant devaluations of the Bolivian peso through a floating exchange rate helped lower the prices of exports, improving their competitiveness. The government also declared tax rebates for exports and established an export promotion institute, hoping to expand market-oriented policies and thereby exports. The attempts to force Bolivian producers to compete with the prices of international products after years of protection were often unsuccessful. The government emphasized import liberalization through tariff reform, realistic exchange rates, aggressive import tariff collection and the promotion of nontraditional agricultural exports and minerals. Imports increased after a uniform tariff of 20% was introduced[lxxxii] but were made more expensive by the lower exchange rate. Import and investment permits were eliminated and Brazil surpassed the US as the leading supplier of Bolivian imports.[lxxxiii]

The government entered into an IMF stabilization program and in four years, Estenssoro achieved economic and social stability and established the country's institutions firmly in democracy. The central bank focused on keeping inflation in check, improving the financial viability of government banks, and improving the ailing commercial banking system. The new boliviano replaced the peso as the official currency to redress the damage done by the hyperinflation.[lxxxiv] The power of the tin miners union was reduced and 75% of the workers in the government-owned mining corporation were laid off. However, a large portion of economic activity still was not reflected in official export figures – the export of coca paste or cocaine and the smuggling of other illegal goods. Estimates of coca-related exports during this time range from US$600 million to US $1 billion per year.[lxxxv]

A substantial shift was seen throughout the decade in the relative importance of tin and natural gas exports. Tin as a percentage of total exports declined from 37% in 1980 to 12% in

1987, while natural gas increased from 21% to approximately 44% of exports. Official exports in 1987 only totaled US$569 million, the lowest level of 1980s, but competitiveness did increase after 1985 due to the abolishment of taxes and the adoption of the floating exchange rate. Nontraditional exports composed mainly of sugar, soybeans, coffee, beef, and timber reached a high of nearly 19% of all exports. In 1988 it was estimated that cocaine revenues fell below US$300 million and hydrocarbons became leading export, accounting for over 50% of government revenues in 1985. Timber exports, mainly to Brazil, surpassed all other legal agricultural exports in 1987 and totaled US$31 million.[lxxxvi] A 1987 policy change abolished export taxes, allowing small miners to sell their exports without the assistance of Banco Minera de Bolivia and boosting their output and foreign sales.[lxxxvii] Imports reached approximately $777 million, their highest level in the decade, with an estimated additional $500-600million in contraband imports. Unlike exports, import composition changed only slightly. Capital goods, mostly machinery and equipment for industry and transport, accounted for nearly 42% of all imports, followed by raw materials and intermediate goods, dedicated primarily to import-intensive manufacturing (40%) and consumer goods (16%).[lxxxviii]

In 1988, the currency was relatively stable, exports rose to US$599 million, and imports fell to US$700 million. The tariff for capital goods was decreased to 10%, a level that was scheduled to be uniform again by 1990. Over the next five years, during the Paz Zamora Administration, the market reforms started by Estenssoro were advanced, but limited economic growth was achieved. In 1990 the government dropped the rest of the tariffs to a uniform rate of 10% from 16% as planned, with a largely neutral incentive structure that did not discriminate among sectors. The capital goods rate has only a 5% tariff and some books and publications have a 2% rate. The WTO stated that the country had a liberal trade policy for goods and services and does not apply permits and other types of non-tariff barriers. There is no trade discrimination and no sectors of the economy are subsidized.[lxxxix] In 1990, Bolivia approved three laws in order to promote private investment.

In the same year, new discoveries of natural gas in Argentina signaled that Bolivia needed to find a new market for gas exports. Talks for a natural gas pipeline between Bolivia and Brazil intensified.[xc] From 1990 onward, the country has focused its trade relations increasingly on preferential agreements with countries such as Chile, Mexico, Cuba, the Andean Pact and MercoSur. It has unilateral preferential and zero tariffs for a list of products from the US (through a framework of the preferential tariffs law for Andean countries) and from the European Union.[xci]

In 1991 the Bolivian government eliminated a certificate rebate program under which the exporters of "non-traditional" goods received certificates equal to 6% of the value of the export. The certificates were to offset the 10% value-added tax charged on all purchases in Bolivia and was replaced with a "drawback" scheme that rebated either two or four percent of the value of most "non-traditional" exports.[xcii] In early 1992 Presidents Paz Zamora and Alberto Fujimori (of Peru) signed an agreement whereby Peru ceded an area of 327 hectares to Bolivia for it to develop a free zone at the port of Ilo in southern Peru. This gave Bolivia access to the sea through a free port for its international trade.[xciii] In 1992 the government continued with the goals of the Andean Pact and eliminated the tariffs on all but 11 products coming from its three other members (Venezuela, Colombia, and Ecuador).

In 1993, the Sanchez de Lozada government took office with a privatization agenda for the country. The Export Law was established to replace the drawback program, whereby the government grants rebates of all the domestic taxes paid on the production of items later exported. By year-end the government reduced debt owed to commercial banks from $700 million in 1985 to $8.8 million,[xciv] and signed a gas sales contract with Petrobras in Brazil.[xcv] The following year, the country signed the Marrakech agreement giving birth to the WTO. Bolivia seeks to increase access to developed-country markets and to obtain reductions in non-tariff barriers to trade, which are the main constraints to Bolivian exports.[xcvi] From 1993 to 1997, the share of reported trade flows in GDP rose from 36% to 43% as the country further opened to trade.[xcvii]

In 1997, the country created the Ministry of Froegin Trade and Investment that shares responsibility for the formulation and implementation of the country's trade policy with the Ministry of Foreign Relations.[xcviii] The country also began to implement an associate agreement with MERCOSUR that provides for the gradual creation of a free-trade area covering at least 80% of trade between parties over a 10-year period, though economic crises in the region derailed the integration process. As of 2001, Bolivia's main markets for exports are the EU (27%), NAFTA (20%), the Andean Community (21%), MercoSur (18%). In the same year, a bilateral treaty between the US and Bolivia came into effect. [xcix]

Bolivia's trade liberalization and progress has changed directions as of late. A founding and active member of the WTO, the government of Bolivia now considers that instead of receiving benefits from developed countries for their autonomous liberalization, the country has been penalized by having to compete with subsidized exports or with products that have received much domestic support. Bolivia supported the draft declaration of the Cairns group, to which it was admitted just before the Seattle-round, and which clashed with the EU position. This clash, as well known, was one of the main causes for the Seattle failure. Because of the failure there have not been any positive outcomes for Bolivia, so far, from participating in the WTO. Among other requests, in 2001's Doha Conference Bolivia asked for: a commitment to end discrimination against agriculture and fully integrate into WTO rules, a commitment to achieve fundamental reform of agricultural trade through elimination of all forms of export subsidies, and special treatment provisions for developing countries to be an integral part of the outcome of the negotiations.

From 1999 to 2001, Bolivia once again experienced near zero growth rates, owing to a sharp fall in the price of minerals and tougher control on cocaine production. New items such as quinoa, meat, wines and beer have been added to the traditional export list while the completion of the Brazilian pipeline has increased the importance of natural gas. In 2000, Bolivia exported goods and services valued at US$1,229 million, or 13% of the country's GDP. The value has

remained relatively constant over the last 20 years whereas imports have shown an increasing trend. Imports have grown to approximately $US1,977 million. Due to its limited expansion of exports, the country has limited trade-negotiating power, a chronic deficit in its balance of trade, and an underdeveloped manufacturing sector.[c] The poor performance of exports suggests that in spite of Bolivia's efforts in trade agreements, little has been achieved reaching beyond paperwork. In addition to the stagnant export sector, domestic demand is weak. The government needs funds, however without access to international financial markets, it must ask for aid. The aid will most likely come at the expense of free access to Bolivia's mineral reserves, which the masses are fiercely opposed to.

> "But like the poor of Honduras and Argentina, Peru and Ecuador, Bolivians have understood that it is they who pay the bill for privatisation, that the growth they were promised has stalled, that the country's exports are worth less than they were before Bolivia signed up for globalization and that the gap between their miserable standard of living and that of the tiny elite has widened. They have understood that privatisation means higher prices for essential utilities, that however hard they work their children remain unschooled and that they live and die in poverty. They have learned, too, that when they protest, an elected government will shoot them, just as the dictatorships used to." (The Guardian, 21st October)

In January 2004, the country announced that it had decided to suspend FTA talks with Chile. A month prior, Bolivia imposed "safeguard measures" on five products imported from Peru. The country imposed 40% tariffs on these products as a "retaliation against Peru's imposition of a 12% tariff on Bolivian edible oil" that occurred in October. [ci] Another trade controversy has formed with Argentina, over exportation of the Bolivian banana and importation of Argentinean meat. The country forced President Gonzalo Sanchez de Lozada to resign on October 17th 2004 due to pressure after months of strikes and street clashes that left at least 80 dead. Bolivia's labor federation of transport workers, coca growers and miners had joined natives and intellectuals in protesting the plan to export Bolivian gas through Chile, as well as their long-

standing opposition to his IMF-imposed free market policies.[cii] Opposition to the government is rallying behind Evo Morales, a supporter of the coca growers, who almost defeated Lozada in the presidential elections. The Pacific LNG consortium estimated that the project's $20 billion in revenues would bring $5.5 billion to Bolivia over two decades, cut its dependence on Brazil, and increase its GDP by 16%. Since the spoiled plans to export gas through Chile and send it north, Bolivia's reputation as an investor- friendly country has been tarnished.

Section VI: Case Study Analysis

Using the two frameworks outlined early, further discussion of the events that transpired throughout each country's liberalization history is warranted. With more concentrated exports, I expected to see a country have a more difficult time maintaining liberalization. There will be less broad-based support to maintain commercially open policies in the event of negative shocks to the economy, and a stronger push from national companies for high tariffs/protectionism to combat competition. Furthermore, by diversifying into other goods, the country's economy becomes more stable as it is less susceptible to international fluctuations of prices. Constituents will be willing to give up a volatile high-growth and high concentration approach to trade for a lower growth path with less volatility. In turn consumers and international pressures will begin to mount on the policy-makers of the country, further committing the country to a liberal trade policy.

Chile – Liberalization occurred through tariff reduction and diversification away from dependency on copper. In Chile, the initial broad-based support for a liberalization policy came from the policy-makers themselves, the "Chicago Boys." This wide constituency of foreign-educated advisors supported continual liberalization but took care to explain the long-term benefits and educate the public along the way. When the country fell into a recession during in the 1980s, the trade front retrenched slightly, but mostly on the import/tariff front. As seen in the HHI averages, exports remained relatively diverse during this time. Stability in the country

eroded, but this was due in part to regional factors beyond control, such as the debt crisis and a recession in the US. It is important to note as well, that during these difficult times Chilean firms began to operate more efficiently and increased their productivity, allowing for more successful competition on an international level. By implementing another export diversification strategy in the mid-1980s, Chile was able to pull out of the recession, increasing the country's stability, earnings and standard of living. Since that trying time period, the country's policy makers have continued to support liberalization on all fronts. While the government is no longer homogenous in support for liberalization, the business class and consumers have formed a broad-based constituency to pressing for continual liberalization. In this way, original cohesive vision of the "Chicago Boys" has been continued.

Bolivia – Despite having an export base that has diversified over the last two decades, the country has retrenched. The re-closing situation in Bolivia has stemmed from instability in the economy, due to a plethora of reasons. While exports have grown promoting stability, external factors such as regional difficulties, slow growth of main trading partners and external financial crisis have outweighed the strides export diversification has made. While the country has a diverse set of trading partners, evidence suggests that regional dependency in this case have caused problems. The currency crisis in Brazil and Argentina, increased trade protection measures by Brazil, Chile and Peru, and the expiration of the gas contract with Argentina have all weakened Bolivia's sustainability and export earnings. The contagion from the area spread to Bolivia, contributing to dissatisfaction with globalization.

Additionally, the country never gathered the type of support for trade liberalization that Chile/Mexico did. During the export diversification focus in the mid-1980s, Bolivian producers never became efficient enough to compete with the prices of international products. While export diversification followed due to favorable tax policies and certificate rebate program, the overall value of exports did not grow. Without sustainable gains in productivity or efficiency, further liberalization was impeded by businesses due to cheap goods and high competition flooding the

market. While there is some business support for the liberalization of trade (i.e. the company that tried to push for the pipeline), these few actors are not politically influential enough to sustain liberalization in light of citizen opposition. Bolivia never achieved citizen support for trade liberalization; standard of living didn't increase despite exportation of natural resources, coca eradication initiated at the demand of the international community led to job loss that was not successfully replaced, and enough domestic demand was never generated to spur development of the manufacturing sector. Export diversification is a limited strategy; it will not be able to overcome all of these difficulties and allow a country to maintain commercial openness.

Mexico – Changed from a closed country that was dependent on one export to a liberalized trade environment with a diverse set of exports. Around the 1980s, when exports were 80% tied up in petroleum, the economy became instable in part due to enormous debt, high inflation, a rise in interest rates and a decline in international oil prices. The debt crisis in 1982 caused domestic businesses to mobilize in support of a governmental liberalization program. Additionally, international pressure from the World Bank forced policy-makers to give up import substitution policies for a stress on export diversification. Export-led growth occurred mostly through investments by multinational corporations, which benefited from the cheap labor costs in Mexico. During the negotiation of NAFTA, Mexico's exporters benefited immediately from the removal of US tariffs on 75% of Mexican products as well as other favorable terms by the year 2009. This large time period was given to allow Mexican industries the ability to reform and thus compete against US markets more efficiently. While the achievement of these goals and the success of the trade agreement are hotly debated after its 10-year anniversary, the government did continue to liberalize through forming trade agreements. This suggests either pressure from the US, the WTO, or international supporters for continual liberalization despite the recession of 1995. While the country's overall growth has slowed, trade has increased immensely albeit in an extremely regionally focused direction. The diversification of exports in this situation seems to be the first step in supporting continual liberalization to countries other than the US. However, an

increased standard of living must be seen among all constituents and increased productivity and efficiency must be achieved by businesses or there will be a risk of retrenchment pressures forming.

Venezuela – Like Mexico, the country's trade began as highly concentrated in petroleum. However, unlike Mexico, Venezuela has yet to diversify away from the petroleum. While several governments have tried to promote non-petroleum export growth, as seen in the HHI, the country is still highly dependent on petroleum products. The country will grow and prosper when oil prices soar, as happened during the 1970s. However, strong growth will be volatile due to the country's dependency on international commodity prices. Additionally, the state has immense interests tied up in both non-traditional and petroleum exports, meaning that trade policy can be changed at any whim of the government. High levels of state involvement in the private sector in many cases have led to inefficient production and products that are not competitive in the world marketplace. Unfortunately for Venezuela, diversification policy has been unsuccessful thus far, and the country is on a path of government intervention and trade retrenchment. Chavez has used the country's long recession to switch policy and continually close borders in order to protect domestic interests. In the long run, the country will continue to be instable until the private sector operates more independently from the public sector.

Section VII: Empirical Findings

Further support for the idea that more diverse exports generate more sustained openness has been found in empirical evidence. While the evidence supported the idea of diverse exports, support was not found for the argument that diversity in countries was an important factor in maintaining commercial openness. Results can be found in Table 1 of the Appendix. Empirical calculation was performed using data dealing with world bilateral trade flows from a database known as the World Trade Analyzer (WTA) assembled by Statistics Canada. The database includes bilateral trade flows for all countries from the period 1980-1997, categorized by

Standard International Trade Classification (SITC). Also included in the WTA are the yearly bilateral trade values between all countries of the world during the same time period according to the 34-industry basis used by the U.S. Bureau of Economic Analysis.[4]

Using this data, each individual country's total export value was calculated, and then a Herfindahl Index was calculated for each country's export concentration and export country-destination concentration. Due to time constraints, HHI calculations were inserted into a working model of trade sustainability, developed by Henisz and Mansfield (2003). Their model takes into account the effect of the following variables: initial level of import penetration, unemployment, political institutions, exchange rate, availability of public and private capital, economic shocks. It also allows for unobserved country-specific and time-specific effects and correlations in error structures across time. The results found an important association between export concentration by product and by country and subsequent changes commercial openness (defined by changes in import penetration). The evidence suggests a strong negative association between export concentration by product and the predicted percentage change in import penetration.

Holding all else equal a country, such as Indonesia in 1985 that is one standard deviation more concentrated in the products that they export is predicted to reduce their level of import penetration by eight percent as compared to a country at the mean of the concentration of its exports during the same year, like Colombia. This is a substantial effect as the mean level of change in import penetration in the sample is 2.7% and a standard deviation is 21%. By contrast, there was a strong positive association between export concentration by country and the predicted percentage change in import penetration. Holding all else equal, a country with one standard deviation more concentration in the countries to which they export, such as Belize in early 1980s, is predicted to increase their level of import penetration by nine percent as compared to a country at the mean of the concentration of its exports, like El Salvador during the same time period.

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[4] The Statistics Canada world trade data are made available here through a Distributor license purchased by the University of California, Davis

Combining these two effects suggests that a country able to diversify the products that it exports while engaging in trade integration with one partner or a small set of partners could expect to increase its import penetration by 10-25%. (e.g. Mexico which decreased its concentration by product from 0.2905 to 0.0635 and increased its concentration by country from 0.4373 to 0.6740 over the period 1980 to 1997. Or Honduras which decreased its concentration by product from 0.1797 to 0.1390 and increased its concentration by country from 0.2953 to 0.4494 over the same period.) These effects are significant in stable democracies but not in the subsample of other countries with available data, which suggests that there is an important role for the political aspect of trade liberalization as opposed to other causal mechanisms. It is important to keep in mind that the existent of this association does not mean that a government policy to enhance diversification will cause more sustainable openness. Government intervention to foster the optimal diversification strategy will have an associated set of costs, which need to be evaluated before assessing completely whether or not an export diversification policy would be worthwhile.

Section VIII: Limitations

While both the case studies and empirical evidence advocate that export diversification strongly affects the sustainability of trade liberalization, this paper is not suggesting that it is a panacea for commercial openness. Many other factors, including political, economic, and social conditions, play a significant role in the sustainability of trade liberalization. As seen in the case of Bolivia, the broad base of exporters has been overpowered by individuals' pressure on the government to retrench. An open trade policy has failed to provide accumulation of physical and human capital, made minimal improvements in production efficiency, and tolerated continual existence of inequality and social exclusion. Longstanding administrative weaknesses such as a corrupt legal system, underdeveloped financial markets and poor governance, have caused loss of important constituents that should favor international trade due to an increased standard of living. However, the developments in Bolivia should be monitored carefully, as maybe the country is

going through a difficult time after passing such broad liberalization measures. Perhaps the country will end up continuing to liberalize, and the current problems will look like a mere blip on the map, resembling Chile's problems during the mid-1980s. Bolivia may also be an example of a country that did not chose the optimal portfolio of goods to export.

There are two other issues that do provide reasonable arguments against the export diversification theory that I have proposed. The first problem stems from the original economist reasoning for trade: specialization by each country in areas of comparative advantage for greater benefits overall. Comparative advantage in traditional trade theory would stem from an increase in specialization, which would then lead to greater instability in a country. As a country exports more diverse products, greater stability is achieved but the benefits of specialization are sacrificed and comparative advantage will be harder to accomplish. (Love 1979a) (Siegel 1994) The importance of the impact of these gains from export diversification versus the losses of the benefits of specialization remains to be assessed. A comparison between these two issues would constitute an interesting area for follow-up study. The second difficulty in my argument is one of causality: it is possible that broad liberalization itself generates more diverse exports and thus the argument has causality backwards. While this argument regarding which order of occurrence has merit, the issue would be better viewed if considered a cycle. A country may begin liberalization through tariff reduction, but when it begins to focus on export diversification it will lead to either stronger support for the liberalization or lead for a call to backtrack. I argue that the export diversification will lead to stronger support for the maintenance of a liberal trade policy, regardless of whether it occurred at the beginning of the country's commercial openness or towards the end. Until the world is composed entirely of multilateral free trade agreements, there is room for liberalization and export diversification policies will direct movement in this direction.

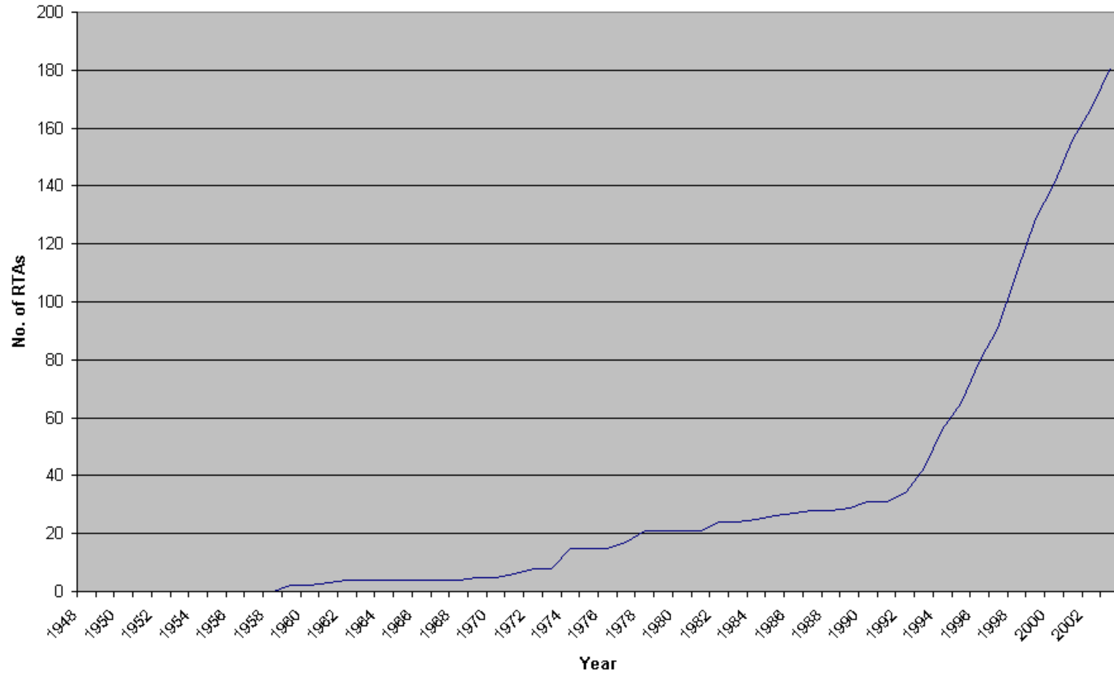
Section IX: Conclusions

Despite the limitations discussed above, the interesting preliminary findings of this research merit further exploration. I have argued that regional versus multilateral trade liberalization is not of utmost importance when exploring sustained commercial openness, instead export diversification plays a substantial role in trade liberalization policy durability. Two main theoretical frameworks, the policy approach and the portfolio approach, support my argument that greater diversity in exports generates more sustained openness. While export diversification is not the panacea for sustainable commercial openness, case studies and empirical data have shown the importance of this type of strategy in for continual liberalization. A less concentrated set of exports leads to greater support among influential constituents, which in turn pressures policy-makers to maintain liberalization. Export diversification will also promote continual opening because domestic constituents desire less volatility and more stability in overall earnings.

Additional research should explore the costs associated with implementing this type of export oriented trade policy in order to better understand whether or not government's should proceed with this type of program. Specifically, it would be interesting to explore the cost of losing the advantages of specialization versus the benefits provided by export diversification. Finally, it must be kept in mind that these arguments are based on assumption that liberalized trade indeed brings benefits to individual countries, as economists have theorized in traditional trade theory. If nations like Bolivia and Venezuela continue on their path of commercial closing, further investigation may be warranted to investigate whether or not this theory applies to all countries. Perhaps developing countries are actually acting in their best interest by continuing to protect infant industries and the economic model must be reevaluated in light of present day country-development discrepancies. With continued research in this field, a more complete picture will be generated for all countries, showing how to best mitigate the negative effects of liberalization and receive as many benefits of trade as possible.

Section X: Appendices

Chart 1:



Source: World Trade Organization -http://www.globalpolicy.org/globaliz/charts/rtatable.htm

Chart 2: Country HHI Index by Year

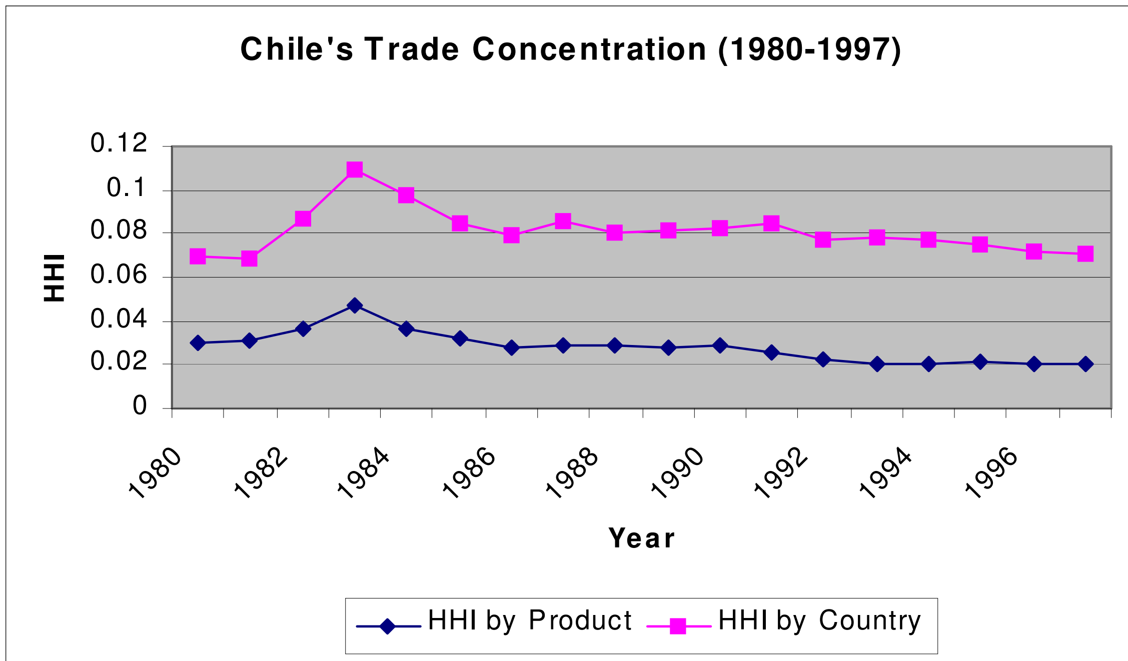
Chile		
Year	AvgOfSumOfExportShareSquared1	AvgOfSumOfExportsharesquared
1980	0.030088	0.069785
1981	0.031391	0.068322
1982	0.035986	0.086451
1983	0.047336	0.109392
1984	0.036613	0.097464
1985	0.032328	0.084692
1986	0.027697	0.078774
1987	0.028965	0.085483
1988	0.029047	0.080692
1989	0.027859	0.081498
1990	0.028621	0.082666
1991	0.025669	0.085125
1992	0.022554	0.077678
1993	0.020856	0.077813
1994	0.020269	0.077339
1995	0.021394	0.075160
1996	0.020728	0.071679
1997	0.020285	0.071245

Mexico		
Year	AvgOfSumOfExportShareSquared1	AvgOfSumOfExportsharesquared
1980	0.290545	0.437368
1981	0.187757	0.288254
1982	0.200855	0.297795
1983	0.169092	0.403197
1984	0.144033	0.393481
1985	0.154875	0.425082
1986	0.170847	0.457035
1987	0.127781	0.425979
1988	0.092656	0.439922
1989	0.107534	0.498642
1990	0.122393	0.497330
1991	0.107252	0.478859
1992	0.063494	0.628029
1993	0.065792	0.671728
1994	0.067744	0.689354
1995	0.068951	0.668062
1996	0.067970	0.661221
1997	0.063591	0.674067

Bolivia		
Year	AvgOfSumOfExportShareSquared1	AvgOfSumOfExportsharesquared
1980	0.101374	0.162005
1981	0.172627	0.222840
1982	0.255052	0.307847
1983	0.267162	0.309121
1984	0.321074	0.347589
1985	0.367389	0.384147
1986	0.314207	0.348112
1987	0.235767	0.274937
1988	0.180740	0.219043
1989	0.117346	0.149730
1990	0.103865	0.136410
1991	0.111015	0.159236
1992	0.071992	0.122545
1993	0.055140	0.139323
1994	0.055707	0.161838
1995	0.044442	0.138312
1996	0.044777	0.115340
1997	0.044725	0.121323

Venezuela		
Year	AvgOfSumOfExportShareSquared1	AvgOfSumOfExportsharesquared
1980	0.136482	0.140435
1981	0.145642	0.156036
1982	0.161320	0.169503
1983	0.163859	0.175003
1984	0.185040	0.206654
1985	0.180626	0.238251
1986	0.269023	0.335546
1987	0.158312	0.198757
1988	0.265006	0.329684
1989	0.250594	0.316170
1990	0.213627	0.290306
1991	0.237829	0.277356
1992	0.025365	0.148217
1993	0.251485	0.306064
1994	0.216440	0.277961
1995	0.211456	0.268394
1996	0.295218	0.350766
1997	0.307237	0.363925

Chart 3: Country Graphs of HHI Index by Year



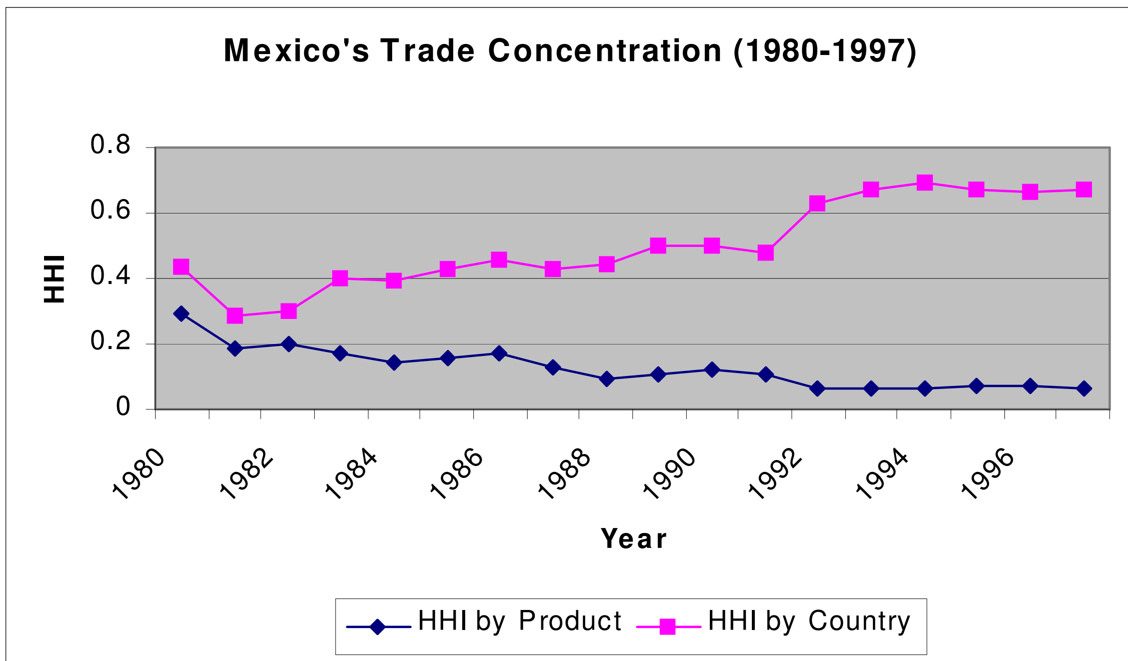
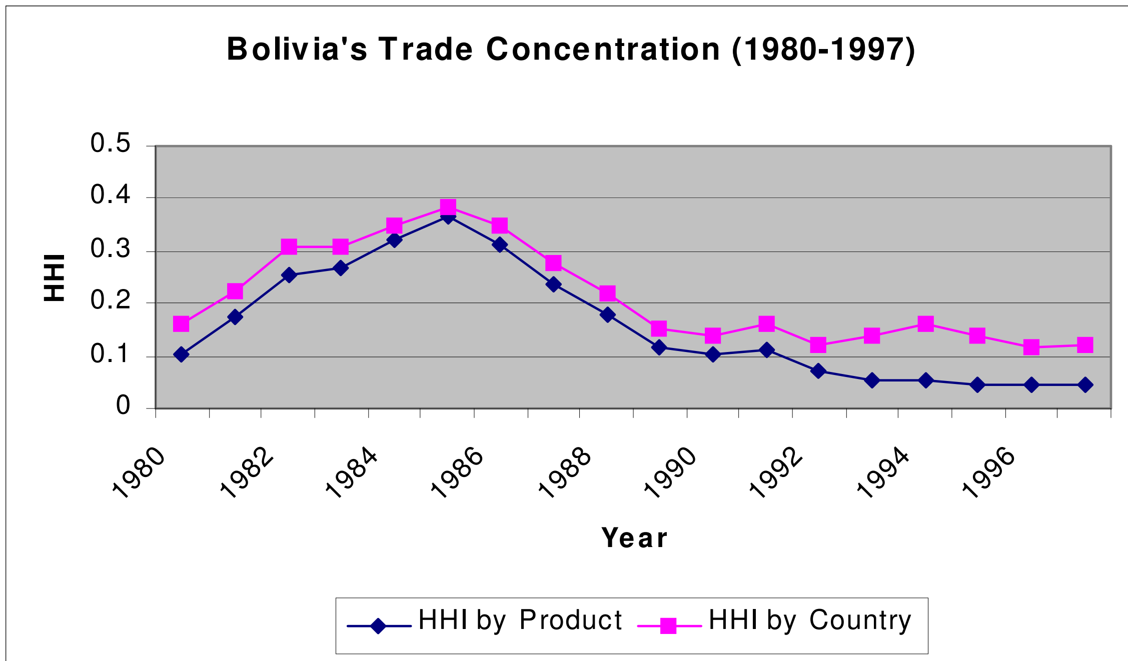


Chart 3: Country Graphs of HHI Index by Year (Continued)



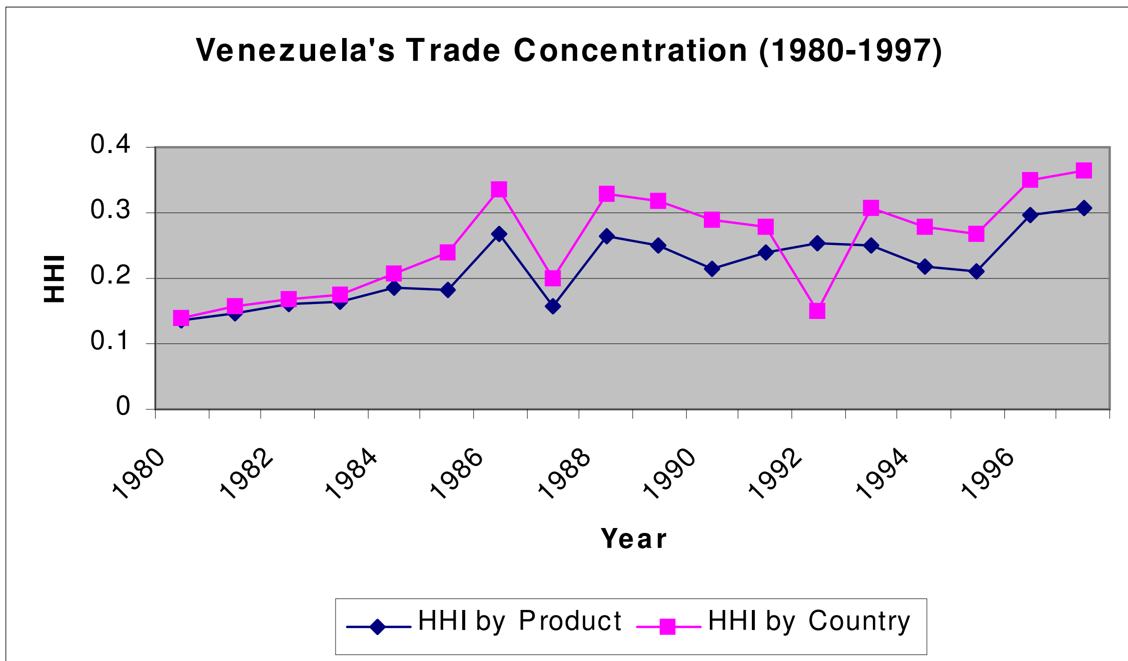


Chart 4: Country Comparison of HHI in 1997

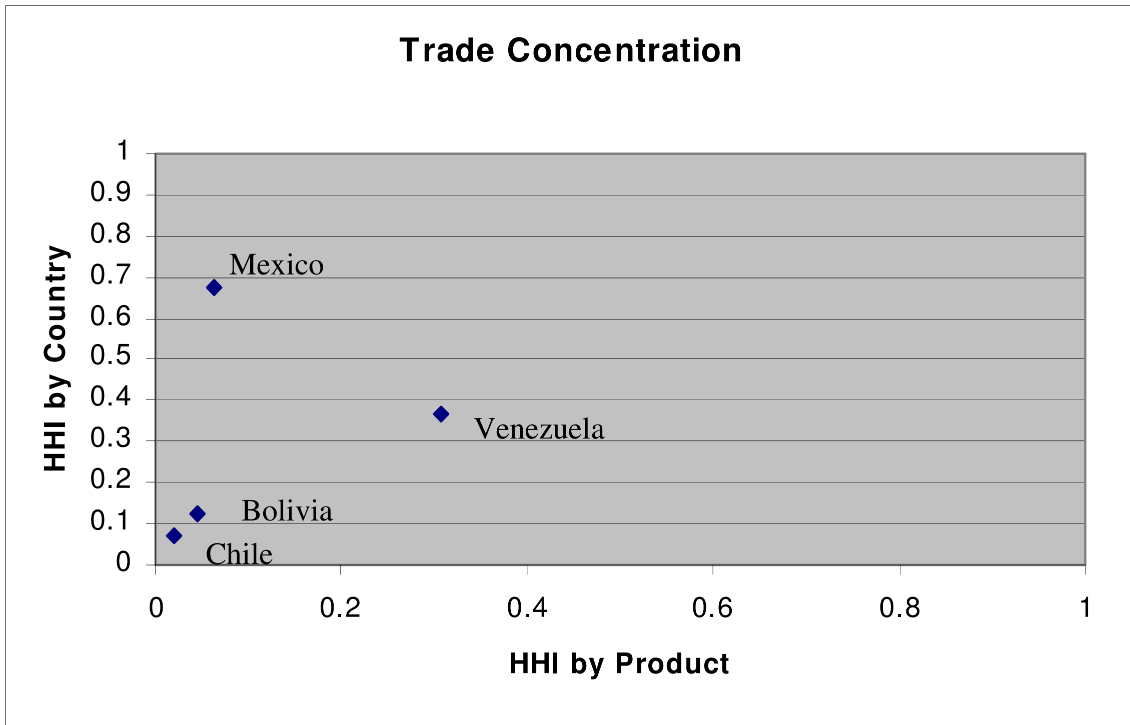


Chart 5: Worldwide Comparison of HHI in 1997

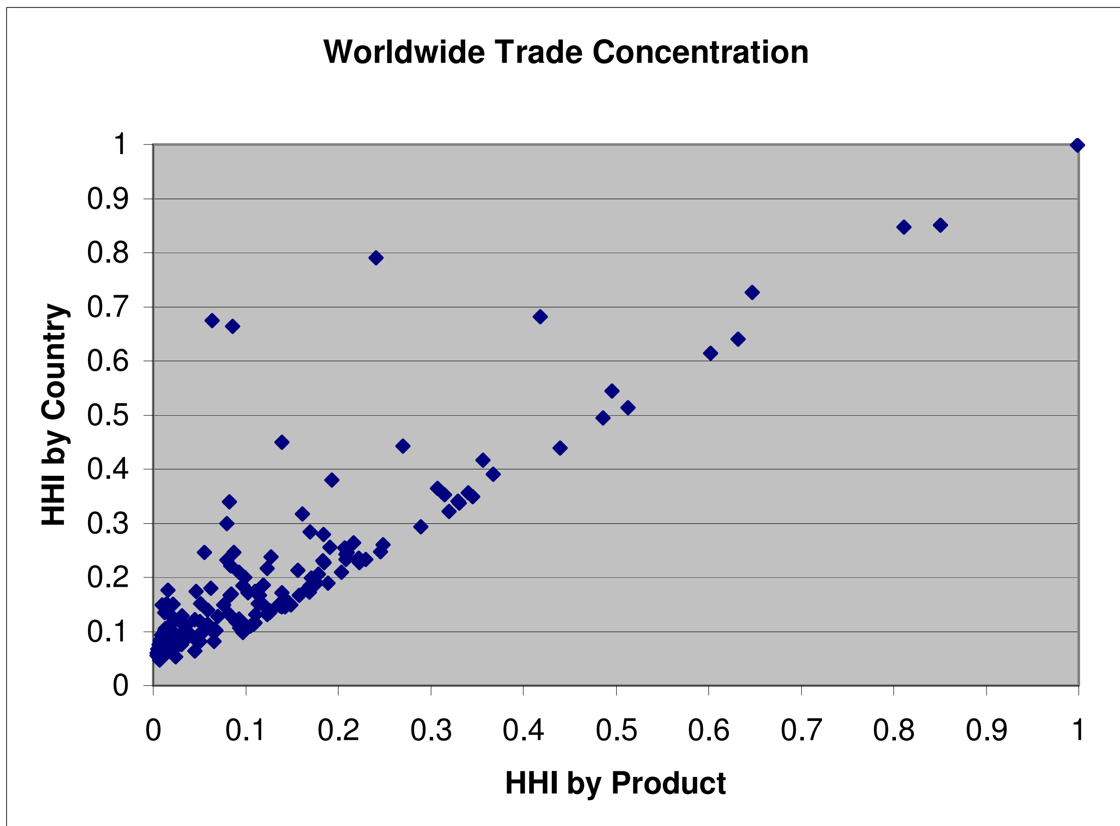


Table 1: Empirical Results: **<u>Regressions of Percentage Change in Import Penetration as a Function of Unemployment, Political Constraints and Concentration by Product & Country</u>**

	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)	(12)	(13)	(14)	(15)
N	2532	2532	1008	731	670	670	670	587	539	539	539	144	131	131	131
# Countries	149	149	96	58	51	51	51	44	41	41	41	26	22	22	22
R-squared	0.18	0.30	0.30	0.72	0.73	0.73	0.74	0.39	0.39	0.37	0.40	0.90	0.91	0.91	0.91
Sample	All	All	All	All	All	All	All	stable democ	stable democ	stable democ	stable democ	other countries	other countries	other countries	other countries
Concentration of Exports					-0.278		-0.672		-0.659		-1.219		-0.321		0.646
by Product					*0.123*		*0.013*		*0.036*		*0.000*		*0.127*		*0.347*
Concentration of Exports						-0.154	0.426			-0.150	0.565			-0.392	-1.068
by Country						*0.334*	*0.042*			*0.448*	*0.006*			*0.080*	*0.144*
Level of Import Penetration		-0.012	-0.012	-0.007	-0.008	-0.008	-0.008	-0.009	-0.010	-0.010	-0.010	-0.013	-0.015	-0.015	-0.015
		0.000	*0.000*	*0.000*	*0.000*	*0.000*	*0.000*	*0.000*	*0.000*	*0.000*	*0.000*	*0.000*	*0.000*	*0.000*	*0.000*
Political Constraints			0.001	-0.136	-0.141	-0.141	-0.141	-0.273	-0.187	-0.234	-0.146	-0.055	-0.137	-0.156	-0.170
			0.987	*0.014*	*0.038*	*0.040*	*0.034*	*0.000*	*0.026*	*0.007*	*0.081*	*0.628*	*0.238*	*0.186*	*0.157*
Unemployment Rate			-0.001	-0.005	-0.006	-0.014	-0.006	-0.023	-0.015	-0.019	-0.009	-0.001	-0.003	-0.003	-0.002
			0.858	*0.087*	*0.207*	*0.029*	*0.225*	*0.001*	*0.076*	*0.030*	*0.253*	*0.749*	*0.570*	*0.592*	*0.665*
Political Constraints X			0.001	0.012	0.014	0.014	0.013	0.034	0.025	0.031	0.018	-0.013	-0.010	-0.009	-0.008
Unemployment Rate			*0.877*	*0.007*	*0.032*	*0.032*	*0.037*	*0.000*	*0.030*	*0.011*	*0.107*	*0.235*	*0.430*	*0.505*	*0.519*
Real Effective Exchange				0.000	0.000	0.000	0.000	-0.001	-0.001	0.000	-0.001	0.000	0.000	0.000	0.000
Rate				*0.000*	*0.000*	*0.000*	*0.000*	*0.164*	*0.237*	*0.326*	*0.265*	*0.000*	*0.000*	*0.000*	*0.000*
Change in Real Effective				-0.031	-0.027	-0.030	-0.025	-0.102	0.083	-0.100	0.081	0.027	0.029	0.026	0.020
Exchange Rate				*0.450*	*0.500*	*0.466*	*0.523*	*0.117*	*0.221*	*0.146*	*0.224*	*0.586*	*0.557*	*0.593*	*0.685*
Change in Terms of Trade				0.721	0.625	0.590	0.623	0.626	0.723	0.546	0.712	1.247	1.329	1.293	1.235
				0.001	*0.010*	*0.016*	*0.009*	*0.007*	*0.011*	*0.052*	*0.010*	*0.004*	*0.021*	*0.023*	*0.032*
Gross Private Capital				0.001	0.001	0.001	0.001	0.001	0.000	0.000	0.001	-0.002	-0.002	-0.002	-0.002
Formation / GDP				*0.013*	*0.210*	*0.255*	*0.166*	*0.026*	*0.459*	*0.549*	*0.186*	*0.479*	*0.519*	*0.544*	*0.607*
Gross International				0.014	0.015	0.015	0.015	0.012	0.014	0.013	0.014	0.026	0.028	0.025	0.025
Reserves / Imports				*0.000*	*0.000*	*0.000*	*0.000*	*0.001*	*0.000*	*0.000*	*0.000*	*0.003*	*0.008*	*0.006*	*0.005*

Notes: P-values reported in italics under OLS coefficient estimates using panel-corrected standard errors.
Coefficient estimates on IGO, country and year indicator variables omitted for the sake of brevity

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