

INTEGRATION ALTERNATIVES FOR ARGENTINA: A GENERAL EQUILIBRIUM ANALYSIS

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EXECUTIVE SUMMARY

Argentina has an ambitious trade negotiations agenda for the coming years, both at the multilateral level (WTO) and the regional level (FTAA, MERCOSUR-EU, etc.).

In this paper an initial assessment is made of the economic impact of the concessions (on the part of Argentina and of the future partners) involved in such agreements. For this purpose, a Computable General Equilibrium (CGE) model is used, which reflects the interrelations between all economic sectors and identifies the winners and losers after trade liberalization.

The model used was developed at the Foreign Ministry's International Economy Centre (CEI), based on the Global Trade Analysis Project (GTAP) model. In the CEI version, the model adds nonstandard features, such as growing returns to scale in the manufacturing sectors, capital accumulation in the medium term and a positive relationship between trade openness and the productivity of the factors involved. In order to make the model operational (calibration), the latest GTAP database version is used.

With a deliberate focus on the negotiations agenda of Argentina, five trade integration scenarios were simulated: (i) Free Trade Area of the Americas (FTAA), (ii) A free trade agreement between the countries of MERCOSUR and the European Union, (iii) A combination of (i) and (ii) above, (iv) A free trade agreement between the countries of MERCOSUR and the United States (4 + 1) and v) Free world trade. In general terms, these agreements are simulated by setting bilateral tariff rates at zero. Accordingly, the simulated scenarios are the upper limit of the results that could be obtained from the simulated trade liberalization agreements.

The simulations use a GTAP data base aggregation of sixteen sectors and ten regions. This enables the

detection of the main aggregate, sectorial effects and the trade patterns of the trade integration scenarios.

At the aggregate level, all simulated trade integration agreements are beneficial to Argentina. The order of the five scenarios according to their effect on real GDP is as follows: FTAA + MERCOSUR-EU, Free World Trade, MERCOSUR + EU, FTAA and, finally, 4 + 1. Real GDP increases in each scenario amount to 7.2%, 5.6%, 4.3%, 3.5% and 2.6% respectively.

This shows that the "multipolar" strategy is the one providing the greatest wealth among the alternatives considered. Simultaneous negotiations with the FTAA and the European Union even surpass the benefits that would derive from free world trade (which would be explained by the preferential access to be gained to these markets).

This also shows that any additional opening is in the interest of our country: even 4 + 1, which is the least advantageous of the alternatives analyzed, offers increased wealth compared to the initial situation.

A comparison between the results of the FTAA and 4 + 1 shows that our country would also benefit from a greater integration with Latin America.

It can also be seen that in any scenario, but particularly in the FTAA and 4 + 1, the loss of preferential access to the Brazilian market is very significant for our country, which confirms that MERCOSUR is the most appropriate platform for Argentina's international integration.

In trade terms, none of the scenarios considered offers significant trade balance changes, but they do in terms of exchange volumes. The greatest increase is found in the free world trade scenario, in which exports grow by 28.5%, followed by FTAA + MERCOSUR-EU, in which external sales increase by 27%. The remaining scenarios are arranged in the same order as

in the previous case: exports grow by 16% under the MERCOSUR + EU agreement, 14% under the FTAA and 9% in the 4 + 1 scenario.


In terms of the different sectors, *Primary Sectors* and *Light Manufactures* emerge as the most favoured sectors of trade liberalization in any of the scenarios outlined (with average growth of 4.5% and 6% respectively), whereas the production of *Heavy Manufactures* does not experience major alterations in any case (with a slight growth under FTAA + MERCOSUR-EU, under the FTAA and under 4 + 1 and a slight decline under MERCOSUR + EU and free world trade). Prominent among the former are *Vegetables and Fruits and Oilseeds*; among the latter, *Meat Products and Food Processing and Textiles and Clothing*, whereas in the case of *Heavy Manufactures*, the *Petrochemical Industry* and *Metal Products*, sectors stand out.

Worthy of mention is the case of *Primary Sectors*, with increasing production in all scenarios but with falling export levels in the scenarios of MERCOSUR + EU (-5.7%), FTAA + MERCOSUR-EU (-4.7%) and free world trade (-25%). This is explained by the convenience of processing all raw materials in the country and then exporting them with higher added

value: external sales of light manufactures grow by 60%, 82% and 93% respectively in the three scenarios.


The importance for Argentina of preferential access to the Brazilian market is evident in the case of *Heavy Manufactures*. The two sectors that would face the greatest difficulties in redirecting their exports are *Vehicles and (Spare)-parts and Machinery and equipment*, due to the fact that, in all scenarios analyzed, the drop in sales to the Brazilian market is not offset by increased sales to other destinations.

Finally, although it may seem obvious, it is interesting to assess the changes in Argentine trade patterns in the different scenarios considered: Brazil systematically loses importance, and absorbs 14% of Argentine sales in the case of free world trade (down from the initial 31%) and 18% under the simultaneous FTAA + MERCOSUR-EU agreement. The US accounts for 15% of our markets under 4 + 1 (up from the initial 8%) with the European Union accounts for 32% under MERCOSUR-EU (up from the initial 16%). In all cases, Argentina would achieve more diversification in its export destinations, with consequently lower macroeconomic vulnerability (lower risk of contagion through the trade channel).



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