

Introduction

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1 The New Protectionism and Latin America

Latin American countries are liberalizing their trade, following a long period in which the preferred path to development was based on import substitution. Along the way, these countries have discovered that the rules of international trade are not as transparent as they appear in textbooks. There are multifarious mechanisms, denoted collectively as The New Faces of Protectionism, which prevent Latin American countries from gaining secure access to foreign markets, despite the fact that they face low tariffs for most of their exports.

Between 1945 and 1970, trade among developed countries was progressively liberalized, largely through multilateral agreements to reduce tariffs. The success of these agreements was so complete that developed countries have set near-zero tariffs on the majority of the products they import, especially from other developed countries. In fact, average tariffs in these countries have come down from 40 per cent in 1947 to 4 per cent in 1994 (Staiger 1995). This experience stands in contrast to that of Latin American countries which, encouraged by ECLAC (Economic Commission for Latin America and the Caribbean), embarked on a heterodox development strategy based on import substitution and did not involve themselves in the negotiations to liberalize trade. The shift in economic focus which began in Chile at the end of the 1970s led to a reassessment of trade in Latin America. By that time, however, the liberalizing thrust in developed countries had declined, and the impediments to trade which are the subject of this book became relevant.

The new protectionism differs from classical forms of protectionism such as tariffs and quotas. It consists of measures such as minimum quality standards, ecological dumping allegations, threats of anti-dumping

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and anti-subsidy measures, phytosanitary restrictions and technical barriers to trade. In view of the growing importance of these forms of protection, we must develop new tools of analysis in order to understand their effects and to limit the damage to the trade of countries engaged in the trade liberalization process. The purpose of this book is to analyze these new forms of protection from two points of view: first, via theoretical studies of contingent protection and of the protectionist use of minimum quality standards; and, second, through five case studies of sectors affected by such measures in a small open country. The case studies refer to the Chilean economy, but the lessons are applicable to the other Latin American which have followed the trend towards openness and exports.

There are good reasons to believe that the new forms of protection may seriously affect the development of a small open economy's exports. As an example, in recent years the Chilean economy has been affected by measures which include:

1. A new law governing the recycling of packaging materials (the Töpfer Law in Germany) making it prohibitive to export fresh fruit packed in wooden boxes. The consequence was a significant increase in the costs of fruit exports and the bankruptcy of firms involved in box manufacture.
2. An unilateral ban on Chilean fruit exports to the United States, because of the discovery of two grapes supposedly contaminated with cyanide.
3. Allegations of dumping and phytosanitary problems in fishmeal exports to Mexico, a country with which Chile had recently signed a free trade agreement.
4. A potential dumping allegation affecting salmon exports to the United States; salmon being one of the biggest growth industries of recent years.
5. Difficulties in exporting wooden moldings to Canada because the standards of that country require them to be made of a single piece of wood; whereas in Chile moldings are assembled out of shorter pieces.

The new protectionism has led to the most recent multilateral negotiating rounds concentrating less on lowering tariffs and more on reducing these new trade barriers. This was already evident in the Tokyo

Round of the GATT (General Agreement on Tariffs and Trade) which ended in 1979, which was the first round that attempted to make progress in this field. However, eliminating non-tariff barriers has proved to be considerably more difficult than expected. Unlike the simple goal of lowering tariffs, today's negotiators face a host of protectionist tools which are difficult to classify and quantify.

1.1 Standards with protectionist effects

From their beginnings in 1947, the initial GATT agreements established that standards and norms should not be used with a protectionist intent.¹ The original GATT agreements proved unable to prevent the use of protectionist standards, since they lacked effective mechanisms to ascertain whether a country was breaking the rules. Furthermore, it was argued that the setting of standards was the prerogative of each country, and that to restrict their use infringed national sovereignty.

In some cases –for example trade restrictions based on the use of standards (quality, phytosanitary, environmental and technical standards)– it is difficult to distinguish between legitimate domestic policy decisions and those that conceal protectionist aims. Is it acceptable, for example, for the United States to impose a measure that supposedly protects dolphins, but which puts foreign competitors in the tuna market at a disadvantage? Is it legitimate for the United States to criticize Japan's competition policy and accuse it of being protectionist? Given that such measures enjoy support both from the import substituting firms as well as from organized interest groups (environmentalists, for example), it is politically difficult for governments to avoid using them. The GATT Uruguay Round tried to establish rules to regulate this protectionist behavior, going beyond those established in previous rounds. Membership in the new World Trade Organization (WTO), GATT's successor, is open only to countries that are signatories of the expanded GATT agreed in the Uruguay Round and a series of additional requirements.² However, the effectiveness of the new agreements will only be known when jurisprudence is accumulated under the new rules. The examples that follow show the universal use of standards in protection.

1.1.1 The case of hormones in meat

In 1989 the European Union (EU) banned the sale of meat and side-products produced with natural or synthetic hormones. On the basis of GATT rules, the United States alleged that there was no internationally recognized scientific evidence to show that treatment with growth hormones is harmful. In response to the exclusion of exports worth an estimated US\$ 97 million, the US imposed tariffs equivalent to this amount on products coming from the European Union, and tried unsuccessfully, to get a GATT panel to resolve the case (National Research Council 1995). Recently, the WTO panel ruled in favor of the US, allowing the US to suspend concessions (i.e. raise tariffs) on US\$117MM of imports from the European Union.

1.1.2 The case of automobile efficiency standards (CAFE)

In 1975 the US introduced legislation designed to increase car fuel efficiency, the CAFE (Corporate Average Fuel Efficiency Standards), setting minimum standards of fuel economy for automobiles. CAFE penalized car companies whose average fleet (i.e. cars sold in a year) fell below a certain standard. The efficiency standard, currently 27.5 miles per gallon, implies that a vehicle manufacturer has to pay a US\$ 50 fine for each mile per gallon under the standard, on each vehicle sold.³ This type of standard penalizes foreign manufacturers specializing in luxury vehicles, whose average efficiency is worse than the norm. On the other hand, North American manufacturers can compensate for the high fuel consumption of their expensive cars with sales of small cars, thereby increasing average efficiency. The EEC (European Economic Community) filed a complaint with a GATT arbitration panel. The EEC argued that a tax based on the fuel efficiency of each automobile model or, alternatively, a gas tax was the best way of increasing efficiency. The US, for its part, argued on formal grounds that the measures were not discriminatory and that, in any case, they were within their rights according to GATT Article XX (dealing with the conservation of natural resources). The panel found in favor of the EEC but only on the basis of a technicality. It recommended that the US make the necessary changes to avoid discriminating between automobiles produced by the same company but it accepted the United States' argument regarding the use of averages, which was the fundamental point in discussion.

1.1.3 Argentine meat and hoof-and-mouth disease

Over the last two decades Chile has managed to eradicate a series of agricultural plagues, such as hoof-and-mouth disease and the fruit fly, and this has enabled Chilean agricultural products to be exported to countries which impose strict sanitary standards. In most cases, the elimination of plagues has been beneficial for the country, but there are some cases where the attempt to exterminate a plague may be interpreted as a protectionist measure. Consider the eradication of hoof-and-mouth disease, to which Chile has devoted significant resources, mainly due to the fact that foot-and-mouth disease was endemic in Argentina.⁴ The declared aim of the policy was to eliminate hoof-and-mouth disease to allow Chile to export beef. However, during the long period in which this policy has been in force, Chile has exported only small amounts of meat. This is understandable, for Chile is a country which has no comparative advantages in beef production. However, the policy managed to reduce meat imports from Argentina, as it prevented imports of cattle on the hoof due to phytosanitary restrictions. Only in recent years has it been possible to import vacuum-wrapped off-the-bone beef from Argentina, and this has given rise to numerous complaints from Chilean beef producers. Thus, the effort to eliminate hoof-and-mouth disease can also be seen as a mechanism for suppressing imports of Argentine beef. Furthermore, Chile has recently introduced a non-standard method for grading meat, causing argentinian (and US) beef producers to complain that it represents a technical barrier to trade.⁵

1.2 Contingent protection

Contingent protection is another difficult problem that has been discussed in the GATT negotiating rounds. The distinguishing feature about anti-subsidy and anti-dumping measures (as well as similar measures such as safeguard clauses imposed when imports grow too fast), is that they threaten exports even when not in force; hence the term contingent protection. The effect of contingent protection is due to the implicit threat of punishment, unless the foreign exporter behaves more “cooperatively” with the domestic industry. The mere existence of anti-dumping measures changes the environment faced by an exporting firm, as it is threatened with the possibility of punishment if the importing country decides to carry out an investigation, which in general occurs at the petition of domestic competitors. One of the big achievements of the Tokyo

Round was to establish codes which set rules for the design of national anti-subsidy (countervailing duties) and anti-dumping legislation. However, attempts to restrict the abuse of contingent protection by bringing it under a GATT jurisdiction code have not been completely satisfactory (Marceau 1994), despite the fact that the recent Uruguay Round has managed to limit abuses in the administration of the codes in some countries. For example, until the Uruguay Round, the United States used a series of administrative laws which biased the results in favor of declaring dumping (Boltuck and Litan 1991). After this negotiating round, the US agreed to modify its rules to reduce such biases. However, following complaints by the traditional users of anti-dumping legislation, it was decided to weaken the new standards by introducing exceptions as well as other changes which reproduce the protectionist characteristics of traditional US antidumping legislation (Palmer 1995)

1.2.1 The use of anti-dumping legislation

Anti-dumping measures are especially appropriate for protectionist purposes. By *dumping* we mean price discrimination between countries or, alternatively, the practice of selling in export markets at a price below cost. The difference between the two prices⁶ is known as the margin of dumping, and when this margin is positive the foreign firm is said to be engaged in dumping. From a theoretical point of view, anti-dumping regulation is redundant. Indeed, on paper, its goal is to prevent predatory competition from abroad, which does not require a special law but only the extension of national anti-monopoly legislation to cover competition with foreign countries. However, as many authors have insisted (Prusa and Hansen 1993; Staiger and Wolak 1994), the more elastic nature of anti-dumping legislation makes it possible to exercise protectionism in sectors facing greater international competition due to the tariff reductions arising from multilateral agreements.

In the period 1980-1988, the US, the main user of these measures, instigated 411 anti-dumping actions, of which 147 resulted in a favorable outcome, 108 were withdrawn by their proponents, while the remainder were rejected.⁷ According to the GATT anti-dumping code, after initiating an investigation, three circumstances have to be demonstrated before dumping can be punished. Firstly, it has to be shown that dumping is actually taking place, i.e. that there is price discrimination between countries.⁸ After showing the existence

of a positive dumping margin, the regulator has to show that the industry has suffered *material damage*⁹, in other words, a substantial damage. Finally, it must be shown that dumping is responsible for the damage. If these conditions are fulfilled, the code authorizes the importing country to impose a surcharge high enough to eliminate the margin of dumping. Alternatively, the exporter can make a commitment to raise its prices (known as a price undertaking).

In the US, in order to avoid political pressures the procedure to determine whether dumping or material damage is occurring is administrative.¹⁰ However, the US Congress has modified the administrative procedures and introduced a bias towards declaring the existence of dumping even when this does not exist. In addition to the protectionist effects of punishment, mere investigation has a significant effect on exporters. Staiger and Wolak (1994), have suggested that this is due not only to the fact that the legislation allows retroactive measures, but that in addition the investigative process itself has protectionist effects, and this is one of the reasons for their existence. This is the type of reaction that gives rise to the theory of Contingent Protection (Fischer 1987; Fischer 1992; Reitzes 1993; Prusa 1994).

2 Theoretical Aspects

This book is divided into two parts. The theoretical section of this book explores both forms of protection: those based on the threat of future punishment and those based on the use of quality standards or norms. The second section begins with an overview of the reforms in trade policy in Latin America, their effects and the threat posed by the new forms of protection. The main body of the second section treats five case studies of the effects of these new forms of protection in Chile.

2.1 Contingent Protection

This chapter carries out a theoretical analysis of contingent protection in a simplified setting designed to highlight the main features of this type of protection. Two firms, one in the exporting country and another in the importing country, compete in the importing country's market. The competition faced by the domestic firm lowers its profit. Contingent protection is a mechanism which threatens sanctions whose probability

depends on the observable behavior of the foreign firm. This signal might be the margin of dumping or the extent of market penetration by the foreign firm. A higher value of the signal increases the likelihood of punishment. For example, a bigger margin of dumping makes both detection and punishment of the foreign firm more likely. Moreover, the sanction on the foreign firm may depend on the value of the signal. In general, the observed value of the signal depends on the actions of the two firms. Hence, the domestic firm might choose to modify its behavior so as to increase the probability of a punishment for the foreign rival. The setup is that of a dynamic game, as both firms realize that their present actions affect the likelihood of a future sanction on the foreign firm (anti-dumping measure, anti- subsidy tariff, etc.). The chapter describes the firms' strategic reactions under contingent protection and shows that the effects depend on the type of competition between the firms as well as on the type of punishment. In the case of dumping, the foreign firm tries to reduce the likelihood of punishment, and this means lowering the margin of dumping, i.e., lowering prices in its own market and trying to raise prices in the foreign market. This means that under quantity competition, the foreign firm reduces exports. The domestic firm, meanwhile, will try to raise the probability of a punishment by increasing its sales, which will tend to raise the margin of dumping. The end result is that in the first period, i.e., prior to the possible punishment, total sales are higher and imports are lower. In this particular example, for small punishments, consumers in both countries benefit from AD legislation during the first period. The results of this model correspond quite well to the observed behavior of the salmon industry in Chile, which was recently threatened by a dumping investigation in the United States. In this case, the reactions of the Chilean firms have been as follows:

1. Attempts to raise the price in the export market (price undertaking), a strategy that often leads to a suspension of the investigation.
2. Lowering the price in other markets so as to reduce the margin of dumping.
3. Cutting back exports and directing surpluses towards alternative markets.
4. Lobbying to try to influence the results of the investigation.¹¹

The preliminary determination in the case of Chilean salmon exports has found that two out of five firms are dumping, with margins of 2.9 per cent and 5.6 per cent respectively.

2.2 Protection and Standards

In this chapter, Ronald Fischer and Pablo Serra examine the use of quality standards as protectionist measures. The authors consider two different models of standards. In the first model, quality enhancements reduce a negative externality: for example, the standards governing the pollutants produced by automobiles. It is assumed that the quality enhancement does not affect directly the utility perceived by consumers.¹² To underline the importance of standards as barriers to trade, note that three of the cases studies that follow document protection based on standards. Unlike most other protectionist measures, standards serve, in principle, to correct for externalities. Accordingly, there is a theoretical justification for their use. However, it is difficult to distinguish a protectionist standard from one that is set at the level that corrects an externality. There are two reasons why a country might impose a protectionist standard. In the first place, it may serve to raise relative costs for foreign producers, thereby enabling rents to be transferred to national firms. Secondly, it is easier to raise standards if the costs can be transferred to foreign producers.¹³

It follows, therefore, that it is natural to define a protectionist standard as one that is higher than the standard the country would impose if all firms were domestic. On the basis of this definition, it is shown that the quality standard chosen by a social planner maximizing domestic social welfare is always protectionist. This chapter suggests that the relative size of the domestic and foreign markets will influence the definition of the standard that is eventually imposed. When the foreign competitor's own market is small, the domestic producer knows that a high standard is needed to eliminate the foreign firm from its only important market. In this case the costs of eliminating the foreign firm are high, and the domestic firm may prefer not to press for a minimum quality standard that excludes the foreign firm. The reason is that the profits under monopoly may be less than under duopoly, due to the higher cost of the standards needed to eliminate the foreign firm. On the other hand, if the foreign market is large, the costs of raising quality in order to adapt to the domestic standard are high for the foreign firm. Hence the foreign firm may abandon its export market even when the standard required of exports is relatively low. In this case, the domestic firm lobbies for the lowest standard that excludes imports.¹⁴ The chapter also analyzes the standard desired by the social planner which, it is shown, may be higher or lower than the standard desired by the domestic firm.

The second model analyzes the case where standards are used to reduce an informational asymmetry:

consumers do not know the quality of the goods they consume. In this case, standards are required in order to exclude units of the good whose value to consumers is less than the cost of production. Using a simple specification in which a higher quality of a good indicates that the useful component of the good is a larger fraction of each unit sold, the authors show that consumers would prefer lower standards than those preferred by producers. A social welfare maximizing planner would set a standard that is excessively lax from the point of view of both foreign and domestic firms. Firms would prefer the planner to restrict the amount of goods closer to the monopoly quantity. In this case, the planner is not protectionist, since it harms domestic firms. The situation is different when the average quality of imports is lower than that of domestic production (for all minimum standards) and consumers cannot identify foreign goods. In that case, a welfare maximizing planner would choose a higher standard that favors domestic firms at the expense of foreign firms: i.e. it would be a protectionist standard. However, this source of protectionism (which is due to the unobservability of the country of origin of the goods) can be readily eradicated by requiring labels on the goods that indicate the country of origin of the goods, a universal procedure. Hence, the only explanation for a protectionist standard is due to the pressure of domestic producers at the expense of domestic welfare.

3 The New Protectionism in Practice

What are the practical effects of the new forms of protectionism? The second part of the book presents a series of case studies that examine the effects on different sectors. An introductory section provides a description of the changes in the approach to trade in Latin America in the last decade.

3.1 Latin American Trade Regime: Reforms and Perceptions

In this section, Ronald Fischer and Patricio Meller examine Latin American countries and the effects of the reforms that have taken place recently. In general, these countries have changed from the inward oriented economic attitude sponsored by the United Nations Economic Commission for Latin America (ECLAC), towards an outward looking perspective that is part of the “Washington Consensus”. The paper details the changes in the level of tariffs and in quantitative restrictions, showing that there is a clear divide between the

80s and the 90s, with recent tariff structures that are flatter and lower. The authors document an explosion in Free Trade Agreements (FTAs) within Latin America. Even if these agreements are not always effective and are riddled with excluded goods and services, they represent a change in perceptions that indicates a willingness to trade with neighbors that did not exist previously.¹⁵ The effect has been a doubling in the rate of growth of exports in the last decade, coupled with an especially high growth rate in intra-LA trade. Cross-border investments have also become common. Nevertheless, the amounts exported by these countries are small. Even a country with low, uniform tariffs and few other forms of protection, such as Chile, did not get to export one thousand dollars of exports per capita, a quarter of the corresponding value for OECD countries.

A worrying trend for the area is the growth in the new forms of protection as traditional trade barriers are lowered. A survey of the major Latin American countries and their trade partners shows an increase in the use of sophisticated methods such as the use of standards, certification procedures and antidumping and anti-subsidy measures against other countries in Latin America. Moreover, there is a willingness to fall back on administrative protection with measures that are cumbersome and protectionist. Even countries that are members of a customs union, such as MERCOSUR, can indulge in costly trade wars using these instruments. Developed countries have also stepped up their use of these measures and they appear less enthusiastic in their support of free trade. It would be ironic if, when LA countries finally start to believe in the benefits of free trade, the developed countries were to close the door on their imports.

3.2 Poisoned Grapes, Mad Cows and Protectionism

In his chapter, Eduardo Engel examines the different reactions of importing countries in two occasions where imported products were suspected of being contaminated and hence presented a potential health risk. His aim is to put forward a new definition of a protectionist measure via two case studies. Engel proposes defining as protectionist any measure that reduces world welfare.

Firstly, Engel studies the well known case of a shipment of Chilean grapes in which two grapes were found to be contaminated with a non-lethal dose of cyanide on arrival in the United States. As a consequence, the Food and Drug Administration (FDA) banned the entry of all Chilean fruit exports to the US.

The losses to Chilean agriculture were estimated at US\$ 300 million. Subsequent investigations have shown that the grapes must have been contaminated on arrival in the US. Despite many attempts to obtain compensation, the US government has refused. Engel contrasts this response to the case of “mad cows”. The countries of the European Union (EU) tried to prevent British beef entering the rest of the continent, fearing it might be contaminated with bovine encefalopathy (mad cow disease), a disease which was suspected of being transmissible to human beings. Despite a real health risk, in contrast to the Chilean case, the EU offered to compensate the United Kingdom for up to 70 per cent of the costs of destroying the contaminated herds. Notwithstanding this fairly generous compensation, the United Kingdom boycotted EU meetings and prevented important decisions being taken, until the other countries in the EU accepted a limited culling plan rather than the original proposal. The comparison between the two cases enables Engel to compare different definitions of a protectionist standard. If one considers world welfare, the ban on British beef is not protectionist. In the case of the Chilean grapes, it is difficult to believe that the embargo maximized global welfare, which means that it might have a protectionist component. Engel concludes, firstly, that incentives are required so that regulators in the importing country internalize the cost of their decisions on the exporting country; and, secondly, that speedy consultation procedures need to be set up to prevent worsening the problems caused by import bans on phytosanitary grounds. Engel’s analysis is important because the Chilean case highlights that food exporting developing countries are vulnerable to unilateral embargoes at any time. Hence the multilateral trading organizations must establish clear rules for the exclusion of products and create compensation mechanisms and rapid response procedures.

3.3 Trade and the Environment: Mining.

The chapter by Raúl O’Ryan and Andrés Ulloa examines the effects of allegations of environmental dumping on Chile’s mining industry (mainly copper). Environmental dumping is defined as the ability of firms to set lower prices when looser environmental standards in the country reduce production costs relative to other countries. The chapter begins with a detailed exposition of the arguments for and against the use of trade measures to correct environmental externalities in exporting countries. Next, it analyzes the validity of the arguments for setting up a new type of trade impediment to punish environmental dumping. The

authors conclude that unless the externality spills over to other countries, it is difficult to justify the use of environmental production standards. They also argue that optimal environmental standards depend on the specific location, for it is not a matter of indifference whether a mine contaminates an inhabited, agricultural area or an uninhabited desert. However, they note that the effect of the threats of environmental dumping on Chilean mining do not depend on the fairness of the arguments, since Chile cannot influence the internal decisions of consumer countries. In response to the potential threat, the state mining company is implementing a decontamination plan which will invest more than US\$1 billion between 1997 and 2000 in sulfuric acid plants, tailing treatments, filters and other items. Private mining companies, for their part, have already installed low-pollution technology. The effect of all these investments is that within a few years, Chile will produce twice as much as in 1994 copper with less pollution.

However, environmental threats to Chile's copper exports persist: the possibly unsustainable use of subterranean waters in fossil beds by mines in Northern Chile could form the basis for new arguments to restrict the entry of Chilean copper. Worse still, new ISO 14,000 environmental standards regulating the entire life cycle of the final product could restrict exports to markets which traditionally have not used environmental arguments to restrict imports, such as those in Asia. Under the new norms, all components of the final product have to have been produced under ISO 14,000 standards. This will force Asian countries wishing to export to countries implementing ISO 14,000 standards to impose the standards on their own inputs. Finally, the study also considers the possibility that copper may be declared a health risk in uses such as roofing, water pipes, and others.

3.4 Trade and the Environment: Forestry

This chapter studies the effects of environmental considerations on the development and trade in one of Chile's most dynamic growth sectors in the last twenty years: the forestry sector. Without forgetting the issues of pollution already covered in the case of mining, it concentrates on a different issue, namely, the fact that environmental activism has fundamentalist aspects that make it ignore scientific considerations, in its desire to stop the exploitation of native forests. The authors believe that in some cases environmentalist motives have been hijacked by protectionist interests. They point out that cellulose producers in Scandinavian

countries have developed clean technologies and then have joined lobbies against cellulose imports from less clean producers, usually from developing countries. In an effort to contain these threats, developing country firms have had to adopt standards that are higher than those that are efficient (even if environmental effects are included), raising costs and making them less competitive.

The authors argue that even though effective environmental protection of forests is fairly new in Chile, most of the industrial raw materials for the forestry industry originates in plantations grown in highly eroded non-forested lands. Moreover, plantations reduce the pressure on native forests. Hence, rather than being harmful, this plantations have a favorable effect on the environment. The threats of environmental protection have had the perverse effect of lowering the investment in plantations and reducing the interest of large corporations in investigating sustainable use of native forests. The authors show that the arguments about the disappearance of native forests in Chile are misguided on average (though there may be localized problems), since the native biomass is growing at least at a rate four times higher than the rate of extraction. The costs of the protectionist threats facing Chilean exporters are large and according to the authors, they do not even achieve the effect that is sought, namely, the protection of native forests.

3.5 Protection and Labor Standards

In this chapter, Alejandra Mizala and Pilar Romaguera examine the possibility that differences in labor standards be used as threats to trade. To this end, they consider whether Chile should modify its labor standards in the event of being invited to join NAFTA (North American Free Trade Agreement), given the possibility that the changes have an efficiency cost. After a comparative review of labor legislation, the authors find that at the formal level, Chilean labor legislation is on a par with that of the United States and Canada, so is not necessary to introduce significant modifications. However, they warn that, under the side agreements on labor required in NAFTA, countries need to ensure compliance with their own labor laws. Mizala and Romaguera argue that Chile lags behind in compliance: there are sectors where supervision of labor legislation is precarious. This is especially serious, given the context of these agreements, in the export sector. This chapter examines the problems in four major Chilean export sectors: forestry, mining, salmon production, and fruit. The first conclusion is that there are enormous differences in compliance with

the norms between firms and subcontractors, for which reason the authors propose legislation be modified to make firms responsible for the labor problems (especially safety) of their contractors. Secondly, they find that the sectors with the biggest problems are those that are furthest away from population centers and least accessible, hence poorly supervised: forestry camps and salmon farm rafts, for example. The authors point out that this is an area where Chilean unions have made alliances with their counterparts in Canada and United States, so that negotiators in these countries sometimes have information on labor legislation infringements which their Chilean counterparts themselves do not know about.

3.6 Investment Risk and Latin American Multinationals

In this chapter Jorge Friedman looks at foreign direct investment carried out by Chilean firms, and the problems they have faced. The chapter's first contribution is to show the surprising importance of Chilean foreign investment, which as a percentage of national product exceeds that of several developed countries. The chapter analyzes the reasons why Chilean capital has been almost wholly invested in neighboring countries. According to Friedman, early liberalization and privatization in the Chilean economy provided Chilean entrepreneurs with know-how concerning the operation of Latin American economies in the process of liberalization. This know-how gave them a comparative advantage compared with entrepreneurs in countries in the initial stages of liberalization, and also with respect to foreign firms ignorant of the particular characteristics of the region's economies. Much of Chilean investment has been directed at the electrical sector, where regulatory systems similar to Chile's have been adopted in Argentina and Peru. This system of electricity regulation is more modern than those established in most developed countries (apart from the United Kingdom), which has given Chilean electrical companies an additional advantage in competing for electrical companies undergoing privatization. Other sectors that have received significant investment are supermarket chains, forestry products, private pension funds, banks, wine makers, and health insurance companies. Friedman notes that Chilean investors have chosen to ally themselves with developed country firms, so as to have stronger support in the face of nationalistic threats. These threats are one of the most important problems facing Chilean investments in neighboring countries, and it has become a threat to their expansion. Friedman examines a series of instances where various threats such as the possibility of changes in the rules

of the game, discrimination against foreign investors, violation of agreements, and direct attacks on Chilean staff in foreign firms have tended to slow the pace of investment. These threats have a negative effect on the external investments of Chile (a country without great influence in the region), and are equivalent to the effect of contingent protection on trade.

4 Final Comments

The papers collected in this volume suggest that the new forms of protectionism may be even more effective in distorting trade than traditional measures such as tariffs and quotas. As this is an emerging issue, the technocrats in charge of developing country's negotiations do not have experience in these issues and, needless to say, the new protectionism is not taught in international trade courses. However, they involve issues that need to be understood in order to reach sustainable international agreements and in order to design responses that anticipate these new threats to trade. There is, as yet, no general theoretical framework that would allow us to determine what are the desirable results of international negotiation on these subjects and that would allow us to compare it to potentially achievable results in trade treaties or multilateral negotiations. This book is an attempt at analyzing these issues by combining a theoretical framework with the experience of cases in which these new forms of protection are important for developing countries.

Notes

1 Notwithstanding this restriction, the initial round of GATT in 1947 established that norms and regulations could be used to “order” a market, a loophole which allowed the infamous marketing orders which have prevented, for example, the entry of Chilean grapes during harvest periods in the United States.

2 These include the: Technical Barriers to Trade Agreement (TBT, the Standards Code), which disciplines the abuse of technical regulations related, even indirectly, to trade; the Sanitary and Phytosanitary Agreement, which controls the use of sanitary and phytosanitary measures that affect trade; and finally, the Anti-dumping and Countervailing Subsidy Codes, which constrain national laws dealing with dumping and export subsidies.

3 For example, if company A had an average efficiency of 25 miles per gallon, it would pay a sum of US\$ 125 ($2.5 \times \text{US\$ } 50$) per vehicle sold. If the average efficiency was above the standard it would not pay a tax, nor would it earn a reward.

4 Argentina shares several thousand kilometers of thinly populated frontier with Chile. Periodically smuggled cattle infect Chilean herds. When this happens all cattle in a large neighborhood must be destroyed in order to contain the disease.

5 Despite the protectionist consequences, the elimination of hoof-and-mouth disease has probably generated unintended positive externalities for Chile. Importing countries are more willing to relax their phytosanitary requirements given that Chile has managed to eliminate an endemic disease of a neighboring country, thereby increasing their confidence in phytosanitary mechanisms in Chile.

6 For example, between the domestic and the export price.

7 In most of the cases that were withdrawn, the accused firms reached an agreement with domestic firms to raise their prices, i.e. they agreed to be less competitive.

8 In general the margin of dumping is positive if export prices are lower than prices in the country of origin. Another possibility is to compare prices with those in other export markets or with a constructed cost figure.

9 “Harm that is not inconsequential, immaterial or unimportant”, *Trade Agreements Act*, 1979, an uncommonly vague definition.

10 In the EU, the process is less administrative, and for that very reason more subject to pressures. The procedure in Chile is similar to the European one.

11 The Chilean salmon exporters association hired a lobby group headed by Robert Dole, Republican presidential candidate in 1996.

12 As in the case of car emission standards. This is an important restriction of the model that avoids quality issues that are usually analyzed in the Industrial Organization literature on standards.

13 This argument arose from an observation by Eduardo Engel.

14 The model assumes that producing under two different quality standards has a high cost, or alternatively, that there is an important fixed cost attached to each variety. In both cases, only one standard is actually produced. Fischer and Serra (in press) treat the more complex case in which both standards can be produced simultaneously.

15 As is well known, FTAs do not imply an unambiguous trend towards multilateral free trade.

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