The prospects for a Latin American common market

by Mark Sonnenblick and Peter Rush

In his August 1982 book *Operation Juárez, EIR* founder Lyndon H. LaRouche argued for the formation of an Ibero-American common market and a joint continental renegotiation of its foreign debt.

These measures, LaRouche argued, are required under *any* international environment. If the United States and the other OECD nations come to their senses and reverse their present suicidal course of confrontation with LDC development and agree to a favorable debt renegotiation, the Ibero-American common market would coordinate a quantitative and qualitative jump in the development process of every country in the market. If not, it provides the only feasible method for nations to successfully resist the threats to the very existence of their societies and their sovereignty now being leveled against them by means of the international financial system.

EIR is currently preparing a detailed econometric analysis of such a proposed Common Market, with use of the LaRouche-Riemann model. The following draft was prepared as a summary overview of the subject to guide the full study. It first reviews the general trade picture of the major countries in the region, to see their degree of potential self-sufficiency in major commodity areas, and then examines the ability of the continent to respond to several scenarios of differing degrees of economic conflict—including a possible generalized cut-off of imported items.

When the Latin American Free Trade Association expired in 1981, intra-zonal trade was only 15 percent of the total trade of the countries in the area. But this low figure does not accurately portray the region's true potential for self-sufficiency. A preliminary assessment suggests that the region currently has in place the productive capacity needed for supplying from within the region on the order of 80 percent of all current imports and over 95 percent of total consumption.

That does not solve all supply problems, and there are some real vulnerabilities to potential economic warfare. But regional economic security *can* be defended, largely because governments like that of Brazil during the past decade have made the huge investments needed to achieve self-sufficiency in all but the very highest technologies.

Energy

Unlike Japan, Western Europe, and the United States, Ibero-America has zero vulnerability in energy. Its crude oil production peaked in 1979 at 5.5 million bpd, while consumption of oil products was only 4.4 million barrels per day in the same year. Venezuela has installed capacity to increase its pumping by perhaps over 1 million bpd almost instantly, and Mexico could increase pumping by 1 million bpd fairly quickly. Only the smallest countries currently lack adequate refinery capacity, and Brazil itself has refinery capacity almost double what it is currently using.

The region is fully self-sufficient in steam coal and other energy sources, except the recharges for Brazil's one operating nuclear-electric plant, and heavy water for Argentina's Atucha I nuclear reactor.

Food

Again, the continent is essentially self-sufficient here, in an area often used as an economic bludgeon. According to FAO statistics, self-sufficiency ratios for all of Ibero-America in all major food areas are over 100 percent, with cereals the only exception, at 97 percent. Argentina, especially, can increase production immensely through double cropping, fertilizing, and use of now-idle land.

Metals

Ibero-America is a major world supplier of every common and most strategic metal ores. Until a decade ago, it exported ores and imported metals. Today, Ibero-America has enough refinery capacity to be more than self-sufficient in raw steel, primary aluminum, refined copper, primary refined zinc, primary refined nickel, refined lead, and refined tin. There are probably still shortages of capacity in some shapes of steel, with zero or deficient capacity in many specialty steels and alloys.

The region lacks refining capabilities in many of the less common metals whose ores it produces.

Other materials

Metallurgical coal is, in volume terms, the most serious deficit item in the region. It is needed to make steel. We do not recommend the wide-spread Brazilian method of substituting for it by turning forests into charcoal. In 1980, Ibero-America imported 6.1 million tons of metallurgical coals and produced very little of it. Colombia and Peru have known deposits which could supply this demand in future years, but for the moment, the U.S.S.R. and Poland seem to be the obvious suppliers, should the West embargo Latin American trade.

The region is bountifully supplied with raw materials and processing capacities for wood and paper, cement, glass, and most similar classes of items.

Fertilizer

Until recently, the region was highly dependent on outside sources of fertilizer and its feed-stocks, especially phosphates and potash. For phosphates, Peru, Brazil, Colombia, Chile, and Mexico have huge reserves. For potash, which the region spent almost $400 million importing in 1981, there are few options to the OECD countries other than Eastern Europe, whose surplus capacity is slightly greater than Ibero-America's import needs.

Consumer products

Today, the region has capabilities for self-sufficiency and even large-scale export of almost every manufactured consumer product. The only area where there is not full self-sufficiency in production of the components for these products is electronics, where substantial proportions of items like TV tubes are imported from the Orient. No great harm would be done if such imports were eliminated.

The only consumer area in which imports would have to be continued is medical products, of which only part of the $400 million imports could or should be substituted.

The region's main weaknesses, not surprisingly, are in chemicals and machinery production. Here, according to latest available figures (1980), the deficit of the seven largest countries in total chemical trade (total imports minus total exports) was $5.6 billion. This is a very sizeable deficit, which, if suddenly made unavailable under conditions of economic warfare, would impose a severe hardship on the industrial processes that utilize these chemicals. However, since 1980, both Mexico and Brazil have brought on line significant new capacities in chemical production, so the situation is not as grim as these figures suggest.

With respect to machinery, non-electrical equipment had a net import of $8.125 billion (imports $9.6 billion, exports of $1.475 billion), while electrical machinery had a $3.1 billion deficit (imports of $3.7 billion, exports of $624 million). The loss of these imports would also be serious, though here again, Brazil has a very significant degree of underutilized capacity in many areas of machinery.

Scenario I: Total trade embargo

Given the gravity of the current world crisis, and the bad precedents set in the Malvinas, it is certainly possible that the OECD would respond to united Ibero-American debt action with retaliatory economic warfare.

There is no doubt that such an embargo would shortly shut down a large share of the industrial capacity of Mexico, Brazil, Argentina, Chile, and the other nations which have significant industrial plant imported from abroad. The critical problem is that of spare parts for foreign-manufactured machinery which would be unavailable under such a scenario.

The Ibero-American countries have survived periods of difficulty in obtaining external inputs. During the depression, their import capacity was cut by more than half, due to lack of exports and lack of credit. Then, during World War II, machinery, fuels, chemicals, and shipping were all requisitioned for the war effort, and available only in short and irregular supply. Yet, Ibero-America's industrial output increased during those periods.

Today's machines are more complex than those of the 1930s. But, the region's capital-goods engineering capabilities have grown a hundred-fold. For example, Brazil's total capital goods production was $3 billion in 1977 and its total capacity is roughly $8 billion now. According to the Association for the Development of Basic Industry, Brazil has the technology and the facilities to produce 92.5 percent of its 1982 capital goods needs, with capacity to spare.

Such a scenario, however, is as politically improbable as it is economically dismal. The reciprocal effect on the United States and Europe from such a radical embargo would be great. Also, it would politically push the region into the arms of the Soviets, and thus carries a high geopolitical penalty.

Scenario 2: U.S. trade embargo

A somewhat less disastrous scenario, one which has already been mooted in radical monetarist U.S. circles, is a unilateral U.S. boycott of imports from and embargo of exports to any Ibero-American economy that defaults on its debt. However, this threat was made on the assumption that only one country, not a whole continent, were to take this action. The effect on the U.S. economy of such a continent-wide action would be swift and drastic, not only wiping out many U.S. export-oriented companies, but also by denying the United States many imports. Such a move would be extraordinarily difficult to implement politically in the United States.

Nonetheless, it is instructive to examine Ibero-America's options in the event of such a scenario. The two essential questions to be examined in this event are: 1) what critical spare parts imports come from the United States that could not be readily replaced; and 2) what imports other than spare parts are supplied in such quantities that finding alternate suppliers would be impractical.

With the best available foreign trade statistics, we have

calculated the relative import dependence on the United States, Europe, and Japan, of the main Ibero-American importers of machinery and chemicals—the two primary areas of severe import dependence.

Certain rough conclusions can be drawn. In most areas of machinery, Europe, and also Japan, are capable of taking up the entire slack left by a United States withdrawal from the market. Exemplary is Japan, which in most machinery categories presently exports many times the total Ibero-American import. If requested to take up the slack left by a U.S. withdrawal, a 5 or 10 percent increase in exports would cover the deficit. For Europe, similar calculations can be made, which will show similar ratios. And in Europe the presently spare capacity allows for almost instant increases of production by 10, 20, or more percent. Europe (most notably Italy) also has the chemical capacity that Japan lacks.

Thus, in general, the threat to cut off Ibero-America on the part of the United States is a "threat" to throw a trade bonanza to Europe and Japan.

Scenario 3: The credit cut-off

A more likely possibility than either of the above under a unilateral debt rescheduling and interest suspension "debt bomb," and associated common market formation by Ibero-America, is the suspension of all extensions of credit from the OECD nations to the continent.

Under such an OECD policy, there would be no cut-offs of trade per se, but Ibero-America would have to pay cash, or barter on equal exchange of values, for everything it imported. There would be no suppliers' credits, no short-term loans, no long- or medium-term loans, and no new lending of any kind.

In effect, that would limit Ibero-American nations' imports to a figure somewhat below their exports, below by an amount equal to the sum of profit remittances, technology payments, net freight charges, and any other permitted or essential service payments.

In 1980, the entire continent had a combined commercial balance of payments deficit of $7.5 billion. This included the trade balance plus net services other than profit remittances and interest, and movements of capital. Profits were another $5 billion.

To deal with this shortfall, Ibero-American nations forming a common market would have to fully mobilize the human and capital resources of their economies on what amounts to a war footing, including emergency measures, currency and banking reforms, and government direction of investment to ensure maximum use of limited resources.

Therefore, certain categories of services, most importantly those corresponding to Ibero-American tourism abroad, will be expected to be hostage to the crisis, and savings of several billions can be expected.

For the remaining $6-$8 billion, two options exist. First, where essential imports are now purchased abroad, but where existing regional capacity is underutilized, the creation of a Common Market Central Bank and a common currency unit of account permits the issuance of intra-bloc credit to put the underutilized facilities to work producing the needed items. Second, luxury imports have to be cut.

It appears that anywhere from zero to $6 billion is the approximate size of the ultimate import reduction required, depending on the extent of utilizable spare capacity. Most of the sacrifices would have to be borne by the middle classes in Brazil, Mexico, Venezuela, and Argentina. Central America is already suffering.

The magnitude of the figures presented suggests that only a portion of the region's new development programs would have to be triaged for the time being, as well as more than $6 billion that is devoted to construction of new facilities.

In any event, the resulting economic pattern in Ibero-America will be significantly better than that which would result from the unfettered application of IMF "conditionalities" under the existing monetary order.

Common market potentials

The following considerations apply to all three scenarios. Under any of the eventualities, a top priority must be attached to fostering intra-bloc trade. For lawful reasons, most nations have generally preferred or been forced to go outside the continent for both imports and exports, with the minor exception of trade between Argentina and Brazil.

Immediately, the recessionary conditions in Brazil, Argentina, Chile and to a slight extent so far in Mexico, define a short-term potential to cover the deficit in import-purchasing capacity identified above. A conservative estimate is that at least 10 percent of Brazil's industrial capacity could be put back into production in weeks if external demand were there. The comparable figure is 25 to 50 percent for many industries in Argentina, Uruguay, and Chile.

Brazil, in particular, has the capacity to produce most of the machinery required, for example, by Mexico and Venezuela. Brazilian businessmen estimate that Brazil has the capacity at present to produce domestically about 80 percent of the machinery that is now imported. And what is now imported is, in most cases, well under 50 percent of the machinery consumed in each branch of the investment goods industry. Mexico's degree of self-sufficiency is much less: in machine tools, less than 25 percent of the country's needs can be met domestically. Argentina is stronger in the consumer areas, and its capacity to produce capital goods at this moment is not clear. Chile has a chemical industry, now running at well below capacity.

In the worst-case scenario of total trade cutoff, of course, the region would have no choice but to make the best of what it could produce domestically, which would be a very difficult process, but not in principle impossible. The appropriate models for the kind of problem presented are the Soviet experience in the 1930s and 1940s, the U.S. experience in World War II, and the Ibero-American experience during the 1930s and early 1940s.