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Argentina's decision to impose quotas on Brazilian imports for two years effective July 31 set off a crisis within the four-year-old Southern Cone Common Market (MERCOSUR) trade bloc. Argentina's decision prompted Brazil to postpone talks on MERCOSUR auto and industrial policy scheduled for early August.

Only a hastily arranged meeting between Argentine President Carlos Saul Menem and Brazilian President Fernando Henrique Cardoso caused Argentina to lift the restrictions, averting a more serious rupture.

On July 15, the Argentine government approved the application of quotas until July 2002 for textile products from Brazil, China, and Pakistan. To get around the MERCOSUR prohibition on quotas, Argentina published a resolution that recognized the provisions regarding quotas in the accords of the Asociacion Latinoamerica de Integracion (ALADI) rather than those of MERCOSUR.

Brazil's chief trade negotiator Jose Alfredo Graca Lima said, however, that the ALADI pact, signed in April 1987, was superseded by the Asuncion Accord, which in 1994 established MERCOSUR. "Any measure adopted by Argentina has serious implications for the MERCOSUR member countries, and in this case it lacks legal support," said Graca Lima.

Crisis brewing since Brazilian devaluation

The quotas are the most obvious sign of the discord that has been growing between Brazil and Argentina since Brazil devalued its currency in mid-January. Recession-struck Argentine industries, which ship more than a third of their exports to Brazil, feared a flood of cheap Brazilian imports.

"Brazilians have to understand that a devaluation is equal to protectionism and that in some cases fears of a flood in imports came true, which is what we are discussing right now," said Argentine Foreign Minister Guido Di Tella.

Argentina restricts imports

The dispute seriously threatened MERCOSUR, which also includes Paraguay and Uruguay and associate members Chile and Bolivia. Brazil postponed technical talks, scheduled for early August, on automobile trade, sugar import tariffs, and industrial policy in retaliation for Argentina's decision to restrict imports from Brazil. Felix Pena, Argentine undersecretary for foreign trade, said Argentine industries face damaging competition from Brazil in 25 sensitive product areas including shoes, dairy products, and textiles.

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Meanwhile, the World Trade Organization (WTO) said on July 26 its dispute settlement body had established a panel to investigate US allegations that Argentine's tariff-rate quota on footwear imports violate free trade rules. But Argentine shoe manufacturers rejected the charges. "We plan to demonstrate to demand the industry secretary adopt urgent measures to stop in whatever way he can the indiscriminate entry of low cost [Brazilian] shoes and end their subsidies," said Carlos Bueno, president of the 1,500-member Shoe Manufacturers Association. "Argentina's shoe market has contracted during the recession and manufacturers lost market share since Brazil's devaluation while Brazilian imports have increased dramatically," said Industrial Development Institute economist Horacio Cepeda. Shoe exports to Brazil from Argentina dropped 56% between January and May compared to the same period last year, while trade in the other direction jumped 71.6%, Cepeda said.

MERCOSUR ministers to meet

President Julio Sanguinetti of Uruguay the temporary president of the trade bloc called a special meeting of the MERCOSUR foreign relations and economy ministers for Aug. 4 in Montevideo to discuss the crisis between Argentina and Brazil. MERCOSUR, the world's third-largest trade bloc with some US$15 billion in goods exchanged annually, has been weakened in 1999 by the Brazilian devaluation and by the political upheaval in Paraguay.

Although MERCOSUR expanded trade among its four members to US$18.2 billion last year from US$3.6 billion in 1991, the regional economic slowdown particularly strained relations between Brazil and Argentina. In June, Brazil concluded free trade talks with Latin America's second-largest trade group, the Comunidad Andina de Naciones (CAN), which groups Peru, Venezuela, Colombia, Ecuador, and Bolivia. Argentina complained that Brazil led the talks without consulting the rest of the MERCOSUR members (see NotiSur, 1999-05-21).

In July, the Argentine government sent a formal protest to Brazil regarding tax breaks it extended to US automaker Ford Motor Co. to build a US$1.3 billion car plant in the state of Bahia. Argentina complained that the generous incentives contravened an automobile-industry agreement within MERCOSUR.

The protest forced President Cardoso to re-examine the incentives and the government then cut the amount of tax breaks for Ford to a quarter of the original. "MERCOSUR is at a difficult juncture, perhaps the most difficult in its history," Jorge Hugo Herrera Vegas, Argentina's ambassador to Brazil, said following Brazil's decision to postpone trade talks.

As the crisis intensified, on July 29 Menem flew to Brasilia and, after meeting with Cardoso, agreed to lift the restrictions on imports from Brazil. "This eliminates a big cloud over Argentina's relation with Brazil," Argentina's Foreign Minister Di Tella said.

Dispute tests resolution mechanisms

The latest row is pushing the two countries to test little-used trade dispute panels because political solutions have proven elusive. Until this year, MERCOSUR's political leaders settled trade disputes. However, Cardoso, who has fallen in public-opinion polls, and Menem, in the final months of his mandate, may find their ability to impose solutions limited.

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While economic concerns are overriding, Brazil's pressure on Argentina is also political. The Brazilians, who are seeking to exert greater influence in Latin America, were annoyed by Menem's overtures to join the North Atlantic Treaty Organization (NATO). Menem's support for dollarizing the Argentine economy also angered Brazil's government. [Sources: Associate Press, 07/26/99; Clarin (Argentina), Inter Press Service, Notimex, 07/27/99; The New York Times, 07/28/99; Reuters, 07/26-28/99, 07/30/99]

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