

## MERCOSUR: The Regional State of South America

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### Abstract

In the economic arena of globalization, scholars often speak of countries that have joined together economically to form economic alliances. These usually include NAFTA and the EU, but almost never MERCOSUR. This is unfortunate as MERCOSUR is developing into a major economic bloc. Its impact on the global economy is no longer limited to South America. Just how MERCOSUR differs, for example, from NAFTA and from the EU is the focus of this essay. Some of the problems that remain among the members of this regional state are discussed. However, it is argued that the significance of MERCOSUR as a global network is that it has moved well beyond being a regional state. It has created alliances with Africa, the EU, and China. It has resisted the attempts by the FTAA to create an economic bloc that would unite the Americas from Canada to Chile. MERCOSUR is well on its way to becoming a network society, but it is a society that aligns itself with those that have been disenfranchised by the WTO, the World Bank, and the IMF.

Prior to the use of modern electronic technology, countries established trade routes that supplied the metropole with a wide range of materials from its trading partners that were geographically linked. During the Age of Exploration, sea routes provided this link between metropole countries and their colonies. With the rise of the nation-state, governments created economic alliances that encouraged trade with some nations and not with others. This was done by means of treaties, tariff control, and governmental alliances. What makes the modern era different is globalization. This term is usually meant to include liaisons between governmental agencies, nation-states, rather than with countries (geographical regions) or nations (the people of those nation-states). The process of globalization begins with the development of regional-states. The *Mercado comum de Sur* (MERCOSUR) is such a regional-state. It is composed of a core of countries in South America (Argentina, Brazil, Chile, Paraguay, and Uruguay) that function as an economic super-state. The next stage of economic develop occurs when these regional-states create treaties that align them with other governmental agencies that are beyond their own geographical regions. The North America Free Trade Agreement (NAFTA), for example, is composed of the United States, Canada, and Mexico and they function as a regional-state. They want to unite with MERCOSUR to create a larger economic zone that unites the Americas from Canada to Chile. MERCOSUR has resisted this attempt because of past economic experiences that ended in failure for Argentina. However, a similar movement to create a new network with the European Union (EU) exists and it has proved to be successful. This group is called the Mercosur-European Business Forum (MEBF). This new alliance has moved MERCOSUR from being a regional-state into a

global economy based on larger economic networks. Castells (1996) refers to this new alliance as a network society. MERCOSUR is becoming a network society.

Kenichi Ohmae (1995) has argued that in a world of near instant communications, the nation state is irrelevant. One of the outward symbols of its existence is the national border, staffed by uniformed officials checking papers and manning barricades. But what use are such border controls in the world of the Internet? What is happening is that economics and technology are enforcing a new scale on geopolitical organization. Boundaries are created by nation-states and those boundaries will continue to exist. However, economically, those countries are borderless. For example, although Italy is a nation-state, economically it is made up of two very different economic sectors. The southern part of the country is agricultural while the northern part is industrial. From the perspective of a global economy, only Northern Italy functions within the new network society. For this reason, Ohmae (1995) argues that the nation state has become an unnatural, even dysfunctional, unit for organizing human activity and managing economic endeavor in a borderless world. It represents no genuine, shared community of economic interests; it defines no meaningful flows of economic activity. In fact, it overlooks the true linkages and synergies that exist among often disparate populations by combining important measures of human activity at the wrong level of analysis.

How does a country move from being a territory in which people reside into being a nation? What happens that transforms this nation itself into a governmental agency known as the nation-state? How do nation-states reorganize themselves into regional-states? What makes a regional-state move the bond that unites them geographically with their neighbors into a new entity, a borderless state, which functions globally beyond national borders? In this essay, these concerns are addressed. It is argued that MERCOSUL is in transition from a regional-state into a network society due to its new alliances with the EU, Africa, and China. The story begins with mercantilism.

#### **Mercantilism and the Genesis of Globalism**

The earliest form of capitalism is called mercantilism. It was defined by the distribution of goods from one region to another along well established trade routes. This practice occurred among Arab traders during the 7<sup>th</sup> and 10<sup>th</sup> centuries. They bought goods for a low price in one region and sold them for a profit in another. This system of global trade contrasted with the preoccupation of local markets that defined Europe during the Middle Ages. Europeans did not depend on global trade routes whereas the Arabs were located on such routes and depended on them in doing business with other empires such as Egypt, Persia, and later Byzantium. These countries have a long tradition of mercantilism. This global trade system was extended and spread along northern Africa, Southern Italy (Sicily), Spain, the Middle East and Asia. Although Romans traded overseas with neighboring countries, they were not as well rewarded by these ventures as were the Arab traders who not only established such routes, but dominated them. However, the Crusades brought feudal Europe into contact with this new world of mercantilism. Europeans went through a Renaissance. They soon learned how to benefit from such trade routes; they borrowed the Arabian concept of "tariff" and adopted the mysterious mathematical concept of zero that was instrumental in maintaining global trade accounts. Luca Paciolo, a Venetian mathematician, used this concept in 1494 to introduce the concept of double-entry bookkeeping, an important instrument needed for the banking practices by the Peruzzi and the Medici families of that era for the expansion of European mercantilism. Why is this concept of mercantilism held to be the

earliest form of capitalism? It characterized the method that dominated the organization of local industries that obtained raw materials such as silk from the East and distributed these materials to local workers who would use these raw materials to create products for a wage. Their employers would then take the products and sell them for a profit. The banks were clearinghouses that were used to transfer funds against accounts.

Mercantilism was capitalism for the state and not for the individual. Jean Baptiste Colbert, the minister for the French king from 1661 to 1683 defined mercantilism as follows:

- The economic status of a nation is linked to the rise of the money economy. It measured its well-being by its possession of precious metals or bullion (gold and silver). Bullion was considered to be hard money, the source of prosperity, prestige, and strength.
- For a nation to be prosperous, it needed more bullion. This means that it needed a favorable balance of trade. It needed, in essence, to export more than it imported.
- Tariffs are needed to reduce the dependence of foreign competition. Tariffs should be high on important manufactured goods, but low on imported raw materials. Hence, a profit could be made in turning raw materials into exported manufactured goods.
- If a mercantile nation is to be great, it needed to control sea routes. It needed a strong naval force that could bring in sources of raw materials from its colonies, produce products from them, and sell them to captive markets. Hence, such great nations were called metropolises and they needed colonies to sustain the economic wealth of the motherland.
- The development of a mercantile system of global trade was the responsibility of the government. It must establish economic development and enforce economic and trade policies.

### **The Rise of the Nation-State**

Mercantilism alone cannot account for all of the economic changes that took place in Europe since the Middle Ages. It can account for the colonial economy during the interim of 1600-1750, but it cannot account for other factors that changed a nation of kings into a nation of states. These include the commercial revolution, the decline of the medieval economy, and the rise of the nation-state. Feudal economies, for example, were based on agricultural production. Such economies consisted of a **king** who controlled money and provided his kingdom with security, the **nobles** who controlled agriculture, the **merchants** who controlled trade, the **priests** who controlled social behavior, and the **serfs** who controlled nothing as they served as the labor force that supported the feudal system. This medieval economy declined with the rise of the bourgeoisie, the merchant class. Empires broke up into regions and these regional groups competed with each other. There were a series of religious wars that were directed against Rome. National wealth was associated with the wealth of a nation, the wealth of the people. It was no longer deemed to be the wealth of the sovereign or the empire. These factors established the conditions that made the rise of the nation-state a reality.

These coherent regions were not just territories; they were sites of power. Each region wanted to achieve economic self-sufficiency. Spain exercised rigid control of commerce of her empire. It used its Spanish Armada to dominate the earlier stages of the Age of Exploration. It established Spanish-born overlord (*peninsulares*) in the New World to control the native working class. It established a body of colonial affairs, the Council of the

Indies, as a part of its maritime council (*casa de contracción*) in Seville. This ruling body controlled the large feudal estates (*encomiendas*) in New Spain. Germany also worked at increasing its national revenue, the national treasury (*Kammer*). France, of course, expanded on mercantilism. Jean Baptiste Colbert, the chief minister of Louis XIV was the chief architect of economic regulation. He prohibited the export of money, levied high tariffs on foreign manufactures, and gave liberal bounties to adventures that encourage French shipping. England was also concerned with economic self-sufficiency. This island nation decided to challenge Spain and its domination of the seas. English seamen preyed upon Spanish vessels. Sir John Hawkins and Francis Drake set about to destroy the Spanish Armada so that they could control the sea routes. They eventually won and began their own version of expansion during the second phase of the Age of Exploration.

One of the conflicts that took place in Europe during the early stages of the quest for nation-statehood had to do with those parts of the empire that were aligned with Catholicism and those that were engaged in Protestantism. Unlike traditional Catholicism that emphasized the authority of the Church, Protestantism placed its emphasis on the individual and not the Church. It promulgated tenets that emphasized a moral based on hard work. Weber (1930) attributed this new attitude towards wealth and the work ethic with the rise of capitalism. He argued that the "Protestant Ethic" created the values necessary for capitalism to emerge as the new economics of Europe: Each person created a surplus or a profit from his labors and this wealth must be reinvested and used wisely. Nevertheless, the Catholic countries fought with the Protestant countries and this period is known as the "Thirty Year War." At the end of the battle, over 300,000 people had been killed in battle. Millions of civilians died of malnutrition and disease, they had been robbed and looted, and their homes burned by invading troops. Germany, the center of Protestantism, agreed to a religious settlement with a predominance of Protestantism in Northern Germany and Catholicism in Southern Germany. This agreement took place in 1648 and is known as the Treaty of Westphalia. In the meanwhile, France and Spain continued to fight each other over religious issues and settled their dispute with the Treaty of the Pyrenees in 1659. At that time, France replaced Spain as the greatest power in Europe. Why is the Treaty of Westphalia important? It established the concept of the nation-state. Many refer to this political structure as the Westphalian-state. Nevertheless, the nation-state was a new political entity. Since then, it has become the dominant form of state. What this treaty claims is that the populations of the world now live in states and these nation-states guarantee the existence of their collectivity as a nation, preserve its distinct ethnic identity and social history, provide a territory where a national culture and ethos resides, and provide them with social and political legitimacy. Nations have to do with people, but a nation-state is about the government responsible for those people. It has a territory and it is marked by borders and boundaries. Within those boundaries there are laws and a national consciousness, a cultural nationalism, and a sense of national identity. The nation-state is responsible for creating transportation networks within its borders; it has the obligation of creating and directing a national educational system; it has to maintain military forces to protect its borders; and it issues passports to its citizenry when traveling outside of its borders and visa for those who wish to enter its perimeters.

Under the rubric of globalization, there is much discussion about the demise of the nation-state. Nation-states, it is argued, are not eternal. There appears to be a global shift in the world that is molded by economic and technological forces. The political arena is no longer limited to the nation-state. Global economic forces have made the nation-state

dysfunctional as a unit that manages the flows of economic activity in a borderless world. The nation-state, it is argued, has become unnatural. It represents no genuine, shared community of economic interests. It defines no meaningful flow of economic activity. Hence, one has to turn to regional states as natural economic zones.

**The Creation of Regional States**

The first regional state was the Association of South East Asian Nations (ASEAN) that was established in Bangkok, Thailand, in 1967. Within the last two decades, this phenomenon has multiplied. Other nation-states have unified to internationally to form regional-states. This linking of the governments of contiguous nation-states into a larger regional-state emerged in Europe (European Union, 1992), North America (NAFTA, 1994), and South America (MERCOSUR 1991, MERCOSUL, 1991). Why is this important? It meant that a new kind of community developed that went beyond the nation-state. Countries are associated with regions; nations are associated with peoples and possess boundaries and they have much to say and do about the common language and culture of the people within its border. Nation-states, on the other hand, are governments. They have to do with laws and procedures that relate to the citizenry within a nation. What makes the regional-state different is that it is a new governing entity that extends beyond the boundaries of any nation state. The European Union, for example, is a regional-state. It has a common currency, a shared passport system, interregional laws, and regional trade policies. For many economist and political scientists, the regional-state marks the end of the nation-state and the beginning of a larger non-contiguous entity, the network society (Castells, 1996).

Community	Definition
Country	Countries are located in regions. A country defines a territory.
Nation	Nations have to do with people. They tend to be homogenous and share a common history. Many nations share ethnic traditions.
Nation-State	Nation states are governmental units. They have to do with the organization of people, their laws, the creation of currency, the education of its citizenry, postal services, telephonic communications, interstate highways and the determination of other services and social policies.
Regional-State	A regional state is a confederation of nation-states within a geographical region that form a global natural economic zone. Its unification provides an ideal entry way into the global economy. The European Union (EU) is a regional-state. The Mercado comum de sur (MERCOSUR) is modeled after the EU.
Network Society	This community occurs when a regional-state operates among non-contiguous nation-states

### **The European Union**

How did this new concept of governance begin? After the Second World War, six European Nations (France, Germany, Belgium, Luxemburg, The Netherlands, and Italy) decided that the best way to prevent another global conflict was through the control of coal and steel production, the main resources required for the production of weapons of war (ECSC, 1952). By 1959, the group met in Rome to sign a treaty (Treaty of Rome, 1957). They wanted to expand the scope of their cause and create an extended European Community. They resolved to do this in two ways. First, they needed to ensure the economic and social progress of their countries by means of a common action that would eliminate the barriers that divided Europe. For this purpose they created the European Economic Community (EEC). This agency would be concerned with the improvement of the living and working conditions of its people, remove the existing obstacles to balanced trade and fair competition, and to ensure greater social harmony by reducing the existing economic differences between the various regions. This group was concerned with confirming the solidarity that binds Europe. The second way in which the group supports their common cause was through the control of nuclear energy (Euratom, 1957). One decade later, these groups united to form the European Community (EC, 1993).

### **The North American Free Trade Association**

The next group to unite across geographic regions was Canada, the United States and Mexico. They launched the North American Free Trade Agreement (NAFTA) and formed the world's largest free trade area. The Agreement purports to bring economic growth and rising standards of living for people in all three countries. There are major differences, however, between NAFTA and the EU. There is no common passport system among these three countries within North America. The United States has a liberal immigration policy towards Canada, but a highly restricted one against Mexico. Furthermore, these countries do not share a common currency and the monetary exchange rates among these countries vary greatly. In addition, Europeans travel freely among their member nations, such travel is highly restrictive among NAFTA countries. NAFTA is a trade agreement among nation-states. The EU, on the other hand, goes well beyond economic policies. It is a genuine regional-state; these countries comprise the United States of Europe.

### **MERCOSUR: Mercado Comum De Sur**

In 1991, Brazil, Argentina, Paraguay and Uruguay created a trading zone among their nation-states. The agreement was formulated by the Treaty of Asunción (1991) which allowed these nations to establish common markets, promote scientific and technical development, establish common external tariffs, and coordinate economic policies. This regional-state is known as the *Mercado Comum de Sur* (MERCOSUR in Portuguese, MERCOSUL in Spanish). Later, in the Treaty of Ouro Preto (1995), other countries were added as associate members (Bolivia, Chile, Colombia, Ecuador, Peru, and Venezuela). Mexico was also included into the treaty as an associate member.

How did this regional-state differ from the NAFTA group? There are many similarities between NAFTA and MERCOSUR. Both are organized as economic super states. However, MERCOSUR has expanded far beyond the NAFTA group. It has included regional and non-regional members as part of its associate membership. This means that MERCOSUR is on its way towards becoming network a society. The current President of Brazil, Luiz

Inacio “Lula” da Silva, wants to include the whole of South America as part of MERCOSUR. The United States is threatened by this expansion as it makes MERCOSUR stronger than NAFTA. It also places the Free Trade Association of the Americas (FTAA, 1994) in opposition to NAFTA. MERCOSUR under the leadership of Brazil is countering the attempts by the United States to unite both North and South America into one mega-regional-state.

Another difference can be found in immigration policies. There is a greater tolerance among MERCOSUR nations with the exception of Argentina with its preference for European immigrants. Nevertheless, MERCOSUR allows for a greater movement of people within its regional-state than NAFTA. Within the political arena, MERCOSUR is unique in that it has opposed the International Monetary Fund because its policies have provided an unprecedented concentration of wealth due to globalization.

MERCOSUR has worked well with other economic groups. It has worked closely with the EU from its inception. Members of the EU have provided blue prints for their development and MERCOSUR is modeled after the EU. Brazil and Argentina comprise 40% of the economy of Latin America and they have attracted the attention of China which has invested \$19 billion in Latin America. After all, MERCOSUR has the largest reserves of natural resources in the world. Its energy reserves consist of oil and hydroelectric power. Venezuela is a part of this energy reserve and its President wants to create a transnational oil company that would be owned by Argentina, Brazil, Bolivia and Venezuela.

#### **MERCOSUR-European Business Forum (MEBF)**

Two regional states have a vested interest in MERCOSUR. One of these is the regional-state of NAFTA. This group consists of the United States, Canada, and Mexico. The drive to combine the Americas into a common trading bloc comes from the United States. It has been instrumental in creating a group, the Free Trade Association of the Americas (FTAA, 1994) and they have repeatedly met with MERCOSUR and its associates, but Brazil and Argentina have resisted joining this economic bloc. The other group that is interested in MERCOSUR is the European Union (EU, 1992). Transnational Corporations (TNC) in Europe have worked well with MERCOSUR. They have established the Mercosur-European Business Forum (MEBF, 2003) and have worked together to launch free trade negotiations between the two regional-states. As a consequence, the European side of the MEBF includes car manufacturers (Volkswagen, Fiat, Renault, DaimlerChrysler, and Peugeot), the chemical giant (BASF), electronic mega-corporation of Germany (Siemens), the Repsol Oil Conglomerate of Spain, European banks (Banco Santander, Centrol Hispano, Banco Bilbao Vizcaya, and the Banco do Investimento de Portugal), the telecom giants (Telefónica and Telecom de France), the world leader in steel production (ARCELOR headquartered in Luxemburg), and national employers federations (German BDI, Spanish CEOE, French MEDEF, and the Italian CONFINDUSTRIA). The South American side of MEBF includes the Argentinean Bidas Corporation, the Brazilian Petroquímica da Bahia, Brazilian food producer SADIA Group, the Companhia de Melhoramentos de Sao Paulo, and FANAPEL (the Uruguayan paper company). REPSOL YBF (2003) is one of the ten major private oil companies in the world and the largest private energy company in Latin America. Recently, Petrólos de Venezuela, a state run company, is working with MERCOSUR to make the whole of South America self-sufficient. How do these Transnational Corporations operate within MERCOSUR? Some corporations establish branches in South America, but most of them operate through Foreign Direct Investments (FDI).

### Direct Investment in MERCOSUR By The European Union

Direct investments by one transnational corporation within one nation-state into the economic structure of another nation-state plays a prominent role in the global economy. In the 1990s, there was an extraordinary surge in the flows of foreign direct investment within the world economy.

Interim	Billions of Dollars
1990	240
1995	318
1996	359
1997	464
1998	644

Hence, FDIs have an impact on capital formation and this is especially true for developing nations. The most important reason for this surge of FDI flows has been from cross-border mergers and acquisitions among the major transnational corporations. These FDI flows take place among developing and developed nations. Among the developed nations, the United States remains the larger single recipient of FDI flows (attracting 193 billion dollars in 1998), followed by the United Kingdom (63 billion). Among the nations of the developing world, China (45 billion dollars) leads Brazil (29 billion). There are several reasons why nations invest abroad (Wrobel, 1999). They invest in countries that have a large market and demonstrate a potential for growth. They also seek access to regional or international markets for their exports. They seek countries that are endowed with natural resources and that demonstrate a stable infrastructure. The major sources of FDI outflows come from the United States and the European Union. Japan no longer dominates the investment market due to its economic problems. Which organizations provide FDI into MERCOSUR? *Petróleos de Venezuela*, from a developing country, is one of them. The others are the EU and NAFTA. However, it is the EU that has worked closely with MERCOSUR. Most of these investments are in services rather than in industry.

The European Union is the main investor in MERCOSUR. Argentina received billions of dollars as FDI inflows. One of the largest sources of income came from the acquisition of Argentine Oil Company by YPF, the Spanish oil giant – Repsol. Brazil also received FDI inflows along with Uruguay and Paraguay. An interesting FDI inflow into MERCOSUR resulted from the great demand for automobiles in Brazil during the 1990s. The demand for cars rose faster in Brazil and Argentina during this period than in other parts of South America. Both nation-states tried to revive their automotive sector through investments (Ciravegna, 2003). One of the investors in this business sector was Fiat, the Italian automobile manufacturer in Turin. Fiat (Camuffo and Vopato, 1998) decided to invest in MERCOSUR by working with the engineering sector in South America to create a “world car.” This was an automobile that was built for South America and its geographic demands. Rather than import cars, Fiat developed regional factories that worked with international groups to create the P178 line of Fiat cars (Palio, Siena, Palio Week End, and Strada). The result of this FDI combined a FIAT car with a GM gearbox system. These two transnational corporations currently produce 11 different gearboxes in Europe and Latin America. These two



corporations continue to work together in other ways. In Brazil, for example, the GM pickup truck emerges as a FIAT truck.

### Concluding Remarks

Under the leadership of Brazil and Argentina, several South American nation-states came together to create a regional-state, MERCOSUR. Uruguay and Paraguay were among the founding members of this regional-state. Later, Chile was added as a member due to its DFI inflows into MERCOSUL. With the passage of time, other countries in South America became associate members. These treaties resulted in an economic bloc that drew the attention of NAFTA and the EU. The United States tried to bring MERCOSUR into its plans to create another economic bloc, one that united the Americas, but the South American nation-states refused the offer. They did pay attention, however, to a similar offer from the EU and created a network known as the MEBS. This alliance resulted in a large inflow of FDIs into Brazil and Argentina, thereby strengthening their regional-state. However, under the leadership of the President of Brazil, Luiz Inacio "Lula" da Silva, new liaisons have been created with Africa and China. Hence, this regional-state is now part of a larger economic entity, a network society. MERCOSUR is now a global economic force.

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