

# WESTERN PA INTERNATIONAL BUSINESS

A newsletter for the global business community in Western Pennsylvania

Fall 2002

## MERCOSUR: COMMON MARKET OF THE SOUTH

### What is Mercosur?

Mercosur is a regional trading alliance founded in 1991 by Argentina, Brazil, Paraguay, and Uruguay. The goal of the alliance is to promote trade among the member countries, which historically have traded more with Europe and the U.S. than with each other. Recently, Chile and Bolivia have entered into associate membership with the original four trading partners. Associate members enjoy trade preferences and are gradually converging toward full member status, although they do not accept the common external tariffs that the member countries have adopted.

The Mercosur agreement calls for a gradual elimination of all tariffs on goods originating in and traded among the member states.

At the time of the inauguration of the customs union in January 1995, approximately 80% of all products traded—about 8,000 categories of goods—began to be traded duty-free within the block. Only a few sensitive products such as sugar, autos, and petrochemicals continue to have intra-Mercosur tariffs.

Mercosur is still far from being a true common market, but the members have managed to achieve a customs union, although the Common External Tariff (CET) does not cover all items and numerous national variations still exist. For those products covered, an imported good carries only one tariff—if it is further traded among member countries, it passes duty-free.

Negotiations to achieve a full common market status by 2006 continue, although the current

state of the economies of Argentina and Uruguay may slow these discussions. As a common market, Mercosur will be required to do much more than simply reduce and harmonize tariffs; it must also coordinate the economic, legislative, environmental, infrastructure, and technology policies of the various member countries. For a variety of economic and even historical reasons, members have a long way to go to achieve these goals and there is no final date for full commitment to common market status among the members.

There are substantial differences in wealth and economic stability among member and affiliate countries (see Table 1). Argentina, formerly one of the wealthiest of the South American countries, is essentially bankrupt and is struggling to choose among several unpalatable economic alternatives. Uruguay and Paraguay both have state-sized economies—that is, they are not major exporters or importers—and they are also beginning to experience problems in the financial sector due to Argentina's crisis. Chile is a free market state that does well by itself competing

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## WHAT IS MERCOSUR? *continued from page 1*

on an international basis, while Brazil is the 800-pound gorilla that dominates Mercosur discussions.

Mercosur has the potential to be an important regional trading alliance. The combined population of the six member and affiliate countries is 243 million—more than two-thirds of South America's population—with a total GDP of approximately \$1.1 trillion. Mercosur's territory covers nearly 4.6 million square miles, comprising 70% of the total landmass of South America, and stretching from the tropical jungles of northern Brazil to the sub-Antarctic zone of southern Argentina. It includes some of the world's most important agricultural and mineral resources. The wide variety of topographies, climates, and resources provides substantial opportunities for member countries to expand their production or to develop complementary production.

Mercosur is considered a success in achieving its principal goal: the promotion of trade among member countries. In 1999, intra-Mercosur trade represented 22% of total trade by the member countries, a 50% increase from that of ten years earlier. By contrast, intra-EU trade in 1999 represented 61% of total EU trade.

While both Pittsburgh and the state of Pennsylvania have seen trade with the Mercosur countries increase over the past few years, exports to these countries still represent a small part of total exports (see Table 2). The NAFTA countries of Canada and Mexico, representing a combined 37% of Pennsylvania's total 2001 exports of \$21.9 billion, are still our biggest trading partners. The EU follows with 27% and trade with Brazil and Argentina represents only 3.3% of the total. However, while this is a small proportion of Pennsylvania's exports, the number compares favorably to Ohio (1.7%) and New York (2%). 

**Table 1 Mercosur Countries at a Glance**

	Population	Language	Estimated 1999 GDP per capita	Estimated Exports in 1999	Estimated Imports in 1999
<b>Mercosur Members</b>					
Brazil	174 million	Portuguese	\$6,150	\$46.9 billion: 18% to the U.S., 13% to Argentina	\$48.7 billion: 23% from the U.S., 13% from Argentina
Argentina	37 million	Spanish	\$10,000	\$23 billion: 24% to Brazil, 21% to the EU	\$25 billion: 28% from the EU, 21% from Brazil, 22% from the U.S.
Uruguay	3.4 million	Spanish	\$8,500	\$2.1 billion: 45% to Mercosur, 20% to the EU, 7% to the U.S.	\$3.4 billion: 43% from Mercosur, 20% from the EU, 11% from the U.S.
Paraguay	5.7 million	Spanish	\$3,650	\$3.1 billion: to Brazil, Argentina, and the EU (details not available)	\$3.2 billion: 34% from Brazil
<b>Associate Members</b>					
Chile	15 million	Spanish	\$12,400	\$15.6 billion: 27% to the EU, 16% to the U.S., 14% to Japan	\$13.9 billion: 24% from the U.S., 23% from the EU
Bolivia	8.3 million	Spanish, Quechua, Aymara	\$3,000	\$1.1 billion: 16% to the UK, 12% to the U.S., 11% to Peru	\$1.6 billion: 32% from the U.S., 24% from Japan, 12% from Brazil

Source: 2002 World Almanac

**Table 2 Pittsburgh Metropolitan Area Merchandise Export Totals to Selected Countries** (Thousands of Dollars)

	1999	% Change 1993-1999
Canada	\$1,410,513	90%
Mexico	\$397,487	121%
All South America	\$156,722	(43%)
Argentina	\$15,070	(75%)
Brazil	\$80,642	(0.2%)
Caribbean & Central America	\$74,775	25%
All Europe (including non-EU countries)	\$977,885	24%
All Asia	\$710,432	4%
All Africa	\$58,309	13%
Near East	\$104,773	(29%)
Australia	\$49,246	(18%)
World	\$3,940,324	32%

Source: Exporter Location Series, Census Bureau, Department of Commerce

## How Is MERCOSUR DIFFERENT FROM THE EU?

Despite its success in increasing trade among its member countries, Mercosur differs from the European Union in several important ways.

### **No supra-national laws, institutions, and regulations**

The more than 50-year-old EU has succeeded in establishing certain laws, regulations (such as environmental), and institutions such as the European Central Bank and the European Court of Justice that have supremacy over the laws and institutions of the member countries. For example, trade disputes with U.S. companies will be decided upon by the Court, rather than by the judicial system of an individual country. By contrast, Mercosur has not yet established a supra-national infrastructure, and may never, in fact, move as far in that direction as has the EU.

### **No common currency**

With a few exceptions, notably the English pound, 12 of the 15 member countries of the EU have now moved to a common currency, the euro, which has one exchange rate to the dollar. By contrast, Mercosur members retain their own currencies, each with its own exchange rate.

### **No free movement of citizens**

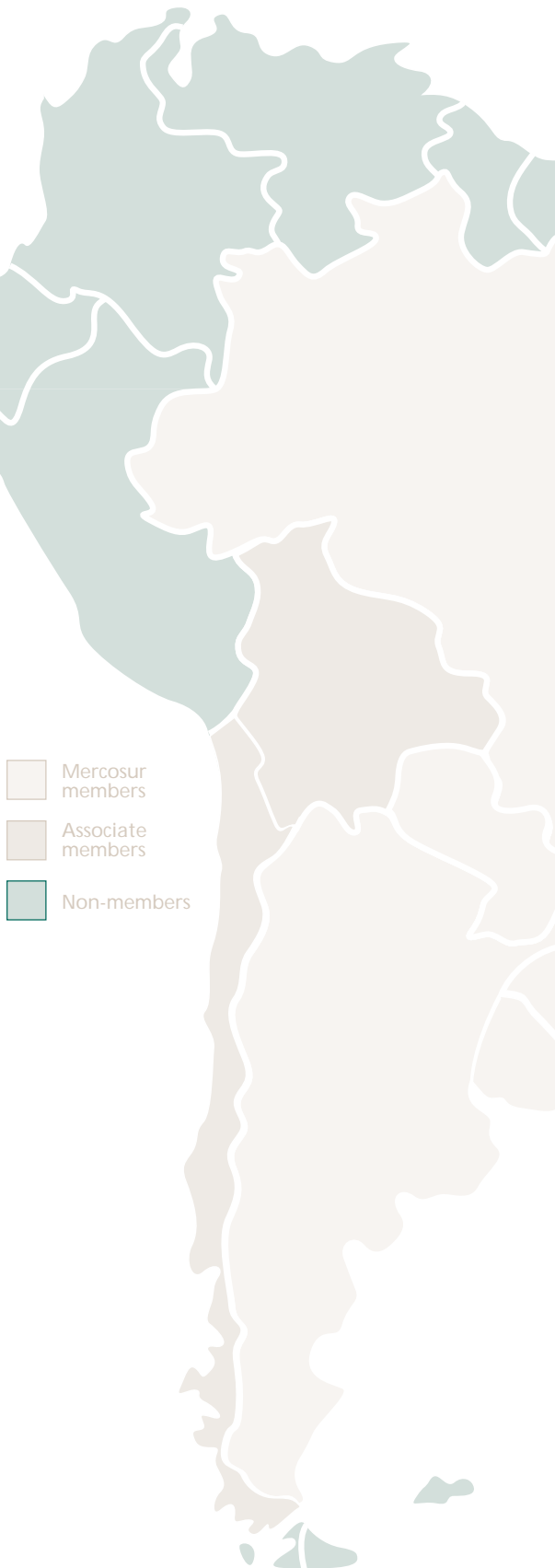
Citizens of EU member countries may move freely—whether for pleasure or for permanent relocation—among the EU countries. There are apparently no plans for Mercosur member countries to permit such an easy exchange of labor.

### **No common product standards**

The EU has succeeded in establishing uniform standards and specifications for many, though not all, products. This standardization can benefit the U.S. exporter, in that it is easier to sell a uniform product throughout the EU markets. On occasion, however, the standardization process can work to the U.S. company's disadvantage (see the Fall 2001 issue of this newsletter).

### **EU a consortium of developed countries; Mercosur a mixture of developed and developing countries**

While the relative prosperity of various EU countries does vary, in general, EU members are considered developed countries and enjoy relative economic and political stability. In addition to this strength, the structure of the EU and its institutions is such that no one country dominates common market discussions. Mercosur, by contrast, contains some relatively stable and developed countries as well as others that are bankrupt, weak, and/or developing. These obviously have more volatile economies. Finally, the fact that Brazil's economy is so much larger than any of the other members enables its interests to dominate many, if not most, Mercosur common market discussions. 



# MERCOSUR COUNTRY CONDITIONS

## *The Crisis in Argentina*

Argentina, formerly a prosperous country, is bankrupt. It has defaulted on a total of approximately \$193 billion of government, corporate, and provincial debt. The default was heralded by a run on the country's banks, and the government finally prohibited withdrawals and is now contemplating giving government bonds in return for deposits. Citizens are unable to cash paychecks or make purchases. Foreign banks and investors, uncertain of the ability of the government to stabilize the situation, are reluctant to make further investments.

It is never easy to predict exactly the timing and the gravity of such a crisis, but there were many signals of Argentina's rising problems over the last few years. In the early 1990s, in an effort to tame rag-

ing inflation, Argentina pegged the peso to the dollar. For a while this action curbed inflationary pressures, but the strong performance of the U.S. dollar during the nineties correspondingly made the Argentine peso uncompetitive in the foreign markets. The current account deficit (trade payments plus the interest on foreign loans) kept increasing and, as a result, Argentina had to keep borrowing more money to pay the interest on existing debt. In late 2001, the government defaulted on the foreign loans.

Whereas in the 1982-1983 crisis, most creditors, which were foreign banks, recovered about 60 cents on the dollar of investment, most creditors today expect to recover nothing. Lack of confidence in a coherent economic

policy further erodes the situation. There is potential for civil and political disorder. In short, the near-term outlook for Argentina is bleak. (For current information as well as answers to frequently asked questions about exporting to Argentina, visit the U.S. Commercial Services Web site at <http://www.comerciousa.org>.)

## *Uruguay*

A smaller economy now in its fourth year of an economic downturn, Uruguay is beginning to suffer from the Argentine crisis. Argentina was formerly both a major investor in Uruguayan businesses as well as a major source of tourist income—of which all activities have ceased. Argentines had been withdrawing money from their Uruguayan bank accounts steadily for the past few months

## Where Are the Opportunities in Mercosur?

In any economy, market demand and competition rise and fall as macroeconomic conditions change. The U.S. Commercial Service in the two largest Mercosur economies identifies the following industrial sectors (see Table 3) as among the leading sectors for U.S. exports and investment. (Comparable analysis for Paraguay and Uruguay was not performed in 2001.)

**Table 3 Leading Sectors for U.S. Exporters to Mercosur**

Country	Industrial Sector	Value of 2001 Market in \$US Billions
Argentina	Telecommunications equipment	\$2.8
	Computer hardware and peripherals	\$1.7
	Travel and Tourism (outbound)	\$1.6
Brazil	Computer hardware and peripherals	\$6.0
	Telecommunications equipment	\$17.9
	Oil and Gas machinery and services	\$6.3
Associate Members		
Bolivia	Oil and Gas machinery and services	\$1.0
	Mining	\$2.8
Chile	Pollution control equipment	\$2.5
	Computer hardware and peripherals	\$1.2
	Telecommunications equipment	\$.5

since the default, but this activity increased in May when the central bank prohibited one of its members from sending cash to its Uruguayan subsidiary. Alarmed at growing lines of Argentines pulling out their money, Uruguayan citizens began withdrawing their own funds, and credit rating agencies hurried to downgrade Uruguay's bonds. As a result, the value of the Uruguayan peso dropped, further increasing the burden of dollar debt.

In late May, the International Monetary Fund came to the rescue, offering Uruguay a second big loan—perhaps as much as \$1.5 billion—on top of the \$930 million it lent in March. Uruguay's President Jorge Batlle pushed through another package of emergency spending cuts and tax increases. These actions have stabilized the situation for the time being. But in Uruguay, as in Paraguay and Brazil, market confidence has been undermined by a lack of progress on painful but necessary reforms.

### **Paraguay**


Paraguay is experiencing some effects from the Argentine crisis, in part due to the fact that many Paraguayans who worked in Argentina have been forced to return to their own country to find jobs. The coun-

try continues to run substantial deficit financing, which the government had hoped during the last three years to address by privatizing the telephone and sanitary systems, a move designed to encourage domestic and foreign investment. However, a continuing political crisis, with divisions within the dominant parties, have slowed this initiative, and nothing further on the fiscal front is likely to occur until the elections, which should be held later this year. On the positive side, Paraguay is not experiencing inflation, and it has a small banking system which is to date relatively isolated from the Argentine problems. (For current information on Paraguay and Uruguay, visit the U.S. Department of Commerce Web site at <http://www.buyusa.gov>.)

### **Brazil**

The crisis in Argentina has not directly affected Brazil to any significant degree. However, there are signs of strain in the Brazilian economy, mostly due to the effect of the huge debt load assumed in the past few years. Brazil continues to run a large current account deficit, which has to be financed through inflows of foreign capital attracted in part by Brazil's privatization and sale of many assets. High interest rates and a relatively high inflation rate pose additional economic challenges.

In the short term much will depend on the presidential elections of October 2002. If the left-leaning candidate—Luis Inacio Lula da Silva, who has lost in the last three elections but who currently enjoys a 40% majority in the opinion polls—wins, there is a possibility that his populist economic policies could lead to accelerating inflation, a break with the International Monetary Fund, and possibly even the repudiation of Brazil's foreign debt.

As of mid-June, the rapid rise in Brazilian bond yields indicates declining investor confidence. The value of the Brazilian currency, the real, has fallen 17% against the American dollar, with most of the loss occurring in the first two weeks of June. To restore investor confidence, the Brazilian government recently announced that it would draw on its \$10 billion line of credit with the IMF and use the funds to buy back some of its foreign debt. While the underlying Brazilian economy is performing adequately, investors will need to keep a close watch on the high debt load and the results of the election. (For current information, visit the U.S. Commercial Service Web site at <http://www.focusbrazil.org.br>.) 

## IMPLICATIONS FOR U.S. EXPORTERS TO MERCOSUR COUNTRIES

While there are still profitable and secure trading opportunities with South American countries, there is no denying that in the summer of 2002 there are some signals of possible future problems. Prudent exporters will obtain financing through letters of credit confirmed by U.S. banks; however, it is also possible that some banks will be offering these instruments more selectively than in the past. It is also possible that the stresses of the Argentine crisis, as well as other economic uncertainties, could cause the Mercosur arrangements to slow, or even to be repudiated. Exporters must make an effort to stay abreast of current economic and political issues in the countries with which they have dealings.

## GOVERNMENT ASSISTANCE SITES AND CONTACTS *U.S. Commercial Service*

The U.S. Government's lead agency for developing and expanding American exports. With six offices in the countries of Mercosur, the U.S. Commercial Service produces original market research, advocates on behalf of American companies, and introduces them to new distributors, partners, and customers. Western Pennsylvania companies seeking to begin or expand sales in this region should contact the U.S. Commercial Service in Pittsburgh at 412-395-5050 or Office. Pittsburgh@mail.doc.gov.

### *U.S. Department of Commerce Trade Information Center Hotline 1-800-USA-TRAD(E)*

Provides basic export counseling and information on regulatory requirements, trade events, government programs, sources of financing, market research, and country and regional information, economic updates, and counseling.

### *Pennsylvania Department of Community and Economic Development*

<http://www.inventpa.com>

For information on trade missions and other economic programs offered by the state.

*The economic and political conditions described in this  
issue are current as of July 15, 2002.*

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## WELCOME

The International Business Center welcomes Keith Kirkham, head of the Pittsburgh Office of the U.S. Commercial Service of the U.S. Department of Commerce. Keith came to the Pittsburgh area last August from his prior post with the Commercial Service in the American Embassy in Tokyo, Japan. Keith has joined the editorial board of the Western PA International Business Newsletter.

# TV ANTENNAS MAKE EBENSBURG COMPANY HEARD ROUND THE WORLD

What's a small, family-owned business based in Ebensburg, Pennsylvania doing in places like Brazil, Papua New Guinea, Suriname, Bolivia, and Chile? Making money, for one thing.


Systems With Reliability, Inc. develops and manufactures UHF, VHF, and FM antennas and passive transmission systems. Many of these antennas are engineered to be site-specific, to enable broadcasters to use less high-cost energy. SWR started exporting in 1993, selling little at first. But exports now represent approximately 35% of the company's \$5 million in annual sales. "I have two antennas in Chile, two in Bolivia, one in Argentina, three in Brazil, plus others in Costa Rica, Venezuela, Suriname, and Mexico," says David Edmiston, SWR's senior vice president of sales.

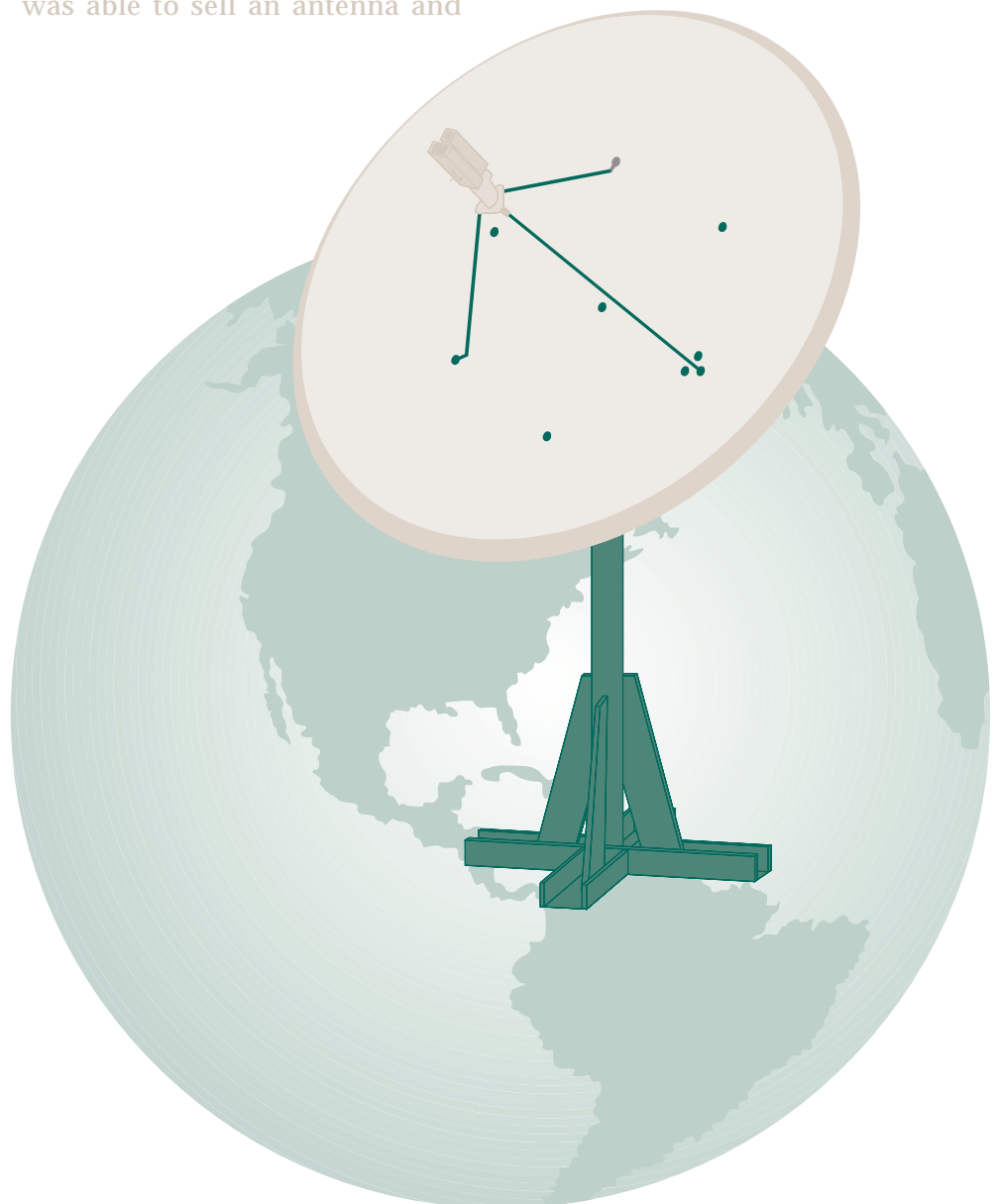
Getting started with exporting took a little time, but Edmiston is enthusiastic about the support he received. "There is so much help out there it's unbelievable!" he says. "All you have to do is ask! At first I felt almost embarrassed to ask simple questions, but I always got back a wealth of information from sources like the Pittsburgh Office of the U.S. Commercial Service, the Southern Allegheny Planning and Development Commission, and the Center for Global Competitiveness at Saint Francis University. They all went one hundred percent out of their way to help."

Trade missions organized by the office of the Governor of Pennsylvania are another important key

to success, Edmiston adds. "The missions have a lot of pull when the Governor goes along. The organizers set up meetings tailored to your needs with the key decision makers of companies. You start meeting at eight in the morning and continue until eight or nine at night. And the meetings work both ways, too. I needed a good source of copper, so when I went on a mission to Mexico, I was able to sell an antenna and

buy copper. The trade missions are the reason we do as much export business as we do."

In 1999, SWR was a winner of the Governor's Export Excellence Award. And even SWR's Web site (<http://www.swr-rf.com>) shows its commitment to exporting, as it is set up to be accessible in approximately twenty languages. Exporting is a key to SWR's continued success. 





# University of Pittsburgh

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