Free Trade Agreements are Just Band-Aids for Real Latin America Investment Reform

February 23rd, 2011

Exclusive: Look at investment, regulation and tax schemes as core drivers of economic cooperation, says leading LatAm expert

By Tarun George

Jerry Haar, Professor at Florida International University, does not have a very high opinion of the various FTAs between the US and Latin America. With expertise in corporate strategy, regional economic integration and Latin American marketing, he tells us why the Nearshore needs to do much, much more than simply removing tariffs in order to compete globally with the likes of India and China.

Does a more cooperative trade environment between the US and Latin America have spillover benefits in outsourcing?

Haar: I think the free trade agreements in place right now between the US and Latin America are actually more symbolic than practical. The main issue is not trade; it's the investment, regulatory and tax environment in the host countries. A tariff level of zero doesn't mean a thing if there are pernicious labor rules, the infrastructure is bad, or there is a public safety issue. All that adds to the cost of doing business.

Companies do want a tax environment that they can live with, but they're also looking at wage rates, corruption levels, and of course flexible labor markets – not markets where it costs more to fire a bad employee than to keep him on the payroll with all the damage he does.

So yes, the FTAs are helpful, especially to the manufacturing industries. But for outsourcing services specifically, unless the investment climate in Latin America improves, the spillover benefits from those trade agreements may be minimal.

I shouldn't care whether an American is doing my job, or a Mexican.

What is the US perception of Latin America right now? Is Nearshore outsourcing being blamed for job loss at home?

Haar: What's really taking jobs away from people is increases in productivity and the application of new systems, technologies and processes. But that's not a convenient scapegoat. The amount of human capital necessary to turn out certain goods and services has been continually declining irrespective of the number of trade agreements, currency prices, or any other factor. It's technology that's destroying these jobs and creating affordable price competitive goods for consumers. We have a multiplicity of choices thanks to technology.

Sure, outsourcing is one part of that job loss. But there's also a certain amount of cultural discrimination going on. Why is it that when a job goes from a unionized state like Ohio to a right-to-work state like Mississippi, nobody says a word? Whether my job goes offshore or just out of state, I'm still out of a job. I shouldn't care whether an American is doing my job, or a Mexican. But public opinion is still set against offshore outsourcing.

Yes, the President did speak about Colombia in his State of the Union speech, and that may make some Americans feel more secure about Latin America. But the trade relationship between Latin America and the US has already been set. There aren't going to be any tremendous fluctuations in the coming years. It's like people shifting from Pepsi to Coke, and then the next year from Coke back to Pepsi. The bandwidth for change is not that great, and it's the same with our Nearshore trade relationship.

What are the obstacles that Latin America faces in terms of expanding as a global business destination?

Haar: The fundamental problems are the same now as they were five or ten years ago. Productivity, quality of labor, infrastructure, public safety – if you have a **Nearshoring** operation, these are things you're worried about. It's an entire slew of microeconomic factors, not macroeconomic.

Just instituting free trade is not enough. You need to focus on the circuitry and plumbing of commerce – factors like innovation, technology, education, a straightforward tax and regulatory framework – these are the unfinished tasks for Latin America if it's going to compete globally.

*(Editor's note: Former Costa Rica President Oscar Arias echoed many of the same sentiments in our writeup of his opinions **here**.)*

These are factors that are important for competition even within the region itself. For example, we have Brazilian companies doing very well in Mexico, and it's safe to say they've put a few Mexican firms out of business – Mexican firms that could have held their own and maybe even penetrated the Brazilian market in turn, *if* there were flexible exchange rates, access to capital, less corruption, infrastructure, improved supply chain logistics, etc. Yes, there has been incremental progress over the last ten years, but the main problems endure.