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1st Session }

THE POLITICAL ECONOMY OF THE WESTERN HEMISPHERE: SELECTED ISSUES FOR U.S. POLICY

SELECTED ESSAYS

PREPARED FOR THE USE OF THE

SUBCOMMITTEE ON INTERNATIONAL TRADE, FINANCE, AND SECURITY ECONOMICS

OF THE

JOINT ECONOMIC COMMITTEE
CONGRESS OF THE UNITED STATES

SEPTEMBER 18, 1981

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LETTERS OF TRANSMITTAL

September 10, 1981.

To the Members of the Joint Economic Committee:

Transmitted herewith for the use of the Joint Economic Committee, the Congress, and the interested public is a collection of essays entitled "The Political Economy of the Western Hemisphere: Selected Issues for U.S. Policy." The collection includes 11 separate studies that were selected because they dealt with topics that were likely to be of interest to the 97th Congress.

We wish to thank the Congressional Research Service of the Library of Congress for making available the services of Alfred Reifman, Senior Specialist in International Economics. He directed, edited, and contributed to the volume. Individual papers were written by a number of different scholars from research organizations, universities, and the Federal Government. The project was planned and supervised for the committee by Kent H. Hughes.

The views expressed in the selected essays are those of the individual authors and do not necessarily represent the views of the Joint Economic Committee or of its individual members.

Sincerely,

Henry S. Reuss,
Chairman, Joint Economic Committee.

September 4, 1981.

Hon. Henry S. Reuss,
Chairman, Joint Economic Committee, Congress of the United States, Washington, D.C.

Dear Mr. Chairman: I enclose a collection of individual studies entitled "The Political Economy of the Western Hemisphere: Selected Issues for U.S. Policy." The collection was prepared by Alfred Reifman, Senior Specialist in International Economics of the Congressional Research Service.

The collection includes 11 different essays on topics that were picked because they were likely to arise sometime during the 97th Congress. The essays explore U.S. relations with our neighbors in Canada, Mexico, the Caribbean, and Central America as well as attempting to assess the implications of South America's extensive experience with development minded military governments. Separate essays treat last year's exodus of Cuban refugees and the extensive problems in the Cuban economy that prompted at least some of the emigration. The whole collection is a reminder of how closely political and economic events depend on one another.

For the non-oil exporting countries in South and Central America, energy and high levels of international debt have become closely rerelated phenomena. Separate essays in the volume detail the prospects of greater energy production in the hemisphere and the need for continued borrowing in international financial markets.

Alfred Reifman and his colleague Albert Mayio, an economic consultant and former foreign service officer, have rendered us a considerable service in editing and reviewing the individual contributions to the volume. I also wish to express my thanks to Dr. Kent H. Hughes of the committee staff who supervised the Western Hemisphere project for the committee and to Ms. Susan McGinnis, formerly of the committee staff, who helped review a number of individual papers.

It should be understood that the views expressed in this study are those of the individual authors and do not necessarily represent the view of the members of the subcommittee or the committee staff.

Sincerely,

GILLIS W. LONG,
Chairman, Subcommittee on International Trade, Finance, and Security Economics.

SEPTEMBER 1, 1981.

Hon. GILLIS W. LONG,
Chairman, Subcommittee on International Trade, Finance, and Security Economics, Joint Economic Committee, Congress of the United States, Washington, D.C.

DEAR MR. CHAIRMAN: I am pleased to transmit a collection of 11 studies on "The Political Economy of the Western Hemisphere: Selected Issues for U.S. Policy."

The studies are divided into three parts:

(1) An Overview which is an introduction and summary of the entire volume;

(2) Regional and Country Studies section which contains essays on Central America, the Caribbean, South America, Cuba, and Canada; and

(3) A section on Economic Studies which examines Latin America's debt problem, the outlook for hemisphere oil and gas production and exports, prospects for a North America free trade arrangement, and United States policy concerning immigration.

The volume was prepared under the general direction of Alfred Reifman, Senior Specialist in International Economics at the Congressional Research Service. He and Albert Mayio, a CRS consultant and retired foreign service officer with extensive experience in Latin America, reviewed and edited the essays.

A committee headed by Dr. Kent H. Hughes of the staff of the Joint Economic Committee planned the volume. On the planning committee were Larry K. Storrs and Barry Sklar of the Congressional Research Service.

Sincerely,

GILBERT GUDE,
Director, Congressional Research Service, Library of Congress.

CONTENTS

OVERVIEW

THE UNITED STATES AND THE WESTERN HEMISPHERE IN THE 1980's: INTRODUCTION AND SUMMARY

By Albert Mayio and Alfred Reifman

The following collection of essays has been prepared for the 97th Congress with the purpose of exploring some of the main aspects of our relationships with Canada, Latin America, and the Caribbean. The focus has been on questions that are likely to arise during the course of the 97th Congress.

This volume is divided into three parts: (1) this introduction and summary; (2) regional and country studies; and (3) selected economic studies.

The first section is an overview of political and economic developments in the Western Hemisphere that affect our relations with countries of the area.

The second section consists of six essays dealing with U.S. relations with Central America, the Caribbean, South America, Canada, the massive flight of Cubans to the United States in 1980, and the state of the Cuban economy.

The third section includes four essays covering Latin America's debt problem; the prospects for Western hemisphere oil and gas production; the proposals for trade integration of the United States and Canada, and for integration of these two countries with Mexico; and U.S. immigration policy.

A number of important topics have not been dealt with in detail. A partial list of desirable topics that were omitted includes political and economic studies of a number of individual countries; an analysis of U.S. trade with and aid to Latin America; an examination of the role of the Church in the political affairs of the area; and a review of U.S. human rights policy. Perhaps a future volume will treat the subjects mentioned with the breadth and depth they deserve.

The immediate U.S. concern in the hemisphere stems from the political turmoil in Central America. A widening civil war there raises the possibility that a victory of the guerrilla forces could well lead to the spread of Soviet power in that area.

Of less immediate but a long-run and greater concern revolves around our more troubled relationships with Mexico and Canada. The increasing interchange of people, capital and goods amounts to a growing *de facto* economic integration of North America, a development which neither the Canadian nor the Mexican governments regard as an unmixed blessing.

On the other hand, our relations with the Caribbean region, except for Cuba and Grenada, seem to be in good shape. This may well be the result of the increase in attention and in economic assistance to the area by the United States and other countries over the last few years. A strong democratic tradition may also have something to do with the relative stability of the English-speaking Caribbean countries. In seven elections held over the last two years in the region in which parties sympathetic to Cuba participated, moderate forces won: Jamaica, Antigua, St. Kitts-Nevis, Dominica, St. Lucia, St. Vincent, and Guyana. However, the longer run prospects for political stability in the area are uncertain. Most of these economies are weak and depend heavily on the tourist trade which is very sensitive to business fluctuations in the United States, Canada and other industrialized countries. Recognition of the fact that the current level of external economic assistance may not be enough to enable the weaker Caribbean countries to cope with their profound structural problems is prompting the Reagan administration to develop a joint aid effort with Mexico and Venezuela.

Our relationships with the democratic regimes of South America—Venezuela, Colombia, Ecuador, and Peru—are reasonably good but clouded somewhat by persistent misgivings about our motives and fears of our intervention elsewhere in the Hemisphere. With the military regimes that rule the bulk of South America's population—Argentina, Brazil, Bolivia, Paraguay, Chile and Uruguay—our relations were cool at best under the Carter Administration but may be now on the mend.

The strains in our hemispheric relations are not all, or even primarily, our fault. Canada is in the throes of a bitter constitutional crisis. Oil-rich Mexico seeks to play an important role in hemisphere and world affairs, and this often leads to opposition to U.S. policies toward Latin America and toward the Third World. Venezuela, a founding member of OPEC, also aspires to a more active role in world and regional affairs. Argentina and Brazil, even if they were not under military rule, would still be pursuing activist foreign policies not always consonant with American policy.

Although the authors write from different vantage points and disciplines, their essays reflect a common awareness of the need to rethink the basic premises of our policies towards the other nations of the hemisphere in the light of the changes that are occurring in these countries.

No consensus was sought, however, nor does any emerge from the various essays in the volume on redefining U.S. interests in the region and on what changes in our policies would best serve U.S. interests. In some cases, policy options are presented; in others, the authors have chosen to let the options be inferred from their analyses. In both cases, the aim is to focus on the factors that should enter into policy rather than to recommend specific policies.

In the following essay, *Richard Millett* focuses on the most immediate Communist threat in the hemisphere, the possibility that a Castro-like regime may emerge out of the virtual civil war that is raging in El Salvador, building up in Guatemala and perhaps only in remission in Nicaragua. Political violence is nothing new to the area, Millett writes; what is new are the main actors in that violence. The current conflicts, he writes, no longer pit sectors of the armed forces and the traditional ruling groups against each other. Instead, peasant, labor and middle class groups now strive to overturn the civil-military elite that has dominated these three countries for so long. Important elements of the Church, organized labor, and even traditionally moderate sectors of the Social Democratic and Christian Democratic parties support this effort. Complicating U.S. policy towards the area is the growing involvement of Mexico, Venezuela and Western Europe.

In Nicaragua, the Marxist-influenced Sandinista Liberation Front (FSLN) has moved the nation steadily to the left in both domestic and international affairs. In Guatemala violence may become worse than in El Salvador. In El Salvador, Millett believes, the junta is attempting to meet the insurrectionary movement by reforms as well as force of arms. In Guatemala, the military seem determined to meet the leftist challenge by force alone. In Honduras, although the military are slowly preparing to return the country to civilian rule, the social problems are immense and may be beyond the capacity of moderate political forces to deal with. In Panama, high hopes that the country will prosper as a result of the treaties with the United States have brought about a certain political stability. In Costa Rico, growing economic troubles pose the threat that the strong tradition of democratic rule may be eroding.

The United States is in a difficult position in Central America, Millett argues, because it is compromised in the eyes of the Central American leaders by past support of the right. It cannot serve as a mediator, and it cannot withdraw from the area because this would undermine whatever chance the moderate political forces have. Direct military intervention by the United States, Millett believes, would meet with massive resistance and criticism not only in Central America but throughout Latin America.

Since mediation, withdrawal, and direct intervention do not seem feasible to him, Millett sees as a fourth option a flexible pragmatic country-by-country approach based on an effective program of economic aid. However, given the current lack of enthusiasm in the United States for foreign aid, it may be too late, Millett concludes, for even an ambitious and ample program to bring about peace and development in the area.

In the third essay, *Abraham Lowenthal* examines the main traditional premise of United States policy toward the Caribbean: The area is of critical military and economic importance to the United States. Contrary to this premise, however, the United States pays only sporadic attention to the region. These bursts of attention, Lowenthal writes, occur only when the region's political and economic stability seems to be threatened. After the Dominican crisis of 1965, it was not until the end of the 1970's that Washington refocused its attention on the Caribbean. What made it do so were Cuba's increased activity in the Caribbean, the shattering of Central America's stability, and the perception of the large extent of the Caribbean migration to the United States.

In Lowenthal's view, the military importance of the region has declined. New technology has reduced the value of naval bases and other installations in the area. The share of U.S. trade passing through the Panama Canal is falling. The primary means of protecting the United States against military threats in the Caribbean, according to Lowenthal, rests on U.S. negotiations with the Soviet Union, as exemplified in the understanding keeping nuclear-equipped submarines out of Cuba.

With respect to other U.S. economic interests, Lowenthal points out that the share of U.S. trade and investment have been declining steadily since World War II. Moreover, the region is no longer, if it ever was, a critical source of strategic materials such as oil and bauxite.

Lowenthal considers only two types of U.S. policy feasible for the Caribbean. The "activist" approach would combine concern for security and political stability in the Caribbean with increased support for economic and social development. This implies reinforcing the U.S. presence in every field: military, political, economic and cultural.

The "developmentalist approach", according to Lowenthal, would emphasize the sound long-term development of the Caribbean region. The best security for the United States, he believes, rests on viable, effective societies that meet the needs of increasing numbers of their citizens. In his view, a consensus exists within the Caribbean on the nature of the region's problems and how the United States could help. A sustained commitment to the area's economic development would do more for U.S. security than a policy directed primarily at containing Cuba and Communism.

In the next essay, *Albert Mayio* discusses the origins, performance and possible successors to the so-called "new authoritarian" regimes of South America: Argentina, Brazil, Chile and Uruguay. (Peru's military regime, which held power from 1968 until 1980, is considered briefly.) Also called "bureaucratic authoritarian" or "corporate" states, these new-style regimes are distinct from the traditional Latin American "caudillo" or strong-man dictatorships in several aspects:

(1) They are ruled by the military as an institution.

(2) They suppress traditional mechanisms for expressing the popular will such as elections, parliament, political parties, the media and labor unions.

(3) They are committed to accelerating economic development and (except in Peru in 1968–75) to controlling inflation by orthodox, conservative policies. These policies are designed to encourage foreign private investment and private enterprise: freezing wages, reducing government transfer payments to the poorer sectors of the population, restricting credit, lowering import duties and reducing non-tariff barriers.

In Mayio's view, the economic performance of the various military regimes has been mixed. In Brazil, Uruguay and Chile, after slow starts, gross domestic product (or GDP—GNP less international transactions), has increased rather impressively. Argentina and Peru, however, have experienced about the same erratic economic growth under military rule as they did under civilian governments.

The record on inflation has also varied. Chile has done very well; the other countries have not.

The human costs under military rule have been enormous. The worst, however, seems to be over. The number of reported arrests, disappearances, and deaths have dwindled to low levels. The leftist terrorist forces have been crushed. In Ecuador and Peru, constitutional government has been restored (in 1978 and 1980, respectively). Although political liberalization is being resisted by the hardline military faction in Brazil, much has already been accomplished. In Argentina, the new president, General Viola, is under heavy pressure to move swiftly to constitutional government. In Uruguay, the military rulers appear to be in a quandary as to their next step following the defeat of a new constitution which they made the mistake of submitting to the people for approval. In Chile, the military regime has indicated that political liberalization may begin within the next few years and be complete by 1990 or so.

It is, therefore, possible that the military will relinquish control to civilian political parties within the next few years. However, the military in South America have a tiger by the tail. The scale and intensity of the military repression have been unprecedented in modern South American history. There is a real possibility that the working class and large segments of the middle classes in these countries have become more radicalized by what has happened, auguring increased strength for the left. Those guilty of committing atrocities or of inspiring them fear they will be called to account if political liberalization becomes a reality. In Brazil, the names of military and security personnel alleged to have been involved in atrocities are already being publicized in the media, and is one of the reasons why the hardline factions are opposing liberalization.

The constitutionalist sector within the armed forces seems strong, however, and public opinion seems, except possibly in Chile, to be growing against a prolongation of military rule.

Which tendency will win out, and in which countries, depends on the skill and flexibility of the military and civilian leaders, on whether world economic conditions are propitious for South America, and on the popular will. The outcome is, therefore, uncertain.

On a wide variety of issues that affect the interests of our citizens, however, the United States must deal with the military regimes as they are. It cannot, therefore, maintain an adversary relationship with the military regimes in South America and still effectively protect and promote those interests. On the other hand, the United States can ill-afford, by word and deed, to alienate the pro-democratic constituency in South America. This, Mayio concludes, is the challenge U.S. diplomacy faces in South America in the 1980s.

In the following essay, *Barry Sklar* examines the mass flight of Cubans to the United States in 1980. He sees this as a result, after a first startled reaction, of a conscious decision by the Castro regime to get rid of a large number of people, particularly those who were manifestly disgruntled and otherwise "antisocial." The Castro government also saw that the exodus would relieve some of the economic pressure on Cuba as well as cause problems for the United States.

An important factor in the alienation of so many Cubans with their regime, according to Sklar, is to be found in the visits of more than 100,000 exiles from the United States which the regime permitted in 1979. These exiles spent an estimated $100 million in Cuba. The stories they told of their life in the United States served to highlight in very personal terms the contrast between a dreary Cuban life-style and that of the emigres in the United States. In Sklar's view, the episode demonstrated: (1) the damage a sudden swelling of the refugee stream can do to the United States; (2) the economic and political strains in Cuban society that make so many Cubans eager to flee, and (3) Castro's power to open and shut the doors of escape at will.

The economic strains underlying the Cuban exodus of 1980 are examined in more detail in the essay by *Russell Swanson*. Here he documents the lack of improvement in the Cuban level of living over the last five years. Per capita consumption of food has increased only slightly during that period; health and educational services have improved only marginally. Per capita supplies of clothing and of key staples such as sugar, rice, beef, and coffee have diminished. The housing shortage has worsened. Unemployment is high and increasing. In part the trouble arises because of natural disasters in agriculture and reduced access to traditional fishing grounds because of the strict enforcement by other countries of the 200-mile economic zones. Another factor has been the steep rise in the cost of imported commodities. The inherent inefficiency of a centrally-planned economy is still another source of trouble. According to Swanson, prolonged economic austerity has resulted in declining worker incentives, morale, and productivity.

Only a massive increase in Soviet economic aid prevented a major downturn in the Cuban economy in 1976–80. Swanson believes without Soviet aid, Cuba would have been forced to cut imports by half. With Soviet aid at about $3 billion annually, Cuba now depends on Moscow for about two-thirds of its imports as compared with 45 percent in 1971–75.

Swanson does not foresee a major downswing in the Cuban economy so long as the U.S.S.R. continues to subsidize it. Rather, he sees the malaise being reflected in increasing absenteeism, deliberate work slow-downs and the black market. To cope with the situation, Castro has initiated some economic reforms. He evidently also hopes to arrange for some orderly, long-term emigration of perhaps 1–2 million people and for an end to the U.S. trade embargo. Castro, concludes Swanson, is not above threatening a new large-scale exodus to induce the United States to negotiate a better *modus vivendi.*

Following Swanson's essay, the discussion shifts to Canada. In their essay, *Edward Nef and Emerson Brown* review our over-all relations with Canada. Canada is involved in a prolonged constitutional crisis over the power of the central government versus the provinces. At the same time, Canada remains committed to protecting its sovereignty from possible encroachments of the United States. The leaders see their country's autonomy endangered by the increasing interchange of business and culture between the two countries, in which the United States has an advantage in terms of sheer numbers.

The two authors see increasing difficulties in negotiating satisfactory solutions to bilateral problems such as fishing rights, restrictions on investments, particularly in Canada's energy resources, provincial subsidies to business and restrictions on border trade. Some of the difficulties arise because, on the Canadian side the respective powers of the provinces and the federal government are in a state of flux, and, on the American side, our economic problems are nudging us to increased nationalism and, possibly protectionism.

Nef and Brown do not think our essentially amicable relationship with Canada is in any real danger. They believe, however, that both sides need to intensify their efforts to improve the consultative and negotiating processes.

The first essay in the economic studies section is a discussion by *Albert Fishlow* of Latin America's debt problem. Fishlow points out that foreign debt is not only a problem, it is also a solution. Debt is clearly a burden—it must be repaid. But, it is also a source of investment funds that should increase output permanently. Foreign debt repays itself and then some, if only part of the resultant increase in output must be used to service the debt. This is so, providing, of course, that the real rate of return from the investment exceeds the real costs of debt servicing. The problem with increasing indebtedness, Fishlow writes, is that the increased returns from the investment are not likely to be forthcoming immediately or may not be forthcoming in the shape of increased exports or reduced imports. In Fishlow's view, to deal with this problem requires import and consumption restraint and greater incentives for exports. In the longer run increased exports are the only way to escape the external debt trap. But since it takes time and a robust world economy to raise exports, Fishlow sees increased borrowing by Latin America as imperative over the next few years. Foreign private banks are, however, increasingly reluctant to sustain, let alone increase, the present scale of lending to countries like Brazil with large debt burdens. Fishlow believes new approaches are urgently needed to assure adequate capital flows. Otherwise the Latin American countries may not be able to make the structural changes needed to substitute new energy for imported oil and to develop their capacity to export. He outlines several institutional changes that could improve the international financial recycling system.

These fall into three broad categories: (1) make private lending more attractive by reducing private bank risk, either through some kind of insurance or by transferring part of the commercial bank portfolios to the World Bank in exchange for World Bank bonds; (2) augment the resources of the official institutions, principally the World Bank and the International Monetary Fund, so that they could participate jointly with the private sector in loans to developing countries; (3) encourage direct recycling of OPEC surpluses either through a special facility attached to the World Bank or through a new agency which would index OPEC deposits and interest rates to inflation. The purpose would be not only to only protect the OPEC countries from seeing their financial assets eroded by inflation, but also to commit them to make only moderate increases in the future in the real price of oil according to a negotiated formula.

Fishlow acknowledges the difficulties of the various courses of action. He is confident, however, that careful negotiations could lead to the adoption of one or a combination of the three approaches. In any case, he argues, unless new ways are found to recycle OPEC surpluses, the developing countries are likely, at best, to experience only limited growth and, at worst, financial problems that could have severe repercussions not only on them but on the industrialized countries as well.

To the extent that the political instability of Central America—and for that matter of Latin America—is the result of economic factors, the strains of adjusting to upward spiraling energy costs since 1973 certainly count as an important source of discontent. In the Caribbean area, for example, the great increase in external aid since 1976 has been more or less offset by the rise in the import bills of the poorer Caribbean countries, even though Mexico, Venezuela and Trinidad-Tabago are currently providing as much as a third of the financing necessary to cover these bills. Other factors, such as the slowing of export growth as a result of the slow-down of business activity in the industrialized countries, may be as important a cause of Latin America's economic troubles as the increased oil bills. A great increase in energy production of Mexico, Canada and Venezuela could help all the Latin American and other oil-importing countries.

Jerome Fried examines this possibility in his essay. He notes that while all three countries have vast reserves, there are great difficulties in exploiting those in Canada and Venezuela. The technological problems in converting Canadian tar sands into marketable petroleum and of processing Venezuelan heavy oil rule out, in Fried's opinion, these two countries as having much of a positive impact on the world situation in the medium term. The one country that does have rather easily exploitable reserves greatly in excess of its needs is Mexico. Mexican national policy, however, he points out, calls for the minimum amount of oil production needed to earn enough foreign exchange to meet the country's import requirements and service its external debt. There is, of course, always the possibility that Mexico will find its need for foreign exchange much greater than now envisaged as its economic development programs move into high gear. In Fried's view, however, the increase in Mexico's production and exports is not likely to be large enough to have a perceptible impact on the world oil situation over the next decade or so.

North America's economic integration is the subject of *Sidney Weintraub's* essay, the penultimate essay in the series. Economic integration with the United States, Weintraub points out, is a solution that springs readily to the American mind, given our own historical experience and the more recent example of the European Economic Community. Moreover, *de facto* economic integration of North America is proceeding apace anyway because of the easy and growing interchange of people, money, and materials that proximity makes possible.

Weintraub warns, however, that as natural and desirable as this *de facto* process of integration may seem to Americans, it does not seem so to Canadian and Mexican political leaders and to their business communities. For decades the governments of these two countries have sought to reduce the dependence of their economies on the United States. Up to now these efforts have been to little avail against the multiple ties that mesh the United States economy into the other two economies. Oil now gives Mexico a possible means of diversifying its export markets and sources of imports. It has already started on this route by limiting the amount of petroleum that can be exported to any one country (i.e., the United States) and by seeking to tie the sales of its petroleum to other industrialized countries to exports of other products. Canada, now a small net importer of oil, and pledged to free trade, seeks to lessen U.S. influence on its economy by controls on foreign investment and, more recently, by measures to reduce the role of foreign oil companies in the development of its energy resources. Early returns suggest the latter move is costing Canada dearly in a reduction of investment in oil exploration.

Weintraub discusses a variety of trading arrangements principally involving Canada and the United States but also possibly Mexico as well. He sees Canada deriving great benefits from being able to compete freely in a rich, mammoth North American market. But the advantages to the United States seem, in his view, to be less tangible; we already have a large enough home market.

Free trade between the United States and Mexico presents a different order of problems (and opportunities) on both sides because Mexico remains much less developed than either the United States or Canada. Despite this objection and his doubts that the formidable political obstacles can be overcome, Weintraub believes that the idea of some form of North American trading arrangement should be explored more intensively and debated in terms of specific sectors and problems rather than, as has been mostly done up to now, on the basis of general principles and nationalistic emotions.

The Weintraub essay does not deal explicitly with the impact of a possible North American integration scheme on Latin America or with the status of the various economic integration agreements and proposals in Latin America itself. As Fishlow and others have stressed, export expansion is also one of the imperatives for Latin America. This is especially true for the oil importers. But it is also valid for the oil-exporting countries of the region: Mexico, Venezuela, Ecuador and Peru. These countries need to expand their non-oil exports in order to raise employment and income now and to prepare for the time when their oil gives out.

In the last essay, *Joyce Vialet* discusses the problem of legal and illegal migration from abroad and particularly from Latin America.

U.S. immigration law since the 1920's has been dominated by two features, Vialet writes, both of which no longer reflect current realities. First, the focus of the law has been on Eastern rather than on Western Hemisphere immigration. Second, domestic considerations have been the primary influence in the shaping of our immigration code.

The major regional source of legal immigration is now the Western Hemisphere. This immigration rose from 1.2 million persons in the 1956–65 period to 1.7 million in 1967–76, an increase of 42 percent.

The Western Hemisphere is also the largest source of illegal immigration. High population growth, rapidly developing economies, and strong ties to the United States, Vialet writes, are the main "push" factors behind this immigration, while employment in the United States, at wages considerably higher than those at home, is the major "pull" factor.

Controversy surrounds almost all aspects of illegal immigration, ranging from the numbers involved to the costs and benefits of the movement. Illegal immigration is important in relieving unemployment in Mexico, Central America and the Caribbean. Closing this "safety valve", Vialet writes, raises serious foreign policy problems. On the other hand, she observes, those most concerned with the effect of undocumented workers on the U.S. labor market are most likely to push for measures to curb the flow. Complicating the issue, Vialet writes, citing the work of labor economists Clark Reynolds and Michael Wachter, is the possibility that there may be a shortage of U.S. workers in the 1980's while Mexico and other countries continue to have large numbers unemployed. Vialet believes a recasting of U.S. immigration policy is likely during the 1980's, with equal weight being given to the two hemispheres and to foreign and domestic considerations.

REGIONAL AND COUNTRY STUDIES

THE UNITED STATES AND CENTRAL AMERICA

By Richard Millett*

Summary

After decades of relative neglect, Central America has recently become the focus of considerable attention and concern by those involved with United States-Latin American relations. Although the economic and even the strategic significance of the area is quite limited, it has taken on a high symbolic value as forces on the radical left seriously threaten, for the first time in this century, traditional United States hegemony.

Political violence and foreign involvement in internal affairs is nothing new in Central America. Indeed, armed force and foreign influences have more often than not been the determining factors in political developments. What has changed, however, is the nature of these forces. Internally, the current conflicts no longer pit sectors of the armed forces and traditional ruling elites against each other. Instead, emerging radical forces are striving to completely overturn the existing order, replacing it with a socialist state. Important elements of the dominant Roman Catholic Church, of organized labor and even sectors of traditionally moderate Social Democratic and Christian Democratic parties have supported this effort. On the international scene, traditional United States dominance is being challenged not only by Cuba, but also by the growing regional involvement of Mexico, Venezuela and Western Europe.

The key to this change was the 1979 Nicaraguan revolution which, after almost a year of virtual civil war, ended the 43 year rule of the Somoza family. The Marxist-influenced Sandinista Liberation Front (FSLN) since then has moved the nation steadily to the left in both domestic and international affairs.

Encouraged by Nicaragua's revolution, the Salvadoran left launched an all-out political and military effort to topple the mixed civilian-military junta in that nation. While El Salvador's government responded to this threat with a mixture of reforms and force, Guatemala's military rulers seem determined to defeat the growing insurgency in their country by force alone.

Prospects are not quite so unfavorable in the rest of the region. A slow process of return to civilian rule is underway in Honduras, but to date no faction has shown a real capacity for dealing with that nation's massive social problems. Recent elections in Panama show serious weakness in the ruling party, but relative stability has been

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maintained since the ratification of the Canal Treaties. Costa Rica continues its tradition of relative democracy and stability despite rising economic problems. In all three of these nations a continued failure to deal adequately with serious economic weaknesses and mounting pressures for social reforms could produce a dangerous deterioration in political stability in the coming decade.

Despite considerable attention and effort by the United States in recent years, violence in the region has continued to increase and no stable, effective moderate alternative to the radical left has developed. The middle has actually lost strength in Guatemala, El Salvador and Nicaragua over the past three years. Continuing polarization, suspicion of United States motives and endemic weaknesses will all pose serious obstacles to the Reagan administration's efforts to develop an effective Central American policy.

Policy options in Central America seem very limited. The heritage of suspicion as a result of past policies makes it difficult for the United States to serve as a mediator between governments and the left. Withdrawal from the region or at least from the most troubled nations would produce severe criticism in the United States. Direct intervention would be even more unpalatable. Support for an OAS peacekeeping force is probably unobtainable. Attempting to restore stability through economic and military assistance would be costly and might still prove ineffective. What may be needed is a country by country approach, coordinated with other democratic nations and conditioned by pragmatic realities, not ideological presuppositions.

Introduction

From the CIA-sponsored overthrow of the left-leaning Guatemalan administration of President Jacobo Arbenz in 1954 until the inauguration of President Jimmy Carter in 1977 the United States had given little serious attention to the Central American area. Except for disputes with Panama over the future status of the Canal Zone, American interests seemed limited and secure. Investments were limited, exports from the region were predominately agricultural and easily obtainable elsewhere, and even Central America's geo-political importance seemed to be in decline. Beginning with the announcement of the signing of a new Canal Treaty with Panama, however, interest in and concern about the six small republics between North and South America have reached the highest levels in half a century. Revolution in Nicaragua, civil conflict in El Salvador and escalating guerrilla activities in Guatemala have all contributed to transforming this part of the world from a neglected backwater into a major focal point of United States relations with Latin America.

I. Background to the Current Crisis

The Central American region covers over 203,000 square miles and includes six independent nations: Guatemala, El Salvador, Honduras, Nicaragua, Costa Rica, Panama, and the self-governing British enclave at Belize. The population of over 21,000,000 is growing at a rate of approximately 3 percent per year. Over half of these people still live in rural areas and agriculture dominates both the domestic and export economies.

During the first years of independence, 1823–1838, Central America, excluding Panama, was united into a single nation. Since the break up of the original confederation, numerous efforts have been made to revive the Central American union, but with limited success. In 1958 the five northern republics began the formation of a Central American Common Market to promote the economic development and integration of the region. The Common Market's first decade was relatively successful, but political events since then have effectively halted further progress towards integration.

During the early years of independence, Great Britain was the dominant external economic and political power in Central America. Control of the area around the port of Belize was expanded, the colony of British Honduras was established and, for a time, efforts were made to exercise British sovereignty over the Bay Island of Honduras and the Atlantic Coast of Nicaragua. United States' interests became important with the discovery of gold in California in 1848 and the subsequent use of transit routes across Nicaragua and Panama by thousands of frantic gold seekers. In 1850, the United States and Great Britain concluded the Clayton-Bulwer Treaty, providing for joint control over any future canal route across Central America.[1]

A few years later a Tennessee adventurer named William Walker, with a handful of armed North American followers, installed himself as President of Nicaragua. A combined Central American army, with some support from the United States, the British and Cornelius Vanderbilt, whose transit routes were threatened by Walker, finally ended this adventure in 1857. In 1860, an unsuccessful attempt to revive this project led to Walker's execution in Honduras. Despite official American opposition, strong Central American suspicions of U.S. interests and operations in their area can be traced to this episode.

American economic interests in Central America expanded in the 1870's when Minor Keith of Boston began banana cultivation in Costa Rica. In 1899 he incorporated the United Fruit Company which, with its rival the Standard Fruit Company, became the region's dominant economic and, at times, political power. Strategic interests in the area also increased with the expansion of U.S. power and territory in the Caribbean following the Spanish-American War.

This led to a revival of interest in trans-isthmian canal projects. In 1901 the Hay-Pauncefote Treaty with Great Britain ended the restrictions of the Clayton-Bulwer Treaty, making possible U.S. control over any canal. At first, it appeared that a canal would be constructed across Nicaragua, but in 1902 Congressional sentiment switched to favor a Panamanian route. A treaty was negotiated with Colombia, which then controlled Panama, but failed of ratification in the Colombian Senate.

[1] For details on these and related negotiations see Mary W. Williams, *Anglo-American Isthmian Diplomacy, 1815–1915* (Washington, D.C., 1916).

The Panamanian Catalyst

Angered by this, President Theodore Roosevelt gave his support to a revolution which separated Panama from Colombia. A new agreement, the Hay-Bunau-Varilla Treaty, was rapidly concluded with the Republic of Panama and ratified by both sides. From its inception Panamanians were bitter over several aspects of this treaty which no Panamanian citizen helped negotiate and which was considerably more advantageous to the United States than was the earlier treaty with Colombia.

As construction of the Panama Canal progressed, U.S. interest in Central America grew. Commercial as well as strategic interests in the region were increasing in the early years of this century with investments in mining and lumbering in addition to bananas and with private U.S. banks making loans to several governments.

Major concern focused on conditions in Nicaragua where General Jose Santos Zelaya ruled. A series of events strained relations, including rumors of possible discussions with Japan over construction of a trans-oceanic canal, negotiations with British rather than U.S. banks for a new loan, and, finally, the executions of two American citizens during an uprising against Zelaya. Diplomatic and military pressures forced the Nicaraguan president to flee to Mexico, inaugurating a period of political instability. In 1912, to prevent supporters of the former President from regaining power, the United States launched a major intervention, defeating forces of the Nicaraguan Liberal Party. A small force of Marines remained in Nicaragua until 1925 to discourage further uprisings. Dependent on American support for its survival, the regime of President Adolfo Diaz hurriedly concluded the Bryan-Chamorro Treaty, giving the U.S. exclusive rights over any future canal construction.

The 1920's and 1930's

United States influence over Central America reached a peak during the following two decades. Diplomatic and economic pressures helped topple governments in Guatemala and Costa Rica. U.S. government and United Fruit Company influences became the dominant political factors in Honduras. Marines were stationed in Panama's Chiriqui Province from 1917 to 1919. After World War I a Special Service Squadron of Navy cruisers based at Panama provided further military support for U.S. policy.

The prevailing situation was summed up in a January 1927 memorandum by Under Secretary of State Robert Olds which noted:

> Our ministers accredited to the five little republics stretching from the Mexican border to Panama . . . have been advisors whose advice has been accepted virtually as law. . . . We do control the destinies of Central America and we do so for the simple reasons that the national interest absolutely dictates such a course. . . . Until now Central America has always understood that governments which we recognize and support stay in power while those which we do not recognize and support fall.[2]

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[2] Confidential memorandum by Under Secretary of State Robert Olds, Jan. 2, 1927, State Department Decimal File, Record Group 59, National Archives, Washington, D.C. 817.00/4350.

Marines returned to Nicaragua in 1926 when another civil war broke out in that nation. In an effort to restore peace, the United States forced both sides to disarm, undertook a commitment to supervise Nicaraguan elections, and trained and equipped a new, combined military-police force known as the *Guardia Nacional*. One General, Augusto Cesar Sandino, resisted these arrangements, launching a five and a half-year guerrilla warfare compaign against the Marines and the *Guardia*.

The 1930's saw considerable changes in U.S. policies toward Central America. Unable to subdue Sandino, the Marines left Nicaragua in 1933, turning over command of the *Guardia Nacional* to an English-speaking politician, Anastasio Somoza Garcia. Within four years, Somoza had Sandino murdered, overthrew Nicaragua's President and installed himself in power, inaugurating a family dynasty that would last until 1979. In El Salvador, efforts to bring down the government of General Maximiliano Hernandez failed, leading to an abandonment of U.S. policy of recognizing only legally elected governments. In 1936 a major revision of the Panama Canal Treaty increased the annual payment to Panama and removed a few of the most disliked aspects of the original treaty.

The Post World War II Period

During World War II every Central American nation declared war on the Axis powers, receiving in return U.S. military aid and training. The post-war era saw Central America rapidly relegated to a marginal position in U.S. foreign policy as pressures generated by the Cold War and the Korean conflict occupied our attention. The major exception to this pattern was Guatemala where U.S. fears of communist influence led to increasingly strained relations. Arms were sent to Honduras and Nicaragua and, in 1954, a CIA-organized and equipped exile force succeeded in overthrowing Guatemala's government.

In 1955 the United States and Panama concluded another revision of the Canal Treaty, again increasing the amount paid to Panama and placing additional limits on U.S. operations within the Canal Zone. Panamanian grievances continued, however, especially those surrounding claims to titular sovereignty over the Zone, including the right to fly the Panamanian flag. These issues produced a series of conflicts, culminating in the January 1964 riots which took the lives of twenty Panamanians and four U.S. citizens. Relations between the two nations were broken for several months and were only renewed following a U.S. agreement to negotiate an entirely new canal treaty.

Most of Central America remained closely aligned with the United States during the 1960's, usually supporting American positions in the United Nations and the Organization of American States. Guatemala and Nicaragua even provided bases for the U.S.-sponsored 1961 Bay of Pigs invasion in Cuba. Less dramatic, but of at least equal significance was the growth of American investment in the region during this decade, a trend encouraged by the development of the Central American Common Market.

The Rise of Violence

Violence, at times supported by Cuba, plagued much of Central America during the 1960's. Guerrilla groups were active in Nicaragua and Guatemala, with their activities in the latter nation taking the life of a U.S. Ambassador. In 1969 war between El Salvador and Honduras disrupted the Common Market and damaged the economies of both nations. Pressure from the United States and the O.A.S. ended the fighting, but could not restore amicable relations between the two nations.

Conditions continued to deteriorate during the 1970's. The military dominated politics everywhere except in Costa Rica, often maintaining its control through blatant electoral fraud. Opposition to this situation grew steadily, especially in El Salvador and Nicaragua where important elements of the Roman Catholic Church began to protest violations of human rights and call for basic social and political reforms. A series of natural disasters, notably earthquakes in Nicaragua and Guatemala and hurricanes in Honduras, added to the region's problems. Finally, Guatemala revived its long-standing claim to Belize, adding another potential conflict to the tensions already increasing in that region.

In the meantime, some progress was being made in the long-stalled negotiations and an agreement on basic principles was signed in 1974 by Secretary of State Kissinger and Panamanian Foreign Minister Tack. By late 1976 political conditions in Central America were clearly deteriorating, but U.S. policy remained basically unchanged from the levels of low interest, little aid, and support for the status quo which had prevailed for over twenty years.

II. The Carter Administration and Central America

When President Carter took office there was little expectation that Central America would emerge as the primary area of concern in his administration's dealings with Latin America. Preoccupations over the region increased steadily, however, during the President's term in office.

Initial concerns centered on Panama and the necessity of completing negotiations for the canal treaty. Accordingly on August 10, 1977, agreement on two new treaties was announced. Formal signing took place the following month at a ceremony attended by most of Latin America's heads of state. The treaties provided for recognition of Panamanian sovereignty over the Canal Zone and the establishment of Panamanian jurisdiction over the area following a transition period. Operational control over the canal would be transferred to Panama on December 31, 1999. Until then, actual operations were to be managed by a new U.S. government agency, the Panama Canal Commission, with a nine member board, five of whose members would be United States citizens. Until 1990 the chief administrator would be a U.S. citizen with a Panamanian deputy, but in the 1990's these roles would be reversed.

A separate treaty on the Permanent Neutrality and Operation of the Panama Canal provided for the permanent neutrality of the Canal and guaranteed expeditious passage to all United States "vessels of war and auxiliary vessels." Considerable opposition developed in the Senate over the vagueness of parts of this treaty, leading to the announcement in October 1977 of a joint Statement of Understanding by President Carter and Panama's leader, General Omar Torrijos, guaranteeing to both nations the right to "defend the Canal against any threat to the regime of neutrality," and also "the right to act against any aggression or threat directed against the Canal or against the peaceful transit of vessels through the Canal." Furthermore, it specified that, in case of emergency, U.S. or Panamanian naval vessels seeking to transit the Canal would have the right to "go to the head of the line." [3]

Announcement of the terms of these treaties produced strong criticism from those who believed that the United States should retain the Canal Zone and sole jurisdiction over Canal operations. Allegations of Cuban-Communist influence within the Panamanian government were raised in efforts to defeat the treaties. The current economic and strategic significance of the Canal also became a subject of considerable dispute. The Joint Chiefs of Staff testified before the Senate Foreign Relations Committee that the treaties would in no way jeopardize our security, but several retired officers presented contrary testimony. As 1977 came to an end, the fate of the treaties seemed much in doubt.

The ratification process in Panama was much quicker. In late October 1977, a national plebiscite had returned a better than 2 to 1 majority in favor of ratification. However, conditions and reservations added to the treaties during debate in the U.S. Senate began to threaten Panamanian support for the agreements. Most significant was a reservation presented by Senator Dennis DeConcini of Arizona which specified the right of the United States to use military force to insure transit rights through the Canal. Urgent efforts by the administration finally succeeded in adding another reservation in a form acceptable both to the Senate and to Panama. On March 16, 1978, the Senate approved the Neutrality Treaty by a vote of 68 to 32 and on April 18 approved the Panama Canal Treaty by an identical vote. The exchange of instruments of ratification took place in June 1978, but did not become effective until April 1, 1979. The two treaties took effect six months later, on October 1, 1979.

Even after Senate ratification, there was a hard-fought battle, particularly in the House over legislation to implement the Treaty, and lawsuits questioned the legality of the entire process. In addition, a series of problems delayed the confirmation of U.S. appointments to the new Panama Canal Commission until early 1980. By the summer of 1980, however, major issues concerning the canal seemed, at least for the moment, to be settled.

The rest of Central America attracted limited attention during the Carter administration's first year. However, human rights concerns did lead to some pressure for improvements in conditions in Guatemala, El Salvador, and Nicaragua. In the first two cases, the major

[3] The text of the treaties as originally signed, the Statement of Understanding and numerous supporting documents are included in an October 1977 State Department Publication, *Panama Canal Treaties Information*. The final treaties, with all amendments and reservations, are in two volumes issued by the Organization of American States in 1979 as publication No. 57 in the Treaty Series.

apparent results were attacks on U.S. policy and termination of existing military assistance agreements by the Guatemalan and Salvadoran Governments. The Somoza dictatorship in Nicaragua, more concerned with the image of U.S. support, made minor cosmetic concessions, but resisted pressures for substantive reform.

Attention to Nicaragua dramatically increased following the January 1978 murder of opposition leader Pedro Joaquin Chamorro, publisher of the conservative daily, La Prensa. With mass demonstrations and general strikes against the Somoza regime, President Carter took a personal interest in matters relating to that nation, calling for an end to press censorship, seeking guarantees of expanded political freedoms, and personally deciding on questions involving military sales or training. Again, Somoza made apparent concessions in response to U.S. pressures, receiving in return a letter from President Carter expressing appreciation for the perceived improvements in human rights.

The August 1978 seizure of Nicaragua's *Palacio Nacional* by guerrillas of the Sandinista Liberation Front (FSLN), followed by the outbreak of virtual civil war as FSLN units seized several of the republic's major cities, produced an abrupt shift in U.S. policy. Initial efforts by the U.S. to promote a cease-fire and begin negotiations over the replacement of General Somoza as Nicaragua's President were ignored. Once his troops had regained control of the cities, however, the Nicaraguan dictator did proclaim a limited political amnesty and accepted proposals for political mediation by a three-nation team sent by the Organization of American States (OAS).

The Dominican Republic and Guatemala joined with the United States in making up the mediation team, but the dominant role of the United States was recognized by all Nicaraguans. Initial expectations were that an arrangement would be worked out for replacing the Somoza administration with a relatively broad-based, moderate-controlled regime, that the military would be purged and reorganized, and that some form of international supervision would be exercised over subsequent Presidential elections. In many ways this formula paralleled that employed by the United States and the OAS in the 1965 Dominican Republic crisis.

Mediation efforts in Nicaragua proved unavailing. Efforts to arrange a plebiscite to determine General Somoza's continuance in the presidency encountered a series of road blocks set up by the Nicaraguan government. Concessions to these objections split the opposition, causing those on the left to withdraw from the mediation. Efforts to work out a compromise between Somoza and his more conservative opponents continued until January 1979 when the mediation finally collapsed.

Placing most of the blame for failure on Somoza, the Carter administration responded by withdrawing the Peace Corps and the U.S. Military Mission, suspending most aid projects and reducing the staff at the U.S. Embassy. The upshot was the discrediting of the moderate traditional opposition in Nicaragua and a rapid growth in FSLN strength. Other Latin nations, notably Venezuela and Panama, also increased their support of efforts to topple Somoza.

In March, U.S. Ambassador Mauricio Solaun returned to the United States and a few weeks later resigned his position. Lawrence Pezzullo, then serving as Ambassador to Uruguay, was selected as Solaun's replacement. At his own suggestion, Ambassador Pezzullo was instructed not to present his credentials to the Somoza regime and to increase pressures for a change in government.

Meanwhile, conditions in Nicaragua steadily worsened. By late May, when the Sandinistas launched their final offensive, the economy was on the verge of collapse. Somoza's defenses began to crumble as fighting spread rapidly. In June, an emergency meeting of the OAS turned down a U.S. proposal for sending a peace-keeping force to Nicaragua, but adopted an Andean group resolution calling for Somoza's ouster and the establishment of a new government including the FSLN.

The United States at that point established direct contact with the FSLN and with the provisional government. At the same time, efforts directed to the FSLN provisional government to give a greater share of power to moderates and conservatives achieved little success. Somoza, on the other hand, was ultimately persuaded to turn power over to an interim regime on July 17. This arrangement, designed to salvage part of the old army, fell apart when Somoza's hand-picked successor announced he would continue the fight against the Sandinistas. Strong U.S. pressure, rapid disintegration within the government's forces, and continued Sandinista advances quickly ended this effort. On July 19, 1979, the FSLN took control of Nicaragua.

Despite the FSLN's long history of Marxist influence and Cuban support, the Carter administration was determined to establish good relations with Nicaragua's new rulers, hoping in the process to promote political and economic pluralism and limit Cuban and Soviet influence. Emergency aid was provided, and a bill for an additional $75 million in reconstruction aid was introduced in the Congress. A series of problems, however, held up passage of this bill, undercutting the Carter administration's efforts at gaining credibility with Nicaragua's new government. At the same time, growing radical strength within the Nicaraguan government and accusations of its support for uprisings elsewhere in Central America further complicated relations.

While the United States was preoccupied with events in Nicaragua, internal violence had escalated steadily in El Salvador. By the fall of 1979 the military government of General Carlos Humberto Romero seemed to be losing control of the situation. Encouraged by the United States, a group of junior officers staged a coup and installed a mixed junta of officers and moderate-left politicians. Disturbances continued to spread, leading to the collapse of the first junta and the formation of a second with Christian Democrats assuming the civilian roles. Strong support by the Carter administration helped prevent a threatened right-wing counter coup in February 1980 enabling the junta to issue a sweeping agrarian reform law. Nevertheless, violence continued, claiming the life of the nation's Archbishop, Oscar Arnulfo Romero, in March.

Growing violence within Guatemala also concerned the Carter administration in early 1980, and relations with that nation began to show signs of considerable strain. Ambassador Frank Ortiz made efforts to persuade Guatemala's government to halt the growing slaughter of moderate politicians and labor leaders, but his efforts proved unavailing. Relations with Guatemala reached a low point when Ortiz was recalled and George Landau was nominated to replace him. The Guatemalans praised Ortiz for at least trying to understand their situation, bitterly attacked President Carter and Assistant Secretary Bowdler and refused to give formal acceptance to Landau's nomination. There was even discussion in Guatemala's Congress of severing relations with the United States, but the Lucas administration refused to go this far, evidently hoping that a change of administration in Washington would produce a more acceptable nomination and an altered policy.

Somewhat more successful were relations with Honduras. Its military ruler, General Policarpo Paz Garcia, visited the United States in early 1980 and subsequently pledged a return to civilian rule and reforms that would broaden participation in the political process. Liberal Party victories in the April 1980 elections for a constituent assembly gave some credence to these pledges. Despite this hopeful development, overall prospects for U.S. policy in Central America in the late summer of 1980 were not bright. Marxist influence in Nicaragua, continuing civil conflicts in El Salvador and Guatemala, and major economic problems throughout the region with no signs of rapid resolution posed serious dilemmas for U.S. policy makers.

Under the Carter administration, the basic thrust of U.S. policy had been to support moderate democratic reform elements, such as Christian Democratic parties, as the main vehicle for reducing human rights violations, promoting economic growth and undercutting the appeal of the radical left. Events in the past two years in Guatemala, El Salvador and Nicaragua, however, have tended to discredit, marginalize or even destroy moderate leadership. To date, Washington has found no truly effective way to deal with this growing polarization. Continued failure in this area could leave the United States with few viable alternatives other than acceptance of the spread of hostile, radical regimes throughout Central America or the support of some sort of military intervention to salvage unpopular military governments. Either course would involve grave political risks.

III. The Current Situation

Guatemala

Guatemala's population, approximately 7,000,000 in mid-1980, is the largest in Central America. Nearly half of these are Indians, speaking a variety of languages, often living at a subsistence level, and traditionally having little influence over national politics. Guatemala has a total area of 42,042 square miles, but population is very unevenly distributed throughout this area. Some of the central highlands areas are severely overpopulated, while the northern tropical Department of El Peten is very thinly settled. Guatemala's population is 69 percent rural.

Until recently, Guatemala had been experiencing relatively steady economic growth, with the gross domestic product per capita reaching $880 in 1978. There were, however, huge variations in the distribution of this income, with the figure for the rural population as late as 1975 being estimated at $89. Land distribution aggravates this problem with 26 percent of the rural population owning no land and nearly 90 percent living on plots too small to provide minimal family needs.[4]

Both health and educational standards are quite low. Infant mortality runs at 77 per 1,000, and many of the leading causes of death are directly related to the inadequate nutritional level of the population. Few Guatemalans complete more than a few years of elementary school, and over half the adult population is totally illiterate. Inadequate housing, a problem compounded in urban areas by the 1976 earthquake, is another major problem.

Guatemala's economy is heavily dependent upon agriculture. There was relatively steady growth in industry during the 1960's and 1970's. but recent disruptions in trade within the Common Market, where Guatemala had always enjoyed a very favorable trade balance, a severe decline in construction, and a sharp decline in foreign investment have combined to end this expansion. Coffee accounted for over half the total value of agricultural exports in 1977, followed by cotton, sugar, beef, cardamcm (an aromatic seed used as a spice and in medicine) and bananas. Of these exports, about 39 percent went to the United States. The U.S. provided 31 percent of Guatemala's 1978 imports, making it the U.S. largest customer in Central America.[5] Tourism, especially from the United States, was also a significant source of income, but this, too, showed a significant decline in early 1980.

Despite the decline in foreign investment and the beginnings of capital flight in recent months, Guatemala retains by far the largest international reserves in Central America and has the second lowest external public debt. This position is maintained by extremely conservative budgetary policies, by relatively high coffee prices in recent years, and by a rapid growth in domestic petroleum production. Guatemala, alone in Central America, is potentially self-sufficient in this vital commodity and has even begun to export small quantities to the United States.

Recently Guatemala's political problems have overshadowed its economic difficulties. Internal violence and military domination of politics have been a part of the Guatemalan political scene for years. A leading authority on Guatemala has observed that "violence and the potential for violence are created by a combination of the loosening of social cement, and the politics of demobilization: thousands of individuals are without access to economically and psychologically satisfying relationships which can meet their basic human needs." [6]

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[4] Inter-American Development Bank. *Economic and Social Progress in Latin America, 1978 Report* (Washington. D.C.. 1979). p. 268. Jerry Weaver. "The Development Process in Central America: Problems and Prospects." unpublished manuscrpt prepared for the 1979 State Department Conference on Central Amercia. p. 7.

[5] Report of the U.S. Agricultural Attaché in Guatemala to the Department of Agriculture. Jan. 26. 1979. Report on Economic Trends in Guatemala and their Implications for the United States. issued by the American Embassy in Guatemala. April 1979.

[6] Jerry L. Weaver, "Guatemala: The Politics of a Frustrated Revolution," unpublished manuscript.

The level of internal violence began to escalate in 1979. Several leading reformist politicians, including former Foreign Minister Alberto Fuentes Mohr, were killed by right-wing terrorists. Guatemala's President, General Romeo Lucas Garcia, responded by telling Guatemalans that violence was "an allergy one must learn to live with," while Vice President. Francisco Villagran Kramer observed that "death or exile is the fate of those who struggle for justice in Guatemala."

Guatemala's problems are further complicated by charges of corruption within the government and the military, especially in construction, development in the Department of El Peten, and efforts to expand the nation's lumber industry. There have even been conflicts between the administration and segments of the traditional oligarchy, involving such issues as cement production and taxes on coffee production.

More serious is growing guerrilla strength, bolstered for the first time by the significant participation of Indians. Growing Indian discontent first achieved wide-spread notice with the massacre of 100 Kekchi Indians in the town of Panzos in May 1978. Disturbances have continued ever since, notably in the highland departments of El Quiche, San Marcos and Huehuetenango. There the military has apparently lost control of significant parts of the rural area to the radical EGP guerrillas. In March, a confrontation between Indian women and Army troops in the market town of Nebaj resulted in the machine-gunning of several women and the strong condemnation of the army's tactics by the normally conservative Bishop of El Quiche.

For much of 1979, United States criticism of developments in Guatemala was muted as attention concentrated on events in Nicaragua and El Salvador. Some officials expressed the view that conditions were improving and reports of internal violence were greatly exaggerated. Consideration was even given to a resumption of military assistance and credits. The massacre January 31, 1980, at the Spanish Embassy in Guatemala effectively ended consideration of this possibility. When radicals occupied the Embassy, Guatemalan forces, over the Spanish Ambassador's protests, stormed the building. In the ensuing confusion, most of the rebels and their hostages, including a former Vice President and a former Foreign Minister of Guatemala, lost their lives and the Spanish Ambassador took refuge under the protection of U.S. Ambassador Frank Ortiz.

Since then, U.S. pressures on Guatemala for major changes in political practices and improvements in human rights conditions have increased. In his April 8, 1980, Pan American Day speech, Assistant Secretary of State Bowdler stated that Guatemala must "improve the political process so that it functions freely and democratically," and stressed the need for reforms in social and economic conditions. Failure to deal with these problems, he declared, was responsible for "the high incidence of violence which threatens to polarize and radicalize Guatemalan society." [7]

To date, such appeals have produced no evident positive effects. Guatemalan conservatives have openly denounced what they perceive

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[7] Address by Assistant Secretary of State for Inter-American Affairs William G. Bowdler to the Pan American Society, New York, N.Y., Apr. 8, 1980.

as U.S. efforts to interfere in their internal affairs. Full-page statements were published in local newspapers attacking U.S. policy in general and President Carter and Assistant Secretary Bowdler in particular. At the same time, nothing the Carter administration did ended leftist Guatemalan criticism of the United States or diminished the fundamental suspicion of that sector concerning American intentions and policies towards their nation.

Prospects for better relations are clouded at best. Escalating political violence and polarization—which is what U.S. policy most wants to prevent—is precisely what is taking place in Guatemala today. The inability to control events in El Salvador and Nicaragua has cost the United States credibility with the respective governments and military establishments, while our human rights policies have failed to persuade the opposition of our good intentions. The September 1980 resignation of Vice President Francisco Villagran Kramer removed one of the last moderate voices within Guatemala's government. The government, the military, and the conservative business community seem to expect that the Reagan administration will end pressures over human rights and resume military sales and training. Consequently, future United States efforts to improve the political climate will require convincing the Guatemalan government that concerns over security and subversion do not negate the American commitment to support basic human rights. But even should such a message be understood by the Lucas administration, it is uncertain that it would respond positively to it.

Belize

Present problems and future prospects in Belize, formerly British Honduras, are heavily dependent upon developments in Guatemala which still maintains a claim to much of its territory. Belize contains 8,867 square miles and has a population of nearly 150,000, giving it a population density one-tenth that of Guatemala. Sugar is the dominant export, although exports of clothing have increased in recent years. The predominately black population speaks English and enjoys a much higher literacy rate than does neighboring Guatemala.

Guatemala's claims to the territory, which are based upon British failure to fulfill the terms of a 19th century treaty, were revived in recent years by preparations for granting independence to Belize. While claiming all of Belize, Guatemala has repeatedly indicated that it would be satisfied with a slice of territory in the South which is believed to have large oil deposits. Such a cession, however, is strongly opposed by Belize's ruling Peoples United Party led by George Price. Moreover, the acquisition of this territory by Guatemala would leave her in a weaker position vis-a-vis Mexico, which has claims on her territory.

Guatemala's interest in compromise, however, may be too late. The British seem intent on granting Belize full independence with or without Guatemalan agreement. This would produce a serious internal crisis in Guatemala with clear potential for international conflict. In response to threats of military action by Guatemala, Great Britain has built up its military forces in Belize, while seeking support for Belizean independence in the United Nations. Last October that body, by a vote of 123 to 1 with 7 abstentions reaffirmed Belize's right to self-determination, independence and national integrity. For the first time, even the other Central American nations failed to support Guatemala. The following month a decisive victory by Price's party in Belize's elections represented a further setback to Guatemala's hopes.

In recent months the Guatemalans have shown increased interest in a compromise settlement which would involve abandoning most of their territorial claims. Meetings have been held with British and Belizean officials but to date no final agreement has been reached. As long as those claims remain unresolved, however, British plans to grant the territory full independence remain in abeyance and the potential for conflict persists.

El Salvador

In the Central American area, El Salvador is currently the subject of the most intense United States concern. With a population of over 4,500,000 crowded into an area of only 8,259 square miles it has a population density equivalent to that of Japan. In contrast, however, El Salvador remains a predominantly agricultural nation with nearly 60 percent of the population living in rural areas. Coffee is the dominant export crop, followed by sugar and cotton.

El Salvador's demographic pressures have created a desperate and worsening social situation. About 70 percent of all farms were under two hectares in size as of 1971. A recent study showed that as of 1975, 41 percent of all rural families owned no land at all. Infant mortality rates of 59.5 per 1,000 for the nation as a whole reflects a rate of 120 per 1,000 for the rural poor. National illiteracy is approximately 40 percent, with a much higher average prevailing in rural areas. Of children under 5, about 73 percent are malnourished, and 80 percent of rural and 51 percent of urban housing is considered inadequate.[8]

In 1978, El Salvador had a Gross Domestic Product of $615 per capita. Political disturbances, capital flight, and the near total collapse of foreign investment have undoubtedly seriously reduced that level and have also combined to increase the unemployment/underemployment rate, which was previously estimated at as high as 50 percent. In an effort to prevent total collapse of the financial sector, the Government recently nationalized 50 percent of all banks. Despite such measures, financial prospects remain most precarious.

The political situation is at least as desperate as that in the social and economic areas. Since 1931, El Salvador's politics have been dominated by the military and, with the exception of a single four-month period, only army officers have served as President. Army rule has generally supported the dominance of the nation's economy and society by a small group of wealthy, extremely conservative families.

In 1969 growing migrations by Salvadorans to neighboring Honduras helped precipitate a brief war between those two nations. Over

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[8] Weaver, op. cit., p. 5. Inter-American Development Bank, op. cit., p. 257. United States Agency for International Development, "El Salvador: Agricultural Development—Research, Education and Extension," Capital Assistance Paper, 1977, pp. 19–27.

a hundred thousand Salvadorans were forced out of Honduras, adding to population pressures within El Salvador and raising urban unemployment. In addition, the rupture in relations, still in effect in the fall of 1980, cost El Salvador a valuable market for its manufactured goods and denied it a traditional source of food.

On October 30, 1980, a peace treaty between the two nations was finally signed in Lima, Peru, but even when it goes into effect it will still take considerable time to restore trade to its former level. Encouraged by the oligarchy and angered by civil criticisms of the war's results, the Army used massive fraud to deny victory to the Christian Democrats in the 1972 presidential election.

When elements of the party supported a brief uprising after the elections, the military exiled its leaders and systematically destroyed the Christian Democrats' rural organizational structure. The vacuum thus created was soon filled by much more radical groups.

Colonel Arturo Molina, who became President in 1972, made gestures at reforms, even securing passage of a modest agrarian reform law. In the face of strong oligarchical pressures, however, the law was never implemented. Discontent grew steadily, and in 1977 the Army again used blatant fraud to perpetuate itself in office. Protesters were shot, and U.S. complaints of human rights violations were answered by terminating the military assistance pact.

Growing repression led to a conflict with much of the Roman Catholic Church, most notably El Salvador's Archbishop, Oscar Arnulfo Romero. In response, the government and right-wing para-military groups, such as ORDEN and the White Warriors Union (UGB) began attacks on socially-oriented priests and lay workers. In 1977, 19 priests associated with peasant organizations were expelled from El Salvador, another 12 were imprisoned and two were murdered. A threat was even made to kill every Jesuit in the nation, and several bombs were exploded at the Catholic University. The regime issued a draconian law of Public Order in November 1977 which provided for the imprisonment of clergy and others whom the government believed advocated "doctrines that tend toward the destruction of the social order." It also made criticism of the government or of the social order a crime, even if it was expressed by Salvadoran citizens while they were outside the nation.

While the government moved to the right, mass organizations were forming on the left. Most important was the Popular Revolutionary Bloc (BPR) which claimed over 80,000 members by the end of 1980. It included major peasant groups, labor unions, and the national teachers organization. Similar, smaller coalitions included the United Popular Action Front (FAPU) and the 28th of February Leagues (LP–28). Close to or allied with each of these coalitions was an armed, clandestine group, the Popular Liberation Forces (FPL) associated with the BPR, the Popular Revolutionary Army (ERP) linked to the LP–28, and the Armed Forces of National Resistance (FARN), identified with FAPU.[9] These gained publicity and funds through a series of spectacular assaults on banks and kidnaping of wealthy individuals.

[9] For detailed descriptions of each group see Cynthia Arnson, "Background Information on the Security Forces in El Salvador and U.S. Military Assistance," Resource pamphlet issues by the Institute for Policy Studies (Washington, D.C., 1980).

Growing pressures for government reforms, an easing of repression, and broadening of the regime's political base had few visible effects until 1979. Then, alarmed by the prospect of Somoza's fall, the Romero government made belated efforts at reform. The Law of Public Order was repealed, and overtures were made for talks with the Christian Democrats and other moderate groups. Lack of credibility, compounded by an apparent inability to control elements of its own security forces, brought failure to the government's efforts.

On October 15, 1979, a group of younger officers in El Salvador's army, reportedly encouraged by the United States, overthrew the Romero government and installed a mixed military-civilian junta and cabinet, including representatives of a wide variety of moderate and democratic left groups. The junta promised a broad program of basic reforms: freeing political prisoners, disbanding rightwing paramilitary groups such as ORDEN, promoting agrarian reform, and providing improved benefits for urban workers and slum dwellers.

Much of the left, distrustful of the military and perhaps fearful that successful reforms would undercut their own appeal, continued mass demonstrations, demanding an accounting of all those who had disappeared during the previous two years, urging a further purge of the military's officer corps, and demanding economic concessions, including 100 percent raises for factory workers. To support such demands, various groups occupied government buildings and foreign embassies. Government responses varied from efforts at negotiation and compromise to firing on groups of demonstrators. The junta's ability to control its own security forces came increasingly under question.

On January 3 and 4, 1980, the civilian members of the original junta resigned, charging that the military was unable or unwilling to institute basic reforms and to break its traditional ties with the oligarchy. A new government hurriedly formed with the participation of the Christian Democrats, but a few weeks later continued violence led to a split within that party and the resignation of one of its members from the junta. The Party's most notable leader, Jose Napoleon Duarte, then entered the junta and also took over the Ministry of Economy. Following this step, a series of reforms, including promulgation of an agrarian reform law affecting 80 percent of the nation's rural families, and nationalization of 51 percent of all bank ownership were quickly announced. Opposition to the government from both left and right continued however, leading U.S. Ambassador Robert White to remark at the end of March 1980 that "The level of violence is rising to such a degree that unless this Government can . . . bring it under control, there's danger of civil war." [10]

Convinced that it offered the last hope of averting all-out civil war with the consequent danger of a Marxist take-over, the United States gave quick support for the new regime. But, as pressures from both left and right against the junta mounted, this position became increasingly hard to maintain.

Late in 1979, the Carter administration approved the sale of riot control equipment to El Salvador and reprogrammed $300,000 in mili-

[10] *New York Times*, Apr. 6, 1980, p. E–2.

tary training funds for that nation. With the collapse of the first junta, U.S. involvement became even more direct. Larger amounts of assistance were requested, and a new Ambassador with impressive credentials, Robert White, was appointed. When Ambassador White's confirmation was held up in the Senate, Deputy Assistant Secretary of State James Cheek was dispatched to El Salvador where he stayed for a month. In February he played a major role in averting a threatened right-wing coup.

Considerable opposition to the expanded U.S. role developed from human rights and church groups in both El Salvador and the United States. El Salvador's Archbishop Oscar Arnulfo Romero even wrote directly to President Carter asking him not to provide military assistance which he believed would only intensify repression. The Archbishop's murder a few weeks later in March 1980 and the subsequent riots at his funeral in which at least 31 people were killed and scores wounded only serve to underline the extent to which violence had become the dominant reality of the Salvadoran political scene. Killings for political reasons have occurred every day in the last two years, but three sets of murders stand out. Six leaders of the leftist Revolutionary Democratic Front were assassinated in November 1980. In December, four American women missionaries were killed. In early January 1981, two American advisers and the Salvadoran land reform chief were assassinated in their hotel. By the end of 1980, more than 10,000 persons had died in El Salvador, and according to Christopher Dickey, writing in the Washington Post, "many reliable sources blamed the government forces for most of the deaths." [11]

Under these circumstances, the junta's efforts to halt the rapid polarization of Salvadoran society and to deal with its overwhelming social and economic problems have been largely frustrated. Unable to create an effective domestic power base, the government has had to rely on support from the United States and the military in order to survive. The reliance on the military identified the junta with an institution widely viewed as corrupt, repressive and the basic cause of many of the nation's problems. Efforts to purge officers charged with human rights violations or suspected of support for possible conservative counter-coups are severely limited by the strength of personal ties within the officer corps and by a serious shortage of competent officers capable of dealing with the escalating security threats. As a result, El Salvador's new leaders have never convinced domestic or foreign opinion that they have gained full control over their own armed forces.

The role of the United States in maintaining the Salvadoran junta has been vital. Much of this support has been open. Economic assistance totaled $82 million as of mid-January, 1981, while military assistance in the form of credits under the Foreign Military Sales program amounted to $10.7 million, and training funds added up to $750,000.[12] The United States has also sought to muster international support for El Salvador's government and to counter efforts by the left to discredit the regime.

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[11] Christopher Dickey, "In El Salvador. U.S. Backs Shaky Coalition With Uncertain Prospects," Washington Post, Feb. 25, 1981.

[12] Department of State, Jan. 17, 1981, Statement on Increased U.S. Military Assistance to El Salvador, p. 1.

One result of the crisis in El Salvador was, under the Carter administration, American support for a program of basic reform which, on paper at least, was well to the left of anything previously backed in Central America. At the same time, the Carter administration became increasingly alarmed over the mounting violence, the blame for which it ascribed primarily to the government's own security forces. The murder of the four American women missionaries on December 4, 1980, was the last straw, and it suspended economic and military aid to the junta the following day, pending an investigation of the crime. A U.S. investigating commission was then dispatched to El Salvador. It reported on December 12 that it had found "no clear evidence linking Salvadoran security forces to the murder there of four American women missionaries." [13] On December 17, the State Department announced it was resuming economic aid but conditioned the resumption of military aid on a reduction in violence and on "progress in the investigation of the murders of four American missionaries and six prominent leftist leaders." [14]

Although, according to Ambassador White, the Salvadoran government did not carry out a thorough investigation, nonlethal military aid was resumed on January 14, and lethal military aid was restored on January 17, 1981.

President Reagan's administration has made it clear that it will continue support of the present government and that it is prepared to increase both economic and military aid. The order of magnitude of the economic assistance proposed has ranged up to $100 million, and the *Washington Post* has reported that the administration is thinking of a military assistance program of between $25 and $30 million.[15]

In considering military aid to El Salvador, Congress faces a difficult decision because of the sharply conflicting views on what is happening in that country. The administration is convinced that external support of the guerrilla forces coming primarily from Cuba poses a growing threat of renewed and intensified guerrilla warfare against the government. Ex-Ambassador White holds an opposite view. Testifying before the House Appropriations Committee on February 25, 1981, he insisted that the present government "is perfectly capable of handling the situation without U.S. military aid." [16] He said that the junta had put down the so-called "final" guerrilla offensive in January without "one cartridge coming from the United States." However, White said, an injection of U.S. arms would increase random killings by government forces and bring about a surge of popular support for the extreme left.[17]

White's testimony was attacked by State Department spokesman William Dyess the next day. Dyess said the main disagreement between Ambassador White and the State Department concerned where the immediate principal threat was coming from. "He (White) seems

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[13] K. Larry Storrs and Mary Jeanne Reid Martz, "El Salvador: U.S. Interests and Policy Options". Issue Brief IB 80064, Congressional Research Service, Library of Congress, Washington, D.C., Jan. 9, 1981, p. 22.
[14] Ibid., p. 23.
[15] The *Washington Post*, Feb. 2, 1981.
[16] Ibid., Feb. 26, 1981.
[17] Ibid.

to think it is coming from the right," Dyess is reported to have said, "We think it is from the leftist insurgents." [18]

In essence, the disagreement boils down to differences in judgment about how far the polarization public opinion in El Salvador has progressed. In White's view, the polarization has not gone very far, since the insurgents have not been able to mobilize popular support as yet. On the other hand, the government has failed also to rally support to its side, because its repressive methods are widely perceived to be largely responsible for the slaughter that is going on. More military aid to the government and less prodding by the United States to observe basic human rights, in White's view will encourage the government to become increasingly repressive and will provoke a shift in popular support to the leftist forces.

In the administration's view, the polarization has gone far enough so that the provision of arms from the Communist countries will assure a leftist victory unless the government receives substantial military aid.

Honduras

Honduras has traditionally been the least developed and, in terms of official United States policy, most neglected nation in Central America.

Before the recent violence in Nicaragua and El Salvador, Honduras had the lowest per capita income, $410, in Central America. Illiteracy ran over 40 percent and the average life expectancy of 52.1 years was the lowest in Central America.[19] Coffee and bananas are the dominant exports, with other agricultural products and small amounts of timber and minerals making up most of the balance.

Debt service problems have been less of a problem in Honduras than in much of the rest of Central America, but debt has grown steadily in recent years, especially with the need for external funding for two major projects, a $500 million hydroelectric plant and a $150 million pulp and paper industry. Both projects are scheduled for completion in 1985.[20]

The military has been the dominant force in Honduran politics since General Oscaldo Lopez Arellan overthrew the reformist government of President Ramon Villeda Morales in late 1963. The years since have produced an odd mixture of reform, corruption and conflict. Honduras, too, suffered economic dislocations as a result of the 1969 war with El Salvador, problems which were compounded by severe hurricane damage that year and again in 1974. There have also been minor clashes with guerrilla forces, occasional examples of serious human rights violations and a series of military coups, toppling incumbent presidents in 1972, 1975 and 1978. The 1975 coup ended the domination of General Lopez Arellano, following the revelation of his acceptance of large bribes from the United Fruit Company.

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[18] Ibid., Feb. 27, 1981; Inter-American Development Bank, op. cit., p. 300; January 1980 Report on Economic Conditions in Honduras, prepared by Paul H. Wackerbarth, Economic Officer, United States Embassy, Tegucigalpa, Honduras; Inter-American Development Bank, op. cit., p. 300.

[19] Ibid.

[20] Wackerbarth, op. cit.

The most unusual aspect of the Honduran experience was the effort, under military direction, to promote some degree of social and economic reform, an effort most evident from 1972 to 1978. During this period, the government adopted an ambitious agrarian reform program which benefited 32,000 families, increased public investment in the economy from $47 million in 1970 to $157 million in 1978, and devoted much of this new investment to agricultural development.[21] At the same time, inflation was generally controlled, averaging 6–7 percent. By 1979, prospects for continued economic growth in Honduras were probably the best in Central America.[22]

This economic progress took place with only limited attention and assistance from the United States. Some special funds were targeted for the families which obtained land under the agrarian reform program, and a Military Mission was maintained in Tegucigalpa, though levels of military assistance and credits were reduced steadily during the 1970's. In general, though, the United States ignored Honduras, a situation which did not really change until 1979.

The cause for recent interest is, of course, fear that the revolution in Nicaragua and the continuing violence in El Salvador might serve to destabilize Honduras. The State Department attached $5 million for Honduras to the 1979 request for $75 million in reconstruction assistance for Nicaragua. In September 1979 testimony before the House Foreign Affairs Committee's Subcommittee on Inter-American Affairs, Assistant Secretary of State Viron P. Vaky justified efforts to provide such assistance by praising the Honduran Government's "demonstration of social awareness and its commitment to return that country to constitutional rule," adding that Honduras was "central to the 'bridge-building' process we hope will emerge in Central America." [23] In fiscal year 1980, about $60 million was obligated for economic assistance (including a loan guaranty for housing of $10 million). In fiscal year 1981, about $31 million was obligated for economic assistance, and for fiscal year 1982, A.I.D. has requested about $36 million.

In 1980, the administration obtained a significantly expanded military component, $3,530,000 in Foreign Military Sales credits, $447,000 or an increase of $122,000 in military training (IMET) funds and a proposal for a one-year lease of ten UH–1H helicopters. In 1981, Foreign Military Sales credits will amount to $5 million and training funds to $420,000. In justifying these requests, Deputy Assistant Secretary of State John Bushnell declared that:

> A greater sense of confidence in Honduras of the Government's ability to control its frontiers is key to regional stability. It is important that Honduras not be used as a conduit for the infiltration of men and arms to feed conflicts in neighboring countries.[24]

Serious obstacles to U.S. efforts to promote Honduran stability were posed by growing corruption within the armed forces, with

[21] Weaver, op. cit., pp. 11–12.
[22] Gabriel Siri, "Perspectivas de crecimiento a corto plazo de la economia Hondurena." unpublished manuscript, January 1979.
[23] Statement by Assistant Secretary of State Viron P. Vaky beforethe Subcommittee on Inter-American Affairs, Committee on Foreign Affairs, House of Representatives, Sept. 11, 1979.
[24] Statement by Deputy Assistant Secretary of State John A. Bushnell before the Subcommittee on Foreign Operations, House Committee on Appropriations, Mar. 25, 1980.

consequent public alienation, and by fears that the April 1980 elections for a Constituent Assembly, which would begin the process of a return to civilian rule, would be rigged to favor the National Party. The corruption, symbolized by the Army awarding of a Mercedes Benz and a Rolex watch to most higher ranking officers, remains a problem and has aggravated discontent among younger officers. To date, the United States, while expressing its disapproval of such practices, has found no effective way to encourage their elimination.

Results of the electoral process have been more promising, although in the pre-election stage the Christian Democrats and other parties on the left were barred from the ballot, provoking widespread charges of registration fraud. It was feared that the National Party would be given a clear majority in the Constituent Assembly which would then be transformed into a new Congress that would choose a civilian President to avoid direct elections. Efforts to head off this possibility included a direct letter from President Carter to General Policarpo Paz Garcia, the Honduran Head of State. General Paz Garcia responsed by pledging honest elections and indicating that the military favored later direct congressional and presidential elections with participation by the Christian Democrats and other previously excluded groups. The Liberal Party victories in the April 20 voting give credence to his pledges. Economic and social problems in Honduras remain severe, but U.S. influence and credibility seem higher there than anywhere else in Central America and the possibility of maintaining stability and promoting positive development remains an open option. As yet, civilian political leaders in Honduras have failed to respond to their nation's problems with any sense of urgency. This attitude, combined with growing economic difficulties and continued corruption, could ultimately frustrate U.S. efforts to promote stability.

Nicaragua

Historically and recently, Nicaragua's internal politics have attracted more United States attention than have those of any other nation in Central America. At present our major preoccupation is over regional implications of the 1979 Nicaraguan revolution which brought to power a group of young, militant guerrillas, at least to some degree influenced by Marxism and favorably disposed towards Cuba because of that country's past support.

Nicaragua's area of 53.398 miles, roughly the size of Iowa, makes it the largest nation in Central America, but its population of approximately 2,400,000 gives it the lowest population density. Surprisingly, it also claims the region's highest percentage of urban population, 55.5 percent in 1978.

Even before the devastation produced by the 1978–79 civil war, statistics gave a dismal picture of social conditions in Nicaragua. Even official data acknowledged an illiteracy rate of 47.4 percent, third highest in the Western Hemisphere. Average life expectancy of 55.2 years was the Hemisphere's fourth lowest.[25] Less than 20 percent of the rural population had access to adequate health services, severe malnutrition was rampant, and 84 percent of rural homes had no sanitary

[25] Inter-American Development Bank, op. cit., p. 332.

facilities.[26] Other results of four decades of Somoza family rule included the highest rate of chronic alcoholism in Central America and the highest homicide rate in the world.[27]

Like most of Central America, Nicaragua's economy is heavily dependent upon agriculture which produces 23 percent of the GDP, but employes 42 percent of the economically active population. Coffee, cotton, meat and sugar are the dominant exports. Export agriculture was, until recently, controlling 54.6 percent of the productive land.[28]

The 1978–79 civil war severely damaged the economy. The GDP fell by 5.9 percent in 1978 and by a considerably larger, though still undetermined, amount in 1979. Capital formation declined 46 percent in 1978 and fell even more sharply in 1979. Inflation reached 17 percent in 1978, and the currency was devalued. By August 1979, total material costs of the conflict, including physical damage, loss of production and capital flight, probably amounted to over $1.5 billion. Over two-thirds of the vital cotton crop was not even planted in 1979; cattle herds were seriously reduced; much of the nation's industrial plant was destroyed; and commercial businesses and warehouses were looted. The national treasury was pillaged with only $3.5 million left behind in the Central Bank against an external debt of $1.5 billion. Unless they were refinanced, scheduled payments on this massive debt would require over 60 percent of normal export earnings for the next three years.[29]

The fighting also exacted an appalling human toll. Over 35,000 Nicaraguans were killed, another 100,000 were injured and nearly 10 percent of the population were made homeless. At one point, over 6 percent of Nicaragua's total population were refugees in neighboring nations, and even more forced to seek shelter with relatives or in camps within Nicaragua.[30] In addition, the government had to be completely reorganized and had to deal with a severe shortage of trained, experienced personnel. Most of those with experience had been associated with the Somoza family and had either fled, been arrested or been dismissed from government service.

The new government consisted of a five-member junta and a cabinet made up of a broad range of both moderate and left individuals. It soon became apparent, however, that real decision-making power was controlled not by the junta, but rather by the nine-member FSLN National Directorate, a young, administratively inexperienced and Marxist-influenced body. This dual structure, aggravated by individual differences within the junta and the Directorate, complicates relations considerably. The Cubans found it easier, for both ideological and structural reasons, to deal directly with the Directorate whenever they wished to do so. United States relations with the new regime are fur-

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[26] Weaver, op. cit., p. 4.

[27] Richard Millett, *Guardians of the Dynasty* (Maryknoll, N.Y., 1977), p. 253.

[28] Weaver, op. cit., p. 3. For details see Richard W. Lethander, "The Economy of Nicaragua," unpublished Ph. D. dissertation, Duke University, 1968.

[29] Statistics on the economic costs of the Nicaraguan civil war are compiled from Inter-American Development Bank, pp. 355–7; from Gabriel Siri, "Estado actual de la economia de Nicaragua," unpublished manuscript, March 1979; from Instituto Centroamericano de Administraction de Empresas, "Evaluacion de dános econimicos sufrido pro la industria y el comerico de Managua, Masaya, Crazo y Leon durante in insurrecion armada de Junio/Julio, de 1979" (Managua, 1979); and from data submitted to me by the Nicaraguan Central Bank in September 1979.

[30] Department of State, Agency for International Development, "Nicaragua: Civil Strife," Situation Report No. 3, Aug. 2, 1979.

ther hampered by a heritage of distrust built up by the belief of many of Nicaragua's new leaders that the Somoza regime had been created and, until its last days, supported by the United States.

Despite these handicaps, the Carter administration determined to pursue a policy in Nicaragua of trying to live with the revolution. Direct financial assistance was provided for reconstruction, multilateral grants and loans were promoted; public criticism of the new government's programs and leaders was muted; and other democratic nations, such as Venezuela, West Germany and Costa Rica, were encouraged to support the new government. The hope was that, as a consequence of a friendly and supportive policy, the potential radicalism of the new government might be tempered, its dependence on Cuba and the Soviet bloc avoided; and domestic, economic, and political pluralism preserved. To date the success of this effort has been mixed at best.

Trouble for the Administration's policy developed in both the United States and in Nicaragua. Initially the policy met with some success as several million dollars in emergency aid funds were provided and a parade of high-ranking government and Sandinista leaders visited the United States. The major problem arose as a result of a series of delays and obstacles to a proposed $75 million aid package. Inability to provide this assistance, most of which was designed to help rebuild Nicaragua's private sector, damaged the administration's credibility in Nicaragua. It has also contributed to growing demoralization within Nicaragua's private sector.

Within Nicaragua, problems for the Carter administration came from what was perceived as the leftward drift of the government. In December 1979, major cabinet changes removed some of the moderate representatives and replaced them with members of the FSLN Directorate. Among those posts affected were the key Ministries of Defense and Planning. In March 1980, a high-ranking Nicaragua delegation visited Moscow where a series of agreements were signed providing for trade and assistance; the U.S. response to the Afghanistan situation was criticized; and party-to-party relations between the Soviet Communist Party and the FSLN were established. Finally, in April, the moderate members of the junta, Violeta de Chamorro and Alfonso Robelo, resigned.

Alarm was also expressed in Congress and in the press over the growing Cuban presence in Nicaragua, and the number of Nicaraguans being educated in Cuba. Most of the Cubans were reportedly working with the national literacy campaign or providing rural medical services. Literacy and health had long been targeted by Nicaragua's new leaders as areas of major national concern, and in both cases national resources were clearly inadequate. A massive national campaign, based in part upon an earlier Cuban model, was mounted to eliminate most of the problem during 1980. Language, previous experience, relatively low cost, and ideological sympathy all played roles in Cuba's offer and Nicaragua's acceptance of help for this program. To date the United States has provided virtually no government support to this effort.

In the field of health, U.S. military medical teams did operate in Nicaragua in late 1979. But after 90 days, funding ran out, and they had to withdraw, turning over their work in some areas to Cubans.

Not all Cubans, though, were teachers or medical personnel. Some were active in agriculture, fishing and other areas of the economy. Of greater concern was the strong Cuban influence in the training of the new Army and, after Panama withdrew its mission, in the development of the police.

The May 1980 decision to add two leading moderates, Arturo Cruz, formerly President of the Central Bank, and Supreme Court Justice Rafael Cordoba Rivas to the junta calmed some fears as did the reopening of the independent *La Prensa*, which was nearly as outspoken in its criticism of the new government as it had been of the Somoza government. Neverthless, fears among the private sector over long-range government policies and growing Cuban influence remain. The demand of the traditional political parties for municipal elections in the near future is also a potential source of conflict. All of this complicates United States efforts to keep a low profile while trying to encourage pluralist trends within the revolution. The Carter Administration remained publically committed to a policy of supporting Nicaraguan reconstruction and abstaining from interference in its internal affairs.

The heritage of past relations and the ideological presuppositions of many of the Sandinistas have always made this a difficult position to maintain. Evidence that left-wing guerrillas in El Salvador were being supplied arms from Nicaragua led the United States on January 22, 1981, to suspend payments to Nicaragua from the $75 million economic support fund. Currently, some grant aid to the private sector and to the Red Cross is still being given, but the remaining $15 million was suspended in April 1981 by the Reagan administration. An economic assistance package amounting to about $20 million has been proposed for fiscal year 1982, but it is unlikely to be approved unless the Administration is convinced that arms shipments from Nicaragua to El Salvador's guerrilla forces have definitely ceased.

Costa Rica

In contrast to most of the region, Costa Rica has a long tradition of political democracy, individual freedom and respect for human rights. Following its 1948 civil war, Costa Rica even abolished its army, replacing it with a small militarized police force, the *Guardia Civil.* On the political front only once since 1948 has the party in power won two consecutive presidential elections.

With an area of 19,653 square miles and a population of over 2,250,000, Costa Rica is in both area and people Central America's second smallest independent nation. (Only El Salvador has a smaller land area, 8,200 square miles while only Panama has a smaller population 1.9 million). Its gross domestic product of $1,099.1 per capita in 1978 and its 89.8 percent literacy rate are the highest in the region. Although Costa Rica receives a higher percentage of its GNP from manufacturing (22.3 percent in 1978) than from agricultural (19.2

percent in 1978)[31] agriculture products, notably coffee and bananas, are still the most important exports.

In recent years, Costa Rica has experienced growing financial problems. Inflation, especially in basic foods, has increased markedly since 1974. From 1973 to 1977 the external public debt grew by over 380 percent, rising from $337 million to 1,303 million. International reserves declined sharply from 1975 through 1977.[32] All indications are that these trends have continued ever since.

Financial problems have been further aggravated by a severe decline in the rate of economic growth. Much of this is due to the impact of disturbances elsewhere in Central America, especially those in Nicaragua during 1978 and 1979. These caused disruptions in trade with the rest of Central America, a sharp decline in tourism, and a fall-off in foreign investment, which peaked in 1975.

As demonstrated by the literacy rate, social conditions in Costa Rica offer less problems than in most of Central America. There is more equitable land distribution than in any other Central American country, though many rural families still lack sufficient land to adequately support themselves. Only 14 percent of the nation's urban dwellers are classified as poor, a fact which explains why slum areas, so visible elsewhere, are not nearly so prevalent in Costa Rica. Studies made from 1974–1976 indicated that 12.3 percent of the nation's children suffered from malnutrition, by far the lowest rate in Central America and the only case in which the percentage had declined from a decade earlier.[33]

Costa Rica's political and economic situation has enabled the United States to maintain cordial, usually tranquil relations. In return, the Costa Rican government has generally supported the United States in regional and world forums. In the June 1979 OAS meeting on the Nicaraguan crisis, it was the only Central American nation to join the United States in voting for the final resolutions calling for the replacement of the Somoza regime.

Costa Rica's generally friendly attitude toward the United States may be waning. Growing numbers of Costa Ricans are expressing anger and disenchantment over the meager results of their ties with the United States. The deterioration in economic conditions in recent years threatens their efforts to create a middle-class society and sustain political stability. Since the economic troubles have not produced the violence common to much of the region, the United States has shown little interest in dealing with them. This attitude was reflected by Assistant Secretary Bowdler in a speech on Central America on April 8, 1980, in which he spoke in some detail about conditions in the other four nations, but devoted only one brief, passing reference to Costa Rica.[34]

Specific as well as general issues have also weakened U.S. ties with Costa Rica. In a controversy over tuna fishing rights, Costa Ricans interpreted United States actions as demonstrating that our government was more concerned with the interests of a few California fish-

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[31] Inter-American Development Bank, pp. 227–229.
[32] *Ibid.*, pp. 455 and 457.
[33] *Ibid.*, p. 141.
[34] Address by Assistant Secretary of State William G. Bowdler to the Pan American Society, New York, N.Y., Apr. 8, 1980.

ermen than it was with the well-being and dignity of a small, democratic ally. Failure to provide significant assistance in dealing with the problems created by the massive spillover of Nicaraguan refugees during 1978–79 also produced considerable anger. Many Costa Ricans resent what they perceive as U.S. neglect of their problems and a failure to appreciate the role they could play in promoting political moderation and respect for human rights throughout the region. They see Washington as responsive only to violent crisis and fear that their very real, but manageable economic problems will be ignored until their nation, too, experiences bloody civil conflict.

Despite such problems, Costa Rica is still far from being in a critical condition. The political weakness of the current administration has meant that considerable maneuvering for the February 1982 election has already taken place. Virtually all indications are, however, that these elections will produce no major shifts in domestic or international policies. The challenge for the United States in its relations with this nation is to find a way to help out with its very real social-economic problems before they reach the crisis stage.

Panama

Historically and economically, Panama stands apart from the rest of Central America. Its geographic position, its preoccupation with issues involving the Canal, and its past history have combined to differentiate Panama from the other republics. It is not a member of the Central American Common Market or its Secretariat (SIECA), nor does it participate in the Central American Bank (CABEI). For these and other reasons, the State Department handles Panamanian relations through an office completely separate from that charged with Central American Affairs.

Panama's territory, including the former Canal Zone, covers 29,848 square miles and includes a population of about 1,900,000. The country can be divided into at least three distinct regions. The area around the Canal includes most of the major cities and virtually all the industry; it has long dominated the nation's politics. The region up towards the Costa Rican border, notably the province of Chiriqui, contains the best agricultural land. The land stretching from the Canal to the Colombian border is largely undeveloped jungle and swamp and still represents the major gap in the Pan American Highway.

After Costa Rica, Panama has the region's highest GDP per capita, $1,254 in 1978, and literacy rate, 79.3 percent. Life expectancy, 67.9 years, is also second only to that of Costa Rica.[35] There are, however, wide regional and class variations in income distribution, educational opportunities and health standards. Studies in 1974–76 indicated that 21.5 percent of children under five suffered from malnutrition, an increase of 116.2 percent in just a decade.[36]

Panama's economy is heavily influenced by the United States. Total American investment reached a value of $2.4 billion by the end of 1978. This was nearly three times the combined value of investments in the rest of Central America. The bulk of this investment was con-

[35] Inter-American Development Bank, op. cit., p. 342.
[36] *Ibid.*, p. 141.

centrated in trade, finance and insurance.[37] This reflected not only interests directly linked to the canal, but also the growing importance of Panama as a financial center.

U.S. influence is also reflected in trade statistics. In 1977 the United States took 46 percent of Panama's exports and provided 31 percent of its imports.[38] Bananas were the most important export, followed by frozen shrimp.

Like much of the region, Panama faced mounting debt problems during the 1970's. This was aggravated by virtual economic stagnation from 1974 through 1978. By the end of 1977 the external public debt, much owed to private U.S. banks, had reached nearly $1,000 per capita, by far the highest in Central America.[39]

While not producing the bonanza hoped for by many Panamanians, ratification of the Canal Treaties does seem to have had a beneficial economic impact. Economic growth resumed in 1979, and exports for the first half of the year increased 15 percent over the same period in 1978. The U.S. Department of Commerce attributed this change to "the implementation of the Canal Treaties," and to "renewed Panamanian efforts to attract foreign business." [40]

Since 1968, Panamanian politics have been dominated by General Omar Torrijos, Commander of the National Guard, a combined police and military force. On October 8, 1978, he announced that he was stepping down as Head of State and transferring his power to Aristides Royo who would replace Demetrio Lakas as President. General Torrijos retained his command of the National Guard and is still generally recognized as the dominant power in politics, a fact exemplified when he, not President Royos, made the decision to admit the former Shah to Panama.

Relations with the United States are still dominated by issues related to implementation of the Canal Treaties. Delays in several areas, including confirmation of U.S. appointments to the new Canal Commission, have produced numerous expressions of public concern by Panamanian officials and even led to a sharp exchange of letters between Presidents Royo and Carter early in 1980. In general, though, the transition has gone remarkably smoothly. Joint U.S.-Panamanian police patrols have worked well; Canal operations have continued uninterrupted; and most American employees have stayed on their jobs, although many observers fear an exodus of these employees when current contracts expire.

Several issues remain to be clarified regarding military operations within the former Canal Zone. One of the more significant is the future status of the U.S. Army School of the Americas where much of our training of Latin American officers is carried on. To date, reductions in Congressional appropriations have done more to limit the school's operations than have any actions taken by the Panamanian government. This could change, however, as Panama recently indicated serious reservations concerning a U.S. project to train Salvadoran officers at the school.

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[37] U.S. Department of Commerce, *Survey of Current Business*, vol. 59, No. 8 (Aug. 1979), p. 27.

[38] U.S. Department of Commerce, "United States Foreign Trade Annual, 1972–1978," *Overseas Business Reports* (August 1979), p. 30.

[39] Inter-American Development Bank, op. cit., p. 457.

[40] U.S. Department of Commerce, "World Trade Outlook for Latin America," *Overseas Business Reports* (April 1980), p. 4.

Other issues offer at least the potential for future problems. One of these involves charges of Panamanian involvement in international drug trafficking. Another was General Torrijos's continuing desire to play a larger role in third-world affairs in general and Central American/Carribean developments in particular. His strong support for the FSLN during the Nicaraguan civil conflict and publicized offers to help defend Costa Rica against Nicaragua created some tension at the time. This became apparent during the June 1979 OAS meetings.

Until the recent sudden death of Torrijos, the regime appeared to be relatively secure, although it showed signs of losing popular support during the 1980 fall elections. Any regime change, especially towards the left, could re-open numerous issues related to the control and operation of the Canal and its associated military bases. With respect to relations with the United States, these appear to be generally better than they have for some time, though how long this will be true is uncertain.

Interregional Prospects

Regional integration in Central America is obviously dependent upon relations between the nations of the region. In the current climate of suspicion and conflict, prospects in this area are clouded at best. Regional discord has been so severe that, for a time in 1979, only Guatemala had relations with all the other nations of the region.

Political alignments within Central America have changed remarkably in the last two years. At the start of 1978 the Northern four nations, Guatemala, El Salvador, Honduras and Nicaragua, were all under the control of conservative-military-dominated regimes. The major problem was the still unresolved conflict between Honduras and El Salvador, but even that seemed on the verge of resolution. Today, Guatemala alone remains a bastion of hard-line, right-wing rule. The nations of the region are suspicious of each other, fearful of external interference in their affairs, and deeply divided over future courses of action. The conflict in El Salvador has raised fears of support for one faction or the other by both Guatemala and Nicaragua. The continued presence of several thousand former soldiers of Somoza's National Guard in Honduras keeps relations between Nicaragua and Honduras on edge. Even Costa Rica has been accused of harboring training bases for forces opposed to Nicaragua's government. Prospects for conflict seem to exceed chances for expanded cooperation.

Current conditions make projections based on past data for Central American Common Market trade irrelevant. Two studies published in 1978 take a somewhat optimistic view of prospects for regional integration and its potential significance for Central development, but their major contemporary value is probably as guides to what might be possible if political problems are resolved.[41]

The United States has strongly supported Central American economic integration largely through the Agency for International Development's Regional Office for Central American Programs (ROCAP).

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[41] William R. Cline, ed., *Economic Integration in Central America* (Washington, D.C., 1978). Royce Q. Shaw, *Central America: Regional Integration and National Political Development* (Boulder, Colo., 1978).

ROCAP has helped channel U.S. support to a host of regional organizations including the Common Market. It assists regional educational projects, such as the Central American Business Administration Institute (INAE), promotes research by the Institute of Nutrition in Central American and Panama (INCAP), cooperates with regional efforts to deal with specific agricultural problems such as coffee rust and rising pesticide concentrations.[42]

In the long run, regional cooperation and integration could still be key factors in Central America's development. By encouraging the survival of organizations designed to promote this process and by helping to establish models for regional cooperation in dealing with common problems, United States assistance, handled by ROCAP, remains important.

External Actions and U.S. Options in Central America

The only certainty in Central America's immediate future is the continuance of conflict. The time when the region consisted of a string of obedient client states whose governments were dependent upon United States support for their survival has ended. Today, Venezuela, Mexico, Cuba, Western and Eastern European blocs, and Japan have the potential to compete with the United States for influence in the region. American ability to operate within this changed environment will have an important bearing on relations in the 1980's.

Venezuelan involvement in Central America, both on its own and as a leader of the Andean Group, gained considerable attention during the Nicaraguan civil conflict, but its origins go back several years. Many leaders of Venezuela's *Accion Democratica* took refuge in Costa Rica in the early 1950's, and these ties remained after these leaders returned to power in Venezuela. The nation's other major party, COPEI, is part of the world Christian Democratic movement and has close ties with Central America's Christian Democrats. When El Salvador's Christian Democratic leader, Jose Napolean Duarte, fled into exile after the 1972 elections, he was received in Venezuela, remaining there until his return to El Salvador late in 1979.

The 1974 election of Carlos Andres Perez brought a considerable increase in Venezuelan interest in and economic aid to Central America.[43] He actively supported opposition to Nicaragua's Somoza regime both diplomatically and militarily and sent warplanes to Costa Rica to protect that nation against Nicaraguan government incursions. The 1979 inauguration of Luis Herrera Campins of COPEI as President reflected lowered Venezuelan interest in foreign affairs, but by no means ended involvement in Central America. The Herrera administration still provides aid, supports democracy, encourages regional Christian Democratic parties, and hopes to head off the emergence of radical Marxist regimes in the area. In many ways, these aims parallel U.S. policy goals, but Venezuela's desire to forge an independent foreign policy and the current government's open support of Christian Democratic parties limits the potential for coordinated policies. The U.S. is

[42] For a detailed description of ROCAP's present status and future plans see its "Country Development Strategy Statement. Fiscal Year 1982," issued January 1980.
[43] For details of Venezuelan policies towards Central America through mid-1979 see John Martz, "Venezuelan Policy Towards Central America," unpublished manuscript, 1979.

already suspected of favoring Christian Democratic parties, an attitude resented by other political groups. Under current circumstances, Washington can hardly afford to become too closely identified with a single, usually small minority faction of the political spectrum. One important development under the Herrera administration has been a joint agreement with Mexico to supply most of the Central American nations with petroleum at very favorable terms. This both insures a constant energy supply and reduces the immediate impact of OPEC price hikes on Central America's already shaky economic situation.

Cuba's current role in Central America is the subject of considerable debate. Fidel Castro has never attempted to conceal his support of the Sandinista government in Nicaragua, a position emphasized by his participation in the revolution's first anniversary celebrations. But he has always claimed that the Cuban role is one of assistance, not direction. This assistance is most visible in areas such as health and education in which several thousand volunteers are currently working. The Cuban role in providing political advice, military training, and continuing arms supplies is less evident, though it certainly exists. More controversial are charges of Cuban assistance to guerrilla movements in El Salvador and Guatemala and charges by the Costa Rican government that Cubans have helped foment labor disturbances in Costa Rica. While making no effort to hide its sympathies, especially in the case of El Salvador, Cuba denies charges of direct involvement, but evidence to the contrary has now been compiled by the Reagan administration. Cuba's sale has been in exploiting discontent in El Salvador and Guatemala, however great it is probably true that these areas would be subject to considerable turmoil even if Cuba played no active role.

Mexico's potential role in Central America is difficult to assess. It took a lead in diplomatic moves against General Somoza and, through the ruling Revolutionary Party (PRI), established contacts with the FSLN long before it took power. Since then Mexico has provided aid, including petroleum deliveries at a concessionary price. Mexico has also exerted pressure for reform in both Guatemala and El Salvador and has been critical of U.S. proposals for military aid to El Salvador. Its common border with Guatemala and its interest in the status of Belize insure continued Mexican interest and involvement in developments in Guatemala. The motivation for the growing Mexican involvement in the rest of Central America is subject to varying interpretations. Explanations offered include the traditional desire to demonstrate a foreign policy independent of that of the United States; providing an alternative to Cuban support; and currying favor with Central American revolutionary governments as a means of disarming domestic left-wing critics.[44] How direct this involvement will be and how extensive and successful it will be remains an open question.

Perhaps a portent of future Mexican policy was the clear warning sent by Mexican President Lopez Portillo to President Reagan not to intervene with military force in El Salvador. The Mexican leader predicted that any such action could result in the "Vietnamization of

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[44] Alan Riding. "Mexico Pursues Role of Leader for Carribean Region," *New York Times*, Aug. 20, 1980, p. 8.

Central America," and made it clear that this would have a profoundly negative effect on U.S.-Mexican relations.

The Soviet Union has kept a rather low profile in most of Central America, although charges that its Embassy in Costa Rica is used to coordinate Communist activities throughout the region abound. The recent visit of a high-level Sandinista delegation to Moscow and the agreement to begin direct air service between Moscow and Managua may portend a change in Soviet tactics. Until now, however, the U.S.S.R. has left most contacts with opposition groups in the hands of the Cubans and has placed most direct economic ties and assistance in the hands of Eastern European nations such as the German Democratic Republic.

In an interesting reversal of traditional policy, the United States has recently encouraged greater participation by Western Europe and Japan in Central American affairs. Their share of regional trade has increased significantly in the past two decades. Their official contributions to Central American national and regional development programs have also increased markedly. On the political front, European Christian Democratic and Social Democratic parties have evidenced increasing willingness to support related parties in Central America, but their involvement has been much less public than that of Venezuela. In the case of Japan, the major recent development has been the revival of speculation concerning possible Japanese participation in the construction of a new, sea-level canal.

In most cases, however, the United States' major allies have left responsibility for Central America with the United States. Their reluctance to become too deeply involved stems partly from historical and geographical factors, partly from the low levels of their own interests in the region, and perhaps as much as anything from the extreme difficulty of exercising effective influence under present conditions.

United States options are also limited and, often, not too promising. A return to the open interventionism of the 1920's would have disastrous political consequences both at home and abroad. There is little current evidence of either civilian or military support for any such action.

There is also little backing for a policy of withdrawing from much of the region, especially from Nicaragua, El Salvador and Guatemala, and simply letting events run their course for the next few years. United States strategic and economic interests in the region, except for Panama, it is true, are quite limited. A case could be made that on a cost-payoff basis, continued or increased involvement in El Salvador or Guatemala is unlikely to prove worthwhile, and that it would therefore be logical to cut back our commitments there and concentrate our efforts on more promising opportunities in Costa Rica and Honduras. However, a passive policy risk loss of United States influence not only in Central America, but also perhaps throughout the hemisphere.

A major, well-funded and bi-partisan effort to stabilize the region, to promote economic development, would seem to offer a credible alternative to violent revolution as a means of producing significant social change. Rodrigo Madrigal Nieto, Costa Rican Congressional leader, has long urged just such a policy, a mini-Marshall Plan for Central America.[45] Compared to the total budget, costs would be relatively modest, perhaps a billion dollars a year above current aid levels. Funds would be used to encourage economic growth, fund agrarian reforms, underwrite expansion of health and educational facilities, and provide support for dealing with the massive debt problems plaguing much of the region. The prospects for such a program are extremely dim, given budgetary restrictions, the political unpopularity of foreign aid, and the difficulties in the way of a bi-partisan approach to the crisis in Central America.

While there is no consensus on what policy to follow, there is widespread recognition as to the seriousness of the situation and the mixed results of past policies.[46] There is also a growing fear of a possible domino effect in the region, with the Nicaraguan revolution being the forerunner of victories of the extreme left in El Salvador, Guatemala and, ultimately, Honduras. Luigi Einaudi, then director of policy planning office and of the State Department's Bureau of Inter-American Affairs, in May 1980 declared that "In Central America, a once stagnant order is disintegrating before our eyes." In response, Einaudi urged "not to resist change, but to participate in it in new constructive ways." [47]

"New and constructive" participation in change has, however, been difficult to achieve. Efforts have been hampered by a lack of credibility throughout the region as a result of decades of neglect and of widespread perceptions of an indecisive United States policy during the Nicaraguan revolution. Central Americans are also all too aware of the tendency of successive administrations to be easily diverted from serious attention to the problems of their region by crises in other areas deemed of greater economic or strategic importance. The combination of limited resources, inconsistent attention from Washington, and growing cynicism and fear among moderate democratic leaders in Central America has consistently crippled United States efforts to formulate and execute positive new policy initiatives in the region.

What is left is essentially an effort at crisis management and loss minimization. There is also some effort to enlist private sector assistance in this effort. On April 9, 1980, President Carter inaugurated a program called Caribbean/Central American Action headed by Governor Bob Graham of Florida. The purpose of this ostensibly private venture is to promote private sector interest and participation in the Caribbean/Central American region and to coordinate the efforts of already existing groups working in these regions.[48] In Central America such a program might play a positive role in Costa Rica and perhaps in Honduras and Panama, but it is difficult to imagine it having a serious impact on the other nations. Their situation is currently neither con-

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[45] Rodrigo Madrigal Nieto first advanced this concept in a speech to the April 1979 National Meeting of the Latin American Studies Association in Pittsburgh, Pa.

[46] For examples of bi-partisan support for the analysis see the quotes of Senator Edward Zorinsky (D-Nebraska) and David Durenberger (R-Minnesota) cited in Richard Millett, "Central American Paralysis" *Foreign Policy* (Summer, 1980), p. 114.

[47] Luigi R. Einaudi "Informal Remarks on Central America and the Caribbean" Washington, D.C., May 22, 1980.

[48] "Remarks of President Carter at the Reception for the Caribbean/Central America Action Group," Washington, D.C., Apr. 9, 1980.

ducive to private investment, nor responsive to the person-to-person contacts promoted by this effort.

There is probably no single policy for Central America which can effectively promote United States' interests throughout the entire region. The approach with the greatest possibility of some degree of success would probably be a flexible, pragmatic, country by country approach. In Nicaragua this might mean continued efforts to support the private sector and promote pluralism, while at the same time recognizing Nicaragua's right to run its own internal affairs and doing nothing to exacerbate the Sandinista's fears of possible intervention.

There are virtually no good options left in El Salvador. Combining opposition to an armed take-over by the radical left with encouragement of the existing government to broaden its base of support and actively seeking some peaceful means of resolving the conflict is a most difficult position to maintain, but it may be the best available. What must be made clear is that in the final analysis only the Salvadorans, themselves, can prevent the virtual destruction of their nation.

In Guatemala, it remains to be seen whether the Lucas regime will be any more responsive to suggestions from President Reagan than it was to those from President Carter. There is some evidence that many influential Guatemalans realize the total reliance on force only exacerbates, rather than resolves, their problems. The United States must find some way to promote this concept, but just how to do this and what to offer in the place of violence is subject to considerable debate.

In Panama, Costa Rica, and Honduras the problems are somewhat similar. All three face mounting economic problems, growing challenges from the left and problems of internal leadership. The challenge to the United States in these cases is to demonstrate a genuine, long-range commitment to change while at the same time making it clear that ultimate responsibility for their future rests in their hands, not ours. Projecting a serious concern without combining it with an over-riding paternalism is no easy task.

In his April 8, 1980, speech to the Pan American Society, Assistant Secretary Bowdler summarized the challenge facing United States relations with Central America:

> Central America is in a critical period of its history. Our support for peaceful change can increase the likelihood that more democratic and equitable societies will evolve out of the present crisis. Conversely, our failure to be responsive can only help the enemies of freedom.[49]

The problem is that our efforts to be responsive have consistently been overtaken by events. Speaking on the NBC White Paper, "The Castro Connection," former Secretary of State Kissinger observed:

> . . . what is going on now in Central America is extraordinarily dangerous for us. We have not found a definition of a moderate, democratic alternative in the name of which we can replace the oligarchies and resist the totalitarians. So a process is starting in which we are far behind the power curve and . . . which has spread already from Nicaragua to El Salvador—which is bound to affect Guatemala and certain to have an impact on Mexico which will then be a very grave matter for us.[50]

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[49] Speech by Assistant Secretary of State William G. Bowdler to the Pan American Society, New York, N.Y., Apr. 8, 1980.

[50] Transcript of "The Castro Connection," NBC White Paper, Sept. 3, 1980, pp. 68–69.

The challenge articulated by Bowdler and Kissinger's pessimistic assessment together sum up the necessity for and the grave difficulty of fashioning an effective Central American policy. The amount of effort and resources involved in any such effort would probably have to be larger than those ever previously applied to that region. The dilemma is in determining if, at this late date, these costs still offer enough of a chance of success to outweigh the price of a collapse of United States influence in Central America.

THE UNITED STATES AND THE CARIBBEAN IN THE 1980's

By Abraham F. Lowenthal*

Summary

Recent events and trends in the Caribbean and in the broader international system have caused the United States to focus once again on its relationship with the countries and territories of its "third border." Government officials, the media, the foundations, and scholars have all been rediscovering the Caribbean, as has often happened in United States history.

The 32 contemporary Caribbean entities are remarkably diverse, yet overwhelmingly alike: diverse in culture, language, size, economic and political organization, colonial tradition, economic performance, and international links, but similar in their shared experience with colonialism, poverty, dependence, insularity, fragmentation, overpopulation, and—in almost every case—extensive interpenetration with the United States, especially through the massive immigration of people.

With populations continuing to rise, agricultural productivity declining, industry stagnant, and balance-of-payments disequilibria intensifying, the capacity of Caribbean units to secure equity and growth and to incorporate more employed workers—while preserving democracy and without sacrificing autonomy to a metropolitan power—is being questioned. A key issue for the 1980's will be how the United States responds to this quandary.

In approaching this question, the United States must examine its interests and how they are changing. Traditional concepts of security, economic, and political interests are still frequently asserted, but these should be reviewed in the light of changing technologies, trade and investment patterns, and political alignments. The key United States interest in the Caribbean in the years ahead may be none of the traditional ones, but rather the effect of continued migration from the region on our society.

Four different United States approaches toward the Caribbean are defined and discussed. They differ among themselves regarding the relative degree of attention paid to traditionally conceived concerns and the degree and form of United States involvement though likely to be most effective in protecting United States interests.

The two most likely approaches for the United States in the 1980's are the activist and the developmental strategies. Activists are concerned with immediate impact and with countering Cuba's influence

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by stressing bilateral economic assistance, security programs, economic sanctions against Cuba and economic incentives to those who reject Cuba's influence. Developmentalists would emphasize multilateral aid, long-term regional cooperation and integration, and deeper structural issues in the region.

Proximity, dependence, vulnerability, history, and migration make the Caribbean a special region for the United States. How this country should approach the region in the 1980's is open for debate, but the United States should seek ways to make its considerable impact on the region more consistently positive.

INTRODUCTION

The Caribbean is rising once again on the agenda of U.S. foreign policy.[1]

Various events have caused the United States to renew its concern with the Caribbean: the Nicaraguan Revolution and that proclaimed in Grenada; Central America's intensifying civil strife; Jamaica's drift toward bankruptcy and polarization; Cuba's stepped-up activity in the region; the achievement of formal independence by several Caribbean mini-states and pressure for independence by others; and extending awareness in the United States of the extent of Caribbean migration to this country.

Whatever the reasons, signs abound that increased attention is being paid to the Caribbean. Early in his administration, President Carter determined that the Caribbean deserved priority. Top U.S. government figures—including then-Secretary of State Cyrus Vance, then U.N. Ambassador Andrew Young, and Mrs. Carter herself—all visited the region, and former Undersecretary of State Philip Habib led a high-profile mission there in 1979 to review U.S.-Caribbean relations. The number of foreign service, AID, and ICA staff assigned to the region was expanded and their quality upgraded. The State Department, for the first time, appointed a Deputy Assistant Secretary of State specifically charged with responsibility for overseeing U.S. relations with the Caribbean. A Caribbean Military Task Force facility was established at Key West, and the presence of the U.S. Navy in the Caribbean was made much more evident by a series of port calls and naval maneuvers. The Voice of America is now establishing a powerful transmitter in Antigua, capable of beaming medium-wave broadcasts to the entire region.

The Caribbean (together with Sub-Saharan Africa) has been accorded special emphasis in the programs of the International Develop-

[1] Analysts differ about whether to define the Caribbean primarily in geographical, cultural, or political terms. For the purposes of formulating U.S. policy toward the region, however, the Caribbean is best conceived as that set of insular and dependent territories, in or bordered by the Caribbean Sea, concerning which the United States has historically felt a special security interest, arising primarily from their proximity and their presumed vulnerability to external penetration. All the Caribbean islands, together with Belize on the Central American isthmus and Guyana, Surinam, and French Guyana on the South American mainland would fit this definition of the region.

This essay focuses on the Caribbean region, thus defined, and does not deal with the countries of Central America's isthmus. Central American nations differ importantly from those of the Caribbean in their degree of independent viability, in their social and economic structures and in their degree of interaction with the United States. Although U.S. policies toward Central America and toward the Caribbean affect each other, the problems posed for the United States in each case are different.

ment Cooperation Agency (IDCA), the new coordination unit. Budgets for U.S. economic assistance to the Caribbean have been doubled since 1976. To coordinate and expand foreign aid to the Caribbean, the U.S. Government took the lead in 1977 in establishing the Caribbean Group for Economic Cooperation and Development. This is a consortium of 10 donors and 14 Caribbean countries which reports channeling over $300 million to the area in 1979. To supplement all this governmental activity, the Carter administration helped to launch, with considerable fanfare, a "private sector entity" (Caribbean/Central American Action) to work on improving U.S. relations with these regions.

President Reagan and his advisers on Latin American affairs have also demonstrated their strong interest in U.S.-Caribbean relations.[2]

Renewed public interest in the Caribbean has been mirrored on the private side. *U.S. News and World Report*, *Time*, *Newsweek*, the *New York Times*, and the *Washington Post* have all run feature articles on the Caribbean in the past several months. NBC and CBS have run television "specials" on the region. The *New York Times* has opened a Caribbean bureau, operating from Miami. Foundations and scholars are rediscovering the area.

This turn toward the Caribbean is not without precedent, of course. The United States has long been deeply involved in the Caribbean, America's Mediterranean. It is an involvement that has often been far from happy. One need only think back sixty years to the era when United States had soldiers in the Dominican Republic, Haiti, and Nicaragua, virtual protectorates in Cuba and Panama, and a de facto colony in Puerto Rico. Even in the past few years, many "crises" have erupted within the Caribbean basin.

The Bay of Pigs, the Cuban missile crisis, and the 1965 U.S. military intervention in the Dominican Republic provoked a concern in the United States to reexamine the nature of this country's relationships with the area. Studies of Caribbean policy were commissioned by the State Department and by such private organizations as the American Assembly, the Council on Foreign Relations, the Twentieth Century Fund, and the University of Pennsylvania.

Within three or four years, however, interest in Caribbean policy had fallen off once more, as in the past. The recommendations of the State Department's Caribbean Study Report of 1968 were never carried out. The University of Pennsylvania's report was never published. The Twentieth Century Fund's original project was never finished (though a more recent report for the Fund finally was published). The American Assembly's report and Robert Crassweller's study for the Council on Foreign Relations were published, but neither received much attention.

United States foreign policy paid little attention to the Caribbean from the late 1960's until the late 1970's. Official U.S. programs of all kinds were cut back, foundation interest declined, and academic enthusiasm waned. Only at the end of the 1970's—when Fidel Castro's Cuba began to strengthen its Caribbean links, when Central America's

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[2] See, for example, James D. Theberge "Rediscovering the Caribbean," *Commonsense* (Spring, 190), 1–20 and Roger Fontaine, Celtio DiGiovanni, and Alexander Kruger, "Castro's Specter," *The Washington Quarterly* (Autumn 1980), 3–28.

stability began to crumble, and when Caribbean migration to the United States became more visible in the context of the mainland recession—did official Washington begin to focus again on the Caribbean.

Between bursts of attention, the United States Government tends to treat the Caribbean as a matter of low priority and not to question long-standing assumptions and axioms. When a perceived "crisis" emerges, however, Washington tends to see the Caribbean in terms of traditional premises, and often, therefore, formulates policies that fail to take full account of the region's political and economic dynamics.

The current rekindling of U.S. interest in the Caribbean provides a chance to think through some fundamental questions about U.S.-Caribbean relations: What kind of region is the Caribbean today and how is it evolving? What are U.S. interests in the Caribbean, and how are they changing? What are the different ways in which U.S. aims might be promoted, and the likely risks and benefits of each way? To what extent are special U.S. approaches, specifically designed to affect this particular region, feasible or desirable? What would they entail?

The Caribbean Today

The contemporary Caribbean comprises 32 political entities with a population totalling some 30 million people. Thirteen of these units are not independent countries, ten having achieved independence since 1960. Several territories (including Antigua, Monserrat, Anguilla, and St. Kitts-Nevis) are actively seeking independence in the next five years. Some (Guadeloupe and Martinique, for example) seem ensconced in their long-standing colonial relationship. Puerto Rico's status, a perennial subject of discussion, is less clear than ever, after the nearly equal vote registered in 1980 by the pro-statehood and pro-commonwealth forces.

The Caribbean territories are remarkably diverse, yet overwhelmingly alike.

Most are tiny; two-thirds of the islands of the Caribbean could fit simultaneously into the King Ranch in Texas. Cuba is by far the largest island, occupying more than half the area of all the other Caribbean islands combined, but even Cuba is smaller than the state of Ohio.

Five different basic racial groups (black, white, oriental, native Indian, and East Indian)—and their numerous subgroups and combinations—mingle with varying degrees of integration and hostility. Even more different languages are spoken within the region, including European languages and their derivatives, plus the creole mixtures with African and Indian tongues. Caribbean religious sects include mixtures of the borrowed and the invented, the traditional and the ultramodern, and of indigenous, European, African, North American, and Asian influences.

Economic organization runs the gamut from the tax havens of the Bahamas—reportedly the largest single Eurocurrency market outside London—to Cuba's institutionalized socialism (where free market transactions are beginning to be permitted again), with all manners of hybrid in between. The Dominican Republic, where long-time dictator Rafael Trujillo's vast personal fiefdom passed to government ownership after his assassination in 1961, has a very high share of its economy in the public sector, but tries through generous incentives to encourage private investment, domestic and foreign. Jamaica's previously strong private sector became massively disgruntled during the 1970's; both Jamaica and Guyana, which chose to build various forms of socialist-oriented (or at least state-capitalist) mixed economies, are now concerned about how to re-attract and stimulate private investment. Grenada, where the principal exports are bananas and nutmeg and the main economic potential is tourism, is apparently opting for "socialism" in a ministate where no form of economic organization can much alter the obvious constraints on growth.

Economic productivity ranges from the depth of Haiti, the only nation of the Americas to rank among the very poorest countries of the world, to the relatively high but uneven performance of Martinique and Guadeloupe, the Bahamas, Puerto Rico, Trinidad-Tobago, and Barbados. The region includes four out of six of the countries with the lowest per capita GNP in the Americas (Haiti, Dominica, Grenada, and Guyana) as well as eight units with per capita GNP among the highest (Martinique, Trinidad-Tobago, Dutch Antilles, Guadeloupe, Puerto Rico, Surinam, Bahamas, and Barbados).

Although the overall per capita income figures in most of the region are high by comparative LDC standards, bitter poverty is widespread. Seventy-five percent of pre-school children in the Dominican Republic suffer from malnutrition, for example. One-third of Jamaica's people have annual per capita incomes under $200; two-thirds of Haiti's rural population were reported in 1978 to have annual per capita incomes below $40. The region's poverty is highlighted, and its effects aggravated, by its juxtaposition—through migration, tourism, and the media—with prevalent living standards in the United States and other industrial countries. This juxtaposition, and the Caribbean's striking dependence, make plausible (if not entirely warranted) V.K. Naipaul's characterization of the region as the "Third World's Third World."

Most of the Caribbean economies are in deep trouble. Higher prices for petroleum and other vital imports pose additional strains on the economies. Jamaica has had seven consecutive years of negative growth, even by the Castro's government own account, is not much more impressive. Barbados' gains and significant growth in the Dominican Republic counter the regional trends, but the latter country has been hard hit by the exploding price of oil. In 1973, the Dominican Republic made almost twice as much from sugar exports as it spent on oil imports; by 1979 oil imports cost about $75 million more than the country's income from sugar.

The Caribbean countries share, apart from natural beauty, a number of painful characteristics. They are small, mostly densely populated, and heavily dependent on exporting a few primary products. They are extremely susceptible to international economic fluctuations and also to the vagaries of the weather. (The path of Hurricane David in 1978, sparing Barbados at the last moment and devastating Dominica instead, vividly illustrates this last point.) Most have relatively few known resources beyond the sun; those with a broader resource base—Jamaica, for example—have often been unable to capitalize fully on their advantages. All the islands have limited domestic markets and insufficient savings and financial capacity. Agriculture is weak and declining through most of the region. Per capita food production in Jamaica, for example, was 11 percent lower in 1974–76 than it had been in the mid-1960's.

But while agriculture is declining, so is the push toward industrialization. The region-wide burst of "industrialization by invitation" during the 1960's has run out of steam. The major Caribbean islands (except Puerto Rico) show a stability in the share of national production accounted for by manufacturing and a declining trend in employment accounted for by manufacturing. Unemployment and underemployment are distressingly high across the region. Even official statistics show unemployment rates exceeding 30 percent in some countries despite the fact that a relatively low share of the population is considered economically active (about 30 percent in most Caribbean territories compared with almost 45 percent in the United States).

Socially and culturally, the Caribbean territories are insular; even in those (Belize, Guyana, Surinam, and French Guyana) physically situated on the mainland, 90 percent of the population live in coastal enclaves. Most are searching for identity and meaning, trying to draw on the shared and exceptional experiences of slavery, migration, and colonialism to derive an acceptable heritage. Their social structures, economies, patterns of race relations, and modes of interaction with the external world all bear the mark of centuries of colonial rule and of plantation societies.

The Caribbean's history has always been largely shaped, and even written, from outside; the very concept of the area as a region is largely an externally imposed idea. A few outstanding Caribbean intellectuals—Naipaul, Franz Fanon, Aime Cesaire, C. L. R. James, Eric Williams, Juan Bosch, William Demas, and Arthur Lewis among them—have projected Caribbean experience onto a much broader canvas. Their work, and the lives of Caribbean peoples, have reinforced the notion of this as a region, with common problems and opportunities despite different cultural and colonial backgrounds.

Most Caribbean territories are still not well integrated internally (an exception is perhaps Cuba since its revolution, and there in part by exiling over one-tenth of the nation). Many, indeed, are more fragmented now than a generation ago; the Dominican Republic's civil war of 1965, Trinidad's 1970 Black Power uprising, Bermuda's race riots, Jamaica's urban violence, Guyana's political strife, and the constant struggle over status in Puerto Rico all exemplify this point.

Even less are the Caribbean territories integrated regionally. The West Indies Federation of 10 territories established in 1958 lasted only until 1961; it could not survive parochial rivalries, especially between Jamaica and Trinidad (and their respective leaders). The Eastern Caribbean, most recently under colonial rule, is fragmenting into ministates so small as to raise the real possibility that one or another could be taken over relatively easily by international criminal elements, such as those involved in the narcotics trade. Interchange between the Commonwealth Caribbean countries and the Spanish, Dutch, and French-speaking countries is still minimal. Cuba, effectively isolated by U.S. policy from the rest of the Caribbean from 1960 until the mid-1970's, has expanded and strengthened its relationship with both the English-speaking Caribbean and the rest of the region in recent years, as has Venezuela, but pan-Caribbean movements are still incipient and fragile.

Politically, the Caribbean territories face contradictory currents and tensions. Most of the independent countries are formal democracies, but the institutions of representative government are severely strained, as has been shown by the coups in Grenada and Surinam and, in different ways, in Jamaica and Guyana, where political violence has intensified. An extended period of deceptive political "stability," at least in the sense of long-lasting governments, may be coming to an end in several countries. Long-standing practitioners of "doctor politics,"—Lloyd Best's unimprovable phrase to describe the role of Caribbean scholar-statesmen—are at or near the ends of their careers with the next stage of politics consequently hard to predict, but almost certainly volatile.

Jamaica, once considered politically highly developed, seemed close to social implosion during the 1980 election campaign; the possibility of a military coup there was no longer unthinkable. In the Dominican Republic, where the first peaceful transition in its history from one elected president to another in 1978 was achieved only with significant involvement by Washington at the crucial moment, constitutional government is still fragile. The governments in several small islands of the Eastern Caribbean—St. Lucia, St. Vincent, Dominica, and Antigua—are shaky. Even Barbados, the epitome of stable politics, is nervous about the influence of leftist activists, at least on neighboring small islands. Puerto Rico, generally considered a successful case of modernization, faces a real possibility that deepening economic problems and the continuing impasse over status will eventually lead to an intensification of the now sporadic violence. Haiti, long ruled by "Papa Doc" Duvalier, is now ruled by his son "Baby Doc"; no one knows when this dynasty will end, but it surely will do so. And in Cuba, where Fidel Castro has directed a highly institutionalized authoritarian regime for twenty-one years, overt dissidence is increasingly evident.

Polarization, rather than regional consensus, seems to be the prevailing political trend. Grenada's leftist coup and the quasi-leftist coup in Surinam have been matched by a rightward swing (albeit through elections) in the politics of Dominica, St. Kitts, and Antigua, and most recently by the decisive election of Edward Seaga in Jamaica. Pan-Caribbean unity is increasingly unlikely as several of the islands move in sharply divergent directions.

Internationally, most of the Caribbean units are satellites in search of an orbit, or perhaps of multiple orbits, in the sense of regular and predictable relationships with central powers. The United States acts increasingly as the principal metropole, as the Western European nations have been withdrawing from the area. Mexico and especially Venezuela have shown some interest in expanding their relations with the Caribbean, an interest which has reached its most concrete expression to date in mid-1980 with the signing of a Venezuela-Mexican commitment to sell oil to several Caribbean and Central American states on favorable terms that contribute to long-term development projects. The Soviet Union's close relationship with Cuba makes Russia a Caribbean actor, although Soviet influence has so far been small outside of Cuba itself.

Almost all the island states have preferential trading agreements with various metropolitan powers. All Caribbean units are heavily dependent on foreign commerce; for many, that means trade primarily with the United States. Cuba and Puerto Rico each receive massive subsidies (at roughly comparable levels) from their respective metropolitan sponsors, as do Martinique, Guadeloupe, and French Guyana. Foreign aid to the other independent Caribbean islands is higher on a per capita basis than to any other group of countries, but much less that what Puerto Rico receives from the U.S. government, Cuba from the Soviet Union, and the French colonies from France.

The high volume of trade with the United States—eight billion dollars worth of trade take place each year between the United States and the Caribbean—is an example of another shared characteristic of most of the Caribbean units: the high degree of interdependence with the United States. Not counting Puerto Rico, the United States has over $4.3 billion in direct private investment in the region, (of which over $1.2 billion took place in the past decade); 25 percent of U.S. worldwide investments protected by the Overseas Private Investment Corporation (OPIC) are in the Caribbean. More than 75 percent of the bauxite the United States currently imports (more than half of our total consumption) comes from the Caribbean, and about $4 billion of refined petroleum products.

The most significant links, however, between the United States and the Caribbean are people. Most of the Caribbean economies depend heavily on tourism, and cater primarily (and increasingly) to U.S. travelers. Some countries are even attracting significant numbers of retired Americans as permanent residents. Thousands of young Americans attend marginal medical schools in the Caribbean. U.S.-based criminal syndicates find the Caribbean a congenial base for narcotics and gambling operations (following in the wake of numerous U.S. based "buccaneers" of various types who have roamed the Caribbean since the colonial period). And American culture—high and low—pervades the area, at all levels and in all classes.

The most dramatic and expanding tie between the United States and the Caribbean is provided by the region-wide stream of migrants to the United States. Over 4 million Caribbean citizens have entered the United States, mostly since World War II. Close to 20 percent of all living Caribbean-born people reside in the United States by now. In the last few years, more than half the annual population increase of most of the region's countries—over 80 percent of the annual increase in the labor force in some—has entered and stayed in the United States, legally and illegally.

Many of the Caribbean immigrants have been from Puerto Rico, which has exported more than 40 percent of its total population to the mainland since World War II. Puerto Rican migration has slowed notably in the past fifteen years, but the dip in Puerto Rican migration has been more than compensated for by the increase from other Caribbean sources. The flow to the United States is unquestionably region-wide, and appears to be intensifying. Five of the six countries in the world with the highest per capita rates of legal migration to the United States are Caribbean, and illegal migration is at least equally intensive from the region. Over a million Cubans have come since 1960, more than 400,000 Dominicans, at least 300,000 Haitians, and about a million West Indians.

What might have seemed at one time like a series of unrelated events—the influx of Puerto Ricans to a booming postwar United States; the exodus of Cubans, in various waves, fleeing Havana under Castro; the surge of Dominicans escaping the country's turbulent political struggles during the mid-1960's; the stream of Haitian "boat people" risking death to find work; the flight of Jamaicans fearing radicalism at one level and those seeking jobs at another; the stream of students coming to study in U.S. universities—appears increasingly to reflect a more fundamental, continuous, and probably irreversible response both to regional population pressures and the demand for cheap labor of the U.S. economy.

What underlies the contemporary crisis in the Caribbean is the ever deeper and more obvious tension among different goals. Caribbeans from different backgrounds and tendencies all want economic growth, improved equity, fuller employment, political participation, enhanced autonomy, and more confident self-respect. But these goals may not be simultaneously compatible. The region's experience suggests that development strategies which emphasize growth often undercut equity and autonomy, that efforts to expand employment undermine efficiency, and that a stress on national autonomy may threaten prospects for economic expansion.

With populations continuing to rise, agricultural productivity declining, industry stagnant, and balance-of-payments disequilibria intensifying, the capacity of Caribbean units to secure equity and growth and to incorporate more employed workers—all while preserving democracy and without sacrificing autonomy to a metropolitan power—is being questioned. The central issue in U.S.-Caribbean relations for the 1980's will be how the United States responds to the turmoil in the Caribbean, brought about by the region's political and economic troubles, shifting external alignments and massive migration.

U.S. Interests

What is at stake for the United States in dealing with the Caribbean? What are U.S. interests, and how are they changing?

Traditional discussions of U.S. interests in the Caribbean mainly emphasize military security and economic concerns. The military security interest has usually been conceived in terms of keeping hostile political and military influences away from this country's "third border." That was the aim of both the Monroe Doctrine and the Roosevelt Corollary, landmarks in U.S. foreign policy. It is also usually emphasized that various, long-significant U.S. military assets dot the region; that some 7 percent of this country's imported oil comes from or is refined in the Caribbean; that the Caribbean provides access to the Panama Canal, long considered vital for U.S. commerce and defense; and that key sea lanes through which U.S. trade passes, cross through or near the Caribbean. The economic interest, as traditionally conceived, involves U.S. investment in and trade with the region, as well as secure access to various mineral and raw materials. From the mid-19th century until World War I, the period when many of the current axioms of U.S. policy toward the Caribbean were fashioned, the region accounted for a high share of this country's foreign commerce and investment, and U.S. policy aimed to protect and expand U.S. economic interests.

Some analysts continue to think of the Caribbean and the challenges it poses for U.S. foreign policy in these familiar terms. They stress the continued relevance of long-standing security doctrines which make it imperative for the United States to maintain friendly border regions. Some may argue that important U.S. business and financial interests are threatened by recent trends in the Caribbean, and that the United States should reassert its regional leadership in the 1980's, particularly in the context of a deteriorating international situation.

Other analysts doubt that the Caribbean is still very important to the United States in these traditional terms. They see changing technology and shifting geopolitics as having altered the strictly military significance of the Caribbean as well as the feasibility of excluding foreign influence. They argue that U.S. naval bases and other military assets in the region are no longer vital; indeed, most of the remaining U.S. military installations in the Caribbean are currently due to be closed by the mid-1980's. They point out that the Panama Canal, although still useful, is no longer essential in the sense it used to be. A shrinking share of U.S. trade passes through the Canal; some of the world's increasingly vital oil super-tankers are too big to enter the Canal, as are the aircraft carriers around which U.S. fleets are organized.

Nor, they observe, can the United States any longer exert the total control of this region it once enjoyed. From 1898 to 1969, no hostile naval force ever entered Caribbean waters, but Soviet naval formations have been doing so regularly since 1969 and obviously can and will continue to do so. Although the United States retains its interest in preempting potential military threats posed from or through the Caribbean, these analysts suggest that the primary means for protecting that interest is not in Caribbean policy but in great agreements, as exemplified by the U.S.-U.S.S.R. "understanding" keeping nuclear-equipped submarines (and apparently submarine tenders) out of Cuba.

In economic terms, too, they stress that the relative significance of the Caribbean for the United States has declined steadily since before World War II, when it accounted for more than 11 percent of U.S. direct foreign investment and an even higher share of foreign commerce. By 1978, U.S. investment in the Caribbean (exclusive of Puerto Rico) amounted to only 2.5 percent of U.S. foreign direct investment. The share of U.S. petroleum imports coming from or through the Caribbean has been declining over the past several years, not increasing. Nor does the United States depend in any meaningful sense on any other commodity imported from the Caribbean; bauxite, by far the principal import from the region, is available from many countries.

However one evaluates this debate on security and economic interests, three facts surely will make the Caribbean important to the United States in the 1980's.

First, the cluster of such a considerable number of like-minded sovereign nations, comprising the largest bloc of democratic government in the world, gives the Caribbean a weight in international forums far outweighing the region's demographic or military weight. The fact that various Caribbean statesmen have taken a leading role in international forums underlines and reinforces this point. Cordial relations between the United States and the Caribbean are likely to draw their support for U.S. foreign policy initiatives; conflictive relations, or outright hostility, would array them against the United States. Caribbean nations provided nine votes to condemn the Soviet invasion of Afghanistan, for example, and almost as many votes to support Israel's position. Were the United States to be ringed instead by a cluster of hostile states, its international situation would become more difficult.

Second, the Caribbean's relations with the United States makes this region, in the eyes of many, a kind of litmus test of the attitudes and policies the United States will adopt toward Third and Fourth World countries generally. How the United States responds to the needs and priorities of its closest neighbors in the developing world is important as a symbol of the kind of country the United States is.

Finally, and most important, the Caribbean will be significant to the United States because of increasing interpenetration between the two. Except for Mexico and Canada, no other region is so closely bound to the United States. The large and active Caribbean community resident in this country, linked to the home countries by return visits, continuing migration, remittances, and the like is already a fact in the political life of Miami and New York and not a negligible factor in the foreign and immigration policy debates.

How the United States treats the Caribbean, through conscious policy or by inadvertence, will affect the region greatly, for no other set of countries is as dependent on its relationship with the United States as the Caribbean group. What happens in the Caribbean, in turn, will inevitably affect the size, composition, and character of the emigration from the area, and thus the quality and character of life in the United States.

The degree of inevitable U.S. involvement in Caribbean affairs occasioned by this interpenetration—including the mutual importation of cuisine, music, dance, cinema, literature, political ideas, crime, and even political techniques—converts U.S. "foreign policy" problems into domestic or "intermestic" ones, and and vice versa. Immigration policy—what to do about the many thousands of Caribbean people who enter the United States each year—illustrates this point most obviously, but the same merging of domestic and foreign phenomena occurs with health care, narcotics regulation, education, youth unemployment, and other issues.

What occurs in the United States is often echoed in the Caribbean. The economic, political, and cultural processes of the region are profoundly influenced by proximity to the United States. Grenada's New Jewel Movement—to take a dramatic example—is led primarily by returned students influenced by Black Power movements in U.S. universities in the 1960's; their coup used arms imported from the United States. Jamaica's newly-elected president, Edward Seaga, was born and educated in the United States; many other leaders—in politics, business, and education—have been trained in this country, and Americans of Caribbean descent are making their presence felt in business, politics, and the professions.

Alternative U.S. Approaches to the Caribbean

Four different approaches to U.S. policy toward the Caribbean may be distinguished.

The traditional approach, not in vogue for some years but imaginable in the 1980's, would be essentially to ignore the Caribbean region except for continuing vigilance against the possibility of a direct military security threat in the region (with a low tolerance for ambiguity on that score).

A second approach would be for the United States to disengage from the region. Under this approach, Washington would cease not only to send in the Marines and AID missions but also cease to preoccupy itself with the region's political or economic trends.

A third approach, essentially that of the Carter administration, is for the United States to do whatever it can to maintain political stability and military security in the Caribbean, including increased support for economic development in the Caribbean, through bilateral and/or regional aid programs, and encouragement of private investment.

A fourth policy, recommended by many leaders in the Caribbean itself, would be for the United States to transform the nature of its Caribbean involvement and concentrate on long-term economic and social development, even if this should mean continuing to tolerate divergent models and ideologies in the region. In schematic form, these options are recapitulated below.

4 ALTERNATIVE U.S. APPROACHES TO THE CARIBBEAN

	High	Low
I. Traditional:		
Degree of concern with military security	X	
Degree of concern with other issues		X
II. Disengagement:		
Degree of concern with military security		X
Degree of concern with other issues		X
III. Activist:		
Degree of concern with military security	X	
Degree of concern with other issues	X	
IV. Developmental:		
Degree of concern with military security		X
Degree of concern with other issues	X	

The Traditional Policy

The historic U.S. approach to the Caribbean combines studied indifference to the region's underlying economic and social realities with keen sensitivity to potential military security threats to the United States and a consequent aversion to political instability. This is the policy that has been in effect for decades, with intermittent exceptions. Under this policy, the United States government concerns itself little with the Caribbean colonies of other countries, the Caribbean territories under dictatorship, and politically stable countries with constitutionally elected governments. Under the policy, then, the United States would focus only on countries moving to the pro-Cuban left or internal anarchy. Even in the latter case, however, the United States would not concern itself deeply until and unless conditions suggest the possible onset of a threat to unquestioned U.S. interests. At that point, the United States would use whatever means are needed—including military intervention—to neutralize the threat.

The historic policy's attraction derives from its apparent low cost and from its simplicity. It provides criteria which allow top policy makers to concentrate on other regions except under (more or less) clearly defined circumstances: when events in the Caribbean pose the danger that hostile extra-hemispheric influence might increase their presence and influence within the region.

One key difficulty has always plagued the traditional U.S. approach to the Caribbean, however. Although it is precisely the weak, dependent entities like those dotting the Caribbean which experience instability and provide recurrent openings for the exertion of outside influence, U.S. government policy has done little until recently under the traditional policy to help the Caribbean territories (aside from Puerto Rico) overcome their disadvantaged condition. The Caribbean units have never been able to resist by themselves the encroachment of external power, which Washington considers threatening, but neither have they been able by themselves to undertake the processes of national and regional development and integration which might help make them less vulnerable to foreign penetration.

The United States has taken an exceptional interest in domestic political changes within the Caribbean, but has resisted engaging itself in a more fundamental and continuing way. The United States has so often been drawn into unpleasant Caribbean entanglements, including military interventions, because while it had traditionally regarded the area as of strategic concern, it never adopted the kind of positive, long-term measures such a concern might imply.

The fitful nature of U.S. policy towards the Caribbean has had its costs. Each U.S. intervention tends further to undermine self-confident national development. Each U.S. intervention—overt or covert—fuels anti-American movements across the region, as the cases of Guatemala and Santo Domingo exemplify. Each also strains the domestic consensus on foreign policy. And each makes more distant the day when international laws against military coercion and intervention will have real force.

THE DISENGAGEMENT ALTERNATIVE

An approach to the Caribbean, based on premises opposed to those of the historic U.S. policy, would be for the United States to attempt to disengage itself as much as possible from the Caribbean.

Underlying this approach, expressed in some academic circles if rarely debated in official Washington, is the premise that the U.S. has little or nothing to worry about in the Caribbean and can safely disregard the area, and that the Caribbean itself might well be better off if Washington left it alone. Strategic threats in the Caribbean, it is argued, can only be dealt with by negotiations and understandings between the United States and its allies, on the one hand, and the Soviet bloc on the other. This view holds that U.S. economic interests in the region are neither overwhelmingly important nor likely to be substantially affected even if some Caribbean government became hostile to the United States. Those countries will sell to and buy from the United States almost inevitably, unless Washington itself imposes economic sanctions, as it did with Cuba. American policy makers, attentive publics, and eventually the electorate at large, should be educated, therefore, to accept a substantial U.S. withdrawal from Caribbean involvement. U.S. officials, it is further argued, should rid themselves of their traditional nervousness about Caribbean turbulence and leave the people there alone, to develop or to stagnate, to revolt or to ally, or to stew in their own juices, whatever the flavor.

However impractical the disengagement formula for the Caribbean may seem in the present U.S. political climate, it does have some attractive features. Certainly, the United States has often acted in the Caribbean on the basis of shibboleths sanctified by repetition but unsubstantiated by analysis. Surely the kind of U.S. intervention in Caribbean affairs which characterized the 1920's and the 1960's has been counterproductive. Furthermore, it may be persuasively argued that U.S. disengagement, if it could be sustained, would even enhance U.S. security. Given the predictable instability of Caribbean politics and the likelihood (and indeed the possible beneficial effects) of substantial socioeconomic transformations there, one advantage of disengagement would be to facilitate routine diplomatic, cultural, and commercial relations with all Caribbean territories. Each Caribbean nation's own urge to avoid both confrontation with the United States and the consequent option of dependence on another world power, would thereby be reinforced. Nationalist regimes in the Caribbean would arguably reject foreign alliances if they did not regard these as a necessary defense against U.S. hostility.

Disengagement by the United States from the Caribbean, however, is probably not really feasible. It is not clear, furthermore, that its implications for the Caribbean would be unambiguously benign.

The fact is that the United States cannot withdraw from involvement in its own border region by a unilateral act of will, as it could (though even then with some difficulty) from Vietnam. Geography—strongly reinforced by history, politics, and economics—makes the United States a major presence in the Caribbean. The Caribbean territories cannot escape the shadow of the United States, whether benign or stifling. Nor can the United States easily escape the presence and influence of the Caribbean, especially because of sustained immigration, which brings the region's problems to our shores.

Given the proximity and vulnerability of the Caribbean territories and the indifference toward them of the Latin American countries (with the significant exception of Venezuela, and lately of Mexico), the United States is bound to be involved in the region and to have a major impact, no matter what policy is adopted by an administration in Washington. Moreover, were the U.S. government to attempt to remain only minimally involved in Caribbean affairs, it might find itself unable to remain so because of the significant American private sector's engagement in most of the major areas of the Caribbean economy.

Finally, the fact is that President Reagan as well as former President Carter in the 1980 electoral campaign, called for expanded public and private involvement by the U.S. in the Caribbean. Moreover the legacy of two centuries of U.S.-Caribbean relations make it unlikely that Washington, in the near term, could adopt and implement a consistent policy of disengagement. The challenge for U.S. policy is how to relate to the Caribbean nations, not whether to do so.

An Activist Caribbean Policy

A third approach to U.S.-Caribbean relations—essentially that adopted by the Carter administration and earlier by the Alliance for Progress is for the United States to retain its long-standing special concern with Caribbean military security and political stability, but to couple that concern with increased economic and technical aid to achieve economic and social development. Rather than wait for anti-American trends in the region to worsen, it is argued, the United States should head off problems by helping the Caribbean nations to deal with the issues that face their societies.

More concretely, the activist U.S. approach to the Caribbean stresses augmenting U.S. economic assistance to the region, especially through bilateral accords intended to highlight the visibility of the U.S. government. It implies beefing up the U.S. presence throughout the area: politically, militarily, culturally, as well as through the private sector. Activists also advocate using non-aid instruments—trade and tariff policies, and other measures to facilitate the transfer of capital and technology—to support the region's development. The "activist" approach aims to turn the Caribbean away from Cuba's influence and instead to improve bilateral and subregional relationships with the United States. Efforts (of various kinds) to counter Cuba initiatives, and even to isolate Cuba, mark the "activist" approach.

The advantages of the activist approach to U.S.-Caribbean relations are obvious. Focusing more attention and resources on the region should enable the U.S. government to affect U.S.-Caribbean relations in a more timely and effective way. The scale of Caribbean entities is such that even limited U.S. moves can have an immediate and perceptible impact. The Caribbean is so dependent that an infusion of U.S. resources is likely, at least in the short run, to fix the region even more firmly in the U.S. orbit. The timing of an activist initiative toward the Caribbean is attractive: Cuba's internal difficulties are growing, while internal Caribbean trends are toward cooperation with the United States.

The risks of the activist approach should also be emphasized, however. One danger, already evident by 1980, is that unrealistic expectations may be aroused within the region. Prime Minister Seaga of Jamaica, for instance, has already called for a sustained program of aid to Central America and the Caribbean at the level of $3 billion per year. Sober assessments about the resources likely to be available to U.S. aid agencies in coming years suggest that aid to the Caribbean will be much more modest. There is a risk, therefore, that focusing attention on the Caribbean will produce a troublesome gap between rhetoric and expectations on the one hand and implementation and impact on the other.

Second, the preoccupation of U.S. policy makers with Fidel Castro's Cuba provoke, or at least exacerbate, deep strains. Caribbean leaders typically perceive Castro as primarily a Caribbean actor, not mainly as a Cold War instrument. At times they find it useful to "play the Cuban card" to derive increased legitimacy with certain domestic constitutents or to strengthen Third World ties. Some leaders argue that U.S. readiness to give the Cuban issue priority leads to recurrent tensions. Intensifying Cold War measures in the Caribbean could damage U.S.-Caribbean relations directly and reduce the chances of cooperating with other external powers—Canada, Mexico, Venezuela, the OECD donor countries—to promote Caribbean development; on the other hand, the United States has successfully increased World Bank lending to the Caribbean partly, no doubt, to diminish Castro's influence.

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More generally, the activist approach to the Caribbean carries the risk that Washington will become interventionist. Even assuming benign intent, active U.S. pursuance of political goals in Caribbean affairs may stifle local initiative or provoke nationalist reactions. Moreover, to the extent that U.S. interest in the Caribbean appears to be instrumental—not really concerned with the region's people but rather only with threats posed to the United States—the chances increase that an active U.S. presence in the Caribbean would backfire.

The Developmental Approach

The fourth alternative U.S. approach—one not surprisingly favored by many Caribbean leaders—is the adoption by Washington (and others) of a sustained commitment to Caribbean development. Such a commitment—a decision to take a continuing interest in the whole region's intermediate and long-term development prospects—would differ from the "activist" approach mainly because it would emphasize economic development rather than military security, concentrate on longer-term processes rather than on immediate impact, and because it would feature increased tolerance for a diversity of political and economic approaches in the region.

Operationally, a sustained U.S. commitment to Caribbean development would involve a significant increase in aid, primarily through multilateral as opposed to bilateral channels; non-aid concessions to help Caribbean development; a lower U.S. profile in the region; and an abandonment by Washington of efforts to reverse or at least contain the Cuban revolution. Rather than build up the visible U.S. presence in the region, Washington would downplay its own role and lay the foundations for a healthier U.S.-Caribbean relationship in the future by focusing on the region's underlying social and economic dilemmas. Rather than worry about countering Cuba, this approach would stress attacking the problems for which Cuba's proposed solutions are finding responsive constituencies: inequity, malnutrition, illiteracy, and poor social and health services, especially in the rural areas. This approach would support moves to bring the region into better touch with itself; closer economic cooperation and interchange among all the countries of the region, including Cuba, would be considered desirable under this approach, not as something to be thwarted.

According to its advocates, the developmental approach responds to a fundamental U.S. interest—a "security" concern in a much broader sense—in having viable, effective societies on our Third Border, societies which meet the needs of increasing numbers of their citizens. The approach reflects the moral concern that one should care about how he affects his neighbors, and on the practical realization that festering problems in societies so intertwined with our own will eventually affect this country.

A long term developmental approach would avoid preoccupation with the momentary twists of the Caribbean kaleidoscope in order to allow policy makers to concentrate on underlying issues. Enough consensus exists within the Caribbean on the nature of the region's problems and on how the United States could help that it is plausible to believe that a sustained U.S. commitment would make a difference.

A few U.S. initiatives—to help improve the region's agriculture, to improve the Caribbean's access to U.S. markets, and to regularize Caribbean migration to the United States—could have a major impact on the region.

Three drawbacks affect the developmental approach:

One problem is the danger of exaggerated expectations discussed in connection with the activist stance. It is not clear that the aspirations of Caribbean peoples can all be achieved, even with substantial foreign assistance. Some of the obstacles to sustained, equitable growth in the Caribbean may be inherent in the situations of at least some of these islands. No set of U.S. programs is likely to satisfy the aims of all Caribbeans. What is more, even successful economic growth would not by itself necessarily produce an environment congenial to U.S. values and interests.

Second, there is an inherent contradiction between populist and even more so, Castorite, economic and social organization and expecting domestic and foreign persons and businesses to continue investing in the area. Even trade can be expected to suffer once a government's ties with the international financial community are broken.

Finally, it is obvious that the developmental approach would be hard to adopt within the U.S. political process. The U.S. Congress is not likely to favor an open-ended, no strings commitment to support socio-economic development in a number of small countries, particularly if the case is made that they are insignificant in strategic terms. Only if the national political leadership were to succeed in convincing the American people that their welfare depends in part on Caribbean development could one imagine public support for a U.S. policy toward the Caribbean based on regional development rather than on containing Cuba and its challenge.

Sketching Out a Positive U.S. Approach

The first two approaches this essay discusses—the traditional one and its obverse—are ideas lacking substantial support among policy makers in the early 1980's.

Near term policy-relevant analysis should focus on how to implement a positive U.S. policy toward the Caribbean in the 1980's—either an activist concern aimed first, but not exclusively, at containing Cuban-Soviet influence, or a developmental approach emphasizing longer run socioeconomic processes.

Under either concept, one can identify a number of key points on which changed U.S. policies could favorably affect the Caribbean and Caribbean-U.S. relations in the 1980's. These would involve the following measures:

The United States and other donors could strengthen Caribbean agriculture, allocating funds for adaptive research and technology, expanding the availability of and improving access to credit, encouraging investment in rural areas, and enhancing local and foreign marketing procedures. Special incentives might be devised to encourage Caribbean production of winter fruits and vegetables for which the region has a natural comparative advantage vis-a-vis the U.S. market.

Access to U.S. markets could be improved, both for agricultural and other primary products and for manufactured goods.

Tariff and non-tariff barriers could be lowered within the GATT/MFN framework or on the basis of a special negotiated set of regional arrangements. (A reduction of the U.S. tariffs on rum and cigars would have a more positive effect on several Caribbean countries than any other immediately implementable steps, for instance.) Marketing arrangements for sensitive products such as textiles and beef could be renegotiated to favor Caribbean exports. And assistance could be provided to Caribbean countries to improve their marketing capacity in the United States.

The export earnings of Caribbean countries mainly dependent on the export of one or two major products might be stabilized through stronger support of international commodity and stockpiling arrangements.

Better provisions could be made to help the Caribbean territories cope jointly (with external assistance) with hurricanes and other natural disasters, as predictable as they are unexpected.

Tourism, mainly from the United States, to the Caribbean could be expanded by a variety of joint actions—for example, shared air transport facilities, jointly agreed routings, increases in duty-free imports for tourists, a change in U.S. income tax provisions to allow expenses for business-related conventions held in the Caribbean to be treated as are conventions in Canada and Mexico.

U.S. investors could be encouraged both by specific U.S. policies and by the general U.S. government approach to the Caribbean to view the region as a secure forum for investment. This could encourage increased transfers of U.S. capital and technology.

Present temporary workers' programs could be expanded and special, larger immigration quotas might be legislated to increase emigration from the Caribbean areas to the United States, especially from islands where unemployment is particularly high.

Priority could be given to helping the Caribbean cope with its extremely critical energy problems. Perhaps no other region of the world has been harder hit by the oil price rise since 1973 than the Caribbean, where almost all energy comes from oil. A major breakthrough in solar energy production, one unlikely to occur without major technological investments from the U.S. and other advanced industrial countries, would probably mean more for Caribbean development than all other imaginable innovations combined.

Most of these resources would cost money, either to U.S. taxpayers or to particular U.S. interests. Expanded Caribbean agricultural exports might hurt producers in Florida and elsewhere, a lowered tariff on Caribbean rum would hurt Puerto Rican firms, and a tax break on conventions in the Caribbean could hurt U.S. hotels, for example. Various measures would cost the U.S. taxpayers, as well. An international aid package at twice current levels would be required to implement these policies, and a substantial share of the increases would have to come from the United States.

Against these undoubted costs, one should note that the gains to tiny Caribbean economies of these concessions would be very large as compared with their cost to this country. One should emphasize, too, that perpetuating the status quo also has its costs—in terms of migration and of opportunities for anti-U.S. movements, and the less tangible cost of the discredit into which the market approach to development would fall as a result of further failure of status quo policies to bring about faster and sounder economic growth.

Some Key Issues for the 1980's

Whether the U.S. government adopts an "activist" policy toward the Caribbean or prefers the "developmental" approach, Washington will have to deal in the 1980's with at least eight specific issues:

(1) Whether to continue the recent cool and restrained pattern of relations with Cuba, to return to more hostility between Washington and Havana, or to try to improve relations between the two countries;

(2) How to respond to the possible emergence in the Caribbean of other regimes committed to socialist forms of economic organization and/or to close relations with Cuba or even directly with the Soviet Union;

(3) How to respond to the demands for increased foreign aid from countries in the region (such as Jamaica) newly committed to a market economy and to expanded foreign investment;

(4) How to treat the question of Puerto Rico's status;

(5) How to respond to continuing pressures to "decolonize" the remaining non-independent territories in the Caribbean;

(6) Whether to favor bilateral or multilateral means for implementing U.S. policies toward the Caribbean, and how to engage other powers in a constructive way;

(7) How to deal with authoritarian regimes of the right; and

(8) Whether to fashion preferential policies toward the Caribbean contrary to universal policies on trade, finance, immigration, etc., or to confine its Caribbean initiatives to measures consistent with global U.S. policies and practices.

Responses to these central questions are likely to be linked.

Contemporary Cuba poses three challenges to U.S. foreign policy: a socialist approach to development and politics; political alignment with the Soviet bloc and other anti-U.S. groupings; and the pursuit of military cooperation with the Soviet Union. The third point—the real sticking point in U.S.-Cuban relations—is a major question and deserves fuller treatment than can be given here. Activists and developmentalists generally agree that Cuban military interventionism should be discouraged, but they differ regarding the weight they give to Cuba's economic and political challenge and on how they would respond.

Those who view Cuba as America's principal antagonist in the Caribbean, as a hostile influence to be countered and contained, argue that Washington should take no (further) steps to legitimize the Castro regime's hold on Cuba or its influence in the region, given that regime's current policies. On the contrary, the United States should hold out, it is argued, for significant changes in Cuban policy, including the withdrawal of its forces from Africa, and particularly those oriented toward the Caribbean (including Puerto Rico) and to Central America—as a condition precedent for any moves to normalize U.S.-Cuban relations.

Similarly, activists assert that the United States should discourage Caribbean nations from following Cuba's approach to development. Opinions differ considerably, however, about how far the U.S. government should go to discourage Caribbean units from emulating Cuba. Activists in general would at least use political and diplomatic influence to prevent "second Cubas" (like Grenada) from proliferating. Some would favor using economic sanctions against those who cooperate with Cuba and would offer economic assistance to those who resist Cuba's blandishments. Some would probably favor the exercise of military force or covert action to prevent a Castroist takeover in the Caribbean, or to reverse one. Some, indeed, might favor U.S. efforts to topple the Castro regime itself.

As for implementation, activists tend to favor bilateral ways and means to heighten U.S. visibility and leverage.

The developmental approach differs on these issues. Because it concentrates on underlying social and economic problems, not on Cuba or on pro and anti-U.S. turns, the developmental approach favors steps to lower the region's political temperature and to improve the prospects for regional integration. Cuba's re-entry into the Caribbean and the normalization of its relations with the United States would therefore be favored by developmentalists. Decisions by other Caribbean islands to adopt Cuba's path or coloration would not lead to ostracism unless those islands chose to isolate themselves from the rest of the Caribbean community. Developmentalists would have the donors decide how much assistance to provide a Caribbean nation not on the basis of their nation's attitude toward Cuba, the U.S., or private investment, but on the efficacy of its development programs and projects. Some envision a future time in which Cuba and Puerto Rico, as the more highly industrialized countries of the region, would become the engines of development in an integrated Caribbean community.

Whether and how other powers external to the Caribbean—primarily Mexico, Venezuela, and Canada—can and should be asked to join efforts to assist Caribbean development depends in part on the approach Washington adopts. Mexico and especially Venezuela are already and increasingly engaged in the Caribbean in commercial, financial, and even political affairs. Each has its own perceived interests which do not necessarily coincide with each other's, let alone with those of the U.S. government. Neither government, for example, shares Washington's preoccupation with isolating Castro's Cuba (though neither, on the other hand, is very friendly with Cuba—Venezuela, in fact, is now rather distant). To the extent that the United States brings to the Caribbean its global Great Power concerns, Mexico and Venezuela, and perhaps Canada as well, will understandably shy away from overt cooperation with U.S. policies. To the extent, however, that the United States relaxes its overt security and political concerns, it may be possible not only to induce significant cooperation by these other countries but to get them to take leading roles in assisting Caribbean development, thus circumventing some of the fears and resentments that the United States engenders in the Caribbean.

Does the unique character of the Caribbean (and of U.S.-Caribbean relations) warrant regional preferences that conflict with broader U.S. policies on trade, finance, immigration, and the like? There can be no doubt that the Caribbean is special, and that its relationship with the United States is unique. Proximity, dependence, vulnerability, history, and migration make it so. For some, activists and developmentalists alike, these qualities justify a "special relationship" between the United States and the Caribbean. Other analysts argue, however, that unique qualities do not necessarily warrant special U.S. policies explicitly contradicting broader U.S. policies or agreed international instruments. Whatever Washington's rhetoric about "special relationship," history suggests that this country's stakes in the Caribbean will not long sustain the adoption of policies and practices which contravene its worldwide interests.

What can be sustained, if U.S. leaders wish, is a commitment to seek out ways to affect the Caribbean area positively, within a consistent global policy framework. Considerable scope for such positive impact exists, with small adjustments—on tax provisions, air traffic agreements, travel regulations, etc.—that may have large consequences in a region so dependent on the United States.

The challenge for U.S. policy toward the Caribbean is to be sensitive to the effects the United States has on the region and vice versa, and to make those effects more consistently positive. However that challenge is dealt with, it will have to be faced in the 1980's.

THE FUTURE OF THE NEW STYLE MILITARY REGIMES OF SOUTH AMERICA

By Albert Mayio*

I. Introduction

For a brief moment in history, South America seemed on its way to a future of democratic government. The moment was from September 1955—when the Argentine president and dictator, Juan Peron, was deposed in a miltary coup—until March 1964 when the Brazilian armed forces ousted President Goulart and installed themselves as the new government.

In the interim, the two remaining dictators of South America's larger countries, Rojas Pinilla of Colombia and Perez Jimenez of Venezeula were ousted and constitutional governments established in those two countries and in Argentina. In four countries, Brazil, Chile, Uruguay and Bolivia, constitutional regimes had already been functioning for some time—Uruguay since the early 1900's; Chile since the 1930's; Brazil since 1945, albeit not without short-lived military interventions in 1954 and 1961; Bolivia since 1952. Only in three countries did the military still dominate the government—Peru, Ecuador, and Paraguay. Even in Peru and Ecuador, however, the military interventions were of the "moderating" kind—in Alfred Stepan's sense of the "military restricting themselves to the removal of the chief executive and the transference of power to alternative civilian groups." [1] In Paraguay, the latest of a long line of dictators, General Alfredo Stroessner, had been in power since 1954. The other three countries of South America, Guyana, Surinam, and French Guiana, were still colonies of Britain, the Netherlands, and France, respectively. With the establishment of the Inter-American Development Bank in 1959–60 and the inauguration of the Alliance for Progress in 1961 to speed economic and social development, the outlook for democratic political government in South America seemed bright, at least on the surface.

As it happened, considerable economic and social development has taken place in South America since the early 1960's. However, except for three countries—Venezuela, Colombia, and Guyana—this development has been mostly achieved under authoritarian military regimes rather than under democratic auspices and under military regimes that were and are significantly different from traditional South American military governments.

The new regimes are remarkable on two counts: (1) except for Peru, where the regime was comparatively mild, they have been the most repressive in the 20th century history of their respective countries; (2) they have arisen in countries that were among the most economically advanced nations not only in Latin America but of the developing world.

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[1] Alfred Stepan, *The Military in Politics: Changing Patterns in Brazil*, Princeton University Press, 1971, p. 63.

The following discussion attempts to explain why these regimes came to power, their performance in power, their durability and their possible successors. The purpose is to draw observations from their history and evolution which may serve as guideposts for U.S. policy.

II. The Rise of the New Authoritarianism

The Attributes of the New Authoritarianism

The "new style" military regimes, known variously as "bureaucratic-military regimes," the "new authoritarianism," "authoritarian-corporate states," differ from traditional Latin American authoritarianism in at least five respects: [2]

The armed forces rule as an institution rather than as a body subordinate to an individual such as a Trujillo or Somoza.

The military regime adopts a technocratic and bureaucratic approach to policy. Policy is determined and carried out as a result of the interaction of high-level technocrats and the military leaders on the basis of their shared values and goals rather than on the basis of attempting to meet the varying and conflicting economic demands of all sectors of society, and particularly those of the "popular" sector (the working and lower middle classes).

The very vehicles for expressing these demands—elections, legislatures, political parties, the media and labor unions—are suppressed.

Little dissent is permitted, and dissenters are dealt with harshly.

There is a strong commitment to economic development and to a particular ideology of development. In Brazil, Argentina, Chile, and Uruguay, the ideology of development is that of internationally-oriented free enterprise, despite the fact that in Brazil, Argentina and Uruguay, state-owned enterprises continue to play an important role in the economy. Its hallmarks are the promotion of the development of heavy industry and of conditions favoring foreign private investment, the opening of the economy to competition from abroad through lower tariffs and reduction of non-tariff barriers, orthodox monetary and fiscal policies, and the curtailment of labor's bargaining power. In Peru, however, under the regime of General Velasco Alvarado, 1968–75, the policy was markedly different. The state was to be the prime mover of development, by carrying out a social and economic revolution and exerting a dominating role over all phases of the economy primarily through its ownership of basic industrial sectors such as mining, public utilities and petroleum.

The Reaction to Populism

That the new authoritarianism arose in precisely the countries that were among the most modernized and most economically developed

[2] There does not seem to be a consensus among scholars as to the distinguishing features of the "bureaucratic-authoritarian state." The attributes given here are based on the author's interpretation of: (1) the definitions of David Collier, "Introduction," and Guillermo O'Donnell, "Tensions in the Bureaucratic-Authoritarian State and the Question of Democracy" in *The New Authoritarianism in Latin America*, edited by David Collier, Princeton University Press, Princeton 1979, pp. 4–5 and p. 292, respectively; (2) on the observations of other contributors to that volume.

of Latin America is no accident. In these countries, it was a reaction to the populism that has been the major political force in South America since at least the 1930's. Latin American populism was the response of the urban middle classes to the depression of the 1930's and particularly to the failure of the elites of the landed, commercial and export interests to prevent unemployment and the decline of the levels of living suffered during the period. Since the late 19th century, exports of primary products had brought about considerable economic development. However, the middle classes that emerged as a result of this development were substantially different from the middle class in the industrialized countries. According to James Malloy:

> In the main, it was a class of liberal professionals and public and private white-collar employees who were dependent in the sense that they did not control hard sources of wealth but lived off wages, salaries and fees. A large sector of the middle class depended on public employment, a phenomenon often referred to as premature bureaucratization; the tendency of the formal governmental apparatus to expand faster than underlying socio-economic structures.[3]

Originally strongly supportive of the oligarchy, this middle class now rebelled against it. Unable by itself to gain control of governments, it forged coalitions with workers and small farmers to gain control. However, middle class populists, according to Malloy, have tended to look upon these allies as "backward groups whose main role was to follow the lead of the populist elite, that is the progressive sectors of the middle class."[4] The refusal of the working classes in Argentina under Peron to be dominated by the middle class populists helps to explain the political turbulence of the most developed and balanced economy in Latin America.

According to Malloy, Latin America populist political parties had three declared goals: (1) achieve economic independence from the industrialized countries and particularly the United States, i.e., "anti-imperialism"; (2) eliminate semi-feudal institutions and policies; and (3) promote social benefits for all sectors of the nation. These goals were to be achieved with the state and its bureaucracy controlling the nation's resources to assure their "local reinvestment and equitable distribution."[5]

While populism was statist, Malloy writes, it was not socialist. It was perceived by its leading exponents as a rejection of both socialism and capitalism, and, accordingly, as a third route to economic development. While it was rhetorically anti-imperialist and anti-capitalist, populism held that the economic backwardness of their countries made it impossible for them to do away with capitalist internal trading and financial system.[6] The countries could achieve effective independence from "imperialism that made them semicolonial appendages" by a process of evolutionary reform that would reduce the power of the local oligarchy. This oligarchy, according to the populists, "identified its interests with those of the imperial powers, thereby becoming agents who plundered the local economy for the benefit of their foreign allies."[7]

[3] James M. Malloy, "Authoritarian and Corporatism in Latin America," University of Pittsburgh Press, Pittsburgh, 1974, p. 8.
[4] Ibid., p. 12.
[5] Ibid., p. 11.
[6] Ibid.
[7] Ibid., p. 10.

Populist regimes mobilized multi-class support in three ways: (1) they offered symbolic participation via charismatic leadership (Vargas and Peron), nationalist rhetoric and acts such as the expropriation of foreign corporations; (2) they increased wages and salaries in the private sector, expanded public employment and raised public salaries; (3) they organized vertical organizations in which labor, management, independent professionals, and small farmers were grouped together under the auspices of the state to promote cooperation and mutual understanding.[8]

The most serious attempts to apply this corporate principle of organization were taken by Vargas of Brazil in his *Estado Novo* concept that took shape in the 1937–45 period and by Juan Peron in the 1946–55 period. Although the corporate state never came close to being realized, even in these two countries, it remains a powerful idea as the attempt of the military regime to build one in Peru in 1968–75 illustrates. Despite quite opposite economic policies from those of Velasco Alvarado, the corporate idea still lurks in the other authoritarian modernizing regimes of South America.

"By the 1940's," Malloy writes, "the principles of a nationalist-oriented welfare state had become so deeply implanted that even status quo regimes at least had to pay lip service to them." [9]

The Economic Background

There was, however, an inherent contradiction between the populist objective of state-sponsored economic development and increasing the levels of mass consumption. Inflation was the direct result of the inability of populist regimes to overcome this contradiction. From the 1940's to the 1960's, inflation was to prove intractable in most of the more developed countries of South America. It was the root of the balance-of-payments crises which in turn were the main elements in the stop-and-go economic performance of Argentina, Peru, and Chile, the secular stagnation of Uruguay and the drag on Brazilian economic expansion.

It is a mistake, however, to lay exclusive responsibility for the rise of the new authoritarianism on the inability of populist governments to control inflation or, for that matter, to assign overwhelming importance to the economic problems of the region. Colombia and Venezuela also shared many of the same problems and yet managed to deal with them under a competitive, pluralist political system. Albert Hirschman, who has explored the problems of Latin America's economic development as profoundly as any one, has this to say: "As everyone knows, purely political factors—and in particular the reactions to the Cuban revolution—the 'great fear' of the Latin American ruling groups, the spread of guerrilla tactics and the determination of the United States to prevent a 'second Cuba'—have contributed mightily to the installation of authoritarian regimes in one Latin American country after another since 1958." [10]

The table below summarizes the performance of these countries with respect to consumer prices and to gross domestic product (GDP–GNP less foreign transactions).

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[8] Ibid., p. 14.
[9] Ibid.
[10] Albert O. Hirschman, "The Search for Economic Determinants" in *The New Authoritarianism in Latin America,* op. cit., p. 71.

SOUTH AMERICA: NEW STYLE MILITARY REGIMES—AVERAGE ANNUAL RATES OF GROWTH OF REAL PER CAPITA GROSS DOMESTIC PRODUCT AND CONSUMER PRICES PRIOR TO COUPS, 1964–76

[In percent]

Country	Year of coup	Precoup growth rates: 1950 to coup year — GDP	Precoup growth rates: 1950 to coup year — Prices	Precoup growth rates: 3 yr prior to coup — GDP	Precoup growth rates: 3 yr prior to coup — Prices
Brazil	1964	3.6	32.2	2.7	50.7
Argentina	1966	1.3	25.0	4.1	23.5
Peru	1968	2.8	8.0	1.2	12.1
Uruguay	1973	−.3	27.9	−1.0	35.4
Chile	1973	2.1	25.5	2.1	39.4
Argentina	1976	2.2	28.8	2.6	71.4

Source: Per capita GDP, 1950–76, U.N. Economic Commission for Latin America (ELCA) (Spanish) Series Historicas del Crecimiento Economico y Social de America Latina, Santiago, Chile, 1977; consumer prices: International Monetary Fund (IMF), International Monetary Statistics, "Yearbook 1980," 1981.

The table clearly brings out the chronic inflation of the region, with only Peru showing a relatively moderate rate of price increases. Uruguay's secular stagnation stands out as does Argentina's slow growth in the 1950–65 period. On the other hand, Brazil's rate of growth is high by any standard, and Peru's growth rate reflects some dynamism.

In the immediate pre-coup period, the data reflect—though, because they are averages, in a greatly understated way—the acceleration of inflation in all countries except Argentina. With regard to GDP, Brazil, Peru, and Uruguay show a substantial deterioration as opposed to the long-term trend (again understated because of averaging). Chile's performance, however, shows about the same average annual rate of growth while Argentina shows a much better performance than the long-term trend.

In the coup years themselves, inflation spurted upward in all countries, and GDP grew little, if at all. However, it is impossible to assert a one-way causation to economic factors as determining the decisions of the respective military establishments to overthrow the elected governments. Parliamentary stalemate, work stoppages, political turmoil and violence interfered with economic activity and worked to shoot the inflation rate up and the GDP growth rate down. The struggle for power over economic, social and foreign policy was more the cause of poor economic performance than the result of it.

III. The Breakdown of Democratic Regimes

An examination of the events leading up to the breakdown of democratic government and the military take-overs tends to confirm the importance of noneconomic factors in the rise of the new authoritarian regimes.

Brazil—1964

By the early 1960's, the feeling was widespread among the military and the politically conscious population of Brazil that the political institutions of the country were in crisis. Since 1945, no single major party had significantly increased its following. Elections were run on the basis of short-term alliances in which frequently parties that stood for different policies at the national level allied themselves at the local and state levels. Populist parties that joined together with their closest ideological counterparts found themselves sharply divided over policy once they were in office.

In the context of sharply reduced growth and rising inflation, one of the symptoms of the political crisis was the frequency and relative inconclusiveness of elections and other kinds of political confrontation. According to Alfred Stepan, normally in Brazil, the presidential election, which was held every five years, was the only political contest in which national power was perceived to be at stake. However, between October 1960 and March 1964, six major political confrontations took place, all of which were, in Stepan's words, "relatively inconclusive." [11] The first of these was the brief but stormy term of Janio Quadros who was elected in October 1960 but resigned after only seven months in office because of his inability to get Congress to approve a stabilization program and other reforms and who, according to Stepan, had hopes of being given a Gaullist mandate to carry out major political and economic reforms.[12] The mandate was not forthcoming.

The second confrontation took place after Quadro's resignation between Vice President Goulart and the military who opposed his succession to the office of the presidency because of his radical populist and neutralist views. The crisis, which verged on "near civil war," in Stepan's phrase, was resolved only after the armed forces permitted Goulart to assume office but under new rules that sharply curtailed presidential powers.[13]

The "fiercely contested" congressional and gubernatorial elections of 1962 were the third polarizing event of the period. These were immediately followed by President Goulart's "long, bitter campaign" to hold a plebiscite to regain former presidential powers and the plebiscite in itself of January, 1963, which he won. In October of that year, Goulart set off another confrontation when under pressure of the armed forces, he requested Congress to grant him authority to declare a form of martial law for 30 days. The request provoked such a storm of opposition from both the left and the right in Congress that he withdrew the request three days later.[14]

Finally, Goulart's campaign in March 1964 to push for his reform program brought political polarization to the breaking point and swung opinion within the military to the position that Goulart had to be removed from office. Goulart's campaign began with a massive rally on March 13, 1964, which was widely televised and broadcast. Announcing that he intended to carry out far-reaching reforms in the land tenure system, constitutional reforms such as the enfranchisement of illiterates (which would have almost doubled the size of the Brazilian electorate) and an oil company nationalization program, Goulart was perceived to be threatening to by-pass Congress if it refused to go along with his proposals. The threat of the use of force, was, according

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[11] Alfred Stepan, "The Military in Politics: Changing Patterns in Brazil," The Rand Corp., Princeton University Press, Princeton, 1971, p. 151.
[12] Ibid., p. 148.
[13] Ibid., p. 178.
[14] Facts on File Yearbook, 1973, p. 352.

to Stepan, implicit in Goulart's attempt to mobilize the populist forces of the country. (Similar rallies were scheduled for principal cities throughout the country.) [15]

In response to this perceived threat, the governors of the states of Sao Paulo and Minas Gerais announced on television that they were making arrangements to defend their states against any attempt by Goulart to carry out a revolution from above.[16]

Within the military, the feeling grew that the nation was preparing for civil war, as many different groups began to arm themselves. The crowning blow, however, was a naval mutiny on March 26, 1964, in which more than a thousand sailors and marines barricaded themselves in an armory in Rio de Janeiro. Goulart's refusal to support his navy minister in attempting to quell the mutiny was interpreted as blatant interference with military discipline and convinced the remaining constitutionalists within the armed forces that their very existence was threatened by Goulart's continuance in office. On March 31, the army launched its coup and within forty-eight hours had taken complete control of the government.[17]

The Brazilian military coup of 1964 was of a different order than previous military interventions. These had reflected the predominant view among the armed forces that they should be "a moderating" influence. That is, they could check or remove an administration believed harmful to the nation and transfer power to alternative civilian groups but should not overthrow the parliamentary system itself or undertake to assume direction of the country for long periods of time.[18] Well before 1964, however, the view had gained ground among the military that no existing political group was competent to rule the country. This view and its corollary that the military should become the director and not merely the moderator of the entire political system had been developed at the Superior War College over a period of years. At this institution, civilian experts in all aspects of economic development interacted with military officers, both as fellow students and as lecturers. The experience led to the formation of a strong cadre of senior military officers and civilian technocrats used to working with each other. More important it also gave the officers the confidence that they could in collaboration with their civilian advisers govern the country better than the old political parties had done.[19]

Argentina: 1966 and 1976

The Brazilan example was not lost on the Argentine military. Like their Brazilian and other South American counterparts, they had long conceived themselves to be the non-partisan guardian of the nation's destiny. In previous interventions in politics, they had restored civilian government as soon as they believed it feasible to do so. Thus, after the ouster of Peron in 1955, they ruled until 1958 when they thought it was safe to turn power back to the political parties. In 1962, they deposed President Frondizi because he had legalized the Peronist parties for the 1962 elections. In 1963, the Argentine military, still reluctant to wield governmental power directly, permitted new national elections to be held. The Radical party

[15] Stepan, op. cit. 199–201.
[16] Ibid.
[17] Ibid., p. 206.
[18] Ibid., p. 63–64.
[19] Ibid., p. 186.

of Arturo Illia won the election with a plurality—the Peronists having been denied the right to run their own candidates. When it became apparent, however, as a result of several Peronist victories in provincial and local elections, that the Peronist party would win the next national elections, the military deposed Illia and named General Juan Carlos Ongania, a retired commander-in-chief of the army, as president. Taking their cue from Brazil, the Argentine armed forces had come to the conclusion that they would have to rule for some time if they were ever to rid Argentina of Peronism.[20]

They changed their minds, however, when after four years of military rule, escalating terrorist violence made it clear that Peronism was still a political force to be reckoned with.[21] Ongania was deposed in March, 1970 and replaced by a junior general Roberto Levingston who was apparently an interim choice while the armed forces decided what to do next. After a few months in office, Levingston was ousted, and the commander-in-chief of the army, General Alejandro Lanusse was named president in March, 1971. Lanusse, the leader of the liberal faction of the armed forces, prepared the way for a return to constitutional government. In the elections of March 1973, the Peronist party, which fell short of a majority by only a small margin was declared the winner. In elections held in September, Peron himself was elected president.

Peron died in office on July 1, 1974. His successor, Isabel Peron, his widow and vice-president, governed in name only. Her advisers, all from the right wing of the Peronist movement, not only succeeded in polarizing the movement but in plunging the country into near-chaos as inflation rose out of control, and terrorist violence seemed headed the same way. When the armed forces intervened this time, in 1976, the hard-liners were in control and determined to crush not only the terrorist left but to put an end to populism as a political force.

Peru

While populism has been a major force in Peru's political life since the 1920's, collaboration between the conservative parties and the military had effectively kept it from winning power. Many of the populist tenets came to be held, however, by a relative newcomer to Peruvian politics, the Popular Action Party whose presidential candidate, Fernando Belaunde Terry, won the election of 1963. Belaunde's term was marked by a fierce political struggle over reform, the rise of guerrilla violence, and a major dispute with the United States over the expropriation of a U.S.-owned enterprise, the International Petroleum Company.

By 1964, the high command of the armed forces had become increasingly convinced that the political parties were bringing about the disintegration of the country. For several years the military's "think" tank, the Center for High Military Studies (CAEM) had been analyzing the country's problems from the point of view of national security. Focusing on Peru's potential for national defense against a possible Communist or a Chilean attack, the CAEM studies concluded that the country was too under-developed to defend itself

[20] Peter G. Snow, *Political Forces in Argentina*, Praeger Publishers, New York 1979, p. 68.

[21] Ibid., p. 142.

adequately, and its lack of development was the result of its dependence on foreign countries, particularly the United States and the power of the Peruvian oligarchy. Julio Cotler cites one particular statement in a CAEM study which he believes sums up the essence of the CAEM's findings. "The sad and desperate reality is that, in Peru, real power is not Executive, Legislative, Judicial or Electoral Power, but that which is held by landowners, exporters, bankers and North American companies." [22]

Chile

Argentina, Brazil and Peru, though different in many respects had one thing in common: the military regimes that came to power in the 1960's were following a tradition of political intervention that went back a long way. On the other hand, in Uruguay and Chile, the armed forces had not intervened in political affairs in decades, although the pretexts for intervention certainly existed. Both countries had long suffered economic stagnation, inflation and periods of ineffectual government. Both had well-established labor movements, with Communists and Socialists commanding the allegiance of a substantial part of organized labor. Moreover in Chile, as a result of its alliance with the Socialists, the Communist party had been a major political force since 1938 when the candidates of the Popular Front comprising Socialists, Communists, and the Center Radical Party won the presidential elections.

The Chilean armed forces thus had long considered themselves politically neutral and subordinate to civilian control. Their change into a dictatorship determined to transform the political system under which Chile had lived under for generations did not come overnight. The same process of erosion of the center as had occurred among the Chilean electorate at large led eventually to the defeat of the constitutionalists within the armed forces who for decades had been the dominant faction.

Many factors contributed to this disintegration of the center forces. Chilean politics for generations had been marked not only by a high degree of competitiveness but, because of that competitiveness, no political party after 1925 had received a majority of the vote in either a municipal or congressional election. In fact, according to Arturo Valenzuela, in all but two elections, those of 1965 and 1967, in which the Christian Democrats obtained 42.3 percent and 35.6 percent respectively, no party received more than 30 percent of the vote.[23] A second feature of Chilean politics was that its five major and several minor parties covered the full political spectrum. A third characteristic of the system was that it was highly polarized between left and right.

Valenzuela stresses that polarization developed as a result of the instability of the center in the Chilean politics. In his view, this was the major factor in the chaos of the Allende years and the rise of the new authoritarianism in Chile. Just as no single political party was

[22] Julio Cotler, "A Structural-Historical Approach to the Breakdown of Democratic Regimes," edited by Juan J. Linz and Alfred Stepan, the Johns Hopkins University Press, Baltimore, 1978, p. 193.

[23] Arturo Valenzuela, *The Breakdown of Democratic Regimes: Chile*, The Johns Hopkins University Press, Baltimore, 1978, p. 3.

able to win a majority in the Chamber of Deputies, neither was any single party nor tendency able to win the Presidency on its own. Accordingly, parties had to form coalitions in order to influence policy and enjoy patronage. The parties to the coalition were not always of similar ideology. Candidates of the center won the presidency in 1938 and 1946 with the support of the left; the elections of 1932 and 1964, with the support of the right; and the elections of 1952, with support from both left and right. In 1958, although the right won the plurality on its own, centrist forces joined with it to make the government work.[24]

In the 1970 presidential elections, the Marxist Salvador Allende, whose leftist coalition had obtained 43.9 percent of the vote in the 1969 Congressional elections, won only 34.9 percent of the popular vote. Allende's attempt to put through a program of radical social and economic reforms foundered on the combined opposition of the centrist and rightist forces in Congress. In the process Allende's program generated confrontation after confrontation not only at the national level but at the provincial and local levels. Pro-government extremists clashed with the opposition in violent encounters, and polarization intensified as both sides accused the other of subverting democratic institutions and practices.

These included not only the Chilean Congress and the presidency, but the courts, the *Contraloria* (an independent agency similar to the U.S. General Accounting Office but with wider scope and greater power), the constitutional tribunal and the armed forces themselves. Valenzuela attributes not a small part of the blame for the political and economic turmoil to the Chilean media, and to the Central Intelligence Agency. "The media," he writes, "saturated every corner of the small country [and] became the principal exponent of the most extreme views. Opposition papers, and in particular, the influential *El Mercurio* which had received large sums of money from U.S. Intelligence, were particularly skilled in rallying the vast army of opposition groups and organizations.[25] Valenzuela describes several CIA operations against Allende as revealed in a Senate Select Committee report.[26]

What finally turned the tide within the armed forces against constitutionalism was the threat by the revolutionary left to arm the working classes into a parallel and hostile army. The threat proved to be greatly exaggerated. The extreme left was able to organize a few defense squads, but by and large the Chilean working class like the Chilean middle class was not only not willing to support radical social change but was divided even over support of Allende.

Landsberger and McDaniel, citing contemporary public opinion surveys, concluded: "In sum, the working class was incapable of acting as a strong, united bulwark of the Allende government for a variety of reasons, including the weakness of its organizations and the plurality of its members' preferences." [27]

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[24] Ibid., p. 7.
[25] Ibid., p. 79.
[26] United States Senate Select Committee to Study Government Operations With Respect to Intelligent Activities, *Alleged Assassination Plots Involving Foreign Leaders*, U.S. Government Printing Office, Washington, D.C., Nov. 20, 1975, pp. 225–54.
[27] Henry A. Landsberger and Tim McDaniel, "Hypermobilization in Chile," *World Politics*, July 1976, p. 50.

Nevertheless, not even the commanders-in-chief of the three services—all of them stout constitutionalists—could withstand the pressure from within the ranks to oust the Allende government and take control of the nation's destiny.

Uruguay

Prior to the 1973 military take-over, Uruguay had experienced only one coup in the 20th century, that of President Gabriel Terra's in 1933. Terra's coup was neither inspired nor controlled by the military, although they acquiesced in it.[28]

The Uruguayan military tradition was thus constitutionalist. Neither the economic stagnation which began in the mid-1950's nor the social and political tensions of the 1960's which sprang from this stagnation had prompted the Uruguayan armed forces to intervene as their Brazilian and Argentine counterparts had done. Even in the late 1960's, when the Tupamaro guerrillas began to intensify their terroristic campaign, the military did not see fit to take over the government.

The decisive politicizing of the Uruguayan military apparently began in September 1971 when President Pacheco put them in charge of all anti-guerrilla activity. Martin Weinstein writes: "The military, given carte blanche and unhampered by judicial or constitutional restraints, proceeded to employ repressive techniques that moved far beyond those that any administration had dared to employ in any systematic or sustained manner. The use of torture and drugs were weapons the Tupamaros could not withstand. In the ensuing months the army enjoyed almost total success against the guerrillas, all but destroying their infrastructure, capturing hundreds of active supporters and detaining thousands of other suspects." [29]

Their victory over the Tupamaros apparently gave the Uruguayan military a self-confidence they had never had before. How much they were influenced by the Brazilian military's economic performance, or if they were directly influenced by the Brazilians to take over control of Uruguay is not clear. Certainly they had in President Bordaberry a man who had demonstrated a capacity for authoritarian rule and a determination to bring Uruguay out of its long stagnation. The armed forces were not content with a civilian strong-man, however. In February 1973, they mounted what Weinstein calls a "quasi-coup." Bordaberry was permitted to continue in office, but he shared powers with a newly created National Security Council whose members would include the commanders-in-chief and a number of ministers. Congress was later dissolved by Bordaberry. Some deputies were jailed; leftist political parties and organizations disbanded, trade unions were abolished, key labor leaders imprisoned, opposition newspapers were closed, and many editors and reporters arrested.

In early 1976, strains increased between Bordaberry and the military. Bordaberry, according to Arturo Porzecanski, wanted to abolish all political parties permanently and establish an absolute corporate state "with an all-powerful executive and a corporate chamber consist-

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[28] Marvin Alisky, *Uruguay: A Contemporary Survey*, Frederick A. Praeer, New York, 1969, pp. 32–33.

[29] Martin Weinstein, *Uruguay: The Politics of Failure*, Greenwood Press, Westport, Conn., 1975, p. 128.

ing of representatives of the land-owning industrialist and professional classes." [30] The military were ambivalent. In Porzecanski's view, most top military officers favored as a long-run solution a "limited democracy" in which a new generation of politicians would slowly acquire increasing authority in administration and political decision-making within limits set by the military.[31]

Bordaberry apparently rejected this plan. On June 12, 1976, he resigned under pressure and was replaced by an interim president and then by Aparicio Mendez, a conservative politician and constitutional lawyer. Under the military's plan, Mendez was to serve as president for five years. He was then to be replaced by the choice of the two largest political parties who also would rule for five years. Free elections with more than one candidate would be held five years thereafter—i.e., in 1986.[32]

IV. The Military in Power

Primarily because of Brazil's rapid growth under its military regime, the view has arisen that the bureaucratic-authoritarian state may be the most effective way of bringing about accelerated economic growth in developing countries.

How have the economies fared under the new style military regimes?

Military Populism: Peru

Before answering this question we should distinguish between the Peruvian military regime of General Velasco Alvarado during the period 1968–75 and the military regimes of Argentina, Brazil, Chile, and Uruguay.

The Peruvian military regime under Velasco Alvarado carried out a virtual social and economic revolution. As one of the first actions it expropriated the U.S.-owned International Petroleum Corporation. It then executed a variety of reforms touching almost every aspect of the economy—land ownership, the tax system, education and labor-management relations. It nationalized hundreds of foreign-owned companies. In foreign policy, it set about improving relations with the U.S.S.R. and other Communist countries and became a leading advocate of Cuba's return to active membership in the Organization of American States. In addition, it bought helicopters, artillery and other arms from the Soviet Union and other Eastern European countries as well as jets and other military equipment from Western European countries.

Peru's leftist revolution from above came to an end in August 1975 when General Velasco was ousted in a shift to the right within the Peruvian armed forces because of the disastrous economic situation attributed to Velasco's policies. The more conservative economic policy followed by Velasco's successor checked but did not reverse the deterioration of the economy. Overwhelmed by problems and eager to restore their badly damaged unity, the Peruvian armed forces

[30] Arturo C. Porzecanski, "Authoritarian Uruguay," *Current History*, February 1977, p. 85.
[31] Ibid., p. 85.
[32] Ibid.

allowed a constitutional assembly to be called by June 1978. In the national elections of May 1980, Belaunde, who had been removed from office twelve years before, emerged the winner and was permitted to assume the presidency again.

The Anti-Populism Drive

Where Peru undertook to push the populist strategy further than it had ever been taken in South America, the other military regimes of the region set out to destroy populism as a major political force. To that end, the labor unions were stripped of their legal right to strike or otherwise severely restricted. Wages were adjusted by the government in accordance with its view of what the economy could afford, usually substantially less than the growth of productivity. Foreign investment was encouraged with a variety of new incentives and guarantees to remove the shadow of hostility and uncertainty cast by the vascillating policies of former regimes. Tariffs were lowered, and quantitative restrictions on imports were reduced sharply or removed. Political party activity was prohibited or severely restricted. Dissidence was harshly treated. Tight monetary and fiscal policies were adopted in most countries at one time or another. Foreign exchange rate and tax policies were designed to give more incentives to large agricultural producers and exporters, minerals producers and exporters as well as to manufacturers.

There were, however, substantial differences in emphasis on these various policies as between the military regimes of the various countries and between the successive military administrations within the same country. These differences are brought out below in the discussion of the individual regimes.

CHILE

The Chilean military regime probably went furthest in attempting to dismantle the welfare-populist state and convert Chile into a model market economy. Under the influence of a group of young economists trained at the University of Chicago, the so-called "Chicago boys," monetarist policies were rigorously carried out. The government's sector of the economy, swollen by the large number of firms that had been nationalized under the Allende regime, was sharply reduced.

Price controls were abolished, interest rates freed from long-established ceilings. Foreign banks were allowed to establish themselves in the country. Duties on imported goods were brought down to about 10 percent as compared with an average tariff level of 100 percent as of 1973, and some tariffs as high as 600 percent.[33] Government spending was reduced so that the public sector deficit which had been 55 percent of spending in 1973 had dropped to 4 percent in 1978. This was accomplished by dismissing many workers in the public sector, freezing the wages of others who remained and by the divestiture of many government-owned firms. The tax system was reorganized, tax collection procedures improved. The multiple exchange rate system was unified.[34]

The short-term results of the reforms carried out by the Chilean regimes were almost disastrous. Unemployment reached a peak of 19.6

[33] *The Economist*, "Chile", Feb. 2, 1980, p. 18.
[34] Ibid., p. 21.

percent of the labor force in March 1976. Real wages fell by about a third between 1973 and 1976. Not all of the costs of unemployment and loss of real wages are attributable to government economic policy, however. The world recession of 1975 hit Chile hard, as the price of copper, the country's main export fell sharply, and GDP fell 14 percent. By 1977, however, the economy was well on its way to recovery and expansion, and the rate of increase of per capita GDP has remained high since then. However, it was not until 1979 that the 1971 level of real per capita GDP was recovered. Income inequality had also apparently increased up until 1976, but wage increases and social spending by the regime since then may have made the problem of income inequality no worse than it was before the coup of 1973.[35] The unemployment rate had declined to about 10 percent in 1980, but about 5 percent of the labor force was employed under the government's minimum employment program.[36]

The number of persons arrested for political reasons since the coup may be 100,000 or more.[37] Most of these arrests occurred immediately after the coup on September 11, 1973, and most were released apparently by November of that year. By early 1976, an estimated 4,300 were in police custody, many without any charges having been made against them.[38] By the end of the year, most of these prisoners had been released but new batches were taken in subsequent years, and the practice of torture in interrogations still continued. Amnesty International surveyed some 1,500 cases of detainees during 1979 and found that most of those arrested "were taken to secret places of detention and tortured by, among other methods, electric shock, suspension and severe beatings." [39]

In 1980, about 1,100 persons were arrested on political grounds and 96 complaints of serious mistreatment including torture were received by the Chilean courts.[40] There were no "disappearances" (abductions of persons never heard from again). In fact, since 1977, there have been no reported disappearances, although 635 cases from the period 1973–77 remain unsolved.[41]

Some liberalization has occurred in the last few years. While the political parties remain formally dissolved, and freedom of speech and assembly are still restricted, some criticism of government policies is permitted. Labor unions continue to be restricted in their activities but collective bargaining except for the civil service and maritime sector has been restored and the right to strike though hedged with restrictions, has been restored.[42] The media are generally not subject to prior censorship, but they are closely monitored. The government also retains the right to banish persons to remote areas for up to three months without charges, court review or the right of appeal.[43]

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[35] Department of State, *Country Reports on Human Rights Practice for 1980*, Washington, 1981, p. 372.
[36] Ibid.
[37] Lester A. Sobel, Chris Hunt, and Mary E. Clifford, editors, *Latin America 1973*, Facts on File, Inc., New York, 1974, p. 128.
[38] Congressional Research Service (CRS), Library of Congress, *Human Rights and U.S. Foreign Assistance*, November 1979, p. 169.
[39] *Amnesty International Report 1980*, Amnesty International Publications, London, England, 1981, p. 119.
[40] Department of State, *Country Reports on Human Rights Practices for 1980*, Washington, D.C., 1981, pp. 369, 370.
[41] Ibid., p. 369.
[42] Ibid., p. 376.
[43] Ibid., p. 375.

Economic and political policies differed greatly between the Ongania regime (1966–70), the Levingston-Lanusse period (1970–73), and the Videla regime (1976–81). They seem to be changing once again under the recently installed Viola regime.

During the Ongania period, a free market ideology was proclaimed but not publicly stressed, although reforms designed to liberalize the economy were initiated. The labor unions were forbidden to engage in political strikes, that is, strikes undertaken for political ends, but strikes for better pay, fringe benefits, better working conditions and to demand redress of work grievances were permitted and occurred with some frequency. The stabilization program relied on an incomes policy rather than on tight monetary and fiscal policies. While the unions were given little choice as to the specific wage adjustment formula chosen, considerable care was taken to make it as acceptable to organized labor as possible.

While employers could not increase prices beyond the current inflation rate and increases in the cost of inputs, they were free to grant higher wages than the wage guidelines indicated just as long as they did not increase prices above the guidelines. Higher productivity enabled many firms in the more modern sectors of the economy to grant higher wages. Foreign investment was encouraged, and taxes on agricultural exports were reduced to give producers and exporters greater incentives. Import duties were substantially reduced from the excessive levels inherited from previous governments but only after consultations with the affected industries and some compensatory tax concessions to them.

The program conceived and executed by economy minister Krieger Vasena in the period 1967–69, was highly successful in strictly economic terms but a failure politically. Even though unemployment had been reduced, and real wages, particularly in the sectors where the peronist labor unions were strongest, had risen, the loyalty of the unions to exiled leader Peron and to the peronist movement remained intact.

This became apparent in May 1969, when a series of riots and demonstrations erupted in several cities, and terrorist violence took on systematic features. Ongania was deposed by the commanders of the armed forces in June 1970 and replaced by a relatively junior general, Roberto Levingston. In March 1971, Levingston was replaced by the commander of the army, General Lanusse. During the Levingston-Lanusse period, the stabilization program was virtually abandoned, and economic policy became more populist. The result was an intensification of inflation, renewed balance-of-payments problems, lagging growth and increased political activity in a climate marred by increasing terrorism.

After the interval of the presidency of the two Perons—Peron died in July 1974 after about nine months in office and was succeeded by his wife and vice president Isabel—the Videla regime which ousted Mrs. Peron in March 1976, adopted a hard-line political and economic approach. Between 1976 and 1979 the number of persons abducted by the security forces and never accounted for—the so-called "disappeared" was estimated from 6,500 to 20,000 persons, according to the

State Department's human rights report of 1980.[43] The report notes that "there is substantial evidence that most of the persons were adducted by the security forces and interrogated under torture; as most have not reappeared, many observers believe they were summarily executed." [44] Since late 1978, the number of disappearances has declined sharply. In 1976 and 1977 thousands of persons "disappeared." In 1978, about 500 cases of disappearances were reported. In 1979, the number was 44,[45] and in 1980, 28.[46]

The number of persons held without charges has also been reduced significantly. Since 1974, about 8,200 persons have been held for political reasons under government custody. Most have been released. In December 1980, the Argentine government acknowledged that it was holding about 1,550 persons. Of these about 600 had been tried and convicted, another 400 were in the process of being tried, and about 550 were being held without trial or charges. As of early 1981, eight new arrests had been made, and 888 persons have been released from detention.[47]

On the economic side, the minister of economy, Martinez de Hoz, froze wages and carried out a monetarist stabilization policy. New incentives and assurances were given to promote foreign investment in Argentina. Import duties were drastically cut. The state enterprises, however, were not sloughed off and continued to be a drain on the budget, so much so that Martinez de Hoz, who resigned in mid-March 1981 after five years in office, is reported to have said, "State expenses are the root of the problem." [48]

The problem was his lack of success in turning the Argentina economy around on to a path of self-sustaining growth. While he had succeeded in bring the inflation rate down from over 400 percent to about 100 percent in 1980, this was still very high.

Martinez de Hoz's replacement, Lorenzo Sigaut has been confronted with immense problems. By July 1981, unemployment had doubled over last year, the inflation rate had moved into triple digits, three devaluations had reduced the value of the peso by two-thirds since the beginning of the year. According to a report in the Washington Post, rumors of a coup against the Viola regime were widespread in Buenos Aires in early July, 1981.[49]

The article reported that the navy commander-in-chief, one of the three-man junta that speaks for the armed forces, had warned president Viola he would be replaced if he does not resolve the crisis quickly. A New York Times article of the same date reports that the Argentina navy was pressing for a return to civilian rule.[50]

BRAZIL

There have been altogether five different military presidents in Brazil since the 1964 coup. Under General Castello Branco, the first

[43] Department of State. *Country Reports on Human Rights Practices for 1979.* Washington, D.C., February 1979, p. 239.
[44] Ibid.
[45] Ibid., p. 240.
[46] Department of State, *Country Reports on Human Rights Practices for 1980.* Washington. D.C., 1981, p. 329.
[47] Ibid., p. 330.
[48] The Wall Street Journal. Mar. 24, 1981.
[49] The Washington Post, July 5, 1981.
[50] New York Times, July 5, 1981.

president, (1964–67), strict austerity measures were carried out, and heavy emphasis put on reforming the economy along free enterprise lines. Wages were frozen (despite the inconsistency with a free market philosophy), government expenditures slashed, credit tightened, and strikes were banned.

The old political parties were abolished. In their place, a government-sponsored party, the National Alliance of Renovation (ARENA) was established as the majority party with its membership consisting largely of persons militating in the former conservative parties. A second party, the Brazilian Democratic Movement (MDB) was authorized as an opposition party to impart some legitimacy to the new political system.[51] The predominance of ARENA over the MDB was to be assured by what Philippe Schmitter has termed "periodic purge and manipulation by the executive." [52] The power of the executive to keep both parties, but particularly the MDB, under control resided in the executive's authority to suspend political rights and eligibility for public office for a period of 10 years, to remove any official in the three branches of the government, and the power of the government to arrest and imprison any person suspected of subversive activities. These could and were often interpreted as including "defamation" of the government and armed forces.

These powers were frequently used during the administrations of generals Castello Branco, da Costa e Silva (1967–69), and Medici (1969–74). More than 300 politicians were deprived of their voting rights and eligibility for public office for ten years by the Castelo Branco administration. Among those included were ex-presidents Quadros, Goulart, and Kubitschek. Government ministries, state legislatures, municipal councils, labor unions and student organizations were urged, and several state governors were removed.[53]

In addition, anti-coup officers and especially those who had been promoted out of rank order by the Goulart regime were purged. In April 1946, for instance, 122 officers were formally expelled from the military and more expulsions continued throughout the year. Also many officers who were considered to have shown "weak" revolutionary attitudes were told they could expect no promotions ever if they remained on active duty.[54]

The economic performance of the Castello Branco administration was only fair. Inflation was only slightly reduced; growth did not improve over the pre-coup levels; and foreign investment failed to respond to the new incentives. Moreover, the recession that gripped the industrial southeast of the country continued.

The Brazilian economy only really recovered and expanded under the presidencies of Generals Costa e Silva and Medici with Delfim Netto as finance minister, 1967–74. Robert Kaufman writes that while the economic strategy remained the same as under his predecessors—the strengthening of upper middle class demand for consumers dur-

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[51] Russell H. Fitzgibbon and Julio A. Fernandez. "Latin-America: Political Culture and Development," Prentice-Hall, Inc., Englewood Cliffs, N.J., 1981, p. 281.

[52] Philippe C. Schmitter, "The Portugalization of Brazil," in Authoritarian Brazil, edited by Alfred Stepan, Yale University Press, New Haven, 1973, p. 281.

[53] John J. Johnson, "Brazil in Quandary," *Current History,* January 1965, p. 14.

[54] Stepan, op. cit., p. 223.

ables and attracting direct foreign investment and import credits from abroad—Delfim opted for a looser monetary and credit policy, preferring predictable annual price increases of about 20 percent rather than absolute stability. Wage rates were indexed but apparently at less than the rise of the cost of living, and exchange rates were indexed. Exports were subsidized. Trade was liberalized. Beginning in 1970, the producers' goods industry was stimulated, and a variety of large scale investment projects were pushed.[55]

In Delfim's seven years, the Brazilian economy grew in real terms at an average annual rate of 10 percent. Delfim's term was helped by favorable world economic conditions, Kaufman notes—world trade expanded rapidly, and Euro-dollar funds became plentiful for investment in the third world countries. Delfim's ascendency coincided, however, with increasingly repressive measures. Kaufman comments: "An outburst of wildcat strikes, scattered terrorism and assorted acts of peaceful protest furnished the pretext for hard-line military factions to take the offensive." [56] The president was granted unrestricted powers to protect national security—and these were used to the hilt.

Arrests, dismissals, police surveillance and strict censorship continued without much relief during the first three years of the Medici administration (1969–74). This administration was particularly noted for its use of torture in dealing with actual or suspected opponents, Kaufman writes.[57]

President Ernesto Geisel (1974–79) a moderate, was widely expected to initiate a period of "decompression" or relaxation of tensions caused by the repressive tactics of the Costa e Silva and Medici regimes. Instead, during the first three years of his administration, he continued the repressive measures of his predecessors, though on a lesser scale. He also suspended Congress for several months after the opposition party, the MDB, had blocked a government bill to reform the judicial system. To prevent the MDB from being able to kill future government-sponsored bills and to deny it any possibility of winning state or residential elections, he enacted a number of constitutional amendments governing future elections and congressional procedures.

A turning point in the Geisel administration occurred in late 1977, when massive strikes by university students and growing public anger over the security forces' use of repressive procedures threatened to bring about a violent confrontation between the regime and the public. Arbitrary arrests, suspicious deaths of political prisoners and incidents of torture decreased further. In 1978, Geisel ousted several hard-line generals from their posts, relaxed press censorship and reaffirmed his commitment to "abertura" or political liberalization. He also was able to muster sufficient support among the armed forces for his choice, General Joao Figueiredo to succeed him as president.

During his term, Geisel moved to reduce Brazil's dependence on military and foreign policy ties with the United States. In March 1977, his administration, citing a State Department report that was critical of Brazil's human rights record as interference in Brazil's

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[55] Robert R. Kaufman, "Industrial Change and Authorization Rule," in *The New Authoritarianism in Latin America*, op. cit., pp. 172–173.
[56] Ibid., p. 173.
[57] Ibid., p. 174.

internal affairs, cancelled a 25-year-old program of U.S. military assistance and refused a U.S. offer of $50 million in military aid.[58] A $4.5 billion contract was signed with West Germany, over U.S. protests over the lack of adequate safeguards, to provide nuclear power plants, technology and facilities to enrich uranium and process the fuel into plutonium.[59] Large arms orders were placed in Great Britain and France, and commercial ties were expanded with the Communist countries. Brazilian representatives joined the non-aligned nations' resolution against Zionism, colonialism, neo-colonialism, racism and apartheid and strengthened ties with the Marxist Angola regime.

A huge, state-sponsored development program was initiated, and domestically owned businesses were favored with heavily subsidized loans for a wide variety of agricultural, industrial and commercial projects. The consequences of the expansionary program were a steep rise in the inflation rate and a substantial slowing of the growth rate as compared with the Delfim years.

President Figueiredo has attempted to carry out the commitment made by his predecessor to bring about a political liberalization that will pave the way to a full return to the democratic system. Legislation abrogating civil rights and liberties guaranteed in the Brazilian constitution of 1946 has been repealed. Amnesty has been declared for all former enemies of the regime except those accused of criminal acts of violence. Almost all restrictions on the press have been removed, although the government still exercises controls over television and broadcasting. Student organizations have been permitted to re-establish themselves. The restrictions on labor union activities have been mostly removed, and strikes, even of civil servants, have been permitted. The two-party system has been dissolved, and new parties have been allowed to organize. Even the various Communist parties and splinter groups have reappeared.

Accompanying the liberalization process have been strikes, demonstrations, and generally uninhibited criticism of the government and the military. Figueiredo has tacitly approved the warnings of some of his cabinet ministers that excesses in the name of democracy would not be tolerated. He has not, however, resorted to repression, despite the pressure exerted upon him by the clearly disturbed hard-line factions. These are believed to be responsible for a number of terrorist incidents in 1980 and 1981. The possibility that the liberalization process will be reversed should the hardline factions manage to become ascendant again within military circles can not be dismissed.

With Delfim Netto again the economy minister, some attempt was made to control inflation but not at the expense of development. Inflation increased to an annual rate of 83 percent in 1980 and was rising even faster as of early 1981. Per capita GDP rose 3.6 percent in 1979 and 4.8 percent in 1980 as compared with a 1.9 percent and 3.3 percent increase in 1977 and 1978, respectively.

While these rates of growth are high by almost any standard, especially in the context of high energy prices and a less than booming world economy, they are considerably lower than those of the Costa

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[58] Facts on File, Inc., *Latin America 1977*, New York, 1978, p. 77.

[59] Robert M. Levene, "Brazil: The Aftermath of Decompression," *Current History*, February 1976, p. 53.

e Silva and Medici years. Rates of growth of GDP tell nothing, however, about how the fruits of growth are shared among the various sectors of the population and about the social and political tensions that arise when large sectors believe they are being discriminated against by the governing regime. According to Levene, President Figueiredo in his first six months in office, faced more strikes than had taken place during the last six turbulent months of the Goulart regime.[60] More than a million workers were involved in these strikes which were staged to protest the more than 29 percent drop in real wages that occurred in 1979.[61]

URUGUAY

In the area of human rights violations, the Uruguayan military regime is considered by Amnesty International as one of the worst offenders.[62] Violations on a massive scale occurred in the army's campaign against the Tupamaro terrorists in 1971–73, but a second wave of repression took place between 1975 and 1979. The prime targets in the 1975–77 period were Communists and far-left activists, many of whom, according to the State Department, were apparently arrested for political activities which were legal when carried out.[63] Other arrests were of members of labor, media, university and professional groups who had "little or no apparent connections with politics."[64] Torture and other forms of mistreatment were routine, according to Amnesty International, but after 1977 arrests and reports of torture have decreased.[65] The organization estimated that at least 1,500 "prisoners of conscience" and other political prisoners in a population of 2.5 million had "disappeared and not yet been accounted for."[66]

According to Uruguayan government statistics as of 1979, about 6,000 prisoners had been turned over to the military justice system, about 1,300 were subsequently released and some 3,000 others were freed by judicial order (many conditionally). As of December 1, 1980, an estimated 1,219 prisoners were still under the jurisdiction of the military justice system, either awaiting completion of trials or serving sentences. Another 200 or so were new prisoners arrested during the year.[67]

According to Robert Kaufman, it took the military some time after taking over power to agree on an economic strategy. Part of the reason was the scarcity of conservative technicians capable of devising plausible economic strategies. Uruguay's universities were dominated by the law, liberal arts, engineering and medical faculties; most of the country's firms were too small to have developed the right persons. Part of the reason also for the slowness to develop a strategy was a deadlock between what Kaufman calls hard-line nationalists and the more internationally-oriented generals. The latter eventually won out with the appointment of Alejandro Vegh Villegas as economy minister in September 1974.[68]

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[60] Ibid., p. 50.
[61] Ibid.
[62] Amnesty International, Inc., *Amnesty International Report 1977*, p. 158.
[63] Department of State, "Uruguay" in Country Reports on Human Rights Practices for 1980, Washington, 1981, p. 544.
[64] Ibid.
[65] Amnesty International Report, 1980, London, 1981, p. 166.
[66] Ibid., p. 167.
[67] Department of State, op. cit., p. 546.
[68] Kaufman, op. cit., p. 183.

Vegh Villegas's policy was similar in substance to those followed by the Chilean and Brazilian military regime but included, unlike the Chilean stabilization program, a price freeze as well as a wage freeze. Foreign investment was encouraged by giving investors Central Bank guarantees that they could repatriate their earnings at any time. Import restrictions were liberalized. Incentive measures were also taken to increase exports of manufactures and of traditional agricultural exports.[69]

Vegh Villegas was unable, however, to sell off inefficient state enterprises to private interests because of the opposition of the employees who had ample backing among the military. He also ran into opposition within the general staff which criticized the "undue" influence the International Monetary Fund was llegedly exercising on economic policy. Against the latter charge Vegh Villegas was upheld, however, and his policies remained intact.

Economic Performance

Table 2 summarizes the per capita GDP and consumer price behavior under both civilian regimes and the military regimes.

The table indicates that Argentina under the military regimes of 1966–73, and Brazil and Uruguay, under their respective military regimes, achieved substantially higher rates of gowth of GDP than their respective predecessor civilian regimes. Chile did somewhat better under the military regimes than under the previous civilian regimes. The Peruvian military regime did less well than under the predecessor regimes, and the Argentine military regimes of 1976–80 did only somewhat better than the immediate predecessor regimes of 1973–76. Similar mixed results are shown in the behavior of consumer prices. Three countries experienced about the same average annual inflation rates under military as under civilian administration--Argentina (1966–73), Brazil, and Chile. Peru, Uruguay, and Argentina (1976–80), suffered substantially greater rates of inflation under military regimes than under civilian regimes.[70a]

The averages of the tables are somewhat misleading, however, in that they do not show the trends of recent years, say, from 1975–80. These are shown in Table 3.

TABLE 2.—SOUTH AMERICA: AVERAGE ANNUAL RATES OF GROWTH OF REAL PER CAPITA GDP AND OF CONSUMER PRICES, 1950–80

[In percent]

Country	Coup year	Precoup period, 1950 to coup: GDP	Precoup period, 1950 to coup: Prices	Military regime period: GDP	Military regime period: Prices
Argentina	1966	1.3	25	3.8	27
Brazil	1964	3.6	32	5.9	29
Chile	1973	2.1	26	2.9	29
Peru	1968	2.8	8	1.0	21
Uruguay	1973	−.3	28	3.5	61
Argentina	1976	2.2	29	2.8	125

Source: Economic Commission for Latin American (ECLA), "Series Historicas del Crecimiento de America Latina, Cuadernos Estadisticos de la CEPAL (ECLA)" Santiago, Chile, 1978: GDP, 1976–80, calculated on basis of population growth rates as given in Inter-American Development Bank, "Economic and Social Progress in Latin America," 1979, and 1976–80 GDP as given in CEPAL, "La Economia de America Latina en 1980", Notas Sobre la economia y el desarrollo de america latina", No. 33, January 1981. (1980 GDP estimates are preliminary.)"

[69] Ibid.

[70a] Guyana, Suriname and French Guiana are excluded because of their small populations, affinity with the Caribbean group of nations (Guyana is a member of the Caribbean Commonwealth of Nations), and recent colonial status.

TABLE 3.—SELECTED SOUTH AMERICAN MILITARY REGIMES: RECENT TRENDS IN REAL PER CAPITA GROSS DOMESTIC PRODUCT AND CONSUMER PRICES

[Year by year percentage change over previous year]

Year	Argentina		Brazil		Chile		Peru		Uruguay	
	GDP	Prices	GDP	Prices	GDP	Prices	GDP	Prices	GDP	Prices
1974	(1)	(1)	6.7	28	2.3	505	3.7	17	0.6	77
1975	(1)	(1)	2.8	29	−14.5	374	0	24	2.5	82
1976	−4.2	443	6.1	42	1.6	212	0	34	1.8	51
1977	11.0	176	1.9	44	6.9	92	−4.1	37	2.5	50
1978	−4.7	175	3.3	39	6.2	40	−4.8	58	3.1	49
1979	7.2	160	3.6	53	6.8	33	1.0	67	7.5	81
1980	0	101	4.8	83	3.8	35	.6	59	4.2	42

[1] Indicates civilian regime in power.

Source: ECLA and IMF, op. cit.

GDP and price performance are only two indicators of economic performance, and they are by no means complete reflections of the efficiency of economic policy either under military or civilian regimes. External factors such as weather, other natural disasters, the state of world markets for South America's exports, the supply of international finance, and high oil prices may outweigh the role of domestic policy. In the period under review, oil prices increases have undoubtedly increased world inflation and made it more difficult for oil importing countries to control domestic inflation.

On the other hand, the military governments have had at their disposal far greater coercive powers than the civilian governments they replaced. In addition, the supply of funds from abroad has been greater in the period of the military regimes than it was under the civilian governments of South America. Moreover, world markets, except in 1975, may have been much more favorable to South America's exports than at any time since World War II and the Korean War.

Year by year changes shown in Table 3, convey a somewhat different impression from that imparted by Table 2. In Chile, for example, after the disastrous year of 1975, a year when the bottom fell out of the world market for copper, Chile's main export, the growth rate bounced back strongly in 1977 and remained at a high level though 1979, falling sharply only in 1980. Argentina's GDP performance in 1976–80 was extremely erratic, perhaps even more so than under any other previous regime. Brazil shows steady improvement after a bad year in 1977. Uruguay showed a strongly improving trend in GDP until 1980. Peru's stagnation as indicated by Table 2 is confirmed by Table 3.

With respect to inflation, the table brings out a more or less steady reduction of inflation in Chile since 1974. In contrast, the inflation rate has been increasing steadily in Brazil since 1977, decreasing slowly in Argentina, running high in Peru, and moving erratically in Uruguay.

The full costs of the economic growth achieved under the military regimes are not yet known. In all four countries, large sectors of the population have not shared proportionately in the economic growth; and income inequality has probably been accentuated because of the control over wages at levels below the pace of inflation.

Given the spotty performance of all but Chile with respect to inflation and the erratic growth performance of Argentina and Uruguay, it is by no means clear that the new-style military regimes have proven to be superior to their predecessor civilian regimes in bringing about satisfactory economic development—high growth without inflation.

V. The Future of the Military Regimes

The democratic ideal, despite the long, arduous, fitful and generally unsuccessful struggle to realize it in practice, remains one of the permanent goals of Latin American society. It is the key to legitimacy, so much so that even the current group of military rulers, do not renounce the restoration of democracy as the ultimate goal of their own regimes. While Latin American concepts of democracy may vary from group to group and may not altogether square with North American or Western European definitions, the idea that power comes from the people and that the people's wishes should be conveyed through representatives of their own choosing is deeply held by large sectors of the literate population of Latin America. It is significant that the Uruguayan generals deposed their eager and willing instrument, President Boraberry, when he insisted on the corporate form of organization as a permanent political solution to Uruguay's problems. Even in Chile, which has taken on many of the earmarks of a corporate state, its ruler, General Pinochet, professes to reject corporatism both as an interim form of government and as a long-run objective.[70b]

In Brazil, Chile, Argentina, and Peru many military officers were constitutionalists. Most of them subscribed to the idea of the armed forces being the guardian of the nation and the moderator in time of crises that endangered the intergrity of the fatherland. Many of them were not at all convinced that even the various crises of the 1960's and 1970's were serious enough to justfy the overthrow of constitutionally elected presidents and the banning of competitive politics. Some of these military men, including the Commander-in-Chief of the Chilean army, General Schneider and his successor General Prats, paid for their beliefs with their lives. Others were purged from the services or denied promotions.

The constitutionalists remain a potent force in the military of Brazil and of the Southern cone countries. Otherwise it would be difficult to explain the continuing pressures for liberalization in Brazil and Argentina or the emergence from time to time of high ranking military commanders in Chile who challenge—unsuccessfully so far—General Pinochet's dictatorial rule.

The fact is that while the top command of the armed forces may be insulated from the public at large, the lower ranking officers are not. They come largely from the middle classes, and they are sensitive to the currents of opinion in these circles. True, the traditional moulders of public opinion such as the media, the political parties, the trade unions, the Church and the arts are greatly handicapped by the restrictions placed upon them by the military. However, the restrictions have

[70b] Thomas G. Sanders, "Chile: The New Institutionality and the Consultation," American Universities Field Staff Reports, No. 5, 1978, p. 2.

not been total, and in all the countries they have been relaxed to some extent. Public opinion still exists. It is shaped not only by the messages received from the traditional sources but also by personal experiences and by underground news, rumors and gallows humor and by the seemingly innocuous media articles whose writers are gifted in conveying between-the-line messages critical of the regimes.

For all the powers of coercion which they dispose, the military regimes remain sensitive to changes in public support. This support they had in ample measure when they ousted the civilian regimes. In Argentina and Uruguay, terrorism and inflation were widely perceived as requiring drastic measures. In Peru, the paralysis of government seemed irremediable except by authoritarian means. In Chile, the violence of the clashes between Allende's supporters and his enemies had created an increasingly chaotic situation. In Brazil, the political stalemate, the leftist and neutralist tendencies of the Goulart government, and the bitter opposition to these tendencies threatened to lead to prolonged violence and disorder.

In each of these situations, the armed forces did not move to overthrow elected governments until they were sure that they would enjoy broad public support for their actions. Even in their most repressive periods, it is probable that the armed forces still enjoyed some measure of support outside the traditional right-wing, since the full extent and severity of the abuses was not known. Government control of television, radio and intimidation of the print media combined to keep the general public in ignorance of what was really going on and to mislead it into believing that almost all the victims in Argentina and Uruguay were terrorists or terrorist sympathizers and in Chile and Brazil agents of violent revolution. That innocent people were also victims was excused on the grounds that the government was waging a civil war against the common enemy of subversion and that war inevitably takes a heavy toll of innocent people.

It is also probably true that while the number of victims must be reckoned in the tens of thousands, a large number and perhaps most of them were from the extreme left or had some ties with them, and many were undoubtedly guilty of atrocities of their own. On the other hand, although many politicians, trade union leaders and other political activists suffered harrassment or deprivation of political rights, by and large except for those of the extreme left, they were not persecuted. If they had been, the scale of the jailings and killings would have had to be much larger—perhaps in the hundreds of thousands.

In Brazil where the media and the opposition had greater freedom to speak out, public opinion did shift against the Brazilian military, forcing it to move in the direction of greater liberalization. Public opinion now seems to be moving against the Argentine and Uruguayan regimes as well. It may be shifting also against the Chilean regime. In Brazil, the signs of the popular pressure are evident in the criticisms appearing in the media. In Argentina, Uruguay, and Chile, the signals are more subtle—sly writing, absence of crowds at state-sponsored ceremonies, the rejection of a government sponsored referendum.

How will the military react to this loss of public support?

In Brazil, it has reacted by proceeding with liberalization despite the resistance of hard-liners. In Argentina, the situation is uncertain, with some high-ranking navy officers going public in their criticisms of the slowness of the liberalization process. In Chile, it is difficult to ascertain what the state of public opinion is. It may be that the public is still too intimidated to make its views felt. On the other hand, it could be that ample public support still exists for the Pinochet regime, less perhaps for what it stands for than out of fear of what might follow it. In Uruguay, the public has declared itself in favor of a return to constitutionalism by rejecting in a popular referendum last November a new charter which would have formalized the military's power over the government. After months of indecision, the regime now appears to be moving toward the restoration of civilian government.

Assuming, though, that the military does relinquish direct governing power within the next several years, is its withdrawal likely to be final? There is no way of knowing how the political parties will behave under a restored constitutional regime. The harsh experience under the military regimes may have made the political parties more amenable to compromise and accommodation and more willing to seek a consensus on important issues. On the other hand, they may go back to their old ways and once again enmesh themselves in a situation of prolonged immobilism, thus inviting political turmoil and precipitating another wave of military takeovers.

We cannot predict the eventual outcome. It may be helpful, however, to see what kind of regimes have replaced authoritarian regimes in the past.

Possible Successor Regimes: Some Precedents

South America has been perhaps the richest region in the world in terms of the wide variety of forms of political organizations that have arisen there. True, the European Communist model may be imperfectly drawn in Cuba; Peron's Argentina of 1946–55 was only a pale approximation of Italian fascism; and no South American state has come close to approximating the totalitarianism of Nazi Germany. Still the many varieties of constitutional governments, the many kinds of military governments and of civilian authoritarian governments have made South America a showcase of political experimentation with its several cycles of repression and liberalization since the various countries won their independence from Spain and Portugal in the 19th century. While a return to democratic government seems the most likely outcome in the short-run, say, the next four or five years, the failure of the political parties to develop a working consensus among themselves on the changes needed to bring about effective government could lead in the longer run to a number of different political systems: (1) other authoritarian regimes similar in nature to the rightist regimes of the present; (2) Cuban-style Communism; (3) fascism; and (4) civil-military populism. In the section that follows, three cases of transition from an authoritarian regime to constitutional government are presented, those of Colombia, Venezuela, and the Dominican Republic as well examples of the other four kinds of political organization.

DEMOCRACY

A number of relatively peaceful transitions from authoritarian military regimes to civilian government have taken place in recent

South American history. In Colombia, the overthrow of the oppressive Rojas Pinilla dictatorship in May 1957 led first to an interim military junta and then in August 1958 to the election of Alberto Lleras Camargo, the first of four presidents to serve under a unique arrangement by which the Liberal and Conservative parties agreed to share power alternately. This arrangement worked effectively until recent years when internal dissension in the two parties and the rise of terrorist activity posed the threat of renewed instability.

In Venezuela, after the overthrow of the Perez Jimenez dictatorship in 1958, terrorist groups supported by Cuba posed a challenge to the democratic regime in the 1960's. A second challenge facing Venezuelan democracy was the possibility that Perez Jimenez would return to power as a result of an election victory. Both challenges were met without massive reprisals or terrorist countermeasures.

A more difficult transition from military to civilian rule occurred in the Dominican Republic. In 1961, General Rafael Trujillo, who had ruled the country for 30 years was assassinated. Trujillo's death brought about a period of turmoil. The long-exiled left-of-center Juan Bosch was elected president in December 1962, overthrown by the military in September 1963, restored to office in a counter counter coup by the pro-Bosch forces in April 1965, and set aside as a result of the intervention of the United States in that year. In new elections held on June 1, 1966, Dr. Joaquin Balaguer, a former president and associate of Trujillo, won, in part because of the poor campaign waged by Bosch.[71]

In Fitzgibbon's words, Balaguer "gained strength by relative success in purging his image of earlier association with Trujillo while retaining, in the minds of the lower classes, some credit for distribution of largesse under Trujillo's auspices." [72] Balaguer was reelected in 1970 and 1974. In the latter election, however, he was unopposed because all his opponents had withdrawn in protest over the expectation that the elections would be rigged against them. They dropped their demands that Balaguer's election be annulled only after he pledged he would not run for office again. Balaguer broke his pledge, and ran for another term in the 1978 election. He was decisively defeated by Antonio Guzman. Guzman, whose term expires in 1982 has recently announced his decision not to run for office again. He would be the first president in his country's 137-year history to surrender power voluntarily, a move hailed by the *Washington Post* as strengthening "a still unsteady democratic tradition." [73]

MORE AUTHORITARIANISM

In the 1920's and 1930's, it was common for one authoritarian rightist regime in South American government to be followed by another rightist regime. Since World War II, and until the present epoch of the new authoritarianism, a rightist authoritarian regime has usually not been succeeded by another of the same cast, except for Paraguay, Ecuador, and Bolivia. In the present era, Brazil offers the case of five different rightist military regimes in succession, each, however, with its

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[71] Russell H. Fitzgibbon, "Latin America: A Panorama of Contemporary Politics," Appleton-Century-Crofts, New York, 1971, p. 172.
[72] Ibid., p. 172.
[73] The *Washington Post*, July 8, 1981.

own style. These changes of leadership were the result of a consensus within the armed forces which, while not easily arrived at, set certain limits to the range of maneuver, thereby avoiding armed confrontation between opposing factions.

In today's circumstances, it is conceivable that harder-line factions may take over the leadership of the armed forces and re-institute a repressive administration or bring about an authoritarian civilian regime controlled by these factions. The climate does not seem propitious for this kind of shift, however, given both the crystallization of public opinion which now seems better informed of the scale and severity of past abuses and the liberalization trend in all the regimes reflecting the decline in influence of the harder line factions.

CUBAN-STYLE COMMUNISM

Another type of transition from a rightist military regime is provided by pre-1959 Cuba. Here a small group of people, in Theodore Draper's phrase, "young, city-bred ex-students, which at its peak may have numbered 1,000 persons, overthrew the Batista dictatorship which had an army of over 40,000." [74] How could such a small group have defeated Batista? The answer Draper gives is that Castro's guerrillas did not defeat Batista's army in any military sense. "The engagement between the two sides," he writes, "were so few and inconclusive that Batista's abdication caught Castro by surprise." [75]

As Draper tells the story, in the spring of 1958, Castro had called a mass uprising against Batista. When this failed to materialize, he decided on full-scale guerrilla warfare. The purpose was, through bombings, sabotage and hit-and-run raids, "to provoke Batista to employ counter-terror." This Batista did. "The army and secret police struck back blindly," Draper writes, "indiscriminately, senselessly. The students blamed as the chief troublemakers were their chief victims. It became safer for young men to take to the hills than to walk in the streets. The orgy of murders, tortures and brutalities sent tremors of fear and horror through the entire Cuban people and especially the middle class parents of the middle class students." [76] The impact on Batista's own army was disastrous. Draper writes: "This universal revulsion in the last six months of Batista's rule penetrated and permeated his own army and made it incapable of carrying out the offensive it launched in May against Castro's hideout. Batista's army just evaporated." [77]

Draper's concluding observation on the self-destruction of Batista's army is worth quoting:

> Castro's guerrilla tactics, then, aimed not so much at defeating the enemy as at inducing him to lose his head, fight terror with counterterror on the largest possible scale and make life intolerable for the ordinary citizen. The same terror that Castro used against Batista, has been used against Castro. And Castro has responded with counterterror just as Batista did.[78]

[74] Theodore Draper, "Castro's Revolution: Myths and Realities," Frederick A. Praeger, Inc., New York, 1962, pp. 13–14.
[75] Ibid.
[76] Ibid.
[77] Ibid.
[78] Ibid., p. 15.

One might add from the perspective of 19 years since Draper's book was published, ". . . however, more effectively." Castro has virtually eliminated his critics by exile, imprisonment or execution. At the same time he has carried out certain reforms which seem to have retained for him the support of a significant part of the most military sectors of the population. Dillusionment and discontent seem, nevertheless, to be spreading even in these groups.

FASCISM

Another possible successor to the present South American military regimes is fascism—a hierarchical political system headed by a dictator who maintains control by means of a mass party and its militias as well as by domination of the armed forces and who carries out policies favoring the middle classes against both the upper classes and the working class. Although in the late 1930's there were other movements more avowedly fascist such as the "integralista movement" in Brazil, the *Alianza de la Juventud Nacionalista* in Argentina and the *Movimiento Nacional Socialista de Chile*, Argentine peronism and Brazilian "getulism" were the mass parties which most closely resemble the fascist movements of Italy and Germany. They both, it is true, fell far short of their European models, particularly in that they catered more to the working class than the middle classes. But as Paul Lewis points out, Peron had already incorporated or initiated all the essential features of European fascism before his deposition in 1955.[79] Given more time, Lewis believes, Peron's Argentina could well have become a full-fledged fascist state. Peron was in power, after all. Lewis points out, for only 12 years as compared with Mussolini's 22 years. Moreover, he was becoming more conservative and more oriented toward the middle classes.

Many writers take issue with the idea that peronism or any other movement in Latin America closely resembled fascism. Alistair Hennessy, for example, disagrees that the mass movements of Peron, Vargas and others were fascist movements. "Fascism," he writes, "like other political movements inspired by the European example—liberalism, conservatism, socialism and communism—failed to take root and was modified, under Latin American conditions, until the connections appeared tenuous and the similarities superficial." [80] Hennessey cites a number of reasons for the absence of the "conditioning factors which gave fascist movements in Europe their distinctive style." Three of these seem particularly important.

(1) The absence in Latin America of the experience of total war meant the absence of what had been in Europe the main impetus to mass political mobilization. It also meant that the Latin American military focussed their energies on internal policies and would not brook the rise of political paramilitary formations—"alternative sources of firepower."

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[79] Paul H. Lewis, "Was Peron a Fascist? An Inquiry Into the Nature of Fascism," *Journal of Politics*, February 1980, p. 256.

[80] Alistair Hennessy, "Fascism and Populism in Latin America," in *Fascism: A Reader's Guide*, edited by Walter Laqueur, University of California Press, Berkeley and Los Angeles, 1976, p. 256.

(2) The Church refused to lend support to fascist groups which in Europe—even in Spain—were "anti-clerical."

(3) Latin America lacked a strongly organized left, the catalyst which mobilized the counter mass-movement of fascism.[81]

Whatever validity these arguments of Hennessy have had for the past, in the 1980's, the fascist outcome cannot be dismissed out of hand. While South Americans still lack the experience of total war, they have been undergoing a traumatic experience not unlike war in that the terrorist and counter-terrorist operations have cost thousands of casualties and untold suffering. On the other hand, the South American armed forces remain determined not to permit the creation of paramilitary bodies such as Mussolini's "black shirts" or Hitler's stormtroopers. One of the strong influences in the Brazilian events of the early 1960's was the fear in the armed forces that if they delayed the coup for very long, they might find themselves facing the armed resistance of disciplined workers' militias. Another feature common to the various South American military regimes is the fear that a charismatic military figure might emerge from their ranks, as Peron did, to develop a mass political base of support outside the armed forces. It is for this reason that the armed forces, except in Chile, have set fixed terms for their presidents, barred presidential succession and chosen leaders who seem to lack charismatic qualities.

In Chile, General Pinochet appears to have become the dominating figure of the armed forces. He has repeatedly ousted high ranking military officers who have disagreed with him, including the Air Force Commander who was a member of the original 3-man military junta. In power since 1973, he shows no inclination to relinquish it any time soon.

CIVIL-MILITARY POPULISM

It is possible that the high human toll of the military repression of the last few years in South America has radicalized politics in the region as never before. In this case, the threat of a Cuban-style outcome will be reinforced. On the other hand, the left has been drained of many of its most militant figures by execution, imprisonment or exile. Whether these losses doom it to impotence in the future or whether new and more revolutionary cadres will arise to take their place remains to be seen.

It seems more probable, however, that, crippled as it is, the leftist impulse may take another direction, that of civil-military populism instead of Cuban-style communism.

This may be so because the current military regimes of Argentina, Brazil, Chile, and Uruguay have not fully lived up to the rationale for their assuming power. This rationale has been well-put by Luigi Einaudi and Alfred Stephan:

> The military institution came to see existing social and economic structures as security threats because the structures were either so inefficient or so unjust that they created the condition for, and gave legitimacy to, revolutionary protest. In both countries [Peru and Brazil] the officer corps believed that these conditions were ultimately a threat to the military institution itself.[82]

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[81] Ibid., p. 257.

[82] Einaudi, Luigi R., and Alfred C. Stepan. "Changing Military Perspectives in Peru and Brazil," in *Beyond Cuba: Latin America Takes Charge of its Future,* edited by Luigi R. Einaudi, Crane, Russak and Co., New York, 1974. pp. 98–99.

Their observation seems to express well the dominant view of the armed forces, not only in Peru and Brazil, but in Chile, Uruguay, and Argentina as well. The Peruvian military did attempt to deal with the social agenda implicit in the national security doctrine referred to by Einaudi and Stepan. Some of their reforms were undoubtedly ineptly carried out or ill-advised and are likely to be overturned. Others, such as land reform and measures to meet the needs of Peru's long-neglected Indian population, are probably irreversible and may have mitigated significantly the sharpness of internal conflict.

In the other South American countries, the military regimes have made little or no attempt to alter the conditions that gave rise to social protest. From all accounts, inequality of income distribution has increased, and the living levels of the working and lower middle classes have either eroded or failed to keep pace with productivity gains.

As a result, a populist countercurrent within the military may have been set in motion. There are ample precedents. The Peruvian regime, under General Velasco Alvarado's leadership in the period 1968–75, is only the most recent example of military populism. Another recent example is the rise to power in 1970 of General Juan Torres in Bolivia after a six-year spell of right-wing military governments. Torres was allied with students, miners, urban workers, and leftist political parties. He was overthrown by a right-wing military faction, after only 10 months in office.

But the emergence of Torres as a leftwing military leader is not an isolated case in Bolivia. In 1936, Colonel David Toro attempted to carry out a socialist program but was replaced a year later by Colonel German Busch. Busch attempted to carry out a similar program. He was killed in 1937. From 1943 to 1946 a leftist government headed by army major Gualberto Villarroel and his ally, the Nationalist Revolutionary Movement (MNR), attempted a generally leftist policy, encouraged the unionization of nation's mines and undertook to improve the lot of the huge Indian population. Villarroel's government was overthrown in 1946, but the MNR continued an underground struggle which culminated in a successful insurrection in 1952. The MNR dominated Bolivian politics until November, 1964 when it was overthrown by a military coup.

Peron is the most conspicuous, and in terms of lasting influence, the most successful of the Latin American populist dictators, with the possible exception of Getulio Vargas of Brazil. Peron dominated Argentine politics from 1943 until his death in office as president in 1974, even though he spent the years 1955 to 1973 in exile in Spain. An army colonel in 1943, he was a leading member of a pro-German officers' group which deposed a right-wing, neutralist civilian government in that year. Using his post as labor minister to build a constituency among the heretofore politically neglected working class, Peron was so successful in this enterprise that he handily won the presidency in 1946. In the early 1950's, he became more solicitous of the middle classes, and a degree of disillusionment set in among his working class constituency. Forced out of power by the military commanders in 1955, Peron in exile managed to restore his appeal to his old constituency and reasserted control over the bulk of organized labor, thus enabling his political party to maintain the largest following in the country.

He was permitted to return to Argentina in 1973, was elected president in September of that year and died after less than nine months in office. Although his short second presidency and the presidency of his wife who succeeded him were marred by bitter factionalism within his movement, it is too soon to write peronism off as a spent force.

There were other attempts to establish military populist dictatorships before those in Bolivia and Argentina. In Brazil in 1922, a group of junior officers at the Copacabana fortress in Rio de Janiero revolted against their superiors in a quixotic and unsuccessful attempt to overthrow the traditional order. Two years later in Sao Paulo, junior officers (*tenentes*, literally lieutenants) deposed their commanders and proclaimed a vague reform program which included the establishment of minimum wages, regulations of work for women and children, state ownership of natural resources, and the break-up of the large estates. The rebellion was crushed within a few weeks, but many of the survivors were to reappear again in the 1930's and 1940's either as advocates of revolution; as in the case of Luis Carlos Prestes who became leader of the Brazilian Communist party. "*Tenentismo*," Johnson writes, "was made to symbolize both protest and self-sacrifice in the public mind." [83] Edward Lieuwen describes a number of other instances of social reformist efforts undertaken by the Latin American armed forces in addition to those already mentioned: Chile in 1925, Cuba in 1931, Paraguay and Bolivia in 1936; Ecuador, 1944; Venezuela, 1945; El Salvador, 1948; Costa Rica, 1948; Panama, 1952; Colombia, 1953; and Guatemala, 1950.[84]

There were other military coups, of course, in the old style. Their leaders either sought personal power and profit or were bent on crushing challenges to the oligarchies with which they were allied or on supporting one group of oligarchs against another. These were far more successful in holding on to power than the military populists. They were, however, operating in countries far less politically and economically developed than those of today.

Nationalism

A strong influence in these leftist military movements was nationalism, a response natural enough in countries which felt themselves at the mercy of the industrialized countries and saw their ruling elites as agents and allies of foreign capital. From the late 19th century until World War I, South American nationalism was directed against European, primarily British, capital. In the 1920's, the United States became for many Latin Americans—and not just those of the left—the embodiment of "economic imperialism." Only by reducing Latin America's dependence on the United States and on Western Europe and by restricting foreign investment, the theorists of the nationalist school held, could Latin America free itself of economic bondage and develop its full potential. One of the reasons for the ready embrace by Latin America of the import substitution strategy (ISI) in the 1940's and 1950's was the strong pull of the nationalist idea.

[83] John T. Johnson, "The Military and Society in Latin America," Stanford University Press, 1964, pp. 202–203.
[84] Edwin Lieuwen, *Arms and Politics in Latin America*, Council on Foreign Relations, Frederick A. Praeger, Inc., New York, 1960, p. 60.

Guillermo O'Donnell sees the strength of these nationalistic views as creating great strains within the ranks of the military. On one side are the chief technocrats of the military regimes and the upper business, elites, which, he writes, have a strong "transnational" view. They believe in an integrated world market in which trade and capital move freely across national boundaries. They are the most dynamic capitalists of their societies. "Unabashedly motivated by profit, they are the driving force behind the accumulation of investment capital which is given added sanction by an ideology that asserts that the maximization of profit will in the long run improve the general welfare." [85] O'Donnell sees an inherent conflict between this view and the dominant ideology of the South American military:

> But a great problem with BA (the Bureaucratic-Authoritarian state) is that the other central actor in its institutional system—the armed forces—tends to be the most nationalistic and least capitalistic of the state institutions. With their sense of mission, the martial values with which they socialize their members, and their doctrines of national security which presuppose the existence of a nation characterized by a high degree of homogeneity in the orientations and actions of all civilians, the armed forces are the state institutions most predisposed to define appropriate behavior as that which is inspired by an introverted and exclusivist vision of the nation. In addition, the profit motive appears to them to be of secondary importance, at most, and sordid in comparison with the larger concerns and ideals that derive from their own orientations. Profit may be necessary, but in any case it should not become "excessive" or work against the mission of homogenizing the totality of the nation.[86]

O'Donnell's phrase, the "introverted and exclusivist vision of the nation" has to be seen in relation to the opposite view held by the technocratic and business elites which have received the support of the top commanders of the South American armed forces. This view is that the populist sectors must be politically excluded from the decision-making process because these sectors interfere with the internationalization of the national economies. "Political exclusion," O'Donnell writes, "is achieved by liquidating the institutions of political democracy and in effect denying citizenship to the populist sectors." [87] He writes:

> The "bureaucratic-authoritarian" state, as embodied in the South American military regimes, increases inequality. It promotes a pattern of capital accumulation which is highly skewed toward benefitting the large oligopolistic units of private capital and some state institutions. The pre-existing inequities in the distribution of societal resources are thus sharply increased. Moreover, the "bureaucratic-authoritarian' state promotes an increasing "transnationalization" of the productive structure, resulting in a further denationalization of society. . . .[88]

This behavior of the bureaucratic-authoritarian regimes runs fundamentally counter, O'Donnell asserts, to the inherent military view, now effectively suppressed by the top commanders, that all sectors of the nation must have access to the state.

VI. Implications for U.S. Policy

The nature and history of authoritarian military regimes in the more modernized countries of South America give rise to a number

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[85] Guillermo O'Donnell, "Tensions in the Bureaucratic-Authoritarian State and the Question of Democracy," in *The New Authoritarianism in Latin America*, edited by David Collier. Princeton University Press, Princeton, 1979, pp. 300–301.
[86] Ibid., p. 301.
[87] Ibid., p. 292.
[88] Ibid., p. 293.

of observations that seem relevant to the formulation of U.S. policy towards the region.

(1) The dynamics of Latin American politics are so complicated and factionalism so pronounced that it is dangerous to build a foreign policy on the premise that anti-Communist authoritarian military regimes will remain in power indefinitely.

(2) Military regimes in the more modernized societies are not likely to endure indefinitely for two basic reasons: (*a*) relying primarily on technocrats for advice, they become increasingly isolated from the population at large, and less and less sensitive to the needs of the main interest groups, such a labor, small farmers, and the middle classes; (*b*) internal disunity within the armed forces is likely to grow the longer the military have direct responsibility for government. These internal tensions are particularly likely to worsen when the policies followed by the top commanders are at variance with the ideas of a large part of the officer corps. This seems to be the case with the present regimes. The internationalist orientation of these regimes appears to some sectors of the military to be making the national economies excessively dependent on the United States and other industrialized countries to the detriment of national needs and national business.

(3) Despite the failure of representative government to prosper in most of South America, there remains a strong commitment to democracy among a large part of the politically articulate citizenry and a strong constitutionalist orientation within the armed forces. While these sectors were unwilling or unable to prevent the overthrow of constitutional governments in the 1960's and 1970's, this should be interpreted in the light of the prolonged failure of the civilian political parties to come to some consensus on the pace and scope of reform. It was this lack of consensus that led to ineffectual government and to a widespread feeling everywhere in South America that things had gotten out of control. This is why the military were determined to carry out a revolution of their own in the case of Peru and a counter-revolution in Brazil, Argentina, Chile, and Uruguay against the populism that had dominated politics in these countries for generations. The mixed economic performance of the military regimes and the harsh experience with repressive tactics employed everywhere, except in Peru now, raise the possibility that the moderate sectors of the left, right and center may be able to overcome their historic differences and reinvigorate the constitutionalist sentiment in the military.

(4) It is uncertain, of course, that the moderate sectors will prevail over the radicalization process caused by repressive military rule. It is also uncertain that even if they succeed in doing so, they will be able to forge an operating consensus that will make effective democratic government possible. The failure to achieve such a consensus would most likely further radicalize politics and facilitate the advent of more extreme political systems.

(5) In South America, the radicalization process could lead to a right-wing totalitarian regime—fascism; a left-wing non-communist or anti-communist civil-military populist state; a combination of particular features of both systems; or a Cuban-style regime. A combination of fascism and populism seems to have been the direction in which Peron of Argentina and Vargas of Brazil were headed before they were

deposed by their respective armed forces. Although the two leaders started from different positions—Peron from the left and Vargas from the right—each moved some distance toward the other end of the spectrum to increase his popular support. Neither was able to acquire the monopoly of power over all the major institutions—the armed forces, the Church, the trade unions, the business community, the cultural community of the universities and the arts—but it was not for lack of trying. Peron came closest to achieving this objective. Perhaps if he had had the personal courage to mobilize his considerable support within the military, he could have crushed the rebels against him and succeeded in establishing a totalitarian state.

(6) While the last possibility mentioned—the emergence of a Cuban-style regime—seems likely in the shorter-run, a renewal of intense repression could strengthen the revolutionary left over the longer-term. The possibility of a Communist take-over in one or more of the South American countries cannot, therefore, be dismissed out of hand.

(7) There is no guarantee that an anti-Communist authorization or totalitarian regime will adopt a policy that supports U.S. positions toward the Soviet Union and its allies. Argentina under military rule took advantage of the U.S. grain boycott not only to sell large quantities of grains to the Soviet Union but to enter into large long-term contracts with it. Peru, under the Velasco regime, adopted a neutralist position and obtained $650 million in Soviet credits for the purchase of tanks, heavy artillery and the first surface-to-air missiles in South America. In Brazil, the military regime has moved from avowed pro-U.S. positions to a more independent posture. Bolivia under the Torres regime adopted an anti-U.S. foreign policy and accepted military and economic aid from the Soviet Union. Peron at the zenith of his power in the late 1940's and early 1950's adopted a virulent anti-U.S. stance.

(8) While the United States cannot afford to underestimate the strength of the will to democracy and constitutionalism in South America, on a wide variety of issues that affect the lives and interests of our citizens and the future of world peace, the United States must deal with the authoritarian regimes of South America as they are, and not as it would like them to be. It cannot, therefore, maintain an adversary relationship with these regimes and still effectively protect and promote the immediate and ultimate interests of its citizens. At the same time, it cannot afford to alienate or demoralize the pro-democratic constituency in these countries. Finding the way to meet both imperatives may be the major challenge facing the United States in South America in the 1980's.

CUBAN EXODUS—1980: THE CONTEXT

By Barry Sklar *

Summary

The decision of Fidel Castro to promote the exodus of thousands from Cuba was a spontaneous act in reaction to events surrounding a dispute over political asylum at the Embassy of Peru. However, for some time the Cuban Government had been interested in permitting emigration to the United States.

The decision was designed to relieve substantial pressures on Cuba that had been building because of economic and political problems. The Cuban economy has been in a period of a sharp decline. The per-capita growth rate fell from 8.2 percent in 1978 to 3.1 percent in 1979. The loss of about 25 percent of the sugar crop because of blight, the loss of almost the entire tobacco crop because of blue mold, the recurrence of swine fever which further reduced the amount of meat for domestic consumption, and a drop in the last fishing catch by 25 percent has seriously affected the Cuban economy. These new problems further exacerbated the economic situation already plagued by inadequate housing, and shortages of food and clothing.

The Cuban leadership, since the fall of 1979, has acknowledged the serious economic situation. The Cuban people were being told that 21 years of economic hardship would continue for some time in the future. They were told that they would have to continue to endure shortages, as well as the rationing of basic foodstuffs and clothing. They also were admonished to work harder and more efficiently. The visits to Cuba during 1979 of over 100,000 exiles from the United States became part of this economic setting and significantly contributed to the unsettling of the Cuban populace.

A significant segment of the Cuban population has been alienated by the 21 years of a highly structured, all-pervading political system under Fidel Castro. These people have become nonparticipants and many are considered to be "anti-socials" by the government. In reaction to signs of unrest which began to appear in December 1978, the Cuban Government began to conduct a crackdown against black-marketeering and other anti-social activity. Those most affected by this economic and political setting are the unskilled, semi-skilled blue collar workers, and the anti-social elements which include criminals, homosexuals and prostitutes. The number of anti-socials appears to have been greatly exaggerated in the media, however, judging from the fact that only a little more than 1 percent of the total as of August 1980, were being held as potentially excludable under U.S. law.[1]

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[1] See p. 111.

The Cuban decision to permit large-scale emigration was taken in the face of a deterioration of relations with the United States. The Cuban perception that normalization of relations would be pushed well into the next presidential term, and therefore would not, in the long-term, damage prospects was another key factor of the Cuban decision. The immigration issue, could become the catalyst that moves the United States and Cuba toward talks in 1981 on the various issues in the U.S.-Cuban agenda.

INTRODUCTION AND BACKGROUND

The sudden migration of over 120,000 Cubans to the United States, rather than being an isolated occurrence, is part of an intricate set of factors related to economic and political developments in Cuba as well as a function of the steadily deteriorating U.S.-Cuba relationship. The current refugee situation has become an issue which not only has serious implications for Cuba's domestic political and economic situation and for its system in general, but also has implications for U.S.-Cuba relations. The refugee issue, which began as a dispute between Cuba and the governments of Peru and Venezuela over political asylum, also affects Cuba's foreign policy in terms of its position in the Third World and its relations with its Latin American neighbors. Implications from the domestic U.S. perspective are especially serious as policymakers grapple with a myriad of problems related to immigration law and the effect internally of this latest influx of refugees.

This paper will place the refugee issue into the context of the economic and political situation within Cuba and the state of the relationship with the United States. The background to the problem will be discussed with specific reference to the political asylum dispute and the early stages of the movement of the refugees out of Cuba. The motivation and character of those who are leaving Cuba will be explored. The section on U.S.-Cuba relations will provide additional perspective as the refugee situation is placed into the overall fabric of the state of the relationship.

This paper is based on the coverage provided by the major U.S. press since the massive refugee exodus began, on discussions with on-the-scene reporters, Cuban press and radio reports, and on discussions with officials of the Office of Cuban Affairs at the Department of State, as well as officials of other executive branch agencies. Discussions were also conducted with diplomats assigned to the Cuban Interests Section in Washington. The paper also draws on the author's experiences in Cuba and discussions held in Havana with Cuban officials, the latest in October–November 1979.[1a]

The spark for the current refugee situation was provided on April 1 when six Cubans, seeking political asylum, crashed through the gate of the Peruvian Embassy in Havana; a Cuban policeman guarding the Embassy was killed in an exchange of gunfire. This was the latest in a series of forcible entries into the embassies of Peru and Venezuela by Cubans seeking political asylum, which had become the source of a contentious diplomatic dispute between Cuba and the two govern-

[1a] U.S. Library of Congress. Congressional Research Service. Cuban Foreign Policy at the end of the Seventies: A Report on Discussions with Cuban Foreign Policy Officials, November 1979, by Barry Sklar. Washington, 1979.

ments. The Cuban Government, earlier, had been especially incensed by the actions of the Peruvian Government, which had ordered its Ambassador to Havana to provide diplomatic protection for a group of Cubans he initially talked out of seeking asylum. The Ambassador was subsequently recalled by Lima. After the April 1 incident, the Peruvian and Venezuelan governments demanded that the Cuban Government grant safe-conduct passes to the 40 people that had sought refuge in the two embassies.

On April 4, President Castro denounced the "deceit and cowardice" of the Latin governments that, at the "bidding of the United States," participated in the diplomatic and economic boycott of Cuba. He specifically charged the embassies of Peru and Venezula with providing protection for "common criminals, bums, and anti-social elements." His most significant statement that day, however, was the announcement that Cuba was withdrawing the guard from the Peruvian Embassy.

As a result of what seems to have been a miscalculation by the Cuban Government, upon receiving word that the guard had been withdrawn, Cubans in vast numbers flocked to the Embassy. Within 72 hours, until the point when the Cuban Government actively began to prevent people from approaching the Embassy by erecting barricades in the Miramar neighborhood, 10,800 Cubans crowded on to the Embassy grounds.

After some days, as health and sanitary conditions rapidly worsened, the Cuban Government announced that all those in the Embassy would be permitted to leave Cuba with the exception of those who had forcibly entered the grounds. On April 16, after Peru and other nations agreed to accept a certain number of refugees from the Embassy, the first planeload left for Costa Rica, where they were to be transported to Peru. Other countries, including Spain, West Germany, Canada, and the United States agreed to take a share of the refugees. The United States said it would accept 3,500.

The Cuban Government, however, angered by the anti-Cuban manner in which Costa Rican President Carazo greeted the first arrivals, stopped the flights after two days. The Cubans were also angry over Costa Rican plans to create a huge staging area for the refugees in San Jose. The Costa Rican Government said the staging area was to facilitate the orderly dispersal of the refugees to the final country of destination, but, in Cuban eyes, it was a deliberate attempt to create anti-Cuban propaganda over refugee conditions.

The Cuban Government cleared the way for what became an exodus of thousands to the United States on April 21, when it announced that evacuation of those who wanted to leave would be permitted by boats arriving from Florida. *Granma*, the official daily newspaper and organ of the Cuban Communist Party, clarified the announcement by reporting on April 22 that the Cuban Government would comply with requests from those bringing boats from Florida seeking to evacuate relatives in addition to refugees from the Peruvian Embassy. According to *Granma*, and to statements by Fidel Castro later, the Cuban Government opened the exit gates to accommodate the requests of Cuban exile leaders who traveled to Havana to negotiate the arrangement.

These events notwithstanding, however, there are indications that the Cuban Government in the past months, for a number of reasons—economic, political, and those dealing with foreign affairs—was interested in permitting emigration to the United States. Recent economic and political developments have had an unsettling effect on Cuban life, and pressures on the government were definitely building within the population. In this period, quiet discussions between U.S. and Cuban officials in Washington and Havana focused on the application of the recently passed Refugee Act of 1980 to the question of permitting additional Cubans, principally released political prisoners, to emigrate to the United States. In these same discussions, Cuban officials expressed their government's anger over what they perceived as U.S. encouragement of illegal emigration from Cuba. Specific references were made to the warm reception and accommodation granted to those fleeing Cuba in hijacked ships in a rash of incidents since November 1979. These Cubans who left illegally were granted political asylum and given shelter in this country. The Cuban Government felt that U.S. actions were in violation of the spirit of the anti-hijacking agreement to which the Cubans contend they still adhere, although it is not technically in effect. The Cubans felt also that U.S. actions were tantamount to U.S. encouragement of illegal emigration and increasingly were becoming anxious regarding its effects on the domestic situation in Cuba.

In these discussions the Cubans made references to past experiences of mass migrations to the United States. Based on these conversations, State Department officials—

> did not believe that the Cuban Government would unilaterally exercise the option of lifting the gates to allow discontented elements to leave the country, although a CIA report prepared in January discussed the possibility of such an occurrence.[2]

Publicly, however, in early March, Fidel Castro issued an ominous warning to the United States of the refugee situation which ultimately occurred. In a lengthy speech before the Federation of Cuban Women, devoted mainly to the theme of women's rights in Cuba and the problems of Cuba's economy, President Castro said that if the United States did not take measures to discourage the illegal departures from Cuba, Cuba might take measures of its own. He then referred to the time 15 years before when the port of Camarioca was opened to permit migration to the United States under circumstances similar to the present situation. President Castro said, "We are not going to be taking measures against those who plan to illegally leave the country while they [United States officials] encourage the illegal departure from the country." The spontaneous Peruvian Embassy incident of April 1 provided the set of circumstances by which Cuba's emigration policy was implemented.

Fifteen years ago, in late September 1965, Fidel Castro reacted similarly to a host of illegal exits by sea which he charged were encouraged by the United States because of warm and heralded welcomes given to those leaving illegally. He opened the port of Camarioca to those Cubans who wanted to leave on ships arriving from Florida. In response, President Johnson in October, in a speech at the Statue of

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[2] U.S. Congress. House Intelligence Committee. Subcommittee on Oversight. The Cuban Emigres: Was There a U.S. Intelligence Failure? 96th Cong., 2d Sess. Washington, U.S. Govt. Print. Off., 1980.

Liberty, officially opened the door to the Cubans when he stated, "I declare to the people of Cuba that those who seek refuge here will find it." After one month of haphazard and dangerous crossings, during which 5,000 Cubans entered Florida, the United States and Cuba regularized the departures by aircraft from Varadero. From 1966 to 1973, when the "Freedom Flights" ceased, 260,000 Cubans migrated to the United States to join the thousands that preceded them since Fidel Castro came to power in 1959. In the past 21 years, excluding the numbers involved in the current refugee exodus, 1.5 million people have migrated from Cuba with close to 800,000 settling in the United States.

Prior to the events of the spring of 1980, the most recent Cuban arrivals were 15,000 released political prisoners and their families who have come in the past year and a half. This release of 3,600 political prisoners by the Castro Government came in response to efforts on the part of some leaders of the Cuban exile community at the end of 1978 to establish a closer relationship with Cuba. The United States agreed to admit the political prisoners and their families under the parole authority of the Attorney General.

The United States response in the early weeks of the spring 1980 exodus generally was unclear and uncertain.[3] Taken by surprise by Cuba's sudden lifting of the gates to emigration, the Carter Administration, in a short period of time, both encouraged and discouraged the exodus from Cuba. At the same time that President Carter declared that the U.S. Government would welcome the refugees "with an open heart," authorities were seizing boats involved in the exodus. Meanwhile the Administration attempted to use the multilateral approach by attempting to involve other nations. In early May, a meeting was held in Costa Rica with other concerned nations. The United States, however, was unable to gain support other than the agreement to establish a three-nation commission which would attempt to deal with the Cuban Government.

The influx of thousands of Cubans presented the United States with a series of dilemmas relating to recent U.S. immigration policy. The Refugee Act of 1980, recently enacted, established quotas for refugees that would be accepted from the various countries. The Act provided that applications for asylum would be considered on a case by case basis. The tremendous daily flow of people, however, made the law virtually inoperable. A further complicating factor was the apparent distinction being made between the newly arriving Cubans and the over 15,000 Haitian refugees in Florida. Before the Cuban refugee exodus begun, the Administration ruled that the Haitians were economic, rather than political, refugees and therefore deportation proceedings were initiated. The willingness of the Administration to consider the Cubans as applicants for political asylum and to ignore economic considerations led to charges of "double standard" and discrimination by those who saw the Cuban and Haitian cases as similar. Perhaps the major complication, however, was the fact that U.S. public opinion generally was negative. It reflected concern with regard

[3] For an analysis of the Cuban situation as it related to U.S. immigration policy, see U.S. Library of Congress. Congressional Research Service. Refugees in the United States: The Cuban Emigration Crisis. Issue Brief No. IB80063, by Charlotte Moore, May 16, 1980. Washington, 1980.

to the burdens this influx of people would have on the already strained U.S. economy.

The Exodus in Context

The desire of tens of thousands to emigrate to the United States, arguably, is not particularly a Cuban phenomenon. Long lines of people applying for visas at U.S. Embassy buildings and consulates in major Latin American cities are stark testimony to the reality of the "pull factors" attracting people to this country. The contrast of this nation's general affluence with Latin America's general poverty, the belief that opportunity awaits those who work for it, and the way of life within a democratic and open political system are major factors which draw people to try to migrate to the United States. A study done by the Kettering Foundation in the early 1970's found that one out of every three persons in Latin America wanted to migrate to the United States.[4] A recent State Department report stated that 4 million visa applications per year are received from people who want to immigrate to the United States.[5] In terms of actual numbers, Western Hemisphere immigration to the United States in the 1967–76 period showed an increase of 43.4 percent over the 1956–65 period. From 1967 to 1976, 1,507,434 people from Latin America, the Caribbean, and Canada migrated to this country.[6] In addition, INS and the Bureau of Census acknowledge that from 3 to 6 million people are in the United States as illegal aliens.

Those factors that draw immigrants to the United States played a large role in the Cuban exodus. Cuba's present social, economic, and political situation provide additional keys to understanding this latest wave of migration.

The collectivist philosophy of socialism has brought Cuba a way of life that has not been accepted by the nation's entire population. Government policies in the name of the common good have been responsible for education and public health systems which are ranked among the best in the developing world as evidenced by Cuba's very low rate of infant mortality, as only one example. Policies of equitable distribution of the nation's limited resources, on the one hand, while eliminating the extremes of rich and poor so prevalent throughout Latin America, have been undertaken at great individual sacrifice on the part of the Cuban people. The social and political system also requires a collectivist approach with its strong demand for mass participation at highly structured and organized government-sponsored activities which pervade all facets of Cuban life. A significant segment of the Cuban population, reacting against this style of life and to pressures and influences from within and outside the country, after 21 years have chosen to leave for the United States. The following is a discussion of the economic and political setting in Cuba which provided the context for the exodus of 1980.

Economic Situation

The Cuban economy is in a period of sharp decline. The projected growth rate for 1980 is 3 percent. This continues the decline begun in

[4] Washington Post, May 8, 1980.
[5] Washington Post, May 28, 1980.
[6] U.S. Library of Congress. Congressional Research Service. U.S. Immigration Policy: The Western Hemisphere. Issue Brief No. IB 80–69, by Joyce Vialet, April 9, 1980. Washington, D.C., 1980.

1979 when the growth rate fell to 4.3 percent from the 1978 figure of 9.4 percent.[7] In per capita terms, the rate of growth fell from 8.2 percent in 1978 to 3.1 percent in 1979, and is projected to fall to 1.8 percent in 1980.[8] The sugar output is projected to fall to 6.5 million tons in 1981, from the 1979 production of 8 million tons. This has limited foreign exchange earnings and has slowed imports of badly needed raw materials and technology.[9] Cuba's hard currency debt is $2.5 billion to $2.8 billion and a debt roll-over could add $100 million in interest charges at a time when hard currency is in limited supply.[10] To meet Cuba's basic investment and consumption needs, massive economic assistance is required. Thus far, Cuba has been able to stay afloat because of Soviet economic assistance which amounts to $8 million per day.[11] In the past months, the current economic situation has been seriously affected by the destruction of at least 25 percent of the sugar crop because of blight, the loss of practically the entire tobacco crop because of blue mold, and the recurrence of swine fever, which affects pork production and thus reduces the amount of meat for domestic consumption. The last fishing catch was down by 25 percent. The tobacco crop failure, in part, is responsible for Cuba's first large-scale unemployment problem; since 1959, with the layoff of 25,000 tobacco workers, Cuba is now in the unusual position of importing tobacco for domestic consumption. Unemployment has occurred in the construction industry from the severe reduction of building materials usually received from the Soviet Union and other Socialist countries. These relatively recent problems further affected the economic situation that for many years has been plagued by inadequate housing, lack of quality goods, and shortages in food and clothing.

Cuba's serious economic plight has been acknowledged by the nation's leadership and has been made known to the Cuban public since the fall of 1979 through a series of major addresses by officials, including Fidel and Raul Castro. In these speeches, Cuban officials have not only spoken of the acts of nature that have severely damaged the island's economy but also addressed themselves to the problems created by the lack of raw materials and manufactured goods. In a speech much reported in the U.S. press (although made in a closed session of the National People's Government Assembly on December 27), Fidel Castro gave a comprehensive account of the plight of the Cuban economy, referring to shortages, the high cost of energy and other problems. References were made to the problem of receiving goods from the Soviet Union and other socialist countries that are not necessarily needed, such as TV sets, while such needed items as towels, sheets, and other textiles are not received.

Raul Castro, in a speech on December 4, spoke about unjustified absenteeism and lack of motivation among the workers and charged

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[7] Telephone conversation with Carmelo Mesa-Lego, University of Pittsburgh. Data taken from his forthcoming book, The Economy of Socialist Cuba: A two decade appraisal. Albuquerque, University of New Mexico Press. Scheduled publication, March 1981.

[8] Ibid.

[9] Business Week, May 5, 1980.

[10] Forbes, May 12, 1980.

[11] The Soviet's payment over the world price for Cuban sugar and the subsidy for Cuba's energy expenses form a large part of that figure.

It should be kept in mind that, as a general rule, economic statistics concerning Cuba (as with most developing countries) are hard to verify, and accordingly should be used with care.

that many workers deliberately worked at a slow pace so that production goals would not be upgraded. Problems of worker motivation were noted by Vice President Carlos Rafael Rodriguez during this writer's discussions with him in Havana in November.[12]

In recognition of growing discontent and unrest, speeches and actions by the government leadership in the 1979–80 fall and winter months demonstrated an attempt to address the popular grievances against the economic system. In his December 4 speech, Raul Castro railed against government officials who shirked responsibilities and said that the Party would not tolerate those officials who did not fulfill their duty. He also said that the government was developing a new wage system which would benefit the workers, and he announced that the labor laws were being modified.

Significant economic measures were taken in response to public pressure. The wage reform plan will increase the minimum wage and readjust pay scales. In addition, a certain amount of private business is now being permitted on a free market basis, especially in the sale of agricultural products. Licenses have been issued to craftsmen and entrepreneurs to establish their own businesses. Other significant structural changes are being made in an attempt to reduce the rigidity in the economic system, which in this 21st year of revolutionary government, in a material sense, has not yet fulfilled the hopes of the Cuban people for a better way of life.

The Government's will to take action was demonstrated in mid-December when the Ministers of Transportation and Public Health were fired. This proved to be a precursor of the largest governmental shakeup in the history of the regime in January, in which more power was consolidated under Fidel Castro himself and members of the Council of Ministers were made directly responsible for the day to day operations of the various ministries.

The Cuban government has created a vehicle by which people publicly express their opinions and air their grievances against the system. The weekly publication, *Opina*, which solicits citizen opinion on all facets of life in Cuba, is so popular that it sells out within minutes after hitting the newsstands.

The speeches and measures pronounced in this period conveyed another important message that had particular relevance to the refugee situation that occurred. The Cuban people were being told, very directly, that 21 years of economic hardship would continue for some time in the future. Fidel Castro in his December 21 speech said that Cuba was—

> sailing in a sea of difficulties. We have been in this sea for some time and we will continue in this sea, sometimes more stormy and other times more calm, but the shore is far away. . . . We will march through a sea of difficulties; we will not be crossing it.[13]

The Cuban people were being told that the shortages that they have endured would continue. They will have to work harder and more efficiently.[14] They would have to continue to contend with the rationing

[12] Sklar, Cuban Foreign Policy at the end of the Seventies, p. 8.

[13] Fidel Castro. Speech before the National People's Government Assembly, December 27, 1979.

[14] In March it was announced, for example, that the textile industry was being put on a full-time schedule to increase production and to create jobs. (Radio Havana, March 18, 1980.)

of basic foodstuffs, clothing, and other commodities. They will, therefore, have to continue to limit themselves to the 2 pounds of meat per month, 1½ pounds of chicken per month, 2 ounces of coffee every 15 days, 4 meters of cloth per year, two packs of cigarettes per week, one pair of shoes, one pair of trousers, one dress and two shirts per year.

The visits to Cuba, in the past year, by thousands from the exile community in the United States, became a significant part of this economic setting. In 1979, 100,000 members of the "Comunidad" (as they are referred to in Cuba) visited families and friends as part of the "dialogue" established by Fidel Castro and exile community leaders. The motivation for the Cuban Government to initiate the "dialogue" was both political and economic. It was seen as an opportunity to transform the exile community into an agent for, rather than against, normalization with the United States. The Castro government permitted the visits and released 3,600 political prisoners. The "dialogue" created some good will and needed foreign exchange. In 1979, visitors from the "Comunidad" spent $100,000,000. Whether or not the Castro Government foresaw the ramification of the exile visits, it is clear that they have played a significant role in today's situation.

The stark contrast in American and Cuban lifestyles was evident every day as members of the exile community and their Cuban friends and relatives exchanged emotional greetings and farewells. The success stories of members of the Cuban exile community in Miami told to their brethren in Cuba's cities, towns, and rural villages were underscored by the photographs of the houses, businesses, and cars, stylish quality clothing, expensive jewelry, calculators, tape recorders, and cameras. The exiles brought other symbols of affluence for their Cuban relatives and friends to see. A typical city scene in Havana of teenagers sporting Levis and T-shirts from Disneyworld and with slogans familiar to the United States such as "Better in the Bahamas," "Marlboro," and "Adidas" was evidence of the changes seen since the influx of the thousands of visitors from the exile community. It also created a strong demand for American goods brought in by the visitors, stimulating the black market where jeans sell for $125–$250, and shirts for $70.

The stimulation of consumerism in an essentially non-consumer society has had an unsettling effect on everyday life in Cuba. The recent increase in petty crime in Havana and evidence of prostitution, a relatively new phenomenon in today's Cuba, indicates that there is a need for money to buy the goods that are now available. Various reports from refugees newly arrived in the United States indicate that beyond the drive to purchase the jeans and shirts, many have to augment their food supply through purchases in the black market. Participation in the black market, an extra-legal and counter-revolutionary act, has created a degree of tension among the people that has political ramifications.

Political Situation

Cuba's highly structured and all-pervading political system, under 21 years of rule by Fidel Castro, has alienated a segment of the population. Loyalty to the regime is measured in terms of participation in government-sponsored mass organizations and programs. Those who choose not to participate in mass organizations like the Committees for the Defense of the Revolution, the Union of Communist Youth, and the Federation of Cuban Women have chosen not to be in the mainstream of Cuban life. They are less likely to accept the exhortations of the government for continued sacrifice in the name of the Revolution. The majority of these people are considered to be "anti-socials" by the government. While it is not possible to determine the actual loyalty of Cubans who are participants in the political system, those who have chosen to exclude themselves are more likely to represent dissatisfied elements of the population. Even among those who are considered participants, there are indications that there has been a diminishing of revolutionary zeal and fervent support of the government.

The somewhat unsettled situation in Cuba today, much related to the economy as discussed above, has had its effects on the political climate. Signs of unrest and discontent began to appear in December 1979 when anti-Castro posters and leaflets were reported to have been seen in Havana and a clandestine printing press reportedly was discovered. At this time, it was reported that 40 arrests were made, many of them being released political prisoners.[15]

It is conceivable that the presence, in the streets of Havana, of hundreds of released political prisoners was responsible for some of the unrest and tension present in this period before the exodus. Most of these former prisoners had been given their exit permits by the Cuban Government and were waiting for processing by the U.S. Interests Section for entry into the United States. The Cuban Government repeatedly pressed the United States to speed the processing; some officials believed that the United States deliberately was foot dragging in order to keep this discontended and disruptive element in Cuba as long as possible. Many of these former prisoners held menial jobs or were unable to obtain work because of their status. Some of the former prisoners were involved in an incident at the U.S. Interests Section on May 2 at the time of the exodus.[16]

In his December 27 speech before the National Assembly, Fidel Castro declared that there was going to be a crackdown against this growing "extremist" element. His appointment of Central Committee Member and trusted associate Ramiro Valdes as Minister of Interior in January emphasized Castro's new hard line. Since then, in the past months, the government security crackdown has produced arrests for black-marketeering, petty crimes, and other anti-social activity. This has created some tension among those who look to the black market for foodstuffs and other commodities. According to some of the arriving refugees, those arrested for petty crimes are placed on "conditional liberty" which entails strict probation and loss of job and pension rights. Refugees also complain of the arbitrariness of the "Ley de Peligrosidad" (Law of Common Danger) by which the police make sweeping arrests for anti-social behavior. According to some accounts,

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[15] Boston Globe, April 11, 1980.

[16] The former prisoners and family members had been called to the Interests Section so that U.S. officials could respond to their increasing pressure to speed the processing procedure. While being addressed by the U.S. staff outside the entrance, they were attacked by Cubans who, according to some sources, were government security agents. As of this writing, of the 389 people who sought refuge in the building, about 19 remain. The others have returned to their homes after questioning by the Cuban authorities. Some of the former political prisoners in the group were able to leave for the United States via Mariel.

many people have been arrested under this law for associating with anti-social elements even though it may be in work surroundings. The presence of armed police and unarmed military (albeit in casual activity and seemingly off-duty status) is a phenomenon that was not seen in Havana by observers a few years ago.

In addition to the increased activity of the security apparatus, refugee reports indicate greater surveillance of the population by the neighborhood Committees for the Defense of the Revolution. These block committees serve as an efficient communication and mass mobilization system but also are the watchdog of the neighborhood's revolutionary adherence and spirit.

The university system, which offers the opportunity of higher education to the masses, is also going through an uneasy period according to some reports. Radio EFE of Madrid reported that there have been rumors of students from the University of Havana and other study centers being expelled for "ideological diversionism." [17] Another report said that a "cleansing" of the university had been occurring.[18]

Some reports of discontent emanating from Cuba center on reaction to Cubans serving in the armed forces in Africa. One refugee reported that "most mothers" are against their sons going into the military because they are sent abroad.[19] Negative reaction to Cuba's African involvement notwithstanding, it is generally believed that Cuba's "internationalist" policy has had a positive effect on the effort to reinstall revolutionary zeal in support of the Revolution.

Those Involved in the Exodus

The actual determination of the type of person leaving Cuba under these circumstances can only be made after careful screening and analysis by involved U.S. Government agencies such as the Immigration and Naturalization Service and the Department of Health and Human Services. Preliminary information, based on journalistic accounts of discussion with refugees and informal comments and impressions from U.S. Government officials at various levels, gives uneven and imprecise information on the refugees. At best, as the refugee situation continues to unfold, only generalizations can be made.

Whereas earlier heavy migrations from Cuba brought to this country, first, political supporters of the Batista regime along with those from the business sector, and then those from the professional and skilled classes, this new influx seems to be composed of lower, semi-skilled or unskilled working class Cubans. Many of the refugees seem to be what the Cuban government considers the "anti-socials." They are the non-supportive, non-participative, anti-system elements, which includes the vagrant, the petty criminal, the homosexual, and the prostitute. Many, however, are respectable family members who are students, lower level government employees, truck drivers, restaurant workers, and laborers. In fact, there is some evidence that some of the new arrivals were formerly exemplary militant supporters of the Castro government who simply have lost faith in the power of the government to improve their economic plight.

[17] Radio EFE, March 13 in FBIS Daily Report, Latin America, March 17, 1980.
[18] Washington Post, April 10, 1980.
[19] Washington Post, May 11, 1980.

Suspicions and charges on the part of U.S. officials that the Cuban government was taking advantage of the situation by emptying the nation's jails of common and hardened criminals began to be heard as individual men, more hardened and rougher in appearance than earlier arrivals, were placed on boats ahead of those from the Peruvian Embassy and those with relatives in the United States. The White House on May 14 accused the Cuban government of taking hardened criminals out of prison and mental patients out of hospitals and forcing boat captains to take them to the United States. Many of the refugees say they were released from jail on the provision that they leave for the United States on boats from Mariel. The Washington Post reported (May 2) that the Cuban government seemed to be giving preference for departure to those who had served jail terms.

The Cuban government has denied a deliberate policy of foisting Cuba's undesirables on the United States. *Granma* on May 15 said that the anti-socials are leaving voluntarily and that the government has not permitted the departure of persons involved in crimes or acts of bloodshed. The article also stated that mentally ill persons on the boatlift were probably there because they had been requested by relatives who arrived in Mariel to take them to the United States.

Official statistics from U.S. Government sources indicate that the number of criminals and other undesirable elements is lower than originally reported in the media. Out of the total of 120,737 Cuban refugees, 1,656—a little more than 1 percent—are being held in Federal correctional institutions as "potentially excludable" under U.S. immigration law.[20]

One problem with determining the number of actual criminals is the fact that a certain percentage of this element has committed relatively minor crimes, such as purchasing an item on the black market. Further complication in determining the number of criminals is that, reportedly, many ordinary people are voluntarily professing that they are homosexuals, prostitutes, or otherwise have engaged in anti-social behavior, in order to receive exit papers from Cuban authorities.

It is significant that even the Cuban government, in a departure from its earlier position, seems to be accepting the fact that individuals other than anti-social "lumpen" (scum) and anti-government "reactionaries" are making the decision to leave Cuba for the United States. A *Granma* editorial of May 19 related the phenomenon of emigration from underdeveloped countries to developed nations to the poverty that results from the unequal distribution of resources in the world. The government organ mentioned the large numbers of Mexicans, Haitians, and other Latin Americans who want to migrate to the United States because of economic conditions. *Granma* noted, significantly, that "It does not occur to anyone to call them dissidents." After making this point, however, the editorial charged the United States with the destabilization of Cuban life which promoted the mass exodus; and it reverted to the characterization of "lumpen" (scum) for those leaving Cuba.

In the context of announcing a tough Administration policy toward Cuban criminals and rioters at the Fort Chafee processing center in early June, presidential press secretary Jody Powell said on June 7,

[20] Cuba-Haiti Refugee Task Force, August 25, 1980.

". . . it would be grossly unfair . . . to look at all of those Cubans as if they were like the few hardened criminals." He said that there is evidence that Fidel Castro "exported these undesirable elements to the United States in a calculated effort to disguise the fact that the vast majority of those Cubans . . . were and are law-abiding citizens whose only purpose was to seek freedom and reunification with their families."

In the short-term domestic political context, the Cuban government has been able to turn the events of the spring of 1980 into positive advantage. The decision to open the gates to all who desire to leave permits the government to rid the country of that segment of the population that has not participated in the system as well as those who have been extremely unhappy under the regime. Mixed in among the political prisoners, the vagrants, and the other anti-socials are the workers, students, and reportedly, even government and military personnel whose unhappiness created pressures on the Castro government. Those Cubans who remain after the exodus has taken its course generally will be those who have more readily accepted the system and will continue to sacrifice and work within it. This of course is based on the assumption that all of those who desire to leave will be able to do so.

A further political advantage for the Castro government is the fact that the events of April and May have developed within Cuba a revolutionary fervor not seen in many years. Reaction of pro-Government Cubans to the exodus of those they deem disloyal, and to the perceived threat from the United States, has whipped up zealous support of the Castro government.

The *Granma* editorial of May 19, which may have been written by Fidel Castro himself (according to speculation that major *Granma* editorials on the exodus have been written by the Cuban President), also sent a message to the Carter Administration. It was made clear, in response to the announced desire of the United States Government to discuss the emigration situation with the Cuban government, that "We are ready to discuss and negotiate with the United States our problems and global relations, but not isolated and partial problems which interest only them and their strategy against Cuba." The Cubans believe that the question of emigration is inextricably related to the entire set of issues that comprise the U.S.-Cuba agenda. They regard consideration of the emigration issue alone as working toward partial solutions at best. The United States, on the other hand, does not want to be drawn into a full discussion at this time and would rather deal only with the immediate problem of emigration.

United States-Cuba Relations

The current influx of Cubans into the United States must be seen in the context of the present state of the U.S.-Cuba relationship. Although the Cuban decision to open the gates seems to have been a spontaneous one which seized on the moment provided by the situation at the Peruvian Embassy, the act itself was apparently an implementation of a policy designed to relieve substantial pressure on the Cuban system.[21]

[21] The components of the policy remain vague, so far as what has been revealed to the public. Insofar as the policy is described in this narrative, its existence became evident partly because of discussions with U.S. and Cuban officials and partly through perceptions suggested from news reports.

A significant complementary factor influencing the immediate decision, very likely, was the Cuban assessment of the U.S. election year political picture as it related to the normalization of relations process. For some time it has been clear that the Cuban government believed that the normalization process was essentially stopped since it would not be politically feasible for the Carter Administration to deal with Cuba on substantive bilateral issues as the presidential election approached. In fact, because of the deterioration of relations, symbolized by the Soviet brigade issue, Cuban officials believed that Cuba would become a campaign issue and that, therefore, the prospects for resuming the normalization process would be pushed well into the next presidential term.[22] Consequently, the decision to allow thousands to migrate to the United States, while provoking the expected ire of the United States, was not seen as one that would further affect or damage the short-term normalization prospects.

During the Carter Administration, relations with Cuba have evolved from the highest, most positive plane to a low, negative state reminiscent of the early 1960's. This period saw positive approaches toward the normalization of relations with the opening of the Interests Sections in the respective capitals, the relaxation of certain provisions of the U.S. embargo, release of U.S. prisoners by Cuba, opening of a dialogue with the exile community with the resultant release of 3,600 political prisoners, the signing of maritime and fishing agreements, along with numerous other examples. Negative aspects of the U.S.-Cuban relationship in this period included continued U.S. concern over Cuban military involvement in Africa, U.S. perception of a strengthening of Cuban military ties with the Soviet Union as well as the perception of a new Cuban aggressiveness in the Caribbean and a growing sense of competition with the Cubans in the area. The negative side of the relationship is also fueled by the Cuban perception that the United States is threatening Cuba with new cold war rhetoric and newly aggressive military activity which included the renewal of spy-plane flights, clamor over the presence of a Soviet training brigade claimed to be remnants of the Soviet force in Cuba withdrawn after the Cuban missile crisis in 1962, the establishment by the United States of a Joint Caribbean Task Force at Key West designed to increase U.S. military presence in the Caribbean, and military maneuvers at the Guantanamo naval base, as well as military maneuvers in the Caribbean. The recent U.S. decision to station 20 electronic warfare planes, equipped to intercept Cuban military communications, and 10 A-4 attack jets at the Key West base—10 minutes from Havana—increases Cuba's perception of threat. Anti-Cuban presidential campaign rhetoric, such as the suggestion by Ronald Reagan that the United States blockade Cuba or mine harbors as a response to the Soviet invasion of Afghanistan or other Soviet action, has contributed to what seems to be the development of a renewed siege mentality on the part of the Cubans.

In past months different sectors of the Cuban Armed Forces have been placed on alert status, and in March, the military command called over Havana radio for increased readiness, citing Fidel and Raul Castro's statements on the negative turn in U.S. policy toward Cuba

[22] Sklar, Cuban Foreign Policy at the end of the Seventies, p. 4.

which "has virtually returned to the cold war era."[23] In his speech on May 1, Fidel Castro announced that a territorial militia would be formed to help defend the nation against external threats. Two recent incidents—one in which Cuban fighter planes were involved in an attack on a Bahamian patrol boat, and a second in which Cuban fighters buzzed a U.S. helicopter involved in rescue efforts of surviving Bahamian seamen—may well be attributed to a sense of tension and nervousness among the Cuban military in these times.

With the advent of the refugee situation, tensions have been further exacerbated as a result of Cuban decisions as to who may leave for the United States and the manner in which the exodus is being handled, U.S. policy on the new arrivals, the numerous reported incidents between the boat captains and Cuban authorities at the port of Mariel, and the heightened invective on the part of the nations' leaders against one another.

U.S. officials, angered over Cuba's sudden, unilaterally exercised emigration policy, have criticized the Cuban government. The influx of Cubans is wreaking havoc with the U.S. immigration system, operating under legislation only recently passed, and is forcing the United States to deal with contradictions in immigration policy vis-a-vis the Cuban and Haitian cases. Also reacting to reports that the Cubans were forcing boat captains to carry criminals, the mentally ill, and other undesirables rather than relatives of exiles in the United States, U.S. officials have lashed out against the Cuban leadership. On May 5, in his remarks before the League of Women Voters where he spontaneously declared an "open heart and open arms" policy to Cubans fleeing the Castro government, President Carter attacked the "inhumane approach" of Fidel Castro. In referring to the incident in front of the U.S. Interests Section in Havana, in which reportedly government-sponsored supporters attacked 800 former political prisoners and others, President Carter said that it was "mob violence instigated by Castro himself."

From the very inception of the developing refugee situation, even before the incident at the Peruvian Embassy, the Cuban government, as stated above, viewed the refugee problem as part of the bilateral relationship with the United States. References were made regarding another Camarioca similar to 1965; charges were made that the United States was promoting instability in Cuba through U.S. immigration policy; and comments were made with regard to the United States during Cuba's feud with Peru and Venezuela over the political asylum issue.

The pro-government demonstration of one million Cubans on Quinta Avenida in front of the Peruvian Embassy on April 19, Fidel Castro's May Day speech at the Plaza de la Revolucion, and the huge demonstration of 5 million Cubans (half the nation's population) in various cities across the island on May 17 were highly emotional and vitriolic expressions of anti-American sentiment not seen in Cuba since the days of the Bay of Pigs in 1961. The scheduled joint military maneuvers in the Caribbean, Solid Shield 80, was the object of much anti-American sentiment at this time; the U.S. cancellation of the Guantanamo exercises of the maneuvers on the eve of Fidel Castro's May

[23] FBIS Daily Report, Latin America, March 27, 1980.

Day speech was an attempt by the United States to dampen this fervor. The May 17 demonstration was a visual reminder of the Cuban argument that the real problems were the continued economic embargo ("blockade" in Cuban parlance), the U.S. naval base at Guantanamo, and the resumption of the spy-plane fights. Significantly, because of security concerns in light of the foreseen anti-American tone of the May 17 demonstration, most of the diplomats assigned to the U.S. Interests Section in Havana and their dependents were sent to the United States a few days beforehand. The parade of 1 million passed in front of the former U.S. Embassy building on Havana's Malecon without incident as the demonstrators heeded Fidel Castro's admonitions for a peaceful and non-violent march.

Cuba, on May 23, formally rejected the request of the three-nation (Costa Rica, Great Britain, United States) commission established at the meeting in San Jose in April, for negotiations on the refugee exodus. The Cuban government called the proposal, which would have allowed refugees to travel to nations willing to receive them, "totally unacceptable," and called it "an international attempt to meddle in Cuba's internal affairs." [24] Cuba has indicated that it would be in touch with countries on a bilateral basis.

In the short term, at least, the current refugee situation seems to have severely damaged Cuba's relations with prestigious Latin American neighbors previously supportive of Cuba. Peru was the nation that initiated the efforts several years ago in the Organization of American States to permit member nations to deal with Cuba if they so chose, in effect, ending the OAS embargo on Cuba. Venezuela and Costa Rica had amicable relationships with Cuba. In all three cases, however, the present governments in power are more conservative than those that had previously had a closer relationship with Cuba. Mexico, a long-time supporter of Cuba, remains supportive of the Castro government; President Lopez Portillo visited Havana in late July.

Cuba's image in the Third World has been damaged to a certain extent as other nations see Cuba with an international refugee problem not usually associated with progressive, developing states. This issue compounds Cuba's image problem, which has been seriously affected by the Soviet invasion of Afghanistan because of Cuba's close association with the USSR. Cuba's loss of the long-sought Security Council seat in the United Nations was a setback to its prestige in the Third World. The Cuban government's call for a non-aligned ministerial meeting in Havana in July to consider the "international situation as a whole" conceivably was designed to shore-up its relations with the Third World.

Recent Developments

The tremendous flow of refugees entering Florida via the boatlift has slowed to a trickle as Coast Guard operations, in compliance with President Carter's announced policy of mid-May, have prevented ships from leaving Key West for Mariel. It is estimated, however, that about 100 refugees per day have entered the United States, bringing the total, as of the end of August 1980, to just under 121,000. This represents an increase of 7,000 over the 114,000 that came in the spring exodus.

[24] Washington Star, May 24, 1980.

Although some Cuba observers feel that the exodus of those dissatisfied with the Cuban system is yet incomplete [25] it is unlikely that the Cuban Government will attempt to encourage the resumption of a mass migration to Florida at this time.

The United States and Cuba, at present, hold steadfast to their conditions for talks—the United States wants only to address the refugee situation and Cuba wants to discuss the entire range of issues between the two countries, including the U.S. embargo. Although the two nations are exchanging notes, the basic positions have not changed, i.e., the impasse remains. Cuba is adverse to arriving at partial solutions and also understands the effect of electoral politics on U.S.-Cuba relations. From the Carter Administration's perspective it is highly unlikely that officials would be receptive to reaching an accommodation with Cuba, at this time, on those issues that have been obstacles these many years.

The U.S. and Cuban responses to the spate of hijackings by Cuban refugees in August underlines the respective policies of the two governments. In a series of communications, the United States related the immigration issue to the hijacking problem. The Cuban Government specifically was urged to take back those refugees who are dissatisfied with conditions that they found in the United States, as well as those who are ineligible to stay under U.S. immigration law. The Cubans responded that, for various reasons, they would not permit the return of those who left. They also said that the time was not propitious to enter into discussions on all the issues with the United States. The Cuban Government assured the United States, however, that all the hijackers are being placed in prison.

The immigration issue, although the most recent on the U.S.-Cuba agenda, could very well be the catalyst that moves the two nations toward talks, in 1981, on the various items in contention.

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[25] If, as estimated, at least 250,000 people wanted to leave, about 130,000 remain in Cuba with their wish unfulfilled. The figure 250,000 is derived from the fact that 2 percent of the Cuban population voted against the adoption of the Constitution in 1976. It is therefore acknowledged by Cuban Government sources that about 2 percent of Cuba's approximately 10 million is dissatisfied with the Cuban system and would opt to migrate.

CUBA: REVOLUTION PUT TO THE TEST

By Russell Swanson *

As Cuba enters the 1980's, the Castro government faces its most serious economic challenge since the transition from capitalism to socialism in the early 1960's. Revolutionary fervor among both the young and the old is on the wane because of continuing consumer austerity. At the same time, the prospects for dynamic economic development are bleak for at least the next decade. With limits on Soviet aid and the ineffectiveness of traditional palliatives such as income redistribution, the Castro regime—like its Caribbean neighbors—will be hard pressed to obtain the necessary funds to stimulate economic development and to satisfy mounting consumption demands.

Although the dilemma is not an immediate threat to the *political* security of the Castro government, it does set the stage for:

Major systemic economic changes that would overturn the fundamental ideological tenets of the Cuban *economic* revolution.

A serious test of the Cuban-Soviet relationship while Moscow is faced with mounting economic problems of its own.

A shift in U.S.-Cuban relations associated with possibilities of renewed legal and illegal emigration pressures and increased interest by Havana in the normalization of commercial relations.

Economic Slowdown

Cuba's economic performance over the first Five-Year Plan (1976–80) has been unimpressive and has fallen far short of original goals. Drafted against a backdrop of high world sugar prices and guaranteed prices and markets in the U.S.S.R. and Eastern Europe, the Cuban Plan fell victim to: (*a*) the inevitable "boom or bust" world sugar cycle, (*b*) inflation in the developed West that raised import prices, (*c*) an unparalleled series of natural disasters that seriously affected agriculture—the backbone of the economy, (*d*) the inherent inefficiencies of a centrally planned, nonmarket economy, and (*e*) abnormally low labor productivity as a result of declining worker incentives and morale.

Budget.—The economic slowdown is epitomized by the national budget, which encompasses virtually all aspects of the government-owned Cuban economy. After increasing about 10 percent per year between the mid-1960's and the mid-1970's, total government expenditures were planned to increase only 2.7 percent in 1979 and 1.3 percent in 1980 in current terms, a probable decline in real terms. Expenditures in 1980 for economic development declined 1.3 percent while outlays on public health and education increased 16 percent and defense spending increased 3.4 percent. The emphasis on social services at the expense of investment further dampened the already poor growth

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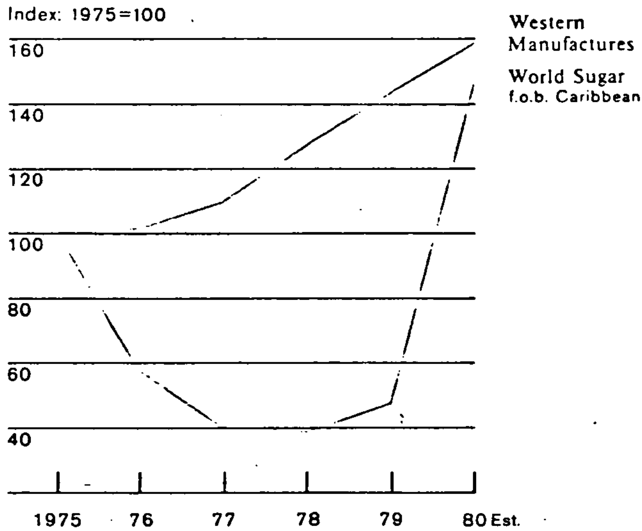
Export Price Indexes



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prospects and, ironically, did little to expand the relatively high quality of health care and education.

Export Crops.—The all-important sugar sector, after steady progress through most of the 1970's, was decimated in 1980 by sugarcane rust that led to a 15-percent decline in output. The mercurial tobacco crop was also devastated by disease, while the fishing industry—heretofore Cuba's major success story—was hit by reduced access to traditional fishing grounds primarily because of strict enforcement of 200-mile economic zones. Even the citrus sector, which received massive investment outlays over the past decade, performed poorly.

Food Crops.—Domestic food production fared slightly better, but output still fell far short of requirements. Production of rice, most pulses, meats, and vegetables were well below target and in some instances declined over the period. On the other hand, rootcrops, dairy products, and poultry and egg production registered gains. The mixed performance reflects continued mismanagement, shortages of imported inputs, and inadequate incentives for the private sector that grows most of Cuba's vegetables. As a result, Havana was forced to spend precious foreign exchange on many commodities that could be grown at home.

Industry—Like the other sectors, industrial performance was mixed. Output in the important nickel industry—Cuba's second largest foreign exchange earner—declined by about 15 percent between

1975 and 1979. Moreover, overly ambitious expansion plans were delayed because of rising imported machinery costs. Production of tires and such important consumer items as shoes and textiles dropped even more drastically or feel far short of plan because of forced cutbacks in imported raw materials. Only in the electricity and petroleum refining sectors—both of which depend totally on imports from the U.S.S.R. and Eastern Europe—did performance live up to plan.

Construction.—Despite some gains, the construction sector in general also was hit hard by material shortages and labor problems. The major shortages of material stemmed from import shortfalls from the U.S.S.R. In the long-ignored housing sector, Cuba was not only unable to meet planned goals but could not even maintain the housing stock at the current levels.

Foreign Payments.—Cuba's experience with the 1976–80 plan underscored Cuban dependence on sugar and the value of Soviet beneficence. During the period, Cuba's hard currency terms of trade deteriorated sharply, reflecting the steep drop in world sugar prices and rapidly rising prices for Western manufactures. Even though Cuba borrowed heavily in Western financial markets—boosting its hard currency debt to an estimated $2.5 billion in 1979—the volume of imports from the West plummeted. A tripling of world sugar prices in 1980 will result in some improvement but will not make up for the previous losses.

Only a massive increase in Soviet assistance prevented a major downturn in domestic economic activity. In 1976–80, Soviet aid in the form of sugar and petroleum price subsidies and project aid has soared over the levels of the previous five years as Moscow sought to meet Cuba's minimum import needs. Moreover, most of the aid was shifted from repayable balance-of-payments and project aid to outright grants. In addition, Moscow purchased 775,000 tons of sugar annually between 1976 and 1979 for hard currency to supplement lagging Cuban earnings in the West. Without Soviet largesse, Cuba would have been forced to cut imports by half.

CUBA—PRODUCTION AND GOALS OF MAJOR PRODUCTS

[In thousands of tons]

	1975	1976	1977	1978	1979	1980	1980 goal
AGRICULTURE							
Export crops:							
Sugar	6,314	6,155	6,485	7,350	7,992	6,800	8,000–8,700
Tobacco	41	51	42	40	33	[1] 20	60
Citrus	182	199	178	198	192	NA	NA
Coffee	17	19	16	13	22	NA	NA
Seafood	143	194	185	213	148	NA	350
Food crops:							
Rice	338	335	334	344	390	NA	600
Milk	591	682	722	783	791	NA	1,000
Pork	43	52	58	61	NA	NA	80
Eggs (million dozen)	154	152	154	160	168	NA	167
INDUSTRY							
Nickel	37	37	37	35	32	[1] 30	100
Electricity (million kilowatt-hours)	6,583	7,191	7,707	8,481	9,391	NA	9,000
Steel	298	250	330	324	328	NA	440
Cement	2,083	2,501	2,656	2,712	2,612	NA	5,000
Textiles (million square meters)	144	139	152	156	150	NA	260
Tires (thousand units)	368	266	172	294	302	NA	NA
Consumer items:							
Refrigerators (thousand units)	50	44	46	46	56	NA	100
Shoes (million pairs)	23	22	15	18	16	NA	35
Radios (thousand units)	113	92	120	121	143	NA	300

[1] Estimated.

Dependence on the U.S.S.R.—Lagging domestic and export growth substantially increased Cuba's dependence on the U.S.S.R. over the 1976-80 period. Havana now depends on Moscow for about two-thirds of its total trade, compared with 45 percent during 1971–75. Soviet aid has soared to the equivalent of $3 billion annually—about one-fourth of estimated Cuban GNP. Given the absence of an alternative benefactor, a major reduction in Soviet aid would force Cuba to (*a*) reduce substantially economic activity and the already austere standard of living, (*b*) default on its hard currency debt to the West, and (*c*) forgo any hope of economic growth over the next several years.

CUBA—FOREIGN TRADE ADJUSTED FOR SOVIET PRICE SUBSIDIES

[Million of U.S. dollars:]

	Annual average						
	1959–70	1971–75	1976	1977	1978	1979	1980 [1]
Exports, f.o.b	668	1,870	3,284	3,677	4,545	4,820	5,608
Less Soviet sugar and nickel subsidies	85	171	995	1,444	2,473	2,302	1,035
Adjusted exports	583	1,699	2,289	2,233	2,072	2,518	4,573
Imports, c.i.f	914	2,177	3,880	4,361	4,732	3,088	5,987
Plus Soviet oil subsidy	0	132	362	328	165	365	1,390
Adjusted imports	914	2,309	4,242	4,689	4,897	5,453	7,377
Trade balance	−246	−307	−596	−684	−187	−268	−379
Adjusted trade balance	−331	−610	−1,953	−2,456	−2,825	−2,935	−2,804

[1] Preliminary.

Prospects for Second Five-Year Plan: More of the Same

The prospects for a major upsurge in economic activity or for a substantial improvement in living standards are equally bleak for the second Five-Year Plan that begins in 1981. Like most LDCs, the Cuban economy suffers from:

An inability to generate adequate domestic investment funds or attract additional foreign funds.

Overdependence on a single export commodity that is subject to mercurial price fluctuations on the world market.

Serious supply constraints because of limited domestic resources and low import capacity.

Moreover, its Marxist-oriented economic strategy lessens Cuba's flexibility to exploit the full range of policy options available to nonsocialist, market-oriented economies, while increasing consumer demands complicate Havana's allocation of scarce resources between investment—the only path to sustained economic growth—and consumption. Fully aware of these constraints and the futility of a Polish-type import-investment policy. Havana has evidently initiated a series of rationalization measures designed to exploit Cuba's human and capital base, while relying even more than before on imports from the U.S.S.R. While this strategy will probably ensure against a major reduction in Cuban economic activity, it is highly unlikely to generate the dynamic development necessary to catapult Cuba from underdevelopment. Although Soviet aid will probably continue to meet Cuba's basic investment and consumption needs, it will fall short of what is required to really boost economic development and living standards. A case in point is Soviet petroleum supplies—three-fourths of Cuba's total energy consumption—which are reportedly scheduled to increase at best only 1.5 percent annually through 1984. Cuba's attempts at economic reform are steps in the right direction, but so far they go only part way to solve the economy's systemic shortcomings. For example, while Havana is establishing the beginnings of decentralization and a minor role for private enterprise, the economic decisionmaking process is still handicapped by over-centralization and nonmarket resource allocation.

In addition, the relatively conservative strategy is not without an element of risk. Such measures as general wage reforms and the firing of unproductive workers could backlash if not accompanied by a perceptible improvement in living standards—a highly unlikely prospect at best. Moreover, although Cuba enjoys guaranteed prices and markets in the U.S.S.R., it is still vulnerable to the volatile world sugar market.

Mounting Consumer Unrest

Against this backdrop, older and younger generation Cubans are beginning to lose their enthusiasm for the revolution and, perhaps, to despair over continued austerity. Although long since inured to deprivation and sacrifice, the Cuban populace, particularly those born and educated under Castro, have become increasingly frustrated over the recent lack of improvement in their Spartan lifestyle. Most of the socioeconomic benefits came in the early years of the revolution through the redistribution of income; additional gains have been slow in coming. The overall per capita availability of foodstuffs has increased slightly, and health and educational services have improved marginally. On the other hand, per capita supplies of clothing and such key staples as sugar, rice, beef, and coffee have declined since the mid-1960's. The housing shortage has gone from bad to worse. In addition, large-scale unemployment has become a real threat for the first time since the Castro takeover in 1959. In sum, the Cuban standard of living does not appear to have changed appreciably over the last five years.

The growing divergence between reality and expectations has been highlighted by:

Direct exposure to Western affluence and consumerism through the visits of 100,000 Cuban exiles since early 1979.

Persistent government warnings that the economic difficulties will continue and that lifestyles will not improve appreciably for another 20 years.

For the most part, popular disaffection has been manifest through a mixture of passive and, to a lesser extent, active protestations. Without adequate material incentives, growing malaise and despair have led to serious declines in labor productivity through deliberate work slowdowns and absenteeism. At the same time, black market activities and other economic crimes have been increasing.

Since mid-1979, emigration has reemerged as a channel for protest. After a hiatus of several years, over 400 Cubans left the island illegally and another 15,000 legally in 1979. In 1980, 127,000 Cubans have opted, with Havana's permission, to leave rather than put up with prolonged hardships. More importantly, an estimated 1–2 million Cubans—10 to

20 percent of the country's population—would follow if given the opportunity.

Implications

Against the seemingly insoluble situation, the Castro government may well be forced to adopt a wide range of actions that could have dramatic domestic repercussions and significant implications for relations with the U.S.S.R. and the United States.

Implications for the Revolution.—The growing ineffectiveness of traditional palliatives sets the stage for major economic reforms that would greatly change the management of the economy. As early as 1972, Castro publicly admitted that the economic revolution had "gone too far, too fast" and that it would have to take a step back for the moment. In retrospect, that was the beginning of a journey that has ranged from selective user charges for previously free utilities and the reduction of some ration allotments, to the recent creation of a limited private agricultural market and the use of an income policy of sorts to stimulate productivity. Wider ranging reforms in the offing include more decentralization of decisionmaking and the right to hire and fire at the plant level. Resort to these, and even more far-reaching reforms under consideration, is rapidly overturning many of the fundamental tenets of the economic revolution. If they continue, as is likely, the economic half of the Cuban revolution may be hardly recognizable when compared with its theoretical goals and operation of only a few years ago.

Implications for Cuban-Soviet Relations.—Although Cuban-Soviet relations are as warm as ever, and Moscow has formally committed itself to underwrite the Cuban revolution for another five years, the potential for problems in the patron-client relationship cannot be dismissed. Moscow has invested enormous amounts of aid and resources in the Cuban economy in return for an increasingly significant geopolitical benefit, but Cuba's appetite and need for Soviet largesse appears never ending. Although the overall burden to the Soviet economy has thus far been slight, the hard currency opportunity costs are skyrocketing at the same time Moscow is experiencing its own growing domestic economic problems and increased demands by East European allies. If these competing demands for limited Soviet resources continue—as is likely—they could seriously test the limits of the Moscow-Havana axis.

Implications for US-Cuban Relations.—The anticipated economic problems could also have a significant impact on the United States. For example, Havana could again seek to defuse internal discontent through large-scale emigration—a tactic employed successfully on three previous occasions in the past 22 years. Castro would probably prefer to negotiate a long-term, orderly departure for some 1–2 million Cubans on the periphery of the revolution, but he is not above threatening a new large-scale exodus to achieve his goal. In addition, growing numbers of Cubans could take it upon themselves to leave illegally and thus escalate bilateral tensions.

Castro, on the other hand, could heighten his efforts to normalize commercial relations with the United States in an effort to ease his economic plight. Although the removal of the trade embargo would provide only minimal short-term benefits and could aggravate internal unrest, Castro may believe that access to the US market could eventually provide the foreign investment needed to stimulate development. The trade and investment opportunities would be relatively small from the US standpoint however, and would not necessarily guarantee a solution to Cuba's economic woes.

THE UNITED STATES AND CANADA: A CHANGING RELATIONSHIP WITH OUR NUMBER ONE TRADING PARTNER

By Edward Nef and Emerson Brown*

SUMMARY

The U.S. and Canada have been by far each other's largest trading partner and undoubtedly will continue as such in the foreseeable future. However, difficulties are appearing which could substantially affect how we do business with Canada: On the one hand, Canada is in the midst of a profound Constitutional crisis, pitting the Federal Government against powerful Provinces. The outcome is of great importance to the United States since it will determine whether the U.S. will have one strong unified nation on its northern border or one nation with highly decentralized powers or in the extreme a number of nations to deal with. Control of economic power is a basic issue. On the other hand, the U.S. is undergoing a period of transformation as it struggles with the problems of low productivity, inflation and unemployment. Since the economies of both countries are so interdependent, the results on each side of the border will have substantial effect on the other.

A special relationship, either formal or informal, has always existed between the two countries. U.S. investments in Canada dominate many sectors, while Canadian investments in the U.S. have grown enormously in the last five years. Trade itself has been relatively free of regulatory mechanism, and there have been occasional experiments with free trade arrangements, such as the auto pact. Current trade relations are guided by international agreements, such as GATT. However, Canadian nationalism, real and/or perceived fears by Canadians of domination by the U.S., and the constant awareness by Canadians of the disparity in size of the two nations make particularly important the current range of bi-lateral issues. The pending Fisheries Agreement, restrictions on the free flow of investments, provincial and state incentives, energy problems and the use of tax powers to limit cross-border commerce are among those in the fore.

The changes which are occurring and the issues which continue to create problems may compel some re-thinking on the part of both countries to shape a better trading relationship in line with the realities of today's world.

INTRODUCTION

Take two countries with free and open political institutions, high standards of public administration, strikingly similar cultural, reli-

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gious and social values and demographic origins and traditions, where free enterprise, hard-working people, abundant resources and accommodating climates have enabled them to create, in conventional monetary terms, the world's first and seventh economies. Place them alongside each other on three-quarters of the world's most salubrious continent. Give the relationship a special sense of challenge by making their proportions in human and econometric terms, roughly that of 1 to 10, and by running the main east-west border so far north that one partner has later springs, shorter summers and earlier, longer and more severe winters, with all that implies for agriculture. There you have Canada and the United States, joint holders of all kinds of records for harmonious and mutually advantageous national coexistence. The citizenry of both countries know, without thinking about it very much, that the other is the best possible national neighbor.

Unmarred since 1815 by armed conflict, the relationship in this century has seen the countries allied in two world wars, and joint defenders under UN aegis of South Korea against the 1951 North Korean invasion. They are partners in NATO, and share membership in the United Nations and many of its family of international organizations. They cooperated closely during the post-World War II era of dollar shortages. Though Canada's official doubts about U.S. participation in the Viet Nam conflict antedated the anti-war movement in the United States, it is a curious fact that the numbers of Canadians who enlisted in the U.S. forces to fight in Viet Nam, and of Americans who fled to Canada to avoid military service, were about equal. The "special relationship" between the United States and Canadian Governments may have ended with the Nixon economic measures of 1971, but the more profound relationship that the two populations enjoy—in which each recognizes the other as not domestic, but somehow also not altogether foreign—endures.

The volume of trade—in 1979 about $71 billion combined exports and imports—is enormous, even after setting aside the special free trade in automotive products ($22 billion exports and imports combined in 1979). Each country is a principal foreign investor in the other and this corporate approach to economic integration, on a scale that has aroused misgivings in Canada, and increasingly in the United States as well, is a considerable force. Cooperation on energy matters yields direct benefits to both countries: both governments are cooperating to support the private Alaska Gas Pipeline project, and to facilitate the swap of 150,000 barrels of oil daily, replacing Canadian oil delivered to Northern Tier states with off-shore oil, to save pipeline costs.

Until recently, the principal current bilateral issue from the Canadian perspective concerned the East Coast Fisheries Agreement and Boundary Treaty, signed March 29, 1979, which was meeting opposition in the U.S. Senate. Other important recent problems were: Canadian treatment of advertising expenses for income tax purposes, which has deprived U.S. broadcasters along the border of an estimated $15 million in annual receipts, and the U.S. measure adopted in retaliation (but recently mitigated), restricting the deductibility for income tax of expenses in attending conventions held abroad; governmental efforts to influence the flow of investments across the border; and recent strongly nationalistic Canadian energy policies designed to "Canadianize" the industry. Environmental problems, such as acid rain, are always present also.

Nevertheless, events of potentially substantial significance are occurring which both countries must take into consideration if the relationship is to stay on an even keel. On the one hand, Canada is engrossed in an internal constitutional struggle, the outcome of which will determine the future powers of a central federal government vis-a-vis powers of provincial governments. What happens will inevitably affect how the U.S./Canada relationship develops in the future.

On the other hand, the U.S. is slowly awakening to the realities of its changed position in the world. It is searching for ways to help U.S. industry and may consider measures which could have profound effect on relations with other nations.

Even though the basic relationship is so extensive and interdependent that it undoubtedly will continue to prosper, these current developments in Canada and the U.S. must be recognized by leaders in both countries. This paper describes and analyzes both the changes that are occurring and the bedrock that underlies the relationship.

Canada's Constitutional Crisis

On May 20, 1980, Quebec voted in a provincial referendum to determine whether its separatist Premier, Rene Levesque, should undertake negotiations with the Canadian Government leading potentially to an independent Quebec. The resounding vote against Levesque dashed the dreams of many of the Province's French speaking population. French Quebeckers obviously were unhappy over their position within the Federation, and felt that Quebec had been treated too long as a poor relation, but the majority was not yet prepared to split from the center.

In leading the opposition at the Federal level, Prime Minister Pierre Trudeau promised that the Federal Government and the 10 provincial governments would negotiate a new relationship between themselves if Levesque were defeated. The three major areas for negotiation are social, cultural and economic. The economic relationship in particular presents the nation with complex constitutional questions, since the provinces currently have substantial control over natural resources.

Alberta is the wealthiest Canadian province in natural resources, with 90 percent of Canada's oil and an abundance of gas and coal. Premier Peter Lougheed has made clear his opposition to control over these resources by a distant central government. Indeed, he would prefer to see even more economic power in the provinces. His allies, in varying degrees, are the premiers of the maritime provinces, conscious of the natural resources off their coasts, and the other western premiers. Quebec shares the desire to limit Federal power, particularly in the social and cultural areas.

Prime Minister Trudeau, thus, is entering a difficult period. As a strong Federalist, he is determined to work out a new deal with the provinces, but is reluctant to cede economic power and in fact would prefer to increase federal authority. Key to his effort is the "patriation" of Canada's Constitution, the British North America Act, which is an act of the British Parliament. While all may agree that it is an anomaly to have one nation's Constitution reside in another country's Parliament, bringing it to Canada raises many possibilities for change, such as the amending procedure, which the provinces oppose. The outcome is uncertain; failure to work out a new deal could very quickly rekindle the separatist movement in Quebec and extend it to the West, where feelings of alienation are strong. Conservative Party domination in the west and Liberal Party prominence in the east add to the differences.

A greater degree of regional autonomy in itself may not make all that much difference, to the United States, and it may even be welcomed by regional interests in the U.S. (for example, our northwestern states on occasion may feel a greater affinity for Canada's western provinces than they do for Washington, D.C. or the eastern seaboard states), but genuine balkanization or disintegration of Canada would be real cause for concern. Having three or four countries, possibly of widely divergent political and economic status and viewpoints, on the northern border would create new problems and tensions for the United States.

Fortunately, the bonds of friendship between the people of the United States and the people of Canada appear to be growing stronger, if public opinion polls are any measure. A 1980 Canadian Gallup poll showed that 79 percent of the Canadian population now thinks that the U.S. is its best friend, compared to 58 percent 15 years ago. Another poll indicated that 67 percent of Canadians think closer trade relations with the United States are worth pursuing. An extreme case, but interesting for its occurrence, is the 1980 split in the Conservative Party in Saskatchewan which saw several of its leading members declare support for a policy of Canadian unification with the United States. Of course, polls can change rapidly, and there are many who work diligently to try to reverse such trends. In a time of crisis, such as exists currently over the constitution and Federal/Provincial relations, an effort might be made to encourage anti-Americanism, or at least not discourage it. Canadian nationalism has always been a powerful force.

The "Special Relationship" Between Canada and the United States

Over a hundred years ago Sir John A. MacDonald, father of Modern Canada, set his country on a course of protectionism and links to Britain, and economic independence from the United States. Despite these protectionist policies, a geography neither nation can command made each the other's very best customer. After World War II, when Britain took the initiative to reduce its colonial ties, and in time looked to Europe rather than to its Commonwealth of former colonies, Canada began to deviate from its historic trade policy and to participate in the world-wide effort to reduce trade barriers. Today seventy percent of Canadian exports and imports are either destined to or come from the United States. Twenty percent of all U.S. exports are to Canada, and 20 percent of all U.S. imports are from Canada. Trade between the two countries totalled $71 billion in 1979, more than between any other two countries in the world. In the post World War II era of cooperation, a "special relationship" evolved that seemed in both countries' best interests.

In a May 1979 speech at Stanford, however, U.S. Ambassador Enders affirmed the death certificate for the official special relationship that for the post-war years was accepted, on both sides of the border, as a basic characteristic of Canada-U.S. economic relations. The affirmation of its expiry certainly is accurate as applied to a formal aspect of the intergovernmental relationship. In earlier instances—oil import quotas in the 1950's, and capital controls in the 1960's are examples—when Canadian authorities were surprised and shocked by the U.S. moves, high-powered delegations promptly went to Washington to make the case for exceptional treatment for Canada. Typically, Washington then recognized that in coping with international aspects of an economic problem it had indeed failed to take due account of the closeness and importance of the Canadian connection—and of the domestic U.S. interests directly involved. As a result, exceptions were made for Canada, and if international agreements were in play both countries' legal experts went to work on justifications, or at least rationalizations, for the exceptions. This pattern was broken in 1971 when the United States, in severing the last formal connection between the dollar and gold, imposed an import surcharge intended to help cure large trade deficits. After overcoming their shock—and disbelief that the failure to except Canada could have been deliberate—and choosing not to be satisfied by the fact that the surcharge, which did not apply to duty-free imports, affected Canada less than any other major trading partner, the Canadian government reacted by enacting an export industry assistance program intended to offset any effect the surcharge might have.

This now-defunct special relationship was determined by factors largely beyond government control. It existed at a time when general economic conditions were developing favorably and looked like they would continue to do so; its uniqueness merits careful attention. First it was supported by a corps of officials in both countries who had expert technical knowledge of the subjects at issue, a grasp of their broader implications, and a sound sense of the political reality of the day—of the substantive and procedural implications of a proposed course of action. In most cases there were close personal relations between officials who had known each other for years. Second, this group of officials had the confidence and strong backing of their political masters. And third, in neither nation did an inquiring press, or doubts about infallibility of governments, exist to the degree now current.

The More Profound Special Relation

Granted that the format special relationship has ended, it is important to remember that it had been superimposed on a basic social and economic relationship determined by geographic, and even geologic, conditions that endure, and fostered by institutional arrangements rooted in both countries' domestic law and bilateral and multilateral agreements that also endure.

All bilateral relationships are special, but some are more special than others. Canada and the United States meet this "special" definition better than other pairs of independent nations. The most important factors are these:

Geography: More than 4,000 miles of arms-free border, territories of continental dimension, with strikingly similar diversity of regions.

History: Contemporary modern histories that both stem from the great age of European exploration and colonization; similar stages of national economic and territorial development.

Common religious, cultural, social and ethnic heritages—even extending to the French connection (Quebec and Louisiana).

The two countries share a respect for law based on responsible consent and due process; a regard for personal civil liberties and civic responsibility; mixed economic systems in which market forces sooner or later make themselves felt; and high standards of affluence and welfare. No other pair of nations share such conditions on such scale or with such intensity.

The result, happy or not depending on one's point of view, is that Canadians and Americans who cross the border experience little sense of "foreignness". Each has in the other country a feeling more of order and security and familiarity than alienation. This in turn has made the relationship very much a person-to-person matter and given it a stability and constancy on which neither Washington nor Ottawa can have much direct effect, even if they want to.

There are, of course, salient differences between the two countries, which Americans in particular must take into account:

The American nation is the result of a revolution confirmed by a second armed conflict with the mother country, and a civil war whose gore cemented the Union. Canada remained loyal to the Crown, gained dominion status by an act (British North America Act, 1867) of the British Parliament, and in 1926 attained its present status of an autonomous community within the British Empire, united with the other members of the British Commonwealth of Nations by allegiance to the Crown. The last limitation on Canada's legislative autonomy was not removed until 1931! The heroic and bloody attainment of American nationhood contrasts starkly with Canada's reasonable and expedient evolution as a nation, and to this day colors national attitudes in each country.

In Canada the competing claims of central and provincial governments to the prerogatives of authority are not as clearly defined as in analogous instances in the United States and result in the difficulties Canada is currently undergoing.

There is much greater willingness on the part of Canadians to allow their government to involve itself in their economy. Air Canada and Petrocanada are only two examples of government corporations playing major roles in the Canadian economy. While Americans prefer less government, Canadians prefer more; the third largest party in Canada is the socialist party.

Canada's version of the parliamentary system has important practical ramifications: a lesser role for the Supreme Court than in the United States; the absence of executive-legislature conflict which the parliamentary system automatically assures; national elections at least every five years with campaigns limited to six weeks.

Finally, the most obvious difference between the two nations is size—population, economy, military strength.

These and other significant differences that help make up the national consciousness in each country do not automatically complicate or harm bilateral relations, but they can lead to misapprehensions or misunderstandings that do. Simply because the general level of ignorance about and unawareness of the other country is so much greater in the United States, Americans bear a special obligation not to let superficial considerations distort their view of Canada. At the same time, in perhaps a more subtle way, Americans dealing with Canadians do well to appreciate that the latter as a rule are very knowledgeable about U.S. interests and institutions and decision pressure-points and—such is the way of the world—are not above using this knowledge. Canadian nationalists are particularly adept at this, playing on Canadian fears and exploiting what has been described as the U.S.'s "benign ignorance" of Canada.

Given the huge volume of trade between the U.S. and Canada, it is interesting that it has developed for the most part without regulatory mechanisms or permanent structures. At one point, after World War II, the Governments set up a consultative group on the Ministerial level, but it has not endured. Ministers had little time or interest to maintain such contact on a routine basis. There was no strong supportive structure to continue work between meetings, and since there did not seem to be any master plan guiding the Ministers which gave them specific goals to work towards, the system withered. Trade developments did not change that rapidly or that much, and more routine trade and economic matters could be handled perfectly well by the bureaucracies without need of more than occasional highest level oversight.

Mechanisms such as the International Joint Commission, which under the terms of the 1909 Boundary Waters Treaty could easily have its activities expanded to take on economic issues, have not been used either. The IJC does have large powers in some technical areas which have profound economic consequences, such as regulation of water levels and flows, but it has never been seriously considered as an arbiter, planner or manager of U.S.-Canadian trade relations.

Rather, the preference has been to use multilateral strategies as much as possible.

Canada and the United States are founding members of the trade and payments system created after World War II by the General Agreement on Tariffs and Trade (GATT) and the Articles of Agreement of the International Monetary Fund (IMF). These instruments embody, as an ideal, a regime in which customs duties, applied on a uniform, most-favored-nation basis to the goods of other participating countries, are the only governmental barrier to imports, in which such barriers are to be reduced if not eliminated, and in which currency practices are not to be used to restrict or subsidize international trade.

The latest Tokyo round of GATT negotiations saw the U.S. and

Canada agree to substantial reductions in tariff barriers between the two countries, so much so that it is estimated that 90 percent of goods traded between the two countries will eventually be free of any tariff barriers. The Tokyo round also resulted in a significant reduction in disparity between currently high Canadian duties and relatively low U.S. tariffs. Canadian rates, which are in excess of 15 percent, will be gradually reduced by an average of 43 percent, to approximately nine percent. After implementation, Canadian duties on all United States imports will average about six percent and United States duties on Canadian industrial goods, a token less than one percent. There were particularly significant gains for U.S. exports in such sectors as machinery, paper, chemicals, wood products and computers. More stubborn problems continue in the area of textiles, footwear, and rail cars. Buy Canadian and Buy American laws also remain stumbling blocks, and government subsidies on both sides of the border continue to irritate the other partner.

Both countries are parties to the many multilateral agreements which govern so much of the world's economic and trade affairs such as GATT, Intelsat, and the OECD. The U.S. and Canada have been satisfied that the multilateral framework provides opportunity for mutual growth of trade while assuring a degree of economic independence.

When multilateral strategies have proven inadequate, however, both countries have been willing to try new ideas and to negotiate new arrangements. The two most important areas are in the automobile industry and in defense production: the Auto Pact, negotiated in 1965, and the Defense Production Sharing Agreement, negotiated in 1959. These are noteworthy developments and will be scrutinized more closely further on; suffice it to say at this point that both represented the negotiation of a free trade zone within the industries affected, and resulted in an expansion of trade and employment in both countries.

There have been occasional, more ambitious forays into free trade between the the two countries, but these have generally proven fruitless. In the mid-nineteenth century, there was talk of such a development, and just prior to World War I, the Liberal Government made it the theme of the 1911 elections and lost resoundingly. Instead, Canada turned to the mother country, Great Britain, and her Imperial Preference System. The move was hastened even more in the 1930's after the U.S. passed the Smoot-Hawley tariff, and world trade collapsed.

A curious side-light to history occurred in 1948, when secret negotiations between the U.S. and Canada led to a draft treaty establishing free trade between the two countries. Presumably, Canada at that time saw its former benefactor and protector in Europe, Great Britain, exhausted by the war and considered its future as best linked to its southern neighbor. Negotiations were carried out, but when the draft was presented to then Prime Minister MacKenzie King, he rejected it. An opportunity for a genuine free trade area between the two countries passed.

Canadian Betes Noires

Canadian perceptions are subject to special sensitivities. A particular example is "continentalism," a term that in one form or another recurs south of the border in a U.S.-Canadian, and sometimes U.S.-Canadian-Mexican, context. The Canadian aversion to proposals of this nature stems from the almost invariable fact that, however cosmic the packaging, Canadians perceive the objective as improving U.S. access to a particular Canadian resource. Of course, Canadians do not regard with similar aversion a continentalism which makes U.S. markets fully accessible for Canadian manufacturers. For Canada, the *ad hoc* approach, working out arrangements over the years for developing natural resources and exporting them to the United States—and if possible elsewhere—has been preferred.

What might be called "hemispherism" is another concept which finds hard sledding north of the border. Americans concerned with the Western Hemisphere's welfare are naturally attracted by the idea of drawing Canada into the regional arrangements that have evolved. The fact that an American president voiced this thought before the Canadian Parliament probably was enough to seal its doom. Canada has established observer status with the Organization of American States, and continues to extend bilateral aid to selected American countries, but is satisfied to limit its participation in general multilateral political entities to the United Nations and the Commonwealth. Physical distance, the virtual absence of cultural ties, a feeling that participation would take place in the U.S. shadow, and the absence of any compelling political or economic interest, make closer Canadian involvement in hemisphere institutions unlikely. Discounted is the American suspicion that Canada avoids any of the difficulties of involvement in hemispheric problems, while reaping the benefits of trade and economic relations.

Finally, U.S. access to the vast Canadian supply of fresh water is a subject apparently pointless to take up seriously with Canadians. Few of them believe that such a vital resource should be exported, and all of them understand that, whatever assurances to the contrary might be given, an agreement to export water as a practical matter would not be reversible. Even if they had not already made up their minds, their observation of the domestic controversy in the United States about interstate water diversion projects would have brought them to this view. Arguments that since Canada survives the winter by eating California fruits and vegetables, it should help "water the garden" fall on deaf ears. Yet export of food to Canada is a policy equally unlikely to be reversed.

Elephant and Mouse?

Canadians with a taste for hyperbole have compared the United States and Canada in terms of an elephant and a mouse. Prime Minister Trudeau has employed the elephant reference, without specifying an animal to represent Canada. Canadian nationalists are particularly fond of the comparison.

There is no gainsaying the proportion of the relationship as measured by population or gross national product, but its relevance depends on the specific issue. At one extreme, the difference in size has nothing direct to do with the rights or wrongs of a basic tenet of trade policy, or a boundary or conservation matter. In the middle range, the direct U.S. and Canadian interests in play are of much the same absolute order of magnitude—with respect, for example, to wheat and feedgrains, nickel, aluminum and forest products trade problems and issues. In the general economic policy area, however, relative size is indeed important. The direction, tempo and amplitude of developments in the U.S. economy exert strong influences on Canada, whereas the converse is usually at most only of regional importance in the United States. Canadians responsible for managing the levers that are supposed to affect the nation's economic performance may be forgiven for thinking that life is unfair when they are confronted with economic conditions generated predominantly south of the border. This has been the case since the mid-1960's, when the excellent U.S. record of stable growth registered over the previous two decades was altered. However, no nation in the world is immune from larger economic trends, and while Canadians may wish to lessen dependence on the U.S., it is hard to believe any other major trading bloc will give it greater stability. At times, Canada is perceived by U.S. critics as seeking all the benefits of economic association while assuming as few obligations as possible.

Finally, the size discrepancy can and often does have important ramifications in specific cases because it means that the matter at issue is generally more important to Canada than to the United States. However, Canada also utilizes the analogy to its full advantage when seeking U.S. understanding, and does not like to be reminded that in some sectors, at least, Americans could be forgiven for thinking the analogy exists in reverse. For example, it has been estimated that seventy percent of U.S. southern agriculture is fertilized by Canadian potash, a rather envious position for a "mouse." Similarly, Canada's energy position is the envy of the U.S., and the "mouse" roared when it reduced oil exports to the U.S.

Issues, Problems and Conflicts

Fisheries

Until recently, fisheries (and boundary matters) headed the agenda of bilateral issues. This was by Canadian determination since the Canadians decided to make it a national issue. The U.S. regarded it as a regional issue.

Fisheries and the inextricably related boundary matters have been a problem between Canada and the United States since the early days of the Republic, and treaties to deal with them go back to the *Convention respecting fisheries, boundary and the restoration of slaves* signed at London, October 20, 1818.

As the treaty record attests, Canadian and American fishermen for almost two centuries have created problems for each other. Their direct interest in conservation and perhaps a basic common decency permitted the development of a structure of fisheries agreements that both sides—with a few lapses—respected. In recent years, however, the acceptance of a 200-mile limit for territorial fisheries, and sanction for this concept in the continuing Law of the Seas Conference—and the possible presence of oil and gas deposits off the coast of New England and the Maritime Provinces gave new importance to definitive delineation of the off-shore boundary.

Thus, after long negotiations, on March 29, 1979, representatives of the two countries signed agreements concerning Pacific and Atlantic coast fisheries, and a treaty on the resolution of the disputed maritime boundary in the Gulf of Maine. The technical details of the agreements, and the rationale that underlay the U.S. negotiating position, appear in an address by Thomas R. Pickering, Assistant Secretary of State for Oceans and International Environmental and Scientific Affairs before the Oceans Policy Forum at Washington, D.C., on April 5, 1979 (published in the State Department Bulletin for June 1979).

The East Coast fisheries agreement was to become operative with the entry into effect of the boundary settlement treaty, and both required Senate ratification. U.S. fishermen, particularly East Coast scallopmen, considered the agreement unfair to them, however, and succeeded in enlisting enough support in the Senate to place it in jeopardy.

The Canadian position is that the agreement was negotiated in good faith over a period of almost two years, and that the duly authorized U.S. negotiators in accepting its provisions must have considered it to be fair. However, Canadians reluctantly agreed when President Reagan decided to separate the two and obtain Senate confirmation on the boundary treaty alone.

Money Markets, Financial Institutions and Investment Patterns

Financial integration of money markets is particularly close and important to the two countries. This is inevitable given the large amounts of money required by Canada to develop her resources. The latest manifestation of this need has been the expensive pipeline projects to bring Alaskan and Canadian North Slope oil and gas to lower Canada and the 48 contiguous states of the Union.

According to Canadian securities dealers, who understandably want to encourage the Canadian Government to promote investment by increasing tax incentives. Canada's total investment requirements will be on the order of $100 billion a year for the next 10 years. The role of the private investor will have to be expanded, since about $25 billion is expected to come from the securities market.

In addition, U.S.-controlled Canadian companies will account for an estimated 42.8 percent of the $9.07 billion in capital spending by manufacturing industries in 1980, according to *Statistics Canada*. This is 44.8 percent above last year's figure. Domestically controlled companies will contribute 47.9 percent while other foreign companies will account for the remainder. Much of this increase is expected to go to mining and oil industries as well as the transportation equipment manufacturing sector.[1]

Most of the long term Canadian borrowing abroad is done by Provinces and corporations. The former are particularly active in the New York capital market. Some of this borrowing may have accounted for the strength of the Canadian dollar in the mid-1970's. Foreign money flowed freely and in large quantities into Canada; astute observers at that time predicted that the inevitable consequence of such large bor-

[1] The Washington Post, June 12, 1980.

rowings would someday be a rapid slide in the value of the Canadian dollar, and indeed in a period of about a year, beginning in 1977, the Canadian dollar fell from $1.03 U.S. to $0.86 U.S., as a result of two distinct but perhaps not un-related developments: (1) capital flight stimulated by the uncertainties generated by the threat of Quebec separation, and (2) the huge increase in Canadian investments in the United States. Canadian corporations were and are being drawn in significant numbers by the promise of large profits to be made here and, more importantly, because they presumably wish to have secure access to the huge U.S. market. Canada, in fact, has become the second or third largest investor in the United States, trailing only Holland and possibly England (Canada has more than $6.2 billion in known direct investments in the U.S., the Netherlands $9.8 billion and Britain $7.4 billion). However, these figures may be suspect, since accounting procedures, corporate fronts in Europe and elsewhere and unreported private investments, often under-estimated, could balloon the total of Canadian investments in the United States to close to $20 billion. The $6.2 billion figure represents a doubling of such investments between 1970 and 1978.[2]

In some U.S. sectors, such as metals and machine manufacturing, Canadian investment has always been first among foreigners. In food, insurance and petroleum. Canada ranks a strong third or second. Canadian investments in the United States, on a per capita basis, are larger than similar investment by Americans in Canada. And not included in such figures are investments such as real estate, which has long attracted great Canadian interest. Finally, an interesting phenomenon has been the increasing transfer of Canadian-owned assets to third country subsidiaries. This results in lower taxes and other advantages; it helps make more difficult the identification of Canada's increasingly large role in the U.S. economy, even in such sensitive areas as cable TV stations.

The role of Canadian banks has also attracted attention in the United States. Not too long ago, Brascan Ltd. of Toronto attempted to take over F. W. Woolworth, the American five and dime chain. Americans were surprised by such a bold move aimed at a major U.S. concern and even more surprised to learn as a result of the proceedings that the world-wide banker to F. W. Woolworth was not one of the large New York banks, but rather a Canadian institution. More recent take-over attempts by Canadians have made the Brascan effort seem relatively minor.

Canadians, on the other hand, were not at all surprised. The size of Canadian banks is impressive indeed. Canada has only a dozen or so chartered banks throughout the nation, making it relatively simple to finance large deals (and take-overs) without needing to form any consortia. Among the top 45 banks of the world, three are Canadian.

Canadian banking legislation is certainly very favorable to the industry. Banks essentially can engage in any activity not specifically prohibited to them. Canada regularly revises its banking laws, and tries to enlarge the number of banks to bring more competition to the banking scene. Canadian banking competes formidably in cross

[2] N.Y. Times—Business Day, Nov. 8, 1979.

border investment activities, and has advantages which are difficult to counter without substantial restructuring of banking laws in both countries.

Finally, but perhaps the most important bilateral issue from the American perspective is operation of Canada's Foreign Investment Review Act, which makes foreign investment in Canada subject to official approval. This was enacted in 1974, symbolic of Canadian sensitivities in this area, and designed (or at least so thought many American investors) primarily to limit U.S. investment in Canada, while posing less of an obstacle to investment from other countries.

In fact, while the enactment of such legislation must have some deterring effect on prospective investment, the basic economic and business factors that determine investment decisions, and the Canadian tradition for scrupulously fair law enforcement, seem to have worked to keep the legislation from having more than marginal influence or being anti-American. However, it has still caused misgivings on the part of many *bona fide* U.S. investors interested in Canada and remains one major issue between the two governments. This is particularly so as the present Canadian government indicates a desire to strengthen the operations of FIRA.

One aspect of U.S.-Canadian trade peculiar to the two countries is the great importance of state/provincial restraints, subsidies or laws. GATT agreements by federal governments may be binding on federal governments; yet, it is Ontario (working with the federal government) which seeks to lure Ford investments into that Province, and it is Pennsylvania which undertakes similar investment incentives to assure that Volkswagen selects that state as the site for its North American *Rabbit* plant.

A further complication is the difference between the U.S. and Canada regarding industrial development incentives. Both the Canadian federal government and provincial governments provide such incentives. The Canadian Federal Government operates regional development activities to achieve balanced growth in addition to more general incentive programs; the U.S. Federal Government operates programs aimed mostly at growth of lagging economic areas. Finally, in the Ford case cited above, the Canadian Government offered outright cash, an attractive factor for the manufacturer at a time when cash flow might have been important.

A recent study of the Canada/Ford deal concluded that the most "important implication of the Canada/Ford deal is its potential impact on the incentives policies of Governments at all levels . . . if this stepped up incentive activity is incorporated in the development policies of all governments, a serious policy problem would assume even larger proportions . . . . The solution . . . is far from clear. When fiscal authority is decentralized, no unit of government can afford to ignore the incentive actions of other governments. Nor can any government be faulted for using available tools to pursue its development objectives". [3]

U.S. states provide incentives which are just as great; in fact, the incentives offered to Volkswagen by Pennsylvania totalled 19.6 percent of total investment (the Canada/Ford deal totalled 12.7 percent).

[3] *The Canada-Ford Deal: A Case Study in Government Business Incentives*, Northeast-Midwest Institute, October 1978.

The point is that states, provinces, and various combinations of those two with their federal governments work energetically to lure investments from one area to another. Such artificial incentives distort trade and complicate substantially the relationship between the two countries. In both countries, the local entity is a key factor, and is not effectively controlled by the federal government.

Taxes can be just as effective in limiting a relationship. The existence of free trade arrangements, the removal of all tariffs, and other arrangements to encourage trade can be over-ridden by tax policy.

This was very effectively shown in the continuing disagreement between the U.S. and Canada over convention taxes and border broadcasting advertising. Several years ago, in an effort to foster the production of domestic television programs and to assist the development of a Canadian weekly news magazine. Canada used its tax powers to make it too expensive for Canadian advertisers to advertise in "foreign" media. The effect was substantial on U.S. border broadcasting stations which derived much revenue from Canadian advertisers who bought time on programs which were beamed back into Canada. U.S. broadcasters, particularly in the Buffalo area (whose programs are regularly picked up by the very large Toronto market), claimed their advertising revenue dropped substantially and complained strenuously to the U.S. Government, which in turn took up the issue with the Canadian Government with absolutely no effect.

In what the Canadians viewed as a retaliatory measure, the U.S. altered its tax laws to make it more difficult for U.S. taxpayers to deduct convention expenses if those expenses were incurred in Canada (and Mexico). The result was that the very profitable tourism/convention trade in such cities as Toronto and Montreal nosedived. They in turn sought assistance from the Canadian Government, but it in its turn failed to budge the U.S. Government (although a new tax treaty negotiated between the two countries could alleviate the problem). The U.S. Senate appeared disinclined to revise the tax provision.[4]

From a strictly economic point of view, the Canadian action did not make much sense. Canada lives far more by its exports than does the U.S., and a spin-off effect of the law, naturally, made it more difficult and expensive for Canadian exporters to advertise their wares abroad. From a trade point of view, Canada should probably have reduced the taxes, rather than raise them for export advertisers.

But the decision was clearly not based on economics. It was based on a desire to develop a Canadian identity separate from the United States; additional advertising revenues accruing to Canadian TV stations, for example, made it more profitable for them to operate and presumably to show Canadian programs, rather than U.S. imports. For a country so close to the U.S. and so overwhelmed by the constant bombardment of U.S. culture, good or bad, the motivation is understandable and one the U.S. could be more sensitive to. On the other hand, it could be argued that the law did little other than to make things more expensive for advertisers and TV stations; the passage of time has seen Canadian advertising rates rise to the point where soon simple economics will make advertising in the U.S. by Canadian

[4] In the closing days of the 96th Congress, the Senate did act to mitigate the problem.

advertising companies feasible and competitive again. Nor have TV stations suddenly become exciting programmers of Canadian culture. Similarly, since the Canadian law also was designed to drive *Time Canada* out of business, it should be noted that *Time* closed its Canadian edition and is now apparently selling its U.S. edition even more profitably throughout Canada. It is true that the Canadian news magazine *Macleans* has been able to develop into a weekly, but given the continued success and circulation of *Time* it probably would have done so without the tax law. It had a good Canadian product to sell and Canadians have bought it. Conversely, the U.S. tax law making it more difficult for conventions to take place in Canada did little other than deliver a retaliatory message and arouse the ire of Canadians and many U.S. conventioneers and tourists.

The Auto Pact

Now in its second decade, the auto pact—the *Agreement concerning automotive products* signed at Johnson City, Texas, January 16, 1965—is a free trade arrangement between Canada and the United States which has rarely lacked criticism from labor leaders, civil servants, politicians and other quarters with a more or less legitimate interest in it. It has survived, partly because the locus of criticism has moved back and forth across the border in close harmony with the trade deficit, and partly because of the considerations that led to its negotiation in the first place.

Before 1965, when the agreement was signed, Canada's automobile industry depended on high tariff protection for its existence. Various proposals were made for development of a more efficient industry; the one that found most favor proposed the remission of customs duties as an incentive to increase "Canadian content"—a practice that risked retaliatory measures from the United States. Recognizing this, Canadian officials suggested that the two governments look for a better solution to the Canadian problem. The agreement that resulted sets forth three objectives:

> Creation of a broader market for automotive products, within which the full benefits of specialization and large-scale production can be achieved;
>
> Liberalization of trade barriers to enable the industries of both countries to participate on a fair and equitable basis in the expanding total market; and
>
> Development of conditions in which market forces may operate effectively to attain the most economic pattern of investment, production and trade.

Each government undertook to avoid actions frustrating the achievement of these objectives, and termination could take place on 12 months' notice. The United States acknowledged that implementation of the agreement would contravene GATT's most-favored-nation provision, and sought and obtained a GATT waiver to permit application of the agreement only to trade with Canada. On its part, Canada took the position that its participation in the agreement did not contravene GATT, because of the nature of the customs duty regime in effect when Canada agreed to the provisional application of

GATT's terms. The discrepancy between the U.S. and Canadian positions was not pursued, in large part because in the mid-1960's the North American automobile was a very special vehicle. Because both countries pursued an import policy vis-a-vis third-country automobiles that was quite liberal compared with those of other western, industrial countries, to the point where imports from overseas now have some 25 percent of the North American market, the agreement's status remains unchallenged.

In agreeing to the arrangement, the United States recognized Canada's need for a transitional period to enable the Canadian sector of the industry to adapt to the new regime. The pressure that has continued in Canada, long after expiry of the transitional period, to require the industry to meet investment and employment targets, and to carry out in Canada an appropriate proportion of research and development activities, and of the more sophisticated manufacturing operations, has been tolerable for the United States only because the trade balance under the agreement has generally been favorable. An associated problem has been Canada's resort to duty remission schemes to attract investment by non-North American automobile companies, and to outright grants to induce North American companies to site new facilities in Canada rather than the United States, described earlier.

The development of trade under the agreement has been impressive. In 1964, the year before the pact took effect, the two-way trade in automotive products was about $700 million. By 1976, the two-way trade amounted to $17 billion, in 1978 it was $21.2 billion and in 1979, $21.8 billion.

The Pact has been of great benefit to both countries. Canada has gained substantially in terms of increased employment and in lower consumer prices for cars; the U.S. has benefited since the trade balance over the years (particularly since 1974) has tended to be in the U.S. favor. Canadians claim the U.S. surplus rose from $0.4 billion in 1973 to $1.8 billion in 1975 and $3 billion in 1979. Canadians are concerned that if current trends continue, the Canadian deficit would reach staggering proportions in the next few years.

These have not been the only concerns. U.S. labor unions have always been skittish about jobs lost to Canada. On their part, Canadians have shown recent unhappiness over the lack of investment in research and development in Canada. The lucrative parts trade occurs mostly in the U.S. while many Canadian plants are producing the larger cars which are now selling less well. While the entire industry is faced with the same problem, Canada thinks that it bears an unfair proportion of the burden. It is worth noting that Prime Minister Trudeau, during Canada's recent national elections, called for another review of the Auto Pact, which has already begun.

The Auto Pact had a precursor in the Defense Production Sharing Agreement, which came into being in 1959. As long ago as 1941 Canada had earned dollars by producing arms and equipment for the U.S. military. The 1959 agreement led to substantial U.S. purchases of military equipment in Canada. Here too, however, Canada has been considering whether the benefits of the agreement warrant its continuation under present terms—criticism in Canada centers on undue reliance on U.S. technology, and the effect thereof on innovation, research and development in Canada.

Energy

As noted in another chapter, "Western Hemisphere Oil and Gas, No Relief for the United States in the 1980's," Canada is now a net importer of oil. Gradual exploitation of its tar sands is not likely to change that position over the next decade. Canadian exports of natural gas to the United States, however, are likely to increase over the coming decade—at the outside by an amount equal to 500,000 barrels per day oil equivalent. Nevertheless, actual and potential Canadian sources of energy are important to world energy supply and demand, and are a major issue in U.S.-Canadian relations.

U.S.-Canadian trade in oil, gas, coal, uranium and electricity takes place by means of private contracts, usually within a framework of unilateral government sanction, facilitated by intergovernmental consultation and agreement. Oil and gas moving by pipeline, and electricity by transmission line, is subject to the further government sanction involved in authorizing rights of way, rate bases and rate of return, and in enforcing environmental and public safety standards. Canadian oil, for example, is licensed for export by a process that requires both provincial and central government approval of the price and quantity involved, and its import is subject to U.S. regulations. Since the early 1970's, when Canada's oil consumption began to exceed additions to proved reserves, and particularly since the 1973 oil embargo, exports to the U.S. have been steadily curtailed. Official cooperation continues, however, in an effort to rationalize distribution patterns to realize economies of transport, both through pipeline projects and by facilitating physical swaps of Canadian oil, supplied to Northern Tier states, and of U.S. or third-country oil supplied to Canadian refineries remote from domestic crude sources.

However, indicative of the Canadian Government's current nationalist policies is the October 1980 announcement of a program to bring sweeping changes in Canadian energy ownership. The Government has presented a complex set of policy and tax rules which should result in a dramatic increase in Canadian ownership of Canadian petroleum industries. The Government proposed to purchase several foreign-owned oil companies, and to tax oil companies with less than 50 percent Canadian ownership.

This move by the Liberal Government surprised, if not shocked, the industry. Opponents of the program who not surprisingly come mostly from the western oil-producing provinces, wonder at the wisdom of such massive expenditures at a time when Canada is short of capital for establishing new Canadian ventures, and predict that the main effect will be to curtail drastically new petroleum exploration activities in Canada at a time when such ventures are particularly needed. In fact, there has been some indication that the prediction is already coming true. While the Government plans to raise the revenue for the purchases from a new energy consumption tax, only one major company, Petrofina of Belgium has sold its assets to PetroCanada, the Government oil company. Since some of these other foreign companies are U.S. multinationals, it was inevitable that Canada's new policy would cause concern in the U.S., not to speak of potential conflicts over GATT and other international agreements. Trudeau provoked strong action in western Canada, where at least one province has refused to pay new federal excise on natural gas sales. Increased western alienation from the east and from the central government has also occurred.

Trade in natural gas has its own peculiar political economy. Canadian exports of natural gas to the U.S. require a finding that domestic supplies are assured for a specified future period, and in the U.S. the transmission and marketing companies are subject to federal and state regulation. The revolution in energy prices precipitated by OPEC has made pricing formulas crucial. This problem has been resolved at the national level by an agreement on a Statement of Principles on Canadian Gas Export Pricing, worked out in March 1980, which helps assure continued performance on supply contracts running into the 1990's.

Canada's own Far North gas reserves, and the natural gas associated with oil production on Alaska's North Slope, may make inevitable the construction of a pipeline system to bring these supplies to market. But the project is of formidable scale—now estimated to cost over $23 billion. A 1977 intergovernmental agreement supports the project but leaves its execution to private enterprise. On the U.S. side, federal support has been made conditional on the exclusion of Alaska gas producing companies as equity participants. Eager to get the project under way, its managers proposed to build the Alberta-California and Alberta-U.S. Midwest legs with financing based on increased Canadian gas exports, to move through these legs pending completion of the northern leg. This construction is now underway, although continually escalating costs raise many questions about the remainder of the system—to Canada's consternation.

In the meantime, exploration for, discovery and production of, more natural gas in the United States is proceeding at a scale that may reduce the U.S. demand for Canadian gas, particularly at the prices set by Canada. This adds to the Federal-Provincial tensions in Canada over natural gas export policy, and is becoming a complex and unfortunate issue between the two countries at the time of this writing.

The happy Canadian knack for letting water run downhill, and using its force to generate electricity, has led to a considerable net import of electric power into the U.S. (some 36 million megawatt hours in 1980, or about two percent of U.S. consumption). Because of the natural seasonal complementarity of demand—peak loads in Canada occur in winter, and in the United States in summer, because of air conditioning, this exchange of electricity is subject to interruptible supply, rather than constant or base-load supply. Since most Canadian utilities price base-load exports on the cost of additional production in the United States, it is likely that the exchange of electricity between the two countries will continue to be mainly of interruptible supplies. However, interesting agreements have recently been reached between New England states and Quebec whereby the former help develop the latter's resources and purchase some of the resultant electric power.

In the nuclear field, U.S.-Canadian cooperation goes back to the earliest research. They are international competitors in the sale of reactors—Canada has specialized in heavy water moderated reactors which use natural uranium as fuel, while U.S. reactors are graphite-moderated and use enriched uranium—but this has not interfered with close cooperation in support of international controls over fissionable material and nonproliferation. Substantial quantities of Canadian uranium are enriched in the United States for export to third countries. Although spent fuel from Canada moves to the United States for reprocessing and storage of waste material, the amounts involved are negligible.

In general, then, U.S.-Canadian energy relations have evolved into a cooperative arrangement of value to both parties. Americans who think, or hope, that there can be a return to the days of massive Canadian supplies to fuel U.S. markets, are not realistic. Equally, Canadians who continue to think such Americans dominate U.S. thinking are equally unrealistic. There is instead a mature awareness in both countries that each can and should cooperate fully with the other, but that each must first look to its own needs from its own resources.

The Wheat Board

Canada is second only to the United States in the world grain trade: In the 1979–80 crop year, it exported 14.2 million metric tons of wheat, compared with 36.1 million for the United States. This substantial performance directs attention to the role of the Canadian Wheat Board, a crown corporation created in 1936, which monopolizes the trade in wheat, oats and barley grown in Western Canada. (The actual physical handling of the grain is in private hands.) Producers use seed subject to the Board's licensing, and are required to deliver to the Board's account any wheat, oats, and barley they wish to sell; they receive an initial payment set by the Board, and, depending on world marketing results, additional payments. The Board has an expert staff and offices in world grain trade centers. Its members are appointed by the national government, and the Board reports to a minister in Ottawa. Producer access to the Board is through an Advisory Council whose members they choose.

The Board and its operations enjoy the solid support of Canada's grain farmers, and the generally high regard of the world grain trade community. From south of the border, it appears to be a valid and successful institutional response to the special agricultural characteristics of a particular region, and the special problems of international grain marketing. Frequent efforts seek to harmonize export policies, and in an ideal world, such an arrangement would yield benefits for both countries. But differences in marketing techniques and economic interests still seem to prevent any real cooperation.

Miscellaneous

The foregoing material covers most of the important aspects of the U.S.-Canada economic agenda, but at any given moment there are other issues of economic significance under official bilateral discussion. In spring 1980, for example, such items included the livestock and meat and horticultural trade, government procurement policy, deep seabed mining, civil aviation relations, and specific trade issues (Canadian restrictions on imports of footwear and horticultural products; U.S. restrictions on imports of specialty steel and industrial fasteners). A defense matter of substantial economic importance was Canada's purchase of new fighter aircraft. The environment/fisheries/boundary category of problems included: the sea catch of salmon spawned in each other's rivers; a U.S. embargo on imports of tuna from Canada triggered by Canadian seizure of U.S. fishing boats in a disputed area; economic costs of implementing a proposed air quality agreement, and of disposing of toxic wastes. The special category of transboundary environmental issues within the purview of the International Joint Commission included: the Garrison water diversion project in North Dakota, the Dickey-Lincoln School hydroelectric proposal in Maine, the Popular River coal-fired power plant in Saskatchewan, the Atikokan coal-fired power plant in Ontario, the aluminum smelter at Massena, New York, the Eastport refinery project in Maine, and the raising of the Ross Dam in Washington and consequent flooding of an area in British Columbia. Overhanging all of these is the issue of acid rain which will need close cooperation between the two countries if the problem is to be resolved. Many Canadians see this as the number one long-term issue in U.S.-Canadian relations, since the use of coal in U.S. industry is largely blamed for the phenomenon.

These matters vary greatly in importance and in their degree of complexity and difficulty. They are alike, however, in that both sides understand that solutions must be worked out through the special kind of international due process to which neighbors locked into peaceful coexistence are subject.

Trade Versus Nationalism

During the 1970's the Pierre Trudeau Government, pursuing a nationalistic line, developed a policy to diversify Canada's trade and economic reliance away from the United States. Known as the "third option," this policy resulted from a review of the available options; the rejected options were (1) closer relations with the United States, and (2) continuation of the *status quo.*

During the years that the Canadian Government actively pursued this policy, U.S.-Canadian trade still continued to expand. There were a number of reasons for this.

First, Canadian efforts to come closer to the European Economic Community were partially rebuffed, or at least not warmly received. An important factor in this reaction was European dislike of the Canadian Government's defense posture: Canadian military equipment had become obsolete and of questionable reliability, and Canada's participation in NATO and the defense of Europe had been diminished by the Trudeau Government to the point where only Luxembourg's relative contribution was less.

Second, Europeans found the Canadian position hard to comprehend. With the richest market in the world at her doorstep, Canada's interest in de-emphasizing the U.S. market for others thousands of miles away seemed unrealistic. The Europeans found even the cultural and political arguments unconvincing, having learned to live with far more dangerous neighbors for centuries, having managed to resist cultural and political domination, and having formed trade relationships, economic partnerships, and even political union of sorts.

Third, of course, was simple geography. Canadian expectations of a marked change in the conduct of Canadian businessmen, who for years have traded across the border with neighbors who speak the same language, use the same measures, and have the same cultural heritage and political traditions, proved unrealistic. Even in less buoyant times it was easier and just as profitable to maintain existing trade ties, rather than try to retool, learn new trading patterns, and ship goods thousands of miles away. Under such circumstances, pure and simple propinquity, more than Government action determined economic results.

Directions for the Future

In the United States three major industries—steel, automobiles, and rubber—now face grinding transitional problems. Canada, with labor costs in general higher than the United States, faces its own structural adjustment problems. Both countries have cities and regions where unemployment is substantially higher than the national averages. And these adjustments are made more difficult because they come at a time when general economic activity is less buoyant than usual.

Without seeking to minimize their severity, however, their magnitude is less than that of problems which both countries have weathered in past decades. One danger lies in self-centeredness that can lead to measures that cause the other harm, inadvertent or not, and leads to a retaliatory exchange. Renewed cooperation in addressing the common predicament bears exploration. It should be no surprise that Canada is exceptionally sensitive to talk of increased U.S. import restrictions.

In the trade field, one possible approach would be a United States–Canada free trade area, eliminating all customs barriers between the two countries, probably in phases by a fixed schedule. Each country would, however, maintain the existing tariffs on trade with third countries.

Free trade area proposals for the United States and Canada recur regularly in academic circles. U.S. law emphasizes removal of trade barriers through a sectoral approach, clearly inviting proposals for other industries along the lines established by the Auto Pact. Section 1104 of the 1979 Trade Act (the Baucus amendment) requires the Executive branch to do a study of ways to strengthen the trade relationship. Sidney Weintraub's essay in this volume examines a United States-Canada free trade area in some detail.

Recalling that the Auto Pact resulted from a common realization that traditional trade measures could not accommodate conflicting national and industry objectives, the sectoral approach to free trade should be thoroughly explored. It offers economies of scale that can benefit industry and labor in both countries. Success of the sectoral approach could illustrate the wisdom of the the sage who remarked that, while Canada would find it hard to move directly into a free trade area with the United States, it might very well back into one while no one is looking. Small business trade could be considered its own "sector" too. It is a very neglected area and much could be done to improve and simplify cross-border trade by small business.

The marked reduction of tariffs since the end of World II focuses attention on non-tariff barriers to trade. In a recent case a Canadian provincial minister, concerned that Buy American provisions were keeping Canadian transportation companies out of the U.S. market, charged that these regulations made mockery of the support which the United States professed for liberal trade policies. The regulations in question have long been part of government procurement practice in this country, and their trade significance increases with the proliferation of federally funded programs in support of regional and local projects. Since similar practices exist in Canada and many other countries, consideration might profitably be given to the major step of working out an arrangement to regulate the practice and limiting its trade-distorting effects.

In the area of investment, the present state of affairs at first glance would seem to call for benign neglect. The $37.3 billion of U.S. direct investment in Canada (1978) is our largest stake in any foreign country, and constitutes more than half of all foreign direct investment in Canada. Canada's $6.2 billion in the United States is its largest direct investment stake abroad, and amounts to 15 percent of all foreign direct investment in this country. These impressive figures have the drawback that they have aroused concern in Canada about the degree of control that the large U.S. investment there allegedly exerts over the Canadian economy, a concern reflected in Canada's Foreign Investment Review Act (FIRA). As noted earlier it is a measure both of administrative fairness, and of the proposals' own merits that more than 90 percent of the projects submitted under FIRA have been approved. However, as Canadian investments in the United States have become increasingly bold, there has been growing concern, especially in Congress, that the rules are unfair: U.S. investment in Canada is severely reviewed and controlled, Canadian investment in the United States is free of all oversight.

Before looking further at future possibilities, the two governments' present operating procedure in conducting the relationship is worth examining. The subject matter involved—trade policy, civil aviation, radio and television, defense, boundary air and water quality, emergency help in fighting forest fires, enforcing fisheries catch limits—is too disparate to be treated in a single agency. It would seem to be best handled initially in the domestic departments concerned. Over the years, officials in both countries have learned which problems they can handle directly with their opposite numbers, and which require interdepartmental coordination or policy-level attention. The diplomatic establishments—Ministry of External Affairs and the Department of State and the two embassies—are in daily contact, working together with the domestic agencies to resolve the matters at hand. Policy-level officials set the tone of the working relationship, and intervene as necessary to make it effective, but most business is carried out routinely at the working level.

Apart from the continuing need to counter the forces in both countries that press for domestic actions regardless of their possible effects across the border, new or additional initiatives at all levels are currently a topic of serious discussion.

Promotion of tourism, for example, is already a joint effort in the New England/Maritimes/Quebec area, and the western border states and provinces are now considering similar joint efforts. The objective, of course, is to stimulate travel by third-country tourists by publicizing the attractions in the entire area on both sides of the border, and working together to ease border formalities. Cooperation between the private and local government interests involved benefit both countries, and support of state/provincial and federal authorities is growing.

There is also a recognized place for a greater role of the state/provincial and local governments as "early warning networks" about problems and policies with cross-border effects. The National Governors' Association and the National Conference of State Legislatures have been active in this area. Translation of the experience of the New England Governors' Conference with their Canadian counterparts to regional conferences across both countries is occurring.

At the national level, the interparliamentary groups meet at regular intervals. The practical advantages of these meetings have been the discussion of broad policy developments, and the evolution, in both bodies, of individuals and groups of acknowledged authority and influence on issues affecting the other country. Replacements are needed as time and electoral fortunes take their toll. The Congressional Caucus on North American Trade offers another vehicle for closer communication, though there is not a parallel Caucus in Canada's Parliament.

Business, professional and academic councils and organizations also have an important place for the discussion of policies and problems. This is particularly so for especially complex and novel developments. The border broadcasting/advertising tax matter, for example, concerns tax policy and the broader issues of regulation of communications at a time when satellite transmission systems, local cable networks, and "home box office" proprietor channels are drastically changing technological and marketing possibilities. Both the private and public sectors are, and will be, heavily involved in the development of new regimes in this important area.

These forums also point the way for accommodation in the more stubborn economic areas—fisheries and government procurement policies and regional development are cases in point.

The shortcoming of these disparate ways of handling the relationship lies in the difficulties of coordinating them. Diplomats talk mainly to diplomats, legislators talk to legislators, and businessmen to businessmen. Nonetheless, suddenly the two nations are embroiled in a fisheries dispute or a border broadcasting issue which should never have occurred and which perhaps could have been avoided by some broader coordinating mechanism than now exists. There is pressure on the two governments at least to explore possibilities for new ways to handle problems.

While they may pale in significance when judged against those that prevail in the other comparable international pairings that come to mind, the problems in the U.S.-Canadian relationship constitute an ample bilateral agenda. Successes in dealing with past problems cannot automatically be assumed for the future. As in the past, the expediency of seeking to resolve them individually, on the merits of each case, or of looking for solutions by linking together separate problems, will be a recurring question—one that in the past has been answered by rejecting linkage.

But the elements that have kept the relationship peaceful and generally serene for so long are fundamental and remain substantially intact. There is good reason to believe that it will continue to be guided by the sense expressed long ago by a Canadian scholar and diplomat. Recognizing that Canada's fate had become inextricably bound with that of the United States, he wrote:

> Canada lies side by side for three thousand miles with a neighbor fifteen times as powerful. . . . She knows that not a country on the Continent of Europe would lift its little finger to help if the United States were to attack her. Her security lies in her own reasonableness, the decency of her neighbor, and the steady development of friendly intercourse, common standards of conduct and common points of view.

When this statement was made, over fifty years ago, the world was indeed different. Canada has changed, the United States has changed, and the economic and political forces at work in the world outside have changed. What has not changed, however, is the common realization that reasonableness, decency, friendly intercourse, common standards and common points of view, exercised by separate national identities, are the bedrock of the relationship and—for all the problems—of its unrivaled success.

Postscript

In the time since this article was drafted, events have continued to confirm trends described. Canadian investments in the United States, spurred by economic uncertainties in Canada and lucrative opportunities in the United States, have grown so rapidly that counter-measures are being seriously considered in the U.S. Congress. Two specific actions are of particular note:

(1) The access of Canadian investors to substantial capital under significantly less restrictive Canadian banking regulations has prompted proposed legislation to subject foreign investors to U.S. restrictions; and

(2) The movement south of Canadian energy investors, discouraged by energy policies in Canada, has resulted in proposed legislation to limit their access to U.S. energy resources on federal lands.

These U.S. reactions, while ostensibly protectionist, are at least in part motivated by a growing sentiment in the Congress that the "rules of the game" are unfair. On the one hand, Canada's national energy policy is clearly designed to reduce and discourage foreign, and particularly the United States, investment in Canadian energy resources, while, on the other hand, Canadian firms have a relatively free hand to act as they wish in the United States. Similarly, while FIRA is increasingly aggressive in limiting new foreign investments in Canada, Canadian firms with enormous capital resources are moving in without restriction on the U.S. market. Major Canadian take-overs of U.S. realty and other businesses, such as the Seagram effort to control CONOCO and Nu-West's effort to take over Cities Service, have prompted this concern.

It is unfortunate, but not surprising, that at a time when both countries should be studying ways to improve the relationship to the advantage of both, the trend is in the opposite direction as nationalism and internal problems take a front seat to real economic opportunities for improved relationships.

ECONOMIC STUDIES

LATIN AMERICA'S DEBT: PROBLEM OR SOLUTION?

By Albert Fishlow*

SUMMARY

The external debt of the non-oil developing countries now stands in excess of $300 billion. Latin American non-OPEC members account for about half the total. Since 1973 Latin American debt has been increasing at an average annual rate of more than 20 percent a year. Amortization and interest payments have risen even faster and now amount to about 40 percent of its earnings from exports of goods and services.

Indebtedness has been a way of coping with the huge increase in oil prices. This is how the most populous Latin American countries, Brazil and Mexico, were able to sustain their imports of capital goods and intermediate products and achieve growth in spite of higher oil costs and soft export markets.

The indebtedness which was a solution now threatens to become the problem. Faced with large exposure and deteriorating indicators of creditworthiness, private banks now seem increasingly reluctant to extend their commitments. Their fear of over exposure comes at a time when new uncertainties cloud prospects for Latin American exports and the oil bill has again increased.

The danger is less massive default by Latin American debtors than a serious slowdown in their economic growth imposed by a reduction in imports caused by mounting debt service. The slowing of economic growth in Latin America would have direct repercussions upon United States interests. U.S. export earnings and investment profits would be adversely affected. So, too, would be our political objective of seeing the Latin American countries progress steadily toward becoming more equitable and more democratic societies.

If such slowing of Latin American growth and its effects are to be avoided, the short-term solution is for them to increase their indebtedness in order to protect themselves against a hostile external economic environment. The Euro-dollar market cannot, however, provide this capital at the same rate as before. More imaginative financing will be needed to permit funds to be channeled to the developing countries.

Three broad approaches, singly or in combination, present themselves. One is to make private lending more attractive by reducing the risks for individual banks through an insurance pool. A second ap-

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proach is to give the international agencies a larger role. A third approach is to induce direct lending by OPEC countries.

The international community can also help by maintaining open and expanding markets for the exports of the developing countries. Current financial obligations of these countries can only be repaid by future exports. Countries must be able to count on increased foreign exchange earnings in the future to justify going into debt. If their exports do not grow, then debt will indeed become the dominant economic problem of the developing countries.

Increased external borrowing would not give Latin American debtors a free ride. They would have to discourage consumption in favor of higher savings and exports. They must conserve on oil and develop alternative energy sources. They must invest wisely or pay the penalty in diminished access to foreign capital markets.

In short, this international response goes hand in hand with internal adjustment policies. Both are necessary if Latin American debt in the 1980's is to play its potentially constructive role, and not to become one more burden among the many.

INTRODUCTION

Since 1973 the world has learned to live, if somewhat precariously, with high-priced oil and record imbalances in international payments. In good part the problem has been met by borrowing by the developing countries. Between 1973 and 1980, developing country indebtedness has grown at an average annual rate of more than 20 percent.

As a consequence, the medium and long term debt of oil-importing developing countries (including Mexico, only recently an oil exporter) probably exceeded $300 billion at the end of 1980. Latin American countries are responsible for about half of this total. Brazil and Mexico not only lead the region, but the world as a whole, and Argentina and Chile in recent years have also become leading debtors.[1]

The importance and vulnerability of Latin American borrowers are highlighted by measures like the ratio of interest and amortization payments to export earnings and the ratio of debt to gross domestic product. Their current debt service ratio of about 40 percent is four times larger than the level for non-Latin Ameican oil-importing, developing countries. The Latin American debt-GDP ratio of 0.3 is half again larger than the 0.2 characteristic of others. The relatively greater burden of Latin American debt service is explained by the importance of private credit, with its higher charges, and by import substitution policies that have reduced exports as a proportion of total product compared to other developing countries.

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[1] This estimate of disbursed debt and service payments excludes the Mediterranean countries commonly calculated in the World Bank estimates. It includes private non-guaranteed loans. The 1980 total debt takes as its base a 1978 level of $216 billion (National Foreign Assessment Center, Central Intelligence Agency, *Non-OPEC LDC's: External Debt Positions*, January 1980, p. 3) to which net external borrowing of $87 billion in 1979–80 has been added. (The latter estimate is derived from International Monetary Fund, *World Economic Outlook*, May 1980), p. 101, after adjustment for the capital flows to the Mediterranean countries.)

The most inclusive estimate of developing country debt, including the oil exporters as well as the countries excluded above, would come to more than $400 billion.

Differences in country coverage and concept (disbursed vs outstanding: publicly guaranteed vs. total: medium and long term vs. total foreign liabilities) bedevil discussions of the debt situation. The resulting numbers can alarm or placate according to preference.

This indebtedness has not escaped notice. Comment has ranged from warnings of an impending financial Armageddon to soothing assurances that market forces are in full command. Concerns have varied from preoccupation with debtor capacity to meet outstanding obligations to fears that shortages of financial capital will limit economic growth of borrowers and industrial countries as well.

This paper addresses some of the issues raised by the current level of Latin American indebtedness—the evolution of the debt, the burden of the debt, the diverse national experience with indebtedness, and implications for United States policy. In the last analysis, the question posed is whether the debt that eased the economic problems in the 1970's will become a problem in its own right in the 1980's.

Facts About the Latin American Debt

Two trends dominate the Latin American experience. One is the explosion of debt in the 1970's. The other is the progressively larger role of private financial flows, especially from commercial banks. Both are clearly evident in appendix table 1, p. 165.

During the last decade, debt increased more than seven-fold, compared to a doubling in the 1960's. Deflated for price change and subtracting the growth of gross national product of the region, real debt increased by 117 percent in the 1970's versus a mere 8 percent in the previous decade. Reliance on external finance has demonstrably increased, while foreign direct investment expanded more slowly: from 1956 to 1965 direct investment exceeded loans; from 1976 to 1980, investment amounted to 20 percent of borrowing. Debt has become the predominant form of capital transfer from abroad.

The access of capital markets evolved in two phases. Before the oil crisis, surpluses in the Euro-dollar market became newly available to selected larger countries whose growth and export performance conferred creditworthiness. After 1973, borrowing was of another kind, a response to the rising costs of oil and other imports, and less vigorous expansion of world trade that penalized exports.

Borrowing was not the only option in the face of the sudden increase in oil prices. One alternative was to use less oil. Individual countries could also compensate by importing less of other products, helped along by the reduced real incomes resulting from adverse terms of trade, or by exporting more. They could thus self-finance their higher oil bill by lowered domestic consumption and investment yielding a smaller trade deficit. To some extent, and especially as time went on, the Latin American countries took such measures. But in the midst of a recession in the industrial West that made exports less certain, a debt strategy was the more attractive one to follow. Gradual adjustment made good economic sense at the national level. At the international level, there was no choice: the oil country surpluses had to be financed or global income would fall. Some countries were required to borrow.

The Latin American choice to do so affected not only the volume of debt but also its composition. During the early 1960's, the principal source of Latin America's infusion of capital were United States loans and grants under the Alliance for Progress. In the 1970's the main source was private bank lending, utilizing after 1973, OPEC surpluses deposited in United States and other banks. Two-thirds of Latin America's debt now is owed to banks, more than twice the level in 1970.

This substitution of private for official finance did not prejudice the growth of the public sector in Latin America. Quite the contrary. Governments, state enterprises or firms with public participation, and official banks remained the principal recipients of private loans. Public guarantee was an important attraction to banks, providing an unprecedented access to capital for the state sector and underwriting its expansion. This was a far cry from the 1950's when Latin American governments pleaded, largely in vain, for official capital to finance public projects.

Private capital is also available quickly and at lower than previous interest rates as competitive forces have reduced bank charges for intermediation. Private capital has the further advantage to the recipients that it comes with fewer political strings than bilateral aid— at least until doubts about creditworthiness emerge. Then banks press for orthodox, conservative policies, political as well as economic. This asymmetry, and even bias, is still a long way from the view that private bank financing is exploitative and interventionist: "Bank loans, open-door regimes and repressive policies have frequently coincided. . . . The technocratic posturing and apolitical rhetoric of bank officials is merely a mask for far-reaching political actions." [2] That view presumes that an export orientation is necessarily bad, fails to see balance of payments problems as even partially the consequence of the disregard of market forces, and interprets authoritarian solutions as wholly of international capitalist imposition rather than related to populist failures.

This is not to argue that private finance does not impose additional burdens. One is a market interest rate that is higher than charged for official loans. Another is a shortened debt maturity structure, as short as the average of 4.3 years Brazil experienced in 1977. A third is the volatility of interest rates, subject to readjustment at six-month intervals. That uncertainty has large quantitative implications. A one percentage point change in nominal interest rates can now change Latin American service costs by almost one billion dollars.

The Nature of the Problem

On balance, because money was cheap during the peak borrowing of the 1970's and because new inflows far exceeded return payments, reliance on debt clearly seemed a sound policy. Now, with real interest rates (after adjustment for inflation) persistently positive instead of negative, and debt service mounting, does the same judgment hold?

To answer that question requires a differentiation between two types of debt problems. One is where the real rate of return on the foreign resources falls short of their cost. The other is a foreign exchange cash flow or liquidity constraint.

For money borrowed in the 1970's, even allowing for higher interest rates to be paid in the 1980's under the current flexible interest rate policy of most international lending, the real average costs are low

[2] Jonathan D. Aronson, ed., *Debt and the Less Developed Countries* (Boulder, 1979), pp. 203, 205.

enough, and even negative in the mid-1970's, so that real return on domestic investment does not seem to be the central issue. But a fundamental limitation of a debt strategy is that one never knows the real cost until the loan has been repaid. This is true not merely because future interest rates may change, but also because the real resources required by the future exports needed to liquidate the debt depend on future price levels, which are uncertain. If export prices move adversely, then debt repayment will turn out to be more onerous than anticipated, and the margin of gain smaller.

Even with these uncertainties, it is likely that the real rate of return on Latin American debt—that is the increased flow of income deriving from the investment represented by the debt—will continue to exceed the cost. There is no similar assurance about the ability to meet short-term debt service requirements. A positive differential between returns and costs does not imply that foreign exchange will be available when payments fall due—even though the debt more than repays itself over the full life of its investment. In the short term, exports may not increase enough to meet the debt service. Only if it is possible for the debtor country to borrow to meet interim obligations can the long run advantages of debt be realized.

Continuing access to capital markets is therefore essential if debt finance is to produce its potential benefits. In the medium term, access to export markets is equally essential. Export growth must not only meet import requirements, but also be sufficient to slow down the high rates of recent debt expansion. Financial and real markets are linked: debt exposure cannot be reduced without expanded exports.

The looming Latin American debt problem is therefore not that costs, even though rising, will outstrip returns, but that capital may be unavailable in adequate quantities, even at higher prices. Respected bankers warn that they are overcommitted, and more reluctant to lend as their developing-country loans mount to significant multiples of the banks' net worth. Since 1975 American banks have increased their lending to non-oil developing countries at a rate of 17 percent a year, more rapidly than the expansion of their capital base. Even this has not been enough. United States banks have not maintained their market share, especially in the last two years. Only the willingness of late-comer European and Japanese banks to expand their loans at 40 percent a year has met demand. Such a rate is not sustainable, leading one industry authority to predict a future limit to nominal growth of lending—at current rates of inflation—of no more than 15 percent a year.[3]

At the same time, Morgan Guaranty Bank's *World Financial Markets* estimates that twelve major non-oil developing country borrowers have needs that will likely expand at annual rates ranging downward from 22 to 16.5 percent between 1981 and 1985. There is thus a gap between demand and supply that can be averted only by higher economic growth in the industrial countries with resulting higher imports from the developing countries, or by increased financial intermediation.

For Latin America as a whole, detailed projections[4] suggest that a regular 15 percent increase in finance could meet requirements de-

[3] *World Financial Markets*, September 1980, p. 8.
[4] See Appendix Tables.

spite slower export growth in the next few years. There would be a reduced rate of economic expansion and higher debt service ratios, but the impact would not be as severe for Latin America as elsewhere.

This is so for three reasons. First, Latin America is the most industrialized region of the developing world. Second, the area has a demonstrated capacity to restrict imports and substitute domestic supply when export earnings and capital flows together fall short of requirements. This flexibility reduces the otherwise fully adverse effects on income. A ceiling of 15 percent on capital flows would, however, mean a significant reduction in the ratio of imports to national product, implying increases in domestic costs and reduced competitiveness in world trade. Third, for the region as a whole petroleum imports have become less important as Mexico and Peru have become oil exporters. Indeed, the region has now changed from being a net importer to a small net exporter of petroleum. This transformation facilitates intra-regional arrangements that only a few years ago seemed impossible. Mexico and Venezuela have recently offered new direct assistance to nine countries of Central America and the Caribbean adversely affected by increases in oil prices. This is in addition to earlier Venezuelan assistance through the Venezuelan Trust Fund of the Inter-American Bank and the Puerto Ordaz Agreement providing long term finance for oil imports to many of the same countries. During his visit to Brazil in August 1980, President Lopez Portillo suggested expanded Mexican exports of oil in exchange for Brazilian iron ore, bauxite, and food.

This better situation of the region as a whole does not eliminate problems of individual countries nor reduce the area's vulnerability to even small declines in exports. Debt service payments are now a regular and large obligation that will amount to more than 40 percent of export receipts over the next several years. These are the consequence of earlier borrowing. A slower growth of exports will aggravate the problem. Moreover, volatile exports implies that capital requirements will also fluctuate sharply. However, the funds available for lending will be limited by economic factors and bureaucratic inertia, raising liquidity problems in the future. Indeed, the supply of private external finance is likely to be smallest for those countries facing a liquidity problem.

Continuing and growing indebtedness over the next several years is a temporary solution, not a long-term panacea. Inflation is not the cushion in easing future repayment that it once was. Now that interest rates have adjusted for inflationary expectations, and the preponderance of the debt is subject to variable interest rates, inflation becomes a disadvantage. Higher interest rates anticipate amortization, and effectively reduce the maturity of the loan. Current debt service ratios are higher than they would be under stable prices.

Second, reliance on external debt can complicate and distort domestic economic policy. Real exchange rates seem to follow a regular cycle of undervaluation and overvaluation. In the undervaluation phase, lending is attractive to the lender because of the improving export performance of the borrower. With increased capital inflows, the exchange rate tends to move toward overvaluation; domestic borrowers contract loans abroad when the exchange rate fails to keep up with domestic inflation and help to perpetuate overvaluation. Sooner or later overvaluation adversely affects exports. The resultant prospect of devaluation sooner or later discourages the local borrowers and perhaps the lenders, frequently provoking a flight of capital. With devaluation and ineffective controls over capital flight, the sequence runs the risk of being repeated.

Third, the debt strategy presupposes continually growing exports regardless of uncertainty over whether expanding markets will be available. Sluggish growth in industrial markets can be offset by greater capital inflows in the short term, but if slower growth induces the industrial countries to increase protectionism, the debtor countries will face even greater problems. The positive accomplishments of the Tokyo Round have not fully allayed fears of diminished market access. New and more effective restrictions remain a threat. They can frustrate an otherwise sound debt strategy.

Finally, reliance on debt postpones but does not avoid the necessity for hard domestic measures: raising domestic energy prices, accepting lower real incomes, shifting resources from consumption to investment and exports, cutting back on national expenditures. Postponing these adjustments may not make them easier to make later on. Obvious issues of income distribution present themselves: whose consumption will be constrained, how will export incentives be distributed, what compensation will energy consumers receive, what role will be taken by state and private enterprises in the new structure of production, etc. In a period of transition to greater popular and civilian participation in politics in some countries, these questions admit of no easy answers.

These additional considerations make even clearer that economic development with large infusions of debt, a model which many Latin American countries are following, is both a solution and a problem.

The next section discusses different national experiences. The concluding section deals with policy options.

A National Focus

There are obviously large differences in indebtedness and in political difficulties among the countries of the region. Debt is highly concentrated. Five countries—Brazil, Mexico, Argentina, Chile and Peru—account for almost 90 percent of the total Latin American debt. Their debt service ratios range from 30 to 70 percent; their debt—GDP ratios, from 15 to 40 percent.

The other smaller countries of the region fall into two groups. One has relatively low debt-income and debt-service ratios, as, for example, Honduras and Haiti. For the most part they are among the poorer countries of the region, countries that have followed conservative economic policies rather than borrowed abroad. The option is perhaps as much necessity as choice.

A second group has the highest debt-GDP ratios in the region. This group includes Guyana, Panama, Nicaragua, Bolivia, Jamaica and Costa Rica. Although the debt service ratios of some of these countries remain below those of the largest borrowers, their situation is more precarious. They cannot compress imports so readily, and their dependence upon a limited range of exports make them vulnerable. Because

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smaller countries are smaller borrowers, banks are more likely to resist rolling over past debt and to insist upon repayment.

It is not surprising that almost all these countries confront a classic liquidity problem. In the past year, Bolivia, Jamaica and Nicaragua (as well as Peru) have rescheduled their debts. Because they have borrowed so heavily in the past to help adapt to a more difficult external economic environment, they cannot easily continue to do so. Each nation runs the risk of moving from one balance of payment crisis to another. The plight of these smaller economies is frequently overlooked because they account for so little of the total debt.

Brazil and Mexico, the two principal debtors, have undergone much closer scrutiny. Not only are these countries important factors in world financial markets, they also have the highest debt service ratios in the region and probably in the developing world. Such static ratios can be misleading. Mexico continues to be a favorite in world capital markets, while Brazil-watchers speculate about when Brazil will be forced to go to the International Monetary Fund for help. The different situations of these countries epitomize the advantages and limitations of debt finance. They repay closer examination.

Mexico's political stability, economic performance, and proximity to the United States had long enabled it to borrow heavily from private sources. By the mid-1970's, and quite independently of the oil price increase, it was obvious that creditors believed Mexican debt levels had reached troublesome proportions. Mexico was faced with a liquidity crisis, exacerbated by a long overvalued exchange rate and capital flight induced by heightened investor concern with populist policies. The country was forced to borrow from the Fund, devalue, and accept restraint in further borrowing and in domestic expenditure. Prospects were for a prolonged and possibly quite difficult domestic adjustment.

The verification of large petroleum reserves and the advent of a new Mexican administration that gained domestic and international confidence rapidly restored creditworthiness. Agreed restraints were breached, and economic growth accelerated, financed by new injections of external finance. More certain prospects for repayment justified large capital inflows and made possible continuing balance-of-payments deficits. The crisis of 1975–76 was forgotten.

Debt adds a degree of freedom to Mexican economic policy by underwriting imports without counterpart exports. Mexico can afford to follow a conservative oil production and export strategy because it is now easy to borrow against oil in the ground that is appreciating in value. That strategy is the more attractive if the terms of borrowing are cheap and their prospective returns in real productive capacity are high. Mexican policymakers now have abundant access to foreign capital, and hence an ability to borrow short-term while investing in long-term projects.

Even Mexico, however, cannot ignore the management of its debt. Under a continuing policy of limited oil exports, the economy's high import elasticity can only be satisfied by a substantial rise in external borrowing. These, in turn, will create interest and amortization obligations. If Mexico were again to fall into disfavor, a new financial crisis would be much more severe. What averts it is external confidence in the country's export capability which ensures a continuing capital inflow.

The liberating role of debt in the Mexican case stands in contrast to the constraint which debt service now imposes on Brazilian policymakers. Interest and amortization payments have risen sharply in the past two years and now average about two-thirds of export earnings, with prospects for a further rise. This increase has occurred despite a spectacular gain in exports. Brazil confronts a burden like Mexico's, but with the fundamental difference that oil appears in the import, not the export, side of the accounts. Lenders recognize Brazil's vulnerability to external circumstances and seek to limit their exposure despite its impressive export performance and favorable long-term prospects. To be sure, diminished confidence in Brazil's economic management has contributed to the nervousness of lenders. A rate of inflation over 100 percent inspires obvious concern. Overly optimistic forecasts also erode confidence when they are not realized.

Brazil's difficulties were predictable. Its access to capital was certain to become more circumscribed as soon as debt service increased to such high levels. Once the supply of external capital dries up, long-term returns become irrelevant. All that matters is the short-term risk. This is obviously present in the Brazilian situation. A $5 increase in the price of a barrel of oil translates into $1.5 billion in additional foreign exchange requirements; a hike of 5 points in interest rates adds some $2 billion. Balance-of-payments difficulties cause creditors to shy away and to precipitate the very liquidity crisis they fear.

Brazil's problem, like that of other Latin American countries earlier, is a familiar one. It will be resolved, whether Brazil goes to the Fund or not, by new evidence that external obligations can be met. Such evidence will likely take the form of slowed economic growth and hence of reduced imports. Brazilian promises of a more rapid and diversified expansion of exports will not satisfy creditors. That is why the Mexican oil finds were so significant: they made capital flow again without a long and costly adjustment.

If Brazil goes to the Fund, it will do so because that route promises to guarantee the needed supply of private capital more effectively than direct negotiation with private lenders. Debt will continue to grow; it will likely double by 1986. The huge interest and amortization charges on outstanding debt swamp even a large (and unlikely) increase in exports over the next few years. Rescheduling will do little good if significant new capital is not also forthcoming.

The liquidity crisis requires Brazil to accelerate its adjustment to high-priced oil and credit by substituting other sources of energy for oil, and by more drastic conservation measures. Resources must be shifted more rapidly toward exports. Domestic savings must be increased significantly to replace the resources now being transferred abroad to pay for the excess of imports over exports.

These requirements are as essential as an assured supply of foreign capital. They make clear that going to the Fund to reassure creditors will only work if at the same time a national consensus can be reached on the austerity program to be followed. That consensus now must include newly active labor unions and political parties, and not just narrow elites. Inadequate attention to the politics of adjustment can cause the best technocratic schemes to fail.

Only a handful of Latin American countries have oil to rely on for obtaining credit needed for development. Many more Latin American countries fall into Brazil's situation where more complex strategies are called for. What the oil exporting and oil importing countries share in common is a continuing reliance on external finance in the short-term, as they carry out policies designed to reduce their reliance on debt over the long-run.

The crucial question, therefore, is whether an adequate supply of external capital is forthcoming for deserving countries. The financial markets alone will not necessarily assure such a supply, given the level of current exposure and the bleak short-term prospects for exports.

Policy Implications

The problem posed by the current levels of indebtedness of some Latin American countries is not a new one. Two decades ago the Economic Commission for Latin America prepared a report on external financing that concluded rather pessimistically that the capital needed because of high debt service would not be forthcoming "inasmuch as a higher proportion of [Latin America's] foreign exchange receipts on current account is now absorbed by the servicing of capital previously invested in the region." [5]

What helped to prove the prediction wrong was a significant increase of official United States capital under the auspices of the Alliance for Progress. The positive impulse of bilateral economic assistance on generous terms no sooner began to wane in the late 1960's when new and larger opportunities were presented by the Eurodollar market. On the merchandise side of the accounts, growing exports after a decade of stagnation were an important source of relief.

These solutions are no longer available today, when the burden of Latin American debt service is twice as great as it was then. The United States is not well positioned to play the role it did in the early 1960's. For one thing, its foreign economic responsibilities and interests have broadened far beyond Latin America. Special attention to Latin America contends with the need for a policy that also responds to United States interests in other continents. Secondly, United States bilateral assistance now amounts to an insignificant proportion of Latin American net capital inflow, less than 2 percent in recent years compared to more than 35 percent in 1961–65. Except for Israel and Egypt, such assistance is provided only to the smallest and poorest countries. Many of these do not confront a debt problem because they never were creditworthy enough to borrow much in private capital markets in the first place.

The great expansion of private finance which came from the Eurocurrency market in the late 1960's and 1970's does not seem likely to recur. Indeed, it is the possibility of less rapid growth of such lending in the future that is a principal source of concern. Caution is now the hallmark of private banks; it makes itself felt in shorter maturities, larger risk premiums, and smaller commitments. Banks now have a far greater exposure in developing countries than they ever intended, and few are eager to be as aggressive as they once were.

[5] Economic Commission for Latin America, *External Financing in Latin America* (1965), p. 202.

Another surge in exports to compare with the results of the new outward orientation of Latin America that began in the 1960's also seems unlikely. At that time the markets of the industrialized countries were expanding at much higher rates than are projected for the 1980's. International trade continues to grow relatively more rapidly than world output, but continuing slow growth in the GNP of the industrial countries restrains the growth of export markets. Latin American countries confront a potential reduction in world export growth from 8 percent in 1965–75 to 5 percent in the 1980's.[6] Despite a commitment to greater exports, and despite a still small share of world trade, these countries will find it difficult to make foreign exchange earnings outstrip requirements for servicing debt in the next decade.

Former sources of relief cannot therefore be relied upon. At the same time, the dimensions of the problem are demonstrably greater. Debt and debt service are larger. Price fluctuations of export products are wider. Oil price increases are a constant threat to the best laid plans of oil importers. Interest rates have varied substantially in response to United States credit conditions and introduce another element of instability.

New policies have consequently been advocated. Debt illustrates the reality of interdependence. Lending countries also would suffer if borrowers confronted limited external finance. One effect is direct: the impact on the stability and profitability of the largest private banks in the developed countries. Another is indirect: the reduced demand for exports of industrial countries because debtors are forced to cut imports and throttle back their economic expansion.

New methods are sought to assure developing country borrowers an adequate supply of credit under more certain conditions and for longer terms. The various proposals differ in their attention to each of these objectives, and in the form which official intervention takes. Three broad approaches can be identified. One is to make private lending more attractive. The second is to augment the participation of official institutions, principally the World Bank and the International Monetary Fund. The third is to facilitate direct recycling of the surpluses of the oil exporters without the intermediation of financial markets.

Common to efforts to encourage continuing private lending is a search for ways to reduce the risks of individual banks. A. W. Clausen of the Bank of America (before his designation as Robert McNamara's successor at the World Bank) calls for an insurance pool, funded by the IMF, to protect banks with larger developing country exposure. Another proposal is for a separate institution that could directly guarantee the debt of developing countries. I have suggested elsewhere transferring part—but not exclusively the most vulnerable—of the commercial bank portfolio of developing country loans to the World Bank in exchange for longer term World Bank bonds. This would raise the willingness of private lenders to finance developing countries while at the same time the repayment of the loans

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[6] These estimates for the 1980's derive from the World Bank, *World Development Report, 1980*, p. 7. The rate of growth for the world exports is put at 5.4 percent annually for the high-case projection of industrialized country growth at 3.6 percent per annum. The low case of 3.0 percent would bring world trade growth below 5 percent.

would increase resources at the disposition of the Bank. Still a fourth alternative emphasizes the potential of co-financing, i.e., formal joint participation of private and official banks in lending for a specific project. Developing countries have greater reason to avoid a loss of creditworthiness with official institutions than with any single private bank.[7]

These possibilities share the attractive feature of bolstering the efficient private intermediation of recent years. Co-financing already has been practiced, and may become more appealing to some banks now hesitant to commit larger sums. But it will do little to change country lending limits or the fear of generalized financial overexposure. Sharing of risk already occurs among banks in Euro-market participations. Insurance or guarantees, to be effective, must be selective. If all loans are guaranteed, bank regulators will hardly be satisfied; if all banks are insured, without regard to the risks they individually decide to undertake, then there is no incentive for prudence. There is also the important issue of who shall pay the premiums or provide the guarantee.

These proposals have not evoked an enthusiastic response from many officials who see them as ways to bail out the commercial banks at public expense. They do not have to be. Schemes that pool risk, even if the banks directly pay the cost, may still be an efficient way of inducing greater lending.

Yet even were some of these steps taken, they would not resolve the problem. Short-term, private bank credit, even in large volume, forces the borrowing countries to live with high debt service and the threat of sudden crises. Longer term and more assured finance are also necessary components of financial strategy for the Latin American nations.

An enhanced role for the official institutions has therefore been proposed. The World Bank has already voted to double its capital stock from $40 billion to $80 billion, and authorization to borrow against assets rather than capital exclusively has been discussed. A ratio of loans to capital of 2:1 would lead to a further doubling of the Bank's lending capacity. The IMF has also increased its quotas for developing countries by about $10 billion apart from the creation of the Witteveen Facility. In addition, it has been proposed that the IMF be allowed to borrow from the financial market directly.

These changes might well restore the relative position of international financial institutions to what they had been before the great increase in private lending. More than a restored market share is involved, however. Beyond the change in the composition of debt, a larger role for the official institutions enlarges the scope for their surveillance function. Individual countries, in resorting to the private capital market, can get themselves and their lenders in trouble. Unlimited finance is not necessarily desirable. Less monitoring has been done in recent years than has been appropriate. There is considerable evidence that bank assessments of risk and risk premiums have not been correct.

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[7] For a description of some of these proposals see Roger Leeds, "External Financing of Development—Challenges and Concerns," *Journal of International Affairs* (Spring/Summer, 1980) pp. 34ff. For my portfolio swap suggestion see Albert Fishlow, et al., *Rich and Poor Nations in the World Economy* (New York, 1978), pp. 67–68.

These steps to reconstruct the financial system have had broad support from developed and developing countries alike. They may suffer only partial implementation, however, under a Reagan administration much less sympathetic to multilateral lending. They may also fall victim to the conflict between developed and developing countries about the relative roles of the International Monetary Fund and the World Bank.

Commercial bankers have tended to feel more comfortable with the former than the latter, while the contrary is true for the governments of the developing countries. Thus, confronted with the prospect of inadequate private bank lending, Morgan Guaranty's *World Financial Markets* calls for an expanded IMF presence:

". . . the Fund must be prepared to accept programs of current account adjustment that lead to a more than short-term use of its financial resources." Morgan Guaranty also suggests that the IMF "must show greater willingness to modify the targets it sets for particular countries when changing external circumstances invalidate the assumptions on which adjustment programs are built." [8] The Brandt Commission goes so far as to recommend a new World Development Fund, although Edward Heath, one of the members of the Commission, in recent testimony has made clear his preference "that the existing institutions adapt themselves, the World Bank in particular, to program lending. . . ." [9]

The distinction between the Fund and the Bank begins to blur as the latter enters into program lending for structural adjustment while the former extends the maturity of its credits and the flexibility of its conditions. Nevertheless, there will still be, and there should be, differences. There is a place for shorter-term management and a place for medium-term strategy. Permitting the IMF to borrow in capital markets will give it the resources to deal better with liquidity crises. With greater resources available to the Bank as well, the international capital markets of the 1980's can function in a way in which public and global objectives as well as private profit maximization can be served.

The third set of proposals to modify the present financial system focuses on tapping OPEC surpluses directly. This approach has gained wider support in recent years as those surpluses have again increased and seem likely to remain large. By-passing the Eurocurrency market would preclude the need for banks to assume the risk of intermediation; the surplus countries would instead bear it. This would involve these countries in financing more of the deficits corresponding to their surpluses without leaving the financial risks to others.

Some proposals call for new international agencies, or new facilities at existing institutions. Other variants favored by many developing countries are preferential prices and concessional loans tied to oil imports. Mexico, Venezuela, and Trinidad and Tobago have entered into such arrangements with Central American and Caribbean countries. Other oil exporters have also increased their direct finan-

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[8] *World Financial Markets*, September 1980, p. 11.

[9] *North-South Dialog: Progress and Prospects*, Hearings before the Subcommittees on International Economic Policy and Trade and on International Organizations, Committee on Foreign Affairs, House of Representatives (96th Congress, 2d Session), p. 183.

cial involvement. Kuwait has taken an equity position in Volkswagen do Brasil; Saudi Arabia contributed more to the Witteveen Facility than any other country, OPEC-based banks have increased their lending to developing countries. These commitments are in addition to concessional bilateral assistance, which though largely limited to the Muslim world, represents a higher percentage of GNP of the donor countries than is true of the OECD countries.

Less helpful to the developing countries is the increasing tendency of the surplus countries to find new channels of investment in the industrialized countries. The low real cost of borrowing that has made Euro-currency loans attractive and advantageous to developing countries has also meant low returns to deposits. Surpluses that are recycled by way of non-bank assets in the industrialized countries may not wind up so readily in the developing countries. Part of the thrust of the new proposals is to assure that they do.

At the same time, there is a political cost attached to a larger OPEC role that the financial advantages should not obscure. Equity participation in developing countries, loans from OPEC-based banks, and contributions to new multilateral facilities all grant the OPEC countries greater power. It may be directly exercised as a result of a larger OPEC share of the votes in international institutions. It may be exercised through a larger say on a range of issues that may extend from the legitimacy of a Palestine state to views on broader development strategy. The exercise of this side of OPEC oil power has been limited thus far. Private bank intermediation has kept the financial threat in abeyance. The industrialized countries should consider how deeply they want OPEC involved, and what the full range of trade-offs is between alternative financial arrangements and greater OPEC assumption of responsibility.

It is for this very reason that some people have sought to link recycling proposals to a broader global agreement that would at least include the price of oil. The Brandt Commission speaks of a package that "could include price indexation related to world inflation, denomination of the price in a basket of currencies or SDR's, and guarantees of the value and accessibility of financial assets which oil producers receive." [10] Others have been skeptical of enforcing such a deal when oil prices are subject to independent demand and supply conditions, and not subject to direct determination.

Yet the relationship between financial recycling and the price of oil cannot be ignored. The abruptness of oil price increases both in nominal and real terms, and the attendant uncertainty, has contributed to lower economic growth throughout the world. Conversely, low returns on financial assets tend to encourage oil producers to leave the oil in the ground. This means higher prices and unnecessary social cost.

It is possible to establish such a linkage short of a global bargain.[11] A modest alternative would be a special lending facility administered by the World Bank which would pay OPEC depositors a return tied to the real price of petroleum. As the price climbed above an agreed-

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[10] *North South: A Programme for Survival* (Cambridge, Mass., 1980), p. 279.
[11] For an initial exposition of this proposal, see North-South Dialog, pp. 27, 34 and the ensuing discussion.

upon level, the percentage of indexation on OPEC deposits to compensate for inflation would decline.

Such deposits would permit long-term lending to the developing countries. Such loans would necessarily also require correction for inflation. The real borrowing rate could be fixed at modest levels, say 2 percent. Depositors might be paid a higher rate, in order to stimulate continuing increases in oil production. The difference could be made up by a levy on World Bank members in proportion to their share of capital.

The surplus oil exporting countries, a handful dominated by Saudi Arabia, have an interest in such an arrangement because it offers them the prospect of a better return on their assets than they have experienced. Their position within OPEC has always been on the side of moderation because of their large stake in world financial stability. Such an arrangement formalizes and provides monetary incentives, for behavior to which they already lean. The developing countries have an unsatisfied demand for longer term loans and the inflation adjustment they are asked to make is a modest cost and one which they are making under current borrowing arrangements. The industrial countries in turn would pay the bulk of the interest rate subsidy—the magnitude of this subsidy would be small compared to current direct assistance—and receive in return assurances of greater oil price and stability in financial markets.

These three approaches to assuring an adequate supply of capital to developing countries in the 1980's are not mutually exclusive; on the contrary they are mutually reinforcing. Finance for development must have elements of private and public interest and expertise if it is to perform its task. Banks, official institutions, and direct intermediation of the surplus countries all have a place. There is good reason to believe that these measures would avert an aggregate shortage of funds in the next decade.

Individual countries would not be fully guaranteed against short-term problems, but there would be no general inability to continue the borrowing that is necessary. Under reasonable assumptions, the debt for the Latin American non-oil countries (including Mexico) may rise by almost as much as 50 percent in real terms over the next decade. That will still be much slower than in the 1970's, and would reduce debt service as a percent of exports and the debt to GDP. This suggests that the debt burden is manageable.

The principal danger is not the wholesale default by developing countries and the possibility that it may bring the world financial system crashing down. The principal danger is that available international finance will be inadequate to maintain a reasonable level of world economic growth in the 1980's. If the supply of funds proves inadequate, it will be the largest debtors—many of them Latin American countries—who will be most in danger. They will have to bear the brunt of the adjustment burden themselves. Because slower growth is experienced in this first phase primarily by the developing countries, the developed countries may not react to strengthen the system in time to avoid slowing of growth of their exports to the developing countries. The burden will fall primarily on the developing countries. Interdependence is still asymmetric.

The role of the United States in averting such an outcome appears no longer primarily financial. The role is now the more diffcult one of leadership in advancing cooperative reform. In many ways the debt issue is the easiest problem for the developed and developing world to solve. Both sides have an interest in continuing the flow of capital and the potential remedies are at hand. If we cannot deal with the Latin American debt problem, there is little reason to be optimistic about other international economic problems in the years ahead.

APPENDIX

TABLE 1.—LATIN AMERICAN DEBT [1]

[In billions of dollars]

	1960	1967	1970	1973	1976	1978	1980
Public or publicly guaranteed	5.5	10.7	15.8	24.8	53.1	82.7	104.0
Official	NA	5.9	8.0	11.0	17.4	22.7	NA
Private	NA	4.8	7.2	13.8	35.7	60.1	NA
Financial markets	NA	2.2	3.7	10.0	30.3	51.5	NA
Banks	NA	NA	2.6	8.4	27.9	44.8	NA
Nonguaranteed	2.9	3.9	6.5	12.3	21.7	30.7	51.0
Banks	NA	NA	NA	NA	16.3	23.0	38.3
Total disbursed	8.4	14.6	20.8	37.1	74.8	113.4	155.0

[1] Excludes Venezuela and Trinidad and Tobago.

SOURCES

PUBLIC AND PUBLICLY GUARANTEED EXTERNAL DEBT

1960: Inter-American Development Bank, *Economic and Social Progress in Latin America.*

1967–1978: World Bank, *World Debt Tables.*

1980: International Monetary Fund, *World Economic Outlook*, p. 102, change for Western Hemisphere, 1978–1980.

TOTAL DISBURSED DEBT

1960–1970: Balance of payments based estimates of cumulative capital inflows, reported in an earlier working paper ("Debt, Growth and Hemispheric Relations") adjusted upward by 1.02. This factor is the relationship between the earlier 1973 estimate and the new direct 1973 estimate.

1973–1978: National Foreign Assessment Center, Central Intelligence Agency, "Non-OPEC DC's: External Debt Position" to which public debt of Ecuador has been added.

1980: 1978 estimate incremented by estimated capital flows less foreign investment, as reported in *World Economic Outlook*.

Nonguaranteed Debt.—Total minus public and publicly guaranteed.

Nonguaranteed bank debt: Proportion of bank loans to non-guaranteed debt for Brazil, 1977/78, in *World Debt Tables*, September 3, 1979.

TABLE 2.—2 ALTERNATIVE PROJECTIONS OF LATIN AMERICAN DEBT[1]

	Billions of dollars[2]					
	Level of debt	Debt service	Current account deficit	Current account (GDP)	Debt service (exports)	Net debt (GDP)[3]
Estimated: 1980	154.8	36.8	21.7	0.044	0.41	0.24
Projection A—High growth, high trade, hard financial terms:[4]						
1983	228.0	58.8	30.9	.040	.40	.23
1986	341.7	101.9	48.4	.038	.42	.21
Projection B—Low growth, low trade, hard financial terms:[5]						
1983	229.9	63.5	37.0	.048	.47	.25
1986	370.3	114.8	64.5	.053	.57	.27

[1] Excluding Trinidad and Tobago and Venezuela.
[2] Assuming price increases of 10 percent per year 1981–86.
[3] Total debt minus reserves.
[4] Average GDP growth of 6.2 percent, 1980–85; export real growth, 7 percent; import elasticity, 1 for nonpetroleum, 0.9 for petroleum; 3 percent real interest rate for private borrowing plus spread of approximately 1.5 percent; 1 percent official interest rate; 6-yr average maturity for private debt; 90 percent loans private, 10 percent official.
[5] Average GDP growth of 5.5 percent, 1980–86; export real growth, 4 percent; import elasticity, 0.8 for nonpetroleum, 0.5 for petroleum; financial terms as above.

Source: Calculations and model in author's more complete, still unpublished manuscript, "Latin American Debt: Problem or Solutions?," from which this version has been extracted.

WESTERN HEMISPHERE OIL AND GAS: NO RELIEF FOR THE UNITED STATES IN THE 1980's?

By Jerome F. Fried*

Summary

Mexico's new oil and gas wealth has stimulated thinking about a possible hemispheric solution to the energy problem of the United States. Seven Western Hemisphere countries besides the United States produce oil or gas or both in excess of their requirements. Only Mexico, Venezuela and Canada are, however, substantial exporters. It is only these three countries, with their enormous hydrocarbon reserves, which have a potential for major increases in exports of oil and gas. This would require the rapid development of Mexican oil, of Canada's natural gas and of the heavy oil resources of Canada and Venezuela.

Prospects are poor that Venezuela exports of oil in the 1980's will grow very much. It will take a decade at least before Venezuela can convert its heavy oil into a marketable product. In the meantime, it will have all it can do to maintain exports of oil at current levels.

Canada is a net importer of oil. Gradual exploitation of its tar sands is not likely to change that position over the next decade. Canadian exports of natural gas to the United States, however, are likely to increase over the coming decade—at the outside by an amount equal to 0.5 million barrels per day oil equivalent.

Mexico alone of the three major exporters has the resources to increase oil and gas exports in the 1980's. Mexican national policy, however, has limited production up to 1982 to 2.7 million barrels per day (mb/d), connoting exports on the order of 1.5 mb/d.

It is uncertain whether Mexican governments will be able to hold to this conservative policy. The external resources required to cope with Mexico's large and growing unemployment, to modernize all sectors of the economy and to meet the essential consumption needs of large numbers of Mexicans now living in poverty seem substantially larger than the foreign exchange that can be earned at the present production and export ceilings. Nevertheless, although much larger oil and gas exports from Mexico are a real possibility in the 1980's. the United States should not count on Mexican exports to the world of more than 1.5 to 2 mb/d.

I. Introduction

Discoveries since 1976 of huge deposits of oil and gas in Mexico and the existence of vast heavy oil resources in Canada and Venezuela suggest that oil and gas exports from these countries could help resolve

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America's energy problem. How strong that possibility is depends, of course, on how soon these countries could process their hydrocarbon resources into marketable product and on how much oil and gas they would be willing to export.

The importance of a substantial increase in Western Hemisphere oil and gas production does not rest primarily on their being more available to the United States than to other importing countries but because any increase in the world supply relative to world demand is beneficial to all importing countries. In most types of emergencies, oil from Mexico and Venezuela would not necessarily be markedly more available to the United States than to other countries. There are a number of reasons for this:

Mexico and Venezuela export oil to a number of countries in order to maximize their commercial bargaining power and in order to avoid excessive dependence on the United States.

The International Energy Agreement provides for sharing scarce oil supplies in the event of a cut in world supplies of 7 percent of more. Even if this were not so, the United States would want to share available fuel supplies with its allies for mutual security as well as to avoid competitive bidding for supplies and a panic run-up of prices for all buyers, including ourselves.

The international oil companies reshuffle supplies in tight situations so as to distribute the burden among all their customers on some reasonably equitable basis. However, in the special case of an Arab oil embargo targeted selectively on the United States, the availability of supplies from Mexico and Venezuela would make it much easier to shift oil around and avoid an excessive burden on this country.

The prospects that the three countries will substantially increase their production depend on conservation policy as well as on financial needs and technological and resource capacity. Policy is particularly important in the case of Mexico which is determined to export only enough oil and gas to cover the external financing requirements of its development effort. The possible range of these requirements is explored below, along with an examination of the prospects for increasing oil and gas exports from Venezuela and Canada.

II. Mexico

A. Oil

Mexico's history of oil production stretches back to 1890. In 1921, with production of 530,000 barrels per day (b/d), Mexico was the world's largest exporter and second only to the U.S. in production. After 1921, production declined, reaching 85,000 b/d in 1930. In 1937, Mexico nationalized its oil industry, confiscating the assets of the foreign oil companies and establishing the state oil company Petroleum Mexican (Pemex). Since 1937 Pemex has been solely responsible for the exploration, development, production and distribution of the country's oil resources. For Mexico, as well as for Venezuela, foreign "exploitation" of the nation's oil resources has been, and remains, a politically sensitive issue, and national control over oil development has been central to oil policy in both countries.

From 1950 to 1975, Mexican oil was produced for the domestic market, increasing from 199,000 b/d to 705,000 b/d. The rise in the domestic consumption of oil was associated with the sustained, rapid rate of economic growth in this period. Oil production did not quite keep up with demand and from 1968 through 1975 Mexico was a net importer. Throughout this period oil production accounted for some 3 percent of the gross national product.

As a result of the new oil discoveries since 1975, oil production has been rising, and Mexico has begun to emerge as a significant exporter of oil. In early 1981, exports were running at about 1.4 million barrels/day (mb/d) and production at about 2.5 mb/d.

Major new oil fields in the Southern State of Chiapas and Tabasco were discovered in 1972. Because these fields have production characteristics comparable to those in the Middle East, a very rapid build-up of crude oil production and proving up of reserves was possible by drilling a relatively small number of wells.

As recently as the end of 1973, Mexico's oil and gas reserves were put at the oil equivalent of only 5.4 billion barrels. On September 1, 1980, proven oil and gas reserves were estimated by the President of Mexico to be between 50 and 60 billion barrels of crude equivalent and probable reserves were an additional 38 billion barrels; the estimate of total possible reserves, a more speculative estimate, was raised to 250 billion barrels.[1] Mexico has joined the select ranks of oil-wealthy countries.

Of the 95 billion barrels of proven and probable oil and gas reserves, 63 billion are estimated to consist of oil and the remainder largely associated gas. An estimate of the maximum which could be produced can be made using a ratio of reserves to production of 15:1 frequently considered consistent with the efficient development of the oil fields. This ratio suggests that maximum potential rate of oil production is 4 billion barrels a year, or 11 mb/d, based on oil reserves of 60 billion barrels, a theoretical maximum rate that could be sustained for 15 years, and for much longer should the exploration program prove out a substantial portion of the reserves now estimated to be possible reserves. Actual production is likely to be substantially less.

The critical determinant of Mexico's rate of production of oil, however, is the government of Mexico's economic strategy for the 1980's, for which oil exports now represent the key external financing factor. In addition, any Mexican government must address the conservationist bias implicit in the widely shared Mexican view that its oil resources represent a patrimony which should be reserved for Mexican use now and for the future.

B. Government Economic Policy

For a better part of the past three decades Mexico achieved rapid economic growth while maintaining price stability and stability in its balance of payments. During this period Mexico shifted from a predominantly rural to a more urban society. A strong and rapidly growing manufacturing industry, presently accounting for 25 percent of GNP, has been established. With economic growth in excess of 6 percent a year, Mexico's GNP in 1979 reached $120 billion, and per

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[1] *New York Times*, Sept. 2, 1980, p. D-3.

capita income, $1,700, ranking it among the more advanced of the developing countries.[2]

Its economic performance was all the more remarkable because it was not dependent on oil production, nor especially dependent on foreign capital. Domestic savings, largely private rather than public, financed 85 to 90 percent of investment during this period. External savings, largely channeled through foreign direct investment and government borrowing in the international capital markets, financed the remainder. As measured by the current account deficit in the balance of payments, foreign investment in Mexico was of the order of 2 percent of GNP a year.

Mexican development strategy focused on areas of rapid growth, particularly capital intensive industry and specialized agriculture. Traditional agriculture, on which 40 percent of the population still depends, has been largely ignored. As a result, despite the impressive economic gains over the last three decades, the mass of the rural population continues to live on a subsistence level. Even more serious has been the increasing unemployment since 1965 as an accelerating population growth began to be reflected in a rapidly growing labor force. Currently, a population of 66 million is increasing at about 2.5 percent a year, and the labor force of 18 million, by 700,000 persons a year.[3] About 10 percent of the labor force is unemployed and an additional 30 percent is estimated to be underemployed, earning less than the minimum wage.

Rising social tensions resulted in a shift of development strategy in the administration of President Echeverria, 1970–76. The strategy sought to increase employment through higher public investment directed to the neglected agriculture sector, to low cost housing and to other social investments. It came to a disastrous conclusion. The government had to have recourse to massive deficit financing to carry out its program, and this and other factors resulted in high inflation, recession, and, by 1976, a dangerous rise in the public external debt. A broadened development approach that had become politically imperative failed because of lack of resources.

It can succeed now because of the new oil reserves. Based on expanding oil production and exports, the government is sharply increasing public investment but, this time, without undercutting private investment or provoking fears of runaway inflation and balance-of-payments crises.

The Global Development Plan of the Lopez Portillo administration calls for an 8 percent growth in GNP through 1985, with development continuing to emphasize industrial expansion. Assuming continuation of the capital-output ratio of 3:1 which has characterized the growth of Mexico's economy, investment at roughly 25 percent of GNP annually will be required to meet this goal. Mexico's rate of growth over the past two decades was on the order of 6 percent annually and was associated with an investment rate of 18–20 percent. (In 1979 the rate of investment rose to 23 percent, and the growth rate increased to about 8 percent.)[4]

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[2] "The Mexican Economy in 1980," Banco de Mexico, February 1980, and other official publications.

[3] "World Development Report, 1981," World Bank, Washington, D.C., 1981.

[4] Sources: "The Mexican Economy in 1980," Banco de Mexico, February 1980, and other official publications.

For the 1980–85 period, a sustained high rate of investment to achieve 8 percent annual growth with relative price stability appears likely. The expanded public investment programs should improve significantly the productivity and quality of life of the neglected traditional agricultural sector of the economy and improve the lot of the urban poor in housing, nutrition, health and other social services.

A sustained 8 percent growth rate will accomplish much, but it does not seem likely to keep unemployment and underemployment from rising in the 1980's. With a million or so new workers entering the labor force annually by the late 1980's, the 8 percent growth may not generate more than 700,000 new jobs each year. The Mexican government will thus be under heavy pressure to accelerate the pace of development. An earlier version of its development program, the National Plan for Industrial Development, 1979–82, had as its goal a 10 percent annual growth rate, but this goal was discarded apparently because of fear that inflation and balance-of-payments troubles might get out of hand if the economy were pushed that hard. Success in managing the current program and the imperative of absorbing more labor into productive employment may embolden the Mexican government to increase the rate of investment to achieve a higher growth rate. Alternatively, of course, the government could plan greater emphasis on rural development, rather than industrial, which would increase employment opportunities for the same capital investment. Acceleration of investment in the 1980–85 period to meet a much higher (say, 10 percent) rate of economic growth would probably result in the emergence of critical bottlenecks—ports, transportation, skilled labor—which could generate an explosive inflation.

Tables 1 and 2 present estimates and projections relevant to the 8 and 10 percent growth rates, respectively. There is nothing sacred about these projections. The intent is merely to show how, under given assumptions, Mexico's energy exports might behave if their volume were managed solely to cover the resource gap generated by a development program based on gradually meeting the current needs of the economy rather than, as in the cases of some oil-producing countries, exporting oil to earn exchange for increasing their monetary reserves or foreign investments.

C. Implications for Future Oil Exports

A sharp increase in the rate of growth of imports will be associated with higher rates of growth of GNP. Accelerating imports generated by rising investment and growth in the economy would confront Mexico with massive deficits on current account (exports minus imports of goods and services) except for the export earnings of oil. It is assumed that Mexican oil exports for 1980–85 will be large enough to finance this deficit with only relatively minor recourse to foreign borrowing. In effect, oil exports would provide the economy with the bulk of the additional "savings" that the escalation of investment requires.

Investments are projected on the basis of a capital-output ratio of 3:1. Thus, for 8 percent growth, annual rates of investment average 25 percent of GNP a year; and for a 10 percent growth in GNP, an investment rate of 30 percent is projected.

Domestic savings, excluding oil-generated "savings," are assumed to remain at their current level of about 18 percent of GNP.

Non-oil exports are projected to grow at a rate of about 7 percent a year that has characterized the growing economy over the past several decades.

Imports are projected to grow at about 12 percent a year assuming a 25 percent investment rate and an 8 percent growth in GNP (Table 1); and at 20 percent a year associated with an investment rate of 30 percent and a growth in GNP of 10 percent a year (Table 2).

The projections are in constant 1979 dollars and the price of export oil is held to $30/barrel.

TABLE 1.—MEXICO: PROJECTIONS OF NATIONAL ACCOUNTS WITH 8-PERCENT GROWTH IN GNP, 1980–85[1]

[In billions of dollars, 1979 prices]

	Actual 1979	Projected		
		1980	1982	1985
GNP	120	130	150	190
Investment	28	32	38	48
Domestic savings, excluding oil	20	23	27	34
Foreign trade sector:				
Exports (nonoil)	6	6	7	9
Imports	12	14	17	24
Net services and transfers	−2	−2	−2	−2
Current account deficit (excluding oil)	−8	−10	−11	−17
Export of oil	6	[2] +11	[3] +12	[4] +16
Percent of GNP:				
Investment	23	25	25	27
Domestic savings excluding oil	17	18	18	18
Nonoil current account deficit	6	7	7	9

[1] See assumptions and limitations on following pages.
[2] 1,000,000 bbl/d.
[3] 1,100,000 bbl/d.
[4] 1,500,000 bbl/d.

Sources: For 1979, "The Mexican Economy in 1980," op. cit., and other official publications. Projections are those of author.

TABLE 2.—MEXICO: PROJECTIONS OF NATIONAL ACCOUNTS WITH 10-PERCENT GROWTH IN GNP, 1980–85[1]

[In billions of dollars, 1979 prices]

	1979 actual	Projected		
		1980	1982	1985
GNP	120	132	160	212
Investment	28	34	48	66
Domestic savings, excluding oil	20	24	29	38
Foreign trade sector:				
Exports (nonoil)	6	6	8	9
Imports	12	14	24	35
Net services and transfers	−2	−2	−2	−2
Current account deficit (excluding oil)	−8	−10	−18	−28
Export of oil	4	[2] +11	[3] +18	[4] +27
Percent of GNP:				
Investment	23	25	29	31
Domestic savings, excluding oil	17	18	18	18
Nonoil current account deficit	6	7	11	13

[1] See assumptions and limitations on following pages.
[2] 1,000,000 bbl/d.
[3] 1,600,000 bbl/d.
[4] 2,500,000 bbl/d.

Sources: For 1979, "The Mexican Economy in 1980," op. cit., and other official publications. Projections are those of author.

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Table 1 indicates that, on the assumption that an annual growth of GNP of 8 percent a year proves sustainable, Mexico would require in 1980–85 oil exports of about 1.1 mb/d by 1982 and 1.5 mb/d by 1985. On the assumption that serious bottlenecks could be avoided and a 10 percent rate of growth is sustainable, Table 2 indicates that the amount of oil exports by 1982 would have to be about 1.6 mb/d and by 1985 would need to rise to 2.5 mb/d.

Taking the maximum range of these estimates (Table 2) and allowing for domestic consumption of oil forecast by the Mexican Petroleum Institute to rise to 1.2 mb/d by 1982, and 1.5 mb/d by 1985, oil production to meet domestic and export requirements would have to be 2.8 mb/d by 1982, and 4 mb/d by 1985. According to the latest official (Pemex) statements, Mexican oil production will be about 2.7 mb/d by the end of 1982. Decisions as to further expansion of oil production will be left to the new administration which will come into office then.

The range of oil exports that have been estimated in Tables 1 and 2, as required to balance Mexico's current account in 1980–85, have been calculated on the assumption of substantially cutting back on foreign borrowing now currently about $3 billion annually. Mexico may, however, opt to conserve its oil reserves and continue its present level of borrowing in the international capital market—an option available to it despite its sizable external debt of $30 billion, because of its oil reserves. To the extent that it follows this policy, the oil exports required would be accordingly less.

Again, if the real price of exported oil rises over the next five years, the magnitude of oil exports required to balance the foreign and investment accounts of the economy would be correspondingly reduced.

In sum, Mexico's oil exports are not likely to exceed 2.5 mb/d by 1985 and might well be substantially less. A plausible range for the 1980's would be between 1.5 mb/d and 2 mb/d. While our estimates are necessarily exceedingly crude, they appear consistent with the current thinking of the Mexican authorities.[5]

Indeed, on November 20, 1980, the Wall Street Journal (p. 5) reported that the Mexican government's new energy plan sets a limit of 1.5 mb/d of oil exports. (The plan also stipulates that no single country will receive more than half of the exported. This, as noted in the introduction, does not detract from the value of Mexico's oil and gas reserves for the United States.)

D. Conservation Policy and Oil Production

Mexico's energy strategy owes much to a strong tradition of "Mexican oil for Mexican use." The strategy is also based on other considerations: (1) All-out production for export could, in addition to intensi-

[5] The projections of Tables 1 and 2, and the conclusions on which they are based are the best we can do, and follow Mexico's official analysis, but are necessarily exceedingly rough, as are most if not all, economic models for predicting the future. We do not know what the future marginal capital-output ratio is. We can not know what will happen to consumption and domestic savings in a Mexico with a high growth rate. We can not predict what will happen to oil prices. We suspect that higher oil exports will strengthen the peso and weaken other Mexican exports. We do know that small changes in any of these factors have huge effects on the residual, in this case on the quantity of oil to be exported from Mexico.

fying inflationary pressures, lead to exaggerated popular expectations of improvement in the quality of life; (2) all-out production could lead to excessive general consumption to the detriment of needed investment in non-oil producing sectors; (3) high oil exports probably would inhibit non-oil exports, and the development of manufacturing, by strengthening the currency and making other exporting difficult; (4) restricting supply tends to increase energy prices and total revenues from oil—the chief lesson OPEC has taught the world; and (5) finally, a contributing factor may be that the conservation strategy is the only one possible for Pemex, the state oil company which is now stretched to its capacity with respect to its technical and managerial skills, manpower resources and the political tolerability of using foreign technicians and subcontractors to meet its present consumption goals.

As keenly aware of the problems of over-dependence on oil and gas revenues as the Mexicans are, it may not prove economically or politically possible for them to limit oil and gas production as they plan (2.7 mb/d and hence exports of 1.5 mb/d in 1980–1985). Under the higher investment, 10 percent average annual growth rate projection, Mexico might need to export 2.5 mb/d by 1985, a substantial amount. But, it might find it necessary and desirable to export more. A 10 percent growth rate might keep unemployment and underemployment from increasing, but it might not significantly reduce the huge backlog of unemployment and underemployment. The pressure to deal with this problem and the huge capital imports necessary for Mexico's planned development, may see import requirements much larger than those projected. At the same time foreign exchange earnings from nonenergy exports and tourism may stagnate or decline as a result of the upward pressure on the exchange rate as Mexico swings from a traditionally deficit current account to a surplus position. This happened in Venezeula and in Britain.

There is no way of predicting what energy policy the Mexican administration that comes to office in 1983 will carry out. Tradition, self-interest, nationalism, and prudence are powerful forces favoring the current policy of conserving Mexico's energy resources for future generations. The momentum of development and political exigencies, however, may force a different strategy in the mid-1980's. In its own planning the United States cannot count on this outcome, but it remains a real possibility.

III. Venezuela

Like Mexico, Venezuela has a history as an oil producer dating back to the 1920's. However, in contrast to Mexico, Venezuela remained a major producer and exporter of oil throughout the past 50 years.[6] As a result:

> In 1978, Venezuela (population 14 million) had a per capita income of $2,910, one of the highest of the less developed countries, as compared with Mexico's per capita income of $1,290.[7]

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[6] Also in contrast to Mexico, Venezuela did not nationalize the domestic subsidiaries of the international oil companies until 1975.

[7] Source: "World Development Report, 1980." World Bank.

Despite several decades of intensive attempts to diversify the economy, oil still accounts for 90 percent of exports and 25 percent of GNP. Venezuela remains vulnerable to any significant decline in oil production or in world oil prices.

Because of the depletion of existing oil fields and the failure to discover new ones, Venezuela's oil production has been declining. In 1979 production was down to 2.2 mb/d and exports to 1.9 mb/d, compared to production of 3.2 mb/d and exports of 3 mb/d in 1973.[8]

Venezuela was forced to borrow heavily in the international capital market in recent years to offset the decline in oil exports. The large jump in oil prices in 1979 brought Venezuela a temporary reprieve from the threat of economic and political instability posed by a weakening oil sector.

Venezuela's principal and, perhaps only, hope of restoring oil production and exports to former levels in this decade lies in the promising offshore deep drilling exploration now underway. The government has recently committed $3 billion to a 5-year exploration program. Current estimates are that the areas under investigation possibly hold as much as 10 billion barrels of recoverable light crude oil of a highly marketable grade.[9] This oil reserve, combined with the existing reserve of 18 billion barrels of predominantly heavy, low-grade crude, can achieve exports of some 2.5 to 3 million b/d through at least the next two decades. Current exports are 1.9 mb/d and Venezuela will have difficulties maintaining this rate since production is not rising in the face of increasing domestic demand.

Despite its promising prospects, the new oil area may not prove out. If so, Venezuela can be expected to step up its current development of the heavy oil sands reserves in the Orinoco area.

The Orinoco Heavy Oil Belt in Eastern Venezuela extends about 325 miles east-west just north of the Orinoco River with a width varying from 25–30 miles. The oil-bearing sands range in depth from 800–1,000 feet along the southern limit to slightly below 4,000 feet along the northern limit.[10]

The estimates of the amount of oil reserves in the Belt are staggering. They vary from 1 trillion to 7 trillion barrels of oil in place. The government's latest estimate is 2 trillion barrels of oil in place. The amount of recoverable oil here depends on which of the different technologies now available for extracting oil from the sands can be successfully applied. Pilot projects have demonstrated a range from 10 percent to 34 percent. At a minimum this would mean 200 billion barrels of recoverable oil. If the optimum technology is used, recoverable oil of some 600 billion barrels is possible—perhaps as much as the total of world reserves of conventional oil!

Enormous as these reserves are, producing the thick, heavy crude, imbedded in sands of considerable depth, and upgrading it to a synthetic crude oil of marketable grade, present tasks of production and refining of equally enormous difficulty. The technology of production and of upgrading the oil is at hand, though extensive preliminary testing at each site will be necessary.

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[8] Source: Ministry of Energy and Mines.
[9] "Outlook on Venezuela's Petroleum Policy," Joint Economic Committee, 1980.
[10] "Outlook on Venezuela's Petroleum Policy," Joint Economic Committee, 1980, and Memorandum on Venezuela's Heavy Oil Belt, Exxon Corp.

The large cost of transporting the thick, heavy oil to a distant refinery argues for on site and integrated production-refining facilities. The capital costs are compelling—on the order of $30,000/barrel per day of production capacity as compared to $10,000/b in the North Sea and $3,000/b in the Middle East. Thus, the installation of a million barrels per day production-upgrading operation in the Orinoco involves an investment of $30 billion. Such capital requirements are a serious constraint, even if the operation were clearly cost-effective. Yet the current world price of oil is now so high that investment in the Orinoco may have become attractive. At the current price the annual gross income from a one mb/d Orinoco oil operation would be in excess of $10 billion.

Currently, planned production in the Orinoco for this decade is largely limited to Venezuela's Cerro Novo project, a commercial integrated production-upgrading facility of 125,000 b/d capacity, scheduled to go into operation in 1988. The time from the design stage to the final completion of the plant will be at least 10 years. Additional projects, if initiated in time, might increase production from Orinoco reserves to possibly 1 mb/d by 1990.

Given the potential these production rates appear quite modest. There are several major constraints on expansion of oil production in a region of such tremendous reserves:

1. The long lead time involved from design to start up of an integrated project is 10–12 years. Much of this time is used for pilot project testing to determine the optimum technology that would assure a high recovery rate for a particular site.

Pilot projects are needed to determine the appropriate technology for developing reservoirs of considerable variation in depth and character of the oil deposits. The recovery rate of oil could vary between 15 percent and 30 percent depending on the technology. A less than optimum technology could mean the loss of billions of barrels of recoverable oil resources. The government strategy for the Orinoco is, consequently, to proceed at a conservative pace and avoid such losses. It is prepared, therefore, to postpone any major development of the Orinoco for a decade or two. Successful conclusion of its present offshore exploration of its conventional oil reserves will strengthen its determination to hold to this strategy.

2. In any case, any near term acceleration of the government's current program for the development of the Orinoco reserves may pose an unacceptable strain on Venezuela's manpower (skilled labor and managerial) and its capital resources. The Cerro-Novo 125,000 b/d project will require a 6,000 man work force over a 5-year period and the construction of considerable infrastructure in the Orinoco region to house, feed, and provide other services for the work force. A much bigger program in this decade may require some form of joint venture with foreign oil companies. This would run counter to the prevailing strong nationalistic sentiment in Venezuela against the development of the country's oil resources by foreign companies.

3. Air and water pollution pose difficulties to be resolved before a much more intensive development of the region can be undertaken.

In short, Venezuela's tar belt has much the same potential as shale oil in the United States or tar sands in Canada and has similar cost and production difficulties. Venezuela, at present, appears to favor a conservative approach to the development of its Orinoco oil resources. It is an approach that is likely to postpone any substantial production of oil from these resources until at least the mid-1990's. Venezuela is not likely to modify this approach even if it fails to discover significant conventional oil reserves over the next five years. Even should it move to a more intensive rate of development of the Orinoco, the long lead times involved would seem to preclude any significant increase in production in this decade above what is already planned.

IV. Canada [11]

Canada, the other industrial country in the Western Hemisphere, has become a net importer of oil. As shown in Table 3, Canada faces the prospect of a continuing decline of oil production and rising oil imports through the 1980's and beyond.

TABLE 3.—EXPECTED CANADIAN PRODUCTION CAPACITY FROM CONVENTIONAL CRUDE OIL RESERVES, TAR SANDS, AND HEAVY OIL VERSUS DOMESTIC DEMAND, 1978-90, SELECTED YEARS

[In thousands of barrels per day]

	1978	1980	1985	1990
Production capacity:				
Conventional	1,620	1,430	937	714
Tar sands and heavy oils	77	155	255	550
Total production capacity	1,697	1,585	1,192	1,264
Domestic demand	1,874	1,900	2,049	2,157
Import demand	177	315	857	893

Source: National Energy Board, Canadian Oil Supply and Requirements, September 1978, pp. 260, 289-294. In "The Western Hemisphere Energy System," November 1979, U.S. Senate, Committee on Energy and Natural Resources, p. 30.

Canada, however, remains a major exporter of natural gas to the U.S. In the 1970's this was on the order of 1 trillion cu. ft. a year (456,000 b/d oil equivalent). Taking account of newly discovered gas fields which still have to be proven out, Canada's recoverable natural gas resources are estimated at 104 trillion cu. ft., (equivalent to 16 billion barrels of oil). The frontier areas (Arctic Islands, the MacKenzie Delta-Beaufort Sea areas and the East Coast Off-Shore) may hold an additional 66 trillion cu. ft. (equivalent to 10 billion barrels of oil). Some Canadian companies contend that at current export prices to the United States, Canada's recoverable gas reserves are at least twice these amounts.[12]

Canada's gas resources, actual and potential, are clearly of sizable magnitude. However, as shown in Table 4, Canada's export potential is projected by the Canadian National Energy Board to remain steady for a few years and then to rise appreciably by 1985, at which time production from the new frontier area gas fields is expected to be available. The official projection shows the emergence of a declining trend after 1990. As noted above, however, more optimistic projections

[11] This section was prepared before Oct. 28, 1980, when Premier Trudeau proposed his National Energy Program for partial nationalization of Canada's oil industry. The program calls for Canadian ownership of 50 percent or more of all oil companies operating in Canada by 1990. The immediate result was a sharp drop in exploration in Canada.

[12] Speech by J. K. Gray, Canadian Hunter Exploration, Ltd., May 8, 1980, before change in Canadian policy.

exist, suggesting a further substantial increase in production if export markets were assured. It might be reasonable to suppose that over the next decade or so, Canadian gas exports to the United States might be in the range of 0.5 to 1 mb/d oil equivalent.

TABLE 4.—EXPECTED NATURAL GAS PRODUCTION CAPACITY AND DOMESTIC DEMAND OF CANADA, 1978–95

[In millions of cubic feet per day]

	1978	1980	1985	1990	1995
Production:					
Conventional areas	7,720	8,340	9,120	8,320	6,990
Frontier areas			2,220	3,090	4,020
Domestic demand	4,430	5,360	6,580	7,380	8,520
Export potential	3,287	2,980	4,759	4,022	2,490
Export potential (oil equivalent, thousand barrels)	547	497	793	670	415

Source: National Energy Board (Canada), February 1979. In "The Western Hemisphere Energy System," November 1979, U.S. Senate, Committee on Energy and Natural Resources, p. 37.

Canada's conventional oil resources, even allowing for possible new discoveries, will not be sufficient to meet Canada's domestic oil requirements. This leaves Canada's unconventional oil resources—oil sand deposits in Alberta and the Athabascan tar sands—as the only possible source of large oil exports in the future.

Canada's heavy oil resources, while not as large as those of Venezuela, are still of vast proportions—possibly as much as 1 trillion barrels of oil in place and as much as 200 billion barrels of recoverable oil that could be upgraded to light synthetic crude. The heavy oil fields have been the subject of increasing Canadian research and experimentation to establish the appropriate technology for their utilization. Limited commercial production in open pit areas that did not require sophisticated technology has already begun. As of 1978, however, total production was not more than 80,000 b/d. The National Energy Board of Canada estimate (1978) of the future production from the oil sand reservoirs puts production of synthetic crude at 550,000 b/d by 1990 and 775,000 b/d by 1995, but no significant production during the 1980's.

Expeditious development of Canada's heavy oil resources over the next 10–15 years could alter the gloomy outlook. However, there is little prospect of such development, and for very much the same reasons as apply in Venezuela—the constraints of long lead time, the magnitude of capital requirements, and a national policy of conservation of the nation's energy resources for future uses.

V. Conclusions

Besides the United States, three Western Hemisphere countries, Mexico, Venezuela and Canada, possess immense reserves of hydrocarbons. Only Mexico, however, has the potential for greatly increasing oil and gas exports in the 1980's.

Canada is now a growing net importer of oil. Despite the fact that large gas fields have been recently discovered, and more large finds appear probable, Canadian projections, which could be conservative, show gas export capacity declining after the mid-1980's owing to the shift from oil to gas for domestic consumption.

During the 1980's Venezuela may be able to reverse its declining exports of crude oil. But to do so it must be successful in its current offshore exploration program. Currently, oil exports are roughly 2 mb/d compared to 3 mb/d at the 1973 peak.

Both Canada and Venezuela have enormous reserves of heavy oil but because of the long lead-times needed for projects to process heavy oil into usable form, it will be the 1990's at least before production from this source becomes substantial. In the meantime, both countries will be hard put to maintain present levels of hydrocarbon exports.

Mexico is a different story. Already the fifth largest producer of crude oil in the world, current production of 2.3 mb/d compares with 450,000 barrels daily in 1973. Production is scheduled to climb to 2.7 mb/d by year-end, the ceiling level established for the period through 1982 when a new government takes office. This level of output would permit crude oil exports of only 1.1 to 1.5 mb/d through 1982.

It is doubtful, however, that the government's ceiling will stick even as long as 1982. Mexico's development program calls for an 8 percent average annual growth of GNP, but this level will fall short of absorbing the nearly 1 million new entrants to the labor force by several hundred thousand persons. The inability to find jobs for new entrants together with the large backlog of unemployment and underemployment may compel the central government to accelerate the development program to achieve higher economic growth despite the great risks of intensifying inflation and steeply increasing imports. It is, of course, impossible to predict what oil prices will be in the 1980's but, on the assumption of constant real prices and ten percent growth of the Mexican economy, our model suggests that crude oil exports of 2.5 mb/d by 1985 will be necessary to cover the external resource gap.

In addition, exports to the United States of excess natural gas associated with oil production could represent the crude oil equivalent of 0.8 mb/d by 1988. With current exports of oil and gas running somewhat below 1 mb/d, the increase of 2.3 mb/d should have a beneficial impact on world energy supply and security of U.S. supply, and should exercise a restraining influence on prices. (Total OPEC exports are currently less than 28 mb/d.)

A decision by Mexico to accelerate substantially its economic growth would probably require greatly increased imports to meet consumption and investment demands and to limit inflation. In this case, oil and gas exports of the order of 4 to 5 mb/d might be necessary. Mexico apparently has the reserves to sustain exports of this size for three or four decades at least. Political resistance to raising production and exports to this level would be very strong however. Not the least of reasons for this resistance is the determination of Mexican planners to build a modern diversified economy able to sustain itself long after the oil is gone, something which may be impossible if Mexico comes to depend too much on oil exports for current consumption.

Exports of oil and gas from Mexico substantially higher than currently planned are technically possible, but it would be imprudent for U.S. energy policy to assume that they will materialize. The most likely assumption is that Mexico will export no more than 1.5 to 2.0 mb/d to the world during the next 5 years.

TRADE INTEGRATION OF THE UNITED STATES, CANADA, AND MEXICO

By Sidney Weintraub*

SUMMARY

The Trade Act of 1974 was amended in 1979 to require the President to "study the desirability of entering into trade agreements with countries in the northern portion of the western hemisphere to promote the economic growth of the United States and such countries . . . " and present the findings to the Congress by July 1981 (Section 1104 of Public Law 96–39, July 26, 1979).

The main argument in favor of free trade is that protectionism has been inefficient. Canada, because of its past protectionism, has developed an industrial structure of many modest-sized plants each producing on a limited scale mainly for the Canadian market. As a result, productivity is lower than in the United States for virtually all industries. In addition, more than 50 percent of Canadian industry is foreign-owned as investors sought to get inside the trade barriers rather than serve Canada by exporting to it.

Mexico, too, has failed to develop many industries which are competitive internationally. In addition, the industrial pattern which developed failed to produce sufficient jobs to absorb all of the rapidly growing labor force. The result has been unemployment or underemployment of about 40 percent of the economically active population and a highly unequal distribution of income.

For both Mexico and Canada, bilateral or trilateral free trade would permit a reduction in protectionism without opening their markets completely to all countries, and it would provide their industries with the opportunity to compete in the large North American market without fear of protection.

The main economic arguments against free trade are that most investment in sophisticated industries would be made in the United States and that Canada and Mexico would become backwashes; the political objections are that free trade would increase the dependency of these countries on the United States.

It is not foreordained that this would be the outcome. Canada has certain locational advantages for attracting investment for a large, barrier-free North American market and Mexico has the advantage of relatively cheaper labor. Indeed, U.S. labor would fear that free trade would lead to industries running away to Mexico to invest.

Various extraneous arguments also are made for or against North American trade agreements. One is that free trade leads inevitably to political union; the evidence of other free trade agreements, and of the U.S.-Canada auto agreement, does not support this. In Mexico and

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Canada, there is concern that the trade agreement proposal is a subterfuge for the United States to obtain control over the level of oil and natural gas production. This concern has been augmented by the proposals made in the United States that there should be a sectoral agreement for energy, a North American energy common market. There is nothing inherent in a free trade agreement that need affect national control over a country's resources. In the United States, there would be concern that free trade, general or sectoral, would automatically translate into free labor movement, especially from Mexico to the United States.

In all these areas, steps beyond free trade—towards political union, free movement of labor or capital, arrangements about energy production or production and marketing in other sectors—would require separate decisions that would have to be concurred in by all the countries.

The principal impediment to free trade in North America is political. The weaker countries economically, Mexico and Canada, fear that free trade would lead to some loss of sovereignty and cultural identity. This impediment can not be overcome by intellectual argument. However, it need not prevent analysis of the potential economic benefits and costs.

I. Introduction

A common strand in Canadian and Mexican thinking is the realization of their deep economic involvement with the United States coupled with their concerns that this will lead to political domination. Both countries have taken measures to impede their economic integration with the United States and to promote national independence.

The purpose of this paper is to examine whether formal integration is possible in this milieu. The paper will neither advocate nor oppose integration among the three countries. Rather, it will examine each set of bilateral relationships and analyze those arguments which support formal integration and those which oppose it. The discussion will be mostly of economics, although in the end the political issue of national independence may be the dominant aspect frustrating formal integration.

From the earliest days after Confederation, Canada's national policy of protectionism (adopted in 1878) was inspired by a desire to build a nation independent of the United States. Canada's protectionism endured much longer than did comparable protectionism in the United States (which also was based on the desire to build national industry and a national market). During the so-called stabilizing development and shared development periods in Mexico, running roughly from the mid-1940's to the mid-1970's, Mexico sought to develop its national market based on domestic industry and agriculture protected by an extensive import licensing system.[1] This is now being moderated, but Mexico remains a highly protectionist

[1] By 1976, before Mexico began to free items from the import license requirements, 85 percent of all imports required a prior license. In value terms, the licensing requirement affected 74 percent of imports (in 1974). A. Nowicki, et al. "Mexico: Manufacturing Sector: Situation, Prospects and Policies" (Washington, D.C.: World Bank, 1979).

country, motivated largely by fear of market penetration from the United States.

Each country has taken steps to control foreign direct investment. The basic Canadian legislation is the Foreign Investment Review Act (1973); the corresponding Mexican legislation is the Law to Promote Mexican Investment and to Regulate Foreign Investment (1973). As the titles indicate, the Canadian law sets up a review process to determine the benefit to Canada of any foreign acquisition or new investment, whereas the Mexican law sets out detailed limits on foreign participation in the Mexican economy. The Mexican controls are more severe than those of Canada, but the inspiration in each case is the same: to minimize domination of the economy by large multinational corporations whose decisions are made mostly in the United States.

In each case, the concern extends to cultural nationalism. In Canada, this has involved the use of the tax system to discourage advertising in U.S. periodicals, most notably Time and the Reader's Digest, and on U.S. television which can be seen in Canada. The issue of U.S. cultural penetration takes a different form in Mexico because of the language difference. At its most profound level, Mexican intellectuals argue that a major cultural difference is that Mexicans look to their history in shaping policy and Americans to their future. Carlos Fuentes has referred to western "assassination of the past" in distinguishing between the Mexican and the western views of progress.[2] Octavio Paz has stated that what separates Mexico and the United States are what he called the submerged sides of their societies, their differences of beliefs, desires, fears, repressions, dreams. The two countries, he said, are two distinct versions of western civilization.[3]

The efforts to moderate the extent of integration with the United States have not succeeded. The United States remains overwhelmingly the dominant trading partner of each. Tables 1 and 2 show this. In 1978, the United States took 70 percent of Canada's exports and provided 70 percent of its imports. In 1978, the United States took 70 percent of Mexico's exports and provided almost 60 percent of its imports. In each case, the 1978 percentages were representative of recent years.[4] Each country relies on the U.S. capital market for much of its external borrowing needs. U.S. corporations are by far the most important foreign investors in industry and mining in each country. The number of non-U.S. nationals who crossed the border legally from Mexico to the United States during the year ending September 30, 1978 was 103 million and from Canada, 52 million.[5] In this milieu, it is hard to maintain cultural independence.

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[2] Interview article, New York Times, Jan. 9, 1980, p. 2.
[3] Unofficial transcript of remarks during the Mexico Today symposium, Washington, D.C., Sept. 29, 1978.
[4] Canadian trade data are from Statistics Canada and the Mexican data from the Banco de México's "Indicadores Economicós." In each case, the data differ from U.S. trade data.
[5] "Statistical Abstract of the United States," September 1979, p. 92.

TABLE 1.—MERCHANDISE EXPORTS BY DESTINATION, UNITED STATES, CANADA, AND MEXICO, 1978

[In percent]

	Exporter		
	United States	Canada	Mexico[1]
Destination:			
United States		70.4	70.2
Canada	19.7		1.0
Mexico	4.7	.4	
Other America	10.7	4.2	13.3
Western Europe	27.8	10.8	8.8
Japan	9.0	5.8	1.8
Rest of World	28.1	8.4	4.9
Total	100.0	100.0	100.0

[1] Preliminary. January to September only.

Note: According to statistics Canada, Canadian-Mexican figures may be understated because Canadian-Mexican trade often takes place via the United States and is recorded as trade with the United States. It is important to stress that the data in each case come from the exporting country and may differ from those of the importing country.

Sources: United States: Department of Commerce: Bureau of the Census, "FT 990/Highlights of U.S. Export and Import Trade," December 1978. Canada: "Bank of Canada Review," December 1978. Statistics Canada, Data Bank, Ottawa, Ontario, Canada. Mexico: Banco de México, "Indicadores Económicos," December 1978.

TABLE 2.—MERCHANDISE IMPORTS BY SOURCE, UNITED STATES, CANADA, AND MEXICO, 1978

[In percent]

	Importer		
	United States	Canada	Mexico[1]
Source:			
United States		70.6	58.3
Canada	19.5		1.9
Mexico	3.5	.4	
Other America	9.8	4.7	5.2
Western Europe	21.2	11.6	23.9
Japan	14.2	4.5	8.1
Rest of World	31.7	8.2	2.5
Total	100.0	100.0	100.0

[1] Preliminary. January to September only.

Note: (Totals may not add due to rounding.) According to Statistics Canada, Canadian-Mexican trade figures may be understated because trade often takes place via the United States and is recorded as trade with the United States. The source of the data is the importing country and may differ from data reported by exporters.

Sources: See table 1.

Apart from their comparable ambivalence regarding interaction with the United States, the two countries are vastly different. Canada's per capita gross national product in 1978 was $9,170 and that of Mexico was $1,290, or 14 percent as large.[6] As can be seen from Table 3, Canada's imports in 1978 were $43.8 billion (U.S. dollars); since Canada's population was then about 23.5 million, this was $1,850 of imports per capita. Mexico's merchandise imports in 1978 were $8.1 billion; since Mexico's population was then 65 million, this was $123 per capita.

While U.S. investment is substantial in each country, the scale is different; the book value of U.S. direct investment in Canada at the end of 1978 was $37.3 billion and in Mexico, $3.7 billion.[7]

Adult literacy in Mexico was 76 percent in 1975 and in Canada 98 percent. Thirty-seven percent of Mexicans in the appropriate age

[6] World Bank "Atlas, 1979."
[7] U.S. Department of Commerce, "Survey of Current Business," vol. 59:8 (August, 1979).

group were enrolled in secondary schools in 1976 contrasted with 94 percent in Canada. In 1977, 34 percent of Mexico's labor force was engaged in agriculture, leaving much leeway for exodus, while the comparable figure in Canada was 6 percent. Between 1970 and 1977, the annual average population growth in Mexico was 3.3 percent and in Canada, 1.2 percent, making for a much younger population in Mexico. Life expectancy at birth in Mexico in 1977 was 65 and in Canada 74.[8]

TABLE 3.—MERCHANDISE IMPORTS BY CATEGORY OF PRODUCT, UNITED STATES, CANADA, AND MEXICO, 1978

	In billions of U.S. dollars			In percent		
	United States	Canada	Mexico	United States	Canada	Mexico
Consumer goods	43.6	7.8	0.5	25.3	17.8	6.1
Industrial inputs and raw materials	81.7	13.5	3.9	47.5	30.8	47.8
Other manufactures, including automotive	43.5	22.1	2.8	25.9	50.5	34.8
Other	3.2	.4	.9	1.9	.8	11.3
Total	172.0	43.8	8.1	100.0	100.0	100.0

Note: (Totals may not add due to rounding.) As noted above, the sources for the data are the importing country. These data differ from those of the reporting country. In the case of Mexican imports from the United States, United States data show these as $6.7 billion in 1978 while Mexican data show them as $5 billion. The main reason for the statistical difference is the inclusion in United States data of exports for Mexican in-bond plants and their exclusion in Mexican import data on the grounds that these imports do not enter Mexico's customs territory.

Sources: United States: Department of Commerce, "U.S. Foreign Trade Annual," August 1979, pp. 19-20. Canada: "Bank of Canada Review," December 1979, pp. S127-128. Canadian dollars converted at average noon spot rates for the year, $1.1402 Canadian per $1 United States. In Canadian dollars, total 1978 imports were $49.9 billion. Percentages calculated from data in Canadian dollars. Mexico: Banco de México, "Informe Anual 1978." Data given in U.S. dollars, p. 142.

TABLE 4.—MERCHANDISE EXPORTS BY CATEGORY OF PRODUCT, UNITED STATES, CANADA, AND MEXICO, 1978

	In billions of U.S. dollars			In percent		
	United States	Canada	Mexico	United States	Canada	Mexico
Agriculture and forestry	28.2	9.6	1.5	19.6	20.6	25.4
Extractive	7.1	8.9	2.1	5.0	19.1	35.8
Manufactures	99.4	27.1	2.1	69.2	58.5	36.7
Other	8.9	.8	.1	6.2	1.7	2.1
Total	143.6	46.3	5.8	100.0	100.0	100.0

Note: (Totals may not add due to rounding.) As noted above, the sources for the data are the exporting country and the numbers differ from those given in official data of the importing country. Thus, while Mexican data show exports of $4 billion to the United States in 1978, United States data show imports (f.a.s.) from Mexico as $6.1 billion, the main reason for the discrepancy is the different treatment of exports from Mexico's in-bond plants.

Sources: United States: Department of Commerce, "U.S. Foreign Trade Annual," August 1979, pp. 17-18. Canada: "Bank of Canada Review." December 1979, pp. S124-126. Canadian dollars converted at average noon spot rates for the year, $1.1402 Canadian per $1 United States. In Canadian dollars, total 1978 exports were $52.8 billion. Percentages calculated from data in Canadian dollars. Mexico: Banco de México, "Informe Anual 1978," p. 144. Data given in U.S. dollars.

In most respects, other than national power, the economic and social characteristics of Canada are similar to those of the United States. (So, also, is the dedication to the substance of democracy.) This is not the case for Mexico. These differences between Mexico and the other two countries vastly complicate any potential three-way economic integration program.

The similarity between the United States and Canada explains why the theme of economic integration between the two countries recurs

[8] Data are from tables in annex to the World Bank's "World Development Report, 1979."

periodically. There has been no comparable analysis of economic integration between the United States and Mexico—that is, until recently, after Mexico discovered vast quantities of oil. Economic integration between neighbors who are similar economically comes into consideration naturally. Economic integration between economic unequals, neighbors or not, does not. In the case of Mexico, therefore, the political resistance to formal economic integration with the United States is reinforced by the economic inequalities.

Economic integration can mean many things. At its simplest level, it could mean doing nothing to frustrate the natural integrative impulses between the United States and the other two countries. The integrative process could go beyond that and seek some unified arrangement for particular industries and sectors, in the manner which now exists in automotive trade and defense production between Canada and the United States. Such industry or sector agreements may (or more generally do not) lead to broader formal economic integration; the U.S.-Canada automotive agreement did not lead to any further integration. Specific industry and sector analysis looking to sectoral integration will not be undertaken in this paper.

The General Agreement on Tariffs and Trade (GATT; Canada and the United States are members, and Mexico is not) contemplates two types of broad integration arrangements, a customs union and a free trade area. Sectoral integration would not be consistent with the Articles of Agreement of GATT. The United States required a waiver from the GATT to enter into the auto agreement. So did the European countries when they formed the Coal and Steel Community.

A customs union entails a common external tariff and free trade in substantially all goods among the member countries. Reaching a common external tariff requires some averaging process which, in the case of Mexico, presumably would involve a gradual lowering of its tariff rates, and in the case of the United States and Canada, presumably some raising of tariffs. For the United States to raise tariff rates after a half-century of consistently lowering them hardly would be an efficient outcome. It does not seem useful, therefore, to contemplate a Mexican-U.S. customs union at this time.

A free trade area also contemplates free trade in substantially all goods among member countries, but each can retain its own tariffs against non-member countries. It is more realistic in dealing with the three countries to think in terms of a free trade area. This would be complicated enough, without the additional problem of reaching a common tariff.

Integration could go beyond a customs union or free trade area. It could involve free factor movement (of labor and capital as well as goods), monetary union (as the European Community is now seeking to achieve), economic union, and ultimately, political union. However, none of these more thorough-going steps is essential if the objective is free movement of goods.

The bibliography appended to this paper contains many entries dealing with the theory and practice of economic integration.

Entry into a free trade area in North America would be a departure in U.S. trade policy. The United States has been the major proponent of the most-favored-nation system. However, the departure need not be in violation of the GATT. Nor would the United States be doing anything not already done by many other countries.

The GATT assumes that movement towards free trade will take place gradually. In the case of the European Economic Community, the time allowed in the basic agreement was 12 years, although the customs union was achieved more rapidly. In its original agreement with Turkey, the EEC anticipated that duties among the member countries would be eliminated over 22 years, although this plan was not put into effect.

In looking at economic integration between the three countries in North America, therefore, the issue is not one of free trade among them now, but perhaps by the end of the century. The time allowed for each country to reach free trade need not be uniform; it could be longer for Mexico, for example, than for the United States. The point at issue is whether a movement towards free trade should begin, with a timetable which is long enough to permit gradual adjustment within the countries and certain enough to permit economic actors to make decisions based on it.

II. The U.S.-Canada Relationship

Two recent Canadian examinations of the U.S.-Canada trade relationship came to opposite conclusions.

The first was the "third option" decision defined in 1972. The three options then considered by the government were: (*a*) "Maintain more or less the present relationship with the United States with a minimum of policy adjustment"; (*b*) "move deliberately toward closer integration with the United States"; and (*c*) "pursue a comprehensive, long-term strategy to develop and strengthen the Canadian economy and other aspects of our national life and, in the process, to reduce the present Canadian vulnerability.[9] The "present Canadian vulnerability" was a reference to the concentration of trade with the United States, the great impact on Canada of corporate decisions made outside Canada, the reliance of Canada on the U.S. capital market, and the perceived diminution of Canadian political independence flowing from these vulnerabilities. Nonpreferential trade agreements later were concluded (in 1976) with the European Economic Community and Japan in pursuit of the third-option policy.

What have been the results? The proportion of Canada's trade with the United States has not altered since the third-option policy was adopted. U.S. direct investment flows have remained fairly stable between $400 and $600 million a year (save for 1976, when there were special transactions involving Canadian purchase of U.S.-owned facilities in Canada). Canadian long-term portfolio issues in the United States increased from about $1 billion in 1972 to almost $5 billion in 1977 (there was an aberration in 1976, when new Canadian issues in the U.S. market spurted to more than $8 billion). Direct Canadian investment in the United States has increased substantially since the early 1970s and in 1977 was almost equal to the reverse flow.

For several years following 1976, the Standing Senate Committee (of Canada) on Foreign Affairs examined the U.S.-Canadian relationship. In its second report, published in 1978, the Committee listed

[9] Mitchell Sharp (then Canada's Secretary of State for External Affairs), "Canada-U.S. Relations: Options for the Future," special issue of "International Perspectives," (Ottawa: Information Canada, Autumn 1972).

four trade options it had considered: (*a*) "Modified tariff protection with a program of domestic remedies"; (*b*) "sectoral free trade arrangements with the United States"; (*c*) "multilateral free trade or unilateral free trade"; and (*d*) "bilateral free trade with the United States." The Standing Senate Committee stated that it would prefer bilateral sectoral free trade arrangements, but doubted that this approach would be of interest to the United States "unless it were as a first step toward bilateral free trade." Its conclusion, therefore, was to "seriously examine the benefits to be derived from free trade with the United States" as the best way to resist the gradual shift of Canadian manufacturing capacity to the United States.[10]

The issue of bilateral free trade arises periodically in both Canada and the United States because the idea has some inherent logic. Free trade has not been put into effect because it also has some dangers for the economic and political structures of both countries, particularly for Canada. The remainder of this section will examine the rationales for the two Canadian positions, for and against bilateral free trade, asking as well if free trade with Canada should be of interest to the United States.

A. *The Arguments for a Gradual Movement to Free Trade*

The position favoring the free trade option is based essentially on unifying the markets for industrial rather than for agricultural goods and raw materials. Much of the latter already moves across the two borders without serious impediment. When the results of the recently-concluded multilateral trade negotiations are fully in effect, 80 percent of U.S. imports from Canada and 65 percent of Canada's imports from the United States will enter free of duty.[11] It is to the remainder of trade, particularly for goods containing a significant amount of processing (value added) in the other country, that free trade proposals are directed.

The arguments in favor of free trade are based on three types of considerations:

1. The consequences to Canadian industry (and to Canadian income) of protectionist policies;
2. The degree of protection that Canadian exports face in entering the U.S. market; and
3. The trade and financial integration which already exists makes independent Canadian macroeconomic policies infeasible in any event and, therefore, greater integration might enhance Canadian influence on mutual policies rather than reduce it.

1. COSTS OF CANADIAN PROTECTIONISM

The central argument of Canadians who favor bilateral free trade is that protectionism has fostered a noncompetitive industry, one generally less productive than in the United States and in which wages are as high as across the border. An excellent summary of the

[10] The Standing Senate Committee on Foreign Affairs, "Canada-United States Relations, Volume II, Canada's Trade Relations with the United States" (Ottawa: Queen's Printer for Canada, 1978), pp. 120–121.
[11] "The Economist," Nov. 10, 1979, p. 125.

free trade position, as seen from Canada, is contained in the following paragraph from the report of the Senate Standing Committee:

> It is evident that in general the present high levels of tariffs are proving to be self-defeating for Canadian secondary manufacturing. The tariff combined with foreign ownership—which is itself a product of earlier tariff policy—has produced or maintained a basically inefficient industrial structure with truncated branch plants producing too large a range of goods with too short production runs for too small a market. Nor has the high tariff actually been able to protect many of these industries once their competitiveness has slipped.[12]

Canada's industry is more protected against imports than is industry in most other developed countries. There is no simple way to measure the level of protection. However, using one common technique, the weighted average tariff applied on industrial imports from most-favored-nation suppliers, the comparison between Canada and other major industrial areas after the reductions from the Tokyo Round of multilateral tariff negotiations (MTN) are in effect will be as follows:

Canada 8.7 percent;
The European Economic Community (EEC), 7.2 percent;
The United States 5.7 percent; and
Japan, 4.9 percent.[13]

The foregoing are nominal weighted average rates. Canada's average duties on raw materials were substantially lower than on semi-finished and finished manufacture, so that effective protection for processing and manufacturing was higher than the nominal protection.[14] In addition, Canada has a special regime to protect machinery made in Canada. Here, too, the story is the same; significant concessions were made in the MTN, but substantial protection will remain. Canada has an array of non-tariff measures comparable to those of other industrial countries.

The advocates of bilateral free trade then trace out the results of this protectionism along the following lines.

Industries were encouraged to establish operations in Canada, for the most part producing for the relatively small Canadian market. In those industries in which scale of production is important to high productivity, Canadian industry has been generally noncompetitive in world markets. Many of the manufacturing plants were established by foreign investors, mostly from the United States, in order to sell within the protected Canadian market. The result is that more than 50 percent of the Canadian industrial sector is foreign controlled. Canadian industry is characterized by a plethora of branch plants of U.S. parents, strung out at or near the border, producing small runs of a variety of products to satisfy the domestic market. There are exceptions to this—such as the automobile industry, for which production on either side of the border is for sale in both countries—but the description is generally valid.

There obviously were benefits from this system. Canada does have an extensive industrial structure, even if not all of it is efficient by

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[12] Senate Standing Committee, p. 116.

[13] Office of the Special Representative for Trade Negotiations, "Results of the United States Industrial Tariff Negotiations with other Major Developed Countries in the Multilateral Trade Negotiations," (Washington, D.C.: June 21, 1979, mimeograph), p. 4. Any "average" tariff level is an inexact measure, particularly when the weights used are imports, since high rates prevent imports. Canada has a significant number of high rates.

[14] The significance of "nominal" and "effective" tariff rates is discussed in the next section on U.S. protectionism against Canada.

international standards, and Canadian incomes are high by any standard. The concern is that a system that fosters noncompetitiveness is not durable. Carl Beigie has commented:

I do not know of any other country as small, in terms of its domestic market, as Canada that has such pretensions about being able to duplicate the industrial structure of the much larger economies. We produce virtually everything in this country and we do not seem to be able to decide whether we want to specialize on the one hand, or protect, on the other.[15]

The Economic Council of Canada, in its comprehensive study Looking Outward: A New Trade Strategy for Canada, noted that apart from Australia, no other industrial country seeks to rely on a barrier-free market of less than 100 million persons for its manufactures.[16]

Protection of the inefficient must adversely affect the efficient. It was noted that Canada's machinery industry has a special protective regime. However, machinery items needed for use in the resource industry are granted remission of import duties in order not to burden resource extraction. This, in turn, has the side effect of distorting the competitive position of the machinery industry. The system used to provide tariff drawbacks for imported items later reexported in a more processed form is another way in which Canada (and other countries) seeks to reduce the adverse competitive impact of import duties. However, such administrative systems have their own problems, such as calculating the amount of appropriate drawback and the interest costs occasioned by delays in making payments. The Organization for Economic Cooperation and Development (OECD) suggested recently that Canada's policy that supports industries which are not competitive at the international level should be temporary in the interest of the entire industrial structure.[17] This is precisely the position of those Canadians who favor bilateral free trade, namely, that while certain industries would not benefit, the potentially competitive industries would.

Canadian output per manhour is estimated to be about 80 to 85 percent that in the United States. These lower levels of productivity do not apply across the board—for example, they apparently do not for steel, cement, and pulp—but are most acute in industries where scale of production is important. Small motors for appliances, major electrical appliances, business forms, and petrochemicals are among the industries in which Canadian productivity has been shown to be lower than in comparable plants in the United States.[18] The advocates of bilateral free trade argue that this lower productivity is a consequence of Canada's protective system.

The competitive disadvantage of lower output per manhour can be overcome in international markets by lower wage rates. However, the evidence is that wages in Canada, including fringe benefits, are comparable to those in the United States. Were the two markets to become completely open to goods of the other, wages in comparable industries should tend towards equalization. Canada would not benefit from

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[15] Senate Standing Committee, p. 45.
[16] Economic Council of Canada, "Looking Outward: A New Trade Strategy for Canada" (Ottawa: Information Canada, 1975).
[17] Organization for Economic Cooperation and Development, Canada (Paris: OECD Economic Survey, June 1979), pp. 48–49.
[18] Senate Standing Committee, pp. 18–19.

bilateral free trade by attracting industries because of lower wage costs, but by the same token it would not suffer either. The gains and losses would derive instead from other competitive features, such as comparative productivity and locational advantage.

A concern frequently voiced in Canada relates to the low level of expenditures on research and development compared with other industrial countries. The facts are not in doubt. In 1977, Canada spent less than 1 percent of its GNP on R&D compared with more than 2 percent for the United States (whose own R&D expenditures had declined from more than 3 percent of GNP a decade earlier). The percentage of patents filed in Canada by Canadians is low compared with other industrial nations, and about 95 percent of the roughly 20,000 patents issued annually in Canada are granted to foreigners, of whom three-quarters are American. It is hard to say whether the low level of R&D is an inevitable consequence of the small size of the average Canadian manufacturing plant. Many Canadians believe that it is, citing the preference to do research in the larger home rather than in the smaller branch plant, and the fact that the capital and labor structures of the small Canadian plants leave little leeway to hire qualified engineers or scientists or to devote capital resources to R&D for a small market.[19] On the other hand, the amount of R&D done in Canada is not outstanding in the automotive industry where the U.S. and Canadian industries are integrated and where Canada can produce for a larger market.[20]

Those who advocate bilateral free trade argue that the major manufacturing areas in Canada, namely, southern Ontario and Western Quebec, have a natural locational advantage because they are closer to the prime industrial areas of the midwest and the northeast in the United States than are many regions in the United States, and that these areas in Canada would have investment advantages regarding transportation, distribution, and raw material costs. This is the opposite of the argument heard frequently in Canada that bilateral free trade would result in sophisticated manufacturing going to the United States while raw material and simple processing industries would remain in Canada.

One final aspect of Canadian trade policy merits comment. While political sovereignty is the basis for a national Canadian trade policy, the results of this policy have different effects on different parts of Canada. A high-tariff policy favors the regions where the protected industries are located at the expense of regions that produce raw materials and must purchase manufactures from a protected source. This was a North-South issue of conflict in the United States. The disparity in Canada is mostly East-West. Many Canadian provinces, and many U.S. states, undoubtedly would benefit if exchanges across their borders could follow natural economic lines rather than political boundaries.

The foregoing, in summary form, are the main arguments in favor of bilateral free trade made by Canadians who believe that current Canadian protectionism is badly conceived and cannot endure if levels of Canadian incomes are to be sustained. In a comprehensive

[19] Ibid., pp. 53–58.

[20] Simon Reisman, Commissioner, "The Canadian Automotive Industry: Performance and Proposals for Progress" (Ottawa: Minister of Supply and Services Canada, 1978), p. 232.

study advocating bilateral free trade, the disadvantages of protectionism were stated as follows:

North American protection results in higher Canadian prices and costs because of three organizational factors: the size of the firm; the level of managerial efficiency necessary to survive; and oligopolistic opportunities offered by the protected market.[21]

This first strand of the pro-free trade case is based on the alleged adverse consequences to Canada of Canadian protectionism. The second strand is based on the need to eliminate U.S. protectionism against Canada. In each country, successive rounds of trade negotiations in the GATT have reduced barriers substantially, but significant barriers remain.

2. U.S. PROTECTIONISM AGAINST IMPORTS FROM CANADA

Eliminating U.S. protection against imports from Canada is by no means as potent an argument in favor of bilateral free trade as that dealing with the consequences of Canadian protectionism. However, it is not a negligible issue either.

The importance of the protective effect of U.S. tariffs on potential Canadian exports is based mainly on the escalation that exists at higher levels of Canadian value added. Because of this, effective import protection is higher than that implied by the stated tariff.[22] Some examples cited in Canadian literature are the relative ease with which Canada can export unwrought nickel to the United States but not the processed product. The same is true for copper, and particularly for forest products. The tariff escalation issue has particular relevance for Canada because of the importance to its economy of resource-based industries.

However, the problem should not be exaggerated. After the concessions granted in the MTN are fully in effect, few nominal tariffs on goods coming from Canada will exceed 5 percent and fewer still 10 percent.[23] These nominal rates, when converted into effective rates by virtue of the duty-free access of most raw materials, can impede imports, but they are unlikely to be decisively protective in many cases.

The same is true of U.S. nontariff barriers. These, at times, have adversely affected Canadian products, again particularly processed raw materials, but are less significant than the broader issue of Canadian competitiveness. Perhaps the most publicized case of a U.S.-Canada trade conflict was the U.S. action in 1973 to impose countervailing duties against Michelin tires produced in Nova Scotia with governmental financial assistance mainly for export to the United States. Other cases dealing with subsidies and countervailing duties, import safeguards, and allegations of dumping, arise from time to time. In a bilateral free trade area, most of these issues would disappear.

It is more fruitful to look at the structure of Canadian exports to the United States than at U.S. protectionism to understand Canadian performance. From 1971–77, the average composition of Canadian exports to the United States was as follows: Food products, 4.6

[21] Ronald J. Wonnacott and Paul J. Wonnacott, "Free Trade Between the United States and Canada: The Potential Economic Effects" (Cambridge, Mass.: Harvard University Press, 1967), p. 5.

[22] Effective tariff rates or effective protection will exceed the nominal protection when the raw materials embodied in an imported product could enter duty free or at a low rate or are produced domestically but are forced to bear the higher rate of the imported good.

[23] Office of the Special Representative for Trade Negotiations, p. 17.

percent; crude materials, 19.2 percent; fabricated materials, 33.5 percent; and end products, 41.9 percent. Breaking down the two largest categories, 52 percent of the exports of fabricated materials were forest products and 65 percent of end-product exports were automotive products.[24] Apart from automotive products, the strongest area of growth in Canadian exports to the United States was in fabricated materials. This tends to underscore the importance to Canada of the tariff escalation issue. At the same time, it illustrates that Canadian export dynamism was possible in this area despite tariff escalation, which, as noted, will diminish as the MTN tariff rates are put into effect.

Another way of looking at Canadian competitiveness in relation to U.S. trade barriers is to note that the United States takes more of Canada's manufactured exports in relation to total Canadian exports than does the rest of the world. For example, 80 percent of Canada's exports of manufactures went to the United States in 1978 and 20 percent to the rest of the world.[25] The United States was the market for only 70 percent of all Canadian exports in 1978 (Table 1), that is, 10 percentage points less than for manufactured exports. The evidence, in other words, is that the United States is less closed to imports of manufactures from Canada than is the rest of the world; or, put differently, that proximity, plus investment by U.S. corporations, facilitates the sale of Canadian manufactures to the United States.

The Canadian fear of U.S. protectionism is more germane to the argument for bilateral free trade than is actual U.S. protectionism. As often as not, Canadian accounts of U.S. nontariff restrictions deal with this pessimism—that export success to the U.S. market brings its own protectionism. If there were a free trade area, export expansion would no longer be accompanied by the fear of U.S. efforts to frustrate the success.

A commitment and a schedule for movement to a bilateral free trade area would permit investors in Canada to plan for a barrier-free market of more than 250 million people rather than for one of 23 million people. The opportunity for Canada to capture a significant amount of new investment would exist.

Whether the investment that followed from the certainty of free trade would be made in Canada or the United States (or in Mexico, if there were trilateral free trade) would depend on considerations of economic efficiency rather than protectionism.

3. CURRENT INDEPENDENCE OF CANADIAN POLICY

Because of the preponderance of Canadian trade with the United States and the unification which already exists of the capital markets of the two countries, the independence of Canadian economic policy is constricted with or without a free trade area. Canadian needs sometimes are taken into account when the United States makes decisions on broader grounds; for example, Canada was exempted from the U.S. interest equalization tax in the 1960s because of its dependance on the United States for long-term portfolio borrowing. However, Canada's interests are sometimes ignored, as they were when the United States

[24] State Department Bulletin, June 1979, p. 4, based on data from Statistics Canada.
[25] Calculated from data in Bank of Canada Review, December 1978.

took significant trade and monetary decisions in August, 1971. Canadian efforts to be exempted from these decisions (particularly the 10 percent tariff surcharge) were fruitless. Canada could not be ignored as easily if there were a formal institutional structure for free trade.

The interdependence of the two economies is not restricted to such external issues as trade and foreign borrowing; it is also difficult for Canada to pursue an independent monetary policy. When interest rates in Canada diverge significantly from those in the United States for any protracted period, these inevitably are reflected in relative exchange rates. This, in turn, must affect the trading and balance of payments relationships between the two countries. Canada does not just live next to an elephant; it lives with the elephant. Efforts to resist this ménage a deux generally have been frustrated, as evidenced by the lack of change in U.S.-Canadian interdependence following the third-option policy.

This argument for a formal free trade arrangement is a straightforward one: if the two countries are to live together, wouldn't a contract protect the weaker one?

B. Arguments Against a Movement to Free Trade

In Canada, the arguments against bilateral free trade have proved to be formidable and they have prevailed. The arguments which have carried the day are a mixture of the economic and political (defined to include cultural).

The economic concern builds on the same facts as the pro-free trade case—lower Canadian industrial productivity, comparable wage rates, a small accessible market in many parts of the country—to conclude that a movement to bilateral free trade would be excessively risky. The fear is that competitive considerations would be unlikely to lead to large scale investment in Canada, but rather to leave Canada in the backwash of development. This polarization argument—that the rich get richer and the less powerful pick up the leavings—will be developed in more detail when discussing potential free trade between Mexico and the United States, but it also pervades Canadian thinking. In the automotive agreement, which by any reckoning must be considered a success in stimulating trade in both directions, Canada insisted on safeguards to deal with what it felt to be its weaker position and at each review of the agreement persisted in the view that the safeguards must be maintained. A free trade area with manifold enduring safeguards for one partner is a contradiction in terms. However, temporary benefits to a weaker partner, such as development financing or perhaps a longer period to reach free trade, are compatible with movement to a free trade area.

The Canadian concern is that adjustments to bilateral free trade, no matter how protracted the transition period, would be particularly burdensome to certain sectors and regions of Canada. The burden, it is feared, would be greatest for those industries least competitive bilaterally (or trilaterally, where the competitive situation might be radically different because of lower Mexican wage rates).

It is hard to sort out what is political and what is economic in the opposition to bilateral free trade since the two are intertwined. When the third option was chosen by the Canadian government in preference to seeking closer integration with the United States, the argument was made that economic integration would lead to political union. This is an issue to which I will return, since history refutes the inevitability of a steady progression from trade integration to deeper degrees of integration. The automotive agreement and the defense production sharing agreement between the United States and Canada have not led to further trade integration steps. This political concern of national and cultural submersion has as one of its major assumptions that the bulk of the economic benefits from bilateral free trade would redound to the United States rather than to Canada. The concern over a backwash effect is both a political and an economic fear.

The argument in favor of bilateral free trade is based on one main assumption—that competition will lead to greater efficiency and productivity in Canada while the failure to liberalize trade further will lead increasingly to Canada becoming a backwash. The argument against bilateral free trade is based on the opposite assumption: why take inordinate risks with the future of the Canadian economy and policy in the face of an uncertain outcome, particularly since present policy has provided Canadians with a high standard of living?

C. The U.S. Interest

The foregoing discussion of the U.S.-Canada relationship has concentrated on the debate in Canada on bilateral free trade. What is the U.S. interest?

In some respects, it is the same as the Canadian. If bilateral free trade facilitates making investments of optimum scale in the most fitting location without the influence of trade barriers dictating decisions, total welfare should increase. How this will be shared between the two countries is not clear and is at the heart of the issue, but there is no a priori reason not to expect the United States to benefit in some way. If those in Canada who argue for bilateral free trade are correct that stagnation will otherwise ensue, this is as much an argument in its favor for the United States because of its interest in a prosperous Canada for trading, investment, and political reasons.

The standard analysis of a free trade arrangement among developed countries looks to the welfare effects that result from trade creation from the reduction of barriers among the members and trade diversion from the discrimination against third countries. Because of the predominance of the United States in Canadian imports, the scope for diversion of trade away from third countries is limited to begin with. What diversion might actually occur for trade in either direction would depend on the levels of the respective tariffs. However, the case for free trade from the U.S. viewpoint would not rest on increasing U.S. exports by diverting the exports of others, but rather on the dynamic effects that could take place in Canada, thereby augmenting both U.S. and third country exports.

The U.S. interest in bilateral free trade thus stems from a combination of efficiency and dynamism arguments.

However, in other respects the U.S. interests are not the same as the Canadian. The United States has no need to shift from a peripheral or branch plant economy or, generally, to increase the size of a potential market by about 25 million people in order to achieve scale economies in its manufacturing plants. There would be some incentives of this type at the U.S.-Canadian border, where the interest in trade integration probably would be greatest, but less so elsewhere in the United States. In sum, the economic issues at stake for the United States in bilateral free trade are of less consequence than for Canada.

So are the political issues, since the impact on sovereignty or national determination is an issue in Canada but not in the United States. It is not clear, either, whether a free trade area with the United States would intensify or weaken the separatist tendency in Quebec.

These political and economic considerations argue that leadership in the debate on bilateral free trade should be left to Canadians, although obviously each party must formally accept (or veto) any decisions.

III. The United States-Mexico Relationship

Bilateral free trade between Canada and the United States has been a subject of discussion and analysis for some time. Most of the arguments for and against the idea can be found in Canadian as well as U.S. sources. Bilateral free trade between Mexico and the United States has not been an issue of debate in either country, and there are no authoritative Mexican sources which can be used directly to analyze the issue. The reason for this is that it was taken for granted that the economic disparities between Mexico and the United States would make Mexico a backwater as far as attracting sophisticated industries if its borders were open to the U.S. products without restrictions. For all practical purposes, this remains the Mexican position.

The political impediments to free trade with the United States are more deep-seated in Mexico than in Canada because the feeling of dependency has been more intense and conflict (such as Mexico's expropriation of foreign oil properties in 1938) relatively recent.

However, a glimmer of consideration does exist in Mexico looking to the possibility of trade integration coming gradually into existence over 20 or more years. (The use of so many qualifying words like glimmer, consideration, possibility, and gradually is deliberate.) For example, the President of Mexico, José López Portillo, told James Reston of the New York Times (February 8, 1979) that a North American common market was a dream that might eventually become a reality if the nations worked on practical problems one at a time.

A. Arguments for a Gradual Movement to Free Trade

The arguments in favor of free trade are based on the same three general considerations cited for Canada:

1. The consequences to Mexican industry (and to Mexican employment and income distribution) of past protectionist policies;
2. The degree of protection that Mexican exports face in entering the United States; and
3. The trade and financial integration which already exists between the two countries.

1. THE COSTS OF MEXICAN PROTECTIONISM

Canada has been protectionist by industrial country standards but Mexico has been protectionist by any standard. The import licensing system used to carry out Mexico's import substitution industrialization has been absolute for many protected industries. If not prohibitive, a tariff permits price competition between imports and domestic production. A quantitative limitation of imports of the Mexican type, however, is designed to prevent such price competition.[26] Whether or not this protection was necessary to establish an industrial base in Mexico (Mexican scholars generally argue that it was), it had some adverse consequences.

Mexican industry generally is noncompetitive in world markets, in part because of the pervasive protection for inputs. About half of Mexico's imports are made up of industrial inputs (see Table 3), so that this burden can be substantial. Another third of Mexico's imports are capital goods; in order to foster industrialization and at the same time not penalize potential exporters, duties on these imports frequently were waived. This encouraged capital intensive forms of production rather than forms using Mexico's ample labor supply. One researcher found that Mexican industry used 101.3 workers per million dollars of output while South Korea used 227.8.[27] In order to overcome the effects of protectionism on export competitiveness, Mexico developed an extensive system of tax refunds (they are called CEDIs, from the Spanish initials) designed to offset the pernicious effect of taxation on inputs. The system is complicated and often arbitrary.

As one examines the composition and conditions of Mexican exports of manufactures, their general noncompetitiveness becomes clear. In 1978, out of $2.9 billion of U.S. imports of manufactures from Mexico, (U.S. import data; the Mexican export figure was $2.1 billion), more than $370 million were under the U.S. general system of preferences and $1.5 billion under special provisions of the U.S. tariff schedule (Sections 806.30 and 807.00) under which the U.S. duty is paid only on the value added in Mexico. Under Mexican regulations, automotive imports into Mexico, including parts, must be matched, dollar for dollar, by exports of these products by the importing companies; that is, no net imports are allowed. In addition to these special regimes, Mexico enjoys preferential treatment in member countries of the Latin American Free Trade Association. Canada gives preferential treatment to some imports from Mexico. If all these are added together, between one half and two thirds of Mexican exports of manufactures enjoy some special treatment without which the exports might not take place. Until August 31, 1976, when the Mexican peso was devalued by more than 80 percent, an overvalued currency compounded the export problems created by import protectionism.

One result of the policy of import substitution as practiced in Mexico has been unemployment and underemployment of about 40 percent among Mexico's economically active population.[28] Mexico in recent

[26] A careful analysis of Mexico's past protectionism is Gerardo Bueno, "The Structure of Protection in Mexico," in Bela Balassa, ed., "The Structure of Protection in Developing Countries" (Baltimore, Md.: Johns Hopkins Press, 1971) pp. 169–202.

[27] Susumu Watanabe, "Constraints on Labour-Intensive Export Industries in Mexico," "International Labour Review," vol. 109 (January 1974), pp. 23–45.

[28] Saúl Trejo Reyes, "La politica laboral," in Gerardo Bueno, ed., "Opciones de Politica Economica en México Después de la Devaluación" (Mexico, D.F.: Editorial Tecnos, 1977), p. 150.

years has been unable to provide jobs for about half of the roughly 700,000 persons who annually enter the labor market. The problem of labor absorption will continue to be intense well into the future because almost half of Mexico's population is 15 years old or less.

The Mexican industrialization model also must be given much of the blame for the inequalities in Mexican society. Mexico's income distribution is one of the most unequal in the world, particularly among middle-income developing countries,[29] and the distribution of education, health, and housing services is similarly distorted.

This pattern of development prejudiced agricultural and mining growth, which had to pay much of the cost of subsidizing industry. Despite high overall economic growth rates, Mexico has needed the escape valve of emigration of its youth to find jobs in the United States, some legally and other illegally, some permanently and some temporarily. The beneficiaries of protectionism have not been the 40 percent of the population which still lives in areas of 2,500 persons or less, and certainly not the unemployed or underemployed. Indeed, the beneficiaries probably consist of a minority of the population.

The consequences of protectionism sketched in above do not necessarily call for bilateral free trade. However, they do suggest that changes in Mexico's protectionism are required, a point on which most Mexican economists are agreed. The opportunity exists for shifting away from the rigid import substitution model followed in the past because of the revenues Mexico will receive from hydrocarbon exports. Some change has taken place. Import license requirements have been eliminated for many (not all) products since 1976. An industrial development plan covering the period 1979–1982 (the end of the López Portillo administration)—1990 has been adopted. The peso was devalued in 1976, which should have an export-promoting effect (although since then the peso/dollar rate has been kept fairly steady despite the higher level of inflation in Mexico than in the United States).

However, Mexico's dedication to import liberalization is, at best, lukewarm. After participating in the Tokyo Round of multilateral trade negotiations and obtaining concessions that would have provided ample leeway to protect industries, Mexico decided in March 1980 not to join the GATT. The reasons for the decision were as much political as economic. The opposition came both from interests benefiting from the present protective system and groups fearful that trade liberalization would increase Mexico's dependence on the United States. This is not an optimistic augury for bilateral free trade.

The options available to Mexico are reminiscent of those adumbrated in Canada by its various study commissions. These include: maintaining the present system, with modifications to eliminate its worst effects; substantial trade liberalization on a multilateral basis; or deliberately seeking closer economic ties with the United States on the ground this is where Mexico's natural advantages lie. The advantage of multilateral liberalization is that it might reduce Mexican trade reliance on the United States; or it might not, just as Canada's "third option" did not in practice. The advantage of regional free trade is that it would go further over time towards free trade with a

[29] Hollis Chenery, et al. "Redistribution with Growth" (London: Oxford University Press. for the World Bank, 1974), p. 8.

limited group of countries while still permitting protection against imports generally; and do this with a definite time schedule that would facilitate planning and investment decisions by private entrepreneurs.

Would Mexico attract industrial investment for supplying the larger North American market if there were a definite schedule to reach free trade? If so, would it be in areas of some sophistication, or would the outcome be that Mexico would become a supplier of raw materials and simple, labor-intensive manufactures while the United States produced most other industrial goods? The answers are uncertain. The arguments against bilateral free trade will be discussed later. What follows are some bases for belief that Mexico might benefit from bilateral free trade.

The main advantage Mexico would enjoy is its lower wages; this could compensate in many industries for lower productivity. This, as already noted, is not an advantage Canada would enjoy in bilateral free trade with the United States. Over time, if the free trade arrangement worked, wages in the United States and Mexico should tend to equalize, but this is decades away at best, and would signify that the free trade arrangement had worked. The investment in Mexican assembly plants, most of them along the border but some in the interior, demonstrates the attraction of low wages for industries with high labor content, such as textiles, apparel, and electronics.

Because of the abundant availability of oil and natural gas, Mexico has a resource advantage, as well as a labor-cost advantage, in the production of petrochemicals. Much of its steel industry is younger and could be modernized further, probably more readily than that in the United States. Assembly need not be just of simple manufactures. If investment in the automotive industry could be made with the prospect not just of the limited Mexican market but of the North American market, Mexico might be more attractive than the United States because of its lower wage rates. In each case, this is speculation based on some, but not exhaustive, research. The point of this speculation is that it need not follow that one large market would concentrate industrial production in the North (the United States) and raw material production in the South (Mexico), any more than this pattern holds today for the lower 48 states of the United States.

There could be impediments to this pattern of production if Mexico limits industrial investment by non-Mexicans. Bilateral free trade does not require the free flow of capital, but the effects of the integration would be more pervasive if this were the case. However, even without freedom for foreign direct investment, many of the investment patterns discussed above could occur, although probably more slowly.

The movement across borders of the other factor, labor, already occurs on a large scale. Just as a free trade area does not require the free movement of capital, it does not require the free movement of labor. The free movement of goods is an imperfect alternative to free movement of labor and capital (factor movement). However, like the movement of capital, the arrangement would be more efficient if labor could move freely. These separate kinds of decisions on factor movements will be discussed later. Prime areas for investment in the interior of Mexico do not enjoy the proximity to the large U.S. market that parts of Canada enjoy. However, the distances are not great and transportation facilities, including transport by sea, do exist between Mexico and the United States. Over the time period contemplated for the gradual movement to free trade, these could be improved.

To summarize briefly, if emotionalism and nationalism in Mexico permitted, a gradual movement to a large bilateral or North American free market for goods is one way Mexico could approach the solution to its most pressing problems of employment and income distribution. It is by no means the only way, but it is a feasible option for Mexico.

2. U.S. PROTECTIONISM AGAINST IMPORTS FROM MEXICO

Many of the points discussed on U.S. protection against imports from Canada apply also to Mexico. Mexican authorities have complained that the escalation in U.S. tariffs limits Mexican exports with higher value added.[30] However, the evidence to support this contention is not convincing; and the tariff reductions of the MTN will make this argument even less valid in the future. What the evidence indicates, as discussed above, is that Mexican exports of manufactures enjoy benefits in the U.S. market which are not reciprocated by Mexican concessions to the United States.

The United States does apply different rates of duty at different seasons on imports of fresh fruits and vegetables from Mexico (and elsewhere) in order to protect U.S. producers during their prime marketing time. This presumably has some limiting effect on Mexican exports, but not much since export timing can be planned. More germane has been the harrassment to which Mexican exporters of these fresh fruits and vegetables, especially tomatoes, have been subjected over the years. These have involved marketing orders which tend to prejudice the sale of the vine-ripened product which Mexico sells and favor the warehouse-ripened tomato marketed by the main U.S. growing area in Florida, efforts to standardize package sizes which are not suitable for the vine-ripened tomato, Congressional hearings on U.S. inspection standards which stray into straight protectionism, and anti-dumping petitions by the U.S. growers. The export of tomatoes and other fresh fruits and vegetables is not a trivial issue for Mexico. Tomato exports to the United States in 1978 were $161 million. The number of Mexicans employed in the growing and exporting of tomatoes and related crops is about 100,000. However, tomato imports into the United States have not been cut off, and Mexico has captured between 40 and 50 percent of the market during the season (which runs from November through June).

The most severe U.S. non-tariff barrier imposed against exports from Mexico is the limitation on imports of cotton, wool, and man-made fibers, textiles, and products. The bilateral agreement between the two countries seeks generally to limit the increase in imports of these products to between 5 and 6 percent a year. This agreement is one of many into which the United States has entered under the umbrella of the international multi-fiber agreement. The agreement clearly limits Mexican exports of these products, but other agreements do the same for other exporters, many of whom are more efficient

[30] For example, see the Mexican assertions on this score in the joint communique of February 16, 1979 issued after President Carter's visit to Mexico. Department of State Bulletin, Vol. 79: 2024 (March 1979), p. 60.

producers than Mexico. If there were no U.S. import limitations, it is not clear that Mexico would be the main beneficiary. This is a point worth stressing. A bilateral free trade agreement which eliminated trade barriers only for Mexico among developing countries would assure that the benefit in textile and apparel trade would accrue to Mexico whereas multilateral free trade would provide no such assurance to Mexico.

As with Canada, a major Mexican concern is the fear that export success will breed U.S. protectionism. As was the case with Canada, Mexico sought and was refused exemption from the 10 percent surcharge imposed by the United States on dutiable imports between August and December 1971. A bilateral free trade agreement would eliminate this fear of U.S. protectionism.

3. CURRENT INDEPENDENCE OF MEXICAN POLICY

The dependence of Mexico on the United States for its exports of goods and services and for borrowing cuts two ways, both in favor of and against bilateral free trade. Anti-gringo feelings are endemic in Mexican intellectual circles and are ubiquitous in the Mexican press. Interdependence is viewed by many as a code word for U.S. hegemony; what many Mexicans seek is an escape from what they consider their country's excessive dependence on the United States. In this view of the bilateral relationship, the inevitable dependence resulting from proximity and asymmetry in economic power is not a basis for supporting bilateral free trade, however beneficial this might be to Mexicans in an economic sense, but to strive instead for more independence. Some of this striving is chimerical. For example, the border industries have flourished because there is a natural mutuality of interest between northern Mexico and the United States. Temporary workers move across the U.S. border by the hundreds of thousands and millions because there is a mutuality of interest between the Mexican worker and the U.S. employer.

Mexico may now be in a better position to diversify its export markets than in the past because of the growing importance of oil. The existence of oil in Mexico has tended to reduce the bargaining asymmetry which has existed between the two countries. Indeed, it was oil which in the first instance stimulated the U.S. interest in potential free trade with Mexico.

The case in favor of bilateral free trade which flows from the mutual dependencies of the two countries is that a formal relationship will give each country some voice in the trade policy decisions of the other. This voice need not cover such vital aspects of Mexico's economic life as the pace of oil and gas exploitation, or the marketing of the products, but rather deal with Mexico's import protectionism. From the Mexican viewpoint, bilateral free trade would make its voice greater than it now is on U.S. trade decisions. As with Canada, the argument can be made that bilateral free trade will increase Mexico's authority vis-a-vis the United States rather than diminish it.

B. Arguments Against a Movement to Free Trade

The arguments in Mexico against bilateral free trade are both political and economic. The political opposition is formidable, so much so that it almost certainly would preclude any concurrence in Mexico to an agreement at this time. The point needs no belaboring. It is so deeply rooted in Mexican history and in the Mexican psyche that it can be altered only with time or as the result of some cataclysmic event that transforms attitudes. In Europe, it took several wars to change German and French attitudes from animosity to cooperation. However, the existence of political emotion need not preclude intellectual debate on the economic merits of the idea.

The economic opposition in Mexico to bilateral free trade also is deeply held, although probably less emotionally felt. It is based on the thesis elaborated first, almost 25 years ago, by Gunnar Myrdal that free trade between rich and poor will result in the poor area becoming what he called a "backwash." [31] The Myrdal analysis has been amplified since by others with respect to the polarization which occurs in economic development between rich and poor regions of the world or within countries. The reason it is believed that polarization will take place is that the infrastructure for industrialization—skilled labor, an entrepreneurial group, good transportation and communication facilities, the existence of many industries that can supply inputs and others which can take the output of an industrial plant, and a congenial bureaucratic structure—exists in more advanced areas to a greater extent than in more backward areas. In addition, in a geographically limited free trade area, some trade will be diverted from the cheapest world source goods to the partner country or countries, thus entailing a burden for the importing country. This cost can be accepted if the benefits are equitably shared among the free trade partners and not borne inordinately by the weaker partner(s). It has been precisely this inability to work out a sharing of the benefits that has prevented the success of most free trade agreements among developing countries.

This same argument of the inevitability of polarization under conditions of free trade has contributed to protectionist policies and import substitution industrialization in many developing countries. "Free trade is for the economically powerful" is a familiar theme among intellectuals in developing countries.

Whether the backwash thesis necessarily would hold during a 20-year transition to bilateral free trade is unclear. Some of the reasons why it might not in the case of Mexico and the United States were given earlier. In addition, it might not hold if the exchange-rate relationship favored the trade of the economically weaker country. There are some experiments now in train between countries with substantial economic disparities, such as between Ireland and Greece and the other countries of the EEC, although these disparities are now as great as between the United States and Mexico.[32]

Finally, one politico-economic concern that Mexico might have is that under bilateral free trade, there could be a drift in loyalties in northern Mexico from Mexico City, with which the natural economic ties are not great, to the United States. This drift need not follow from these economic relationships—they have not weakened national sovereignty in the smaller countries of the EEC which rely on larger member countries for markets for their goods—but could if the center in Mexico did not distribute national benefits broadly.

[31] Gunnar Myrdal, "Economic Theory and Under-Developed Regions" (London: Duckworth, 1957).
[32] According to the World Bank "Atlas, 1979," preliminary per capita GNP ratios in mid-1978 were the following: West Germany : Ireland, 2.8 : 1 ; West Germany : Greece, 2.9 : 1 ; United States : Mexico, 7.5 : 1.

C. The U.S. Interest

In many respects, the U.S. interest in bilateral free trade with Mexico is similar to that with Canada. Bilateral free trade could promote efficiency of production in both countries. (It could also divert trade of third countries, and if diversion dominated, world efficiency would be diminished. Because of the current level of market integration which exists between the two countries, the danger of diversion is minimized.) The United States has a national interest in fostering economic stability in Mexico and in promoting Mexican prosperity (if only because this enlarges the market for U.S. goods, but the motives run deeper than this) and bilateral free trade would be desirable if it facilitated achievement of these objectives.

In other respects, the Mexican relationship is very different from that with Canada. The most significant of these differences stems from Mexico's underdevelopment and the lack of job opportunities for its large and growing labor force. Mexico's choice of an industrialization strategy is Mexico's business, but what Mexico does (or does not do) has an impact on the United States, particularly in the form of persons streaming across the border without documents in search of work. At present, Mexico is unable itself to solve its employment problem, and the solution which results is to export the problem to the United States. Whether or not it is advantageous to the growth of the U.S. economy to have these workers available (there is evidence that it benefits the growth of the U.S. economy as a whole, but probably at the expense of impacted groups within the United States, and there is great uncertainty about the long-term effects of this migration in both countries), the need for an escape valve to relieve internal pressure in Mexico largely removes this decision from U.S. control. Mexico is able to exercise its sovereignty in directing its economy but only by removing a significant element of U.S. sovereignty relating to the size and composition of the U.S. labor force.

Another important difference is that the Canadian market for U.S. goods already is impressive while the market in Mexico is small by comparison. However, the potential market in Mexico is greater than that in Canada.

The resistance in the United States would be greater for free trade with Mexico than with Canada. The low-wage advantage that Mexico enjoys signifies that its labor-intensive industries, such as textiles and apparel and perhaps others like automobile assembly, would grow at the expense of workers in these industries in the United States. It is precisely these labor-intensive industries, in which workers in the United States have limited mobility, that are in the vanguard of U.S. protectionism. U.S. workers would be concerned that low wages in Mexico would stimulate runaway industries leaving the United States in order to use the Mexican labor pool. The previous section discussed the elements of probable Mexican opposition to bilateral free trade with the United States. Segments of the U.S. population might well exhibit even greater opposition, less on political and more on economic grounds. As with Mexico, the answers to this opposition by those who favor bilateral free trade would have to deal with the potential benefit for the entire U.S. society and the ability to deal with particular hardships because the long period of transtition to free trade would permit gradual adjustment. This may not be convincing to those asked to bear the main burden of U.S. adjustment.

Finally, as with Canada, the potential for achieving advantages of scale would be greater for Mexico under bilateral free trade than they would for the United States where the market already is vast. The major countervailing benefit for the United States would be in the dynamism that could be generated in Mexico if bilateral free trade helped Mexico to overcome its employment problem and correct the extreme nature of its income maldistribution.

IV. Trilateral or Bilateral Free Trade?

Looking to trilateral free trade both simplifies and complicates the issue compared with potential free trade between the United States and either of the other two countries, particularly Canada. The simplifying aspect is that political sensitivity in Canada might be attenuated were Canada one of three partners rather than formally in bed only with the elephant next door. The same might be true to Mexico.

The complicating feature is that a negotiation with Canada alone, which would be complex in any event, might become completely bogged down if Mexico were added. The per capita income and wage equivalence between Canada and the United States make their trade integration a less sensitive issue in the United States than would a scheme that involved Mexico as well. The Senate Standing Committee in Canada opposed the trilateral approach, using the following reasoning:

> The European parallel might suggest that it would be wise to proceed from the first to establish a North American free trade agreement to include Mexico and the countries of Central America. The Committee disagrees. It will be difficult enough to negotiate a free trade arrangement with the United States, without further complicating the task. However, it should be understood that any agreement reached should be open to accession subsequently by third countries, just as the European common market provided for expansion.[33]

The bilateral trading relations between Mexico and Canada are not now profound. This can be seen from Tables 1 and 2, which show Canadian trade with Mexico at between one-thirtieth and one-seventieth of that with the United States. This relationship would intensify if Canada and Mexico were part of a free trade area.

Expanding the free trade area to Central America and the Caribbean is not considered since this would complicate the analysis and add small countries more disparate economically with the United States than is Mexico. Mexico is an economic giant to these countries, just as the United States is to Mexico. However, the point made by the Senate Standing Committee on Canada is worth keeping in mind, that any free trade agreement reached, bilateral or trilateral, can be kept open for expansion.

The potential long-term U.S. interest in unifying markets is greater with Mexico than with Canada while the present and near-term interest is greater with Canada. It may be that whatever U.S. interest may exist in market unification with Mexico is best pursued by indirection, by confining free trade negotiations (if any) to Canada at present while allowing the debate to percolate for a time on the idea of free trade with Mexico.

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[33] Senate Standing Committee, p. 123.

It does not seem fruitful to try to resolve these issues in the abstract. If the free trade idea prospers, it can take either negotiating form, bilateral or trilateral, and the precise form an initial negotiation might take need not unalterably prejudice the ultimate form.

V. False Issues

Canadian officials have stated explicitly in the past that one reason for their opposition to bilateral free trade with the United States is that this would lead inexorably to political union. The historical record does not support such a contention. Free trade, particularly a customs union, can be a precursor to political union; the Zollverein was in Germany. However, this is rare. The European Free Trade Association, the Latin American Free Trade Association, the Andean Group, the Central American Common Market, the customs union in East Africa, never led beyond free trade (to the extent that even this succeeded) and, indeed, never contemplated going further. This last point is an important one. Further steps beyond free trade require further separate decisions. The European Coal and Steel Community was a precursor of the European Economic Community because the original six members wanted it that way. There is no inevitable step-by-step process, from sector agreement, to general free trade, to monetary or economic union, and to political union. The issue is a false one.

In Mexico, an issue which is perhaps as sensitive as potential political union is that the United States seeks bilateral free trade mainly as a device or subterfuge to obtain leverage over Mexican oil and gas production. The suspicion did not arise without stimulation from the United States. Several presidential candidates and legislators in the United States have advocated a North American common market for energy using the reasoning that Mexico has available supplies and the United States would provide a secure market.

This, too, is a false issue. There is nothing inherent in a free trade area which would give the United States the authority to dictate the level of hydrocarbon production in Mexico or the markets to which the products are sent. Should the two countries wish to reach long-term agreements for the purchase of oil and gas, this is a decision they can make whether there is a bilateral free trade or not. U.S. tariff and nontariff barriers are not at issue in hydrocarbon sales; they are the heart of the matter in bilateral free trade.

Indeed the U.S. interest is served by Mexican oil production no matter where it is exported. Any exports relieve pressure on the world supply-demand relationship.

Bilateral or trilateral free trade need not involve free factor movement. The free movement of goods is a substitute of sorts for the free movement of labor and capital, and has proved easier to accomplish in practice. Few of the free trade arrangements that exist in the world have included free factor movement. It has not been achieved as yet in Western Europe, although it is an objective of the EEC. Free factor movement need not arise if the countries do not wish it to arise.

On the other hand, economic integration would be more complete if there were freedom of factor movement. Labor moves in great numbers from Mexico to the United States despite the lack of any formal agreement to do so (perhaps as much as 10 percent of the Mexican labor force seeks employment in the United States [34]), but the conditions under which this would take place would be more advantageous to Mexico if this movement were legal. If it were legal, the United States would not find itself in the awkward position of witnessing wholesale violation of its laws and at the same time not wishing to carry out its laws.

In the case of capital, the investment to take advantage of what would be a larger market could be made more efficiently if restrictions on equity positions permitted to foreigners did not exist in any of the three countries. With respect to the free movement of labor, the greatest sensitivity would exist in the United States; in the case of free capital movement and unhindered direct investment, the greatest sensitivities would be in Canada and, particularly, Mexico. Complete freedom of capital movement is unlikely to be agreed to in the first instance even if bilateral free trade were accepted. Neither would free movement of labor.

It is worth repeating that energy union, partial economic union involving free factor movement, monetary union, economic union, and political union, need not accompany or follow free trade. In each case, these steps can be taken if the parties so wish, but each would require a separate decision that would not be obtained easily.

VI. Effects of Integration on Relations With Rest of World

Both Canada and Mexico have as a conscious policy the desire to diversify their trade and economic relations in order to reduce reliance on the United States. The United States, as a world power, has trading and economic interests that are world-wide in scope. Would these interests and objectives be prejudiced if the three countries entered into a free trade arrangement?

To a certain extent, yes. Mexico would lose some of its aura in the third world if it were moving towards free trade with the very country that is the target of most third world demands. Canada's ties with the Commonwealth would be further attenuated. The United States would have to explain to other developing countries (in Latin America and elsewhere) why they could not be given preferential trade treatment in the U.S. market in the same manner as Mexico. These tend, in each case, to be political costs, such as a Mexican loss of political leverage in the third world where it has been active in recent years, or the need by the United States to explain why a relationship with Mexico is different from one with other developing countries. (One could only assume that European countries could have no grievance against a thoroughgoing free trade area in North America.)

In other respects, international objectives of the three countries need not be prejudiced if they entered into a free trade agreement. There would be some tendency to divert trade away from third countries to the member countries, and in a static sense this might frustrate Canadian and Mexican efforts at trade diversification. However, as already stated, given the existing predominance of the United States in their trade, the scope for further diversion is constrained. Moreover, if free trade did result in dynamic gains in effi-

[34] Mexico's economically active population is about 15 million. If Mexicans illegally in the United States number, say, 3 million, the percentage would be closer to 20 percent. The ebb and flow of illegal workers seems to number more than 1 million a year.

ciency, the total trade of Canada and Mexico should expand, so that in absolute terms their trade with third countries need not suffer. The countries of the EEC have increased their trade with each other since the formation of the customs union, but they have not ceased to be formidable world traders at the same time. The same could occur for the three members of a North American free trade area.

One political comment is worth making with regard to relations with third countries. In each case, international influence rests primarily on domestic economic strength. Mexico's influence does not flow from sponsorship of United Nations resolutions, but from its economic growth, its competitive ability in world markets, the size of its market, and, today, its availability of oil. Canada is influential not from Commonwealth membership, but again (to the extent it wishes to be influential) from the state of its economy and society. The perceived loss of U.S. international influence is largely a result of relatively poor economic performance in past decades. If free trade did succeed in enhancing economic growth and national welfare in each of the three countries, this simultaneously would augment their international political influence. The potential for growth enhancement is probably greatest for Mexico and smallest for the United States.

The thesis being argued is that while free trade would involve some alteration of objectives in each of the three countries, this should not be determining. The more salient question reverts to first premises: will free trade work to improve their economic efficiency and growth? If it will, relations of each country with the rest of the world need not suffer since third country trade need not be unduly prejudiced. In addition, the long transition to free trade would permit gradual adaptation by the member countries and others to the changed situation.

VII. Conclusions

The purpose of this essay has not been to advocate but rather to analyze the arguments for and against North American free trade. Five conclusions deserve stress:

1. The potential benefits are substantial for both Canada and Mexico. Economic advantages for them would come from the trade creation flowing from the gradual removal of tariff and non-tariff barriers and the ability to plan for investment in plants of optimum size. Such investment could take advantage of a large market in which there is assurance that success will not breed protectionism. The potential benefits to the United States from economies of scale are negligible since there is no constricted internal market as there is in the other two countries.

2. There are potential economic costs to free trade for each of the countries. These are that there will be a backwash ("hewers of wood and drawers of water") effect in both Canada and Mexico; and in the United States, that industries would run away to Mexico to take advantage of cheap labor.[35]

3. These downside economic risks have been taken so much for granted until now—particularly in Canada and Mexico—that prospective gains hardly get a full hearing. Any analysis of the economics

[35] One recent example supporting this point is the criticism directed against the Ford Motor Company by Senator Howard Metzenbaum of Ohio because Ford was considering building a new plant in Mexico to supply small engines for use in subcompact U.S. cars. Wall Street Journal, Feb. 22, 1980, p. 2.

of free trade in North America must take explicit account of the adjustment possible over an extended time period. This transition could be long enough to cushion shocks.

4. When all is said and done, the case in favor of North American free trade must rest on the premise that each of the three countries would be better off economically than they would be without free trade and share reasonably equally in the benefits. A respectable argument can be made that this would be the outcome. The argument in favor of limiting free trade to North America is based on the assumption that none of the three countries is prepared to accept global free trade.

5. The opposition to free trade would be formidable on political grounds in each of the countries—so much so in Mexico that it has precluded any debate of the economic benefits. The fear of Mexico and Canada is the political analogue of economic polarization, that formal economic integration with the United States would lead to their political subservience. This is an intuitive and not an intellectual argument since subservience does not require a formal free trade agreement. Indeed, a case can be made that the surest way to avoid subservience is to strengthen the Canadian and Mexican economies through freer trade. The political fear in the United States is similarly emotional—that free trade will lead to free migration of labor and the United States would then be swamped by cheap, alien labor.

A debate on the pros and cons of U.S.-Canada free trade has been going on in both countries for years, and it is likely to continue, intensifying and diminishing depending on internal Canadian developments. There has been no comparable debate in Mexico on U.S.-Mexican free trade, and it would be useful to stimulate this, not just in government but among scholars, businessmen, and labor leaders. The purpose of this analysis is to stimulate such debate in all three countries.

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U.S. IMMIGRATION POLICY

By Joyce Vialet*

Introduction and Summary

Two dominant trends are apparent in the development of U.S. immigration law and policy. First, the focus of immigration law since the 1920s has been on the Eastern rather than the Western Hemisphere. Second, our immigration law has been shaped primarily by domestic rather than by foreign policy considerations. However, we appear to have reached the end of an era in the development of our immigration law. A recasting of U.S. immigration law and policy is a likely possibility during the 1980's, with at least an equal concern for the two hemispheres, as well as an equal weighting of foreign and domestic policy considerations.

The major source of legal immigration to the United States has shifted in the last two decades from Europe to North and Central America and Asia. Immigration from North and Central America increased 43 percent during the period 1967–1976 compared to 1956–1965. The increasing number of legal immigrants plus the unknown but considerable number of undocumented aliens entering the United States are indicative of the pressure for migration from other countries in this hemisphere.

In 1979, the Interagency Task Force on Immigration Policy identified 21 countries which have contributed heavily to both legal and illegal migration, 13 of which are located in the Western Hemisphere: Canada, Mexico, Costa Rica, El Salvador, Guatemala, Honduras, Nicaragua, Colombia, Ecuador, Peru, the Dominican Republic, Haiti, and Jamaica. Major "push factors" underlying present and probable future demands to immigrate to the United States include high population growth rates, rapidly developing economies, and strong ties with this country. "Pull factors" include the availability of employment here at wages considerably higher than those available at home.

The discussion of the impact on the United States focuses primarily on the economic impact of undocumented aliens. The Interagency Task Force on Immigration Policy reported that less than 200,000 immigrants have entered the U.S. labor market annually since 1965, accounting for only 5 to 8 percent of the increase in the labor force. Undocumented workers are believed to have considerably greater impact. Some argue that they compete successfully with U.S. workers in the lower wage, secondary labor market and depress the wages and working conditions in occupations where they are present in large

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numbers. Others contend that they take jobs U.S. workers do not want and generally play a useful, albeit illegal, role in the U.S. economy.

The available information indicates that undocumented aliens are more likely to pay taxes than to participate in tax-supported service and benefit programs. They are believed to send considerable amounts of money to their home countries, particularly Mexico. While this contributes to the problems associated with an adverse balance of payments, it also constitutes an indirect form of foreign aid.

Present immigration policy is undergoing a comprehensive review by the U.S. Select Commission on Immigration and Refugee Policy, a 16-member Commission established for this purpose by Public Law 95-412 and scheduled to report to the President and the Congress by March 1, 1981. It seems probable that at that time the Congress will undertake a major review of U.S. immigration law and policy. Factors which are likely to be taken into account in the reformulation of immigration policy are varied and complex, and include current levels of legal and illegal migration, population growth in both the United States and other countries in this hemisphere, projected labor force needs, foreign policy considerations, energy needs, and social and cultural factors in the United States.

There is increasing pressure for a more restrictive immigration policy than our current one, largely on the grounds that there are limits to the number of people the United States economy and society can optimally accommodate. However, others argue that it seems unlikely that we can stop those who are truly determined to come here, short of measures which we are unwilling to take. This argument holds that it would be wisest to attempt to divert this migration into legal channels, in order to make it as beneficial as possible in terms of both U.S. domestic needs and harmonious relations within the Western Hemisphere.

Overview of Current Immigration Law

The basic U.S. law governing immigration and naturalization is contained in the Immigration and Nationality Act (8 U.S.C. 1101 et seq.). Enacted in 1952, it has been frequently and substantively amended over the years. The most recent and among the most significant amendments were those contained in the Refugee Act of 1980, enacted on March 17, 1980 (Public Law 96-212; 94 Stat. 102).

The Refugee Act repealed the ideological and geographic limitations which had previously favored refugees fleeing Communism or from countries in the Middle East. The term "refugee" is now defined by the Immigration and Nationality Act as a person who is unwilling or unable to return to his country of nationality or habitual residence because of persecution or a well-founded fear of persecution on account of race, religion, nationality, membership in a particular social group, or political opinion. In addition, the law authorizes Federal assistance for the resettlement of refugees.

The Carter Administration was unwilling to classify as refugees the approximately 125,000 Cubans and 15,000 Haitians who had recently entered the United States through Southern Florida. Instead it sought special legislation to meet the needs of these groups, which was not enacted. The legal status of the recent Cuban and Haitian entrants remains unsettled.

The number of immigrants admissible annually to the United States is regulated by a worldwide ceiling, a 20,000 per-country limit, and a six-category preference system equally applicable to all independent countries in the world. Until recently, the worldwide ceiling was 290,-000. Under the 1980 amendments, it was reduced to 270,000, not including refugees. Under this worldwide ceiling, each independent country is restricted to a maximum of 20.000 immigrant visas, a number reached in recent years only by Cuba, Korea, Mexico, and the Philippines. Territories and possessions of independent countries are limited to 600 visas annually.

Numerically restricted immigrant visas are distributed according to a six-category preference system which gives priority to family members and those with needed skills. Additionally, there are several categories of immigrants which are exempt from numerical restrictions. Most exempt immigrants are the immediate relatives of U.S. citizens, defined by the law to include the children and spouses of U.S. citizens and the parents of U.S. citizens age 21 and over. These plus refugees adjusting to immigrant status outside the numerical limits account primarily for the discrepancy between the total number of immigrants entering the country and the worldwide ceiling. This discrepancy has frequently been considerable in recent years due to the large numbers of Cuban and Indochinese refugees.

Sources of Legal and Illegal Immigration

The major source of legal immigration to the United States has shifted from Europe to North and Central America and Asia. This trend is clear, first, from an examination of table 1, comparing immigration during the 10-year periods 1956–1965 and 1967–1976. During the latter decade, North America, including Mexico, Cuba, and the West Indies, led all other regions with 1,507.434 immigrants. While this number was augmented by the flow of Cuban refugees, Mexico accounted for one-third of the total, with 550,964 entrants, in what appears to be a continuing trend. The total figure for North American immigration represented an increase of 43.4 percent over the previous decade.

TABLE 1.—IMMIGRATION BY COUNTRY OF BIRTH, FISCAL YEARS 1956–65 AND 1967–76

Country of origin	1956–65	1967–76	Percent change
Total	2,878,153	3,883,219	+34.9
Europe	1,400,051	1,016,110	−27.4
Austria	23,227	6,915	−70.2
Czechoslovakia	22,587	17,804	−21.2
Denmark	14,155	6,337	−55.2
France	41,110	21,631	−47.4
Germany	309,762	89,211	−71.2
Greece	46,696	129,076	+176.4
Hungary	57,878	15,546	−73.1
Ireland	71,023	18,601	−73.8
Italy	197,261	200,279	+1.5
Netherlands	48,853	12,994	−73.4
Poland	86,809	43,968	−49.4

TABLE 1.—IMMIGRATION BY COUNTRY OF BIRTH, FISCAL YEARS 1956-65 AND 1967-76—Continued

Country of origin	1956-65	1967-76	Percent change
Portugal	28,977	122,306	+322.1
Romania	13,530	16,980	+25.5
Spain	17,191	37,773	+119.7
Sweden	20,850	8,262	−60.4
Switzerland	18,254	9,253	−49.3
U.S.S.R	26,428	21,356	−19.2
United Kingdom	248,650	147,135	−40.8
Yugoslavia	40,238	61,833	+53.7
Other Europe	66,572	28,850	−56.7
Asia	224,342	1,052,688	+369.2
China and Taiwan	43,445	166,480	+283.2
Hong Kong	5,965	45,608	+664.6
India	5,416	115,800	+2,038.1
Indonesia	18,425	5,723	−68.9
Iran	5,161	21,984	+326.0
Iraq	2,756	16,291	+491.1
Israel	13,070	20,350	+55.8
Japan	48,931	44,068	−9.9
Jordan and Palestine	7,088	24,849	+250.6
Korea	16,361	166,422	+917.2
Lebanon	4,308	18,003	+317.9
Philippines	27,621	270,078	+877.8
Syria	2,194	9,795	+346.4
Thailand	1,098	32,184	+2,831.1
Turkey	9,345	18,866	+101.9
Vietnam	986	22,811	+2,213.5
Other Asia	12,172	53,367	+338.4
Africa	22,924	63,978	+179.1
Egypt	6,986	25,966	+271.7
Nigeria	677	4,787	+607.1
Rhodesia	500	602	+20.4
South Africa	3,171	5,536	+74.6
Uganda	82	2,283	+2,684.1
Other Africa	11,508	24,804	+115.3
Oceania	11,916	30,207	+153.5
Australia	6,270	13,733	+119.0
Other Oceania	5,646	16,474	+191.8
North America	1,050,983	1,507,434	+43.4
Canada	321,682	138,945	−56.8
Mexico	419,770	550,964	+31.3
Barbados	3,506	16,413	+368.1
Cuba	132,267	302,638	+128.8
Dominican Republic	40,047	121,818	+204.2
Haiti	13,154	56,387	+328.7
Jamaica	14,853	130,404	+778.0
Trinidad and Tobago	3,646	59,728	+1,538.2
Costa Rica	12,868	11,778	−8.5
El Salvador	11,156	19,006	+70.4
Guatemala	9,003	19,098	+112.1
Honduras	11,685	13,316	+14.0
Nicaragua	12,841	7,129	−44.5
Panama	17,688	16,500	−6.7
Other North America	26,817	43,310	+61.5
South America	167,772	212,778	+26.8
Argentina	35,269	25,699	−27.1
Brazil	16,444	14,770	−10.2
Chile	10,191	10,107	−.8
Colombia	46,955	60,665	+29.2
Ecuador	22,620	43,361	+91.7
Guyana	2,135	23,029	+978.6
Peru	16,825	16,265	−3.3
Uruguay	2,023	6,159	+204.4
Venezuela	8,218	5,677	−30.9
Other South America	7,092	7,046	−.6
Other countries	165	24	−85.5

Source: U.S. Interagency Task Force on Immigration Policy, Staff Report, March 1979, p. 124.

This is dwarfed by the increase of 369.2 percent in Asian immigration, from 224,342 during 1956–1965 to 1,052,688 immigrants during 1967–1976. However, the Asian increase clearly reflects the liberalization of the immigration law regarding Asia in 1965. Western Hemisphere immigration, in contrast, has increased in spite of the adoption of a numerical ceiling on immigration from this hemisphere as of July 1, 1968. European immigration fell 27 percent in 1967–1976 compared to the previous 10-year period, and was exceeded by both North America and Asia.

The statistics on apprehensions of illegal entrants are another dramatic indication of the pressure for immigration from the Western Hemisphere. Apprehensions exceeded 1 million each year during 1977, 1978, and 1979. Approximately 90 percent of those apprehended have been Mexicans, but this is generally believed to be primarily a reflection of the concentration of INS law enforcement personnel on the United States-Mexican border. Additionally, the apprehension statistics measure arrests rather than individuals, and are believed to include a large but unknown number of multiple arrests of the same people.

The most frequently used estimate of the percentage of Mexicans among illegal migrants is 60 percent. Other countries in the Western Hemisphere sending large number of illegal migrants include those in the Caribbean and Central America, as well as Colombia, Ecuador and Peru.

According to a recent preliminary review by the U.S. Census Bureau of studies of the illegal population in the United States, "there are currently no reliable estimates of the number of illegal residents in the country or of the net volume of illegal immigration to the United States in any recent past period." [1] However, the authors are willing to offer "cautious speculations" to the effect that: (1) The total number of illegal residents in the United States is almost certainly below 6 million, and may be only 3.5 to 5 million; (2) because of the high degree of return migration, the Mexican component is almost certainly less than 3 million, and may be only 1.5 to 2.5 million; and (3) because they tend to stay, the non-Mexican component makes up a larger share of the illegal population than is commonly believed.[2]

It should be noted that these, too, are speculations, with no firmer base than some others that have preceded them. The figure of 3 to 6 million appears to be a widely accepted current estimate of the illegal population, allowing for seasonal fluctuations.[3] However the final word is that we do not know. The Census Bureau paper concludes:

> Researchers and policymakers will have to live with the fact that the number of illegal residents in the United States cannot be closely quantified. Therefore, policy options dependent on the size of this group must be evaluated in terms which recognize this uncertainty.[4]

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[1] Siegel, Jacob S., Jeffrey S. Passel, and J. Gregory Robinson, Preliminary Review of Existing Studies of the Number of Illegal Residents in the United States. Washington, U.S. Department of Commerce, Bureau of the Census, January 1980 (Rev.), p. 18.

[2] Ibid., pp. 19–20.

[3] For example, U.S. Interagency Task Force on Immigration Policy, Staff Report. Washington, U.S. Departments of Justice, Labor, and State, March 1979, p. 30.

[4] Siegel, et al. (1980), p. 20.

Pressures for Migration

A comprehensive analysis by the U.S. Government of the subject of immigration was completed in March 1979 by the Interagency Task Force on Immigration Policy. This group consisted of the Secretary of State, the Attorney General, and the Secretary of Labor, with staff assistance from the Departments of State, Justice, and Labor as well as from other agencies.

In a discussion of the "push factors" underlying present and probable future demands to immigrate to the United States, the Interagency Task Force on Immigration Policy identified 21 countries which have contributed heavily to both legal and illegal migration, of which 13 are located in the Western Hemisphere. They are Canada, Mexico, Costa Rica, El Salvador, Guatemala, Honduras, Nicaragua, Colombia, Ecuador, Peru, the Dominican Republic, Haiti, and Jamaica.[5] The Interagency Task Force noted that the countries selected tended to have in common the following characteristics:

High population growth rates;

Rapidly developing economies in which GNP has increased markedly while overall income redistribution has lagged;

Strong ties to the United States through foreign assistance, foreign investment, American defense involvement, or territorial contiguity; and

Concentrations of their natives in the United States which serve to attract additional migrants as well as to ease the adjustment of these newest arrivals.[6]

Population growth was identified as a factor of particular importance. With the exception of Canada, all the countries in the Western Hemisphere had grown rapidly since 1960 with continued high growth rates projected until the year 2000 (table 2). This past and projected population growth is translated into actual and projected labor force participation in table 3.

TABLE 2.—ACTUAL AND PROJECTED POPULATION OF SELECTED COUNTRIES

[Population in millions]

	Population, 1960	Population, 1978	Projected population, 2000	Percentage increase, 1978–2000
Western Hemisphere:				
North America:				
United States	180.6	218.4	264.4	21.1
Canada	17.8	23.6	31.6	33.9
Mexico	34.9	66.2	121.6	83.6
Central and South America:				
Costa Rica	1.1	2.1	3.2	53.6
El Salvador	2.6	4.3	8.1	86.9
Guatemala	3.7	6.6	12.3	86.2
Honduras	1.9	3.1	7.0	121.8
Nicaragua	1.4	2.4	5.0	102.7
Colombia	14.1	25.7	37.4	45.2
Ecuador	4.3	7.3	13.1	77.3
Peru	10.8	16.8	30.2	76.6
Caribbean:				
Dominican Republic	3.0	5.1	8.3	63.4
Haiti	3.5	4.9	8.3	69.9
Jamaica	1.6	2.1	3.5	66.4

Note: Statistics prepared by the Population Reference Bureau at the request of the Office of Population, Agency for International Development.

Source: Interagency Task Force on Immigration Policy (1979), p. 222.

[5] U.S. Interagency Task Force on Immigration Policy (1979), p. 220. The countries in the Eastern Hemisphere are Nigeria, India, Iran, Korea, Philippines, Thailand, Greece, and Italy. Statistical information in the following discussion is limited to the Western Hemisphere countries.

[6] Ibid., p. 221.

TABLE 3.—ACTUAL AND PROJECTED LABOR FORCE PARTICIPATION FOR SELECTED COUNTRIES

	Percentage of population			Percentage increase in proportion of population of working age, 1978–2000
	Below age 15, 1978	Of working age		
		1978	2000	
Western Hemisphere:				
North America:				
United States	23.2	65.8	65.9	0
Canada	26.4	65.1	65.7	1
Mexico	47.1	49.3	59.1	19
Central and South America:				
Costa Rica	41.1	55.2	66.6	20
El Salvador	46.4	50.3	60.1	19
Guatemala	43.6	53.1	57.7	8
Honduras	47.7	49.8	52.2	4
Nicaragua	48.0	48.9	52.4	7
Colombia	44.1	52.7	66.5	26
Ecuador	46.0	51.2	61.4	19
Peru	44.0	53.0	58.9	11
Caribbean:				
Dominican Republic	47.5	49.3	66.7	35
Haiti	40.4	55.5	61.7	11
Jamaica	42.8	51.9	62.5	20

Note.—Statistics prepared by the Population Reference Bureau at the request of the Office of Population, Agency for International Development.

Source: Interagency Task Force on Immigration Policy (1979), p. 226.

A major effect of population pressure on already saturated labor markets is migration—frequently to the United States, where wages are higher. The Interagency Task Force notes that, "Per capita incomes are widely used to indicate the rough magnitude of differences in standards of living or economic welfare between nations." [7] Table 4 compares per capita income in the countries in the Western Hemisphere under discussion with that of the United States; only Canada is comparable.

TABLE 4.—GNP PER CAPITA FOR SELECTED COUNTRIES

	1976 U.S. dollars	Average annual growth (percent) 1960–76
Western Hemisphere:		
North America:		
United States	7,890	2.3
Canada	7,510	3.5
Mexico	1,090	3.0
Central and South America:		
Costa Rica	1,040	3.4
El Salvador	490	1.8
Guatemala	630	2.4
Honduras	390	1.5
Nicaragua	750	2.4
Colombia	630	2.8
Ecuador	640	3.6
Peru	800	2.6
Caribbean:		
Dominican Republic	780	3.4
Haiti	200	.1
Jamaica	1,070	1.9

Source: Interagency Task Force on Immigration Policy (1979), p. 229.

In company with many others who have studied the subject, the Interagency Task Force concluded, "The relatively low per capita incomes of sending nations, juxtaposed with the availability of jobs

[7] Ibid., p. 228.

and higher per capita incomes in the United States, explain why the United States is a popular destination for persons from developing countries." [8] A key factor, of course, is the availability of these higher paying jobs. Migrants, particularly from countries in close proximity to the United States, are believed to come here primarily to obtain employment and to escape poverty for themselves and their families, as well as to meet apparent employment needs in this country. The impact of the illegal migrants on the U.S. labor market is discussed below.

Illegal Immigration and the U.S. Labor Market

Considerably more attention has been devoted during the past decade to the impact of illegal, as compared to legal, migrants on the U.S. labor market. This is explained in part by the fact that legal immigrants are generally believed to have less impact. The Interagency Task Force on Immigration Policy reported that less than 200,000 immigrants have entered the U.S. labor force annually since 1965, accounting for only 5 to 8 percent of the increase in the labor force. Further, the immigrants' occupational makeup has closely resembled that of the total U.S. labor force during this period. The Interagency Task Force concluded, "From these two facts it seems highly probable that the impacts involved have been relatively small and they have been spread rather evenly over all occupations." [9] This contrasts with the Task Force's view of illegal migration, summed up as follows:

> Illegal immigration, like the lawful variety, increases the size of the total economy and produces economic benefits for most residents of the United States. However, since illegal migrants are believed to be predominantly low-skilled, the wage rates and job opportunities of low-skilled resident workers are adversely affected.[10]

The great majority of illegal or undocumented aliens either enter the United States surreptitously in search of jobs, or violate the terms of their temporary entry visas by accepting unauthorized employment. The economic motivation of illegal aliens is one of the few aspects of the issue about which there is universal agreement. There is less agreement about the number and nature of the jobs they hold, and about their impact on the U.S. labor market and economy.

The evidence suggests that illegal aliens compete successfully with U.S. workers in the lower-wage, secondary labor market, and that they tend to depress wages and working conditions in occupations and areas where they are present in considerable numbers, most notably in the Southwest. The most systematic examination to date of illegal aliens in the U.S. labor market is the March 1976 study conducted for the U.S. Labor Department by David North and Marion Houstoun.[11] The North/Houstoun study was based primarily on interviews with 793 apprehended illegal aliens, all of whom had been employed in the United States for at least 2 weeks prior to their apprehension by the U.S. Immigration and Naturalization Service (INS).

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[8] Ibid., p. 231.
[9] Ibid., p. 271.
[10] Ibid., p. 272.
[11] North, David and Marion Houstoun, "The Characteristics and Role of Illegal Aliens in the U.S. Labor Market: An Exploratory Study," March 1976. Washington, Linton and Co., Inc.

Regardless of region of origin or previous employment experience, most of the illegal aliens in the North/Houstoun sample "were employed in the secondary sector of the U.S. labor market; i.e., most were employed in low-wage, low skill, low-status jobs." Fewer than one-quarter were employed in skilled jobs, and the majority of these (16 percent) were craft workers. More than three-quarters of the study group were in unskilled and semiskilled jobs, regardless of their educational and occupational attainments in their native countries. A significant number worked longer hours and were paid lower hourly wages than U.S. workers similarly employed. Almost one-quarter of those to whom the question applied appeared to have been paid less than the minimum wage.

Mexicans made up approximately 60 percent of the North/Houstoun sample. Mexican illegal immigrants are believed to be young adults, primarily but not exclusively male; poorly educated; primarily of rural origin; economically motivated; and likely to send a significant proportion of their U.S. earned income home to dependents. Other researchers, most notably Wayne Cornelius of the University of California, have described Mexican illegal migration as being heavily characterized by a temporary seasonal pattern.

The undocumented alien of the East Coast and, to a lesser extent, many other metropolitan areas, appears to be predominantly the non-Mexican visa violator, frequently from the Caribbean or Central America. He or she is generally better educated and more likely to have family ties than the Mexican who crosses the border illegally. Non-Mexican illegals apparently are present, and certainly are apprehended, in fewer numbers than the Mexican illegals; they also appear more likely to be holding higher paid, more attractive jobs. The limited information available specifically on non-Mexican aliens indicates that they are somewhat more successful than Mexican illegals in terms of wages and jobs status, and considerably more successful in avoiding apprehension by the INS.

Other studies have generally corroborated North and Houstoun's findings regarding the low wages and occupational status of illegal aliens in this country. For example, wage data collected by INS on 48,000 illegals apprehended during January through March 1975 indicated that two-thirds of them were earning under $2.50 an hour, and less than 5 percent earned $4.50 or more. Accordingly, illegal aliens are believed by some to be in direct competition with the young, the blacks, and members of other minority groups who are currently experiencing the highest unemployment rates.

On the other hand, Wayne Cornelius argues that domestic unemployment and illegal immigration are not as directly related as is frequently assumed in discussions of the labor market impacts of illegal workers. Quoting:

> The point of departure for public policymaking, with respect to both domestic unemployment and illegal immigration, should be a recognition that the two phenomena are not related to one another in a simple supply-and-demand situation. We must accept the fact that there are certain kinds of jobs—even in an advanced technological society—which most native-born Americans will not do, even at substantially higher wages, because of the nature of the work itself and/or the limited prospects for upward mobility which it offers. Moreover, it is not in the interests of many disadvantaged Americans to take these jobs, which would clearly limit their long-term income and growth potential.

> For generations, the American public has been led to believe that a restrictive immigration policy is necessary to achieve full employment. . . . In fact, there is no evidence whatsoever that "tightening up low-wage labor markets" through a restrictive immigration policy would be highly beneficial to the "structurally unemployed" among the U.S. labor force.[12]

There has been increasing controversy about the extent to which undocumented aliens displaced U.S. workers. Cornelius and others have argued that in many instances undocumented workers take jobs Americans do not want, particularly when the option of welfare is available. Cornelius notes further that undocumented workers are heavily concentrated in small businesses, many of which are dependent on them for survival. The extent to which undocumented workers depress the wages and working conditions of U.S. workers has also been disputed, as has the nature of their overall impact on the U.S. economy.

Impact of Illegal Migrants on Tax-Supported Service and Benefit Programs

Undocumented aliens are barred from participation in the major Federal public assistance programs, including Supplemental Security for the Aged, Blind, and Disabled (SSI), Aid to Families with Dependent Children (AFDC), Medicaid, and the Food Stamps program. All are restricted by Federal law or regulation to U.S. citizens, aliens lawfully admitted for permanent residence, and to other aliens permanently residing in the United States "under color of law," including specified categories of refugees.

The opportunity for fraudulent participation in public assistance and service programs clearly continues to exist. However, in the opinion of a number of observers, undocumented aliens are often reluctant to participate in such programs even if it is not clearly illegal for them to do so. Julian Samora wrote in 1971 that, "The wetback will avoid relationships with institutions generally." [13] If this line of reasoning is correct, presumably undocumented aliens would be unlikely to participate in government programs on a fraudulent basis.

Even less information exists about the impact of undocumented aliens on tax-supported service and benefit programs than about their impact on the labor market. The Domestic Council Committee on Illegal Aliens observed:

> Allegations of heavy illegal alien use of tax-supported income transfer programs are common. An examination of these programs shows that the majority depend on characteristics such as old age, female head of household, or disabled for eligibility. Present information shows that illegal aliens are unlikely to be making heavy use of such programs due to very different personal characteristics. Our tentative conclusion is that the welfare use issue is overdrawn. However, final judgment is dependent on better information delineating the characteristics of the illegal population.[14]

In direct contradiction to the assumption that undocumented aliens constitute a drain on tax-supported services and programs, North and

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[12] Cornelius, Wayne. Mexican Migration to the United States: Causes, Consequences, and U.S. Responses. Cambridge, M.I.T. Center for International Studies, July 1978, pp. 70–71.

[13] Samora, Julian. Los Mojados: The Wetback Story. University of Notre Dame Press, 1971, p. 97.

[14] U.S. Domestic Council Committee on Illegal Aliens, Preliminary Report, December 1976, p. 214.

Houstoun found that the illegal aliens they interviewed were far more likely to have participated in programs that involved the payment of taxes than they were to have been consumers of such programs or services.[15] Thus, 77 percent of their respondents had Social Security taxes withheld; 73 percent had Federal income taxes withheld; and 44 percent had hospitalization payments withheld. The use of tax-supported health, education, and welfare programs was significantly lower. Except for hospitals and clinics, used by 27 percent of the respondents, no other tax-supported program was used by more than 4 percent.

The authors note that their respondents were "typically young male workers, . . . not those of a population likely to receive income transfer payments." The available information indicates that the typical undocumented alien is a young male worker in search of a job, although this information may be biased by INS's concentration on apprehending males.

Despite some caveats, North and Houstoun concluded that the major impact of undocumented aliens in this country was probably on the labor market, rather than on public service and benefit programs. This finding was qualified by the observation that the direct and indirect impact of undocumented migrants who settle permanently in this country will be "more far-reaching and profound" than that of those here temporarily, and will include more use of public services.

Payments Sent to Home Countries by Undocumented Aliens

The amount of money sent to home countries by undocumented aliens has important implications for U.S. domestic and foreign policy. Money sent home by aliens to their native countries contributes to the problems associated with an adverse balance of payments. However, it also constitutes an indirect form of foreign aid. By all reports the amounts involved are substantial, particularly as far as Mexico is concerned.

North and Houstoun found that out of an average gross weekly wage of $120, their study group sent home an average of $105 a month.[16] The Mexican group reported both the lowest weekly wages and the highest monthly sums sent home. They also reported the heaviest family responsibilities in their home country. The Mexican group was supporting an average of 5.4 dependents outside the United States. In contrast, the other Western Hemisphere illegals were supporting an average of 3.6 dependents outside the United States, and the Eastern Hemisphere aliens were supporting 1.8 dependents abroad.

North and Houstoun tentatively estimated that $1.5 billion annually may be sent by illegal aliens in the United States to Mexico, assuming that there were 1 million Mexican workers employed in the United States, and that the average figure of $129 a month reported by the Mexican illegals interviewed reflected the monthly average for all.

This figure, the authors note, is considerably higher than the unpublished estimate by the Department of Commerce's Bureau of Economic

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[15] North and Houstoun. The Characteristics and Role of Illegal Aliens in the U.S. Labor Market, March 1976, p. 142.
[16] Ibid., p. S–6.

Analysis. The Commerce Department's estimate of person-to-person remittances for 1974 was $73.9 million, and included remittances from all individuals in the United States (excluding only legal and illegal commuters), to all individuals in Mexico, including U.S. citizens.

FOREIGN POLICY CONSIDERATIONS

With the exception of the issue of refugees, which has always been considered as having a major foreign policy dimension, interest in immigration has tended to focus primarily on the domestic ramifications. Thus, the Domestic Council Committee on Illegal Aliens noted in late 1976:

> With the possible recent exception of Mexico, the control of illegal immigration has not been an item of concern to U.S. policymakers in the governance of our relations with sending countries. The State Department's country policy papers, which outline U.S. policy goals for the major sending countries, do not in any case cite illegal emigration as an issue although several accord priority to establishing effective visa issuing processes.[17]

However, during the past 5 years there has been an increasing sensitivity to the foreign policy considerations applicable to immigration, and particularly to illegal migration to the United States from other countries in this hemisphere. Reasons for this include the importance of bilateral relations with Mexico, recognition that Mexico may become a major source of oil and gas, political pressure from the Mexican-American community, and a growing realization that economic conditions in the major sending countries are an essential component in the motivation of the illegal migrants who seek employment here.

Quoting again from the Interagency Task Force on Immigration Policy:

> With certain exceptions, immigration is not a critical issue in our bilateral relations with other countries. The major exception is Mexico, where immigration policy and practice are fundamental issues between our two countries. There are several reasons for this: our history, proximity, interdependence and, at present at least, the enormous flow of illegal aliens from Mexico into the United States.[18]

They also note that the issue of illegal immigration is of "principal significance" in our relations with countries in the Caribbean, as well as several other Latin American countries from which large numbers of illegal migrants come. These include the countries of Central America, and Colombia, Ecuador, and Peru in South America.

In the view of the Interagency Task Force, emigrant remittances play a major role in the local economies of the Caribbean to an extent which "makes our immigration policies a key variable in their development." With regards to Colombia, Ecuador, and Peru, the Interagency Task Force concluded that the legal and illegal "immigration flows raise questions about the most effective forms of development assistance, rather than questions of overall bilateral relations."

In general, those who are most concerned about what they see to be the potential negative effects of closing off the "safety valve" for the unemployed provided by immigration to the U.S. tend to be less

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[17] U.S. Domestic Council Committee on Illegal Aliens, Preliminary Report, December 1976, p. 56.

[18] Interagency Task Force on Immigration Policy (1979), p. 285.

in favor of what they view as restrictive measures aimed at markedly curtailing the flow of this migration. Instead, they tend to recommend that the migration issue be viewed in the context of other foreign policy issues and priorities, including the desirability of a politically and economically stable Mexico and Caribbean area.

Conversely, those who are most concerned with the domestic impact, particularly the effect of undocumented workers on the labor market, are most apt to urge the adoption of measures aimed at decreasing the illegal flow of migrants. These include increased border enforcement and penalties for the employment of undocumented aliens.

Summary: Current Issues and Future Prospects

In general, a consensus has been reached that our entire immigration policy is in need of rethinking and change. The current law reflects the fears of the early 1950's and the hopes of the mid-1960's. However, the steady flow of illegal migrants during the past decade would appear to signify that the law is not an effective response to the pressures and needs of the current period.

Factors which are likely to be taken into account in the formulation of future immigration policy, particularly as it relates to the Western Hemisphere, include current levels of legal and illegal migration, population growth in other countries in this hemisphere, projected labor force needs in the United States, foreign policy considerations, and energy needs.

Using Mexico as an example to illustrate the interaction of these needs and their specific potential relevance to immigration policy, Mexico's labor force is expected to increase by more than 100 percent over the next 2 decades. The long-term prognosis is hopeful; the population growth rate has slowed from 3.5 percent in 1972 to an estimated 2.9 percent in 1978.[19] However, the short-term future pressure on the Mexican labor market is evident from the fact that almost half of Mexico's population is under 15 years of age. An estimated 600,000 to 800,000 new workers will be entering the Mexican labor market each year for the next 10 years. Current unemployment and underemployment in Mexico are estimated at 30–40 percent.

At the same time, a shortage of unskilled labor in the United States has been predicted for the 1980's. Quoting Michael Wachter:

> The bottom line of the labor supply analysis is that, by 1985–1990, the number of young workers in the labor force will be declining. The population in the younger age group will be falling and their participation rates, as opposed to the unprecedented increase during the 1970s, will be largely flat. Comparing 1970–1977 with 1985–1990 indicates a demographic transition of immense proportions. The changing outlook for immigration policy is largely a function of the twist in the demographic age structure of the labor force.[20]

Reasoning from the above demographic projections, Wachter predicts "that illegal aliens will be in even greater demand in the United States in the 1980s than they are today."[21] He argues that a new immi-

[19] Nagel, John S. Mexico's Population Policy Turnaround. Population Bulletin, v. 33, December 1978, pp. 3, 35.
[20] Wachter, Michael. The Labor Market and Immigration: the Outlook for the 1980's. U.S. Interagency Task Force Staff Report Companion Papers. U.S. Departments of Justice, Labor, and State, August 1979, p. 181.
[21] Ibid., p. 203.

gration policy is needed to control the flow of migrants entering the country:

> It should be recognized that the United States needs a new immigration policy regardless of whether one believes in easing or tightening restrictions on the number of new entrants. In the current situation and with the coming demographic twist [leading to a shortage of unskilled male workers], pressures for increased illegal immigration will grow substantially. As more illegal immigrants become permanent "non-members" of society, the potential for social, economic and political disruption will grow. The United States must adopt a workable immigration policy; that is, it must control the size of the flow of immigrants and legalize the process.[22]

Clark Reynolds comes to similar conclusions about a future U.S. labor force shortage, and notes that the projected shortage of U.S. workers will coincide with a continued expansion of the Mexican labor force. He concludes:

> In short the United States has an almost certain need for migrant labor in the decades ahead, if it is to maintain its position in the international economy. The migrants need not come from the south, but given the likelihood of a sustained surplus of unskilled labor in Mexico even by its highest projections, most of the migrants will be Mexican.[23]

The foreign policy ramifications of the above are apparent. Again quoting Reynolds:

> The magnitude of Mexico's prospective economic and population growth underscores the fact that changes south of the border will have far more than incremental consequences for the United States. Stresses and strains within Mexico, if they occur, would shake the continent, but success in Mexican development would be likely to carry with it major benefits for her continental neighbors.[24]

The warning contained in this statement is more or less true of other of our Western Hemisphere neighbors, particularly in the Caribbean. Cuba serves as an ever-present reminder of the extent to which "stresses and strains" in other Western Hemisphere countries can "shake the continent." In the case of Mexico, there is also the issue of energy and the question as to what effect it will have on our policy in other areas, including immigration.

It is likely that the Western Hemisphere will receive more attention in any future formulation of immigration policy than it has in the past. Possible specific options which have been considered before and are likely to be considered again, separately or in combination, are: (1) An increased ceiling on legal immigration from Mexico, the contiguous countries, or the entire hemisphere; (2) a large scale temporary worker program, structured in such a way as to avoid the more obvious problems of the Mexican bracero program; (3) provisions aimed directly at illegal migration, such as employer sanctions and tightened border control, with or without regularization of status of certain undocumented aliens already present in the country ("amnesty").

There is increasing pressure for a more restrictive immigration policy than our current one—de facto and de jure. Those who argue for a decrease in immigration do so primarily on the grounds that there are limits to the number of people the United States economy

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[22] Ibid., p. 217.

[23] Reynolds, Clark. Labor Market Projections for the United States and Mexico and their Relevance to Current Migration Controversies. Stanford University, Food Research Institute, July 6, 1979, p. 31.

[24] Ibid., p. 35.

and society can optimally accommodate. Others argue that it seems unlikely that we can stop those who are truly determined to come, short of measures which we are unwilling to take. This argument holds that it would be wisest to attempt to divert this migration into legal channels, in order to make it as beneficial as possible in terms of both U.S. domestic needs and harmonious relations within the Western Hemisphere.

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