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ON THE RELATIONSHIP BETWEEN TRADE AGREEMENTS AND INSTITUTIONAL AND POLITICAL FACTORS

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Resumen:

En el presente documento se busca determinar la importancia que tienen los factores institucionales y políticos sobre el proceso de integración económica de Latinoamérica, donde se presenta una heterogeneidad creciente entre los distintos países.

Mediante un análisis de sección cruzada y datos de panel, se demuestra que los factores institucionales y políticos importan. Además su rol ha ido en aumento al comenzar el presente siglo, debido a dos circunstancias: el 11 de Septiembre y la *Revolución Bolivariana*. Por último, nuestro análisis confirma que los aspectos geográficos, económicos y de política comercial son claves para la formación y ampliación de los acuerdos de integración económica.

Palabras Claves: regionalismo, América Latina, factores institucionales y políticos, sección cruzada, datos de panel.

Clasificación JEL: F14, F15, F50

Abstract:

The present paper focuses on the importance that institutional and political factors play on Latin American (LA) economic integration, where there is an increasing heterogeneity among countries.

By focusing on both a cross-sectional and a panel data analysis for the LA integration process, we prove that institutional and political factors do matter. Furthermore, the role of these factors has been strengthened at the beginning of the present century due two main issues: the 11S and the *Revolución Bolivariana*.

Finally, our analysis also confirms that geographic, economic and trade policy aspects are key elements for the formation and enhancement of economic integration agreements.

Keywords: regionalism, Latin America, institutional and political factors, cross-section, panel data.

JEL code: F14, F15, F50

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1. Introduction

The recent conflict in Ukraine among pro-European integration groups and opponents has increased interest in an analysis of the determinants of regional integration. In fact, the events that are currently occurring in Europe; the failure to define and consolidate a single narrative to advance in regional integration negotiation in Latin America (LA)(Peña, 2010); and the rise of new powers to a top place in the global order, indicate the importance that institutional and political factors play in integration processes.

This paper hypothesizes that in addition to economic and geographic factors that have determined different trends in the degree of regional commitment by LA countries, political and institutional aspects should be considered. Then, the present research aims to analyse the role that this type of factors play on the formation and enhancement of economic integration in LA.

The increasing country-heterogeneity that exists in LA turns it into a case study of special relevance, where two main integration axes can be distinguished. On the one hand, the Pacific axis presents a continuity strategy, i.e. free trade and markets or trade agreements with rich and developed areas; on the other hand, the Atlantic axis presents an alternative strategy for regional integration, i.e. the *Revolución Bolivariana*, which actually means protectionism and integration with other protectionist LA countries. Brazil fits in a third possibility, as it is not aligned neither with the *Revolución Bolivariana* nor the Pacific axis. So, concerning interactions within LA, the increasing heterogeneity among economies in LA means that we cannot speak of a homogeneous continent, where, in addition, the commitment to economic integration is frequently questioned (García de la Cruz and Sánchez Díez, 2008; Florensa et al, 2014).

The signing of an economic integration agreement (EIA) often requires controversial decision making because EIAs generate global benefits that are usually unequally distributed among winners and losers. For example, in a study that examines the effects of a possible trade agreement between the European Union (EU) and the United States (US), Felbermayr et al. (2013) note that the main criticism of its creation is that it would disadvantage other countries.⁴

The delegation of power that comes from the creation of an integration agreement occurs at the expense of a loss of sovereignty of member countries and is usually accompanied by actions and commitments that may be not consistent with economic logic (Wyplosz, 2006). In this way, economic integration processes may differ among developed and developing regions. More specifically, important differences distinguish LA from developed partners that follow the models of new regionalism.⁵With regard to developed countries, although both the EU and the US promote economic liberalization, Europe is more explicitly concerned with politics and institution-building than the US and endorses a North-South model of global co-operation where “the North” assumes some responsibilities for the development of “the South” (Grugel, 2004).⁶Also concerning interactions between the EU and US with the rest of the world, Kohl et al. (2013) compare coverage and enforcement of 14 agreements involving the EU and 11 agreements involving the US. These authors find that the EU tends to include more legally unenforceable activities than the US, which focuses on a more limited range of legally enforceable commitments.

In the Western-sponsored international order, the best example of deep integration is the EU, and it is the world’s largest trading bloc and most successful regional integration scheme (Doctor, 2007).However, the last international crisis in the European context, the globalization of the world economy and increasing interdependence among countries,

⁴ More recently, Felbermayr et al. (2014) find that the TTIP could result in substantial gains for Europe (3.9percent) and the world (1.6percent), but it could harm third countries.

⁵Refers to the processes by which actors engage in activities across state boundaries and develop conscious policies of integration with other states (Gamble and Payne, 1996; Grugel, 2004).

⁶It is worth mentioning that Europe and the US are often compared, but one is a common market while the other is a country. A comparison EU-NAFTA is more appropriate in the context of our research.

provoked an intense discussion regarding the future of the European Monetary Union (EMU). In our view, this discussion culminated with a speech given by Herman Van Rompuy (2013), when he noted that ‘unlike a year ago, it is now widely recognized that the Eurozone will remain intact [...] Our partners in the world, who often underestimated in the past our political will to maintain the euro and the Union, now acknowledge this too. In a sense, as I've said since last October, the “existential crisis” of the Eurozone is over’.⁷

We argue that the (continuity) strategy followed in the “European model” for economic liberalization might be still a strategy to take into account in LA to advance in regional integration negotiations.⁸ The reason is that Florensa et al. (2015) have recently proved that deeper economic integration and trade agreements of higher institutional quality foster exports and are in line with development and industrialization objectives in the LA region. Then, we focus on the importance of institutional and political factors to create and enhance EIAs, as deep integration has been proven to foster trade margins and, hence, to benefit economic development in a number of developing regions, such as North Africa (Bensassi et al, 2012) and LA (Florensa et al, 2014 and 2015).

To our knowledge, Márquez-Ramos et al. (2011) was the first study to empirically analyze the determinants of different integration levels of EIAs by introducing institutional and socio-political variables as causes of EIAs’ formation and enhancement. These authors base on a discrete choice framework. Additionally, they examine the dynamics of the EU integration process. However, there is a lack of existing literature addressing the dynamics of the integration processes in and outside LA.

In the present research, we take into account two integration levels: shallow EIAs (non-preferential trade agreements and preferential trade agreements) and deep EIAs (free trade agreements and customs unions), as further knowledge of the causes of the dynamics of shallow *versus* deep economic integration in LA is highly desirable. Furthermore, we do not only take into account political and institutional factors, but also we consider two additional political issues as two quasi-natural experiments. First, because the EU and the US present distinctly different models of governance towards the developing world and because these divergences may have widened as a result of the events of 11 September 2001 (Grugel, 2004); we analyze the role that these events may have had on US-Latin American EIAs. Second, we consider the role of the *Revolución Bolivariana* that might have promoted the creation of two strategies of regionalism: the strategy of continuity in Chile, Colombia, Mexico and Peru; and the alternative strategy followed in countries such as Argentina, Bolivia, Ecuador and Venezuela.⁹ Finally, we explore the factors behind the institutional quality of trade agreements. Our analysis confirms that geographic, economic, trade policy, political and institutional aspects are key elements for the formation and enhancement of EIAs, as well as for trade agreements of high institutional quality, in which LA countries are involved. This article is divided into seven sections. Following the introduction, section 2 discusses the regionalism and inter-regional experiences in LA and presents the three strategies followed

⁷Note that even under the “existential” crisis of the EU, Croatia became the Union's 28th member. It is worth highlighting that Lithuania has joined the Eurozone by adopting the euro on 1 January 2015.

⁸This argument would be in line with a recent discussion in the workshop on “Drivers of regional integration” (see footnote 10). While Flôres (2014) referred about the “EU disease”, Paust (2014) pointed out that the EU is the best practice model and that we can learn positive lessons from it. Furthermore, it is important to highlight that the 2012 Nobel Peace Prize was awarded to the EU ‘by more than six decades of contribution to promoting peace, reconciliation, democracy and human rights in Europe’, such a divided continent after the Second World War. See “The Nobel Peace Prize 2012”. Nobelprize.org. 26 Oct 2012.

http://www.nobelprize.org/nobel_prizes/peace/laureates/2012/

⁹*Revolución Bolivariana* refers to a leftist social movement and political process in Venezuela led by Hugo Chávez. Its policies include nationalization of private companies, social welfare programs and opposition to neoliberalism and the policies of the IMF and the World Bank.

by different countries in the region. Section 3 presents the background on the determinants of regional integration and the two main hypotheses to be tested. Section 4 describes the methodology and data. An empirical analysis with a discrete choice framework is conducted in section 5. A sensitivity analysis on the determinants of institutional quality of trade agreements is carried out in Section 6. Finally, the last section concludes.

2. Regionalism, inter-regionalism¹⁰ and integration strategies in LA

Experience suggests that strategies of European and LA integration differ and that the commitment to provide deeper integration agreements in LA appears to be lower than in European countries (Schmitter, 1970). According to Delich and Peixoto (2011) and García de la Cruz and Sánchez Díez (2008), there are two different strategies of re-configuration in LA. The first strategy with its axis in the Pacific joins Chile, Colombia, Mexico and Peru that are integrating with countries outside the region such as the US, the EU and Asia (strategy of continuity). The second strategy in the Atlantic includes countries such as Argentina, Bolivia, Ecuador and Venezuela, which appear to have less interest in integration in the global market (alternative strategy). Finally, Brazil is a rising power that is fostering a hybrid order, characterized by a deepening of transnational integration, but an erosion of global governance's¹¹ most liberal principles (Stephen, 2014). In this regards, the BRICS (Brazil, Russia, India, China and South Africa) initiative might be mentioned. Stephen (2014) states that 'despite the integration of rising powers into transnational structures of production, there remains a strong cleavage between the liberal varieties of capitalism in the western heartland and the forms of capitalism prevalent amongst the BRICS. In contrast to the more liberal forms of state of the established powers, the BRICS can be understood as integrated state capitalist state–society complexes: integrated in the global economy, but with a commanding role reserved for state and quasi-state entities in organizing the economy'.¹²In a recent workshop about deepening economic integration among BRICS,¹³ the Indian counterpart discussed the feasibility of a BRICS currency union, which was rapidly ruled out by the Brazilian and Russian counterparts.

The integration strategy in LA countries has changed over the last fifty years. These changes emphasize significant events, such as the restructuring of the original Andean Group into the Andean Community of Nations and the bilateral integration process between Argentina and Brazil, with special emphasis on certain sectors such as the automobile. These changes also include the creation of Mercosur, the incorporation of Mexico in the North American Free Trade Agreement (NAFTA) and the signing of bilateral preferential trade agreements with countries around the world, such as the US and the EU (Peña, 2011).

Although the growing number of EIAs and their expansion of policy areas have been a global trend since the 1990s (Orefice and Rocha, 2014), recent negotiations present at least three features that distinguish new EIAs from most existing agreements.¹⁴ First, the number and geographical size of the economies concerned are greater than traditional EIAs. Second, a number of recent EIAs create vast integrated economic areas, i.e., Asian, transatlantic, or transpacific. Finally, the thematic agenda of recent EIAs is far more extensive and complex

¹⁰The term inter-regionalism (Doctor, 2007; Malamud, 2012) refers to the integration between two regional blocs.

¹¹Global governance refers to the political regulation of transboundary processes and actors.

¹²Stephen, 2014: 923.

¹³ Workshop on “Drivers of regional integration”, organized by the Economic Policy Forum (EPF) and held in November 2014 in Cape Town, <http://www.economic-policy-forum.org/event/epf-roundtable-drivers-regional-integration/>

¹⁴ A recent “continuity” initiative underway since 2010 that encompasses twelve countries of Latin America, North America, Asia and Oceania is the Trans-Pacific Partnership (TPP). This initiative is considered in the literature a mega-regional trade negotiation. Other policy initiatives of regional integration can be mentioned, such as BRICS (“alternative” strategy).

than traditional EIAs, covering many areas that are not included by WTO agreements (Herreros, 2014). As an example, we might cite the case of the energy integration strategy in the Union of South American Nations (USAN). In USAN (2012) it can be read that 'energy integration is precisely one of the subject areas catalysing the birth of the USAN'.¹⁵

In recent years, there has been a clear trend in LA in reviewing concepts, objectives and methodologies concerning the development of regional integration. Currently, LA countries have multiple options in their strategies to join the world and their respective geographical and regional areas. In addition, there is a proliferation of institutional environments with functions and powers that, at least in appearance, seem to overlap (Peña, 2010). For example, Argentina, Brazil, Paraguay and Uruguay are part of an incomplete customs union, i.e., Mercosur,¹⁶ and a preferential trade agreement, i.e., the Latin American Integration Association (LAIA).

In addition, there is a discussion regarding the continuity of Mercosur¹⁷ and the relationship with other regional blocs, such as the EU or the NAFTA. The EU's negotiations to sign an Association Agreement with Mercosur is an illustration of inter-regionalism and proves that the differences on both sides forced the postponement of the original negotiation timetable on many occasions on the principle that 'no agreement is better than a bad one' (Doctor, 2007). In a multi-causal framework, Doctor (2007) distinguishes three theoretical insights that explain the process of EU-Mercosur inter-regionalism: a) the international context; b) the strategic preferences of political actors in both regions that favoured the deepening of their own regional projects; and c) the interests of economic actors.

As a descriptive analysis, to illustrate the heterogeneity in regional integration followed by LAIA countries, Figures 1 and 2 display the tariff change by country¹⁸ distinguishing between countries in the Pacific and the Atlantic Axes. Figure 1 displays higher tariff reductions for imports from Mercosur and LAIA in the Atlantic Axis whereas Figure 2 illustrates higher tariff reductions for imports from developed countries in the Pacific Axis. We observe that Chile has undergone the most far-reaching liberalization process. Specifically, Mexico has experienced greater liberalization with other EIAs that involve developed countries after becoming a member of the NAFTA and signing a free trade agreement with the EU in 2000. Meanwhile, the remaining countries (excluding Chile and Mexico) have liberalized trade with LAIA and Mercosur to a greater extent. Countries in the Pacific Axis show a higher decrease in tariff rates for imports from the world, NAFTA and the EU (this is not the case for Colombia) than countries in the Atlantic axis.

These two strategies (continuity and alternative) may reflect different objectives concerning, for example, the "trilemma of global politics".¹⁹ Countries following the continuity strategy may be more advanced in the process of trade integration and tariff concessions worldwide. In contrast, countries with an alternative strategy may be less ambitious regarding trade integration and favour more their own national policies and tariff concessions to natural partners.²⁰

¹⁵ Page 9: Authors' translation.

¹⁶ Note that regarding Mercosur, Olarreaga and Soloaga (1998) quantified that approximately 30 percent of 9,119 tariff lines were subject to either external deviations from the common external tariff or internal deviations from free trade. Because important gaps remain under the agreement, many authors consider Mercosur an incomplete customs union.

¹⁷ For example, Doctor (2007) states that by 2006, Uruguay and Paraguay suggested that they might consider downgrading their participation in Mercosur.

¹⁸ Tariff data are obtained from the World Integrated Trade Solution (WITS).

¹⁹ See Vigvári (2011) for an application in the EU.

²⁰ Natural blocs can be considered those regional blocs that eliminate tariffs among countries in the same continents, while unnatural blocs are free trade agreements between individual countries in different continents (Frankel et al, 1998).

Figure 1

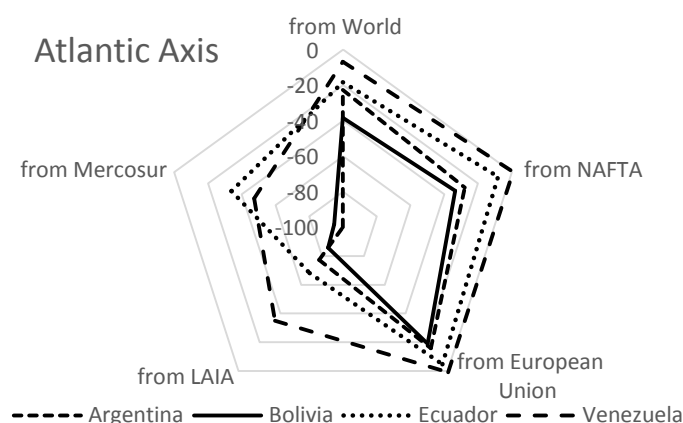
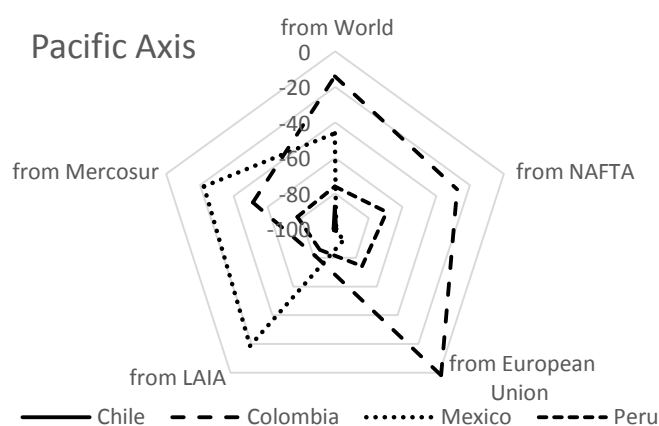


Figure 2²¹



To illustrate the difference between the consequences of following these two strategies, i.e. free trade and markets or trade agreements with rich and developed areas *versus* protectionism and integration with other protectionist LA countries, it might be mentioned that the mean of the effectively applied weighted tariffs among developed countries is much lower than when one (or both) of the trading partners is a developing country (Márquez-Ramos et al., 2012). Additionally, agreements among developed countries or developed and developing countries are more extensive than agreements of developing countries (Kohl et al., 2013), and this fact may explain why EIAs between LA and developed countries have a positive and significant effect on LA exports in specific sectors (Florensa et al, 2014 and 2015), as these EIAs have increased coverage and legality.

3. On the determinants of regional integration

Baier and Berstrand (2004) provide one of the first empirical analyses of the determinants of free trade agreements using a qualitative choice model. Magee (2003) shows that countries are more likely to sign an EIA if they have significant bilateral trade, similar capital-labour ratios and are both democracies. An important contribution of Magee (2003) was to provide

²¹ The tariff changes of Chile range between -85% and -100% and therefore they cannot be appreciated given the scale of this figure.

an estimate when preferential trade agreement formation is modelled as an endogenous choice. The estimates show, however, that the results are highly sensitive to the year used in the cross-section, the variables included in the model and the estimation technique.

Mansfield et al. (2002) find that more democratic countries are more likely to conclude an EIA. These authors tested the following hypothesis: the probability of two countries to sign an integration agreement is greater if both countries are democracies and is lower if both countries are autocratic. Mansfield et al.(2002) analyzed how international co-operation involved in an integration agreement is affected by the control that voters exert over political leaders, which varies between democracies and autocracies (see Jagers and Gurr, 1995).

Vicard (2008) finds that trade and institutional security issues interact in the formation of EIAs. Vicard's results show that countries more open to disputes and trade are more likely to create the most meaningful regional agreements. Malamud and Schmitter(2006) analyze different theories of integration that are considered useful to explain European integration and integration processes elsewhere in the world. These authors critically reflect on the application of the lessons learned from the EU to other forms of economic integration, such as the Mercosur. Several lessons that Malamud and Schmitter consider possible to be transferred are the following: a) integration requires that member countries are democratic; b) regional integration arises from a convergence of interests and not by the creation of an identity; c) integration encompasses nations of different sizes, levels of development and power but requires leadership; d) integration can be peaceful and voluntary but not without conflict; e) integration should begin with a small number of member countries but be open to additional countries; and f) integration may experience excessive institutionalization or an institutional deficit.

Capannelli and Filippini (2009) compare the economic integration process of the EU with the East Asian nations to learn possible reciprocal lessons. These authors consider that regionalism in Asia has developed differently because it has been driven more by markets than by governments. Asian countries also have more disparities in economic development and political systems.

Policies may be structured towards similar objectives of development in developing economies (see point b above). However, it is important to note the regional integration experience of Brazil compared with the remaining Mercosur (or LAIA) members. Brazil includes several elements that damage other LA partners. Moncarz et al. (2011) proved that Mercosur preferences obtained by Brazilian exporters have led, on one hand, to an increase in exports of relatively sophisticated products with which Brazil does not enjoy a global comparative advantage. On the other hand, smaller members of Mercosur export to the region relatively less sophisticated products with which these smaller members have strong comparative advantages. This result suggests that Mercosur has helped Brazil achieve its industrialization objectives but has not contributed to the industrialization of its smaller members. This argument also corresponds with Doctor (2007) who notes that 'a factor of considerable importance was the strategic view Brazil took of regional integration and inter-regionalism as a means of enhancing its power and influence in international for a as well as in the region (this factor gained even more importance after 2003, when Luiz Inácio da Silva became president of Brazil)' (page 292). In addition, non-symmetrical relations and interdependencies co-exist that predict difficulties in formalising inter-regionalism agreements (Doctor, 2007). As pointed out above, although LA countries are natural partners, they are heterogeneous and follow different trade integration strategies.

Contrary to the Asian experience, we hypothesize that regional integration processes in and outside LA may be driven more by governments and therefore by political and institutional factors.

Márquez-Ramos et al. (2011) is likely the most closely related paper to our investigation because they studied the determinants of EIAs by considering geographical, economic and socio-political variables as the main causes of EIA formation and enhancement. According to their results, although economic and geographical variables appear to be the most important determinants in the formation of shallow EIAs, institutional and socio-political factors are more important in explaining deep integration processes. These authors also find that

countries on the same continent are more likely to establish a higher level of economic integration. Their model is more accurate when institutional and socio-political variables are included in the regressions to explain the formation and deepening of EIAs, which helps to determine the desirability of studying this issue in the context of LA.

According to the underlying theory described above, our main hypotheses are two. The first hypothesis is that countries that are more democratic are more likely to form or enhance an EIA. We use a variable that takes a higher value for democratic countries and lower values for autocratic countries (POLITY2) and we expect a positive effect of this variable on the dependent variable. Our second hypothesis tests the effect of political rights on EIAs formation or enhancement and, as we use an index that is higher with a higher lack of political rights, we expect a negative effect of this variable on the dependent variable.

Concerning economic and geographical variables, firstly, we expect that the larger the economic size of the trading countries, the greater the probability of EIA formation or enhancement will be. Then, RGDP measures the sum of the logs of real GDPs of countries i and j and the parameter associated to this variable is expected to be positive signed. Secondly, the more similar the countries' economic size is, the higher the probability of EIA formation or enhancement will be. DRGDP is the absolute value of the difference between the logs of real GDPs of countries i and j , and the associated parameter it is expected to be negative signed. Thirdly, we expect that the probability that a pair of countries will form or enhance an EIA is higher if there is a larger difference in their relative factor endowments as traditional comparative advantages will be further exploited in the LA region. As in Márquez-Ramos et al. (2011), we use absolute differences in the capital stock per worker ratio (DKL) as a proxy for relative factor endowment differences. The expected sign of the parameter associated to this variable is positive.

Fourthly, we expect that a pair of countries will be more likely to form or enhance an EIA when the distance between them is small. We specify the distance variable as in Baier and Bergstrand (2004) and Márquez-Ramos et al. (2011). This variable is called NATURAL and it is defined as the logarithm of the inverse of distance between trading partners. The parameter associated to this variable is expected to be positive signed. Fifthly, we expect that the probability of EIA formation or enhancement increases as the remoteness of a country or pair of countries from the rest of the world rises. We construct the same remoteness variable (REMOTE) used by Baier and Bergstrand (2004) and Márquez-Ramos et al. (2011). When a country is relatively far from its trading partners, it tends to trade more bilaterally with its neighbours, thereby increasing the probability of EIA formation and then, the expected sign of the associated parameter is positive.

Additionally, we take into account whether trading partners are adjacent (ADJ), landlocked (LAND) and whether they speak a common language (LANG). We expect a positive sign for the parameter associated to these variables.

Finally, we analyze the effect of trade flows (TRADE), the intensive margin (IM) and the extensive margin (EM) on EIAs formation and enhancement. As in Márquez-Ramos et al. (2011), we expect a positive effect of TRADE on the dependent variable. Nonetheless, to our knowledge, this is the first time that the effect of the IM and EM on EIAs formation and enhancement is analyzed. In this regard, new trade theories may determine whether an increase in a country's exports is caused by maintaining and enhancing trade relations over time (IM of trade) or the appearance of new products (EM of trade). We may expect that an increasing IM over time leads to lower concessions in regional integration agreements whereas we may expect that greater export diversification is manifested on the formation and enhancement of EIAs, thus the effect of the IM and the EM is expected to be negative and positive signed, respectively.

The data and variables used in this research come from different statistical sources that are listed in the Appendix, together with the expected sign of the estimated coefficient associated with each variable (Table A.1).

4. Methodology and data

In a first step, we estimate an ordered logit where the dependent variable is the level of economic integration among countries. When a country enters into a bilateral trade agreement, the next decision is whether to go further and sign a deeper level of integration. Therefore, we model a series of binary decisions, each decision accepts the current integration level or advances to a higher integration level.

The econometric model is constructed as follows. An ordinal variable Y is a function of an unobserved continuous variable Y^* , which has many threshold points that determine the values the discrete observable variable Y can assume.

We distinguish the following four types of bilateral trade agreements: non-reciprocal preferential trade agreements (NRPTA); preferential trade agreements (PTA); free trade agreements (FTA); and customs unions (CU). Therefore, there must be four values of threshold points. Threshold 1 implies that two countries engage in an NRPTA, threshold 2 implies a PTA, threshold 3 implies an FTA, and threshold 4 represents a CU.

$$Y_i = 0 \text{ if } Y_i^* \leq \delta_1; Y_i = 1 \text{ if } \delta_1 \leq Y_i^* \leq \delta_2; Y_i = 2 \text{ if } \delta_2 \leq Y_i^* \leq \delta_3; \\ Y_i = 3 \text{ if } \delta_3 \leq Y_i^* \leq \delta_4; Y_i = 4 \text{ if } Y_i^* \geq \delta_4$$

The probability model assumes that Y_i^* follows:

$$Y_i^* = \sum_{k=1}^r \beta_k X_{ik} + \varepsilon_i$$

Where X_{ik} $k = 1, \dots, r$ are the covariates and ε_i is the random term with logistic distribution.

We base our calculations for bilateral trade from 1962 to 2009 on the dataset provided by Feenstra et al. (2005) and the World Integrated Trade Solution (WITS); while the EIAs variable is constructed with data available at <http://www3.nd.edu/~jbergstr/> and also the EIAs set out on the website of the World Trade Organization (WTO), as described by Florensa et al. (2014).²² Our dataset includes exports from 11 LA countries to 161 destination countries. To this dataset we add several variables. In particular, we consider geographical (distance, remoteness, adjacency, landlocked status), economic (income and K/L differential), and political and institutional factors (language, democracy, political rights and civil liberties) for all 11 LAIA countries and 161 trading partners.

In addition to the discrete variable taken into account in Márquez-Ramos et al. (2011) as dependent variable, heterogeneity of trade agreements is also considered. In fact, recently, Kohl et al. (2013) developed several publicly available indices to measure trade agreements' heterogeneity, which we use in the present research.

Finally, it is worth mentioning the endogeneity issue. If EIAs increase legality, then some covariates might be correlated with the error term. The use of a continuous variable as dependent variables, as those indexes computed by Kohl et al. (2013), allows relying on Ordinary Least Squares (OLS). Then, we include exporter fixed effects in OLS regressions to avoid for the problem of endogeneity of our variables of interest (sensitivity analysis).

In the empirical analysis, we first perform a cross-section analysis for years 1998 and 2009 using a discrete choice framework.²³ Second, we examine the dynamics of LA regional integration, and then we consider the entire time period: 1962 forward. In the sensitivity analysis, we use the indices computed by Kohl et al. (2013) as LHS variables to analyze the determinants of institutional quality of trade agreements, and the coverage and the enforcement of provisions of LA integration agreements in OLS regressions. Finally, we consider potential endogeneity problems.

²² The construction of trade margins is based on the methodology introduced by Hummels and Klenow (2005).

²³ In this sub-section, we also compare the effect of the RHS variables included in our preferred specification by estimating the marginal effects.

5. Empirical Analysis

5.1. Cross-sectional analysis

In this section, we perform a cross-sectional analysis for years 1998 and 2009. The year selection warrants further discussion. Doctor (2007) states that there was a positive investment climate at the beginning of EU-Mercosur inter-regional negotiations. However, there was a change in the investment climate because of several LA economic crises at the beginning of the new century, as well as potential for political instability and uncertain property rights that exacerbated the downward trend. In fact, in the mid-1990s, states considered engaging other regions to apply open regionalism strategies to a wider area to respond to the challenge of deeper integration in the global economy, ameliorate the impacts of globalization and co-operate in creating a more secure multilateral order (Doctor, 2007). Therefore, the two cross-sections that we examine represent the period before the intensification of the LA integration process occurred (1998) and after the LA crises (2009).

Ordered logit estimates are presented in Tables 1 and 2 for years 1998 and 2009, respectively. In both years, we reject the null that the four cut-points are equal.²⁴ We ran five different specifications that differ in the trade policy variables (Models 1-5). Specifically, Model 1 shows the results when we consider the economic, geographical and political variables; Models 2 to 5 include several lagged variables related to trade policy in a sequential way (EM, IM, Trade and lagged EIA).

Economic and geographical variables present the expected sign and are statistically significant, excluding the variables DKL, in both cross-sections and REMOTE in the cross-section for the year 2009. In both Tables 1 and 2, little variability is observed in the estimated coefficients for the different models. Therefore, the estimates are robust to different specifications.

Concerning political and institutional variables, polity rights have the expected sign, but they are not statistically significant for 1998 (excluding Model 5). However, this variable is significant for the year 2009. This means that the level of economic freedom is an important factor when two countries decide to establish or enhance an EIA that involves LA countries in the most recent period. Otherwise, a greater degree of democracy does not change the likelihood of formation (or enhancement) of EIAs in the most recent period, but it is found to be significant in 1998, excluding Model 5.

We also estimate a generalized ordered logit for our preferred specification (Model 5), which shows that institutional and political variables gain importance at higher levels of integration. Additionally, results obtained for the marginal effects, which are computed with the covariates fixed at their means,²⁵ confirm that the effect of RHS variables differ across different levels of integration. In line with results provided by Márquez-Ramos et al. (2011), we find that although economic and geographical factors are important explanatory factors for the probability of EIAs formation or enhancement, institutional and socio-political variables also contribute to explain the formation of regional integration agreements in LA.

²⁴ In 1998, Statistics (p-value) = 260.33 (0.000); in 2009, Statistics (p-value) = 265.51 (0.000).

²⁵ We exclude dummy variables and the lagged dependent variable from the list of regressors to compute the marginal effects. These results are available upon request.

Table 1. Cross-section 1998

Variable	Model 1	Model 2	Model 3	Model 4	Model 5
Rgdp (lagged)	0.535***	0.457***	0.548***	0.403***	0.487***
	0.061	0.074	0.061	0.075	0.077
Drgdp (lagged)	-0.373***	-0.389***	-0.396***	-0.401***	-0.363***
	0.078	0.077	0.078	0.079	0.078
Dkl (lagged)	-0.025	-0.047	-0.065	-0.082	0.054
	0.221	0.223	0.228	0.223	0.240
Natural	0.919***	0.771**	1.045***	0.688**	0.977***
	0.357	0.363	0.376	0.358	0.370
Remote	0.113***	0.112***	0.101***	0.123***	0.070**
	0.038	0.038	0.039	0.038	0.039
Land	2.712***	2.833***	2.638***	2.914***	2.569***
	0.353	0.365	0.345	0.367	0.367
Adj	2.450***	2.416***	2.509***	2.418***	2.225***
	0.544	0.543	0.548	0.542	0.581
Lang	0.844***	0.810***	0.879***	0.892***	0.722**
	0.317	0.315	0.322	0.312	0.341
P_rights	-0.052	-0.040	-0.065	-0.022	-0.172***
	0.060	0.058	0.060	0.059	0.060
Polity2	0.116*	0.123**	0.104*	0.132**	0.053
	0.062	0.061	0.063	0.060	0.054
Log (EM) (lagged)		0.154			0.029
		0.097			0.098
Log (IM) (lagged)			-0.179***		-0.145**
			0.064		0.070
Log (trade) (lagged)				0.147***	
				0.054	
EIA (lagged)					1.272***
					0.262
Cut 1	18.716	15.865	18.516	15.677	14.740
	3.836	4.182	3.994	3.746	4.125
Cut 2	21.609	18.779	21.435	18.638	17.905
	3.830	4.160	3.991	3.730	4.114
Cut 3	23.082	20.259	22.943	20.106	19.591
	3.832	4.156	3.991	3.733	4.097
Cut 4	24.122	21.293	23.998	21.132	20.646
	3.797	4.125	3.954	3.701	4.075
Pseudo R2	0.294	0.297	0.301	0.301	0.330
Log likelihood	-372.045	-370.308	-368.230	-368.044	-346.183
Number of observations	401	401	401	401	391

Notes: ***, **, * indicate significance at 1, 5 and 10 percent, respectively. The dependent variable is a discrete variable that takes the value of 1, 2, 3 or 4 when an LAIA member was integrated into an NRPTA, PTA, FTA or CU, respectively, in 1998 and 0 otherwise. To avoid endogeneity biases, RGDP, DRGDP, the log of the EM, the IM, trade, and EIA were used for the year 1962 whereas DKL was used for 1980 because of data availability.

Table 2. Cross-section 2009

Variable	Model 1	Model 2	Model 3	Model 4	Model 5
Rgdp (lagged)	0.482***	0.433***	0.491***	0.426***	0.430***
	0.060	0.074	0.061	0.073	0.077
Drgdp (lagged)	-0.311***	-0.319***	-0.331***	-0.320***	-0.282***
	0.068	0.068	0.068	0.069	0.068
Dkl (lagged)	0.104	0.093	0.087	0.076	-0.004
	0.202	0.204	0.202	0.205	0.203
Natural	1.184***	1.077***	1.330***	1.066***	1.188***
	0.296	0.301	0.319	0.309	0.332
Remote	0.046	0.045	0.032	0.051	0.019
	0.035	0.035	0.036	0.035	0.038
Land	2.086***	2.146***	1.988***	2.150***	1.982***
	0.335	0.341	0.321	0.344	0.326
Adj	2.454***	2.450***	2.465***	2.458***	2.464***
	0.555	0.551	0.548	0.555	0.573
Lang	1.020***	0.993***	1.035***	1.037***	0.917***
	0.287	0.285	0.288	0.286	0.294
P_rights	-0.239***	-0.227***	-0.243***	-0.219***	-0.228***
	0.063	0.063	0.065	0.064	0.064
Polity2	-0.035	-0.031	-0.034	-0.027	-0.045
	0.038	0.038	0.038	0.038	0.039
Log (EM) (lagged)		0.098			0.050
		0.086			0.085
Log (IM) (lagged)			-0.155***		-0.127**
			0.058		0.061
Log (trade) (lagged)				0.061	
				0.048	
EIA (lagged)					0.290*
					0.176
Cut 1	10.541	8.856	10.157	9.463	8.008
	3.367	3.687	3.507	3.331	3.802
Cut 2	12.702	11.025	12.334	11.633	10.215
	3.348	3.665	3.486	3.316	3.781
Cut 3	13.080	11.402	12.716	12.009	10.602
	3.343	3.661	3.478	3.314	3.772
Cut 4	15.850	14.178	15.515	14.779	13.461
	3.313	3.639	3.450	3.288	3.744
Pseudo R2	0.260	0.262	0.266	0.262	0.259
Log likelihood	-429.111	-428.329	-425.858	-428.359	-420.027
Number of observations	413	413	413	413	401

Notes: ***, **, * indicate significance at 1, 5 and 10 percent, respectively. The dependent variable is a discrete variable that takes the value of 1, 2, 3 or 4 when an LAIA member was integrated into an NRPTA, PTA, FTA or CU, respectively, in 2009 and 0 otherwise. To avoid endogeneity biases, RGDP, DRGDP, the log of the EM, the IM, trade, and EIA were used for the year 1962 whereas DKL was used for 1980.

5.2. The dynamics of regional integration in LA (1962-2009)

In addition to geographical, economic, institutional and political factors, we consider two additional (political) issues as determinants of EIA formation and enhancement. First, because the EU and the US present distinctive models of governance towards the developing world and because these divergences may have been widened following the

events of 11 September 2001 (Grugel, 2004), we analyze the role that these events may have had on US-LA EIAs (dummy “11S”).²⁶

Second, we consider the role of *Revolución Bolivariana* that may contribute to the two main strategies of regionalism: the strategy of continuity in Chile, Colombia, Mexico and Peru; and the alternative strategy followed in countries such as Argentina, Bolivia, Ecuador and Venezuela. Therefore, we introduce four additional dummy variables: one for Argentina from 2005;²⁷ one for Bolivia from 2006;²⁸ one for Ecuador from 2007;²⁹ and one for Venezuela from 1999 forward.³⁰

Ordered logit estimates (pooled) are presented in Table 3 for the period from 1962 to 2009. We ran seven specifications (Models 6-12) that alternatively include the trade policy variables performed in the previous section and the dummy variables that capture the effects of 11-September and *Revolución Bolivariana*.

Model 6 shows the results when we consider the economic, geographical and political variables; in Models 7 to 9, we add several trade policy (lagged) variables in a sequential way (EM, IM and Trade). Models 10–12 show the most complete specifications that include, in addition to the variables considered in previous models, the lagged EIA, the dummy “11S” (Model 10) and the dummies for Argentina, Bolivia, Ecuador and Venezuela (Model 11). Finally, these dummy variables are included in the same regression (Model 12).

As in the former cross-section analysis, economic and geographical variables have the expected sign and are statistically significant.³¹ The coefficient of the dummy “11S” is negative and statistically significant (Models 10 and 12); this means that the terrorist attack on US soil negatively affected the likelihood of establishing or deepening EIAs between the US and LA countries. Models 11 and 12 show that “Atlantic Axis” countries do not follow a unique integration strategy. Thus, the estimated coefficient for the Argentina dummy is negative and significant whereas the estimated coefficients for the Bolivia and Ecuador dummies are positive and significant. Only for Venezuela, the coefficient is not statistically significant. Regarding institutional and political variables, political rights and the variable POLITY2 have the expected sign and are statistically significant. This means that both the level of political rights and the extent of democratic practices positively affected the chance of signing or enhancing EIAs in the time period 1962-2009.

Obtained results are in line with the fact that Argentina could have been implementing economic policies that negatively affect the probability of signing and enhancing EIAs with third countries. For example, although it has been proved that participation in production networks increases trade flows, many recently implemented strategies in Argentina seek to balance trade and increase the use of local components in, for instance, domestic vehicles.³² Along these lines, Orefice and Rocha (2014) recently suggested that to strengthen

²⁶ This variable takes the value of one if the trading partner is the US from year 2001 forward.

²⁷ Nestor Kirchner and Hugo Chavez narrowed bilateral relations in July 2004.

²⁸ When Evo Morales was elected president, an important opportunity was perceived in Bolivian-Venezuelan relations. Evo Morales became president in 2006.

²⁹ There is a closeness and identification of the President of Ecuador, Rafael Correa, with the Bolivarian Revolution and the Venezuelan government. Rafael Correa was elected president of Ecuador in (late November) 2006.

³⁰ The Bolivarian Revolution is the name given in Venezuela by Hugo Chavez and his supporters to the ideological and social project that began in 1999 with the election of Chavez as president.

³¹ Variable Dkl was not included in pooled ordered logit specifications because of data availability.

³² See “El Plan 2020 para autos y calzados” (“Plan 2020 for cars and footwear” in English), Página/12, 12th May 2011. <http://www.pagina12.com.ar/diario/economia/2-168001-2011-05-12.html>

Table 3. Panel estimation (pooled ordered logit)

Variable	Model 6	Model 7	Model 8	Model 9	Model 10	Model 11	Model 12
Rgdp (lagged)	0.403*** 0.008	0.360*** 0.009	0.398*** 0.008	0.261*** 0.009	0.235*** 0.010	0.238*** 0.010	0.247*** 0.010
DrGdp (lagged)	-0.184*** 0.009	-0.195*** 0.009	-0.194*** 0.009	-0.210*** 0.009	-0.105*** 0.010	-0.131*** 0.010	-0.125*** 0.010
Natural	0.563*** 0.048	0.488*** 0.049	0.627*** 0.048	0.350*** 0.049	0.447*** 0.045	0.392*** 0.046	0.395*** 0.046
Remote	0.128*** 0.006	0.125*** 0.006	0.125*** 0.006	0.127*** 0.006	0.023*** 0.006	0.021*** 0.007	0.026*** 0.007
Land	2.163*** 0.040	2.205*** 0.040	2.105*** 0.040	2.274*** 0.041	1.341*** 0.046	1.302*** 0.049	1.313*** 0.049
Adj	1.894*** 0.077	1.854*** 0.077	1.947*** 0.077	1.798*** 0.077	0.563*** 0.087	0.606*** 0.090	0.596*** 0.090
Lang	1.021*** 0.055	0.985*** 0.055	1.037*** 0.055	1.062*** 0.055	0.404*** 0.057	0.428*** 0.057	0.411*** 0.057
P_rights	-0.060*** 0.005	-0.058*** 0.005	-0.059*** 0.005	-0.051*** 0.005	-0.062*** 0.005	-0.066*** 0.005	-0.066*** 0.005
Polity2	0.051*** 0.004	0.051*** 0.004	0.049*** 0.004	0.049*** 0.003	0.043*** 0.004	0.034*** 0.004	0.034*** 0.004
Log (EM) (lagged)		0.097*** 0.011			0.046*** 0.012	0.078*** 0.012	0.076*** 0.012
Log (IM) (lagged)			-0.101*** 0.009		0.006 0.011	0.027** 0.011	0.024** 0.011
Log (trade) (lagged)				0.192*** 0.008			
EIA (lagged)					3.308*** 0.053	3.299*** 0.053	3.297*** 0.053
Year dummies	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Quasi-natural experiments							
Dummy 11S					-1.349*** 0.228		-1.380*** 0.231
Dummy Argentina from 2005						-0.341*** 0.047	-0.335*** 0.047
Dummy Bolivia from 2006						0.549*** 0.081	0.547*** 0.081
Dummy Ecuador from 2007						0.731*** 0.061	0.739*** 0.062
Dummy Venezuela from 1999						-0.086 0.070	-0.084 0.070
Cut 1	15.479 0.562	13.649 0.603	14.953 0.567	12.084 0.554	8.979 0.577	10.068 0.632	10.528 0.635
Cut 2	17.888 0.563	16.061 0.604	17.37 0.568	14.54 0.554	13.053 0.588	14.171 0.642	14.631 0.644
Cut 3	19.791 0.566	17.968 0.606	19.273 0.571	16.451 0.557	16.094 0.601	17.229 0.658	17.701 0.661
Cut 4	21.333 0.567	19.516 0.606	20.816 0.572	18.015 0.558	18.215 0.606	19.372 0.661	19.843 0.664
Pseudo R2	0.257	0.259	0.259	0.269	0.488	0.492	0.492
Log likelihood	-19737.099	-19698.521	-19680.878	-19433.112	-13592.958	-13490.338	-13475.230
Number of observations	22212	22212	22212	22212	22155	22155	22155

Notes: ***, **, * indicate significance at 1, 5 and 10 percent, respectively. The dependent variable is a discrete variable that takes the value of 1, 2, 3 or 4 when an LAIA member was integrated into an NRPTA, PTA, FTA or CU, respectively, from 1962-2009 and 0 otherwise. To avoid endogeneity biases, the 10th lag of RGDP, DRGDP, the log of the EM, the IM, trade, and EIA were used.

and secure production network activities across countries, governments should reconcile their divergent domestic practices. Nonetheless, this type of strategies are more in line with those distinguishing features of BRICS' capitalism that distinguish it from that of the liberal West, as is the case of the implementation of interventionist industrial policy that includes tools such as strategic trade and investment policies (McNally, 2013 and Stephen, 2014). This interpretation should be taken with caution, as what we actually find is that the dummy for Argentina is negatively correlated with the dependent variable, and not specific Argentinean policies.³³

6. Sensitivity analysis: considering coverage and enforcement of trade agreements

In a second step, we are interested in answering what determines higher coverage and the enforcement of provisions in LA regional integration. Therefore, we append to our cross-section for 1998 and 2009³⁴ three variables that are provided in the dataset in Kohl et al. (2013).³⁵

The database of Kohl et al. (2013) contains a list of 296 agreements (43 with LAIA countries) and provides indices for each agreement. Some pairs of countries have more than one signed agreement between them. For example, Argentina and Bolivia have signed three agreements; they have been LAIA members since 1981 with an index IE of 0.20 (0 is less integration, 1 is maximum integration). Bolivia signed a treaty with Mercosur in 1997 with an index IE of 0.39 and signed another treaty as a member of the Andean Community in 1998 (with an index of 0.27). If a pair of countries are signatories to more than one agreement, we take the greatest integration.

We run cross-sectional regressions for 1998 and 2009 by OLS. Different regressions are run for IIQ, IC and IE as LHS variables. To avoid endogeneity biases, RGDP, DRGDP, the log of the EM, the IM, trade, and EIA were used for 1962 whereas DKL was used for 1980 (see Tables A.2 and A.3 in the Appendix).

Our results show that if there was a regional agreement between two countries, the institutional quality of the agreements and the provisions that are covered and legally enforceable increase in both 1998 and 2009. Trade margins are found to be not significant. The variable POLITY2 is positive and significant in 2009, and a better political quality significantly increases provisions that are covered and legally enforceable but does not improve the institutional quality of the agreements. These results provide evidence consistent with the fact that economic, geographic and language variables are significant in both years. However, the natural and landlocked variables are not significant.

Finally, we include exporter fixed effects in OLS regressions to avoid for the potential problem of endogeneity of our variables of interest as a consequence of omitted variables.³⁶ In addition, we include interactions between groups of countries in LA and institutional and political variables. Specifically, we interact the variables "P_rights" and "Polity2" with a dummy variable equal to one when one of the countries is in the Atlantic Axis, and to zero otherwise ("P_rights_atlantic" and "Polity2_atlantic").

³³Note that we have already controlled for all the potential factors that previous literature shown to be relevant determinants of EIAs formation and enhancement in a discrete choice framework (Baier et al, 2004; Márquez-Ramos et al, 2011). In the sensitivity analysis, we search for the political covariates involved by interacting institutional and political variables with a dummy that equals the value of one when one of the countries is in the "Atlantic Axis".

³⁴We consider the trade agreements that were enforced until 1998 and 2009, respectively.

³⁵ See Table A.1 in the Appendix and Kohl et al. (2013) for further details. The minimum values of IIQ, IC and IE are never zero in Kohl et al.'s (2013) sample; therefore the sample is able to distinguish an agreement with low values of these variables or the inexistence of an agreement.

³⁶In a first step, we included exporter and importer fixed effects. However, as we had an important number of importer fixed effects that were collinear, we rely on the specification that includes only the exporter fixed effects.

Obtained results are shown in the first three columns of Table A.4 for year 1998, and the three last columns of Table A.4 for year 2009. Results show that interactions between the dummy variable for countries in the Atlantic Axis and institutional and political covariates have a significant effect and present a sign opposite to the expected one. In year 1998, although overall property rights and polity2 were not significant to increase coverage and enforcement of trade agreements in LA (see Table A.2), the effect of the interaction “P_rights_atlantic” is positive and significant, then countries with higher lack of political rights in the Atlantic Axis tended to participate in EIAs with higher institutional quality and with higher coverage and legality. In year 2009, the negative and significant effect of “P_rights” (expected sign) on institutional quality (column 4 of Table A.4) and for the index considering the number of WTO provisions legally enforceable of trade agreements (column 6 of Table A.4) is compensated, and is even overtaken, by the positive effect found for the interaction “P_rights_atlantic”.

7. Conclusions

The present paper aims to study the determinants on the dynamics of shallow *versus* deep economic integration in LA. In a first step, we analyze the factors that influence the likelihood that pairs of countries, at least one from LA, sign an EIA or engage in the deepening of existing EIAs. In a second step, we go further into the determinants of heterogeneity of LA trade agreements in terms of institutional design and legal enforceability.

We hypothesize that political and institutional factors play a key role among the determinants of EIAs formation and enhancement. The relevance of political and institutional factors was already found by Magee (2003). However, the related literature has not examined the importance that these factors may also have in the formation and enhancement of LA economic integration processes, a continent where different strategies of economic integration are observed and that has failed to define and consolidate a single narrative to advance in regional integration negotiations. Specifically, three different strategies of re-configuration in LA are observed. The first strategy with its axis in the Pacific, and the second with axis in the Atlantic; while Brazil is a rising power that is fostering a hybrid order, characterized by a deepening of transnational integration, but an erosion of global governance’s most liberal principles.

By utilising both a cross-sectional and panel data analysis of the LA integration process, we prove that institutional and political factors make a difference. Furthermore, the influence of these factors may have been strengthened at the beginning of the current century because of two main issues that affected foreign affairs in several countries: the terrorist attack of 11September 2001 and the *Revolución Bolivariana*.

Our empirical analysis also confirms that geographic and economic aspects are key elements for the formation and enhancement of EIAs in which LA countries are involved. Finally, the studied factors determine the institutional quality, coverage and enforcement of the provisions of these agreements. Obtained results prove that political and institutional factors play a role on the heterogeneity of trade agreements for countries with different integration strategies in LA.

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APPENDIX

Table A.1. Variables and data sources used

Variable	Description	Expected sign	Source
EIA	Discrete variable that takes the value 0 when there is no agreement between trading partners, 1 when the agreement is asymmetrical or one-way, 2 when there is a two-way preferential trade agreement, 3 when there is a free trade agreement and 4 when there is a customs union	Dependent variable Lagged regressor: + (the probability of reaching an integration level depends on the point of departure. Then, the probability of reaching a deeper integration level is higher if the countries already participate in an EIA)	http://www3.nd.edu/~jbergstr/ and WTO
TRADE	Measures bilateral exports from i (LA country) to j	+ (two countries that are major trading partners are more likely to form or enhance a trade agreement)	Feenstra et al. (2005) and WITS
IM: Intensive Margin	Growth in exports because of major exporting quantities of a particular good	- (an increasing IM over time might lead to lower concessions in regional integration)	Feenstra et al. (2005) and WITS. Authors' calculations
EM: Extensive Margin	Growth in exports because of a wider range of exported goods	+ (the greater export diversification, the more likely to form and/or enhance EIAs)	Feenstra et al. (2005) and WITS. Authors' calculations
RGDP	Measures the sum of the logs of real GDPs of the exporter and the importer countries (constant 2005 US\$)	+ (net welfare gain from an EIA between a pair of countries increases with their economic size)	World Development Indicators, World Bank
DRGDP	Absolute value of the difference between the logs of real GDPs in the exporter and the importer countries (constant 2005 US\$)	- (a greater difference in country size reduces the chance of signing an EIA by making it less attractive for the larger country)	World Development Indicators, World Bank
DKL	Absolute value of the difference between the log ratio of capital stock per worker in the exporter and the importer countries (1985 international prices)	+ (traditional trade models suggest that the benefits of an EIA increase the wider their relative factor endowments)	Baier et al. (2006). Authors' calculations
NATURAL	Log of the inverse of the great circle distances between trading partner country capitals (km)	+ (a pair of countries will be more likely to form or enhance an EIA if the distance between them is smaller)	CEPII
REMOTE	Relative distance of a pair of continental trading partners from the rest of the world ³⁷	+ (the likelihood to form or enhance an EIA increases for two continental trading partners as their remoteness from the rest of the world increases)	CEPII

³⁷ The equation used to compute REMOTE_{ij} is (Baier and Bergstrand, 2004):

$$REMOTE_{ij} = DCONT_{ij} x \left\{ \frac{\log \left(\sum_{k=1, k \neq j}^N \frac{DIST_{ik}}{N-1} \right) + \log \left(\sum_{k=1, k \neq i}^N \frac{DIST_{ik}}{N-1} \right)}{2} \right\}$$

Where DCONT_{ij} is a dummy variable assuming the value 1 if both countries are on the same continent and 0 otherwise.

ADJ	Adjacency dummy	+ (neighbouring countries have a higher probability of engaging in an EIA)	CEPII
LAND	Landlocked dummy; =1 if at least one trading partner is landlocked	+ (landlocked countries have a higher probability of engaging in an EIA)	CEPII
LANG	Language dummy	+ (two countries are more likely to form or enhance an EIA if they speak a common language)	CEPII
POLITY2	Varies between 10 (countries strongly democratic) and -10 (highly autocratic)	+ (countries that are democratic are more likely to form or enhance an EIA) ³⁸	Marshall and Jagers (2002)
PR: Political Rights ³⁹	Ranges from 1 to 7, beginning with free and fair elections, competitive parties, the opposition plays an important role and the minority groups have reasonable self-government (value of 1); to lack of political rights as a result of the extremely oppressive nature of the regime sometimes in combination with civil war (value of 7)	- (two countries with higher political rights are more likely to form or enhance an EIA) ⁴⁰	Freedom House Organization
IIQ	Index that reflects an agreement's institutional quality. Takes the values between 0 (low institutional quality) and 1 (high institutional quality)	Dependent variable	Kohl et al. (2013)
INDEX_C (IC)	Number of WTO provisions covered by an agreement (unweighted average of index WTO+, index WTOx and IIQ with provisions that are covered)	Dependent variable	Kohl et al. (2013)
INDEX_E (IE)	Number of WTO provisions legally enforceable of an agreement (unweighted average of index WTO+, index WTOx and IIQ with provisions that are covered and legally enforceable)	Dependent variable	Kohl et al. (2013)

³⁸ POLITY2_{ijt} is the sum of the values of POLITY2 variable for exporter and importer country in year t.

³⁹ An additional political variable has been considered, CIVIL LIBERTIES, which includes the freedom to develop opinions and personal autonomy without interference from the state. This variable was excluded in regressions to avoid multicollinearity because it is highly correlated with PR.

⁴⁰ P_rights_{ijt} is the product of the values of PR variable for exporter and importer country in year t.

Table A.2. Cross-section 1998. OLS regression with IIQ, IC and IE

Variable	Model 13	Model 14	Model 15
Rgdp (lagged)	0.025**	0.017	0.018*
	0.012	0.011	0.009
Drgdp (lagged)	-0.039***	-0.022**	-0.020**
	0.012	0.009	0.008
Dkl (lagged)	0.044*	0.028	0.031*
	0.025	0.019	0.016
Natural	-0.030	-0.032	-0.021
	0.043	0.033	0.028
Remote	0.014**	0.008	0.008*
	0.006	0.006	0.005
Land	0.045	0.006	0.005
	0.053	0.043	0.031
Adj	0.451***	0.355***	0.280***
	0.094	0.082	0.065
Lang	0.144***	0.082*	0.067*
	0.054	0.045	0.035
P_rights	0.003	0.000	0.000
	0.006	0.004	0.004
Polity2	0.010	0.007	0.006
	0.007	0.006	0.005
Log (EM) (lagged)	0.000	0.003	0.001
	0.011	0.009	0.007
Log (IM) (lagged)	-0.006	0.001	0.000
	0.008	0.007	0.005
EIA (lagged)	0.111***	0.034	0.053**
	0.038	0.030	0.026
Constantterm	-1.583***	-1.093**	-1.070**
	0.582	0.491	0.421
Number of observations	328	328	328
R2	0.3124286	0.1915258	0.2335635
AIC	134.4063	31.21424	-116.6486
RMSE	0.290857	0.2485209	0.1983684

Notes: ***, **, * indicate significance at 1, 5 and 10 percent, respectively. T-statistics are provided below every coefficient. The dependent variable is equal to zero when there is not agreement and takes the value of the indexes provided by Kohl et al. (2013), i.e. IIQ, IC and IE, respectively. To avoid endogeneity biases, RGDP, DRGDP, the log of the EM, the IM, trade, and EIA were used for the year 1962, whereas DKL was used for 1980.

Table A.3. Cross-section 2009. OLS regression with IIQ, IC and IE

Variable	Model 16	Model 17	Model 18
Rgdp (lagged)	0.030**	0.022**	0.021**
	0.012	0.010	0.009
Drgdp (lagged)	-0.040***	-0.024***	-0.022***
	0.011	0.009	0.008
Dkl (lagged)	0.043**	0.035**	0.034**
	0.021	0.016	0.014
Natural	0.001	0.007	0.008
	0.044	0.033	0.029
Remote	0.014**	0.007	0.008*
	0.006	0.005	0.005
Land	0.049	0.010	0.009
	0.053	0.043	0.032
Adj	0.433***	0.331***	0.262***
	0.092	0.076	0.062
Lang	0.137**	0.076*	0.063*
	0.054	0.044	0.035
P_rights	-0.004	-0.002	-0.003
	0.005	0.004	0.003
Polity2	0.006	0.009**	0.006*
	0.005	0.004	0.003
Log (EM) (lagged)	-0.002	0.002	0.000
	0.011	0.009	0.007
Log (IM) (lagged)	-0.008	-0.001	-0.002
	0.008	0.006	0.005
EIA (lagged)	0.093**	0.010	0.034
	0.037	0.029	0.025
Constantterm	-1.471***	-1.043**	-1.000**
	0.555	0.480	0.411
Number of observations	336	336	336
R2	0.3170595	0.2111474	0.2486606
AIC	128.8246	16.76386	-132.9959
RMSE	0.2871869	0.2430765	0.194517

Notes: ***, **, * indicate significance at 1, 5 and 10 percent, respectively. T-statistics are provided below every coefficient. The dependent variable is equal to zero when there is not agreement and takes the value of the indexes provided by Kohl et al. (2013), i.e. IIQ, IC and IE, respectively. To avoid endogeneity biases, RGDP, DRGDP, the log of the EM, the IM, trade, and EIA were used for the year 1962, whereas DKL was used for 1980.

Table A.4. Cross-section for 1998 and 2009. OLS regression with IIQ, IC and IE, exporter fixed effects and interactions

Variable	1998			2009		
	IIQ	IC	IE	IIQ	IC	IE
Rgdp (lagged)	0.040***	0.033***	0.029***	0.043***	0.035***	0.031***
	0.010	0.009	0.008	0.010	0.009	0.007
Drgdp (lagged)	-0.037***	-0.022**	-0.020**	-0.034***	-0.020**	-0.019**
	0.012	0.009	0.008	0.012	0.009	0.008
Dkl (lagged)	0.017	0.011	0.02	-0.009	-0.002	0.003
	0.027	0.020	0.017	0.025	0.017	0.015
Natural	0.098**	0.091***	0.076***	0.098**	0.094***	0.076***
	0.038	0.029	0.023	0.038	0.029	0.023
Remote	0.006	0.002	0.003	0.006	0.001	0.003
	0.005	0.004	0.004	0.005	0.004	0.003
Land	0.034	0.004	0.01	0.026	0	0.01
	0.064	0.040	0.037	0.065	0.041	0.038
Adj	0.355***	0.295***	0.231***	0.336***	0.275***	0.214***
	0.095	0.080	0.061	0.100	0.083	0.063
Lang	0.023	-0.026	-0.018	0.008	-0.037	-0.027
	0.046	0.036	0.029	0.046	0.036	0.029
P_rights	-0.005	-0.003	-0.002	-0.015**	-0.006	-0.008*
	0.008	0.006	0.005	0.007	0.005	0.004
Polity2	0.004	0.006	0.007	-0.011	0.001	-0.002
	0.010	0.008	0.007	0.007	0.006	0.005
P_rights_atlantic	0.023***	0.013**	0.011***	0.022***	0.013**	0.011***
	0.007	0.005	0.004	0.007	0.005	0.004
Polity2_atlantic	0.004	-0.004	-0.001	-0.003	-0.007	-0.005
	0.006	0.005	0.004	0.008	0.006	0.005
Log (EM) (lagged)	-0.011	-0.006	-0.008	-0.008	-0.004	-0.005
	0.012	0.009	0.007	0.011	0.008	0.007
Log (IM) (lagged)	0.006	0.009	0.006	0.011	0.012*	0.009
	0.009	0.007	0.006	0.009	0.007	0.006
EIA (lagged)	0.095**	0.004	0.031	0.096**	0.005	0.03
	0.041	0.033	0.027	0.041	0.033	0.027
Constant term	-1.303**	-0.872**	-0.881**	-1.194**	-0.859**	-0.818**
	0.516	0.418	0.361	0.491	0.408	0.354
Exporter fixed effects	Yes	Yes	Yes	Yes	Yes	Yes
Number of observations	328	328	328	336	336	336
R2	0.5709462	0.5523222	0.5480564	0.57506	0.553926	0.548597
AIC	3.726973	-138.6584	-265.8963	-6.59366	-150.788	-280.187
RMSE	0.2342814	0.1885706	0.1553238	0.230879	0.186293	0.153663

Notes: ***, **, * indicate significance at 1, 5 and 10 percent, respectively. T-statistics are provided below every coefficient. The dependent variable is equal to zero when there is not agreement and takes the value of the indexes provided by Kohl et al. (2013), i.e. IIQ, IC and IE, respectively. To avoid endogeneity biases, RGDP, DRGDP, the log of the EM, the IM, trade, and EIA were used for the year 1962, whereas DKL was used for 1980.