

business-orientated economic and political environment and a liberal financial system. Most of the investors believe that Brazil has an economic and political environment unfavourable to business and an illiberal financial system. The report concluded that Brazil's ability to attract capital would be limited compared with the size of its economy.<sup>36</sup> A recent report by the Economist Intelligence Unit makes much the same point.<sup>37</sup>

Moreover, Brazil's recent actions to protect its auto industry illustrate how competition for investment can lead to the wrong policy conclusion: protectionist action rather than domestic reform and adjustment. In March 1995, Brazil temporarily (up to one year, according to the decree) increased tariffs on 109 items originating outside the region, including several motor vehicle items, to 70 percent.<sup>38</sup> When these new tariffs failed to limit auto imports enough to suit the Brazilian government, it imposed an import quota for the remainder of this year of 50% of the cars imported to the date of this further adjustment. Next year, imports by car makers with plants in Brazil will be limited to a fixed proportion of their exports.<sup>39</sup> In addition, Brazil has lowered tariffs on auto part imports, a move that also contravenes MERCOSUR's common external tariff.

It is not yet clear how the Brazilian auto import quota will affect Argentine auto exporters over the medium to long term. Argentina and Brazil have agreed that this quota will not apply to imports from Argentina for the remainder of 1995. Argentina and Brazil will try to negotiate a resolution of this matter by the end of 1995.<sup>40</sup>

This dispute has strained the relationship between Argentina and Brazil to the extent that the Brazilian Industry and Commerce Minister felt obliged to deny Brazil

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<sup>36</sup> The Global Capital Market: Supply, Demand, Pricing and Allocation (McKinsey Global Institute: Washington D.C., 4 November, 1994), pp. 4-5.

<sup>37</sup> "Brazil: Investment - MNCs Find Doing Business Expensive - EIU Business Briefing", Economist Intelligence Unit, Reuter Business Brief, 11 April 1995.

<sup>38</sup> The tariffs affected durable consumer goods, such as appliances, as well as automobiles. See C. William Robinson, *Mercosul What It Is, What It Does*, (Canadian Embassy Brasilia, April 6, 1995), p. 15. The new increased tariffs were later added to Brazil's list of national exceptions to the common external tariff.

<sup>39</sup> Angus Foster, "Deficit Drove Brazil Car Curbs", *Financial Times*, 15 June 1995, p.4.

<sup>40</sup> "Brazil, Argentina Defuse Auto Imports Row", Reuter News Service, 12 July 1995.