

than in Brazil.³² More than 40% of Brazil's population lives in poverty compared to 18% in Argentina.³³ Clearly, Brazil must liberalize its economy further to reach Argentina's level. This will not be an easy job. Yet it is on these reforms that the future of MERCOSUR depends.

Economic policy differences could strain the MERCOSUR relationship between Argentina and Brazil in several ways. Most generally, attempts to develop and sustain a common external trade policy will be constantly bushwhacked unless there is a modicum of convergence on domestic economic policy and practice. More specifically, the better conditions for investment in Argentina will cause foreign companies to invest predominantly in that country for production for MERCOSUR. This represents a good result for Argentina in the first instance, but one that will create considerable unease in Brazil. There is evidence that an early Argentine advantage is occurring. A recent Reuter report notes that "Argentina has been commonly preferred to Brazil as a manufacturing location since the move to free trade between the two countries began in earnest last year."³⁴ Statistics on foreign investment show that flows into Argentina have been considerably greater than those into Brazil.³⁵

Reports suggest that many outside investors believe that the environment for business is more favourable in Argentina than in Brazil. A recent study by McKinsey and Company suggests that international investors perceive a significant difference in the economic policy environment in Argentina and Brazil. In a 1994 survey of investors carried out by McKinsey, there was consensus that Argentina had a

³² Annual real per capita GDP growth rates for 1991-93 were -0.5% for Brazil and 6.6% for Argentina. The 1994 growth rate was 2.6% for Brazil and 4.7% for Argentina. The World Bank, *Global Economic Prospects and the Developing Countries 1995*, (Washington D.C., April 1995), p.79.

³³ Shahid Javed Burki and Sebastian Edwards, "Consolidating Economic Reforms in Latin America and the Caribbean", *Finance and Development*, March 1995, p. 8. Statistics are for 1992 for Brazil and 1993 for Argentina.

³⁴ "Brazil, Argentina Car Dispute Threatens Trade Group", *Australian Financial Review*, Reuter Business Brief, 23 June 1995.

³⁵ Cumulative direct investment flows into Argentina for 1990-1992 were US\$ 9.7 billion compared to US\$ 4 billion for Brazil. *Foreign Direct Investment OECD Countries and Dynamic Economies of Asia and Latin America* (OECD: Paris 1995), p. 25. Total inflows of all private capital into Argentina for 1993 were US\$ 15.1 billion (12% of GDP), compared to US\$ 13.4 billion (4.4% of GDP) for Brazil. The World Bank, *Global Economic Prospects and the Developing Countries 1995*, (Washington D.C.: April 1995), p. 84.