EU-MERCOSUR: AFTER 20 YEARS OF NEGOTIATIONS, A DEAL IS FINALLY REACHED

On Friday 28 June, Mercosur (Mercado Común del Sur – the economic and political bloc comprising Argentina, Brazil, Paraguay, and Uruguay) and the EU finally reached a deal on the trade component of an Association Agreement that has been the subject of negotiations for almost 20 years.

The stop-start history of the negotiations began with the agreement in 1995 to work towards an Association Agreement, with negotiations commencing at the end of the 1990s, before being suspended in 2004 due to a disagreement on goods and services. Negotiations relaunched in 2010 and paused again in 2012. The blocs then formally exchanged market access offers in 2016. Momentum has slowly been gathering since.

This briefing looks at the economic potential behind a deal and what has been agreed, as well as the complexities for European businesses seeking to use it given Mercosur's status as a customs union 'in the making', and the difficult political balance necessary to ratify and apply the agreement.

THE ECONOMIC POTENTIAL

The economic rationale behind the trade agreement is clear. The EU is the world's second largest market, and Mercosur the sixth, with a GDP of approximately EUR 2.2 trillion and a population of over 260 million people.

The EU Mercosur trading relationship is relatively balanced and there are clear specialisms in each market, which suggest a trade deal could successfully develop the economies' complementarity. EU exports to Mercosur are primarily machinery, transport equipment, chemicals, and pharmaceutical products whilst Mercosur's primary exports to the EU are agri-food, non-edible raw materials, and meats and other animal products.

Mercosur’s priority during negotiations was to secure greater access into the EU market for agricultural products (meat, especially beef, sugar, ethanol, poultry, cereals and dairy products), and to reduce the EU's domestic agricultural subsidies.

Key issues

- Following 20 years of stop-start negotiations, a trade deal between the EU and Mercosur was agreed on Friday 28 June.
- The potential economic benefit of a trade deal between the EU and Mercosur is significant.
- While full details are not yet known, the 'agreement in principle' provides for significant liberalisation between the two economies.
- However, the unique nature of Mercosur as a customs union 'in the making' may make the reality of an agreement harder for European businesses to take advantage of.
- Ratification and application will also be complicated. There are some difficult political realities to overcome, including opposition from European farmers and civil society groups.
- Some beef producing countries (including Ireland) will face domestic pressure to reject the deal, while another group of countries (including Germany) strongly support it.

The EU meanwhile sought market access for cars and car parts, as well as dairy products, enhanced access to public tenders and maritime services, as well as intellectual property protections including improvements to medicine patent rules. As with all of its trade negotiations, the EU sought the protection of geographical indications (a form of intellectual property reserving terms such as 'Champagne' to those produced in a given place).

When and if the deal is ratified and applied, it will be the most important bi-regional trade agreement in the world.

THE AGREEMENT IN PRINCIPLE

The text of the trade deal has not yet been published (and will not be until after a 'legal scrubbing'), however, an agreement in principle containing the broad-brush strokes of the deal has been published.

In addition to traditional commitments on tariffs, quotas and rules of origin, the agreement also includes chapters on services, intellectual property, public procurement, sustainable development and provisions for small- and medium-sized enterprises.

On market access for agricultural goods, the EU will liberalise 82% of tariff lines, with the remaining imports subject to quotas. Quotas, which will be phased in over six years for most of these imports, will be applied to beef (99,000 tonnes subdivided into fresh and frozen, with an in-quota rata of 7.5%), poultry (180,000 tonnes duty free subdivided into bone-in and boneless), pig meat (25,000 tonnes with an in-quota rate of EUR 83 per tonne), sugar (elimination of an in-quota rate on 180,000 tonnes of Brazil's EU WTO quota, and 10,000 tonnes duty free for Paraguay), as well as ethanol, rice, and honey. Mercosur meanwhile will liberalise a variety of agricultural products including cheese, milk powders, infant formula, wine, spirits, olive oil, and fruits.

On market access for industrial goods, Mercosur has agreed to eliminate duties on over 90% of EU exports in each of cars, car parts, machinery, chemicals and pharma. Liberalisation will be phased in over sector-specific time periods, mostly at around 10 years. For passenger vehicles, full liberalisation will take place over 15 years (with a seven-year grace period accompanied by a transitional quota of 50,000 units). The EU will eliminate duties on 100% of industrial imports from Mercosur over up to 10 years.

Amongst the provisions on services and intellectual property, the EU has succeeded in gaining access to the highly protected maritime sector, and protection of geographical indications (of which there will be 355 for the EU and 220 for Mercosur). The details of which products gained protected status in the negotiations is not yet available.

A PECULIAR TRADING PARTNER

No matter the strengths of the deal, the nature of Mercosur may pose challenges to European businesses seeking to take advantage of it. Businesses will have to consider how best to do so over the years to come as the liberalisation envisaged in the agreement gradually come into force.

Mercosur, despite its ambition, is not yet the sophisticated single market that the EU is, and once goods enter it, they still face a variety of impediments to circulation within the bloc. There exist hundreds of exceptions to the Mercosur Agreement, and several sectors, including sugar and cars, are regulated through bilateral agreements between Mercosur members. There also exists a wide range of non-tariff barriers between members including licences and phytosanitary measures, which inhibit trade. Mercosur members have been known to impose temporary trade barrier policies such as antidumping, safeguards, and countervailing duties on one another, or on third countries without internal coordination.

Mercosur has also yet to become a true customs union. Whilst the bloc has had agreed common external tariff rates since the 1990s, under a July 2015 Mercosur decision, each member is permitted to maintain a number of exceptions to the external tariff for an established period. Moreover, despite a new Mercosur Common Customs Code being adopted in 2010, it has yet to enter into force, resulting in each member collecting its own customs revenues. Because Mercosur members each collect their own tariffs, businesses importing into one Mercosur member and seeking to move the imported good into another member face a "double tariff" by which the imported good must pay the standardised external tariff each time it crosses a border within the bloc.

Mercosur also suffers from weak institutions and a lack of enforcement tools for their common rules. There is no truly powerful, independent Mercosur civil service equivalent to the European Commission to enforce Member States' compliance with Mercosur's rules, nor is there at present a supranational court like the Court of Justice of the European Union (though there have been attempts to establish one). Only States can bring actions against States for non-compliance with the Mercosur Agreement through arbitration, and these have historically been poorly utilised.

Finally, Mercosur suffers from political instability in both its members and neighbours, and weak intra-regional infrastructure. The bloc's internal political weaknesses were highlighted by its one-year suspension of Paraguay in 2012 and its indefinite suspension of Venezuela in 2016. A lack of good interconnection infrastructure has led to low levels of both intra-regional trade and regional value chain integration.

Mercosur exceptions

Under a July 2015 Mercosur Common Market Council decision, each Mercosur member is permitted to maintain a number of exceptions to the Common External Tariff for an established period. Brazil and Argentina are each permitted to maintain a list of 100 exceptions to the Common External Tariff until 31 December 2021.

Brazil maintains higher tariffs than Mercosur's common tariffs on goods including mobile phones, telecommunications equipment, computers and computer printers, wind turbines, certain chemicals and pharmaceuticals.

THE POLITICS OF RATIFICATION

Before the deal can enter into force at all, there remain meaningful obstacles to ratification and application.

This appears most straight forward from the Mercosur side, where each of the four countries will need to ratify the agreement according to their own constitutional processes. It is likely that this Association Agreement will follow previous Mercosur agreements by entering into force bilaterally between the EU and any Mercosur member that ratifies it, once one does. The practical consequence of this would be that once one Mercosur member ratifies the deal, its businesses could access the entire Mercosur-granted EU export quotas, generating pressure on other governments to also ratify the deal.

On the EU side, Association Agreements usually need to be ratified by both the EU institutions and EU Member States. In the EU Member States this includes some regional parliaments, such as that of the Belgian region of Wallonia, which delayed the signing of the Comprehensive Economic and Trade Agreement (CETA) with Canada in 2016. However, agreements may enter into "provisional application" ahead of ratification following approval by the EU Member States in the Council, and the European Parliament.

Politically in the EU, the agricultural sector and civil society have significantly dialled up the volume on their campaigning around the deal recently.

Agricultural interests have strong reservations on any liberalisation of the sector and an active lobby in Brussels and the Member States. In June, during the final stages of the negotiations, the so-called "beef belt" countries (including France, Ireland, Poland and Belgium) wrote a joint letter to the European Commission calling for the EU not to improve on its existing agricultural quota offers, seeking a segmentation of the quota between high-quality and low-quality cuts (partially achieved), and seeking guarantees on sanitary, phytosanitary, animal welfare and environmental standards (partially achieved). While President Macron has subsequently publicly supported the deal, the Irish Taoiseach Leo Varadkar has said the Irish government plans to conduct a "*full economic assessment*" and veto the deal if it shows the economic risks to outweigh the benefits. Other powerful Member States including Germany and Spain are strongly in favour of the deal, but the domestic pressure to reject the deal in countries like Ireland will be high.

Civil society organisations are also mobilising against ratification of a deal. At approximately the same time as the "beef belt" countries wrote of their concerns to the European Commission, a group of over 340 Non-Governmental Organisations wrote to the Presidents of the EU institutions calling on them to cease negotiations with Mercosur due to what they view as a deteriorating human rights and environmental situation in Brazil. Since the deal was agreed, they have managed to generate significant media attention.

Climate change campaigners are concerned by some of the policies of the new Brazilian government of Jair Bolsonaro, and the consequences of a trade deal stimulating agricultural activity which exacerbates existing environmental problems including deforestation. This argument has been picked up by the agricultural lobby and was also alluded to in the letter from the "beef belt" countries. While the final deal attempts to address these concerns by including an obligation for Mercosur States, including Brazil, to "*effectively implement*" the 2015 Paris Agreement on climate change, and to fight against deforestation, this may not be enough given recent reports of the significantly increasing rate of deforestation in Brazil.

WHEN CAN WE EXPECT TO SEE A FINAL DEAL APPLIED AND RATIFIED?

Despite all the difficulties, it appears there is significant political will in both the EU and Mercosur to get the deal applied and ratified soon. On the Mercosur side, October 2019 will see presidential elections in Argentina and Uruguay which could install governments less favourable to concluding a deal, and therefore there is real pressure on the current administrations to cross the line.

On the EU side, the next European Commission is due to arrive in the Berlaymont in November and will have to oversee ratification. However, there is no doubt that President Juncker and Commissioners Malmström and Hogan see last weekend's agreement as a significant part of their legacies – it caps off a streak that has included trade deals with Singapore, Japan and Canada, and the recent signature of the EU Vietnam Free Trade Agreement.

Now that the negotiating teams have concluded their work and flown back to their capitals, it is time for politicians to step up and sell that deal to parliaments across the EU and Mercosur, and for businesses to begin to assess how best to employ the new opportunities the deal presents.

Political constituencies seek to capture the public debate ahead of ratification

"This is a bad deal for Ireland and for Irish farmers, it's a bad deal for the environment and it's a bad deal for EU standards and consumers."

Joe Healy, President of **Irish Farmers Association**

"Trading more cars for cows is never acceptable when it leads to the destruction of the Amazon, attacks on Indigenous Peoples, and escalating hostility towards civil society."

Naomi Ages, Political Strategist at **Greenpeace**

"This agreement is the biggest the EU has ever concluded and will finally open a market of 266 million consumers that are keen to have access to European goods and services at competitive prices. We still need to know the details but we are confident the final outcome will be balanced and will safeguard the main European interests "

Pierre Gattaz, President of **BusinessEurope**

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