

The New EU-Mercosur Trade Agreement: a New Breath to Free Trade

Written by Vivian Daniele Rocha Gabriel

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After almost 20 years, the end of the negotiations of the EU-MERCOSUR Association Agreement was announced at the end of June 2019, and now, it is pending for signing. Starting in 1999, to counteract the negotiations of the Free Trade Area of the Americas, the EU-MERCOSUR negotiations begun with the exchange of tariff commitments offers and went through several challenges, including strong paralysis between 2004 to 2010 and 2012 to 2016. The deadlock had begun to be solved in 2016, with the exchange of new offers concerning the access to markets in goods, services, and government procurement. After this leverage, the negotiation was almost finished between the end of 2017, at the time of the World Trade Organization (WTO) Ministerial Conference in Buenos Aires, and January 2018. However, sensitive issues such as agriculture, sustainability, geographical indicators, and rules of origin have stuck the negotiations and were only recently dealt with. After a long and rough process, the outcome of the negotiations was set forth during the G-20 Summit, assertively relaunching the integration process between the two blocs.

The new agreement will form one of the biggest and most sophisticated free trade areas in the world. Firstly, because of the magnitude of the trade and investment flows and the huge number of consumers involved. MERCOSUR and the EU together account for a GDP of US\$ 20 trillion, approximately 25% of the world economy, a market of 780 million people and represent a regional trade flow that overcame more than US\$ 90 billion in 2018. The EU is MERCOSUR's second trading partner and figures as the largest foreign investor in the region. In 2017, the EU's stock of investment in the South American bloc was US \$433 billion. Moreover, MERCOSUR accounts as the EU's 8th largest non-regional partner, being the only major trading partner in Latin America with who the EU does not have a preferential trade agreement.

It is important to highlight that the new free trade agreement has triggered great expectations on both sides, including the creation of jobs. For instance, nowadays, more than 855,000 jobs in the EU are related to exports to Brazil alone and over 60,000 European companies have already exported to the bloc. In parallel, MERCOSUR's companies have already employed more than 30,000 people in the EU. It is expected that these numbers will still increase in the mid and long terms fostering the job market related to imports and exports on both sides (EUROPEAN COMMISSION 2019).

However, the statistics have not been the only impressive aspect of this new integration process, but also the new framework that will be established. The trade rules that have been embodied by this international agreement focus on liberalization and market access to agricultural and industrialized goods and services and the reduction of trade barriers. These barriers may be represented by tariffs, a classical way to escalate protectionist measures, and non-tariff barriers, mainly represented by excessive bureaucracy on import and export procedures, rules and regulations, which may be disguised or differ from international standards, and high import duties and requirements[1]. The non-tariff barriers represent the most sophisticated kind of government-imposed restraint on the flow of international goods or services and have been dealt with in the WTO through a couple of international agreements, such as the Sanitary and Phytosanitary Agreement and the Technical Barriers to Trade Agreement. However, because of the lethargic progress of the Doha Round and the competing visions among the members, the WTO has been going through a Catch 22 situation, that is a course of action in which the outcome or solution is especially difficult or

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impossible to achieve due to contradictory conditions. There is a motionless in setting up new trade agreements or modernizing rules already taken. Because of that, new free trade agreements have been adopting new rules to address and fight current non-tariffs restraints that have been faced by international trade actors.

In this context, new topics concerning international trade, some of them overcoming the multilateral framework already enacted, have emerged, registering an escalation of WTO-extra and WTO-plus agreements[2]. Following the most recent preferential trade agreements signed by the EU, such as the Comprehensive Economic and Trade Agreement (CETA) with Canada (in force since 2017) and the Free Trade Agreement with Vietnam (in force since 2016), the EU-MERCOSUR Agreement also overcomes the WTO rules in several topics and aspects becoming a WTO-plus and WTO-extra framework.

For instance, the services chapter includes a list of commitments for all types of services already provided in the General Agreement on Trade in Services (GATS) on the WTO, in each of their modalities: cross-border supply of services (mode 1), consumption abroad (mode 2), commercial presence (mode 3) and the presence of natural persons (mode 4). However, the Agreement goes beyond and touches on immigration-related issues as it provides rules about the movement of foreign professionals temporarily allocated to the other party's territory for the provision of services, licensing procedures for certain services, and transparency. Besides, there are also specific sections with rules for postal services, telecommunications, financial services, and, inserted in the current digital economy-oriented market, an e-commerce section – something that has been discussed in the WTO, but without mandatory rules. Moreover, these segments deal with issues related to anticompetitive practices, industry regulation, taxation of electronic transmissions, among others. Regarding market access, it is important to point out the opening of the market for regional cabotage transport taking into account that, after a transitional period of ten years, MERCOSUR will allow European ships to carry containers by cabotage navigation on the routes between MERCOSUR members (EUROPEAN COMMISSION 2019b).

Also, the MERCOSUR-EU Agreement is innovative because it brings other areas in which Brazil is traditionally resistant to open its domestic market such as Government Procurement. On one hand, the Agreement will open the Mercosur's government procurement market for goods, services, and construction/infrastructure at the federal level for European companies. On the other hand, Brazilian companies will also gain equivalent access to the European market. The opening of this government procurement field may expose the domestic markets to a new level of competition, in which Brazilian and European bidders will compete on an equal footing, something that could be expanded in the future to include government procurement at state and municipal levels. The main concern is that the efficiency of the major European players, more familiarized to an internationalized competition, will be challenging and will demand a boost and improvement by Brazilian companies. Furthermore, the Agreement highlights the importance of corporate responsibility of companies to participate in international bids, being mandatory for them to incorporate best practices into their operations, notably in matters of international trade and regulatory compliance, environmental and labor practices, and anti-corruption actions (EUROPEAN COMMISSION 2019a).

In this context, despite Brazil not having signed the Government Procurement Agreement multilaterally on the WTO yet, it's noteworthy that, through this Agreement, Brazil assumes an unparalleled commitment through regional treaties in this area[3]. The *ratio* for so much resistance lies on the Brazilian purpose to protect the domestic market against foreign competitors on the one hand and, on the other, the overvaluing of some specific internal sectors such as the construction and infrastructure areas for a gradual start and thorough participation in foreign bids – justifying the bilateral and regional commitment then. Following this path, the main criticism to the inclusion of the government procurement chapter in the EU-MERCOSUR Agreement refers to the possible European protectionism against MERCOSUR's companies and their lower level of competitiveness compared to the Europeans – now, even in the Brazilian infrastructure sector, which has suffered after the corruption scandals from the past years related to the Operação Lava Jato (Operation Car Wash) investigations which revealed the involvement of big Brazilian constructing companies in corruption deals.

Even though both topics are examples of innovative and important fields inserted in this new regional framework, the most sensitive topic discussed in the Agreement is how to combine trade liberalization and environmental protection. Concerning the first element, it was negotiated that the openness would be gradual and predictable, so as not to

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harm domestic farmers[4]. From the MERCOSUR's point of view, the EU is traditionally an actor whose market is extremely protectionist for foreign agricultural goods. It may be noticed, for example, the Agricultural Common Policy, which offers financial support to European farmers by subsidizing the prices they pay for producing, besides the lack of competitiveness of the European agricultural products compared to some originated from MERCOSUR, such as beef and poultry meat, soya, sugar, and ethanol. Because of the European lobby based on the sensitivity of the region's agricultural markets, the parties have agreed that the liberalization would be distinct and gradual by product.

At first, the liberalization will proceed immediately for some goods, such as those from the oleaginous sector, then, it will be progressive to others, for instance, roasted coffee – an important product for Brazilian exports – that will be free of tariffs in 7 years. In addition, other products will have widened access to the European market through quotas, such as beef, poultry, and pork meat, sugar, ethanol, rice, honey, and corn meat. All of them will be progressively liberalized in six stages. On the other hand, orange juice and cachaça (a Brazilian spirit) will be subject to a mixed treatment, based on the weight and volume of the products. For cheese, powdered milk, wines, and sparkling wine, for instance, quotas will be offered, being liberalized in 8 years or more.

It is noteworthy that, in MERCOSUR, some sectors have actively lobbied for protection. The most remarkable example is the wine sector from Rio Grande do Sul, in Brazil. Based on familiar farming, they have claimed that the European wine sector is highly subsidized and, with the liberalization, will not face as much taxes as the Brazilian wine sector will do. This would make the European wine more competitive. MERCOSUR negotiators concluded that they could not stop the agreement because of this issue, but at the same time, they could not leave the wine sector helpless. For this reason, a fund was designed aiming at ensuring modernity and more competitiveness for the national product. It will work as a tool to boost the sector as well as it has already been established by the EU through the Regulation (EU) n° 1.308/2013 of the European Parliament and the Council through operational fund programs in the fruit, vegetables, and even the wine sector.

Although trade liberalization has been structured, the agreement has a significant sustainability chapter that values environmental protection. Beyond provisions regarding the implementation of the United Nations Framework Convention on Climate Change (UNFCCC), the Montreal Protocol, the Paris Agreement, the International Labor Organization Conventions, the corporate social responsibility and health standards, among other social-related provisions, the most remarkable issue was the introduction of the precautionary principle. The purpose behind this principle is to anticipate the damage, appreciating the risks to avoid the individual and social consequences (LOPEZ 2010). According to this provision, the mere threat to the environment, in cases when scientific evidence or information is insufficient or inconclusive and there is the risk of serious environmental degradation or to occupational health and safety in its territory, a Party may adopt measures based on the precautionary principle. These measures may involve restraint of trade flows, anytime, even if there is no concrete evidence to a more conclusive assessment.

From the environmental point of view, it means a high level of protection, in which the mere threat of harm, may trigger the enforcement of Article 10.2 of the Trade and Sustainable Development Chapter. However, it could be dangerous for international trade as a whole because it could open margin to disguised discriminations to foreign products with the excuse of environmental protection without scientific evidence. The risk assessment process is not yet very well scrutinized in the Agreement. However, the questions that arise are: Should the damage be risky to whom? Could EU ban a product from MERCOSUR even if, for instance, it contains a carcinogenic substance though not proved, but could threaten European consumers? Would it make sense for the EU to argue this principle if any Brazilian product or action is being harmful to its territory and consumers? Currently, the last issue that could arise is related to the recent cases of fires burning the Amazon, if the serious environmental degradation is considered. Anyway, these questions makes to reflect about how the environment is present in the core of the Agreement and how difficult it will be dealing with these issues, especially for Latin American countries that have more flexible regulation regarding these environmental issues.

Despite the threats of President Emanuel Macron to not sign the MERCOSUR-EU Trade Agreement after the record-breaking number of fires in Brazil's Amazon, the Argentinian elections and the risk of disapproval of the agreement by a new government, and the challenge of ratification by all the MERCOSUR states, all the EU countries and the European Parliament, the timing of the announcement of the EU-MERCOSUR Agreement could not be better for

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globalists and free trade and liberal enthusiasts.

Nowadays, one of the most considerable challenges for the survival of free trade has been the Trade War between the United States and China, a dispute between both economies in raising tariffs on different kinds of products from manufactured to agricultural goods bringing imbalance to international trade. Despite the protectionist environment driven by the US and China, the EU-MERCOSUR Trade Agreement should be seen as a reaction to protectionism, since it involves a significant trade deal in terms of trade flows and framework. It means that, even with all the setbacks and the escalation of a power-oriented environment, the international rule-oriented order is still alive for important actors and they are still shaping the international trade. It is important to bear in mind that these new rules have come with many updates compared to the multilateral trade framework, with a modern inspiration involving technological themes and environmental protections. Finally, it is believed that, at the end of the day, the Agreement will provide an increase in trade flows, freeing tariffs of several goods and fostering market access to both blocs, and MERCOSUR will thrive mainly with its agribusiness exports and EU in exporting industrialized products. However, it is relevant to highlight that not every domestic actor involved in the results of the Agreement will fully win with the negotiations, but the most important issue is that, with the creation of trade-off mechanisms to try to stimulate sectors and minimize losses, the two blocs have tried to mitigate any jeopardies the agreement could cause.

Notes

[1] They may encompass sanitary and phytosanitary measures, technical barriers to trade, quotas, regulatory requirements, among other unfair, discriminatory or excessive requests.

[2] According to the classification developed by Horn, Mavroidis and Sapir, preferential or regional trade rules called WTO extra regulates areas where the multilateral trade rules are inexistent; the WTO plus framework encompass rules that deepen the multilateral framework already enacted and, finally, the WTO Intra agreements simply replicate multilateral trade rules (HORN, MAVROIDIS AND SAPIR 2009).

[3] Brazil has important precedents concerning the government procurement liberalization, two bilateral agreements with Peru and Chile signed in 2016 and in 2018. They have paved the pathway to a wider and stronger liberalization.

[4] This gradual liberalization was provided for industrial goods as well, varying according to the product.

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