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Economic Briefing

Opportunities of the Mercosur agreement

The European Union appears to be on the verge of an agreement with the South American countries of the Mercosur group on a far-reaching free trade agreement. We analyse the possible opportunities for the European industry and consumers. Overall, the agreement would have less of an economic and more of a geopolitical significance and would be a signal for free trade.

The agreement is close to finalisation – despite resistance

After years of negotiations, the European Union could sign a comprehensive free trade agreement with the Mercosur countries, consisting of Argentina, Bolivia, Brazil, Paraguay and Uruguay. The free trade agreement aims to eliminate a large proportion of mutual tariffs, simplify import processes and mutually recognise trademark rights. After the decision by the European Commission, however, the EU member states still have to approve the agreement. This is not a sure thing due to resistance from France and Poland. However, the authorities in Brussels apparently assume that enough votes will be cast in favour for a majority of 65%.

The agreement offers opportunities for the EU economy

Overall, the five Latin American countries, with a combined gross domestic product (GDP) of around 3 trillion US dollars, are only as big as the economy of France. At 60 billion US dollars, the EU's exports of goods to these countries also account for less than 0.3% of European economic output (Chart 1). At first glance, the Mercosur region appears to play a significantly smaller role than other trade partners such as the US or China. Nevertheless, the agreement offers opportunities for the European economy. This is because the region is home to almost 300 million people, and the economy of Brazil, in particular, could grow faster in the future than that of the industrialised countries. An agreement would also eliminate the following tariffs on European exports for this important growth market:

- cars – 35 per cent
- machinery – up to 20 per cent
- chemicals – up to 18 per cent
- pharmaceuticals – up to 14 per cent

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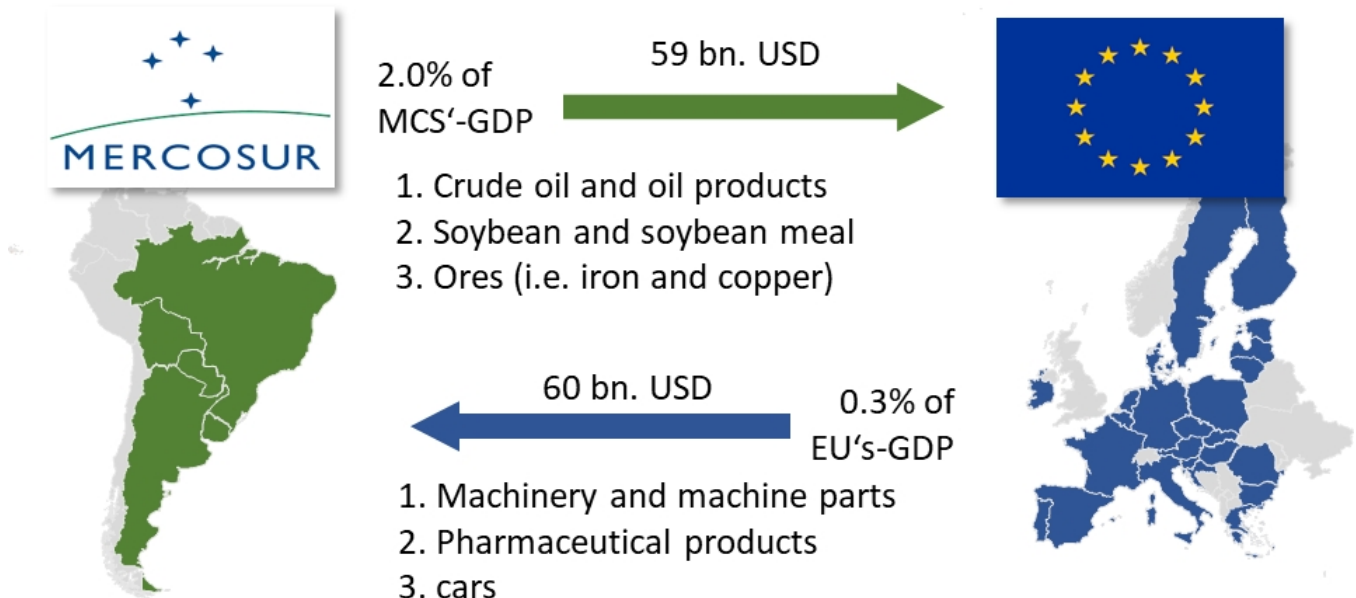
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Chart 1 - Overview of goods trade between the EU and Mercosur

Exports of goods and top three product groups



Source: UN Comtrade, World Bank, Commerzbank Research

These goods already include the EU's main exports to the Mercosur countries. Therefore, the agreement could provide a positive impetus for some ailing industrial sectors. However, due to the relatively low volume of trade flows, the agreement alone cannot revive the EU economy.

Food will not become noticeably cheaper in the EU

The agreement is not likely to fulfil hopes for significantly cheaper beef and poultry in the EU. Although these Latin American countries are important food producers, the envisaged agreement would only provide for tariff reductions on beef and poultry equivalent to less than 2% of annual consumption in Europe. Even these tariff reductions would only be implemented gradually over five years. The food industry is also affected by the large-scale imports of soybeans and soybean meal from South America. However, these imports are already subject to a low customs duty. The price-dampening effects of a tariff reduction would therefore also be limited.

Strategic considerations are at the forefront

Nevertheless, the free trade agreement sends a strong signal in times of burgeoning protectionism. By working more closely with other countries, Europe is making itself less dependent on the US and China. Supply chains can become more stable and diversified. This is also true because South American countries export important raw materials such as copper and lithium. Additional free trade agreements could even mitigate the negative effects of trade disputes with China and the US on the EU economy. This is because goods affected by trade disputes, such as German cars, could be diverted to potential buyers in Latin America. Overall, the agreement with the South American countries could strengthen the European Union's negotiating position with China and other countries.



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