

The EU-Mercosur Free Trade Agreement

A strategic, economic and sustainable win-win

It is time for the EU-Mercosur FTA to be approved. The benefits, on both sides of the Atlantic, could be substantial and could not only facilitate mutually advantageous trade and investment but also contribute to strategic gains and sustainable development.

The four Mercosur countries (Brazil, Argentina, Uruguay and Paraguay) together have a population of 275 million, and their combined GDP makes them the world's sixth-largest economy and therefore one with which we should establish much closer links.

The strategic case

In an increasingly volatile world, the Mercosur countries should be our **natural allies**. They are democratic market economies, with strong cultural bonds to Europe and who share our values.

The Mercosur is **rich in mineral resources** that are in heavy demand in Europe, as the twin green and digital transitions require new suppliers from dependable sources. Many critical raw materials, such as iron ore, bauxite, copper and nickel are extracted in Brazil, while Argentina has vast deposits of lithium. There is thus an opportunity to **diversify away from China** and Russia and other, less-reliable sources of such minerals, and to 'friendshore' with Mercosur¹.

Given that the EU is already the largest importer of these materials from Brazil, why do we need an FTA? That question is based on the assumption of maintaining the status quo. In reality, many countries (Argentina among them) are imposing, or are considering imposing, export restrictions on strategic commodities. The EU-Mercosur agreement will ban or limit most such restrictions, ensuring a continuous and stable supply of vital raw materials for the EU. The agreement therefore can serve as a **hedge against disruption of supply**.

The Mercosur countries currently do not have, and are not negotiating, any similar agreement with the other main economic actors in the world. Thus, were this agreement to enter into force, **European firms will have first mover advantage** to this market and enjoy an edge over our competitors.

If we say 'no' to this agreement, we will be saying 'yes' to something else. The world does not stand still; without this agreement, we are pushing Mercosur closer to China, a process that is already well under way.

The economic case

Some 60,000 European firms export to Mercosur; these companies - and their suppliers - currently **support 850,000 jobs in the EU**.² The EU is the largest trading partner for the Mercosur countries, with the value of trade in goods close to €120 billion in 2022. It is also the largest investor in the region. Yet the remaining untapped potential is immense.

The main economic benefits from this agreement arise as a result of lower costs to trade and greater predictability due to the reduction in, and binding of, tariffs. Mercosur currently has much higher import tariffs than the EU. The average rate is 10-12 %, but for some goods it may reach as much as 35%, and there is also a multitude of other fees and import taxes. It is therefore of **great interest to EU**

¹ [European Economic Security and Access to Critical Raw Materials: Trade, Diversification, and the Role of Mercosur | \(ecipe.org\)](https://ecipe.org/).

² Here you can find data from each EU-country about jobs supported by exports to Mercosur: [EU-Mercosur trade in your town \(europa.eu\)](https://europa.eu/).

exporters to have these tariffs removed. Exporters of products such as motor vehicles, machinery, pharmaceuticals and clothing in the EU will benefit from greater market access.

The EU imposes very high tariffs for certain agricultural products where the Mercosur countries have their strongest competitive advantages, and there will be new opportunities for Mercosur exporters when these tariffs come down. This also presents an opportunity for Europe to limit food price inflation.

With the agreement, **most of the tariffs will be reduced to zero, although the process of bringing them down will be a gradual one so that upheavals can be avoided.** To avoid disruptions to the agricultural markets in Europe, a system of tariff rate quotas (TRQs) has been negotiated, which only allow a certain quota of some sensitive goods to enter the EU from Mercosur tariff-free.

The FTA will also increase predictability. Without the deal, the Mercosur countries have the right to increase tariffs to more than 30% on average. With the deal, however, such tariff hikes cannot take place. Research has shown that the single most important benefit of trade agreements is this increased predictability. Businesses are naturally attracted to a stable and predictable environment. However, economic projections normally fail to capture these effects, which is why they usually **underestimate the economic gains.**³

There are also other benefits in the agreement, for example opening up of the procurement markets, the liberalisation of some trade in services and assistance to SMEs.

The sustainability case

The Mercosur countries aim to expand trade, connect to global value chains with European partners and climb the value-added ladder. They will do so by opening up their economies and making the business climate more predictable. This will spur much-needed EU investment into Mercosur, hopefully contributing to reindustrialisation and creating new jobs in the formal economy. In this way, **trade can lift people out of poverty and contribute to social development.**

Nevertheless, there has been criticism of the agreement on sustainability grounds. Increased trade with the EU, it is assumed, will lead to greater deforestation and other negative effects. However, there are several reasons to believe that this is not the case. Why is this?

First, **the Mercosur countries are becoming increasingly ambitious in their sustainability agendas,** not least on reducing CO₂-emissions and protecting the Amazon rainforest. Brazil is developing its own version of the US Inflation Reduction Act (IRA) and **aims to become a green leader in the developing world.**⁴ Brazil already has a rather green energy mix, and is the second-largest biofuel and hydropower producer globally. It also has the world's seventh-largest wind power production capacity. Uruguay and Paraguay, meanwhile, have a near 100% fossil-free energy mix. In the case of Argentina, it is lagging in its green transition, but it too - along with the other Mercosur countries - is aiming for net zero in 2050, like the EU.

Second, in the event of negative side effects arising from the Mercosur agreement, the EU will soon have several new unilateral instruments that it can deploy. **The deforestation regulation will stop those products that have contributed to this problem from entering the EU market.** Meanwhile, the due diligence legislation will foster sustainable corporate behaviour throughout value chains.

Last, a side letter to the FTA is being negotiated. This will further strengthen what is already the strongest sustainability chapter in any EU FTA.⁵

There is every reason to believe that future trade between our two continents will be based on an increasingly sustainable economic base. This will be one where the EU can contribute to Mercosur with green tech, knowhow and investments, and where Mercosur can contribute with commodities and products that are much greener than goods from alternative import sources.

³ [Economic integration works \(kommerskollegium.se\).](https://www.kommerskollegium.se/en/economic-integration-works)

⁴ [Brazil to launch 'most ambitious' green transition package | Financial Times \(ft.com\).](https://www.ft.com/content/2023/03/23/brazil-launch-green-transition-package)

⁵ With the exception of the recently concluded agreement with New Zealand.