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The Entrance to the European Union of 10 New Countries: Consequences for the Relations with MERCOSUR

Renato G. Flôres Jr.

Special Initiative on Trade and Integration

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This document is part of the first component of the Initiative.

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The impact of the May 2004 enlargement is not, in overall terms, something to worry MERCOSUR decision makers and economic agents. However, this globally non-menacing picture raises, at a closer look, a few concerns demanding pre-emptive policy measures. We shall separate the concerns into five categories, close to the project's main questions:

- *concerning the impact of the enlargement on the European (15) market* - the variety of studies reviewed on this report show gains for the EU15 with the enlargement. Though much intra-industry trade is already taking place, and more will follow in the coming years, usually the EU15 trades higher quality for lower quality goods from the new entrants. Segments in agriculture where the latter can have more advantages still are, and will remain for a few years, carefully controlled. Moreover, it must always be kept in mind that the enlargement is a political move, even if it turns out as a fairly attractive economic deal;

- *concerning MERCOSUR gains in the enlarged European market* - though for many products MERCOSUR will reap further gains, it will lose market share in quite a few products of the shoes & leather, chemicals and cars sectors. In others, like steel or machines, though the overall result is likely to be positive, adjustments will take place. As regards aggregate welfare, the enlargement is positive, be it either under full liberalisation of the MERCOSUR-EU25 trade or under an incomplete one, but the mentioned losses, at the product level, may be sensible. The positive aggregate figures may be interpreted as saying that the algebraic sum of losses and gains is eventually favourable to MERCOSUR;

- *concerning the new entrants gains in the MERCOSUR market* -the new entrants will penetrate deeper (in comparison to the EU15) in selected segments of the MERCOSUR market. These segments are mostly found in a few traditional manufactures and, perhaps a bit surprisingly, also in those with a higher technological content. They will enhance competitiveness effects already present with the EU15, hitting, in particular, electronics and chemical goods, and cars, but also a few products (commodities) in agriculture;

- *concerning the effects on the "agricultural knot"* - the distorting effects of the Common Agricultural Policy (CAP) will take sometime to be fully operational in the new entrants, what may provide a needed extra action time for MERCOSUR. Even when completely implemented -provided the EU doesn't come up with a new "creative scheme" for the CAP-, it seems that its mechanisms will be unable to deter the increasing gains of MERCOSUR's agribusiness. The complexity of the CAP makes it wiser for MERCOSUR, in the Free Trade Agreement (FTA) negotiations, to concentrate on Most Favored Nation (MFN) peaks, in-quota tariffs and (gaining) additional quotas; in this order and, in principle, only on these items. Action in Geneva should be dissociated from this one, concentrating then, in a bold way, in firing at the Blue Box exemptions, curbing, if possible, the Green Box ones, reducing the Aggregate Measurement of Support (AMS) and, finally, the MFN tariffs in general. The new entrants will be a source of undesirable demands for all CAP distortions. This may sometimes put Brussels in check, because of the social tensions -mainly in their farm sector - that will linger on for at least the next ten years. One way the EC may resort to for solving

this riddle is by adding "fat" (special, "extremely green" subsidies) to the Green Box. Though in terms of the EU-MERCOSUR trade flows this might have small to negligible impacts, it is unfortunately very likely that the EU instance in Geneva will become more conservative. MERCOSUR should take this seriously and set efforts to fully understand, monitor and challenge the Blue and Green Box loopholes;

- *the enlargement and distorting effects of the EU-MERCOSUR agreement* - the FTA doesn't seem to be a very distorting regional agreement -with respect to multilateral trade liberalization-, and its trade diversion effects are somehow softened by the enlargement. Even so, it raises an important question MERCOSUR must, sooner or later, face. As perhaps in any North-South agreement it can or will fix -and less, from the available studies, than what is going to happen in the Free Trade Area of the Americas (FTAA)-, the agreement highlights that MERCOSUR may eventually become, essentially, a commodities and agribusiness exporter. Though the pros and cons of this option beg another forum, it seems important to raise this issue as a last conclusion.

THE ENTRANCE TO THE EUROPEAN UNION OF 10 NEW COUNTRIES: CONSEQUENCES FOR THE RELATIONS WITH MERCOSUR

Renato G. Flôres Jr.*

I.   INTRODUCTION[1]

The original call for the *"El Ingreso..."* project mentioned four questions on the 2004 EU enlargement:

(i)   the implied changes in output, trade and the CAP, both in the present 15 members and in the 10 new ones;

(ii) the likely impact on the agricultural negotiations in the Doha Round;

(iii) the impact on the trade flows and relations between the EU and MERCOSUR;

(iv) the impact on the EU trade policy and its implications for the EU-MERCOSUR Agreement.

Though the call is centred on the additional problems the enlargement can bring to the sensible European agricultural sector, something of foremost interest to MERCOSUR countries, the questions cover different issues. They actually encompass a vast spectrum of analyses of the manufactures and agricultural sectors, part of it having already been pursued by several organisations, beyond the EC itself.

The EC has been regularly delivering, for each accession country, "Comprehensive Monitoring Reports" (CMR) on the state of preparedness for EU membership, and has also stimulated research on some of the items above; most specially the first one, given both the great interest in the enlargement from "nearby" members and the fear it arouses in less developed members, like Portugal, Spain, Ireland or Greece. By nearby members we mean not only Austria, Germany and Italy, countries that are close either culturally, or economically, or geographically to most of the new entrants, but also France, a country supposed to gain with the enlargement. Quite a few projects were commissioned in all these countries, in order to get a deeper view from the side of the main winners and losers.

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Apart from this, items (iii) and (iv) nearly make for a single question, as the analysis of the impact on the bilateral relations and trade flows cannot, nowadays, be dissociated from the constraints and demands posed by the EU-MERCOSUR Agreement ongoing negotiations.

These considerations imply that, as outlined in our proposal, different methodologies - along three main lines - will be used for points (i), (ii) and (iii) + (iv) together; innovative modelling efforts being concentrated mostly in this last group. Notwithstanding, the project output will be a single unity where findings in each sub-area will interrelate.

The structure of this report is as follows. Sections II to VI are the core of the study. The first reviews evidences and work on (i), while Section III develops, in more detail, the "agriculture issue" (point ii). Section IV is a little digression on the methodology used to tackle points (iii) and (iv), while Sections V and VI present the results from the corresponding partial and general equilibrium exercises, respectively.

Section VII is a very short tie up, as the executive summary of all the previous information and findings - (hopefully) producing a coherent view of the impact of the enlargement on the EU-MERCOSUR trade in goods relations - appeared already at the beginning of the report.

II. THE ENLARGEMENT AND ITS IMPACT ON THE EU - A CRITICAL SURVEY OF AVAILABLE EVIDENCE

A. The Ten New Entrants: a Few Basic Facts

The idea of "enlargement" has broad connotations for the EU, being considered nowadays as an ongoing process that will surely last for more than ten years. The memberships to be fully accepted in May 2004 are but a wave in a movement that three years later will absorb Bulgaria and Romania, sometime after other republics from the Balkans, perhaps quite later Turkey and which, in principle, does not exclude - some day in the future - other Central European countries, as well as North-African economies. It is a strategic and political decision that, in spite of having its evolution conditioned by manifold external factors, seems to be in the hearts & minds of the key agents of the EU project. This very general point is important to put into a dynamic perspective the analyses which will follow.

The 2004 new entrants comprise the three Baltic republics - Estonia, Latvia and Lithuania -, three of the former "big five" Warsaw pact members - Slovakia, Hungary, Poland and the Czech Republic,[2] also known as the Visegrad group -, a single country from the Balkans, Slovenia, and the islands of Cyprus and Malta.

Tables 1A and 1B shows a few indicators for the new entrants. If one adds to them the two countries supposed to join in 2007 (Bulgaria and Romania) this means that, in the next four years, the EU will be absorbing a bloc of more than 102 million people, roughly equivalent to one half of MERCOSUR. However, these people have a much higher educational level and make for a more homogenous population, with less social inequalities, as evidenced, for instance, by the small spread of the Life Expectancy indicator. Moreover, in spite of its distance to the EU15 figure, the per capita income of this group is higher than that of MERCOSUR members. If measured by the ppp - purchasing power parity -, per capita income results usually higher than the sheer division of the figures in the third and second columns in Table 1.A, ranging, in 1999, from 4,871 euros/head, for Bulgaria, to 14,492 euros/head for Slovenia.[3] Table 1.B shows these values, as percentage of the EU15 average (=100) in 2002.

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[2] One must keep in mind that Slovakia and the Czech Republic formed a single country under the Iron Curtain.

[3] Values computed by the EC.

TABLE 1.A
THE 10 NEW MEMBERS - A FEW BASIC DATA: POPULATION (IN MILLION PEOPLE, 2002),
GDP (IN BILLIONS US$, 2001)[1] AND LIFE EXPECTANCY
(In years, since the date of birth)

Countries	Population	GDP	Life Expectancy
Estonia	1.40	5.50	70.50
Latvia	2.40	7.50	70.30
Lithuania	3.70	12.00	71.40
Slovakia	5.40	20.50	70.20
Hungary	10.00	51.90	69.30
Poland	38.60	176.30	70.20
Czech Republic	10.30	56.80	69.90
Slovenia	2.00	18.80	69.40
Cyprus	0.80	9.10	75.50 / 80.00[2]
Malta	0.39	3.60	75.00 / 79.00[2]
Total	75.00	362.00	--

Notes: [1] These data must be taken with a certain care.

 [2] Men / women.

Sources: The World Bank, Eurostat, the EC.

TABLE 1.B
THE 10 NEW MEMBERS - A FEW BASIC DATA: GDP PER CAPITA, UNDER PPP,
AS PERCENTAGE OF THE EU AVERAGE, 2002
(Data for Cyprus and Malta refer to 2001)

Countries	GDP (ppp)
Estonia	44.6
Latvia	32.2
Lithuania	36.1
Slovakia	49.1
Hungary	51.6
Poland	37.2
Czech Republic	59.8
Slovenia	69.6
Cyprus	80.0
Malta	55.0

Sources: Eurostat.

The distance to the EU15 levels is rather serious. Calculations by the Economist Intelligence Unit (EIU) [2003] show that even the wealthier countries, like Slovenia or Hungary, if experiencing an average annual Gross Domestic Product (GDP) per person growth rate of 3.2 to 4 percent, while the EU15 rate would stay at 2 percent, would need 31 to 34 years to reach the EU15 average GDP per capita. Wealth imbalances will then persist for quite a long time, and will certainly be a source of tensions.

Of course, statements of this kind - which eventually are related to the convergence among the different economies[4] - are a function of the several hypotheses assumed, ranging from demographics to the changes in total factor productivity. Population growth has stagnated in the accession countries, and there are signs that it will approach, for most of them, the negative rates experienced by most EU15 members. If this is a positive contribution to GDP per capita increase, on the other hand, empirical evidences from similar situations (see Baldwin and Seghezza [1996 and 1998], for instance) point out that total factor productivity growth is higher in the incumbent countries. Two simple sets of absolute figures, related to Portugal and Spain, wrap up somehow these arguments and add support to the statements in the previous paragraph. Spain's GDP per capita, in 1960, was US$ 3,379 below the EU15 average, and, in 2001, US$ 3,610; corresponding values for Portugal being US$ 4,700 and US$ 5,637 (all values in 1995 US$, and under ppp).

It is also interesting to contrast the situation *vis à vis* EU15 with the one related to MERCOSUR. Table 2 shows the yearly growth rate for the Visegrad group plus Slovenia. But for the recession experienced by the Czech Republic during 1997-1999 one sees that, contrary to what happened with MERCOSUR countries in the same period, all are economies with annual rates usually higher than 2 percent. Leaving out the Czech Republic, the others have grown at an average annual rate higher than 4.0 percent during the six years displayed.

For the period from 2004 onwards, with the exception of the Czech Republic and Slovakia, a slowing down from the rates at the end of the nineties is forecasted. The better Czech figure is explained by the continuation of its economic recovery, while the Slovakian one reflects the expected dynamism of this economy.[5] Earlier forecasts by the Commission[6] predicted that, with the adhesion process, rates - after going down in the early two-thousands - would soon come back to the past values, with a high probability of reaching the 4-5 percent interval.

Contrasted with any of these estimates, MERCOSUR members continue to show timid growth rates, around or lower than 2 percent, when not negative. Undoubtedly, during 2004, the EU15 will be absorbing a much more dynamic "half MERCOSUR" that, in the medium to long run, may become an even fiercer and more powerful competitor.

In one dimension, however, accession countries are closer to MERCOSUR ones: regional disparities. While among the fifty poorest regions (at the NUTS II level)[7] in the enlarged EU25, thirty-six lie in the ten entrants - with the twenty-nine poorest ones being located in them -, the Prague region, already in 2000, was 21 percent above the EU15 average, and 33.4 percent above the EU25 one. Table 3 summarises, for this year, the distribution, by countries, of the fifty poorest regions.

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[4]   Kaitila [2004] studies β and σ-convergence, for the period 1960-2001, both for the EU15 and the EU15 plus the Visegrad and Baltic economies.

[5]   For a somewhat less optimistic view on these two economies - specially due to specific macroeconomic imbalances - see Johnson [2003].

[6]   Produced by the EC, in the first quarter of 2003. The lower figures which took place in 2001/2002 were mainly due to a significant slowdown in Poland.

[7]   The EC/Eurostat has three different spatial levels to collect statistical data: the NUTS I, II and III. Country data are at the NUTS I level, while NUTS II corresponds to regional data, in the EC language. At present, there are 231 NUTS II regions in the EU15; the ten accession countries are going to account for 46 new ones. The NUTS III level roughly corresponds to "county level" data.

TABLE 2
ANNUAL GROWTH RATE (GDP, IN PERCENT) FOR SELECTED NEW MEMBERS
1995-2000 and estimates for 2004 on

	1995	1996	1997	1998	1999	2000	Accum.	2004 on
Slovakia	6.9	6.6	6.5	4.1	1.9	2.2	31.6	4.0/4.8
Hungary	1.5	1.3	4.6	4.9	4.4	5.2	23.9	4.0/4.9
Poland	7.0	6.0	6.9	4.8	4.1	4.1	37.7	3.8/3.9
Czech Republic	6.4	3.9	-1.0	-2.2	-0.8	3.1	9.5	3.7/3.8
Slovenia	4.1	3.5	4.6	3.8	5.2	4.8	29.0	3.2/4.0

Sources: the EC and EIU.

TABLE 3
THE POOREST 50 REGIONS, IN (RELATIVE) *PER CAPITA* GDP UNDER PPP,* IN THE EU25
Distribution by country, 2000

Country	Number of regions	Average	Min	Max
Poland	16	39.6	29.4	64.9
Czech Republic	7	52.6	49.6	57.7
Hungary	6	44.7	34.7	62.4
Greece	5	59.4	51.9	65.2
Portugal	4	59.6	57.0	61.7
Slovakia	3	42.9	39.1	47.0
France**	3	59.4	55.6	63.5
Spain	2	62.9	58.4	67.4
Latvia	1		34.0	
Lithuania	1		39.3	
Estonia	1		44.2	
Malta	1		60.7	
Total	50	48.3	29.4	67.4

Note: * EU25 = 100.

　　** The three French regions refer to territoires d'outremer (Réunion, Guyane and Guadeloupe).

Source: Eurostat.

As it can be seen, Poland not only has the greatest number of poor regions[8] as one of the lowest averages. Even for a "more advanced economy" like Hungary, its poorest regions display a worse profile than those in the two EU15 laggards, Greece and Portugal.

Welfare distances matter in two dimensions: within the entrants and between them and the present members. Taking into account the reasonably long period for catching up mentioned above, a horizon of around ten years of internal social tensions within the biggest new members can be

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[8]　　One must however take into account the size disparity between Poland and countries like Latvia or Estonia, for instance.

easily expected. It is also worth remembering that the ability to catch up depends on the starting level of the region, as demonstrated even in Spain, for instance, with the development rates, since accession, of Catalunya and Andalucia.

B. Trade Relations

Another important point is how the enlargement countries link themselves with the EU15 and their other neighbours. Table 4 shows the intensity of trade flows between each of the new members and the EU15, highlighting the four most important partners.[9] Poland, Estonia and Slovenia were the biggest global importers, while Latvia and Lithuania were the smallest ones; what signals that these two economies are still rather closed to the EU. An important point to explain the latter - and something that will be further explored below - is the strength of the ties these nations still have with the former USSR. Lithuania, for instance, separates (with Poland) the Russian enclave of Kalingrad[10] from Belarus, while 20 percent of Latvia's two-and-a-half million souls are non-citizens, i.e., Russians.

Germany is clearly the champion in these markets, being responsible for a little more than 41.5 percent of the EU exports to the ten entrants plus Bulgaria and Romania. It is important to remark that Russia held, in the same year, shares of 5.8 and 4.8 percent, respectively, of the imports from Hungary and Poland, being, in most cases, among the four biggest exporters to the new members. This Russian penetration raises additional doubts about MERCOSUR possibilities in the entrants markets.

Overall, taking out the two islands and adding Bulgaria and Rumania, these ten countries have been the EU's most dynamic trade partners. While, from 1995 to 2000, EU global exports grew by 63 percent, to these ten economies the increase was of 112 percent; figures of 84 and 118 percent, respectively, taking place for imports. As Table 5 shows, though the EU15 has been running global trade deficits, it has accumulated surpluses with the same ten countries.

In exports terms, Hungary can already be considered a competitive partner to the EU15, having a positive trade balance with the majority of its members. Actually, there is a strong concentration of trade flows in three of the Visegrad economies: the Czech Republic, Hungary and Poland. Considering the same group of Eastern economies in Table 5, around 70 percent of the EU15 exports to and 68 percent of its imports from them are with these three countries. Moreover, around 60 percent of the trade surplus is due to a single bilateral relationship: the one with Poland.

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[9] Taking globally the ten. Countrywise, positions may differ (Finland and Sweden, for instance, are the main exporters to Estonia).

[10] Known, in the past, as Königsberg, the ancient capital of Prussia.

TABLE 4
**MARKET SHARE (IN PERCENT) OF THE EU-15, AND ITS FOUR MAIN EXPORTERS,
IN TOTAL IMPORTS OF THE NEW MEMBERS; 1999**

	EU15	Germany	Italy	France	Austria
Estonia	73.8	9.4	4.7	2.1	0.9
Latvia	43.4	11.8	3.4	2.4	1.0
Lithuania	44.6	15.5	5.2	2.8	1.0
Slovakia	52.3	26.7	7.5	3.5	5.7
Hungary	64.4	29.2	7.7	4.7	8.9
Poland	74.2	31.8	10.0	7.1	2.2
Czech Rp.	67.0	37.0	5.3	4.8	5.8
Slovenia	69.9	20.7	16.8	11.5	8.3
Cyprus	53.2	7.3	9.0	5.4	0.5
Malta	62.2	8.9	18.8	15.6	0.5

Source: IMF Direction of Trade Statistics.

TABLE 5
**EU-15 TRADE SURPLUS (OR DEFICIT [-]), IN BILLIONS OF EUROS, FROM 1995 TO 2000:
GLOBAL AND WITH TEN EASTERN EUROPEAN (EE) ECONOMIES**
(The 2004 entrants but Cyprus and Malta, plus Bulgaria and Romania)

	Accum. (1995-2000)	2000	1999
Global	45	-86	-14
10 EE econ.	100	17	16

This asymmetry is also present in the pattern of trade, be it in its sectoral composition or in the respective terms of trade (tot). Table 6 highlights quite a few interesting points. The first is a reflection of former Soviet policies which imposed on the Iron Curtain economies a heavy industrialisation process. Exports of manufactures (sectors 5 to 8) are predominant in the five countries, ranging from 85.2 percent for Poland to 94.0 for Slovenia. All countries present nearly the same share of chemicals exports, and quite large figures in the machinery & transport equipment and other manufactures sectors. The latter is predominant for Poland and Slovenia, while the former is for the other three. In the case of Hungary, machinery & transport equipment exports reach 63.4 percent of its total flow. This country, together with Poland, has the biggest, though relatively modest, shares in agricultural exports. These small values - 4.5 and 5.4, respectively - may seem surprising, but result naturally from a few points. The first is the above mentioned high concentration of industrial production. Secondly, it is also a consequence of the still imposed EU15 agricultural barriers, leaving a small penetration margin for the Central and Eastern European produce. Part of these barriers has been dismantled - to the accession countries - after 2000, but many are still on, with some lingering after May, 2004.[11] Finally, bigger agricultural economies like Hungary and Poland are heavily oriented to supplying their internal markets.

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[11]   Notice that data in Table 6 refer to 2000.

TABLE **6**
**SECTORAL COMPOSITION, IN PERCENTAGE OF THE TOTAL FLOW, OF THE EXPORTS TO THE
EU15, FOR THE FIVE BIGGEST ACCESSION ECONOMIES; 2000**

	0+1	2+4	3	5	7	6+8
Czech Republic	1.6	4.3	2.1	4.7	49.2	36.8
Hungary	4.5	2.3	1.4	4.8	63.4	22.2
Poland	5.4	3.1	4.9	4.7	34.9	45.6
Slovakia	1.0	3.5	3.4	5.0	45.7	38.1
Slovenia	1.0	2.6	0.0	4.7	41.0	48.3

Notes: Sectors 0+1- food, beverage and tobacco; 2+4- raw materials; 3- energy; 5- chemical products; 6+8- miscellaneous manufactured goods; 7- machinery and transport equipment.

Source: Eurostat [2001].

The considerations extracted from Table 6 raise further concerns as regards the possibility of MERCOSUR exports penetrating these markets. Not only are they competitive producers in traditional manufacturing sectors where MERCOSUR shares an international position, but their agriculture markets look as close as that of the EU15 as well. Flôres [2003a] had already highlighted this point.

Sectoral information may be complemented by the tot pattern, available - in a partial proxy - for the case of Germany. Table 7 shows the Deutsche Mark (DM) value of one ton of German imports from eight accession countries. As regards manufactures, Hungary - and more even Slovenia - is practically an advanced, or average, exporter to Germany. In spite of the previous evidence on the larger agricultural shares for Hungary and Poland, the first has the highest average DM value for all trade and, by far, the highest one for manufactured goods; while the corresponding ones for Poland are quite low. Among the eight countries in the table, Hungary and Slovenia show the ratios between the all commodities and manufactures values closer to one.[12] The lowest C/M figures are those for Poland, as expected, and Estonia. The former "Czechoslovakia" and the two other Baltic republics have, roughly, the same ratio.

Beyond the Baltic countries, Poland seems to be a lower goods exporter to Germany, presenting absolute figures quite below those for Greece. With the exception of Hungary, the remaining Visegrad countries also have a relatively large distance between the two values, confirming, in spite of the emphasis on industry in their economies, the importance of commodities in their exports' profile. Balkanic Slovenia, as in other dimensions, stands as the (modern) exception.

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[12]   Or the lowest inverse ratios, 2.3 and 1.4, respectively; an indirect way of signalling the importance of manufactures in the global exports (to Germany) flow.

TABLE 7

EXPORTS OF EIGHT ACCESSION COUNTRIES TO GERMANY: DM VALUE OF ONE TON OF GOODS, ALL COMMODITIES AND FINAL MANUFACTURED GOODS, 2000

Countries	All commodities (C)	Manufactured goods (M)	C / M
Estonia	988	5,499	0.18
Latvia	766	2,749	0.28
Lithuania	1,296	4,427	0.29
Slovakia	2,647	8,986	0.29
Hungary	7,075	16,163	0.44
Poland	971	4,489	0.22
Czech Republic	1,682	6,427	0.26
Slovenia	6,807	9,936	0.69
A few comparisons			
Spain	4,654	12,470	0.37
Greece	3,636	5,011	0.73
All German imports	2,103	16,635	0.13

Source: Statistiches Bundesamt [2001].

These evidences point to an exports' pattern to the EU15 that is similar to the one exhibited by MERCOSUR economies. They can be complemented by intra-industry trade (IIT) indexes computed in the interesting study by Gabrisch and Segnana [2003]. The first set of numbers in Table 8 broadly confirms the previous insights. Baltic countries trade is heavily inter-industry - specially for Latvia and Lithuania -, while for Hungary, the Czech Republic and Slovenia the predominance of intra-industry trade has already emerged. Poland is in a borderline situation, only the GLadj[13] surpassing a half. For most countries there are a negligible difference between the basic and the adjusted indexes, signalling that trade with the EU is nearly balanced in the categories used for the calculations. Poland is the most unbalanced, with the adjusted index being a little more than 30 percent higher than the basic one. It must be said that the trade imbalances are always in the direction of a EU surplus. Finally, in all countries, vertical IIT dominates the index; as will be mentioned below, the vertical trade is, once again, mostly favourable to the EU15.

The same applies to the second set of numbers, though one must keep in mind that Bulgaria, Romania and Turkey are included in the calculations. The four members in the table are exactly those in Table 4, and happen to show the highest (unadjusted) GL's, confirming the closer link between their economies and those of the candidates. Trade is less balanced with France and Italy, but, in all cases, vertical IIT predominates.

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[13]   Adjusted Grubel-Lloyd index; see Table 7.

TABLE 8
**GRUBEL-LLOYD INDICES, BASIC AND ADJUSTED (GL AND GLADJ), HORIZONTAL
AND VERTICAL IIT, OF SELECTED CANDIDATE COUNTRIES WITH THE EU15,
AND OF SELECTED EU MEMBERS WITH 11 CANDIDATE COUNTRIES* - 2000**
(Computed for 778 industries, comprising SITC chapters 3 to 8)

	GL	HIIT	VIIT	GLadj	HIITadj
With the EU15					
Estonia	0.260	0.020	0.240	0.267	0.020
Latvia	0.122	0.020	0.102	0.124	0.020
Lithuania	0.182	0.008	0.174	0.206	0.009
Slovakia	0.402	0.088	0.314	0.418	0.092
Hungary	0.508	0.120	0.387	0.509	0.121
Poland	0.423	0.100	0.323	0.551	0.130
Czech Republic	0.598	0.091	0.507	0.637	0.097
Slovenia	0.511	0.113	0.398	0.574	0.127
With candidate countries					
Austria	0.537	0.137	0.401	0.563	0.143
France	0.500	0.050	0.450	0.628	0.063
Germany	0.548	0.084	0.464	0.584	0.089
Italy	0.441	0.106	0.335	0.537	0.129

Note: * These eleven countries are those of the 2004 enlargement, but Cyprus and Malta, plus Bulgaria, Romania and Turkey.

Source: Gabrisch and Segnana [2003].

Two points, among the conclusions in Gabrisch and Segnana [2003], seem relevant for our purposes. Firstly, as it usually takes place in the European project, the IIT dimension of trade of the candidates with the EU is increasing towards values similar to those in the trade among the EU15. As in this case, vertical IIT predominates. However, an important change took place from 1993 to 2000. While in 1993 vertical IIT was mostly to the advantage of the candidates - signalling mainly (their) cost competitiveness rather than higher quality -, the situation reversed completely in 2000, when the quality advantage of the EU15 accounted for about 66 percent of the vertical IIT, while that of the candidates decreased to 34 percent. Closer integration to the EU15, ironically, increased, in the average, the cost of their products.

In a similar vein, Yilmaz and Ergun [2003] analysed the competitiveness and specialisation patterns, *vis à vis* EU15, of the Visegrad countries but Slovakia plus Bulgaria, Romania and Turkey. Though resorting to seven different sets of indexes, instead of using Grubel-Lloyd-like indexes, their conclusions - for the three May 2004 accession countries - are roughly the same as those of the previous study. With the exception of Hungary, that shows some competitiveness in research-oriented goods,[14] the three are mostly specialised in raw-material, labour and, less, capital-intensive goods; loosing somewhat their edge in the first two groups. Moreover, confirming evidences in Tables 4 and 8, their trade with the EU15 is still quite concentrated in a few countries.

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[14] The authors distinguish between easy-to-imitate and difficult-to-imitate research-oriented goods, the two being found basically in SITC groups 5, 7 and 8 (this, only 87 and 88).

All the issues treated till now naturally lead to the Foreign Direct Investment (FDI) question, many, specially those from the accession countries themselves, being hopeful that the present gaps will be quickly shortened by a new surge in FDI, after May 1, 2004. Indeed, FDI flows, which for some countries were even negative in the early period of the transition, started to increase by 1995, reaching a peak in 2000-2001. However, the flows were not very regular, beyond strongly favouring, in absolute terms, the Czech Republic and Poland.

Table 9 gives an idea of the mounting wave, for the Visegrad economies. In spite of based on IMF's World Investment Report, funnily enough, they do not match exactly those from other sources, like, for instance, EBRD [2002].

A careful study of the FDI situation, and its impact on trade flows, would be largely outside the scope of this project. A few bullet points can however be raised:

(i) a main competitor for the FDI flows, sharing top preference with Poland and the Czech Republic, is Russia;

TABLE 9
WORLD FDI INCOMING FLOWS FOR THE VISEGRAD COUNTRIES, 1995-2000
(In US$ billion current)

	1995	1996	1997	1998	1999	2000
Czech Republic	2.56	1.46	1.30	3.72	6.32	4.60
Hungary	4.45	2.28	2.17	2.04	1.94	1.96
Poland	3.66	4.50	4.91	6.37	7.27	10.00
Slovakia	0.20	0.25	0.21	0.63	0.36	2.08

Source: World Investment Report [2001].

(ii) though the bulk of the flows originate from the EU15, the US usually has an important presence;

(iii) not infrequently, FDI is concentrated on a few sectors or firms, with clear trade purposes, specially as regards subcontracting. Elcoteq Tallin, a subsidiary of a Finnish maker of cell phone components from imported inputs (mainly from China), accounts for around 26 to 30 percent of Estonian exports. Machinery and transport equipment are other preferred sectors, with, for instance, Volkswagen Slovakia accounting for over 16 percent of the country's exports.

What is going to happen in this and the coming years is difficult to predict, though a new surge like the one in 1995-2000 doesn't seem very likely. The authors of this study think that a sizeable part of the FDI that will take place will continue to be of the "Smith-Venables Europe 92-type", i.e., either sheer reallocation or increase in the production scale, of existing firms, for the new EU25 space, reinforcing, in the ten entrants, the concentration of specific sectors, like those mentioned in (iii) above.

A final important point as regards FDI is whether - even if a surge like the one in the late nineties doesn't take place - the enlargement will have a diversionary effect on the EU15 investments in MERCOSUR. We think that here the concept of "nearby" members plays a key role. Under this hypothesis, we would venture that diversion can take place for Germany, is likely in the cases of France, Italy and the United Kingdom, and probably doesn't apply for Spain and Portugal. A conjecture that calls for a more substantial support.

C.   Shedding a Little More Light on the Agricultural Sector

The Situation until Now

Notwithstanding the heavy industrialization effort imposed by the former Soviet rulers, most of the accession countries had - and still maintain - a strong agricultural vocation. Table 10 shows key statistics related to the sector. In all countries, agriculture has a larger share in GDP than in the EU15 aggregate; though higher in the Baltic economies and Slovakia, the shares are still fairly considerable in the "advanced economies" of Hungary and Slovenia.[15] Anyhow, even comparing them with recent values as, for instance, the 1989 ones, they represent a substantial drop. On the other hand, the labour force figures have increased since then.

In absolute terms, the Visegrad values plus Lithuania's are the most significant ones. Admitting that output valuations are identical - or, rather, quite close - to those for the EU15, the sector seems to be much less efficient than in the existing Union: for a used surface 29.1 percent of that in the EU15, a labour force equivalent to 55.8 percent generates only 7.1 percent of total (agriculture) value added in the EU15. In other words, land productivity is around a quarter and labour productivity is only 12.7 percent of the corresponding EU15 values. No wonder, a high labour force per ha ratio is evident in most countries, further signalling the low productivity of the sector. In this context, the figures for Poland are particularly noteworthy.

TABLE **10**
THE AGRICULTURAL SECTOR IN THE TEN 2004 CANDIDATES - SURFACE (IN 1,000 HA), VALUE ADDED (IN MILLION EUROS AND AS PERCENT OF GDP) AND LABOUR FORCE (IN 1,000 PEOPLE), 2000

Countries	Surface	Value Added	Labour
Estonia	891	254 / 4.7	46
Latvia	2,488	306 / 4.0	118
Lithuania	3,489	836 / 6.9	262
Slovakia	2,440	560 / 4.5	119
Hungary	5,854	1,913 / 3.9	227
Poland	18,220	4,965 / 2.9	2,698
Czech Republic	4,282	1,846 / 3.4	208
Slovenia	491	847 / 2.9	81
Cyprus	134	329 / 3.5	14
Malta	12	78 / 2.0	3
Total	38,301	11,934 / -	3,776
Total EU-15	131,619	167,197 / 2.0	6,767

Source: EC, processed.

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[15]   The way to compute these shares is, of course, a function of how agricultural output is valued. The percentage figures in Table 10 are not exactly coincident with those estimated, for instance, by the OECD.

These poor ratios - beyond the interesting methodological points raised by Marcours and Swinnen [1998] - are largerly explained by the transition to capitalism. Undoubtedly, the transition represented a strong blow to the agricultural sector, with a sizeable loss of traditional, Eastern markets and a differential increase in the price of inputs - in contrast to nearly stable food prices. Most seriously, monopoly food processors and distributors persisted in dominating each link in the food chain, increasing the gap between prices at the "farm's gate" and final retail prices. Privatisation, devolution of land to ancient owners, together with restructuring of several farms, added to the uncertain and sometimes chaotic situation in many regions. The crisis affected more the animal produce sector, where massive losses of capital brought output down to levels far lower than those in Soviet times.

Pouliquen [2001a, 2001b] summarizes the above problems in the following terms:

a) in the Visegrad, Poland's extremely low productivity is mainly due to the high density of labour per ha (14.8/100 ha), a consequence of the predominance of micro to small farms. Ironically, this pattern - also present in Slovenia - helped in better preserving the sector during the transition. Though in the other three countries the larger farms (700 to 2,000 ha of used surface) have reasonably stood to (disruptive) fragmentation - their labour ratios are 4.9/100 ha for Slovakia and the Czech Republic, and 3.9/100 ha for Hungary - this was not sufficient to avoid a substantial decrease in output, leading to nowadays stagnation. If small to micro properties, nearly entirely devoted to self consumption (subsistence), answer for 60 percent of Poland's agricultural output, they still account for 40 percent in Hungary and 20 percent in the Czech Republic. On the other hand, larger farms account for 10 percent of output in Poland, but for 47 and 65 percent, respectively, in these two other countries. This leaves to middle-sized farms, similar to those common in the EU15, a smallish share in output;

b) the Baltic countries, with the exception of Estonia, present both a pattern and development similar to Poland's.

In the midst of the transition troubles, accession countries tried to fix among themselves preferential agreements for agricultural goods. The Baltic Free Trade Agreement (FTA), which came into effect in January 1997 and increased agricultural trade among its three associates is a good example of such efforts. It has also provided some convergence in farm gate and retail prices across the members. However, upon accession - as happened in 1995 with Austria, Finland and Sweden - all such agreements, as well as those with parties outside the EU will have to be abrogated, being replaced by the EU existing terms on each case.

As a result of these facts, in 2002, all the other new members but Hungary were net importers of food and agricultural products from the EU15. Table 11 gives a detailed picture of the situation.

TABLE 11
TRADE IN FOOD AND AGRICULTURAL PRODUCTS IN THE TEN 2004 NEW MEMBERS - 2002
(In million euros)

Countries	World Trade		Trade with the EU15	
	Imports	Exports	Imports	Exports
Estonia	444.4	132.6	266.5	54.9
Latvia	450.4	107.5	208.5	41.3
Lithuania	563.5	438.0	251.7	158.5
Slovakia	867.6	447.9	354.4	101.4
Hungary	1,167.4	2,439.0	564.7	1,140.9
Poland	3,542.5	2,761.6	1,924.2	1,272.5
Czech Republic	1,977.2	1,383.5	971.8	531.3
Slovenia	739.7	394.4	383.8	102.2
Cyprus	405.2	114.4	250.7	75.7
Malta	303.5	64.5	229.7	7.1
Total	10,461.4	8,283.4	5,406.0	3,485.8

Source: EC, processed.

Taking, from the table, the net world and EU15 trade balances, one sees that the EU15 deficit (-1 920.0) is 88.2 percent of the world deficit (-2 178.0); meaning, as expected, that the EU15 is the great exporter which is reaping profits from the accession economies. Indeed, with the exception of Latvia, Slovakia and Hungary (for this one a surplus), the individual countries deficit with the EU is quite close to that with the world.

The inclusion of this sizeable and more backwards agricultural stake will certainly mean additional stress to the already problematic European common agricultural policy - the CAP.

The Common Agricultural Policy and the New Entrants

As known, the CAP, a policy agreed on 1962 by the six founding members, translated into actions general objectives concerning agriculture, embodied in Art. 39[16] of the Treaty of Rome. It consisted basically of three mechanisms:

i)   protection against low internal prices, through a system of buying surplus output from farmers, when the good falls below a "guarantee price" established for the EU market;

ii) protection against low import prices, through a system of quotas and tariffs on imported goods, when, again, the world price of the good falls below a "guarantee price" established for the EU market;

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[16]   This is the original numbering of the article.

iii) subsidies to achieve a low export price, through a system of refunds for the exporter when, once again, the world price of the good falls below an established value.

The result was a generous indirect income support for farmers, paid out by the EU budget and the consumers, through the high prices of imported agricultural goods. The producer subsidy equivalent (PSE), a standard measure to gauge the extent of agricultural subsidies,[17] is very high for several products or groups of products, notably rice, cereals (wheat, maize, among others), dairy products and bovine meat. Budgetary funds rose from 2 billion euros in 1970 to 11.6 billion in 1980, and then 31.6 in 1990. The EU became an agricultural power and, for most subsidised goods, huge surpluses started to pose questions on the logic of the whole policy.

As a consequence, the CAP underwent major reforms. The latest ones were the 1992 MacSharry Reform, followed by the one in the Agenda 2000 and its revision, mandated by the Berlin Council and done from July 2002 to July 2003. At the same time, following the Agreement on Agriculture eventually included in Annex 1A of the Uruguay Round results,[18] actual negotiations on the CAP began in 2000, at the World Trade Organization (WTO).

There is no point in surveying all the changes and subtle technicalities involved in all these reforms and negotiations. The MacSharry Reform, finalised in May 1992, contained many innovative and positive ideas, though a substantial part of it was not implemented, thanks to the united Franco-German opposition. A most important and feasible idea, however, was the concept of decoupling, that disconnects the amount of subsidy to the volume of production, giving origin to what has been called direct payments to the farmer. Decoupling, together with the already established WTO rules (and others being proposed) marks a starting point to control and progressively force a considerable shrink on the size of the CAP.

The Agenda 2000 reform was again jeopardised, now mostly by France, and the final text which came out of the 1999 Berlin Summit considerably watered down the original proposals by the Commission. Broadly, most of the (further) reductions in support prices triggered by the Agenda were offset by increases in direct payments.

Accession countries, given their economic structure and problems here outlined, see a classical CAP - more generous yet, if possible - as one of the greatest rewards to EU membership. The prospect of enlargement has unfortunately encouraged adoption of distorting market regulation systems, *à la* CAP, even by those more modern economies, committed to the creation of a market-oriented agriculture.

For helping the entrants prepare to engage in the CAP, the EC created programme SAPARD – Special Adhesion Programme for Agriculture and Rural Development, with a budget of 520 millions of euros (in 1999 prices) for the 2000-2006 period. One of the most elaborate preparations is the establishment of the Integrated Administration and Control System (IACS), which, beyond

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[17] Since 1998 the OECD has changed the name of both the Producer and Consumer Subsidy Equivalent into Producer and Consumer Support Equivalent, and modified somehow the way to compute them.

[18] Actually, of the Marrakesh Agreement Establishing the WTO. For this and all legal texts regarding the Uruguay Round results we shall be using WTO [1995].

administrative controls, includes field inspections and on the spot checks for five percent of area aid applications.[19]

In an internal January 2002 document, the EC recognises the food and agriculture imbalance that is taking place in the candidate countries and justifies the CAP for them as a way to minimise it and sustain local production. It targets grains as the most needed sector (the help should also contemplate their use in several kinds of animal food), followed by dairy products and meat, where care should be taken, in general, to avoid surpluses, though a higher and sustainable output of bovine meat would be desirable.

This document set the basis for key decisions taken at the December 2002 Council, in Copenhagen. The controversial direct payments issue, through which producers are (directly) compensated for a fall from the agreed price, was agreed to be progressively introduced in the new members, starting at 25 percent of the EU15 levels, increasing by 5 percent until 2007, and then by 10 percent until reaching the same EU15 levels in 2013. The nominal values agreed in Copenhagen, for market support and direct payments are in Table 12. During the 2007-2013 period, the amount, in nominal values, of CAP 1 expenditures (see the table) is kept at a ceiling equal to the 2006 figure increased by 1 percent/year.

TABLE 12
EU25 - PLANNED AGRICULTURAL SUBSIDIES IN THE CAP, AS AGREED
IN THE COPENHAGEN 2002 EU COUNCIL
(In million euros, 1999 prices)

	2003	2004	2005	2006
EU15	43,770	42,760	41,930	41,660
CAP1*	39,430	38,410	37,570	37,290
CAP2*	4,330	4,350	4,360	4,370
New 10	---	1,897	3,747	4,147
CAP1	---	327	2,032	2,322
CAP2	---	1,570	1,715	1,825
EU25	43,770	44,657	45,677	45,807
CAP1	39,430	38,737	39,602	39,612
CAP2	4,330	5,920	6,075	6,195

Note: * CAP 1 - all CAP subsidies except rural development and related follow-up measures; CAP 2 - rural development and related follow-up CAP measures.

Source: European Council [2002].

Regarding output quotas and other supply management measures there has been much disagreement between the EC and the candidates. A main source of confusion is the lack of appropriate statistics. If more recent data, given the instability, not to say chaos, brought out by the transition, are not a reliable basis for calculating the quota levels, the EC refuses to accept earlier data, from the eighties

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[19]   It is perhaps useful to point out that, in 2002, the European Court of Auditors, based on IACS data, estimated that more than a quarter of all applications for area payments could have been erroneous (Brümmer and Koester [2003]).

for instance, claiming (correctly) that they reflect a situation no longer true. The result is a quite sizeable discrepancy between what has been proposed and what is being asked by the candidates. Table 13 illustrates the situation for the very important case of milk.

<p style="text-align:center">TABLE 13
THE ENLARGEMENT AND AGRICULTURE: TOTAL QUOTAS FOR MILK (IN 10,000 TONS), EC RECOMMENDATION AND ACCESSION COUNTRIES' PROPOSAL
(As by mid-2003)</p>

	Recommended by the EC	Proposed by the country
Estonia	5.60	9.0
Latvia	4.90	12.00
Lithuania	14.60	22.50
Slovakia	9.50	12.40
Hungary	19.50	28.00
Poland	88.80	112.20 to 137.40*
Czech Rp.	25.10	31.00
Slovenia	4.60	7.00
Cyprus	1.30	1.50
Malta	0.50	0.60
Total	174.20	261.30

Note: * Increasing continuously from 2003 to 2008.

Source: EC, processed and European Council [2002].

To the above questions, additional problems plague the new entrants. Proper development of land and land leasing markets, as well as of a clear system of property rights, are still needed for successful farming operation in most of them.

Restructuring will also bring longer term pressures on the sector. These will come from two sources: productivity and technological differentials and detailed implementation of the EU15 standards and food policies. As a concrete example of the first - beyond the aggregate disparity evaluated in the subsection *The Situation until Now* -, the 10AC grain yields averaged 2.3 tons/hectare in 2000, less than half the EU15 average. As for the second (see also Section D below), farmers in the new members will be obliged to meet the EU15 quality standards at the risk of being barred from the enlarged market. In the case of slaughterhouses, for instance, not only cleaning and health standards must be achieved, but also a formidable array of flooring and equipment requirements, together with the application of the EU15 grading system to all carcasses.

The main information one can get from the previous issues is that extension of the CAP to the new entrants was, is and will be a source of tension between them and Brussels. The above decisions can still suffer "corrections", depending on the negotiating clout of each side and the way the enlargement itself evolves.

A Few Impact Evaluations

Detailed simulations of specific impacts, at a disaggregate level, suffer from the previously mentioned uncertainties. Since the late nineties, serious evaluations like the ones included in Tangermann and Banse [2000] have been tried, but of late it seems that the academic community is waiting for a more clear direction - in all the looming decisions - for performing further studies. One thing is however clear: the (progressive) end of the still high tariffs for agricultural products/ sectors, prevailing in both sides. Table 14 shows selected (high) tariffs practised between Italy and the Visegrad group. As can be seen, usual culprits, like cereals, meat, dairy products and eggs, sugar, beverages (alcoholic and non-alcoholic) and tobacco rank high in the protectionist scale.

TABLE **14**
AVERAGE TARIFF RATES APPLIED TO THE ITALY-VISEGRAD TRADE IN AGRICULTURAL GOODS
(*Ad valorem* percent rates, 1999)

Sectors	On Italian exports	On Italian imports
Unmilled cereals	36	21
Meat	32	21
Dairy products and eggs	24	64
Preserved seafood	28	16
Grain mill products	18	31
Bakery products	24	16
Sugar	35	18
Cocoa, chocolate and related goods	25	11
Alcoholic beverages	34	6
Non-alcoholic beverages	34	6
Tobacco products	31	29

Source: EC's TARIC and EU Market Access databases, as elaborated in Grassini [2001].

A few authors, however, have tried to pursue detailed impact evaluations after the Copenhagen Agreement was made public. Perhaps the outstanding work is Jensen and Frandsen's [2003] CGE simulations. Table 15 gives an idea of their results for four products important to MERCOSUR. It is interesting to notice that, with the exception of "other grains", the world output decreases (with respect to a non-enlargement scenario) in all cases.

TABLE 15
OUTPUT CHANGES, FOR SELECTED AGRICULTURAL GOODS, DUE TO THE ENLARGEMENT
(Long-run results, in 1000 t)

Products	On the EU15	On the 10AC	On the RoW*
Wheat	-2,178	+3,371	-1,361
Other grains	-2,291	+5,964	-2,658
Bovine meat	-80	+76	-98
Other meat	-244	+177	-74

Note: * RoW = Rest of the World.

Source: Jensen and Frandsen [2003].

D.   The Incorporation of the Acquis and the Community Policies

According to the latest CMR the overall pace in implementing the famous - and nowadays very extensive - acquis communautaire is reasonably good, all the ten candidates having reached, at the end of 2003, "a high level of alignment with the acquis in most policy areas". In spite of this general praise, many issues still require an "enhanced effort" and a few "issues of serious concern" ("where immediate and decisive action needs to be taken for the country to be ready by the date of accession") remain. Though such issues are spread throughout the ten countries, a very important one stands out as more problematic: Poland.

Poland presents the largest set of needs for "enhanced efforts" as well as the largest one raising "serious concern". Nine points in the latter, covering three chapters of the acquis: free movement of persons, agriculture and fisheries.

In agriculture, together with its Visegrad companions, Poland needs to make considerable progress in the upgrading of agri-food establishments in order to meet public health requirements.[20] In the (sub)area of veterinary and phytosanitary control, it shares with many other candidates the lack of adequate measures relating to Transmissible Spongiform Encephalopathies - TSEs, but is the only country presenting serious problems with animal by-products, record-keeping and tracking systems for (all) animals, and the control of potato ring rot and wart disease.

Adding to the above, the majority of the big candidates (Poland, of course, included) are having problems with the implementation of the systems, software and databases required for the management and transfers related to the CAP and rural development funds, the previously mentioned IACS. This - together with the points (and tensions) outlined in the previous item - raises the possibility that the impact of the enlargement on agriculture will be smoothed out through at least two more years, and may open up a breach for MERCOSUR, if it moves fast and aggressively.

The fact that Poland is a kind of "bad boy" in the present enlargement wave is also important for our project. Together with Hungary and the Czech Republic, it accounts for 78.7 percent of the total GDP of the enlargement (and for 73.1 percent of total value added in agriculture). Actually,

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[20] See also the end of section *The Common Agricultural Policy and the New Entrants*.

for MERCOSUR-related impacts, analysis could focus on these three countries plus - mostly due to their recent positive dynamics - the two smaller economies of Slovenia and Slovakia. Though sticking to the 10-countries group we shall sometimes concentrate the analysis on the five top ones.

E.   The More Sophisticated Evaluations

As mentioned in our proposal, the variety of existing studies on the impact of the enlargement on the EU15 make it senseless - as well as totally outside the available time frame - to start from scratch a model of the reciprocal impacts of the enlargement. After the pioneering effort by IRELA [1997], the Commission was the main responsible for more sophisticated and encompassing studies, culminating in the huge Ezoneplus initiative.[21] This project, though more directed to the monetary and fiscal impacts of the enlargement, generated a considerable amount of information. It was led by the Free University of Berlin and involved the universities of Évora (Portugal), Bologna (Italy), Tartu (Estonia) and research institutes in Finland (VATT), Slovenia (IER) and Poland. It started in July 2001 and holds regular meetings, the last one having taken place in May 2003, in Brussels.

Beyond ambitious projects like Ezoneplus, special emphasis on the enlargement may be found in academic studies conducted for Italy, Portugal and Ireland. Also, there has been a vintage of Computable General Equilibrium (CGE) exercises to address different questions related to the event. Among the most important ones we mention Baldwin *et al.* [1997], Brenton and Gross [1997], Francois [1998], Brenton and di Mauro [1998], Brenton [1999], Keuschnigg and Kohler [1999], Lejour *et al.* [2001], Grassini [2001], Kaminski and Ng [2001], Baldone *et al.* [2001], Bchir *et al.* [2003] and the already mentioned Jensen and Frandsen [2003]; with Brenton and di Mauro [1999] being one example of those more focussed on the FDI question. Not all of these works use the CGE approach - some even resort to the nowadays (quite often debatable) jack-of-all-trades of our profession: gravity regressions -, but nearly all rank among the most sophisticated analyses available of the trade and FDI sides of the enlargement.

In doing any evaluation of this kind, care must be taken to consider which concessions and measures have already been implemented - and whose impacts may be already subsumed in the most recent data - and which ones are still to be enforced, creating new actual impacts. The former point is important because non-agricultural exports of key countries like Hungary, Poland and the Czech Republic, since, respectively, February 1994 (for the first two) and January 1995, face neither quantitative barriers nor customs duties when entering the EU15; the same having occurred (though not entirely yet) in 2001-2002, in Hungary and Poland, with their imports from the EU15.

Notwithstanding, the impact of some of these liberalizations will be perceived in a perspective longer than the date of the data files that have been used for their evaluation. Moreover, non-tariff and technical barriers to trade still persist, and many will disappear only after full integration - with harmonised standards and practices - takes place, being not correct to assume that free trade is already a reality between the entrants and the EU15. Indeed, in a careful study of the information contained in the TRAINS database, Wang identified several Non-Tariff Barrier (NTB)s in force in

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[21]   See the site *http://www.ezoneplus.org.*

world trade. Table 16, based on his work, gives a good idea of the extent of protection still existing,[22] due to be abolished with full membership. It is interesting to notice, beyond agriculture, the almost exclusive presence of sectors related to competitive positions by MERCOSUR, like textiles or steel products.

TABLE 16
NON-TARIFF BARRIERS APPLIED TO EU IMPORTS FROM THE CANDIDATE COUNTRIES
COVERAGE RATIOS FOR THE FIFTEEN MOST HEAVILY PROTECTED SECTORS
(At two digits of the Harmonised System)

HS code	Sectors	Number of NTBs
2	Fruits and vegetables	34
6	Cotton	53
7	Wool	27
12	Coal	52
18	Meat	19
27	Food products n.e.c.	64
29	Alcoholic beverages	20
32	Yarns and threads	81
33	Cotton fabrics	52
34	Other textile products	88
36	Wearing apparel	88
49	Synthetic resins, man-made fibres	79
57	Products of coal	52
65	Basic iron and steel	10
67	Aluminium	50

This point has been overlooked in quite a few studies, as well as by many of their commentators. As an example, while Baldwin *et al.* [1997] argued that enlargement could lead to a 30 percent increase in the total EU15 exports to the new members, Brenton and Gros [1997] stated that, as regarded trade flows, the transition was nearly over, future developments in them being mostly determined by the evolution of income, endowments and preferences. The different findings are, in great part, due to the differing assumptions each one used for the base year of their simulations, on the nature and the level of the trade barriers between the two groups of countries, as well as on the effect of abolishing the existing non-tariff barriers.

Of the above mentioned studies, two deserve a few more words. The first is Grassini's [2001] careful teamwork, associated to the Interindustry Forecasting at the University of Maryland (INFORUM) initiative, with headquarters at the University of Maryland, US. It is a dynamic,

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[22] Though the data refer to 1999, this (NTB) situation hasn't changed much, and the table gives a good idea of the present-day barriers.

multi-regional econometric, not CGE, model, inspired in Lawrence Klein's famous project LINK, where international linkages are established among several (econometric) country models. The study considers the five candidates which were certain by the late nineties (Visegrad less Slovakia, Estonia and Slovenia) and has a much more careful than average treatment of the demand, trade barriers and country linkages modules. A wealthy amount of results is clearly presented and analysed. The other is the more recent and compact (dynamic) CGE attempt by CEPII, Bchir *et al.* [2003], which draws on the model in Bchir *et al.* [2002]. Though not new in methodological terms, it contains a more careful treatment of the agricultural sector, where the Copenhagen Council of Ministers decisions are somehow incorporated into the scenarios (as Jensen and Frandsen's [2003]).

Overall, these more sophisticated evaluations show that, at an aggregate level, the impact of the enlargement on the EU15 is small. Even so, two important points arise from the joint analysis of all these efforts:

i)   at the country level, and depending on the product level of the analysis, there (of course) may be sensible changes in output and trade flows for the goods which the accession countries are heavy demanders or suppliers. This is more crucial, as expected, in the case of agriculture. So, if the ten candidates will become net pork importers, further boosting this EU15 sector, they will be net tobacco exporters, damaging certain local industries of this product in the EU15. Welfare, however, always increases, be it for the "nearby" countries, be it for "distant members", like Portugal or Spain, thanks, in the case of the latter, to indirect effects;[23]

ii)   the results can however vary substantially according to the treatment given to the protectionist barriers now being applied and their dismantling. No one (to the extent of our knowledge) dared to speculate in more depth on the possible CAP scenarios, once the accession takes place, something that may also change part of the conclusions;

iii) at their broader level, the results also confirm that the ten new members are able to be competitive exporters (to the EU15) of selected manufactured goods. This reinforces a point we've been raising in this section, namely that it is in these goods and sectors where their main menace to MERCOSUR lies. An interesting question then would be to check whether such competitiveness, even towards the EU15, is due to absolute or relative comparative advantages. In the European case we believe that both play a role, depending on the product; answering this question for MERCOSUR, demands a deeper comparison of productivity indicators.[24]

Finally, it must be pointed out that none of the above studies considered in depth either economic geography effects - movement of firms in the enlarged EU space - or more sophisticated interactions between the FDI dynamics and trade flows. It is in these areas - together with the progressive loss of structural funds - that lie the fears of the "distant members", which refuse to accept the "increasing-welfare" picture. If these effects will be negligible, the above analyses provide good clues on the impacts; if not, they indeed add a further uncertainty on the direction, intensity and consequences of the impacts.

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[23]   See below a qualification of this last statement.

[24]   We thank Juan Blyde for raising this important point; such analysis - which is, of course, in need - can be better guided by the detailed results in the next section.

E.   Policy Conclusions

The Enlargement is surely not a neutral event as regards MERCOSUR-EU15 relations. From the evidence compiled and analysed in this section, the following bullet points should be stressed:

i)   the EU15, when moving to a EU25 space, will become a richer and stronger partner "less dependent", in broad lines, from MERCOSUR;

ii) in spite of the positive outlook stated in (i), there will be (perhaps serious) tensions during a transition period - we estimate from 3 to 10 years -, specially due to regional income disparities and the extension of the CAP to the 10 new members. Moreover, it doesn't seem likely that a new wave of FDI will take place in these members, though strong and sector specific reallocation movements may occur;

iii) at this stage, the answers to the questions whether MERCOSUR will have easy access to the enlarged market and whether it will not lose existing opportunities in the present EU15 market are not evident yet. However, both seem to be in the negative side to MERCOSUR, though, globally, of a not very large amount;

iv) (point ii) opens up slots for MERCOSUR action, be it with the signing of MERCOSUR-EU Free Trade Agreement, be it directly in its foreign policy towards Europe;

v)   for these actions MERCOSUR shouldn't waste energy with the whole group of new entrants but rather concentrate its (political-economic) diplomatic efforts on Poland - the biggest, most troublesome and very likely its greatest competitor among the accession countries - and one or two more countries. Hungary seems an interesting, less menacing and possibly strategic second target, with an extra, less crucial, option on Slovakia or Slovenia, both simpler and better organised economies.

The developments in Sections V and VI try to sharpen the knowledge on the questions in (iii).

III.   THE AGRICULTURAL KNOT - EXTERNAL CONSTRAINTS[25]

A.   The European Commission Manœuvres

Answers to objective (ii) of the project, and to the agricultural issue as a whole, in its external dimension, are heavily dependent on the trends in the CAP reform - by themselves correlated with the Doha dynamics - and the final settling, in form and volume, of the agricultural subsidies and funds to be allotted to the new members. All this relies on the political context, and useful insights can only be provided if the hottest possible information is fed into the analysis.

As pointed out before, the great theme here, beyond the manifold existing non-tariff barriers, is the CAP reform. Though the recent measures announced in the last week of June, 2003, signal a positive trend in the reform, with the *decoupling* finally taking place in 2005, mixed feelings remain. In particular, sugar, grains and meat - the last two thanks to France - remained outside the overhaul. It is within this context that vehement queries for allowances under the old rules from the biggest enlargement countries, notably Poland, continue, and haven't been completely settled yet.

In spite of the fact that the (mid-term Agenda 2000 review) June 2003 measures cannot be considered bad, they are, as usual, timid and debatable. To begin with, since recent studies like OECD [2000] and USDA [2003], there is almost widespread agreement nowadays that truly decoupled policies are an illusion. Though the EC purpose signals to a more encompassing than expected *decoupling*, there is no assurance that this kind of support will not continue to distort international trade flows. Moreover, nothing really new on tariff and non-tariff barriers came up.

The June 2003 review was of course tailored to fit in the Uruguay Round commitments and prepare negotiating grounds for the Millennium Round and the enlargement. As regards the WTO itself, the EU - not differently from other big agricultural supporters, like the US and Japan - had already mounted comfortable defences, out of the initial obligations demanded by the URAA. Quotas and prohibitions, even small ones, were converted to outrageously high tariffs[26] (beef - 195 percent, butter - 161 percent and wheat - 106 percent, for instance), and creative use of these high conversions, bindings and variable tariffs ensured a nearly unchanged profile of the volume of trade. The Blue Box loophole,[27] one of the results of the Blair House compromise, allowed - through, again, creative classification of CAP payments - meeting, without much pain, the AMS reduction requirements. The Blue Box comprises those direct payments under production-limiting programmes described in Art. 6.5 of the URAA, where exactly *decoupling* fits in. They remain outside the AMS.

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[25]   The facts and ideas in this section, as well as those in Section II, point C before, have benefited from talks at the WTO, in Geneva, and at the Commission headquarters, in Brussels, beyond conversations with Professor Arlindo Cunha, a former Minister of Agriculture and Euro MP from Portugal. Nothing of what here appears, however, can be attributed to these people or their institutions or to Mr. Cunha himself; the authors of this Report being entirely responsible for the whole text.

[26]   This was perhaps to be expected, as the guidelines for calculating the tariff equivalents, set out in Annex V of the Agreement, are (purposively?) flexible and general enough to allow for such wild shots. Though each member describes the adopted criteria and related calculations in his respective Country Schedule, the number and complexity of the Schedules made contesting them, at the end of the Round, a nearly impossible and politically costly action.

[27]   It must be pointed out that the so widely used concept of the "boxes" *is not defined* in the URAA, having as a consequence that its interpretation is not uniform among all authors and negotiators. For the definition of the boxes see the Annex to this section.

Finally, the (once again) creative invention of the TRQ - tariff-rate quota, to comply with the "minimum market access" requirements,[28] successfully closed the toolbox of innovative protection measures. TRQs are a two-tiered tariff system in which a low, or supposedly reasonable tariff is applied to the quantity strictly required to meet "minimum access", together with a (usually very high) MFN rate on all imports exceeding the minimum volume.[29] Moreover, the within-quota access is usually plagued by non-tariff barriers (usually administrative) in such a way that, if in 1995 the average (over all WTO members using TRQs) fill-rate of the in-quotas was 66 percent, it dropped to 44 percent in 2000, WTO [2001, 2002].

All the above strategies, together with the ambiguities and legal flaws of the URAA (see, for instance, O'Connor [2003]) - and the unexpected turn in the US credibility, that the U. S. Farm Security and Rural Investment Act of 2002 (or, shortly, the 2002 US Farm Bill) represented - provide sufficient negotiating cushion for the EU in the present Round. Within this framework, the EC expects that the further decoupled measures will be part of the Green Box, and that it will succeed in securing the survival of the Blue Box.[30] If this comes true, it believes to be able to accommodate the "enlarged CAP" within WTO rules. Frohberg and Hartmann [2002] show evidences confirming that, under these assumptions, the present EU15 AMS constraint could accommodate a EU25 CAP in the lines described in the point C.

A further complication is the end of the so-called "Peace Clause", actually Art. 13 of the URAA. The fact that a member does not exceed its bound commitment levels, and has policies duly allotted to the Green and Blue boxes, does not preclude individual policies from infringing general subsidies disciplines contained in Arts. XVI and XXIII of GATT 1994 and in the Uruguay Round Agreement on Subsidies and Countervailing Duties (SCM). The Peace Clause provided protection to Green and Blue Box measures against these texts, notably Part III of the SCM, on *actionable subsidies*. Though it is difficult - but not impossible - that a CAP measure correctly allocated to the Green Box constitute an actionable subsidy, the situation is completely different in the case of Blue Box policies. To circumvent this possibility, some negotiators claim that Art. 21 of the URAA, which states that the other agreements in Annex 1A (Multilateral Agreements on Trade in Goods) "shall apply subject to the provisions of this Agreement" (on Agriculture) could provide protection from use of the SCM in these cases. However, based on the fact that Art. 5 of the SCM, on actionable subsidies, explicitly links the waiver on agricultural products to the Peace Clause, the dominant interpretation is that this does not apply.

Even in the case of Green Box exemptions, there is growing awareness that they may be debatable. Those under the (environmental) heading for "support and protection of organic production by creating conditions of fair competition" are one of the most questionable as, ultimately, they are an official aid to competition in a well-defined market segment.

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[28] These "minimum access requirements" are nowhere to be found in the URAA. They were part of the *modalities paper*, used during the Round, and amount to allowing imports of at least 3 percent of domestic consumption by 1995, reaching 5 percent in 2000. They can be found in the Country Schedules, but many consider them non-binding. They are one of the innumerable legal oddities of the URAA.

[29] It must be said that, of course, not only the EU resorted to TRQs. Actually, around 40 WTO members (including new ones, like China) have used this device, the majority of which, though, being developed countries.

[30] Recent developments at the WTO (specifically at the end of July 2004) support the idea that the Blue Box will last for quite a time *after* the Round is concluded.

In an even broader range, many Blue and Green Box measures are, at their roots, eventually due to a perception that farming should be subsidised because the European agriculture model is deemed to be different from those pursued elsewhere in the planet. As Grant pointed out, this is a "classic piece of defensive ideology" and is becoming more distrusted nowadays.

B.   After Cancun

As known, the Millennium Round negotiations reached a stalemate last year in Cancun, which only this March began to melt down,[31] with work possibly resuming full swing in the second semester of this year. While many expected in Cancun a concerted position against the EU from the Cairns Group, a new coalition, the G-20,[32] led by Brazil and other main agricultural producers like India, showed a united and coherent front of demands on agriculture. It is however doubtful whether, even with a strong and sustainable coalition, much will be obtained in the present Round. Moreover, drawing on a point in Winters [1987], as the CAP artificially raises the value of land, the Commission is unable to dismantle it at the desired speed, at the risk of creating social and economic disruption in the rural areas. The 2004 enlargement, given the expectations of the ten candidates, will certainly stiffen this viewpoint, adding further rigidities in the negotiation of extra reduction in the domestic support and export subsidies measures.

C.   A Suggested Policy

Within this scenario, we suggest a two-lines strategy for MERCOSUR, separating its strategy at the FTA negotiations from those in Geneva.

At the WTO front, MERCOSUR should - if possible within a broader negotiating coalition - tightly survey and constrain any moves regarding[33] the Blue Box and question, as much as possible, all measures outside the Amber Box. This, together with the usual emphasis on tariff and AMS reductions, as well as on export subsidies measures, seems to be a better negotiating strategy, rather than insisting on broader CAP changes. In particular, it eases the way for alliances with Australia, New Zealand and, most importantly, the US. A tough instance on the Blue Box would constrain the EC as regards additional or too generous extensions of the CAP to the new members.

In the March 2004 Special Session of the Committee on Agriculture, held in Geneva, the G-20 *and* the Cairns Group emphasized the need of drastic reductions in the levels of the domestic support measures - an indirect way to limit ("abolish") Blue Box values, which strengthens our proposal.

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[31]   Negotiating groups met during the whole March in Geneva.

[32]   Commissioner Pascal Lamy, soon after the Cancun meeting, sarcastically called it the G-X, given the varying number of members in the coalition. Though initially bashed or ridiculed by the Commissioner and other developed countries negotiators, the group is gaining room and being recognised - even by him - as a new important player in the Round.

[33]   In the April 2004 Report we said "*press on the* '*abolition*' *of* (the Blue Box)". As abolition seems unlikely -see footnote 31-, we changed the words, though sticking to the spirit of the suggestion (for reasons, we hope, clear in the text).

In MERCOSUR-EU agreement, a pragmatic instance would be to obtain an increase in the fill-in quota of TRQ lines of interest, together with (the possible) substantial reduction in a few high tariffs, present before or after (through the TRQ device) the Uruguay Round. The latter should target products for which the entrants will either be importers or will have a lower competitiveness. If this excludes dairy products, on the other hand, meat - of all kinds -, grains and oilseeds should be a strongly fought for group. The agreement should state that quotas, existing or newly allowed, should be auctioned to the domestic (importing) companies in the EU; what seems the best way to reduce the cumulation of rents associated to them (against the exporter).

If, in overall terms, the enlarged EU agricultural market may remain reasonably closed to MERCOSUR, the strategy here outlined may open a few opportunities. It implies that MERCOSUR negotiators should be clever enough to, contrary to what has been recently waived, dissociate, as much as possible, their interests and commitments in the FTA from those in the Doha Round. In this line, we think it more profitable, in the FTA, to trade European concessions in agriculture with MERCOSUR ones in government procurement and services markets, rather than softening positions in Geneva.

Beyond this, and as the enlargement will also expand the size and scope of the Green Box exemptions, MERCOSUR should set a task force to identify legal loopholes and inconsistencies that would allow to challenge, under the WTO Subsidies Agreement, Green Box expansions (and new Blue Box allocations) since May 2004. The task force should permanently monitor these issues and be able to trigger the needed legal proceedings if the case applies. As it would certainly become an important strategic tool in the EU25-MERCOSUR dialogue, it could, for instance, become a special project at the Montevideo Secretariat.[34]

Finally, MERCOSUR still enjoys a better reputation as regards, for instance, sanitary and phytosanitary standards - mainly *vis à vis* Poland. Given that even assets as such can be eroded if substantial subsidies are eventually granted to the new members, harder vigilance at the WTO can help to bring balance to sudden (and unfair) changes in the level playing field.

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[34] With the help of international organisms, like the Inter-American Development Bank (IDB).

ANNEX TO SECTION III

The Three "Coloured Boxes" of the URAA

As said in footnote 30, the "boxes" are nowhere to be found in the official WTO documents related to the Marrakech Agreement. Actually, they are one of the several concoctions produced by the talks at the Blair House (Washington D. C., United States), which were instrumental for leading the Uruguay Round to a conclusion. At their roots was the effort, by the EC, to save their *decoupling* initiative,[35] by creating a way to put the payments associated to it aside from WTO bounds. The inspiration for the colours came from the traffic lights, but yellow turned to blue and red to yellow (or amber), only green having kept its original meaning. So, in an informal "definition":

- *the Green Box* includes all payments and official help that would raise no objection at all, many being associated to ecological and cultural dimensions considered as key elements in an encompassing view of the agricultural activity;

- *the Blue Box* is basically the one to accommodate those payments related to the *decoupling*, which, by helping farmers to set aside production, may be considered non-distorting;

- *the Amber or Yellow Box* is finally the one which houses the CAP measures that should be either abolished or bounded somehow, as they introduce distortions in the world market. Only measures in this box are subject to quantitative limits.

Ideally, allocations both in the Green and Blue Boxes should raise no concern; at least this is the EC position. However, as argued here, this is not evident at all. Not only Blue Box payments may have rather debatable aspects, as even Green Box allocations can cause market distortions. We venture that - independently of the suggestions made in this section -, cases related to these two boxes may soon begin to appear at the WTO's Dispute Settlement Body. The end of the Peace Clause, as also mentioned in the text, will make it easier drafting the complaints.

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[35] Only *well after* implemented.

IV.   OUR EVALUATIONS: METHODOLOGY

A.   The Broad Questions

As said, items (iii) and (iv) of the project call form a more homogenous block. It is important to highlight that, specially as regards the FTA, two likely effects must be analyzed:

- ef1 - MERCOSUR wins a desirable market access in the EU15 but then must face competitive suppliers from the enlargement countries, that receive at least equal concessions;

- ef2 - MERCOSUR designs its offer to the EU15 considering the existing trade flows between the two blocs but the enlargement distorts, in some members, the expected pattern of the flows.

The result of the first effect is that market access can be minimised, and even nullified in certain cases, by enlargement competitors that steal MERCOSUR's potential market share. As for the second point, different situations may take place. Goods from the new members - *if receiving equal treatment as the EU15 ones* - may gain unexpected markets in MERCOSUR. Though this cannot *a priori* be considered a bad thing, it may however completely change previous welfare evaluations. Moreover, given that MERCOSUR's market size, for the EU15, is only around twice that of the enlargement, it might be that potential EU15 flows to MERCOSUR - even those made attractive by the Agreement - be deviated to the new members. Briefly then, many synergies expected to be created might not take place, and the "optimal level" of the designed (MERCOSUR) concessions may not apply.

The above issues become more dramatic in two well-known cases. The first relates to the agricultural sector, and has been mentioned already. The second deals with non-tariff barriers, a subject on which there is no clear view up to where liberalization will be achieved by the FTA. For the new members, on the other hand, dismantling of non-tariff barriers between them and the EU15 is an integral part of the adhesion schedule. Adding to this that transport costs will be surely reduced, while harmonization of products quality and standards will be enforced; when the *acquis communautaire* is fully incorporated by the new entrants, an enormous competitive edge will be given to their goods, even when competing in otherwise equal terms with MERCOSUR ones.

Of course, from a logic viewpoint, the other side of the previous points is also valid: MERCOSUR may gain an additional market, not initially accounted for. This possibility will also be examined, though, in the case of non-agricultural goods, preliminary evidences suggest that the combined presence of the EU15 and Russia[36] (and the new member's former partners in the Warsaw Pact), plus the US competitiveness, won't leave much room for MERCOSUR goods. As for agriculture, the possibilities stay intimately related to the final design of the CAP, and have been sketched in Section II.

We shall then pursue two methodological lines.

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[36]   As regards the position of the EU15 members, Section II has already provided strong suggestions that this will be the case.

B.   The Partial Equilibrium Analyses[37]

The first more substantive approach continues efforts done by Castilho [2002, 2003a and 2003b] and Flôres [2003a], and works at the six-digit level to identify goods that will be important - because they will either *lose* or *gain* market in one of the blocs - in the EU15-10 Entrants-MERCOSUR[38] triangular flows. Out of the six possible flows between the pairs from this triad, we shall concentrate on the two ones *to the* EU15, and the two *to* MERCOSUR.

The analysis is (broadly) based on revealed comparative advantage indexes, in the way refined by CEPII, Paris, where a "geographic orientation" dimension is introduced. The core statistic is the *trade complementarity index (tci)*, defined by the product of the classical comparative advantage index (exports) with a comparative disadvantage index (imports). The *tci* will be computed at the six-digit level and, for providing answers on ef1, its formula is:

$$TC_{ij,\,a} = CAX_{ij,\,a}.\;CDM_{ij,\,a}$$

where (considering the analysis *in* the EU15 market)

i will be either MERCOSUR (S) or the 10AC, the new entrants (A),

j is EU15 (EU),

a is the particular product and

$$CAX_{ij,\,a} = (X_{i,a}\,/\,X_i)\,/\,(M_{W\text{-}i,\,a}\,/\,M_{W\text{-}i})$$

$$CDM_{ij,\,a} = (M_{j,a}\,/\,M_j)\,/\,(M_{W\text{-}j,\,a}\,/\,M_{W\text{-}j}),$$

with

$X_{i,a}$ ($M_{j,a}$) - bloc *i* (*j*) exports (imports) of product *a*;

X_i (M_j) - bloc *i* (*j*) total exports (imports) of product *a*;

$M_{W\text{-}i,\,a}$ - world imports of product a but those from bloc *i*, and.

$M_{W\text{-}i}$ - total world imports minus those from bloc *i*.

The products for which $TC_{ij,\,a}$, i=S,A, will be greater than 1 denote, in principle, a competitive edge for bloc *i* on product a, as regards bloc *j*. However, this edge may not having been fully exploited. To see this, a further comparison, with another index is needed.

The additional insight is given by one version of a geographic orientation index (GOI). It can be, for instance, the $CAX_{ij,\,a}$ with its version $CAX_{ij,a}^{J}$, where all flows, be imports or exports, are restricted to bloc *j* (i.e., is bloc *i*'s revealed world comparative advantage bigger than when it is restricted to bloc *j*?).

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[37]   Actually, as described in the section, this part of the methodology basically uses trade indexes; calling it "partial equilibrium" is a somewhat hopeful denomination for these more modest tools.

[38]   We shall frequently use, in the remaining sections of this report, 10AC to mean the ten new May 2004 members.

As, in the case of ef1, the 10 new entrants can be considered as the "incumbent", we identify, along the above lines, the products for which

$$TC_{Sj,\,a} > 1 \text{ and } CAX_{Sj,\,a} > CAX_{Sj,a}{}^{EU},[39]$$

as the prospective goods for improved market access from the FTA. However, the position of the 10 Entrants, as regards the same goods, must be evaluated. The candidate countries constitute a *potential threat* if $TC_{Aj,a} > 1$, for the same goods, irrespective of the values of $CAX_{Aj,\,a}$ and $CAX_{Aj,a}{}^{EU}$, though the latter will be also computed.

For the products identified as above, the trade barriers faced by MERCOSUR and 10AC are compared, taking into account what can be expected in terms of lowering MERCOSUR ones through the FTA, and the 10AC still existing through the May 2004 enlargement.[40] The two important cases are:

i) the discrepancy between the (final) trade barriers is remarkable - for these goods market access will be more restrict than expected or even eliminated;

ii) the discrepancy between the (final) trade barriers is not very large, but $CAX_{Aj,\,a} \leq CAX_{Aj,a}{}^{EU}$ - for these goods, subject to a more detailed examination of volumes and other suppliers, it is likely that MERCOSUR won't reap a significant extra market access.

Identification, under ef2, of the possibility of unexpected flows from the candidates, due to the FTA, is made in the same way, reverting the role of the indices. Now $i = A$, EU while $j = S$, MERCOSUR.

In order to give a synthetic picture of the results, the analyses may be complemented by the use of a particular (statistical) multivariate technique: correspondence analysis. From this, a classification and better global characterization of the different impacts and their likely consequences/changes on the EU-MERCOSUR Agreement can ensue.

C.   The Computable General Equilibrium Analysis (CGE) Experiment

The second analytical tool to be used is a static CGE, multi-regions model to analyze the likely flows and gains, in different scenarios. This can be seen as a complement to the previous exploratory, partial equilibrium approach. The model is an extension of the one in Flôres [2003b], with the enlargement countries added to the EU15 region. It has 15 sectors, with four related to agricultural activities.

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[39] For other versions of a GOI, the second inequality can simply be a value lower than 1 for the index (see, for instance, Section V, point A.

[40] For the great majority of these, one will be able to assume *zero barriers,* free trade.

Reminding the six possible flows among the three markets at stake, this exercise not only complements and extends the findings for the four ones studied under partial equilibrium, as sheds light on the prospects opened by the "bigger EU market" to MERCOSUR.

The construction of the scenarios uses information from Sections II and III, beyond that from the partial equilibrium study. Further information on the model is provided in Section VI below.

D.   Note on the Databases Used

For the trade flows we shall work with the databases *pctas*, from UNCTAD, and *comext*, from EUROSTAT, both referred to the year 2000. Actually, in the case of *pctas*, the period 1999-2001 will be covered. For tariff data the basic source will be the 2000 TRAINS database, from UNCTAD, while information on non-tariff barriers will come from an update of a 1996-related database made and previously used by Renato Flôres and Marta Castilho. The partial equilibrium analyses will be conducted at a six-digit level of the Harmonised System. For the CGE exercises the trade flows will come from the same sources, but the country/regions social accounting matrices come from improvements in the 1997 GTAP database done by Flôres [2003b]. Information on tariff and non-tariff barriers will result from combining the previously mentioned sources (including the 1997 GTAP data with the refinements in Flôres [2003b]) with further adaptations to be made.

V.   RESULTS: PARTIAL EQUILIBRIUM ANALYSES[41]

A.   Effect 1: Competition between MERCOSUR and the New Entrants within the EU15 Market

In order to evaluate the effects of the enlargement on MERCOSUR exports to the EU15, under or without the FTA, one must look at the effects of the entry on those goods with important export potential (from MERCOSUR point of view). We first identified these goods and then examined the position of the 10AC on European markets, in terms of specialization complementarities and also of market access advantages. The identification of the products is preceded, however, by a global analysis of MERCOSUR and 10AC trade complementarity.

EU Imports from MERCOSUR: Geographical Orientation and Complementarity

The EU15 is a key trade partner of MERCOSUR. The GOI in Table A (Annex) clearly reveals this fact. For all exports, the EU has almost double the share it displays in total world imports. Obviously, this differs from one sector to another and the EU market, for MERCOSUR, is more important for agriculture & food products than for manufactures.

The sectors for which the EU15 is an important export destination are notably Coffee, rice and other crops; Vegetables and Fruits; Oil seeds and vegetable fats and oils; Vegetables products n.e.s. and Bovine Meat. Together they represent 40 percent of MERCOSUR exports to the EU15. Among other manufactured goods, the GOI shows higher values - though not comparable to the agriculture & food products one - for textiles, apparel & footwear and wood, pulp & paper. The GOI is less favourable for sugar and dairy products and, as we can see from the other columns, the small share of MERCOSUR in the European sugar market is not explained by specialization, but rather by the agricultural policy.[42] MERCOSUR's specialization shows strong complementarity in relation to the EU15 as it concentrates its main comparative advantages on agriculture & food, exactly where the EU15 shows comparative disadvantages (or weak advantages). Table A (Annex) synthesizes the results calculated at an aggregated level - which doesn't necessarily reflect the particularities of isolated products.[43] It shows only the global features of each sector. A disaggregate analysis, at the 6-digit HS level (more than 5,000 products), is made next, in order to identify the export potential of MERCOSUR.

The 13 sectors out of 22 that show complementarity represent 85 percent of bilateral imports. Stronger complementarities are found in Coffee, rice and other crops; Oil seeds and vegetable fats and oils; and Sugar, reflecting above all the strong comparative advantages of MERCOSUR. The

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[41]   Due to the size and format of the Tables/tables in this section, most of them were assembled in the Annex to Section V: Selected Tables. Whenever reference is made in the text to an table with an asterisk after its number (Table K (Annex)) the reader should look for it in the Annex.

[42]   Sugar is one of the most protected sectors among developed countries and so it is in the EU. Aside from the high border protection and subsidies for European producers, the EU maintains special regimes and preferences for this sector within its ex-colonies.

[43]   As our sectors can have more than 900 products (chemicals, rubber and plastics), if there are goods with a very strong comparative advantage the aggregated indicator will not necessarily reveal this fact.

same can also be observed in Wheat, corn and other grains; Vegetables and Fruits; Vegetables n.e.s.; Bovine Meat and Other food products. Among other manufactured goods, strong complementarity is seen in mining and, at a lesser degree, in transport equipment, wood, pulp and paper; metal and its products and textiles, apparel & footwear. This sector distribution shows that complementarities are concentrated in intensive natural resource products, reflecting above all the structure of MERCOSUR comparative advantages and specialization.

Trade Complementarity between the EU and the 10AC

If we consider the market share of the 10AC within the EU (4 percent in 2001), we might suppose that they would not be very strong competitors to MERCOSUR exports (even though MERCOSUR market share is only 0.9 percent). Not only this is not true for particular sectors or products, as shown below, but there are also other aspects that indicate that the competition from these countries must be taken seriously into account. A 58 percent increase in their exports to the EU15 countries took place between 1997 and 2001 (see also Section II, point B), while MERCOSUR exports increased only 9 percent over the same period. As a result, their EU market share has risen from 3 to 4 percent. Moreover, a large part of the trade between the EU15 and the 10AC concerns not only goods, but also FDI flows, as a great part of the recently created bilateral trade is derived from contracts between firms.

Complementarity appears only in a few sectors - two in agriculture and six in manufacturing; disregarding the borderline value for transport equipment -, though not very strong, except for wood, pulp and paper. In all, the 10AC present comparative advantages. For five out of these eight sectors - vegetables, mining, textiles, apparel & footwear, wood, pulp & paper, and metal products -, both the 10AC and MERCOSUR present comparative advantage and complementarity with the EU15, being true competitors.

MERCOSUR Export Potential to the EU

      - Main Potential MERCOSUR Exports -

Combination of the Geographical Orientation Index and the Trade Complementarity Index (TCI) can generate 4 different situations. If the GOI is over one and complementarity exists, the typical case for bilateral trade applies. Without the latter, trade can exist but it will not be explained by specialization in both sides. If both indexes are below one, there is no reason for trade. But if the GOI is under one and the TCI is greater than one, something is missing: complementarity would suggest there is room for trade that is not taking place. Probably other factors - preferences to other countries or trade protection measures - would explain the gap. The latter case is the one we define as having export potential.

We considered, at the HS 6-digit level, only the products for which there is a minimum export offer from MERCOSUR and the 10AC, and minimum import demand from the EU. We retained 4,922 (from a total of 5,021) products (at the 6 digit HS level) that accounted for MERCOSUR exports plus 10AC exports plus EU imports over US$ 100,000. Out of these 4,922 products, 265 show export potential, which means, as we can see from Figure 1, that they represent around 5

percent of bilateral trade - either in terms of value or in terms of number of tariff lines. Obviously, the greatest part of the observed trade is characterized both by positive geographical orientation and complementarity indexes. In contrast, the greatest part of the tariff lines are concentrated in the case $I_{ijs} < 1$ and $C_{ijs} < 1$, but, as expected, it represents only 2.3 percent of the value of bilateral imports.

FIGURE 1
DISTRIBUTION OF THE EU-MERCOSUR IMPORTS ACCORDING TO GEOGRAPHICAL ORIENTATION AND COMPLEMENTARITY
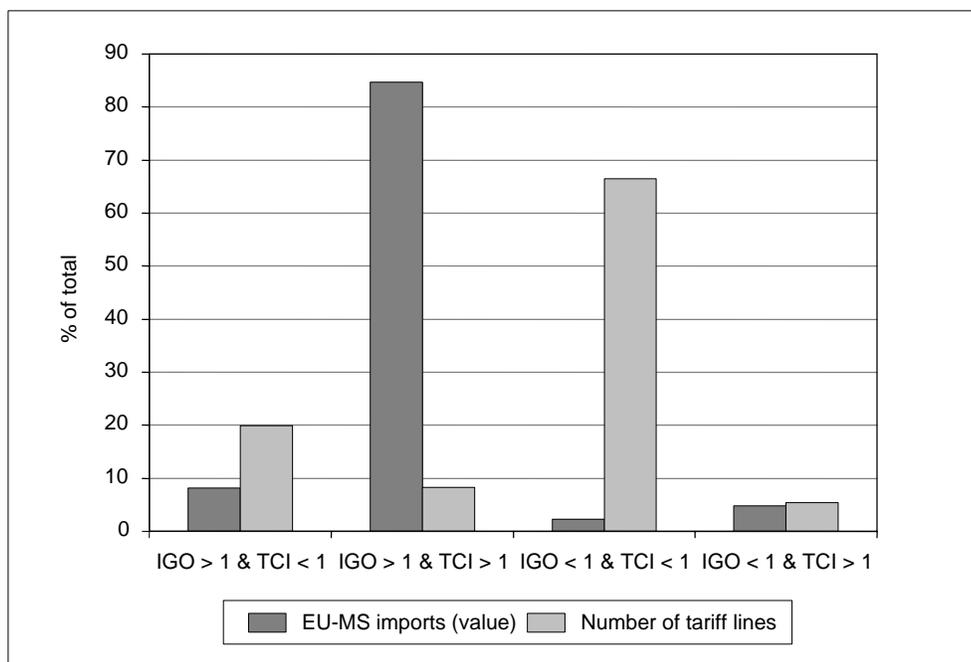
Table C (Annex) shows the main characteristics of the bilateral trade of selected products. They belong to 19 out of the 22 sectors; the only sectors where there is no worthwhile potential are vegetable products, bovine meat and dairy products. The sectors where there are more products with export potential are chemicals, machinery & equipment, mining and textiles, apparel & footwear. These sectors, however, hold a large number of tariff lines and so, in relative terms,[44] there are other - mainly agricultural - sectors that show a large number of selected products - sugar, wheat, livestock and mining.

In general, the trade flows of selected products are very low. The only exceptions are livestock and transport equipment, where current imports represent 85 percent and 68 percent, respectively, of bilateral imports in the sector. This means that even if present trade levels are already high, there is room for exports growth.

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[44]   Number of selected products related to the number of tariff lines of each sector.

- The 10AC and the EU Trade Complementarity for Selected Products -

Among the 265 goods showing export potential to the EU, we can distinguish a first group composed of products for which the 10AC present stronger comparative advantages than MERCOSUR. For this group, MERCOSUR's export potential is probably not going to become reality, due to the new members. Enlargement, in this case, will just reinforce their present comparative advantages. For the other group in which MERCOSUR holds a greater advantage than the 10AC, the export potential will be at risk only if the enlargement gives to new members much higher preferences than those MERCOSUR receives in the FTA. It is described in Table 17 and in the lines below:

i) a first subgroup comprises 58 tariff lines and represents 7.3 percent of MERCOSUR exports with good potential. For obvious reasons, they represent the major part of 10AC exports to the EU15. In this case, enlargement can even worsen MERCOSUR position within the EU market as the new members will benefit from a positive preference margin (the Most Favored Nation -MFN- simple average for this set of products is 4.8 percent).

ii) a second one comprises 122 products and represents the major part of MERCOSUR exports with good potential to the EU. Neither the enlargement nor the FTA will significantly modify MERCOSUR's market access conditions, as current protection is already low;[45]

iii) the third subgroup is where changes in market access conditions for the 10AC can reverse the positive position of MERCOSUR exports. Though MERCOSUR enjoys comparative advantages, as tariffs are relatively high, the accession may give the new members an important preference margin whose impact will depend on the concessions made by the EU in the FTA. A better focus is needed here.

TABLE 17
MERCOSUR EXPORT POTENTIAL TO THE EU: CHARACTERISTICS OF SELECTED GOODS

Description	Number of tariff lines	Composition of EU Imports			Market share in EU	
		TOTAL	MERCOSUR	10AC	MERCOSUR	10AC
RCA MERCOSUR < RCA AC10	58	23.0	7.3	60.2	0.4	15.2
RCA MERCOSUR > RCA AC10 & tariff MFN < 5.0	122	39.2	57.8	19.5	1.8	2.9
RCA MERCOSUR > RCA AC10 & tariff MFN > 5.0	85	37.7	34.8	20.3	1.1	3.1
Total	265	100.0	100.0	100.0	1.2	5.8

Table 18 shows the sectoral distribution of the 85 products of the third subgroup. Twenty-four tariff lines, related to sectors 13, 14, 17, 18, 20 and 21, seem "in danger": the 10AC are already well-positioned and the Generalized System of Preference (GSP) simple average for MERCOSUR

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[45] We consider that tariffs below 5 percent do not bring on significant price changes.

is at least 5 percent. Nineteen are in textiles, apparel & footwear (13), facing a very important competition from the 10AC. This sector represents the greatest part of current MERCOSUR selected products, but the presence of the new members is already superior to that of MERCOSUR. The GSP tariff average is 7.1 percent, but reaches 11 percent in some cases. Other sectors with higher preference margins are transport equipment and electronics. For some the latter, the market share of the new members is already quite high.

TABLE 18
PROFILE OF 10AC "THREATS" TO MERCOSUR: COMPOSITION,
MARKET SHARE AND EU TARIFF (PERCENT)

Sectors	Description	Number of tariff lines	Composition of EU Imports			Market share in EU		GSP - simple average
			Total	MERCOSUR	10AC	MERCOSUR	10AC	
4	Oil seeds and vegetable fats and oils	4	1.9	0.8	2.5	0.5	0.4	31.6
5	Sugar	3	4.8	1.5	6.6	0.4	0.3	105.8
10	Beverages and Tobaccos	2	1.2	0.8	1.4	0.7	0.2	30.7
11	Other Food Products	13	10.7	10.4	11.7	1.1	1.7	26.0
12	Mining	4	9.2	4.7	10.2	0.6	2.2	3.1
13	Textiles, Apparel and Footwear	19	34.1	68.6	30.2	2.3	3.8	7.1
14	Wood, pulp and paper	1	1.4	0.1	1.8	0.1	3.2	4.9
15	Chemical, rubber, plastic products	31	16.4	12.0	18.8	0.8	0.5	3.4
16	Metal and Metal Products	3	0.7	0.3	0.6	0.5	1.3	3.5
17	Motor vehicles and parts	1	4.3	0.5	4.8	0.1	7.4	9.1
18	Transport equipment nec	1	3.1	0.0	1.9	0.0	0.1	5.6
20	Electronic equipment	2	8.8	0.2	6.9	0.0	6.8	8.6
21	Energy goods	1	3.4	0.0	2.6	0.0	11.4	na
	Subtotal	*85*	*100.0*	*100.0*	*100.0*	*1.1*	*3.1*	*..*

Source: PCTAS.

For two other clusters the situation seems unclear. The first comprises the 22 lines from the agricultural and food sectors, mostly processed foodstuff. The protection imposed on MERCOSUR[46] is very high, reaching 106 percent in the case of sugar and giving new members a large preference margin. Until now, the high competitiveness of Southern Cone goods in this area has secured a higher market share; the final form of the FTA will be crucial for the maintenance of this position. In the second cluster, average tariffs are not very high. Most are chemical products, which represent 12 percent of MERCOSUR bilateral exports of selected products. Though barriers are lower than for agricultural sectors, they can reach high levels for specific products (see details below). The 10AC seem also to be important competitors in the mining and metal industries. Their current market share is superior to that of MERCOSUR, but there is a small preference margin for the 10AC, as the GSP can be at a 6 percent maximum.

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[46] Although negotiations are being conducted with respect to MFN tariffs, we present herein the tariff currently faced by MERCOSUR exports-GSP rates.

The EU Border Protection: Tariffs and NTB Applied to 10AC and MERCOSUR

- Is the 10AC Trade already Free? -

The set of all trade agreements established by the EU15 with its numerous partners has built up a kind of hierarchy of preferences in the access to the European market. At the top of this hierarchy stand EU15 neighbours and their ex-colonies. From May 2004 onwards, many of these "neighbours" will leave this condition and become actual members of the EU with, among other benefits, liberalized trade. Tariffs will be zero for almost all products but some quantitative restrictions and NTBs will remain.

Table D (Annex) displays information on the EU tariff protection in 2000. The first part shows the preferential tariff schedules applied to the 10AC. Each country had a different schedule and the one presented herein is a simple average of the ten schedules. The preferences did not initially cover all tariff lines and when there was no preferential rate, MFN was imposed - what explains the fact that maximum rates are frequently the same for all trade regimes. As can be seen, four years before today's accession, imports from the 10AC were far from being liberalised, above all in agricultural sectors. More than that, tariffs applied in these sectors were quite similar to MFN rates - and to the GSP as well. Though not reflecting the current protection status imposed on 10AC exports, these figures illustrate that: (i) even "very preferred" partners face high trade barriers in agricultural and food sectors, and (ii) trade between 10AC and the EU15 has not been fully liberalized yet.

Indeed, from the more recent data available on EU protection [TRAINS, 2002], it is clear that, two years before accession, trade wasn't free yet. Positive tariffs remained on almost every agricultural sector and for selected chemical and metal products as well. Though this is not the current protection situation, it shows that, until recently, quite many barriers to trade were in force. Moreover, as TRAINS data do not include the AVEs for specific duties, its protection figures are down-biased (only the vectors for the preferential, *ad valorem*, rates for 2000 and 2002 were analysed).

Table E (Annex) shows that about 14 percent of 10AC exports to the EU15 in 1999 faced at least one kind of NTB. The most frequent kind is Authorization, Surveillance or Technical measures - affecting almost all sectors and touching 15.3 percent of all tariff lines. Antidumping and safeguard measures are also frequent, reproducing a common feature of the European enlargements: during the liberalization process, the EU always imposed a large number of AD and SG measures on imports coming from their new partners.

EU Protection on Imports from MERCOSUR

MERCOSUR countries benefit from the GSP, even if there are some exceptions. The complications of the European GSP are well known and its rules penalise large developing countries, such as Brazil, India, China and Argentina. One of the restrictive rules eliminates GSP reductions if the share of the country in the specific product is greater than 25 percent. As a consequence, Brazil

and Argentina do not benefit from SGP concessions for several products.[47] At any rate, as information on exceptions was not available, the GSP schedule represents quite well the tariff structure faced by MERCOSUR in the EU market. The simple average in Table D (Annex) is 4.5 percent, which is an intermediate level between the one applied to the 10AC and the MFN. But these indicators are very aggregate and hide tariff peaks or high tariffs: in chemicals, for example, tariffs can rise to a 66 percent height.

The major differences from the 10AC tariff schedule are in manufacturing sectors: tariffs imposed on MERCOSUR exports were higher than those imposed on 10AC exports in 2000, except for energy goods. As tariffs applied to the 10AC are going to be drastically reduced, the differences will become still more evident. The largest differences are in textiles, apparel & footwear (7 percent) and motor vehicles (3.7 percent).

With the accession of the 10AC, common external tariffs will be adopted. In agriculture, they will be the high tariffs practiced by the EU15 (which means that in some cases there will be a rise in the level of protection). This, together with the internal margin of preferences received by the 10AC will indirectly enhance the particularly high protection imposed by the EU on MERCOSUR exports. However, these countries do not have very good competitive skills in these sectors and, as seen, the main 10AC "threats" to MERCOSUR exports are concentrated in the manufacturing sectors.

The level of protection imposed on agriculture can reach 424 percent in the case of certain dairy products (HS 040410), or 255 percent for vegetable residues (HS 230890). It is not uncommon for tariff rates to be higher than 100 percent - in the case of sugar, other food products, bovine meat, oil seeds and vegetables and fruits. This without taking into account the incidence of tariff quotas, which affect a great number of products (1,462 out of 13,574), as they are not considered to be a quantitative restriction either by the WTO or the UNCTAD. Agricultural goods, chemicals, wood, pulp and paper, textiles, apparel and footwear, metals and their products, machinery & equipment and transport equipment are all affected by tariff quotas.

Aside from tariff protection, one must consider also the NTBs imposed on MERCOSUR exports, described in Table F (Annex). In 1999, 12.5 percent of the tariff lines were affected by at least one such measure. This corresponded to 16 percent of bilateral imports. To a large degree, they were authorization, surveillance and technical measures, but some quantitative restrictions were imposed on textiles, apparel and footwear[48] as well as on wood, pulp and paper and chemical goods. Antidumping and Safeguard measures are highly concentrated on one fruit (081120), one chemical product (292242) and finally two kinds of ferro-alloys (720221 and 720229).

However, a great part of the NTB measures faced by MERCOSUR exports are not specific - they are so called "generic" measures and affect all EU15 partners. This is the case notably of all authorization, surveillance and technical measures. There are 199 antidumping, safeguard and quantitative restrictions specific to Brazilian and Argentine exports (from a total of 626), which represent around 4 percent of MERCOSUR exports to the EU. They affect the following

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[47] Such as: dairy products, skin and leather goods, products from the pulp and paper sector, footwear, iron and steel goods, transport equipment (railway, aircraft and ships).

[48] *All* MERCOSUR footwear exports to the EU have been affected by technical norms or surveillance measures.

sectors: textiles, apparel and footwear, wood, pulp and paper, chemicals, rubber and plastics and metal products.

The Selected Products: Deeper Analysis of the "Threat" of the 10AC to Potential MERCOSUR Exports

Table G (Annex) is a detailed presentation of the 85 goods that will be affected by the entry of the 10AC. It is one of the core results of this section.

For the products in Table G (Annex), if the FTA does not allow free entry of MERCOSUR exports, the 10AC will probably compensate their weaker competitiveness by the preference margin.[49]

The 10AC do not compete in crude agriculture products: all selected products are processed, mainly sugar products and vegetable oils and fats. The share of MERCOSUR exports in the EU15 market is inferior to the market share of the 10AC, except for 3 products and, likewise, the weight of the European market in total MERCOSUR exports is also quite low. These are the products for which the export potential is more jeopardized. First, protection is very high for these products - tariffs can reach 136 percent for a kind of refined sugar and seven products face non-tariff barriers. Thus, if new entrants have free access to the European market, the preference margin over MERCOSUR products will be very significant. Moreover, as seen below, the EU offer is not very generous for agriculture and food products, liberalization schedules having not been proposed for the majority of them.

Numerous chemical products also menace MERCOSUR export potential. They are mostly organic and inorganic chemicals - HS chapters 28 and 29. The applied tariff is zero for a significant share of these goods, but there are some products facing positive tariffs (mainly from chapter 29) - there is even one product for which the tariff is 58 percent. The EU offers partial liberalization in 7 years for most of these products. With regard to the other chemical, plastic & rubber products - from chapters 30 to 40 - there is only one such product for which the applied tariff is significant (6.2 percent). Considering then all chemicals, plastic & rubber products, the 10AC menace to them is less intense than to agricultural products.

Leather and skins are, on the one hand, subject to both tariff and non-tariff barriers and, on the other hand, MERCOSUR presents strong comparative advantages. So, this sector is likely to have good export potential and as the 10AC will benefit by better market access conditions, they will possibly try to impair the realization of this export potential. Actually, despite the much stronger comparative advantages of MERCOSUR, their market share is superior for all three products.

Competition of the 10AC is important also in textile & apparel exports. The accession countries have became important suppliers of the EU15 since the fall of the Berlin Wall, replacing even other traditional European partners in this sector, such as the North African economies. The increase in trade in this sector is strongly based on inter-firm relationships (sub-contracting). The enlargement is going to improve the advantages of the 10AC in the EU15 market as current

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[49]   We have retained the products for which the MFN tariff was over 5 percent. The choice of the MFN is due to the fact that negotiations use this tariff and also that it would represent the largest feasible set. But in order to analyze current conditions, we use the GSP as MERCOSUR exports enter the EU under this regime, despite exceptions.

protection is significant and liberalization is envisaged for a 7-year period. The 10AC menace to MERCOSUR footwear exports is quite similar to that of textiles & apparel. Protection is positive, reinforced by numerous NTBs and the 10AC market share is already considerable.

Other products come from different industries: ceramics, aluminium, cutlery, and electrical equipment and vehicle parts. Tariffs are positive in all cases, being higher for electrical equipment and vehicle parts. In these sectors, enlargement will probably deepen the already existing inter-firm relationships and so it will impair the increase of MERCOSUR share in the EU market. Liberalization, for the great majority of these products, is envisaged in 7 years.

Which Liberalization for MERCOSUR under the FTA? An Analysis of the EU offer[50]

The last EU official offer[51] raised the number of products covered from 9,165 to 10,400. The two categories that presented the bigger increases were category "A", immediate liberalization, and category "E", which doesn't establish a timetable for liberalization. The increase was of 17 percent for category A (from 2,998 tariff lines to 3,514) and of almost four times for category E (from 195 to 963).

At present, category A concerns 60 percent of the EU imports from MERCOSUR (see Table 19). The share of current bilateral trade decreases for categories "B" and "C", which is not surprising as proposed liberalization is slower for products facing higher tariffs. Nevertheless, category "E" represents a slightly larger share of bilateral trade - 6.4 percent - and products exported by MERCOSUR to the EU but not contemplated by the offer represents 8.3 percent of total bilateral trade.

TABLE **19**
EU'S NEGOTIATION OFFER TO MERCOSUR

Category	Liberalization on year:	GSP (percent)[1]	MFN (percent)[1]	Composition of EU imports from MERCOSUR (2001)	Number of tariff lines[2]	Number of tariff lines with specific duties[2]
A	0	0.09	0.84	60.3	3,522	15
B	5	1.62	4.21	11.1	2,576	47
C	7	5.23	8.08	9.3	2,997	30
D	10	15.26	17.48	4.6	352	32
E	not defined	49.95	48.62	6.4	980	951
Not covered by the EU offer		5.59	7.12	8.3	..	
Total				100.0	10,427	1,075

Notes: [1] GSP and MFN take into account specific duties;

[2] tariff lines defined at HS 8 digit concerned by the EU 2003 offer. Source: TRAINS for tariffs and trade

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[50] As of end of March 2004.

[51] For an objective analysis of the present status of the negotiation process, see Doctor and Rios [2004].

Products (tariff lines) are defined in the proposal at an 8-digit level. We didn't dispose of the tariff rates for all the products because of classification differences. But from the 3,522 products for which immediate liberalization is proposed, we got information for 3,205 of them, and from these, 3,073 face zero tariffs under the GSP and 1,957 under the MFN regime. As negotiations use the MFN as base rates, we can see that the immediate benefits will affect less products than has been announced: MERCOSUR already benefits from zero tariff in at least 95 percent of the cases. Tariffs imposed on imports classified under category "A" show a simple average of 0.8 percent under MFN and a much lower tariff under GSP. This is also valid for the next two categories (see Table 19): GSP systematically shows a significant difference to MFN and the real margin of liberalization must be calculated based on the current tariff GSP and not on a "theoretical" new one MFN.

Finally, it is important to stress that negotiations do not consider reducing specific duties, as can be seen from the number of tariff lines in Table 19 with specific duties classified in category "E". The greater part of these duties applies to agriculture and food products.

B.   Effect 2: Competition from the 10AC within MERCOSUR Market

MERCOSUR offer was made considering the specialization of the present 15 members and has not taken into account the threat to its domestic production posed by the incoming members. Even if the current structure of the 10AC exports to MERCOSUR is close to that of the EU15, combination of the accession with the FTA will perhaps give them new opportunities. To evaluate this point, we have compared the specialization and the complementarity between MERCOSUR and two EUs: EU15 and EU25. EU25 is simulated as the sum of the EU15 and 10AC trade flows. Obviously, this is a simplified hypothesis that doesn't take into account the dynamic effects and all the changes that can be produced by the future EU25 structure.

Comparison between Specialization of EU15 and EU25: Are there Important Changes?

As seen before, trade between the 10AC and MERCOSUR is not very significant and specialization makes their exports to it very close to the EU15 pattern. This is reflected in Tables H and I (Annex). Indeed, a comparison between the composition of MERCOSUR imports from the EU15 and the EU25 doesn't present important changes. The most important one is in the energy sector, whose imports increase by 60 percent and whose market share attains 5 percent. But even so, it still represents 2 percent of the total MERCOSUR-EU25 imports.

The profile of imports from EU15 and EU25 in terms of comparative advantages and trade complementarity reveals few changes after the accession. As Table I (Annex) shows, complementarity is observed in the same 5 sectors: Beverages and Tobacco; Mining; Chemicals, rubber & plastics; Transport equipment and Machinery & Equipment. Among these sectors, the complementarity is only reinforced in the mining sector. It reflects the fact, revealed by the RCA indicators, that the 10AC reinforce the comparative advantages of the EU15 only in a few sectors such as vegetables, textiles and wood, pulp & paper, but not enough to transform the comparative disadvantages into advantages. The only sector presenting a comparative advantage, and where the 10AC contribute to its improvement, is mining.

The Threat of the 10AC in MERCOSUR Markets

The preceding analysis suggests that accession is not going to affect much the outcome of agreements with respect to MERCOSUR market. But once again this introductory analysis was made for whole sectors, which can hide particularities for certain products. Here, we have selected the products that are likely to be more affected by the 10AC competition in a liberalised environment. They have been chosen according to the following steps:

i)   selection of the products for which the EU25 complementarity shows a significant change in relation to the EU15 complementarity (more than 25 percent of initial value);

ii)   contrast of the previous results with the protection imposed by MERCOSUR, considering that, the higher the protection, the more sensitive it becomes to foreign competition;

iii) finally, the analysis is completed by adding information about MERCOSUR offer to the EU.

We have calculated the trade complementarity index at the HS 6-digit level, disregarding products for which total MERCOSUR imports are inferior to US$ 50,000. We retained the products for which the TCI showed an increase greater than 25 percent of its initial value (EU15) and for which complementarity between EU25 and MERCOSUR was observed. This accounted for 122 of the original 4,401 products.[52]

Few agricultural products represent a threat to MERCOSUR; apart from one kind of pork meat and two kinds of oil seeds, there are 12 food products (preparations of several sorts - meat, cereals, vegetables, from the milling industry and others).

The accession seems to affect more intensively the manufacturing sectors. There are 16 products in the mining sector where the 10AC competition can represent a menace for MERCOSUR producers. As we can see from the last two columns of Table 20, the new members increase the EU share in MERCOSUR market from 15 to 21 percent. From the other manufactured goods, the main threats affect chemicals, rubber and plastic products. The 32 products identified represent around 32 percent of EU imports and the market share would rise by 7 points, attaining 31 percent. Sixteen metal products - more specifically iron and steel products - are also identified as threats. The new EU members have a performing sector, as a consequence of their specialization in heavy industry, as seen before, and this raises the EU market share from 42 to 64 percent. A relative large number of selected products are from the machinery and equipment sector. The 10AC exports would push the EU market share in MERCOSUR from 39 to 43 percent, though their contribution in value is of only 1 percent.

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[52] These are the products defined at the 6-digit level for which MERCOSUR total imports respect the threshold of US$ 50,000.

TABLE 20
PROFILE OF SELECTED GOODS: THREATS OF "EU25" TO MERCOSUR

Sectors	Description	N° of tariff lines	US$ thousands			Composition (percent)		Market share in MERCOSUR	
			MERCOSUR imports from EU15	MERCOSUR imports from 10AC	MERCOSUR imports from EU25	MERCOSUR imports from EU15	MERCOSUR imports from EU25	MERCOSUR imports from EU15	MERCOSUR imports from EU25
2	Coffee, rice and other crops	2	1,765	323	2,088	0.5	0.4	17.1	20.2
8	Bovine Meat	1	2,009	0	2,009	0.5	0.4	27.0	27.0
11	Other Food Products	12	20,696	110	20,806	5.5	4.0	24.6	24.7
12	Mining	16	20,396	8,015	28,411	5.4	5.5	15.1	21.0
13	Textiles, Apparel and Footwear	10	4,645	127	4,772	1.2	0.9	37.4	38.4
14	Wood, pulp and paper	4	2,049	0	2,049	0.5	0.4	35.8	35.8
15	Chemical, rubber, plastic products	32	126,130	42,105	168,235	33.5	32.3	23.1	30.8
16	Metal and Metal Products	16	79,692	43,103	122,795	21.2	23.6	41.6	64.1
18	Transport equipment nec	4	3,080	19,059	22,139	0.8	4.3	6.2	44.5
19	Machinery and Equip.	20	92,011	9,187	101,198	24.4	19.4	39.3	43.2
20	Electronic equipment	1	1,395	3,281	4,676	0.4	0.9	5.5	18.4
21	Energy goods	3	22,549	19,094	41,643	6.0	8.0	1.8	3.4
22	Manufactures nec	1	15	4	19	0.0	0.0	1.8	2.3
	Total	122	376,432	144,408	520,840	100.0	100.0	14.8	20.5

Source: PCTAS.

MERCOSUR Trade Policy

- A General View -

Despite the fact that MERCOSUR is presently involved in several preferential trade negotiations,[53] its current trade regime is relatively simple, with intra-zone trade basically liberalised. Some exceptions persist and vary according to the members, which explains the differences in the Common External Tariff (CET) applied by each country, as seen by the last four lines of Table J (Annex). Beyond the CET, Argentina and Paraguay also apply additional customs rates. The rate imposed by MERCOSUR to other non-member countries is the applied rate and exceptions are restricted to the preferences granted to the *Asociación Latinoamericana de Integración* (ALADI) countries.[54]

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[53] Such as: FTA MERCOSUR-EU, FTA with the Andean Community, FTAA and others that are less advanced (with South Africa, for example).

[54] Mexico, Peru, Venezuela, Colombia, Ecuador, Bolivia and Chile (these, too, are associated members of MERCOSUR).

The simple average tariff of the bloc is 14.4 percent.[55] The average for agricultural products is 13 percent, which is inferior to the one for manufactured goods - 15.4 percent. These are simple averages over the four members - they do not take into account either the size of the country or its share in each import. The global weighted average (by each country's total imports) is slightly higher - 14.9 percent.

Higher tariffs on manufactured goods reflect the protectionism of the bigger partners. Tariff averages for manufactures by member countries are: (i) Argentina: 15.3 percent; (ii) Brazil: 15.9 percent; (iii) Paraguay: 13.2; and (iv) Uruguay: 14.0 percent. Average tariffs are in fact proportional to the size and the industrial development level of each country.

Among the agricultural and food sectors, the most protected are the usual suspects: beverages and tobacco, dairy products and sugar. With regard to other manufactured goods, the most protected sectors (in terms of weighted tariff averages) are: textiles, apparel and footwear, motor vehicles and other manufactured goods.

The higher rates are applied to motor vehicles, textiles and some food products. The maximum rate applied is 35 percent and corresponds to the rate imposed by Brazil on automobile imports.[56] From the 5,114 tariff lines (defined at the HS 6-digit level), 26 face tariffs superior to 25 percent. They belong to the footwear (64) and automobiles (87) HS chapters.

NTBs Imposed by MERCOSUR

A first look at NTB applied by MERCOSUR (Castilho [2003a y 2003b]) countries suggests that these countries make ample use of these measures. In fact, about 70 percent of the products and 77 percent of the imports from the EU15 are subject to some kind of NTB. Nevertheless, one must look with caution at this information: the majority of these barriers are measures related to inspection, authorization, licensing and/or prohibition to protect human health, animals or vegetable life[57] and the high index of barriers also reflects a differentiated imposition according to each member country.

A distinction between non-tariff measures (NTM) and non-tariff barriers must be made. In the United Nations Conference on Trade and Development (UNCTAD) data set used herein, any measure different from tariffs that obstruct trade can be considered as a non-tariff barrier. At any rate, this large definition mixes different measures with different purposes and different restrictive degrees.[58] In the case of MERCOSUR, as can be seen from the imposed measures in Table K

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[55] Simple average tariffs by member countries are: (i) Argentina: 15.0 percent; (ii) Brazil: 15.5 percent; (iii) Paraguay: 13.2 and (iv) Uruguay: 13.9 percent.

[56] The auto sector is traditionally protected in MERCOSUR countries - notably final products - and the existing special automotive regime regulates the intra-regional trade. The higher motor vehicle tariffs reflect the high protection imposed on automobile imports; the other transport products - notably aircraft, but also railway and ships - face lower tariff rates.

[57] Fontagné *et al.* [2001] point to Brazil and Argentina as being the most protectionist countries in terms of environmental barriers out of a large set of countries.

[58] For a discussion about definitions and measures of NTB, see Deardoff and Stern [1997].

(Annex), a lot of them present low effectiveness in actual protection. This is clearly the case of the prohibition measures imposed on a large set of products whose imports continue to be significant. The great majority of these measures came into force in 1997, at the time of the Asian crisis, in order to reduce imports and solve balance of payments disequilibria. They are generic measures and affect all MERCOSUR partners, without discrimination. Additionally, they are redundant for a large set of goods, several of them being imposed simultaneously.

Specific measures such as price measures, antidumping or compensatory or quantitative restrictions, imposed only on specific countries, are very few. They have a stronger restriction capacity than the preceding ones.

Concerning imports from the EU15, the measures in force in 2000 affecting manufactured goods were the following:[59]

- Argentina imposes safeguard measures against metal products (HS ch. 82) imports from several European countries; antidumping measures against paper (HS ch. 48) imported from Austria and Finland and against ceramic products (HS ch. 69) and metal products (ch.82) coming from Italy, and quotas for automobiles (HS ch. 87) for all European countries.

- Brazil imposes antidumping measures on a chemical product (HS ch. 28) imported from the UK and some quantitative restrictions to minerals (HS ch. 25 and 27) and chemical products (HS ch. 28 and 29).

- Uruguay applies some minimum price measures on clothing imports (HS ch. 62) from UK.

Because of the methodological problems and the low efficacy of the majority of the NTMs imposed, we have not taken them into account in the present analysis.

MERCOSUR Imports: Sensitivity of Selected Goods

For reasons mentioned above, NTBs are not considered as an indicator of import sensibility for MERCOSUR. Table L (Annex) - the other core result of this section - presents some characteristics of the 122 selected products, i.e., those for which the FTA can improve the presence of the 10AC in the region.

For most of these selected products, the current presence of the 10AC is very low, despite trade complementarity with MERCOSUR countries. Liberalization can then improve new members' market access.

This is mainly the case of other manufactured goods, other than food products. More than 50 percent of the tariff lines are from three sectors: chemicals (HS chapters 28 and 29), iron and

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[59] Agricultural and food imports are more strongly affected by NTMs (other than authorization and prohibition) than manufactured goods.

steel products (chapters 72 and 73), some mechanical machines and equipment (ch. 84) and finally, glass, crystals and their products (ch. 70).

Agricultural products are very few: 6 out of 122. There is one variety of pork meat, one of fish, and four cereal goods. Liberalization of these products is usually scheduled for within 10 years, but at a faster pace. Food products are more numerous: 9 different kinds of food preparations (vegetables and animals). These 15 (HS) 6-digit level products correspond to 22 at the 8-digit level (in which the offer is made). Liberalization for these products is slower or to be negotiated afterwards (categories E or S). This is not surprising: in general, MERCOSUR countries are very competitive in agriculture and foodstuff. But in temperate agriculture - and products such as cereals - Europe can represent an important menace, mainly to Argentina, where this kind of agriculture is more developed.

Among manufactured goods, inorganic and organic chemicals are rather numerous. Chapter 28 - inorganic chemicals - assembles 8 products. Again the current level of MERCOSUR imports from the 10AC is very low, close to zero, but the TCI shows that specialization can assure a strong increase of trade in the case of tariff reduction. In this chapter the product with the highest TCI is shown. If we take the present level of protection and the negotiation category as indicators of the sensitivity of MERCOSUR imports, these products are not the most important ones for domestic producers as protection is, for all items, inferior to MERCOSUR tariff average. Concerning the 15 organic chemicals, the tariff is also inferior to the average, except for one item (HS 293371), and liberalization is to be achieved in 8 years. This means that this sector is not among the most sensitive to external competition. For them, complementarity can significantly raise, and even reverse, the preceding situation - which means that the enlargement could generate effects not currently noticeable within the EU15.

The 10AC present good competitive position in the iron and steel and the glass industry and they seem to compete with MERCOSUR in both European and local markets. Iron and steel is important mainly for the Brazilian economy, and the applied tariff reflects this importance (the majority of selected iron and steel products face tariffs superior to 15 percent). MERCOSUR classified these products in the category for which the liberalization schedule has not been defined yet.

The differences between the EU15 and EU25 RCA indicators show how competitive in the glass industry the new members are, notably concerning goods for home use. Tariffs are relatively high - they vary from 7 to 21 percent, the latter concerning half of the products in the sector - which indicates that domestic MERCOSUR production is very sensitive to 10AC imports. The liberalization schedule it proposed has reinforced this aspect: 3 products are classified in category "C", one in category "D" and for the remaining 6, liberalization has not yet been scheduled.

Seventeen products, belonging to the very large machinery and equipment sector, were identified as sensitive to 10AC competition. Member countries, notably Brazil, have a relatively important but not very competitive capital goods industry. Although this industry is in general rather protected, this is not the case for selected mechanical goods (chapter 84). On the contrary, the tariff is rather high for electrical and electronic ones (chapter 85); for the majority of tariff lines, liberalization has not been scheduled in the offer yet. As the RCA of EU25 varies significantly to the RCA of EU15, the new members seem to be an important new competitor in MERCOSUR markets.

Finally, we mention that MERCOSUR offer is even more cautious than the European one - though being much more generous than its first version. As Table 21 shows, the category with the smallest number of products is the one that envisages immediate liberalization.[60] This category comprises 95 percent of zero tariff lines, which means that there's virtually no news for the first year of the agreement for European exports. Category E is the most conservative in terms of liberalization: it is related to 28 percent of tariff lines and 41 percent of MERCOSUR total imports in 2003.

The liberalization schedule proposed is quite different between manufactures and agriculture & food. For the latter, liberalization is envisaged within a shorter delay, as 58 percent of tariff lines are concentrated in category C. For manufactured goods, categories D and E are the most important, concentrating more than half of the tariff lines. But category B detains also an important share of tariff lines - 18 percent. Category S - to be defined - is of the same importance for both product groups, answering for 15 percent of the total of both tariff lines.

TABLE 21A
MERCOSUR OFFER: TARIFF AND NUMBER OF PRODUCTS
BY CATEGORY OF NEGOTIATION (2003)

Category	Common External Tariff Simple average	Common External Tariff Maximum tariff	Number of tariff lines	MERCOSUR total imports (percent)
A	0.0	0.0	625	10.6
B	2.0	12.0	1,634	8.5
C	8.1	14.0	1,399	3.6
D	13.1	14.0	1,926	18.7
E	16.0	35.0	2,751	41.4
S	15.0	20.0	1,398	17.2

TABLE 21B
DISTRIBUTION OF AGRICULTURE AND MANUFACTURE GOODS
BY NEGOTIATING CATEGORIES OF MERCOSUR OFFER
(In percent)

Category	Agriculture and food	Manufacture
A	8.4	6.2
B	2.2	18.5
C	58.1	9.1
D	5.2	21.5
E	11.2	30.3
S	14.9	14.3
Number of tariff lines	1.044	8.969

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[60] MERCOSUR offer classifies products into five categories: (i) A, for immediate liberalization; (ii) B, for liberalization during the 8th year; (ii) categories C, D and E that foresee liberalization in 10 years but with different schedules (the first one being faster than the latter). There are still a considerable number of products whose liberalization is yet "to be defined" (S).

C. Policy Remarks

Despite the weak share of the 10AC in the EU15 market, the trade relationship between the two blocs became very intense during the nineties and will become deeper still with the enlargement. This means better access to the respective markets. In the case of MERCOSUR, the FTA agreement will probably be signed by the end of 2004; an agreement for which MERCOSUR's negotiation offer considered only the present EU15 structure.

EU15 imports from the 10AC and MERCOSUR are rather different. As shown in subsections *Trade Complementarity between the EU and the 10AC* and *MERCOSUR Export Potential to the EU*, they are characterized by a high geographical orientation index for most sectors but lower trade complementarity indicators. This suggests that geographical proximity and other institutional factors - including trade preferences - explain the intensity of the bilateral trade. In the case of MERCOSUR, complementarity exists within a larger number of sectors (13 out of 22) but the relative weight of the EU15 in MERCOSUR exports is weaker. Comparative advantages and complementarity are concentrated on manufactured goods in the EU15-10AC and on agriculture and food in the EU15-MERCOSUR imports. Despite the generality of this aggregate analysis, this first panorama highlights the difference in specialization of the two blocs with regard to the EU.

A more detailed view shows that, in agriculture & food, the specialization is really rather different. First, MERCOSUR presents comparative advantages in 16 of the 24 HS chapters, while the 10AC present comparative advantages in only 8. Secondly, the structures differ: if we look at the RCA by HS chapters for both 10AC and MERCOSUR, the only chapters where both blocs present comparative advantages are meat and its preparations, products of animal origin, vegetable products n.e.s. and its preparations (out of 24 chapters).

The differences appear also in the manufacturing sectors, even if in them the competition between the two blocs seems more intensive. The 10AC present a larger number of chapters with comparative advantages - 28 out of 71 - while MERCOSUR shows RCAs superior to one in 19 chapters. At this level of aggregation, there are comparative advantages in both blocs in only 9 chapters. The coincidences are for: footwear, several mineral and metal chapters (including iron and non-ferrous metals), one textile category (wool or animal hair), skins and articles and wood and articles (coal included).

These differences in specialization mean that competition, be it either in the EU15 or in MERCOSUR markets, will occur in more specific sectors.

The first impact that the accession can have on the FTA prospects is with respect to potential MERCOSUR exports. We have identified the products for which a potential exists and afterwards have chosen from among them those for which the superiority of MERCOSUR comparative advantages (related to the 10AC) can be compensated by a significant preference margin. Eighty-five products, at the HS 6-digit level, fit these criteria. Of these, twenty-two belong to the agricultural and food sectors, being, for the most part, processed foodstuff. As expected, these products face high levels of protection, what can give the new members a large preference margin, even if the 10AC accession does not guarantee the same production and trade conditions that benefit current members. In the last EU offer, most of these products will be liberalised within at

most eight years. However, the EU offer has not significantly advanced the case of agriculture and food products: for the majority of these items, liberalization has not been scheduled yet or comprises larger periods and quantitative restrictions; this being the case for thirteen out of the twenty-two identified in the sector.

Among other manufactured goods, the 10AC seem to be competitive in several sectors but only for some of them is the preference margin significant, thus benefiting the 10AC. They are: textiles, apparel and footwear, transport equipment products and electronic equipment. The level of relative protection won't probably change considerably with regard to current levels for chemicals, mining and metal products, despite the competitive menace of the 10AC accession.

The second impact of the enlargement is the competition in MERCOSUR markets. At present, the 10AC exports to MERCOSUR are not very important but these countries will gain better market access due to the FTA.

As one can expect from the specialization patterns in the two regions, few agricultural products exported by the 10AC represent a threat to MERCOSUR's internal markets. The few observed products are several food preparations.

The accession can more intensively affect the manufacturing sectors, notably chemicals (HS chapters 28 and 29), iron and steel products (chapters 72 and 73), certain machines and equipments (ch. 84 and 85) and, finally, glasses, crystals and theirs products (ch. 70). Tariffs are rather high for the last three sectors and the liberalization schedule varies significantly for machine and equipment, being not defined yet for iron and steel and glasses. Indeed, in the last MERCOSUR offer, only about twenty-six of the 122 identified products have a liberalization schedule shorter than nine years.

TABLE A
THE PROFILE OF EU IMPORTS FROM MERCOSUR, 1999/2001

Sector	Description	Geographical Orientation Index	Complemen-tarity Index	MERCOSUR Revealed Comp. Advantage	EU Revealed Comp. Disadvantage	Composition of EU-MERCOSUR imports (percent)
1	Wheat, corn and other grains	1.8	1.30	4.90	0.3	1.200
2	Coffee, rice and other crops	6.1	11.0	7.50	1.5	7.400
3	Vegetables and Fruits	8.6	3.10	2.20	1.4	3.800
4	Oil seeds and vegetable fats and oils	6.6	38.7	27.7	1.4	24.30
5	Sugar	0.1	11.4	16.2	0.7	0.100
6	Vegetable products n.e.s.	9.9	1.30	1.20	1.1	0.600
7	Livestock	1.3	0.30	0.40	0.8	0.000
8	Bovine Meat	8.6	4.20	6.70	0.6	3.500
9	Dairy	0.0	0.30	0.50	0.6	0.000
10	Beverages and Tobaccos	0.7	0.40	0.50	0.8	0.400
11	Other Food Products	2.9	2.50	2.70	0.9	11.70
12	Mining	1.7	4.90	3.50	1.4	9.900
13	Textiles, Apparel and Footwear	2.1	1.00	0.80	1.1	5.100
14	Wood, pulp and paper	2.0	1.40	1.50	0.9	8.300
15	Chemical, rubber, plastic products	0.8	0.50	0.50	1.0	4.200
16	Metal and Metal Products	1.3	1.30	1.40	0.9	6.900
17	Motor vehicles and parts	1.3	0.40	0.60	0.7	5.200
18	Transport equipment nec	0.8	2.20	1.30	1.7	2.400
19	Machinery and Equip.	0.8	0.30	0.30	1.1	3.500
20	Electronic equipment	1.3	0.10	0.10	0.9	0.900
21	Energy goods	0.7	0.70	0.60	1.0	0.500
22	Manufactures nec	1.4	0.10	0.10	1.0	0.200
	Total	1.9	..	..	..	100.0

Notes: see Annex for methodology. Source: PCTAS.

TABLE B
THE PROFILE OF EU IMPORTS FROM THE 10AC, 1999/2001

Sector	Description	Geographical Orientation Index	Complemen-tarity Index	10AC Revealed Comp. Advantage	EU Revealed Comp. Disadvantage	Composition of EU-10AC imports (per cent)
1	Wheat, corn and other grains	3.30	0.2	0.6	0.3	0.100
2	Coffee, rice and other crops	7.30	0.4	0.2	**1.5**	0.100
3	Vegetables and Fruits	10.7	0.6	0.4	**1.4**	0.400
4	Oil seeds and vegetable fats and oils	9.50	0.8	0.5	**1.4**	0.400
5	Sugar	3.80	0.4	0.5	0.7	0.000
6	Vegetable products n.e.s.	17.7	**1.5**	**1.4**	**1.1**	0.500
7	Livestock	6.90	**1.7**	**2.1**	0.8	0.200
8	Bovine Meat	9.40	0.2	0.3	0.6	0.100
9	Dairy	1.10	0.8	**1.3**	0.6	0.300
10	Beverages and Tobaccos	1.10	0.3	0.4	0.8	0.200
11	Other Food Products	4.40	0.9	0.9	0.9	2.500
12	Mining	3.30	**1.7**	**1.2**	**1.4**	2.700
13	Textiles, Apparel and Footwear	7.40	**1.5**	**1.3**	**1.1**	10.90
14	Wood, pulp and paper	4.70	**2.0**	**2.1**	0.9	10.40
15	Chemical, rubber, plastic products	2.40	0.7	0.7	**1.0**	7.300
16	Metal and Metal Products	5.00	**1.3**	**1.4**	0.9	10.80
17	Motor vehicles and parts	4.40	**1.1**	**1.6**	0.7	18.00
18	Transport equipment nec	2.90	**1.0**	0.6	**1.7**	1.500
19	Machinery and Equip.	3.40	**1.1**	**1.1**	**1.1**	18.00
20	Electronic equipment	7.40	0.7	0.8	0.9	10.60
21	Energy goods	18.7	0.5	0.5	**1.0**	4.000
22	Manufactured goods nec	5.70	0.5	0.5	**1.0**	0.900
	Total	*4.70*	*..*	*..*	*..*	*100.0*

Notes: see Annex to the methodology. Source: PCTAS.

TABLE C
EU15-MERCOSUR IMPORTS: PROFILE OF PRODUCTS WITH EXPORT POTENTIAL

Sectors	Description	Tariff lines		EU imports from MERCOSUR	
		Number	Per cent of total (by sector)	US$ thousand	Composition (per cent)
1	Wheat, corn and other grains	2	16.7	252,046	0.80
2	Coffee, rice and other crops	2	3.00	1,564,492	0.00
3	Vegetables and Fruits	2	2.40	797,455	0.00
4	Oil seeds and vegetable fats and oils	5	8.10	5,105,671	0.10
5	Sugar	3	33.3	21,474	24.8
7	Livestock	1	12.5	4,720	85.8
10	Beverages and Tobaccos	2	6.90	86,368	3.20
11	Other Food Products	20	5.50	2,451,191	1.60
12	Mining	31	12.4	2,073,381	1.60
13	Textiles, Apparel and Footwear	30	3.40	1,065,383	22.8
14	Wood, pulp and paper	8	3.30	1,751,850	0.80
15	Chemical, rubber, plastic products	64	6.80	888,813	7.60
16	Metal and Metal Products	30	5.10	1,445,027	4.10
17	Motor vehicles and parts	4	7.40	1,084,343	2.60
18	Transport equipment nec	3	3.80	503,643	68.4
19	Machinery and Equip.	48	5.70	746,086	21.3
20	Electronic equipment	2	1.70	178,894	0.50
21	Energy goods	1	2.80	108,485	0.00
22	Manufactured goods nec	7	4.10	39,023	6.30
	Total	*265*	*5.50*	*21,032,012*	*4.80*

Source: PCTAS.

TABLE D
EU TARIFF PROTECTION, 2000

Sectors	Description	10AC		GSP		MFN	
		Simple average	Maximum tariff	Simple average	Maximum tariff	Simple average	Maximum tariff
1	Wheat, corn and other grains	19.9	80.3	20.0	80.3	20.0	80.3
2	Coffee, rice and other crops	10.7	337.3	9.3	254.9	11.9	337.3
3	Vegetables and Fruits	7.6	110.2	7.5	110.2	8.70	110.2
4	Oil seeds and vegetable fats and oils	8.6	145.8	8.9	145.8	9.8	145.8
5	Sugar	71.8	187.1	71.8	187.1	71.8	187.1
6	Vegetable products n.e.s.	0.1	7.3	0.2	5.1	0.3	7.3
7	Livestock	28.3	94.7	28.3	94.2	28.8	94.7
8	Bovine Meat	53.1	160.4	53.2	160.4	53.4	160.4
9	Dairy	102.5	424.6	105.2	424.6	101.7	424.6
10	Beverages and Tobaccos	20.0	113.7	16.6	61.2	23.0	113.7
11	Other Food Products	16.7	168.2	16.1	168.2	17.6	168.2
12	Mining	0.0	0.0	0.8	8.4	2.3	12.0
13	Textiles, Apparel and Footwear	0.0	0.0	7.0	11.9	8.5	17.0
14	Wood, pulp and paper	0.0	0.0	0.6	7.0	2.8	10.0
15	Chemical, rubber, plastic products	0.2	66.30	1.5	66.3	4.3	66.3
16	Metal and Metal Products	0.1	2.7	0.9	6.3	2.7	9.0
17	Motor vehicles and parts	0.0	0.0	3.7	12.8	6.3	18.3
18	Transport equipment nec	0.0	0.0	0.7	10.5	2.3	15.0
19	Machinery and Equip.	0.0	0.0	0.4	5.8	2.1	13.7
20	Electronic equipment	0.0	0.0	1.4	9.8	2.3	14.0
21	Energy goods	0.1	2.8	0.0	0.0	0.3	2.8
22	Manufactures nec	0.0	0.0	0.6	6.3	2.9	9.0
	Total	*2.8*	*424.6*	*4.5*	*424.6*	*6.4*	*424.6*

Notes: Includes Ad Valorem equivalent for specific duties; 10AC: simple average of all 10 preferential regimes.

Source: TRAINS.

TABLE E
NTBS IMPOSED BY EU15 ON IMPORTS FROM 10AC, 1999
(Per cent)

Sectors	Description	Antidumping and safeguard measures		Authorization, Surveillance, Technical measures, Customs formalities		Quantitative restrictions		Prohibitions		ALL NTBs	
		Frequency Index	Coverage Index	Frequency Index	Coverage Index	Frequency Index	Coverage Index	Frequency Index	Coverage Index	Frequency Index	Coverage Index
1	Wheat, corn and other grains	0.0	0.0	100.0	100.0	0.0	0.0	0.0	0.0	100.0	100.0
2	Coffee, rice and other crops	0.0	0.0	17.9	32.5	0.0	0.0	0.0	0.0	17.9	32.5
3	Vegetables and Fruits	2.4	12.9	13.10	15.6	0.0	0.0	0.0	0.0	13.1	15.6
4	Oil seeds and vegetable fats and oils	0.0	0.0	12.90	4.7	0.0	0.0	0.0	0.0	12.9	4.7
5	Sugar	0.0	0.0	100.0	100.0	0.0	0.0	0.0	0.0	100.0	100.0
6	Vegetable products n.e.s.	0.0	0.0	17.9	51.1	0.0	0.0	0.0	0.0	17.9	51.1
7	Livestock	0.0	0.0	62.5	98.1	0.0	0.0	0.0	0.0	62.5	98.1
8	Bovine Meat	0.0	0.0	83.3	95.2	0.0	0.0	0.0	0.0	83.3	95.2
9	Dairy	0.0	0.0	90.5	90.1	0.0	0.0	0.0	0.0	90.5	90.1
10	Beverages and Tobaccos	0.0	0.0	24.1	30.5	0.0	0.0	0.0	0.0	24.1	30.5
11	Other Food Products	0.3	3.7	40.5	48.5	0.0	0.0	0.0	0.0	40.5	48.5
13	Textiles, Apparel and Footwear	0.1	0.1	33.7	62.5	0.3	0.4	0.3	0.0	34.3	63.0
14	Wood, pulp and paper	0.4	2.6	8.8	16.7	0.0	0.0	0.0	0.0	9.2	19.3
15	Chemical, rubber, plastic products	0.1	1.3	4.4	3.2	0.4	0.9	0.0	0.0	4.5	4.5
16	Metal and Metal Products	1.6	2.5	15.4	14.7	0.0	0.0	0.0	0.0	16.9	17.2
19	Machinery and Equip.	0.0	0.0	0.5	0.3	0.0	0.0	0.0	0.0	0.5	0.3
22	Manufactured goods nec	0.0	0.0	22.5	34.5	0.0	0.0	0.0	0.0	22.5	34.5
	Total	*0.3*	*0.8*	*15.3*	*13.1*	*0.1*	*0.1*	*0.1*	*0.0*	*15.6*	*13.8*

Notes: Frequency index: percent of tariff lines affected by, at least, one measure. Coverage index: percent of sector imports (1999-2001) covered by, at least, one measure.

Source: TRAINS and PCTAS.

TABLE F
NTBS IMPOSED BY THE EU15 ON MERCOSUR EXPORTS, 1999

(Per cent)

Sectors	Description	Antidumping and safeguard measures		Authorization, Surveillance, Technical measures, Customs formalities		Quantitative restrictions		Prohibitions		ALL NTBs	
		Frequency Index	Coverage Index	Frequency Index	Coverage Index	Frequency Index	Coverage Index	Frequency Index	Coverage Index	Frequency Index	Coverage Index
1	Wheat, corn and other grains	0.0	0.0	100.0	100.0	0.00	0.0	0.0	0.0	100.0	100.0
2	Coffee, rice and other crops	0.0	0.0	17.6	6.8	0.00	0.0	0.0	0.0	17.6	6.8
3	Vegetables and Fruits	0.0	0.0	10.7	2.0	0.00	0.0	0.0	0.0	10.7	2.0
4	Oil seeds and vegetable fats and oils	0.0	0.0	12.9	0.1	0.00	0.0	0.0	0.0	12.9	0.1
5	Sugar	0.0	0.0	100.0	100.0	0.00	0.0	0.0	0.0	100.0	100.0
6	Vegetables products n.e.s.	0.0	0.0	16.3	6.8	0.00	0.0	0.0	0.0	16.3	6.8
7	Livestock	0.0	0.0	62.5	85.8	0.00	0.0	0.0	0.0	62.5	85.8
8	Bovine Meat	0.0	0.0	83.3	99.5	0.00	0.0	0.0	0.0	83.3	99.5
9	Dairy	0.0	0.0	86.4	100.0	0.00	0.0	0.0	0.0	86.4	100.0
10	Beverages and Tobaccos	0.0	0.0	23.3	77.2	0.00	0.0	0.0	0.0	23.3	77.2
11	Other Food Products	0.3	0.0	40.1	29.9	0.00	0.0	0.0	0.0	40.1	29.9
13	Textiles, Apparel and Footwear	0.0	0.0	5.9	72.9	22.6	7.4	0.3	0.0	28.6	80.2
14	Wood, pulp and paper	0.0	0.0	7.9	29.6	0.40	0.0	0.0	0.0	8.3	29.6
15	Chemical, rubber, plastic products	0.1	0.7	4.5	4.0	0.40	1.4	0.0	0.0	4.6	4.7
16	Metal and Metal Products	0.3	0.7	0.5	0.0	0.00	0.0	0.0	0.0	0.8	0.7
19	Machinery and Equip.	0.0	0.0	0.5	0.0	0.00	0.0	0.0	0.0	0.5	0.0
22	Manufactured goods nec	0.0	0.0	22.5	5.2	0.00	0.0	0.0	0.0	22.5	5.2
	Total	*0.1*	*0.1*	*8.400*	*15.6*	*4.00*	*0.4*	*0.1*	*0.0*	*12.50*	*16.00*

Notes: Frequency index: percent of tariff lines affected by, at least, one measure. Coverage index: percent of sector imports (1999-2001) covered by, at least, one measure.

Source: TRAINS and PCTAS.

TABLE G
SELECTED GOODS

HS	Description	RCA MERCOSUR (1)	RCD UE (2)	TCI UE-MERCOSUR (3)	RCA 10AC	TCI UE-10AC	Import. UE-MERCOSUR (4)	Export. MERCOSUR -World (4)	Import. UE-10AC (4)	Applied tariff on MERCOSUR - SGP (5)	NTB on UE-MERCOSUR imports (6)
20721	Fowls, domestic, whole, frozen	67.5	0.1	5.30	0.90	0.1	3,725	292,207	14,864	30.10	0
21020	Bovine meat cured	2.30	2.2	5.10	0.00	0.0	0	1,249	219	44.60	1
90122	Coffee, roasted, decaffeinated	1.90	0.7	1.40	0.00	0.0	451	2,919	77	3.100	0
130220	Pectic substances, pectinates & pectates	2.10	1.0	2.00	0.40	0.4	2,713	8,997	3,072	10.60	0
151219	Sunflower-seed/safflower oil& their fractions refined but not chem modified	26.5	0.1	2.20	0.90	0.1	2,136	176,012	18,362	6.800	0
151590	Veg fats & oils nes & their fractions, refined or not but not chemically mod	1.10	1.3	1.40	0.20	0.3	395	3,851	1,219	4.500	1
151790	Edible mx/prep of animal/veg fats & oils/of fractions ex hd No 15.16	9.10	0.1	1.00	0.40	0.0	0	61,586	5,798	14.40	0
152200	Degras & residues from fatty substances or animal or vegetable waxes	7.10	0.2	1.40	1.00	0.2	117	2,698	606	100.8	1
160416	Anchovies, prepared or preserved, whole or in pieces, but not minced	1.10	1.7	1.80	0.00	0.0	52	2,040	52	25.00	0
170112	Raw sugar, beet	4.30	0.4	1.70	2.00	0.8	0	2,831	5,638	123.9	1
170191	Refined sugar, in solid form, containing added flavourg or colourg matter	17.9	0.2	3.10	0.60	0.1	0	10,450	1,207	57.10	1
170199	Refined sugar, in solid form, nes	6.20	0.3	2.00	0.70	0.2	5,325	209,815	50,369	136.4	1
170290	Sugar nes, including invert sugar	7.20	0.2	1.70	0.30	0.1	76	24,752	3,082	47.50	1
170490	Sugar confectionery nes (includg white chocolate), not containg cocoa	2.40	0.5	1.20	1.10	0.5	1,571	108,313	89,210	18.60	0
180310	Cocoa paste not defatted	0.90	2.1	1.80	0.10	0.3	574	15,462	3,805	6.700	0
190300	Tapioca subst prep from starch in flake, grain, pearl, siftg or sim forms	6.00	0.4	2.70	0.00	0.0	29	1,429	0	31.80	0
200819	Nuts & seeds nes incl mx, o/w prep o presvd, sugard, sweetend, spiritd o not	1.40	1.9	2.70	0.10	0.3	76	12,000	5,853	3.400	0

HS	Description	RCA MERCOSUR (1)	RCD UE (2)	TCI UE-MERCOSUR (3)	RCA 10AC	TCI UE-10AC	Import. UE-MERCOSUR (4)	Export. MERCOSUR -World (4)	Import. UE-10AC (4)	Applied tariff on MERCOSUR - SGP (5)	NTB on UE-MERCOSUR imports (6)
200960	Grape juice (incl grape must) unferment&unspiritd,wthr/nt sug/sweet	18.6	0.1	1.90	0.20	0.0	1,197	68,837	5,650	109.3	0
210110	Coffee extracts, essences & concentrates and preparations thereof	10.1	0.8	8.40	0.40	0.4	26,144	190,614	40,785	5.600	0
220710	Undenaturd ethyl alcohol of an alcohol strgth by vol of 80% vol/higher	9.80	0.3	2.60	0.20	0.1	2,497	86,924	6,033	49.80	0
230250	Bran, sharps and other residues of leguminous plants, pelleted or not	27.3	0.1	2.10	0.00	0.0	0	4,907	0	1.700	0
240391	Homogenized or reconstituted tobacco	0.90	2.0	1.90	0.40	0.7	287	3,174	1,350	11.60	0
271091	Petroleum and derivates	6.00	0.5	2.80	1.40	0.6	0	404,345	164,920	Na	0
280521	Calcium	0.90	1.3	1.10	0.00	0.0	25	518	17	5.500	0
281129	Inorganic oxygen compounds of non-metals nes	4.1	0.6	2.30	2.70	1.5	0	4,671	5,036	0.000	0
282010	Manganese dioxide	2.3	0.5	1.10	0.00	0.0	123	5,295	18	3.700	0
282739	Chlorides of metals nes	5.7	0.9	5.00	0.10	0.0	2,764	11,746	929	0.000	0
282760	Iodides and iodide oxides of metals	1.700	1.0	1.70	0.00	0.0	337	1,392	24	0.000	0
283010	Sodium sulphides	7.800	0.7	5.10	0.50	0.3	36	5,515	905	3.800	0
283323	Chromium sulphates	15.30	0.2	3.70	1.40	0.3	107	25,717	1,454	0.000	0
283670	Lead carbonate	3.400	0.6	1.90	0.00	0.0	0	35	0	0.000	0
283691	Lithium carbonates	3.900	1.0	4.00	0.50	0.5	0	3,550	771	0.000	0
285000	Hydrides, nitrides, azides, silicides & borides	3.800	1.2	4.70	0.50	0.6	135	9,225	1,737	0.800	0
290323	Tetrachloroethylene (perchloroethylene)	7.900	0.2	1.20	0.80	0.1	0	7,439	1,535	5.600	0
290420	Derivs of hydrocarbons cntg only nitro or only nitroso groups	3.300	1.7	5.80	1.20	2.1	0	4,285	3,135	1.900	0
290515	Pentanol (amyl alcohol) and isomers thereof	3.600	0.7	2.50	0.00	0.0	217	861	0	3.800	0
290519	Saturated monohydric acyclic alcohols nes	2.600	0.6	1.60	0.10	0.1	99	24,113	624	3.800	0

TABLE G (continued)

HS	Description	RCA MERCOSUR (1)	RCD UE (2)	TCI UE-MERCOSUR (3)	RCA 10AC	TCI UE-10AC	Import. UE-MERCOSUR (4)	Export. MERCOSUR -World (4)	Import. UE-10AC (4)	Applied tariff on MERCOSUR - SGP (5)	NTB on UE-MERCOSUR imports (6)
290543	Mannitol	13.90	0.2	2.40	0.00	0.0	0	7,278	0	57.60	0
290942	Monomethyl ethers of ethylene glycol or of diethylene glycol	6.500	1.9	12.10	0.10	0.1	0	2,400	34	3.800	0
290944	Monoalkylethers of ethylene glycol or of diethylene glycol, nes	3.600	1.2	4.30	0.00	0.0	58	3,250	61	3.800	0
291812	Tartaric acid	5.400	1.3	6.80	0.90	1.1	1,441	10,284	2,296	0.000	0
291821	Salicylic acid and its salts	32.00	0.7	21.8	0.30	0.2	188	13,853	292	2.200	0
320290	Inorganic tanning subst;tanning preps;enzymatic preps for pre-tanning	2.500	0.5	1.30	0.00	0.0	457	9,479	190	0.000	0
320415	Vat dyes and preparations based thereon	1.200	1.3	1.60	0.20	0.3	1,511	5,567	1,341	2.200	0
330210	Mixtures of odoriferous substances for the food or drink industries	1.300	1.3	1.70	0.20	0.2	3,012	63,175	14,917	0.000	0
350300	Gelatin and gelatin derivs; isinglass; glues of animal origin, nes	9.000	1.0	9.30	0.40	0.4	24,371	73,110	9,215	0.000	0
370110	Photographic plates & film in the flat,sensitised,unexposed,for X-ray	1.000	1.1	1.10	0.10	0.1	194	25,964	2,622	0.000	0
370199	Photographic plates and film in the flat, sensitised, unexposed, nes	1.000	1.4	1.30	0.00	0.1	25	5,377	455	0.000	0
370210	Photographic film in rolls, sensitised, unexposed, for X-ray	3.300	0.5	1.80	0.10	0.0	767	20,204	398	0.000	0
370310	Photo paper,paperboard&textile sens,unexp in roll of a width > 610mm	3.100	0.4	1.20	0.00	0.0	1,723	18,392	111	0.000	0
370320	Photographic paper,paperboard&textile sens,unexp f colour photography	3.600	0.3	1.10	0.00	0.0	1,595	77,296	742	0.000	0
380130	Carbonaceous pastes for electrodes&similar pastes for furnace linings	4.000	0.4	1.60	2.30	0.9	0	6,034	8,806	0.000	0
380890	Pesticides includg rodenticides,nes,packagd for retail sale/formulatd	1.100	1.1	1.20	0.50	0.5	304	10,102	6,680	0.000	0

HS	Description	RCA MERCOSUR (1)	RCD UE (2)	TCI UE-MERCOSUR (3)	RCA 10AC	TCI UE-10AC	Import. UE-MERCOSUR (4)	Export. MERCOSUR-World (4)	Import. UE-10AC (4)	Applied tariff on MERCOSUR - SGP (5)	NTB on UE-MERCOSUR imports (6)
390220	Polyisobutylene	3.300	0.9	3.00	0.00	0.0	1,617	9,903	0	6.200	0
391220	Cellulose nitrates (incl collodions)	3.000	0.5	1.40	2.60	1.2	843	9,374	13,900	0.000	0
410421	Bovine leather, vegetable pre-tanned, nes	17.70	0.3	6.00	0.10	0.0	1,838	15,575	390	4.500	1
410431	Bovine and equine leather, full/split grains, nes	13.00	0.9	11.4	0.80	0.7	100,020	568,082	61,476	4.300	1
410439	Bovine and equine leather, nes	13.60	0.3	4.50	0.50	0.2	10,605	304,362	21,707	4.500	1
441119	Fibreboard >0.8 g/cm2 nes	1.600	0.8	1.30	1.10	0.9	423	20,533	33,136	4.900	0
520922	Twill weave cotton fabrics,>/=85%, more than 200 g/m2, bleached	3.000	0.4	1.20	0.80	0.3	254	4,069	1,808	7.400	0
520942	Denim fabrics of cotton,>/=85%, more than 200 g/m2	2.200	0.5	1.00	0.10	0.0	3,744	92,777	5,165	7.400	0
560721	Binder o baler twine,of sisal o oth textile fibres of the genus Agave	169.8	0.3	52.6	0.10	0.0	2,638	45,751	237	10.20	0
560729	Twine nes, cordage, ropes and cables, of sisal textile fibres	8.400	0.6	5.30	0.40	0.2	67	2,817	300	10.20	0
580219	Terry towellg&similar woven terry fab of cotton,o/t unbl&o/t nar fab	4.300	0.6	2.70	0.80	0.5	915	3,013	909	7.400	1
591110	Textile fabrics usd f card clothing,and sim fabric f technical uses	2.600	1.0	2.60	0.40	0.4	95	6,152	1,815	4.500	0
610331	Mens/boys jackets and blazers, of wool or fine animal hair, knitted	1.100	2.2	2.40	0.50	1.1	0	301	219	10.80	0
630520	Sacks and bags, for packing of goods, of cotton	27.70	1.0	26.6	1.10	1.1	0	14,233	1,208	6.100	0
630611	Tarpaulins, awnings and sunblinds, of cotton	3.300	0.7	2.20	1.50	1.0	0	552	394	10.80	0
640199	Waterproof footwear, outer soles/uppers of rubber or plastics, nes	2.900	0.4	1.10	0.80	0.3	240	2,543	875	11.90	0
640320	Footwear,outr sole/uppr of leathr,strap across the instep/arnd big toe	2.200	0.6	1.30	0.20	0.1	87	1,511	231	5.600	1
640330	Footwear,wooden,outer soles of rubber/ plas/leather&uppers of leather	15.30	2.3	35.3	14.6	33.7	256	5,970	8,210	5.600	1

TABLE **G** (continued)

HS	Description	RCA MERCOSUR (1)	RCD UE (2)	TCI UE-MERCOSUR (3)	RCA 10AC	TCI UE-10AC	Import. UE-MERCOSUR (4)	Export. MERCOSUR -World (4)	Import. UE-10AC (4)	Applied tariff on MERCOSUR - SGP (5)	NTB on UE-MERCOSUR imports (6)
640351	Footwear, outer soles and uppers of leather, covering the ankle, nes	1.100	1.2	1.30	0.80	1.0	1,721	7,921	11,703	5.600	1
640359	Footwear, outer soles and uppers of leather, nes	2.600	1.3	3.50	0.30	0.4	4,984	83,649	18,075	5.300	1
640399	Footwear, outer soles of rubber/plastics uppers of leather, nes	5.300	1.1	5.80	1.20	1.3	112,531	1,081,181	388,262	5.400	1
640590	Footwear, nes	2.000	0.9	1.80	1.20	1.1	300	7,770	8,205	7.400	0
690810	Tiles, cubes and sim <7 cm rect or not etc, glazed ceramics	5.200	0.3	1.60	0.30	0.1	123	25,772	3,002	4.900	0
690890	Tiles, cubes and sim nes, glazed ceramics	2.700	0.9	2.60	0.70	0.7	15,982	186,900	88,101	3.800	0
691390	Statuettes and other ornamental articles of ceramics nes	0.800	2.1	1.70	0.50	1.1	412	10,276	10,824	3.800	0
760320	Powders, aluminium, of lamellar structure, including flakes	1.300	1.0	1.30	0.90	0.9	0	1,044	1,219	3.700	0
760521	Wire,aluminium alloy,w a maximum cross sectional dimension exceedg 7mm	3.100	0.7	2.30	0.50	0.4	437	7,807	3,902	5.200	0
821192	Butcher's knives, hunting knives and other knives having fixed blades	3.700	1.2	4.30	0.10	0.1	623	16,576	533	1.500	0
852721	Radio rece nt capabl of op w/o ext source of power f motor veh,combind	2.200	0.8	1.80	1.30	1.1	788	222,804	193,938	8.900	0
852729	Radio rece nt capable of op w/o ext source of power f motor vehicl,nes	5.000	0.2	1.10	0.40	0.1	43	30,972	3,674	8.400	0
870210	Diesel powered buses with a seating capacity of > nine persons	3.200	0.5	1.70	2.40	1.3	1,880	271,237	212,842	9.100	0
871120	Motorcycles with reciprocatg piston engine displacg > 50 cc to 250 cc	0.800	1.6	1.30	0.00	0.1	119	50,557	1,206	5.600	0

Notes: (1) Revealed Comparative Advantage; (2) Revealed Comparative Disadvantage; (3) Trade Complementarity Index; (4) US$ thousand; (5) SGP tariffs; (6) 1 means the presence of a NTB.

TABLE H
MERCOSUR IMPORTS FROM EU15 AND "EU25" (EU15 + 10AC), 1999-2001

Sectors	Description	US$ thousands				Composition (percent)			Market share in MERCOSUR	
		Total imports	Imports from EU15	Imports from 10AC	Imports from EU25	Total imports	Imports from EU15	Imports from EU25	Imports from EU15	Imports from EU25
1	Wheat, corn and other grains	1,189,003	5,079	55	5,134	1.400	0.000	0.000	0.40	0.40
2	Coffee, rice and other crops	566,780	43,917	490	44,407	0.700	0.200	0.200	7.70	7.80
3	Vegetables and Fruits	550,982	44,061	24	44,085	0.700	0.200	0.200	8.00	8.00
4	Oil seeds and vegetable fats and oils	482,534	70,594	238	70,832	0.600	0.300	0.300	14.6	14.7
5	Sugar	23,018	0	0	0	0.000	0.000	0.000	0.00	0.00
6	Vegetables products n.e.s.	313,363	17,963	0	17,963	0.400	0.100	0.100	5.70	5.70
7	Livestock	36,161	2,514	252	2,766	0.000	0.000	0.000	7.00	7.60
8	Bovine Meat	139,472	2,554	0	2,554	0.200	0.000	0.000	1.80	1.80
9	Dairy	403,963	49,933	2,453	52,386	0.500	0.200	0.200	12.4	13.0
10	Beverages and Tobaccos	640,471	244,915	2,355	247,270	0.800	1.100	1.100	38.2	38.6
11	Other Food Products	1,968,842	351,879	2,658	354,537	2.400	1.600	1.600	17.9	18.0
12	Mining	1,576,423	336,417	14,242	350,659	1.900	1.600	1.600	21.3	22.2
13	Textiles, Apparel and Footwear	2,874,202	376,354	2,913	379,267	3.400	1.700	1.700	13.1	13.2
14	Wood, pulp and paper	3,037,441	894,615	4,872	899,487	3.600	4.100	4.000	29.5	29.6
15	Chemical, rubber, plastic products	17,925,328	5,479,864	111,167	5,591,031	21.50	25.30	25.10	30.6	31.2
16	Metal and Metal Products	4,398,770	1,266,624	52,600	1,319,224	5.300	5.800	5.900	28.8	30.0
17	Motor vehicles and parts	7,336,033	2,509,955	26,337	2,536,292	8.800	11.60	11.40	34.2	34.6
18	Transport equipment nec	2,741,104	877,794	21,338	899,132	3.300	4.000	4.000	32.0	32.8
19	Machinery and Equip.	17,215,362	7,106,126	95,952	7,202,078	20.60	32.80	32.40	41.3	41.8
20	Electronic equipment	10,590,927	1,621,074	65,695	1,686,769	12.70	7.500	7.600	15.3	15.9
21	Energy goods	8,773,977	271,784	171,090	442,874	10.50	1.300	2.000	3.10	5.00
22	Manufactures nec	715,776	111,687	480	112,167	0.900	0.500	0.500	15.6	15.7
	Total	83,499,932	21,685,703	575,211	22,260,914	100.0	100.0	100.0	26.0	26.7

Notes: EU25 = EU15 + 10AC.

Source: PCTAS.

TABLE I
CHANGES IN THE TRADE COMPLEMENTARITY BETWEEN MERCOSUR AND EU AFTER ACCESSION

Sector	Description	Complementarity Index MERCOSUR-EU15	Complementarity Index MERCOSUR-EU25	EU15 Revealed Comparative Advantage	EU25 Revealed Comparative Advantage	MERCOSUR Revealed Comparative Disadvantage
1	Wheat, corn and other grains	0.1022	0.1099	0.5003	0.5380	0.2043
2	Coffee, rice and other crops	0.2358	0.2363	0.3997	0.4006	0.5899
3	Vegetables and Fruits	0.2326	0.2085	0.4196	0.3762	0.5544
4	Oil seeds and vegetable fats and oils	0.1682	0.1875	0.4318	0.4814	0.3895
5	Sugar	0.0012	0.0012	0.6103	0.6270	0.0019
6	Vegetables products n.e.s.	0.1484	0.2833	0.1701	0.3248	0.8724
7	Livestock	0.1560	0.1738	0.6787	0.7564	0.2298
8	Bovine Meat	0.0220	0.0196	0.3349	0.2988	0.0657
9	Dairy	0.7442	0.3284	2.5734	1.1357	0.2892
10	Beverages and Tobaccos	2.4643	1.3508	3.9378	2.1584	0.6258
11	Other Food Products	0.4484	0.4016	0.8483	0.7599	0.5285
12	Mining	1.0422	1.0897	1.1294	1.1809	0.9227
13	Textiles, Apparel and Footwear	0.2413	0.2894	0.6685	0.8019	0.3609
14	Wood, pulp and paper	0.7354	0.7693	1.1076	1.1586	0.6639
15	Chemical, rubber, plastic products	3.4157	2.6368	1.9530	1.5076	1.7490
16	Metal and Metal Products	0.7234	0.7318	1.0114	1.0231	0.7153
17	Motor vehicles and parts	0.8024	0.6984	1.2997	1.1311	0.6174
18	Transport equipment nec	2.2398	2.1498	1.6101	1.5454	1.3911
19	Machinery and Equip.	2.2118	2.1332	1.5949	1.5381	1.3868
20	Electronic equipment	0.4620	0.5320	0.5151	0.5931	0.8969
21	Energy goods	0.2284	0.3039	0.1785	0.2376	1.2794
22	Manufactures nec	0.2884	0.3199	0.6825	0.7572	0.4225

Notes: EU25 = EU15 + 10AC.

Source: PCTAS.

TABLE J
MERCOSUR TARIFF PROTECTION, 2000

Sectors	Description	Simple average	Weighted average (1)	Maximum tariff (2)
1	Wheat, corn and other grains	6.0	6.00	11.0
2	Coffee, rice and other crops	9.2	9.10	17.0
3	Vegetables and Fruits	11.8	10.4	13.0
4	Oil seeds and vegetable fats and oils	10.6	8.40	15.0
5	Sugar	19.0	15.5	23.0
6	Vegetables products n.e.s.	8.2	6.70	11.0
7	Livestock	2.6	1.80	7.00
8	Bovine Meat	12.4	4.80	15.0
9	Dairy	18.8	19.0	27.0
10	Beverages and Tobaccos	20.9	20.4	25.0
11	Other Food Products	13.7	12.2	32.0
12	Mining	11.0	10.9	23.0
13	Textiles, Apparel and Footwear	20.3	20.2	33.0
14	Wood, pulp and paper	14.0	13.9	23.0
15	Chemical, rubber, plastic products	11.5	11.7	23.0
16	Metal and Metal Products	14.6	14.7	23.0
17	Motor vehicles and parts	17.5	20.1	35.0
18	Transport equipment nec	11.4	12.2	26.0
19	Machinery and Equip.	13.6	16.6	26.0
20	Electronic equipment	14.4	17.0	26.8
21	Energy goods	1.3	1.80	7.00
22	Manufactures nec	19.3	19.8	24.0
	Total	*14.4*	*14.9*	*35.0*

Notes: (1) weighted by countries' total imports in 2000, except Paraguay (1999).

(2) Maximum tariff among the four countries;

(3) Simple average.

Source: TRAINS.

TABLE K
NON-TARIFF MEASURES IMPOSED BY MERCOSUR TO EUROPEAN EXPORTS, 2000

HS section	Description	All NTB measures		Coverage Index				
		Frequency Index	Coverage Index	Authorization and surveillance	Prohibition	Price Measures	Antidumping and safeguard measures	Quantitative restrictions
I	Live animals, animal products	100.0	100.0	100.0	79.1	0.0	0.0	2.6
II	Vegetable products	100.0	100.0	100.0	53.7	0.0	0.0	0.0
III	Animal or vegetable fats and oils	100.0	100.0	100.0	0.6	0.0	27.4	0.0
IV	Prepared foodstuffs; beverages; tobacco	100.0	100.0	100.0	23.0	1.2	0.0	0.0
	Agriculture and food products	*100.0*	*100.0*	*100.0*	*46.7*	*0.4*	*1.3*	*0.5*
V	Mineral Products	40.6	52.5	52.5	23.3	0.0	0.0	23.2
VI	Chemicals	86.4	89.5	89.5	62.2	0.0	0.3	3.0
VII	Plastics and Rubbers	34.3	38.5	37.9	5.2	0.0	0.0	0.0
VIII	Hides, Skins and Leather and articles	98.6	100.0	100.0	13.3	0.0	0.0	0.0
IX	Wood and articles	100.0	100.0	100.0	75.6	0.0	0.0	0.0
X	Pulp, paper and paperboard	34.7	46.6	39.5	10.4	0.0	6.9	0.0
XI	Textiles	51.3	45.5	45.4	35.1	0.4	0.0	0.0
XII	Footwear	92.7	95.9	95.9	41.8	0.0	0.0	0.0
XIII	Articles of stone, ceramic and glasses	24.3	26.0	24.3	1.7	0.0	1.4	0.0
XIV	Pearls and precious jams	24.0	11.2	11.2	1.2	0.0	0.0	0.0
XV	Base metals and articles	27.9	24.5	24.5	3.2	0.0	0.8	0.0
XVI	Machinery and electrical equipment	95.3	100.0	62.7	66.8	0.0	0.0	0.0
XVII	Transport equipment	94.7	97.0	73.0	82.9	0.0	0.0	42.1
XVIII	Precision instruments	82.4	95.2	82.3	61.7	0.0	0.0	0.0
XIX	Arms and munitions	100.0	100.0	100.0	41.7	0.0	0.0	0.0
XX	Miscellaneous manufactured goods	86.9	92.9	92.4	40.6	0.0	0.0	0.0
	Manufactured goods	65.8	76.0	63.1	50.1	0.0	0.3	8.8
	Total	*70.5*	*77.8*	*65.8*	*49.9*	*0.0*	*0.4*	*8.2*

Source: TRAINS.

TABLE L
SELECTED PRODUCTS

HS6	Description	MERCOSUR total imports	MERCOSUR imports from EU15	MERCOSUR imports from EU25	Trade comple-mentarity MERCOSUR-EU15	Trade comple-mentarity MERCOSUR-EU25	Tariff imposed by MERCOSUR - simple average	Category in MERCOSUR offer
570231	Carpets of wool/fine animl hair,of wovn pile constructn,nt made up nes	469	197	197	1.4	1.7	23.0	E
610311	Mens/boys suits, of wool or fine animal hair, knitted	756	756	756	2.2	2.9	23.0	E
620421	Womens/girls ensembles, of wool or fine animal hair, not knitted	255	72	72	0.8	1.0	23.0	S
630240	Table linen, of textile knitted or crocheted materials	1,195	0	0	0.5	1.0	23.0	E
650300	Felt hats and other felt headgear	198	0	0	0.7	1.2	23.0	E
930330	Rifles, sporting, hunting or targetshooting, nes	936	90	211	1.4	1.8	23.0	S
930610	Cartridges f rivetg/sim tools/for captive-bolt humane killers incl pts	646	0	0	2.1	2.9	23.0	E
930621	Cartridges, shotgun	2,798	1,864	2,003	5.4	6.9	23.0	S
930630	Cartridges nes and parts thereof	5,683	2,006	2,163	3.7	4.7	23.0	S
841822	Refrigerators, household type, absorption-type, electrical	1,063	886	1,015	2.4	3.3	22.3	S
691110	Tableware and kitchenware of porcelain or china	11,298	1,428	1,463	0.9	1.2	21.3	E
160241	Hams and cuts thereof of swine prepared or preserved	11,223	2,230	2,230	0.8	1.6	21.0	S
190520	Gingerbread and the like	2,114	465	465	3.5	5.0	21.0	S
560741	Binder or baler twine, of polyethylene or polypropylene	760	149	149	1.1	1.8	21.0	S
650100	Hat-forms,hat bodies and hoods of felt; plateaux and manchons,of felt	279	20	20	0.9	4.2	21.0	E
701321	Drinking glasses other than glassceramics, of lead crystal	1,085	816	945	2.9	12.8	21.0	E
701329	Drinking glasses other than glassceramics nes	18,555	6,721	8,277	2.3	3.7	21.0	E
701331	Exhibit/kitchenware (ex drinkg glass) o/t glass-ceramics of lead crystal	591	187	576	1.1	12.4	21.0	E
701810	Glass beads,imitation pearls,imitatn precious/semi-precious stones etc	1,942	74	1,048	1.0	3.1	21.0	E
820120	Forks	97	97	97	0.8	1.0	21.0	E

TABLE L (continued)

HS6	Description	MERCOSUR total imports	MERCOSUR imports from EU15	MERCOSUR imports from EU25	Trade comple-mentarity MERCOSUR -EU15	Trade comple-mentarity MERCOSUR -EU25	Tariff imposed by MERCOSUR - simple average	Category in MERCOSUR offer
853931	Fluorescent lamps, hot cathode	86,071	17,695	20,131	3.8	6.9	21.0	E
920210	String musical instruments played with a bow	825	15	19	2.4	3.4	21.0	E
701391	Glassware nes of lead crystal (other than that of 70.10 or 70.18)	1,826	1,183	1,471	4.9	11.8	20.6	E
730439	Tubes,pipe & hollow profiles,I or nas,smls,of circ cross section,nes	8,634	3,403	3,869	0.8	1.0	19.5	S
481830	Tablecloths and serviettes, of paper	3,187	1,066	1,066	1.0	1.2	19.0	E
590110	Textile fabrics coatd with gum,of a kind usd for outer covers of books	749	125	125	5.2	7.2	19.0	E
730441	Tube,pipe&hollow profile,stain steel,smls,cd/cr of circ cross sect,nes	4,494	2,840	2,840	1.2	1.6	19.0	S
731910	Needles, sewing, darning or embroidery, iron or steel	506	167	254	2.2	3.2	19.0	E
701332	Exhibit/kitchenware (ex drinkg glass) o/t glass ceram coef <5 X 10-6 etc	3,922	579	675	2.6	4.2	18.6	E
160413	Sardines,sardinella&brislg o sprats prep o presvd,whole o pce ex mincd	9,750	1,375	1,375	0.8	1.5	18.3	E
210420	Homogenised composite food preparations put up for retail sale	1,798	281	281	0.8	1.3	18.3	E
540333	Yarn of cellulose acetate filaments, single, nes, not put up	6,579	2,498	2,498	1.2	1.7	18.3	S
853921	Filament lamps, tungsten halogen	20,327	11,154	11,390	2.5	3.2	18.3	E
853929	Filament lamps, excluding ultraviolet or infra-red lamps, nes	25,295	10,643	13,282	1.7	2.2	18.3	E
902830	Electricity supply, production and calibrating meters	18,545	2,352	4,802	1.8	2.3	17.4	E/D
850132	DC motors,DC generators,of an output exceedg 750 W but nt exceedg 75KW	13,119	2,478	2,511	3.1	4.1	17.3	E
200540	Peas prepard o preservd,oth than by vinegar o acetic acid,not frozen	3,995	1,881	1,881	1.8	4.7	17.0	S
200860	Cherries nes,o/w prep o presvd whether o not sugard,sweetend o spiritd	5,099	760	760	1.1	1.5	17.0	D

TABLE L (continued)

HS6	Description	MERCOSUR total imports	MERCOSUR imports from EU15	MERCOSUR imports from EU25	Trade complementarity MERCOSUR -EU15	Trade complementarity MERCOSUR -EU25	Tariff imposed by MERCOSUR - simple average	Category in MERCOSUR offer
210230	Baking powders, prepared	1,264	279	279	4.2	5.2	17.0	S
441840	Shuttering for concrete constructional work, of wood	418	418	418	0.6	2.4	17.0	E
721911	Flat rolld prod,stainless steel,hr,in coil,w>/=600mm,thk> 10mm	651	651	651	3.1	3.9	17.0	S
722840	Bars & rods, as, o/t stainless, not further worked than forged	2,954	1,463	1,463	1.9	2.6	17.0	S
722920	Wire of silico-manganese steel	4,283	615	615	0.9	1.2	17.0	S
730890	Structures&parts of structures,i/s (ex prefab bldgs of headg no.9406)	54,627	21,663	21,714	1.1	1.4	17.0	S
401310	Inner tubes of rubber for motor cars etc buses or lorries	20,986	382	4,965	3.0	7.1	16.8	E
391220	Cellulose nitrates (incl collodions)	4,333	2,454	2,454	4.8	6.9	16.5	S/D
210220	Yeasts, inactive and other dead singlecell micro-organisms	1,140	990	990	0.8	1.1	15.8	S
590290	Tire cord fabric made of viscose rayon high tenacity yarns	1,170	827	954	2.0	3.6	15.5	D
200520	Potatoes prepard or preserved,o/t by vinegar or acetic acid,not frozen	10,070	1,110	1,110	0.8	1.2	15.2	S
480620	Paper, greaseproof, in rolls or sheets	1,944	566	566	1.8	2.3	15.0	E
690590	Chimney-pots,cowls,chimney liners etc&oth ceramic constructional goods	269	226	226	2.3	3.5	15.0	D
701931	Mats of glass fibres	4,594	735	735	0.8	1.1	15.0	D
730230	Switch blades,crossing frogs,point rods & other crossing pieces,i or s	1,143	1,143	1,143	5.9	7.6	15.0	E
940600	Prefabricated buildings	21,624	12,395	12,564	1.2	1.7	14.8	E/D
721631	Sections,U,i/nas,nfw than hot rolld,drawn or extrudd,hght 80mm or more	8,955	658	7,683	1.1	1.9	14.8	S
293371	6-hexanelactam (epsilon-captolactam)	11,265	329	1,752	0.9	1.3	14.5	S
853221	Electrical capacitors, fixed, tantalum, nes	25,418	1,395	4,676	0.4	1.1	13.4	E/A
292390	Quarternary ammonium salts and hydroxides, nes	11,314	4,340	4,818	5.2	8.3	13.2	D/B

TABLE L (continued)

HS6	Description	MERCOSUR total imports	MERCOSUR imports from EU15	MERCOSUR imports from EU25	Trade comple-mentarity MERCOSUR-EU15	Trade comple-mentarity MERCOSUR-EU25	Tariff imposed by MERCOSUR - simple average	Category in MERCOSUR offer
721632	Sections,l,i/nas,nfw than hot rolld,drawn or extrudd,hght 80mm or more	11,160	1,126	10,287	1.5	3.0	13.1	S
30371	Sardines,sardinella,brislg or sprats,frozen ex hd No 03.04,livers&roes	25,540	530	530	14.9	20.3	13.0	C
110813	Potato starch	1,860	1,837	1,837	18.6	42.0	13.0	S
110900	Wheat gluten, whether or not dried	10,394	8,957	9,067	13.9	18.3	13.0	S
280620	Chlorosulphuric acid	65	0	0	0.0	1.2	13.0	C
282630	Sodium hexafluoroaluminate (synthetic cryolite)	1,004	361	486	7.0	10.6	13.0	C
283523	Trisodium phosphate	399	319	319	3.6	4.6	13.0	E
284140	Potassium dichromate	208	123	181	7.1	19.0	13.0	na
441131	Fibreboard >0.35 g/cm2 <0.5 g/cm2 not worked or surface covered	171	0	0	0.8	1.0	13.0	D
700320	Cast glass sheets wired	295	129	167	1.4	6.6	13.0	C
701010	Ampoules of glass conveyance or packing	1,535	1,194	1,194	6.2	9.6	13.0	C
300440	Alkaloids or their derives, not cntg antibiotics or hormones, in dosage	38,128	11,198	11,310	6.0	7.8	12.7	S/A
730810	Bridges and bridge sections, iron or steel	691	618	618	0.9	1.2	12.5	E
291631	Benzoic acid, its salts and esters	10,391	3,169	3,691	8.0	13.0	12.1	S/B
292141	Aniline and its salts	3,044	1,849	1,882	0.8	1.5	12.1	S
401191	Pneumatic tires new of rubber nes,having a 'herring-bone' or sim tread	36,205	9,346	9,550	1.7	2.4	12.0	E/B
320190	Tanng extracts of veg orig,nes;tannins&thr salts,ethers,esters&derivs	3,389	1,890	1,999	12.9	18.0	11.4	C/B
840290	Parts of steam or vapour generating boilers nes	18,446	16,826	16,826	2.6	3.7	11.3	D
844833	Spindles,spindle flyers,spinng rings & rg travellers for hdg No 84.45	2,842	1,428	1,428	10.6	14.6	11.2	E/D
841011	Hydraulic turbines & water wheels of a power not exceeding 1000 KW	217	187	187	3.0	4.2	11.1	E
843840	Brewery machinery	1,782	1,677	1,677	18.3	23.9	11.1	D
845819	Horizontal lathes nes for removing metal	3,604	1,012	1,024	0.8	1.1	11.1	E/D

TABLE L (continued)

HS6	Description	MERCOSUR total imports	MERCOSUR imports from EU15	MERCOSUR imports from EU25	Trade comple-mentarity MERCOSUR -EU15	Trade comple-mentarity MERCOSUR -EU25	Tariff imposed by MERCOSUR - simple average	Category in MERCOSUR offer
845931	Boring-milling mches nes, numerically controlled for removing metal	2,311	1,522	1,641	1.3	2.0	11.1	D
845940	Boring machines nes for removing metal	1,790	1,398	1,398	2.4	3.2	11.1	D
846031	Sharpening (tool or cutter grinding) mach n/c for removing metal	4,914	2,830	2,830	5.9	7.6	11.1	E
860290	Rail locomotives nes and locomotive tenders	346	110	110	0.8	1.1	11.1	E
860310	Self-propelld railway cars powerd from external source of electricity	29,270	40	19,099	24.0	30.1	11.1	E
890600	Warships, lifeboats, hospital ships and vessels nes	6,348	607	607	0.9	1.3	11.1	D
680610	Slag wool, rock wool & similar mineral wools in bulk, sheets or rolls	3,156	1,507	1,524	1.1	1.5	11.0	S
680800	Panels,board etc of veg fib,straw etc agglomeratd w/cement etc binders	620	211	211	1.0	1.5	11.0	C
847810	Machinery for preparing or making up tobacco nes	20,802	13,354	13,354	46.4	60.8	11.0	D
890200	Fishing vessels and factory ships	13,783	2,323	2,323	3.5	5.1	10.9	D
121020	Hop cones, ground, powdered or pelleted and lupulin	9,424	1,690	2,013	25.3	56.6	10.1	C
291711	Oxalic acid, its salts and esters	806	132	132	0.8	1.1	10.0	D/B
730210	Rails, iron or steel	45,424	13,510	39,528	13.1	23.9	10.0	D/B
292151	O-,M-,P-phenylenediamine, diaminotoluenes&thr derivatives;salts thereof	22,842	8,707	10,003	6.8	9.8	9.5	S
292130	Cyclanic, cyclenic/ cycloterpenic mono- /polyamines & derivs; salts thereof	2,615	1,025	1,137	3.3	5.1	9.3	S/B
281511	Sodium hydroxide (caustic soda) solid	6,471	1,043	1,355	2.4	3.2	9.2	S
20900	Pig fat lean meat free & poultry fat unrenderd, frsh, chilld, frozn or curd	7,445	2,009	2,009	6.8	9.1	9.0	C
720292	Ferro-vanadium	7,752	2,517	2,643	3.1	4.5	9.0	E
310210	Urea,wthr/nt in aqueous solution in packages weigh more than 10 kg	148,752	6,678	9,531	0.8	1.1	7.7	S
700232	Tubes of glass linear coef of exp </=5X10-6 per Kelvin within 0C-300C	2,034	1,878	1,878	19.6	28.6	7.0	C

TABLE L (continued)

HS6	Description	MERCOSUR total imports	MERCOSUR imports from EU15	MERCOSUR imports from EU25	Trade comple-mentarity MERCOSUR -EU15	Trade comple-mentarity MERCOSUR -EU25	Tariff imposed by MERCOSUR - simple average	Category in MERCOSUR offer
310221	Ammonium sulphate, in packages weighing more than 10 kg	119,742	31,867	55,353	26.0	42.8	6.5	E
293960	Rye ergot alkaloids and their derivatives, in bulk; salts thereof	10,198	2,343	4,788	5.4	9.6	5.2	D/B
281810	Artificial corundum	6,565	1,033	1,033	1.0	1.4	5.0	B
284030	Peroxoborates (perborates) of metals	11,583	11,375	11,375	89.6	204.8	5.0	B
284160	Manganites, manganates and permanganates of metals	614	0	0	1.3	2.7	5.0	B
290316	1,2-dichloropropane (propylene dichloride) and dichlorobutanes	993	0	0	51.4	84.1	5.0	na
290714	Xylenols and their salts	259	214	214	5.1	6.7	5.0	B
290715	Naphthols and their salts	908	342	502	0.8	1.2	5.0	B
291030	1-chloro-2,3-epoxypropane(epichlorohydrin)	12,733	2,081	2,135	9.2	14.2	5.0	B
291422	Cyclohexanone and methylcyclohexanones	2,493	913	913	3.5	5.8	5.0	B
293351	Malonylurea (barbituric acid) and its derivatives; salts thereof	1,140	262	765	9.8	15.5	5.0	B
293940	Ephedrines and their salts, in bulk	1,688	913	925	4.2	5.7	5.0	B
250310	Sulphur, crude or unrefined	77,130	2,493	6,985	2.8	4.1	3.0	A
310229	Ammonium sulphate/nitrate mixtures/double salts in pack weighg > 10 kg	1,382	962	1,334	3.0	3.8	3.0	A
310230	Ammonium nitrate,whether or not in aqeuous sol in pack weighg > 10 kg	36,988	2,863	3,693	2.7	3.3	3.0	A
271016	Petroleum oils, o/ than crude	597,704	11,692	13,568	1.9	2.8	1.5	na
844711	Circular knitting machines with cylinder diameter not exceeding 165 mm	9,811	8,832	9,505	24.0	30.1	0.8	A
844851	Sinkers,needle&oth articles usd in form stitches as pts of hdg No 8447	11,858	10,603	10,645	25.0	32.5	0.8	A
120919	Seeds, beet, for sowing nes	912	75	75	16.6	27.2	0.0	na
270119	Coal nes, whether or not pulverised but not agglomerated	508,577	0	11,641	0.4	1.3	0.0	A
270400	Coke&semi-coke of coal, lignite o peat, agglomeratd o not, retort carbon	126,832	10,857	16,435	0.6	1.5	0.0	A
270810	Pitch	23,182	18,648	20,671	21.2	36.9	0.0	A

VI. RESULTS: COMPUTABLE GENERAL EQUILIBRIUM ANALYSIS

A. Brief Description of the Model

The model used follows the lines in Flôres [1997], being very close to the one in Flôres [2003b]. It is a static CGE model in which strategic interaction takes place in certain sectors. Contrary to the common practice of introducing *ad hoc* "scale gains" in an otherwise perfect competition framework, perfect and (explicitly) imperfect competition sectors interact in the model. This approach[61] was fashioned in Gasiorek *et al.* [1992], who used it to evaluate the impacts of the *Europe 92* Delors's initiative. In general, due to the scale effects - enhanced in the larger markets created by either the regional integrations or the free-trade agreements -, welfare gains are higher than those produced by the perfect competition alternatives (see Baldwin and Venables [1995] and Flôres [1996]).

Initiatives like the EU aim at the creation of an *integrated market* where price arbitrage by producers becomes impossible or, at least, much more difficult. In the EU-MERCOSUR FTA, the two blocs, as markets, remain *segmented*: what is at stake is the creation of a free-trade area and *not* a common market. This means that the model solutions, for the imperfect competition sectors, keep the segmented markets hypothesis.

Another important methodological point is that, beyond tariffs, Flôres [1997] and Gasiorek *et al.* [1992] assumed the existence of additional trade frictions which can be associated to a variety of factors impairing or raising the cost of trade, like transportation, bureaucracy, distribution costs, etc. Integration - or encompassing FTAs - zeroes the tariffs and reduces these latter costs without necessarily eliminating them. In the present exercise, no evaluation was made of these other barriers to trade. So, in our free-trade scenario, when tariffs are abolished, *all* trade costs are set to zero. This is somewhat unrealistic, as there exist additional cost factors between the two blocs, which may still play an important role *after* tariffs have been eliminated. Nevertheless, consideration of a reliable set of values for such variable, even given the regions adopted (see below), amounted to a sizeable extra work, hard to be completed within the present deadlines. In order not to make MERCOSUR "too close" to the EU25, the simple way we used to keep some trade cost differential was never have a zero cost MERCOSUR export to the EU25, or vice versa; a minimum rate of 0.6 percent being applied on all bilateral "free-trade flows".

Imperfect competition sectors play a Cournot-Nash strategy in each market/region, a key parameter being the perceived elasticity of demand in region *i*, for product *j*, when manufactured in region *i'*, *e(i',i; j)*, which is defined as:

$$e(i',i; j)^{-1} = \sigma(i;j)^{-1} + (1 - \sigma(i;j)^{-1}) s(i',i; j)$$

where $\sigma(i;j)$ is the elasticity of substitution, in region *i*, between goods *j* from different origins and *s(i',i; j)* is region's *i'* market share for product *j*, in region *i*. The substitution elasticity $\sigma(i;j)$, a parameter associated to each pair region/sector of the model, is, therefore, an Armington-type elasticity.

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[61] Pioneered in a partial equilibrium setting by Alasdair Smith and Anthony Venables.

Introducing imperfect competition in the way done here allows for two interesting kinds of results. The first is that *short* and *long run* solutions are possible. In the former, the (equivalent) number of firms in each imperfect competition sector is kept constant, so that profits can be different from zero in these sectors.[62] In the latter, profits are imposed to be zero, and the number of firms is adjusted to satisfy this condition. A first consequence of this is that one is able to check whether, *in the long run,* a contraction or expansion takes place in the sector. A second and very interesting one is that the sectoral welfare gain - always under the *long run* solution - can be decomposed into six categories related to the joint effect of liberalisation and higher competitiveness. These categories are:

- *direct* - accounts for the part of welfare accrued by having, thanks to liberalisation, access to the goods at a better price;

- *competitiveness* - this is the true imperfect competition effect, due to strategic interaction among more competitive producers in the enlarged FTA space. Unfortunately, under an incomplete liberalisation scenario for the EU-MERCOSUR FTA (the "realistic" one, see below), this effect is less meaningful;

- *variety* - the model works with an equivalent number of firms, which also serves as a proxy for the variety of goods supplied. In the long run, the number of firms can increase or decrease, having an impact on welfare;

- *diversion* - to be understood here as resulting from a change in the origin of flows, from non-members to members, now more competitive or lower-priced, *thanks to the FTA*. As known, preferential agreements can cause trade diversion and this component is related to such classical concept; though not entirely, as the new suppliers can be either more or less efficient than the former ones;[63]

- *ToT X* and *ToT M* - these two categories identify changes in sectoral terms of trade, decomposed into exports and imports. If *ToT X* is negative, part of the efficiency gain was exported in the (now) lower-priced goods. If *ToT M* is positive, the region succeeded in gaining welfare from its foreign exporters.

Apart from the above considerations, the structure of the model is fairly standard:

i)   in the demand side there is a representative consumer with a Dixit-Stiglitz-Spence CES utility function, in an Armington-like tree structure;

ii)   in the production side, perfect competition sectors have Cobb-Douglas technologies;

iii) intermediate inputs are treated via a shortcut using the input-output (I-O) coefficients;

iv)   wages are flexible, as labour is assumed mobile among sectors, but the (sector specific) capital remuneration rates are kept constant;

v)   here is no money in the model and, in equilibrium, exports equal imports and the usual closures apply.

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[62]   Short run solutions have not been computed in this exercise.

[63]   In classical, Vinerian terms, this category includes both *trade creation* and *diversion.*

An innovation was however introduced, in the treatment of prices in the agricultural sectors in the EU15 and EU25 regions, following the idea in van Meijl and van Togeren [2002]. Basically this amounts to modelling the market price in these regions as a convex combination of the CAP intervention price and the threshold price; the weight of the combination being a function of the EU excess domestic supply (see also Guyomard *et al.* [1993], Surry [1992] and Von Lampe [1999]).[64] This mechanism - which better portrays the functioning of the CAP in a CGE context - was used in the agriculture IIa and agriculture IIb sectors (defined below) and, in spite of the aggregate level of the model, proved binding in both.

Calibration is rather delicate. Linear to cubic cost functions are used for the imperfect competition sectors, to add more flexibility to this key operation.

- The economies were decomposed into 15 sectors, namely:

- agriculture I: agribusiness (except dairy products);

- agriculture IIa: commodities, except wheat, cereals and related, non-specified produce;

- agriculture IIb: wheat, cereals and related, non-specified produce;

- dairy products;

- shoes and leather;

- non-metallic minerals (commodities and products);

- steel industry I: non-ferrous;

- steel industry II: ferrous;

- textiles and clothing;

- automotive I (cars and trucks, as well as parts);

- automotive II (planes and other, specialised vehicles for different purposes);

- machinery and other equipment;

- electronic equipment;

- chemicals (including rubber and plastic products);

- other products and services.

These sectors represent an improvement upon those in Flôres [2003b] and try to take into better account the particular features of the MERCOSUR-10AC trade dynamics. It must be noticed that services are not explicitly included in the model,[65] due to personal views on how to treat, or rather, not to treat them in this kind of CGE structure. Moreover, in spite of the arguments in

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[64] We remind that: *the intervention price* is the minimum price imposed (by the CAP policy) in the domestic EU market; *the threshold price* is a price set for imports (also by the CAP), high enough to discourage them. Threshold prices were secured by variable import duties; though both were theoretically abolished by the URAA (see Section III), the EC kept them somehow by fixing at their level the new, bound tariffs.

[65] They play a rather passive role, their flows (in sector 15) being modified only through the I-O linkages.

Garay and Estevadeordal [1996] and Brenton and Manchin [2002], no detailed treatment of rules of origin, as for instance in Gasiorek *et al.* [2001], was included in the model.[66]

Automotive I and II, chemicals, machines, electronic equipment and the two steel industry sectors, as well as agriculture I (agribusiness), are modelled under imperfect competition.[67] Due to data constraints, their behaviour is better portrayed in the model regions related to the MERCOSUR countries, the US and the EU15 or 25 (see below).

B. Regions and Data

The regionalization adopted is a crucial element for the interpretation of the final results. Decisions concerning the model regions must face one of the most classical dilemmas in CGE practice: due attention to the areas of concern (and those which affect them) allied to care in not fragmenting too much the model.[68] In our case, given the interest in analysing different scenarios from a MERCOSUR perspective, we divided the world into the following 7 (or 8) regions:

- MERCOSUR (Argentina, Brazil, Paraguay and Uruguay);

- Chile + the Andean Community (Bolivia, Colombia, Ecuador, Peru and Venezuela);

- US + Canada;

- the Rest of the Americas - RoA ;

- the EU25 countries which will be considered in two ways: one region, comprising the enlarged EU25, or two regions, comprising the EU15 and, separately, the 10 accession countries (10AC), the latter with the existing protection structure;

- Japan, and;

- the Rest of the World - RoW.

In order to have a minimum compatibility among the different exercises in this project, trade flows among the regions in the model were computed from the *pctas* data file and refer to 2000. A basic data source for building up the structure of each region was the GTAP database, referring to the 2000 year, adapted to the regions and particular features of the present model, along the lines described in Flôres [2003b]. As an example, I-O matrices for Brazil and Argentina, which feature in rather old versions in GTAP, were used in their latest available versions. Also, Armington elasticities came from special sources for these two countries.

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[66] As it would amount to further programming, unable to meet the project deadlines. The authors hope to pursue this in a near future. A (quasi-) educated guess on the effect of including them in this exercise is that the results would turn out more favourable to MERCOSUR, but this needs confirmation.

[67] So that 8 out of 15 sectors are under imperfect competition. Modelling the agribusiness under imperfect competition seems a must; though this is the first time we do it. Textiles and clothing, which in Flôres [2003b] was also in this category, has now been considered, in MERCOSUR, as a perfect competition sector.

[68] A model with too many regions of different sizes, among other practical problems, may add distortions to the model global structure.

As regards the quality of the data adaptation to these regions, the best ones seem to be those for MERCOSUR, the US+Canada, the EU15, the 10 candidates and Japan. The Rest of the Americas is naturally a simplification; flows to the Rest of the World are taken by difference and econometric techniques. In this last region, there are countries that may be relevant for certain sectors, like Australia and New Zealand, or the (former) New Tigers; not to mention certain Asian economies, like China or Vietnam, which are becoming competitive either in specific agricultural goods or in traditional sectors like textiles. However, due consideration to them would make for another project.

Information on the complete protection structure is debatable, even if one sticks to the case of tariffs. Preferential tariffs - specially those originating from trade agreements - are poorly depicted in GTAP and had to be thoroughly reviewed in cases like MERCOSUR. Given the importance of the US and the EU15 in the model, improvements on their protection structure were made with the aid of information from the United States International Trade Commission - USITC website and Messerlin [2001], respectively, as well as the TRAINS software[69] and OECD [2002]. Data from INTAL/ALADI, and recent studies conducted by IPEA in Brazil were also useful complementary sources.

At the level of detail of the present study many nuances and, sometimes, important tariff peaks either disappear or are smoothed out when aggregated to produce a single figure for the sector. Moreover, combining the regionalisation adopted with the already few sectors in the model makes the protection structure of certain regions sometimes a fairly rough approximation of reality. As an example, Chile, beyond its low tariff structure, has an FTA with the EU15, another with the US and preferential tariffs with MERCOSUR, but it is bunched together with the reasonable diversity (as regards protection) of the Andean countries.

C.   The Scenarios

Due to the uncertainties still surrounding the final terms of the EU-MERCOSUR FTA, we were obliged to assume certain possibilities when constructing the scenarios. These relate only to the triad MERCOSUR-EU15-10AC and do not take into account possible outcomes from either the present WTO Round or the ongoing regional integration agreements in the American continent; the *status quo* as regards both, being frozen in the base-year situation.

Out of the multiple basic options on the table - which may be translated into different ways as well as combined in several forms - we worked with two basic outcomes, one optimistic and the other less so (or perhaps, more realistic). The main difference between both, as could be expected, lies in the way agriculture is liberalised. Roughly speaking, as regards the 10AC-MERCOSUR flows, the possibilities of the former are in the more traditional manufacturing sectors, while the latter, though not without potentialities in these sectors, has considerable scope for agricultural gains. This, as confirmed by the results, makes for the main differences between the scenarios outcomes to lie in the market access gains/losses that MERCOSUR experiences in the enlarged EU space. In order to answer the questions posed by the project, the scenarios are always evaluated under the two regionalizations adopted: one with the EU15 separated from the 10AC and another with a single EU25 bloc. In the first one, once the FTA is established the "regions" EU15 and 10AC

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[69]   See also the related discussion in Section V.

keep the mutual barriers prevailing in the base year. The impact of the enlargement is revealed by systematically contrasting results for both cases.

The two scenarios are:

- *Scenarios A* (full liberalization). In this scenario there is full trade liberalization between the two blocs, i.e., MERCOSUR and either the EU15 or the EU25, comprising even those goods which, at present, are set aside in the offers of both blocs. In the case of agriculture, we allowed for two possibilities. Zero tariffs are applied either for those goods whose imports are unrestricted or within the quota, in the case of those under the TRQ regime, making for scenario A1; or a bit more, with the quotas themselves, in agriculture I, being expanded in 65 percent, making for scenario A2.[70] Over quota tariffs, in TRQs, are reduced only in 10 percent, in both cases. Thus, even in this optimistic view, we don't assume a drastic quantitative change in the TRQ quotas, given the controversial state of this debate in the negotiations. Additionally, agricultural subsidies are not lowered (see also the remark below).

- *Scenario B* (the "realistic" scenario). Here, the FTA between the two blocs (i.e., MERCOSUR and either the EU15 or the EU25) is implemented in the following way: In the case of agriculture, zero tariffs are applied only to those goods in categories A-D *of the last official EU offer* (see Section V, point A). This leaves out of free trade many key goods for MERCOSUR, which are in category E and under TRQs; for these, tariffs - in or over quota - are reduced only in 10 percent. As regards manufactures, there is free trade but for those in the union of the sets of unassigned goods in the two offers.

It must be pointed out that, though considering the EU25 bloc substantially avoids the problem of treating how trade, specially agricultural, will be fully liberalized between EU15 and 10AC (the model assumes *it is*), there still remains a decision on how agricultural subsidies will be implemented in the enlarged union. We have adopted a decision that is becoming standard in this type of exercise: we have moved subsidies to the 2006 levels of the Copenhagen agreement (see Table 12).

D. Results

Main Findings

Tables 22 to 28 are a selection of the most interesting results. All deserve careful analysis and will be briefly discussed below. It is worth reminding - specially given the previous remarks on the data-base and the aggregate level of the study - that the figures in the tables should be evaluated in relation to each other *and not taken separately, as a single, precise value.* The importance of this CGE exercise is to identify areas or situations - or rather sectors and scenarios - where things

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[70] This supplementary scenario was added after the June 21 presentation, given the interest it aroused. We have included a modest set of results for it, though enough to show its importance, as expected.

go better *or* worse. Detailed quantification of profits or losses should be made at a greater level of detail,[71] ultimately with the aid of a partial equilibrium model.[72]

Table 22 shows the aggregate results, in terms of welfare GDP and wages, for the four combinations. Globally, under free trade between the two blocs, the enlargement has a slight positive impact on the agreement, increasing by up to 0.2 percentage points its effects on output. Its role is a little more important in the case of the imperfect FTA, signalling that, at this global level, the enlargement opens up opportunities for MERCOSUR. Notice that GDP, rather than wages, is more sensible to the move from the optimistic scenarios to the realistic one. More generous quotas (A2) have a clear impact on welfare.

TABLE 22
GLOBAL RESULTS FOR MERCOSUR. CHANGES IN GDP AND WAGES (%) FOR ALL SCENARIOS

Scenarios	GDP		Wages	
	EU15	EU25	EU15	EU25
A1 - "optimistic"	1.3	1.5	1.4	1.4
A2 - "optimistic"	1.5	1.6	1.4	1.5
B - "realistic"	0.8	1.1	1.2	1.3

The above figures must be complemented by the investigation of what takes place at the disaggregate level. Tables 23a, 23b and 24 describe the changes in trade flows (exports and imports) under the cases studied. The highest increases for exports, in both scenarios A1 and B, are in the commodities (AIIa), shoes & leather, textiles & clothing and steel II (ferrous) sectors. There are also noticeable increases in agribusiness (AI), wheat & cereals (AIIb), steel I (non-ferrous), and auto II (other vehicles). Roughly, results for the enlarged Union are either enhanced or remain the same. The "biggest falls" - though still modest - are in shoes & leather, steel II and auto I (cars), where there is indication that the 10AC will constrain the MERCOSUR export expansion due to the agreement. It is also important to highlight that, under the full liberalization scenario, chemical exports *decrease* (more even with the EU25).

The imperfect FTA doesn't change much the relative pattern between the results for the two European blocs. Only as a data summarising technique, linear regressions were run on the sets of results for each scenario, giving fairly similar relationships:

For scenario A1: eu25 = - 0.185 + 1.019 eu15

For scenario B: eu25 = - 0.283 + 1.036 eu15;

where eu25 and eu15 are the respective export changes for a given sector. Though the correlation between each pair of results is high - signalling that the overall effect of the enlargement is *roughly linear along the sectors*, actual EU25 figures can either be higher or lower than the corresponding EU15 ones.

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[71] Given all the methodological caveats already mentioned we decided not to translate the results into monetary values, something that could easily be misleading.

[72] Section V, as explained, is an example of a (global) partial equilibrium exercise.

MERCOSUR: TOTAL TRADE FLOWS CHANGES (LONG RUN RESULTS) - EXPORTS
Scenarios A1 and B

Sectors	Scenario A1		Scenario B	
	EU15	**EU25**	**EU15**	**EU25**
AI: agribusiness	6.0	7.5	3.0	4.0
AIIa: commodities	8.0	9.0	5.8	7.2
AIIb: wheat & cereals	6.1	6.5	4.0	4.0
Dairy	1.3	1.3	1.2	1.2
Shoes & leather	20.8	19.8	20.8	19.9
Text. & clothing	14.3	14.2	13.3	13.0
Non-met. Minerals	2.8	3.5	2.9	3.3
Steel I: non-ferrous	6.5	6.1	5.0	5.0
Steel II: ferrous	7.5	7.0	6.5	6.0
Machines	3.8	3.9	2.1	2.0
Electronic equip.	0.6	0.4	0.6	0.5
Cars	2.5	2.0	1.8	2.0
Other vehicles	6.2	6.3	4.7	5.3
Chemicals	-0.2	-0.5	0.0	-0.2
Other	1.2	1.5	1.2	1.3

Similar results for scenario A2 are not shown, as they, en general, differ little from those for A1. The single strong discrepancy is in the agribusiness, as shown in Table 23b.

TABLE 23B
MERCOSUR: TOTAL TRADE FLOWS CHANGES (LONG RUN RESULTS) - AGRIBUSINESS EXPORTS
Scenarios A1 and A2

Sectors	Scenario A1		Scenario A2	
	EU15	**EU25**	**EU15**	**EU25**
AI: agribusiness	6.0	7.5	7.8	8.0

The picture in Table 24 attenuates, to some extent, the pattern in the previous tables. With the FTA, MERCOSUR imports increase less than its exports, specially under full liberalization. Apparently, a full FTA creates more opportunities for MERCOSUR than for the Union. However, it is worth noticing that imports of steel I and II, machines, electronics, auto I and II and chemicals have significant increases; all these being sectors of high value added. The impact of the enlargement is - perhaps obviously - less relevant. But, it is again worth noticing that imports of steel II and chemicals have reasonable increases, under both scenarios, and cars also under scenario A1, showing that the 10AC *gain* market share in these sectors, in MERCOSUR. The "realistic" scenario, more than reducing (the not very big) penetration in the agricultural sectors, implies losses in the three just mentioned sectors (and also, to some extent, in the electronic equipment

one). Low or practically negligible[73] increases are found in dairy, shoes & leather and non-metallic minerals. Again, the imperfect FTA keeps the close relationship between the two vectors of changes.

TABLE 24
MERCOSUR: TOTAL TRADE FLOWS CHANGES (LONG RUN RESULTS) - IMPORTS
Scenarios A1 and B

Sectors	Scenario A1		Scenario B	
	EU15	EU25	EU15	EU25
AI: agribusiness	2.5	2.5	1.8	1.8
AIIa: commodities	0.9	0.9	0.3	0.5
AIIb: wheat & cereals	0.7	0.5	0.6	0.6
Dairy	0.4	0.4	0.2	0.3
Shoes & leather	0.0	0.0	0.0	-0.1
Text. & clothing	5.3	5.4	5.3	5.3
Non-met. Minerals	0.0	0.2	0.0	0.0
Steel I: non-ferrous	5.0	5.2	5.0	5.2
Steel II: ferrous	6.0	7.0	3.5	5.5
Machines	4.2	5.0	4.0	5.0
Electronic equip.	3.5	2.8	1.5	2.0
Cars	3.0	3.8	2.0	2.2
Other vehicles	4.5	5.0	4.3	5.0
Chemicals	12.1	14.5	8.4	9.0
Other	2.2	2.3	2.0	2.0

TABLE 25
MERCOSUR: OUTPUT CHANGES (LONG RUN RESULTS)
Scenarios A1 and B

Sectors	Scenario A1		Scenario B	
	EU15	EU25	EU15	EU25
AI: agribusiness	3.1	3.6	2.4	2.9
AIIa: commodities	4.8	5.3	4.1	4.4
AIIb: wheat & cereals	2.6	2.7	2.0	2.2
Dairy	1.2	1.2	0.8	0.9
Shoes & leather	11.5	10.8	10.0	10.2
Text. & clothing	6.2	6.7	6.1	6.5
Non-met. Minerals	1.5	1.6	1.4	1.5
Steel I: non-ferrous	1.3	1.4	1.0	1.2
Steel II: ferrous	2.1	2.3	1.2	1.3
Machines	1.5	1.8	1.4	1.6
Electronic equip.	-2.1	-2.5	-1.5	-2.1
Cars	0.2	-0.6	0.1	-0.1
Other vehicles	2.3	2.5	2.0	2.1
Chemicals	0.1	-0.2	0.0	-0.0
Other	0.5	0.6	0.5	0.5

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[73] The reader should keep in mind that the precision of the present study is in the first decimal; a "0.0" can mean either a small increase or a small decrease (given by the second decimal).

Table 25 shows the changes in output for the same four scenarios. Though it broadly confirms the pattern revealed in the two previous Tables, new insights pop up. The FTA will (always) reduce output in electronic equipment, and (slightly) in the cars and chemicals sectors. In both, reduction takes place when considering the EU25 scenarios, clearly showing the market loss due to the 10AC. Of course, "creative destruction" is more drastic under scenario A1.

For all other sectors, but two exceptions, the enlarged market is beneficial to MERCOSUR, even if sometimes at modest increases of 0.1. The exceptions are dairy, where under the full FTA there is no change, and - the most interesting - shoes & leather where the competitiveness of the 10AC[74] *reduces* MERCOSUR output under free trade and the EU25. Undoubtedly, the cars result raises a flag as regards this (controversial) sector in MERCOSUR.

It is enlightening at this point to re-stress the links of the previous results to those in Section V. It must always be kept in mind the great difference in aggregation level between the two exercises: the main responsible for the apparent differences. A good example of this lies in the three agricultural sectors, all gaining if the EU25 is considered, though the partial equilibrium computations identified a few threats (subsumed in the aggregation performed). The CGE exercise confirmed the findings for shoes & leather, textiles & clothing, the steel sectors, machines and, dramatically, chemicals. For some of them, aggregate output still manages to increase (Table 37), as in machines and textiles & clothing, certainly thanks to the reallocation of flows, due to global efficiency gains.

The most surprising case is cars, where a consistently negative impact of the 10AC appears. However, close inspection of the tables in Section V - as, for instance, Table B (Annex), in its Annex - reveals that these goods had a borderline position. Again, the competitive reallocations determined by the general equilibrium logic showed up now a global threat. In spite of naturally demanding deeper investigation, this signal must by all means be taken seriously.

A Deeper Look on Welfare and Adjustment

Changes in trade flows and output have no clear, unidirectional relation with what happens to welfare - the ultimate goal of any CGE evaluation. As explained in Section A, our approach allows a detailed analysis of what happens, in terms of welfare, with the imperfect competition sectors. Table 38 presents the very important breakdown of the total welfare gain in each of these sectors into the six categories previously described.

The startling point in the welfare decomposition is the high share usually obtained by the *direct* effect. When facing the more powerful and diversified EU economy, MERCOSUR, though improving somewhat the efficiency of its advanced industrial sectors, actually increases its welfare more through access to lower-priced goods than by domestically delivering such goods. The only exceptions are the agribusiness and auto II (other vehicles) sectors, where the *competitiveness* effect dominates the *direct* one. Figures are also close by for the two steel sectors,

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[74]   Confirming Section V findings.

showing an approximate technological match[75] between the two blocs. Things definitely lag behind in chemicals and - a bit surprisingly - in the auto I (cars) sectors, where perhaps (direct) welfare would result from access to less expensive sophisticated parts. This explanation, however, demands a sharper verification.

Taking the *competitiveness* share as a proxy for a measure of higher sector efficiency, one sees that there isn't much difference from the EU15 to the EU25 cases. This confirms the usual statement that, taken globally, the enlarged EU doesn't stand as a significantly more competitive player to the outside, though it so becomes in selected (sub)sectors. Getting down to a little more detail, one sees that MERCOSUR's competitiveness-enhancing challenges, from the enlargement, lie in machines, cars and chemicals, sectors that consequently demand closer attention in the agreement.

The above analysis must be complemented by looking at the figures in the variety column. There are sensible decreases in the number of chemical varieties/firms and in those of electronics, as well as contractions in the machines and auto I sectors. These lower contractions signal, on the one hand, that there will perhaps be less technical changes in the respective industries, and, on the other hand, as said above, that these changes will be beneficial in terms of upgrading the sectors.

TABLE 26
MERCOSUR - BREAKDOWN OF WELFARE GAINS FOR THE IMPERFECT COMPETITION SECTORS (LONG RUN RESULTS)
Scenario A

	Direct	Compet.	Variety	Diversion	ToT X	ToT M
Scenario A: MERCOSUR-EU15						
Agribus.	42.2	53.5	0.2	6.0	-2.0	0.1
Steel I	44.5	44.3	1.7	10.0	-1.5	1.0
Steel II	46.4	45.8	0.2	8.5	-1.2	0.3
Machines	50.4	39.1	-1.0	10.9	-0.2	0.8
Cars	44.5	40.3	-2.5	18.2	-0.8	0.3
O. vehic.	38.0	46.7	0.2	17.1	-2.5	0.5
Elec. eq.	44.1	30.2	-4.0	30.1	-1.7	1.3
Chem.	45.2	26.8	-6.7	34.5	-1.1	1.3
Scenario A: MERCOSUR-EU25						
Agribus.	42.8	54.9	0.2	4.5	-2.6	0.2
Steel I	54.9	39.2	1.2	5.3	-0.8	0.2
Steel II	46.6	45.7	0.1	8.5	-1.2	0.3
Machines	50.5	42.4	-1.0	8.8	-1.1	0.4
Cars	45.7	40.6	-2.6	16.7	-0.6	0.2
O. vehic.	42.6	45.5	0.3	13.5	-2.7	0.8
Elec. eq.	44.3	32.1	-4.1	28.2	-1.8	1.2
Chem.	50.1	25.7	-5.2	29.4	-1.3	1.3

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[75] Or complementarity, given the aggregate level of the sectors in the model.

In the first steel sector, thanks to a certain complementarity between its products and the EU ones, there are signals that MERCOSUR will be able to face the fiercer competition, even expanding the number of plants by nearly 2 percent, without the enlargement. This figure falls to 1.2 in the EU25 case, when the competitive Eastern European producers enter in the preferential agreement. It is also interesting to see the mature status of the agribusiness and auto II sectors, where the change in the number of units is minimal. A negligible change also takes place in the less competitive steel II sector.

The agreement doesn't create much trade diversion, the highest figures in this column coming from auto I, electronic equipment and chemicals, indicating a certain drop in the market shares of more competitive Asian (auto I and electronics) and US producers (electronics and chemicals).[76]

Finally, in nearly all cases the algebraic sum of the two terms of trade is negative, the country exporting a small fraction of its efficiency gains, as expected.

This set of results may be interpreted as showing that the imperfect competition sectors, still "protected" in both blocs by the segmented markets characteristic of the FTA, were able - *at the aggregate level of this model* - to practice a kind of reciprocal dumping (*à la* Brander and Krugman [1983]), what partially "saved" them from more drastic outcomes. This accounts for obtaining not very dramatic results as regards output and exports changes, decreases in these quantities being relatively few. The same pattern appeared in Flôres [2003b], taking only Brazil (and in comparison, for instance, to a carefully conducted study like Harrison *et al.* [2002]).

Another important summary is in Table 27, where global changes in terms of trade are presented. The old terms-of-trade argument for a tariff has been recently recast[77] by Bagwell and Staiger [1999, 2001], to explain the willingness for trade agreements among nations and the existence of institutions like the WTO. Agreements solve a Prisoner's Dilemma in tariff setting, allowing countries to go away from non co-operative Nash (tariff) solutions. Ideally, in an FTA, both countries could improve their terms of trade, what can also be translated into higher access to the other partners' markets. Given the specificity of the introduction of imperfect competition in a general equilibrium framework, the changes in terms of trade are presented separately for the two groups of industries; having being computed, in each case, in a direct way, with respect to the base-year flows.

TABLE 27
**MERCOSUR - GLOBAL CHANGES IN THE TERMS OF TRADE,
PERFECT AND IMPERFECT COMPETITION SECTORS**
Scenarios A1 and B

	Scenario A1		Scenario B	
	EU15	EU25	EU15	EU25
Perfect competition	0.2	0.3	0.1	0.1
Imperfect Competition	-0.3	-0.5	-0.2	-0.3

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[76] This fact is confirmed by other model results not shown in the text.

[77] In a different context, it must be said.

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For the perfect competition sectors, the change is positive in all cases, showing that MERCOSUR improves its ToT even under a less-than-ideal reduction of the EU tariff peaks, in scenario B. Were the model solely in perfect competition this would signal to a significant absolute gain in market access for MERCOSUR.

For the imperfect competition sectors, the terms of trade are negative, i.e., the bloc exports slightly more efficient, lower-priced goods, whose technical advancements were triggered by the greater access given to the competitive imports; however, in each sector, the very efficient goods it still buys (imports) are more expensive than its exports.

Finally, following a practice in Giordano and Watanuki [2001], also used in Flôres [2003b], we draw inferences on the likely structural adjustment areas. The idea is to compare the sectoral increases in value added with the global welfare increase. As this is an approximate measure, instead of taking at face value the several ratios, we cut their distribution at the 0.85 and 1.15 points. Ratios below 0.85 identify sectors were adjustment must take place; those between the two values are considered normal, i.e., the sector situation remains practically unchanged; and ratios above 1.15 are considered to characterize winning sectors.

TABLE 28
STRUCTURAL ADJUSTMENT PROXIES
Scenarios A and B

Sectors	Scenario A		Scenario B	
	EU15	EU25	EU15	EU25
AI: agribusiness	⇑	⇑	⇑	⇑
AIIa: commodities	⇑	⇑	⇔	⇑
AIIb: wheat and cereals	⇑	⇑	⇔	⇔
Dairy	⇑	⇑	⇔	⇑
Shoes & leather	⇑	⇑	⇑	⇔
Text. & clothing	⇑	⇑	⇑	⇑
Non-met. Minerals	⇑	⇑	⇑	⇑
Steel I	⇑	⇑	⇑	⇑
Steel II	⇑	⇔	⇑	⇔
Machines	⇔	⇔	⇔	⇔
Auto I: Cars	⇓	⇓	⇔	⇓
Auto II: Other vehicles	⇑	⇑	⇑	⇑
Elec. Equipment	⇓	⇓	⇓	⇓
Chemicals	⇓	⇓	⇔	⇓

Notes: ⇓ needs adjustment; ⇔ "normal" case; ⇑ winning sector.

The upwards arrows in Table 28 identify, in the EU15 case, a significant number of winning sectors under scenario A, but three less under scenario B, though two "losing sectors" (cars and chemicals) suffer less impact under the latter. And the same six and two more under scenario B. Moving to the enlarged space nearly doesn't change the situation under scenario A, though, under B, a positive and a negative reversal take place. Anyway, cars, electronic equipment and chemicals are sectors which will need adjustment under both scenarios.

E.   Policy Conclusions

As this section has shown, when distortions are introduced in the ideal FTA, results are less interesting. This implies that the non-ideal options deserve a more careful detailing and analysis of their impacts.

Agriculture, which fits into the message just highlighted, shows very promising results in the ideal version, and far from bad ones in the "realistic" case. This is true for commodities, wheat & cereals and the agribusiness, the latter clearly showing the existence of a mature and strongly competitive industry. The enlargement - as portrayed in the model - opens a window for extra gains in these sectors, confirming and reinforcing results in Section V.

Not all Section V findings were exactly reproduced in the model, however. The model seems to have enhanced the negative aspects in the cars, chemicals and electronics sectors and, perhaps, softened those in machines & equipment. Not only the different classification and aggregation levels should account for this. Without denying the importance of the partial equilibrium methodology, we think that the *general equilibrium interrelationships*[78] may have come closer to the (global) truth. This seems particularly valid in the cars sector, where the complex regimes under which it operates both in the EU25 and the MERCOSUR probably masked the effects in our partial equilibrium study.

If, in the optimistic versions *and in both studies*, higher welfare gains are obtained in agriculture, further gains may be reaped if a tough and well co-ordinated policy is conducted at the WTO (see Section III). Given that a large portion of the world production subsidies lies in the CAP, this signals that the EU is an extremely competitive partner, even *vis à vis* the US, *if further dismantling of the CAP is achieved*. As this issue is usually sent to the Geneva forum - be it as a polite escape or as a reasonably logical strategy -, it is never too much to remember that relevant decisions still must take place at the WTO, with consequences that may outpace the present welfare gains. This is also a further argument to *decouple*[79] FTA negotiations from WTO positions, as strongly suggested in Section III.

The WTO dimension is also worth stressing for its different interrelationships with the final objective of this project. Indeed, it is somehow ironic that in sectors where MERCOSUR will undoubtedly reap gains, like shoes & leather, textiles & clothing, and even in agriculture, multilateral liberalisation will almost certainly have an impact on these very gains, by enhancing the market access of competitors the size of India, China or other Asiatic countries. In the case of shoes & leather, the new entrants provide already a "taste of things to come", as depicted in Table 25. On the other hand, the 10AC may add further pressure for a more conservative position of the EU delegation in Geneva, something also undesirable. All this only brings back some of the points frequently put forward by trade theorists like Bhagwati and Panagariya [1996], on the importance and precedence of multilateral over regional negotiations.

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[78] By far, the greatest advantage of CGE exercises.

[79] It was difficult to resist the temptation to use the CAP jargon.

The present study focussed only on market access for goods. The dynamics of other crucial concessions - like, for instance, those regarding foreign direct investment - may greatly affect the results here discussed. However, as pointed out in Section II, the enlargement will at least not contribute to an increase in the FDI flows from the Union to MERCOSUR.[80] Also, given the encompassing character of the FTA proposals, in areas like services, where MERCOSUR lags somewhat behind, the multilateral forum seems, in principle, a better locus for broader exchanges.

Finally, it is also healthy to bring forward a point raised by Roland-Holst and Van der Mensbrugghe [2002a and 2002b] on the diversionary properties of FTAs, which may sometimes induce a growth and re-structuring path opposite to the one triggered by multilateral free-trade. Though in the present case, as suggested by Table 26, trade diversion doesn't seem to be very big, this is important to be taken in consideration in the further sequencing of the agreement.

Negotiations must then not be conducted with a short-term perspective, as nowadays appealing gains may become vapid conquests even before the full implementation of the FTA. Market access concessions and demands must be designed keeping in mind the global MERCOSUR's competitiveness and potentialities, as well as the possible outcomes of the different negotiations in which the bloc is involved. The further liberalization steps that will certainly take place *after* the signing of the basic agreement must also be duly considered.

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[80] It may even divert prospective flows, though this conjecture needs a better analysis.

VII. FINAL WORDS

The impact of the May 2004 enlargement is not, as analysed in the previous sections, something to worry MERCOSUR decision makers and economic agents, in overall terms. However, this globally non-menacing picture raises, at a closer look, a few concerns demanding pre-emptive policy measures. We identified in this study a whole set of such concerns, mainly related to *trade in goods*. As mentioned throughout the text, the *services and FDI dynamics,* two key actors that may change - for the worst or the best - many of the conclusions just outlined, received little attention. No doubt, new interesting projects, incorporating these dimensions, are waiting ahead.

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