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Observatorio de Política

Esta Sección incluye artículos que discuten en forma rigurosa, pero no técnica, temas corrientes de política económica que son de interés por su vinculación al mundo real, aún cuando la literatura económica no los haya todavía incorporado definitivamente y artículos que presentan contenidos teóricos resultados empíricos con un formato de política relevante. Como en todas las revistas en que esta Sección se incluye, un objetivo a destacar es que la misma permite acercar a los investigadores académicos con los formuladores de política aportando, respectivamente unos y otros, desarrollos teórico-conceptuales y empíricos importantes y claridad e información sobre las prioridades de política. Los artículos que se publican en esta Sección son escritos por invitación de los Editores de la Revista.

Argentina and Germany: trade and trade policy

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I will focus my presentation by highlighting and commenting on the following topics:

- bilateral relations between ARG, Germany and the EU,
- the ongoing EU-MERCOSUR-negotiations
- and some other trade related and economic aspects.

Traditionally, Germany is the most important EU-trading-partner for Argentina. The bilateral political relations are good and intensive, and have not been interrupted by the economic and financial crisis of 2001. One should not forget the visit of the German chancellor in February 2002 as a clear sign of solidarity in difficult times. Other political visits and meetings followed, for example the visit of the German finance minister in February 2004, and the meeting of the foreign ministers Fischer and Bielsa in New York in September 2004, during the General Assembly of the United Nations.

But unfortunately this positive and continuous political dialogue is not reflected on the economic side. We have to acknowledge a certain reduction of economic and investment activities in Argentina not only from German, but also from other foreign enterprises, due to the crisis of 2001, and - I must say - also because of some continuing unstable economic, financial and juridical investment conditions in the country.

In the same time, we can observe a certain shift of these activities from Argentina to other Latin American countries, especially to its neighbour

¹ Conferencia inaugural del Seminario Arnoldohain IV, Trade, Integration and Institutional Reforms in Latin America and the EU", Facultad de Ciencias Económicas, Universidad Nacional de Córdoba, 14 al 18 de marzo, 2005.

Brazil. It is a bit too early to conclude that this tendency will continue in the near future. It is also possible that we will see a return of capital flow and investments back to Argentina if the positive economic recuperation since 2003 can be maintained in the coming years, and if the foreign debt problems of Argentina can be sustainably solved. The latter issue being the most important economic policy task for the national government of Argentina in 2005.

The recent macro-economic conditions in Argentina are quite favourable. At least, the first estimates for the growth-rates in 2004 have been higher than expected. The GDP-growth rate for 2004 is estimated to have reached 8,8%, and for 2005 still 6% growth is expected. Additionally, in 2004 gross investments increased by 39%, with a focus on long term goods, and foreign investment increased by 30%, after a substantial decline in the period between 2001-2003.

Furthermore, on the 4th of March the Argentine debt-restructuring-offer was better accepted than expected (with an acceptancy-percentage of 76%), although this means that the creditors have to accept a loss of around 70% of their original investment in Argentine bonds. On the other hand, with this restructuring offer the overall debt decreased from 191 billion US-\$ in 2004 to an amount of roughly 125 billion US-\$ in April 2005. The next challenge will be the negotiation with the International Monetary Fund. It is still open as how the outstanding debt of 25 billion US-\$ will be handled.

Summarizing these macro-economic issues, we can say that Argentina is - of course - able to overcome the economic and financial crisis of 2001, but it is still necessary to implement further structural reforms, especially in the public services sector. The energy sector could cause problems and it is not so clear, if it will be able to meet demands of energy in the coming winter months.

In drawing now the attention to trade and bilateral trade relations. In the overall picture we can observe that the bilateral trade relations between the EU and Latin America increased considerably since 1990. The European Union is Latin America's second most important trading partner and the first trading partner for MERCOSUR (Brazil, Argentina, Paraguay and Uruguay), Chile and the Andean Group.

From the beginning of the 90s to 2002, European Union imports from Latin America increased from 26.7 bn • to 53.7 bn •, and the EU-exports to the region rose from 17.1 bn • to 57.5 bn • (these figures include the Andean Community, the Caribbean region, Central America, Chile, Cuba, Dominican

republic, Haiti, MERCOSUR and Mexico). This positive trend is likely to improve, with the enlargement of the European Union which has become an integrated market of 455 million inhabitants since first of May 2004.

On the other hand I do not want to ignore that from the EU-perspective the significance of trade relation with Latin America in the overall external trade of the European Union is not so high, as it is vice versa for Latin America. In 2003, total EU-imports reached 989.5 bn • and total exports roughly 977.8 bn •.

From total EU-imports only 4,8% came from Latin America, and half of it from the MERCOSUR-region. This means, although trade flow increased in both directions considerably, the market share of Latin America with respect to overall EU-imports from third countries is still comparatively low. This fact can be seen as a challenge for both sides.

And it is not only the distance, transport costs and exchange-rate conditions which contribute to this relatively low market share. We have to add as well, market access conditions, quality standards, promotion activities and simply, a better knowledge of business facilitation, and of demand patterns on the export markets.

If we look only at the trade flow between the EU and Latin America, the most important trading block is the MERCOSUR-market. This means Brazil, Argentina, Paraguay and Uruguay. As I already mentioned, in 2003 EU-15 total imports from Latin America reached roughly 48 bn •, from this amount 52% came from the MERCOSUR.

In the structure of this bilateral trade flow we have to consider that the EU-imports from MERCOSUR comprise 52% agricultural, and 48% non-agricultural products, whereas EU-exports to the MERCOSUR-region consist of only 4% agricultural or food products, and 96% industrial products. These different general trade structures play an important role in the ongoing EU-MERCOSUR-negotiations.

To summarize the most important points:

- trade relations between EU and Latin America have increased, but Latin America's share on total EU-imports from third countries is still rather low;
- with more than 50% the MERCOSUR-block is the EU's most important trading partner in Latin America;
- agricultural and food products represent 52% of total MERCOSUR-exports to the EU;

- up to 2003, the overall trade balance between EU-15 and MERCOSUR is negative for the EU, and strongly negative in trade with agricultural goods.

In June 2000 the EU and MERCOSUR started negotiations for a bilateral association agreement with the objective to achieve a greater level of political and economic co-operation and integration within the MERCOSUR group itself, and with the EU. Furthermore, the agreement should support the development and strengthening of common institutions between the Party States of MERCOSUR, and to liberalize all trade in goods and services between the EU and MERCOSUR, within a framework laid down by the WTO.

With respect to agriculture, co-operation between the two parties looks to promote mutual trade in agricultural products, increasing the compatibility of legislation to prevent the formation of trade barriers. It also looks to implement certain environmental measures in order to promote an agricultural model that is, let us say, multifunctional, or at least environmentally sound, with a responsible use of natural resources.

The issues "Consumer Protection" and "Food Safety" are essential topics for the EU. Therefore it is of significant importance to align sanitary and phytosanitary measures in the MERCOSUR states (which is by far still not the case). To this end, an agreement between the EU and the MERCOSUR group looks to establish and develop mutual information systems for dangerous products, rapid alert systems, and to organize training schemes, and technical assistance for their implementation.

Finally, market access offers are for both sides the most important, and politically the most sensitive part of the negotiations. The first exchange of market access offers took place in June 2001. Since then, we have already seen 15 negotiation rounds, many changes and improvements in the respective offers.

Unfortunately, there was a shift backwards in September 2004, where MERCOSUR Member States cut back their previous offer of May 2004, and therefore also the EU withdrew some parts of their May-offer, which finally led to the failure of the October 2004-negotiation deadline being met.

What are the main reasons for the stagnation of these negotiations?

Both sides could not find an acceptable balance between "give and take" in the different offers.

For MERCOSUR, the EU-agricultural market access offer is by far not

substantial enough, especially looking at the sensitive products like beef, sugar, ethanol, cereals and dairy products, and finally MERCOSUR is not willing to accept a two stage, or the so called "single pocket-approach" where half of the EU-preference quota offer is linked to the outcome of the WTO-negotiations.

On the other hand, the EU expects a better market access offer in industrial goods, services sectors like telecommunications, re-insurance-systems, maritime transports and public procurement. To give you an example, the EU-offer and MERCOSUR-request on sensitive agricultural products are as follows:

Product	EU-quota offer (in tons)	Mercosur-request (tons)
Beef	100.000	315.000 / 325.000
Pigmeat	11.000	40.000
Poultrymeat	75.000	250.000
Milkpowder	13.000	34.000
Butter	4.000	20.000
Cheese	20.000	60.000
Garlic	10.000	20.000
Bananas	30.000	120.000
Wheat	200.000	1.000.000
Corn and sorghum	700.000	4.000.000
Rice	40.000	150.000
Ethanol	1.000.000	3.000.000
Sugar	---	1.800.000
Sheapmeat	---	10.000

50% of each of these categories is related to the outcome of the ongoing WTO-negotiations in the Doha round, especially the minimum market access outcome. In some categories like beef and ethanol it was later on agreed to change the percentage from 50:50 to 60:40. This means, the higher the minimum market access obligations are in the Doha-round, the lower is the second half of the mentioned preferential quotas for the MERCOSUR in the bilateral agreement.

Furthermore, MERCOSUR can only count on the first half of these quotas, if the bilateral agreement is concluded earlier than the WTO-agreement. In response to the worse MERCOSUR-offer in September, the EU specified

the phasing-in mechanisms of these quotas, so that for example the beef quota would start with 6.000 t in the first year, reaching 60.000 t in the tenth year of the application of the agreement.

The level and dismantling of the in quota-tariffs is still open. That means it is not automatically assured that the in quota tariffs are zero as they are in the EU-Chile-agreement, for example.

As you see, there are still a lot of imbalances in the negotiations, and one might think that the EU is by far too restrictive. But, having seen the last MERCOSUR-offer, the responsibility lies with both sides, and MERCOSUR has conditioned a lot of market access offers to criteria which hardly can be evaluated in technical terms.

While the MERCOSUR-offer of May covered 87% of imports, the last offer covered only 77% of imports from the EU. In July the EU-Commission submitted to MERCOSUR a list of 353 tariff lines of key industrial products. Only 30 tariff lines of this request list have been included in the new offer. In the automotive sector the MERCOSUR-side extended the phasing out period of tariff-dismantling from 10 to 17 years, beginning with a first tariff-rate quota of 25.000 units instead of the original oral offer of 60.000 units.

I think these examples are enough to illustrate where we are at the moment. Now, it is very important to continue with these negotiations. Some moves for reinitiating the negotiation-process have already been made. The new president of the European Commission, Barroso, met with the Brazilian President Lula da Silva in Davos on the World Economic Forum where they declared their strong will to finalize these negotiations as soon as possible.

Now, we will have a meeting of the coordinators in Brussels, and then probably a next official negotiation-round in Asuncion (Paraguay) in April or May.

The German government has a strong interest in a successful conclusion of these negotiations. We support the European Commission in its objective to reach an ambitious and substantial association-agreement with MERCOSUR. For us and for the whole EU it is clear that we cannot conclude an agreement where sensitive agricultural products are almost excluded.

But one should not forget that the EU-offer of May 2004 was up to now the most ambitious market access offer that the EU has ever made with third countries, especially in the agrifood-sector.

If both sides - the MERCOSUR and the EU - reflect again their offers and their requests, and negotiate with a strong political will to conclude an ambitious agreement, I think it can be possible to see a compromise in the near future.

But we have still to keep in mind that the total package of the negotiations is not limited to market access questions, there are a lot more issues to solve and to prepare with detailed juridical texts, such as:

- Political Dialogue,
- Cooperation,
- Trade in goods,
- Trade in services,
- Public Procurement
- Vines and spirits,
- Sanitary and phytosanitary measures,
- Geographical indications, intellectual property rights,
- Rules of origin,
- Environment and Sustainability,
- Investment
- Technical Barriers to Trade
- Dispute settlement mechanisms

Although the failure of the October 2004 compromise was as a result of not sufficient market access offers from both sides, it was already clear in August 2004 that the stage of preparing final text-versions in all the different subjects, was well behind the timetable, and totally insufficient to reach the October 2004-objectives.

In my opinion, it is better to wait a bit longer, for a balanced and well prepared agreement-proposal, than to look only at the timetable and at political promises, accepting an unmatured agreement-version with a huge number of technical errors.

With regard to some interesting issues in the context of the multilateral negotiations of the WTO.

As I already mentioned, EU-MERCOSUR-negotiations are in several parts directly linked to the outcome of the ongoing WTO-negotiations in the Doha-Round. On the one hand, the EU links its preferential quota approach to the degree of the minimum market access-obligations for all WTO-members.

On the other hand, the MERCOSUR is trying to condition their market access offer to a compensatory mechanism to neutralize the trade distorting

effect of the EU's domestic support, both for their imports and exports.

As a result of the last round of world trade negotiations, the so called Uruguay Round, which started in 1986 and ended in 1994 (in Marrakesh), in 1995 the WTO was established as an international organisation which sets global rules of trade between nations.

The EU has respected the commitments adopted in 1995 both to reduce the level of tariffs, as well as to reduce the level of domestic and export support for agricultural products. In addition, the EU has concluded a number of bilateral free trade agreements as well as preferential trade arrangements, which have substantially benefited third countries, in particular developing countries.

The EU is by far the world largest importer of agricultural goods. In 2003, the respective imports reached 69 bn • (agric. Exports = 54 bn •). With these agricultural import flows the EU imports from developing countries as much as the following five importers USA, Japan, Canada, Australia and New Zealand all together.

Just to recall, the WTO is composed of governments and political entities (such as the EU) and is a member-driven organisation with decisions mainly taken on a consensus basis. By October 2004, 149 countries had joined the WTO. A vast majority of members are developing countries. The largest and most comprehensive entity is the European Union with its now 25 Member States.

While the EU-Member States co-ordinate their positions in Brussels and Geneva, the European Commission alone speaks for the EU at almost all WTO meetings. This is a big difference to the structure of other countries and country-groups in the WTO-meetings. For example, MERCOSUR is still not represented by one speaker, each Member State can present his own position in WTO-negotiation groups and specialized committees.

After the failure of the first meeting of a new negotiation round in Seattle in 1999, the starting point of the new round of the Doha Ministerial Declaration in November 2001 was, for example, that all members committed themselves to comprehensive agricultural negotiations aimed at:

- substantial improvements in market access,
- reductions of, with a view to phasing out, all forms of export subsidies;
- and substantial reductions in trade-distorting domestic support.

Additionally they agreed that

- special and differential treatment for developing countries should be an integral part of all elements of the negotiation and
- modalities for the further commitments, including provisions for special and differential treatment, should be established no later than 31 March 2003.

Although the EU, other WTO-Member States, and the WTO itself made comprehensive proposals for these modalities, it was not possible to come to a compromise in Cancun in 2003.

But it was not only a certain discrepancy in agriculture, it was also the lack of negotiation-improvements in other issues, like trade in services and in the so called Singapore-Issues such as Investment, Competition, Transparency in Public Procurement and Trade Facilitation, which already made a compromise in September 2003 impossible.

The parties are now working on the basis of the new framework-agreement which was concluded in July 2004. This was very important to relaunch the negotiations which collapsed in Cancun. In part, this breakthrough was possible because the EU made an ambitious offer to end EU agricultural export subsidies as part of a final agreement. Additionally, it was agreed that the so called Singapore-issues are no longer part of the Doha-Work-Programme.

For the EU and for the German government, a successful conference at ministerial level in Hong Kong (13.-18.12.2005) will strongly depend on accelerating the negotiations on trade with non-agricultural goods and trade in services.

Another very important issue is the relation between trade and environment. It is clear that the negotiations in agriculture still have to be improved to get an agreement, especially on the exact levels of tariff-reduction, reducing trade distorting domestic support and export subsidies.

However, here we are technically much better prepared and advanced than in other fields of negotiation. To give you an example of what the EU wanted to offer in these three agricultural pillars, we should look at the EU-modalities proposal of January 2003.

Here, the EU proposed:

1. in the pillar of market access

- a reduction in average tariff by 36% and a minimum of 15 % per tariff line;

- all developed and advanced developing countries provide duty-free and quota-free access to their markets for all imports from the Least Developed Countries (LDCs);
- at least 50% of developed country farm imports from developing countries should enter duty free;
- a set of rules and disciplines should be defined to increase the transparency, reliability and security of the management of tariff rate quotas;
- developed countries reduce tariff escalation on products of particular interest to developing countries;
- substantial budgetary support on Trade Related Technical Assistance;
- to clarify the use of precautionary measures.

2. in the pillar of export competition

- an average substantial cut in the volume of export subsidies and an average 45% cut in the level of budgetary outlays;
- phase out export subsidies for certain products, provided that no other form of export subsidisation, including export credits and deficiency payments, is given for the products in question by other WTO members. Such products should include products of particular significance for developing countries;
- treatment of all forms of export support on equal footing and in particular:
 - subject export credits to strict discipline,
 - food aid in kind to be provided only for well-defined vulnerable groups, emergencies and humanitarian crisis;
 - discipline for state trading enterprises.

3. in the pillar of domestic support

- a 55% reduction in the so called "amber box" support (the most trade distorting agricultural support), starting from the level of commitments made in the last round of negotiations;
- define non-product specific domestic support, as measures not related to the type or volume of production, prices, or the factors of production employed;
- eliminate the "de minimis" exception for developed countries (a loophole in the agreement on domestic support that allows for

subsidies not to be disciplined. This "de minimis allowance" is very important in the domestic support of the USA);

- maintenance of the green box (i.e. no or most minimal distorting support) and their criteria.

When the EU proposed this in January 2003, it was still not clear if the parallel ongoing Common Agricultural Policy reform process could be concluded successfully. As you know, this objective was reached and the Common Agricultural Policy reform package was signed in Luxembourg in June 2003. With this reform, the EU completely changed its domestic support structure, applying the new production decoupled single farm payments, and therefore the EU is now well prepared to meet WTO-requests on reducing trade-distorting domestic support.

In many discussions there was a certain misunderstanding of the impact of the CAP-reform on market access and export competition questions. Some argued that we would now have many more margins to reduce tariffs and to phase out export subsidies.

But in fact, market access questions have almost nothing to do with decoupled farm payments. It is very simple, if we in the EU reduce tariffs, we increase competition with third countries, adding a certain pressure for internal producers, and maybe therefore gains for the consumers.

Market access offers have to be seen in the line of certain market sensitivities, the comparison of production costs and cost components and other strategic factors. It is very important not to destroy markets through exaggerated measures like a tariff-reduction from 100 to 0 in one year. The key is finding the right level of market access, not only in the WTO-negotiations but also in bilateral ones like EU-MERCOSUR. For example, Brazil - as the by far best competitor on the world sugar market (with production costs around 190 US-\$/ton rawsugar) - should understand that the EU (with production costs of around 600 US-\$/ton) cannot totally open up its sugar market from one year to another. And Argentina should understand that we still have some beef producers in the EU which already have faced hard and critical times during and after the BSE-crisis. For that reason it is politically simply not viable to offer an amount of several hundred thousand of tons of duty free beef to the EU directly at the beginning of a future agreement. For sensitive or - let us say - highly protected markets, we need some transition-mechanisms with phasing in-periods.