RELATIONSHIPS BETWEEN EU-MERCOSUR: ANALYSIS OF ECONOMIC COMPLEMENTARITIES IN ASSOCIATION AGREEMENT

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Abstract: The EU and the MERCOSUR Association Agreement in negotiation since 1999 is essentially blocked by trade aspects such as access to markets of agricultural products for the EU and public procurement and services for the MERCOSUR. Since the resumptions of negotiations in 2010 and, despite de fact that the opposite economic cycles in both regions make the deepening of the relations more convenient than ever, there has no been a formal exchange of access market offers. This article shows how to strengthen economic relations in those sectors which currently fall outside protectionist measures by both blocks. Furthermore, the analysis of economic complementarities, competitiveness matrix, made according the ECLAC methodology, TradeCAN (Trade Competitive Analysis of Nation), let us identify those sectorial sectors where action could be taken from today. This analysis classifies sectors according to market share and the strength of demand in rising stars, falling stars, lost opportunities and declining. Based on this classification authors define some policy recommendations as productive and trade policies, productive restructuring policies and other policies that facilitate trade.

Key words: Association Agreement, trade complementarities, European Union, MERCOSUR
JEL Codes: F14 - Empirical Studies of Trade, F15 - Economic Integration

1.Introduction

The effects of the crisis in Latin America and the Caribbean, and particularly in the MERCOSUR countries, were milder than those felt in other regions of the world (ECLAC, 2010). Moreover, the region has made a swift recovery, demonstrating at present a great dynamism explained largely by 1) the emergence of developing Asian countries, particularly China, which has set a new trend in the global demand of raw materials and energy sources; 2) the structural change underway in the management of macroeconomic policy, which has resulted in a high level of autonomy in implementing anti-cyclical monetary policy; and lastly, 3) the decline in poverty rates due to strong economic growth in the period from 2004-2008 (Solchaga Recio & Associates, 2011). To the contrary, the European Union remains submerged in a deep recession whose origin was rooted in the contagion of the subprime mortgage crisis, and which has resulted in profound economic and financial instability, especially in the Euro Zone, wreaking havoc above all in peripheral countries such as Greece, Portugal, Ireland, Italy and Spain. However, unlike what is being done in the United States[3], the crisis in Europe is being handled from an orthodox perspective centered on attaining a fiscal adjustment in order to reduce the public deficit. These restrictive policies, together with the current monetary and financial instability, are effectively prolonging the recession. The growth forecasts are negative for an ample group of countries, essentially those on the periphery, and miniscule for the whole of the EU, as well as the Euro Zone (IMF, 2011a and IMF,

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[3] An analysis of the crisis and of the differences in managing it in the United States can be found in Rodríguez Ortiz, 2011.

2011b). Thus, one can clearly appreciate the opposing cycles that are taking place in Europe and Latin America/MERCOSUR, making the deepening of economic relations between the two regions more relevant now than ever. On the one hand, Europe is taking advantage as much as possible of the economic cycle in Latin America/MERCOSUR and the expansion of demand in general in the region, so as to partially compensate for the negative effects of the contraction of internal demand[4]. For Latin America/MERCOSUR, the EU remains the largest regional trading bloc, claiming a quarter of global GDP and 35% of international trade. As such, the European market is an interesting destination in terms of its size, and a place where Latin American products have yet to reach a significant level of penetration[5]. But moreover, Europe remains an important trade partner from whom Latin America is able to obtain products with greater technological value that can be used to increase the productivity of the Latin American economic fabric in the sectors where a substantial gap still exists compared to developed countries.

On the whole, relations between both regions depend on global and local conditions of such importance that they cannot be easily overlooked. Although it will not be analyzed here, it is fitting to mention the role of Brazil as a catalyst of foreign relations for the rest of the MERCOSUR partners, and, in general, its role as both a regional and global powerhouse; the consequences of the decisions made at the Doha Round and the realist pragmatism which could permeate trade relations in the face of a possible failure in the WTO; the penetration of China in the MERCOSUR economies; and the lack of direction within the bloc itself, with MERCOSUR now finding itself in the midst of a political impasse following the suspension of Paraguay and the incorporation of Venezuela as a full-fledged member. On the part of the EU, important factors include its management of the dilemma in which it finds itself whenever it begins to prepare the new Multiannual Financial Framework 2014-2020; the budgets for this period and all of the new planning of both external and internal political instruments, such as the reform of the CAP, which will put to the test the very productive and commercial capacities of the battered European economies (García de la Cruz, Sánchez Díez and Gayo Lafée, 2007). In this article, the theoretical references linking integration and productive development are reviewed in order to later expound more deeply upon the bi-regional relations between the EU and MERCOSUR. Following this, an analysis will be carried out of the economic complementarities between both regions through the creation of competitiveness matrices according to the ECLAC and World Bank methodologies. The paper ends with some political recommendations as a means of concluding.

2.Productive Development and International Integration:MERCOSUR and the EU.

As regional blocs, both adhere to ECLAC's "open regionalism model"[6], given that,

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[4] This fact is relevant in terms of business results for transnational European companies, particularly Spanish ones, which invested in Latin America throughout the 90s and 2000s. High percentages of income and profits are being generated by subsidies in Latin American countries.

[5] For a detailed analysis of the penetration of MERCOSUR products in the EU, see Sánchez Díez and Ruíz Huélamo, 2012.

[6] The ECLAC defines open regionalism as "a process of growing interdependence at the regional level, promoted both by preferential integration agreements and by other policies in a context of liberalization and deregulation, geared towards enhancing the competitiveness of the countries of the region and, in so far as possible, constituting the building blocks for a more open and transparent international economy. The

despite their vastly different origins, the European Union and MECOSUR are pursuing similar objectives, including the following: the establishment of the free movement of goods, services and factors of production; the setting of a Common External Tariff (CET) together with the adoption of a common trade policy relative to third-party countries or groupings of states; and, at the domestic level, the coordination of macroeconomic and sectorial policies among State Parties.

For MERCOSUR or the EU, international insertion is not an objective per se, rather, a means of strengthening the productive capacities of their economies; in other words, to facilitate productive development. This can be understood as, "the continual transformation of the productive structures in which businesses permanently appear and disappear", as to promote economic development[7]. From a structuralist perspective, the functioning of productive structures is fruit of the interaction of multidimensional forces, innovation and the related processes of learning and propagation, and the complementarities and associated institutional development (Ocampo, 2005:3-43). This being said, it should be taken into account that, in turn, innovation and complementarities are considered variables with tightly-knit causality (Madison, 1991) or triggers of economic growth (Rodrik, 2004). Therefore, productive transformation means an increase in the diversification of export supply, with gains in productivity. The term was utilized by Prebisch to refer to increased diversification of the productive system in order to narrow the gap that separates developing countries from more prosperous economies (Castilla, 2006). In order for this to happen, productive development policies need to be taken into account, along with the analysis of the insertion in the global economy, innovation and technological development, business development and productive links, and the strengthening of productive structures (Machinea, Martín and Bárcena, 2004).

In the case of Europe, integration was accompanied by the articulation of productive development policies from a supranational perspective, chief among them the policy of research and development implemented through the Framework Program, the regional policy that functions via the Structural and Cohesion Funds, competition policy, etc. Beginning in the nineties, with the Internal Market coming into effect in 1993, and the initial stages of a Monetary Union, European institutions focused both their efforts, as well as a significant part of their resources, in establishing productive development policies that would strengthen European productive capacities. It was thought that the free movement of goods and capital, put into effect by the signing of the Maastricht Treaty, together with the efforts some economies would have to make in order to join the Euro, could augment regional differences, thereby resulting in negative consequences in terms of competitiveness. Despite the tardiness of the creation of productive development policies in MERCOSUR, they have been incorporated into its integration strategy[8]. Some

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ultimate goal is to reconcile better international insertion with deepening interdependence among the countries of the region" (CEPAL, 1994).

[7] This interpretation is directly linked to those proposed by Ocampo (2004) and Rodrik (2005), as Machinea and Vera have indicated. For Ocampo, the dynamics of productive structures - and the specific policies and institutions created to uphold them - are intrinsically connected to the economic growth of developing countries. On the other hand, Rodrik suggests that industrial policy can, in a broader sense, be interpreted as a process of self-discovery, with developing countries assuming the least sectorial concentration both in terms of employment as well as production until relatively higher per capita incomes are reached.

[8] An analysis of this can be found in Lucángeli, 2008.

authors have attributed this decision to the necessity of tackling the economic crisis of the last few years[9] in a coordinated fashion, which under no circumstance should be interpreted as a sign of weakness, but rather as a hallmark of the maturity of the very integrationist process (García de la Cruz, Sánchez Díez, Lucena, and Gayo, 2010). These supranational policies have been added to already existing policies in each of the states, such as for example, those developed by the Brazilian Development Bank.

MERCOSUR has created the Productive Integration Group[10], whose objective is to coordinate and manage the productive integration program. Thus, its work is focused on strengthening the productive complementarity of businesses within MERCOSUR, with special emphasis on the integration of production chains of SMEs, as well as businesses from countries with relatively smaller economies, with the aim of deepening the bloc's integration process[11].

Furthermore, MERCOSUR has created two financial instruments in order to allow for the successful implementation of the abovementioned strategy: the Support Fund for SMEs and the Structural Convergence Fund of MERCOSUR (FOCEM). The first, created in 2007, started with $1 billion, 70% of which was contributed by Brazil; 27% by Argentina; 2% by Uruguay; and the remaining 1%, by Paraguay. One year later, the Guarantee Fund for Micro, Small and Medium-sized Enterprises was created, although it was necessary to wait until 2012 for its structure to be approved[12]. The second fund was created in 2005 with the goal of curtailing asymmetries that exist among the different regions of MERCOSUR, thereby guaranteeing that full advantage would be taken of the profits earned from the expansion of markets. It strives to meet this aim by financing projects which promote growth in the least developed regions of MERCOSUR. The fund's financing is $100 million annually, of which Brazil contributes 70%, Argentina 27%, Uruguay 2% and Paraguay 1%. In spite of this financing scheme, resources are distributed inversely, with Paraguay receiving 48% of financing and Uruguay 32%, in comparison to Brazil and Argentina who receive much lower percentages of 10% each. As such, FOCEM has a certain redistributive component in relation to the national economies of the MERCOSUR countries. Among actions financed by FOCEM, special emphasis has been placed on those which improve infrastructure (structural convergence program), in comparison to others such as promoting competitiveness and social cohesion, or strengthening institutions. There exists a great deal of overlap between FOCEM's program and the SME Fund, which is a positive sign in that there exists a shared vision concerning the problems of productive integration, the beneficial contribution that integration can make in strengthening SMEs, and how business activity can in turn facilitate the integration process.

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[9] Dossier: *MERCOSUR y crisis global: profundizar la integración* Pymes al Día, Banco Credicoop Foundation, no. 58, 570172009.

[10] The Productive Integration Group is made up of representatives from the Ministries of Foreign Affairs, Economy, and Industry and Agriculture, as well as those governmental bodies most closely related to formulating policies for SMEs and Science and Technology. It was created by CMC Decision No. 12/08 and it is a dependent offshoot of the Common Market Group (CMG).

[11] Additional information of this type can be found in Lucángeli, 2008 and MERCOSUR's Productive Integration Group, 2010.

[12] The Fund was created by Decision 41/08 and the structure was outlined in Decision 17/12.

To sum up, all of these initiatives are designed to advance the productive development of the MERCOSUR countries within the framework of international insertion; an objective which can be fortified through the promotion of trade complementarities between the EU and MERCOSUR. Nevertheless, negotiations regarding trade issues between the two regions have been, and still are, plagued by difficulties, as will be discussed in the following pages. The deepening of economic relations between the two regions has always been a mutual foreign policy objective; both on the part of MERCOSUR, and also on that of the EU. The former saw the EU not only as an important trade partner and investor, but also as a role model which inspired its integrationist vision, while the latter, although recognizing that MERCOSUR is not among its chief trading partners, has always shown interest in this blueprint of integration, and in it spotted a model for the rest of the continent.

Table 1. Conditions imposed by the EU and MERCOSUR in order to resume negotiations (2005)

On behalf of the EU:	On behalf of MERCOSUR:
The free movement of goods and services at the core of MERCOSUR (no double external tariffs, harmonization of customs laws, regulation in terms of sanitary and phytosanitary measures and industrial products).	Application of special and differentiated treatment for MERCOSUR countries in the sectors of goods and services covered by the agreement, with more extensive transition periods and recognition of the principle of non-mutual reciprocity.
Improved access to markets, which as a minimum extends to 90% of industrial goods, giving differentiated treatment only to those sectors which demonstrate a competitive difference with the EU, with the exception of agriculture.	Creation of new trade tariffs for agricultural and modified agricultural products that go beyond the clause of the Most Favored Nation (MFN). The recognition of a non-reciprocal preference for modified agricultural products in order to make up for those on industrial products.
Improved access to services.	Rejection of the conditionality of the EU and the principle of “poche unique” (“single pocket agreement”) of the WTO.
Guarantees of the protection of mutual interests, such as respect for the rules of origin, the transparency of public markets and the protection of geographical indications.	No concessions for products that benefit from production or export subsidies.
Principle of national treatment with regard to investments.	No concessions with regard to intellectual property or geographical indications.

Source: Created by the authors from European Commission data.

However, this road has been long and complex. In 1992, the Common Market Council and the Commission of the European Community signed an Inter-institutional Cooperation Agreement that was in effect until 1999, when it was thence substituted by the Interregional Framework Cooperation Agreement (IFCA)[13], signed in Madrid in 1995. This agreement, apart from endorsing traditional themes such as those related to trade and investment, also incorporated political elements, such as respect for democracy and human rights, as well as social development, and business and scientific-technical cooperation. This agreement allowed MERCOSUR to ascend to new heights in terms of its international standing, as it was recognized as a model for regional integration. In parallel, negotiations commenced for the establishment of a fourth-generation Association Agreement, in the same manner as was done with Mexico and Chile.

[13] Further details can be found in García de la Cruz, 2000 and Cienfuegos Mateo, 2006.

While in Chile and Mexico hurdles were overcome with relative ease and its Association Agreements took effect at the beginning of the new millennium, negotiations with MERCOSUR have been marked by continual disagreements that ended with the breaking-off of talks in 2004. One year later, the EU and MERCOSUR would set limits that would have to be respected in order to resume negotiations further on (see table 1).

Table 2. State of trade negotiations, early 2012.

Advances made in the trade talks:	**Unresolved issues in the trade talks:**
Rules of origin. Prohibition of duty drawback; type of proofs of origin and special provisions for Ceuta, Melilla, San Marino and Andorra. Sanitary and Phytosanitary Measuures.An agreement has been reached regarding a textual foundation for negotiation. The EU has set four conditions pertaining to the creation of a list of priority products of which MERCOSUR needs to advance the harmonization of import conditions and related matters (import certificates, verification, regionalization, free movement). MERCOSUR insists on including measures on animal welfare in the chapter of the agreement that deals with cooperation, while it also favored harmonization of import conditions of key products proposed by the EU. Chapters concerning instruments of comercial defense and competition.These are nearly resolved. In the chapter that deals with services and establishment, an agreement was reached regarding postal services and, great progress was made on the subject of telecommunications and domestic regulation.	Geographical Indications and Intellectual Property Rights. Advances have not been made. The MERCOSUR delegation insisted on holding out until the exchange of trade offers. At least initially, it is against any measures that go further beyond those recognized in TRIPS. Mechanisms for Resolution of Jurisdiction, Customs, and Trade Facilitation. No agreements were made, although there was a coming together of positions on various matters to be dealt with: competent jurisdiction, confidentiality of proceedings, public audiences, *amicus curiae*[14], information and technical advice for the first, and transit and reference mechanisms for the second. Public Procurement. The development of national legal frameworks in each member state of MERCOSUR was debated, as was also the case when drafting a regional framework. Trade and Sustainable Development. Key within the agenda, its inclusion in the Agreements with Colombia-Peru and Central America have made it crucial. Despite lacking official texts, both parties appear to agree on the core issues: no harmonization of the levels of social and environmental protection of the state parties, that states remain linked by the stipulations of the multilateral framework, including but not limited to: Agenda 21 on Environment and Development, the Johannesburg Action Plan and the declarations of the International Labour Organization.

Source: Created by the authors from European Commission data with information available in February 2012.

Nevertheless, the parties had to wait until May 2010 in order to officially resume negotiations, following the political push given by the framework of the Bi-regional Summit of Presidents and Heads of State held in Madrid under the last rotating presidency of the Spanish Council. Although great advances have been achieved in the areas of political dialogue and cooperation, the principal obstacles remain in place with regard to trade issues. The EU has impeded the liberalization of the exchange of

[14] *Amicus curiae* consists of third party groups who present themselves in court where judicial litigations are processed. These outside groups are not involved in any dispute, yet have a justified interest in resolving the litigation, doing so through offering opinions in order to facilitate the resolution of the proceedings.

agricultural products, protected by the CAP, and MERCOSUR has upheld restrictions on the so-called Singapore issues. Lacking an exchange of offers, some advances have been made on technical issues, although some points are still up in the air (see table 2)[15].

3. Analysis of Economic Complementarities in Association Agreements

In this section we will highlight the productive complementarity that European industry and MERCOSUR could have, by utilizing analysis of trade relations between them. We used the methodology known as the Trade Competitive Analysis of Nations (TradeCAN). Following a brief introduction to the methodology, a study of the trade competitiveness matrices between both regions will be examined.

3.1. Methodological References

The competitiveness of countries can be analyzed through the combined study of the evolution of the products' market share and the evolution of said products in the global marketplace[16]. European and MERCOSUR exports are classified by sector adhering to the "Standard International Trade Classification" – SITC – revision 2 with various levels of disaggregation. From this information we are able to calculate three basic indicators:

- Market Share M_{ij}/M_i
- Percentage of Exports (Contribution) M_{ij}/M_j
- Percentage of Imports M_i/M

Where:

- *M* indicates the total value of imports
- *Mj* is the value of imports that come from exporting country *j*. In CAN/2009 it is assumed that this factor is equal to the total exports from exporting country *j* to the importing market.
- *Mi* is the value of the imports of sector *i*.
- *Mij* is the value of imports of sector *i* which come from exporting country *j*.

These indicators combine in order to be able to enhance the information and carry out more complex analyses and, as a result of said combinations, calculate the competitiveness matrix, which thus allows us to classify the diverse export sectors into:

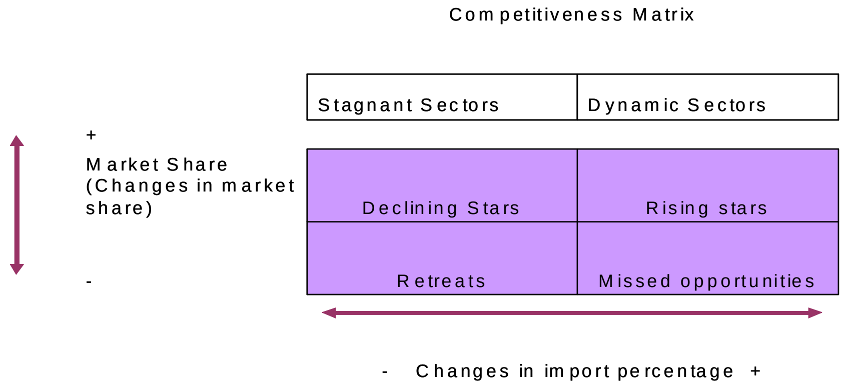
1. *Rising Stars:* This refers to sectors whose international trade is experiencing above average growth and which are gaining market share in the area of reference[17] (improving their competitive position).
2. *Missed opportunities:* This refers to sectors which are dynamic internationally but are losing market share within the market in the area of reference (competitiveness ratio).
3. *Declining stars*: This includes sectors which are losing dynamism internationally but in which the economy experiences increases in market share in the area of

[15] For a detailed look at this issue, see Sánchez Díez and Ruíz Huelamo, 2012.
[16] To see this in greater detail see ECLAC: User manual for the program Competitive Analysis of Nations. Santiago, Chile. ECLAC, United Nations. Available with the acquisition of the database. For other works that use this methodology, please see Mulder, 2009 and Martínez Piva and Cortés, 2003.

reference as a source of imports. In brief, sectors gain in competitiveness within a limited market.

4. *Retreats:* This refers to sectors in which international trade is declining, and moreover, which are also losing market share in the economy of reference. These are sectors which are either very mature or witnessing the substitution of their production for other products.

Figure 1



The competitiveness matrix is calculated according to market share[18], adhering to sectoral disaggregation at a 3-digit level. In this way, it is possible to analyze not only the consolidated competitiveness matrix, but also (through a more detailed analysis) the products which are found within each of the "stars". In the more detailed analysis, only those items which in 2009 represented more than 1% of total regional exports are considered. In order to analyze the competitiveness of European products in MERCOSUR, the latter will be referred to as the importing market and the EU-15 will be referred to as the exporting market. When analyzing the competitiveness of MERCOSUR products in the EU, Western Europe is used as the importing market, considering that it can be representative of the EU, as it includes those countries which are most representative of the region (Austria, Belgium, Luxemburg, Denmark, Finland, France, Germany, Greece, Ireland, Italy, the Netherlands, Portugal, Spain, Sweden and the United Kingdom) and, some countries which, although not members of the EU, are important yet not decisive in terms of significance for bi-regional trade (Iceland, Norway and Switzerland).

3.2. The Competitiveness of European Products in MERCOSUR

EU exports to MERCOSUR increased from $17.960 billion in 2002 to $38.878 billion in 2009, concentrated essentially in the areas of machinery and transport equipment (47%) and chemical products (27%); with an important level of penetration, measured in terms of market share, in sectors such as beverages and tobacco (37%); animal and vegetable oils, fats and waxes (29%); chemical products (26%), machinery and transport equipment (22%) and manufactures (22%) in 2009 (Sánchez Díez and Ruiz Huélamo,

[18] Other possibilities would include the percentage of exports or specialization.

2012). The competitiveness of EU exports in MERCOSUR, analyzed in the competitiveness matrix, show improvements in the periods 2002-2006 and 2007-2009. Looking at the trade dynamism, dynamic and stagnant sectors are differentiated. The participation of the EU's foremost exports in MERCOSUR has increased significantly, rising from 32.4% of total exports in the period 2002-2006 to 83.1% in 2007-2009. Therefore, stagnant sectors have fallen from 67.6% to 16.9% in the same period. In function of the evolution of market share, it is worth noting that EU exports have grown considerably in MERCOSUR, going from 18.3% to 37.4%. Nevertheless, it is important to note that 62.6% of European products in MERCOSUR experienced losses in market share in the period 2007-2009 (see table 3).

Table 3. Competitiveness Matrix of European Union in MERCOSUR, market share of 3-digit industries. Percentage of exports in final year.

		Stagnant sectors		Dynamic sectors	
		2002-2006	67.6	2002-2006	32.4
		2007-2009	16.9	2007-2009	83.1
Gain in markets share		Declining sectors		Rising sectors	
2002-2006	18.3	2002-2006	10.5	2002-2006	7.8
2007-2009	37.4	2007-2009	5.3	2007-2009	32.1
Loss of market share		Retreat		Missed opportunities	
2002-2006	81.7	2002-2006	57.0	2002-2006	24.7
2007-2009	62.6	2007-2009	11.7	2007-2009	51.0

Source: Created by authors from the ECLAC and World Bank´s database Trade Can

The combination of both criteria result in the following (see tables 3 and 4):

- Rising Stars: In global terms they have climbed from 7.8% to 32.1% in the periods considered. This is mainly due to chemical products and machinery and transport equipment; specifically medicinal products, organo-mineral compounds, manufactured fertilizers, pumps and compressors and heating equipment (see table 4). This data indicates that finished products are the frontrunners in this category. The EU is competitive in these products inasmuch as it has increased its market share in MERCOSUR in niches where demand is growing. Therefore, support for these sectors, along with facilitating the trade of these products, is highly recommended. This can be achieved not only by removing tariffs, but also by establishing policies which support exports and foster joint chains of production, via the diverse programs offered by the EU and MERCOSUR for financing productive development.
- Missed Opportunities: These have increased from 24.7% to 51% in the period studied. These consist of products that have relatively higher levels of penetration in MERCOSUR, such as machinery-related items and transport and industrial chemical materials; for example motor vehicle accessories and parts, non-electric parts and accessories, aircraft, passenger cars, etc. This underlines the fact that these are value-added merchandise from mature industries, and, in the majority of cases, they also pertain to sectors where rising stars also exist. In these cases, the endeavors of trade policy should be greater and directed towards recovering opportunities that are being lost, facilitating forays into the Southern Cone market by suppliers from other regions of the world, especially the emerging Asian countries. In these cases, the creation of

joint ventures, business partnerships throughout the production chain, could contribute to the favoring of European products compared with those from other countries.

- Declining Stars: These have been reduced by half, making up only 5.3% of total exports. Of these, no single product comprises more than 1% of total exports.
- Retreats: The decrease of these has been quite significant, dropping from 57% to 11.7%, and again, including products such as machinery-related merchandise and transport material, for example, apparatuses for electrical circuits or internal combustion engines. Also noteworthy are products related to the chemical and paper industries. The Association Agreement should provide opportunities for these sectors to restructure to other niches where future prospects are more favorable, encouraging the incorporation of technological developments, new designs, improved quality or even alternatives uses, etc.

Table 4. Competitiveness Matrix of the European Union in MERCOSUR, market share and percentage of export. 2009.

	Type of star 2007-2009	Market share 2009	Percentage of exports 2009
541 Medicinal and pharmaceutical products;	Rising star	47,92	8.24
728 Other machinery and equipment, specialized;	Rising star	52,82	3.41
515 Organo-inorganic and heterocyclic compounds;	Rising star	29,76	3.01
562 Fertilizers, manufactured;	Rising star	24,42	2.21
743 Pumps (excl. pumps for liquids), compressors, fans;	Rising star	32,59	1.82
741 Heating and cooling equipment and parts;	Rising star	33,85	1.69
514 Nitrogen-function compounds;	Rising star	31,82	1.66
591 Disinfectants, insecticides, fungicides, etc.;	Rising star	28,5	1.49
784 Parts and accessories, n.e.s. of the motor vehicles;	Missed opp.	36,15	6.46
749 Non-electric parts and accessories of machinery	Missed opp.	36,94	3.61
792 Aircraft and associated equipment, and parts;	Missed opp.	32	3.24
874 Measuring, checking, analyzing, control instruments;	Missed opp.	36,14	2.59
781 Passenger motor cars (excl. public service type);	Missed opp.	30,47	2.54
598 Miscellaneous chemical products, n.e.s.;	Missed opp.	36,77	1.75
744 Mechanical handling equipment, and parts;	Missed opp.	43	1.72
583 Polymerization and copolymerization products;	Missed opp.	15,86	1.58
699 Manufactures of base metal, n.e.s.;	Missed opp.	34,1	1.55
745 Other non-electrical machinery, tools, etc.;	Missed opp.	50,7	1.54
716 Rotating electric plant and parts thereof, n.e.s.;	Missed opp.	36,6	1.53
736 Machine-tools for working metals;	Missed opp.	39,03	1.41
778 Electrical machinery and apparatus, n.e.s.;	Missed opp.	17,75	1.38
764 Telecommunications equipment, n.e.s.;	Missed opp.	6,53	1.19
723 Civil engineering and contractor's plant/eqpt.;	Missed opp.	23,12	1.12
674 Universals, plates and sheets, of iron or steel;	Missed opp.	21,28	1.04
772 Elec. apparatus for making & breaking elect. circuits;	Retreat	34,21	2.19
713 Internal combustion piston engines and parts;	Retreat	26,7	2.17
582 Condensation,polycondensation&polyaddition prod.;	Retreat	27,12	1.49
641 Paper and paperboard;	Retreat	26,31	1.01

Source: Created by authors from the ECLAC and World Bank´s database Trade Can. Notes: Missed opp.: Missed opportunities Only sectors that compromise over 1% of total exports in the final year are included.

2.3. The Competitiveness of MERCOSUR products in Europe

MERCOSUR’s exports to the EU shot up from $25.540 billion in 2002 to $55.187 billion in 2009, concentrated mainly on foodstuffs and live animals (36%), and non-edible raw materials (27%) in this last year. The level of penetration of MERCOSUR products in the EU is just slightly inferior to that of European merchandise in the Southern Cone. Across all sectors raw materials lead the way, of which 10% of EU imports come from the region. Likewise, foodstuffs and live animals (2%) and animal and vegetable oils, fats and waxes (5%) are also of importance. The remaining sectors have a market share of under 2% for 2009 (Sánchez Díez and Ruiz Huélamo, 2012). MERCOSUR's trade with Europe demonstrates that dynamic sectors have also increased, reaching nearly ¾ of total trade. However, a decline in importance of products that gain market share has been observed, falling from 75% to 60% of the total (see table 5).

Table 5. Competitiveness Matrix of MERCOSUR in Western Europe. Markets share 3-digit industries. Percentage of exports in final year.

		Stagnant sectors		Dynamic sectors	
		2002-2006	63.0	2002-2006	37.0
		2007-2009	25.9	2007-2009	74.1
Gain in market share		Declined stars		Rising stars	
2002-2006	74.6	2002-2006	41.6	2002-2006	32.9
2007-2009	59.5	2007-2009	16.8	2007-2009	42.7
Loss of market share		Retreats		Missed opportunities	
2002-2006	25.4	2002-2006	21.3	2002-2006	4.1
2007-2009	40.5	2007-2009	9.1	2007-2009	31.4

Source: Created by authors from the ECLAC and World Bank´s database Trade Can

Table 6. Competitiveness Matrix of MERCOSUR in West Europe, market share and percentage of export. 2009.

	Type of star	**Market share**	**Percentage of exports**
	2007-2009	2009	2009
081 Feeding stuff for animals (excl. unmilled cereals);	Rising star	34,23	14.17
281 Iron ore and concentrates;	Rising star	54,51	9.50
058 Fruit, preserved and fruit preparations;	Rising star	12,99	3.47
014 Meat and edible meat offals, prepared or preserved, n.e.s.;	Rising star	17,36	2.95
121 Tobacco, unmanufactured; tobacco refuse;	Rising star	21,25	1.35
792 Aircraft and associated equipment, and parts;	Rising star	1,36	1.25
598 Miscellaneous chemical products, n.e.s.;	Rising star	1,6	1.21
851 Footwear;	Rising star	1,67	1.08
251 Pulp and waste paper;	Declining stars	16,95	3.98
333 Petroleum oils, crude, also from bituminous minerals;	Declining stars	0,91	3.19
287 Ores and concentrates of base metals n.e.s.;	Declining stars	7,37	2.00
781 Passenger motor cars (excl. public service type);	Declining stars	0,52	1.85
931 Special transactions and commodities not	Declining stars	0,3	1.12

class.;			
222 Oil seeds and oleaginous fruit, whisle or broken, for soft oils;	Missed opportunities	37,92	9.22
071 Coffee and coffee substitutes;	Missed opportunities	19,87	4.33
011 Meat and edible meat offals, fresh, chilled or frozen;	Missed opportunities	6,32	3.82
057 Fruit and nuts (not oil nuts) fresh or dried;	Missed opportunities	5,75	3.37
423 Fixed vegetable oils, soft, crude, refined or purified;	Missed opportunities	10,2	1.99
044 Maize (corn), unmilled;	Missed opportunities	16,17	1.38
713 Internal combustion piston engines and parts;	Missed opportunities	1,29	1.13
611 Leather;	Retreats	15,31	1.35
684 Aluminum;	Retreats	2,08	1.19

Source: Created by authors from the ECLAC and World Bank´s database Trade Can
Note: Only sectors that compromise over 1% of total exports in the final year.

A two-fold analysis of the outlook of trade dynamism and market penetration allows us to establish the four product categories that were previously indicated (see tables 5 and 6).

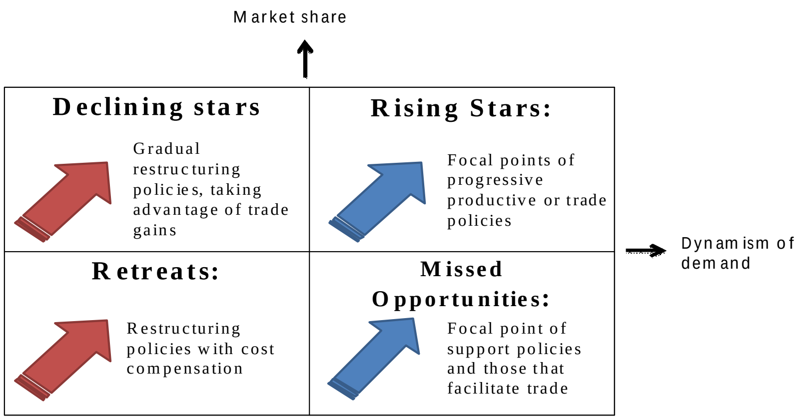
- Rising Stars: A worrying decline of rising stars has been observed, shifting downward from 41.6% in 2002-2006 to 16.8% in 2007-2009. For the most part these are products linked to raw materials, whether foodstuffs or minerals, although also worthy of mention are aircraft and related equipment, as well as chemical products. This specialization shows the interest of MERCOSUR negotiators in guaranteeing the unrestricted access of raw materials to the European market, where in some scenarios market share is already quite high, as is the case for animal feed or unprocessed tobacco.
- Missed Opportunities: These have risen notably, increasing from a marginal position (4.1%) to comprising nearly a third of the total in the given timeframes. The most significant products include foodstuffs, such as coffee, meat and fruit, as well as oils and internal combustion engines. With the exception of this last category, the rest are either products linked to the primary sector or those with little added value. The signing of an agreement that includes agricultural products could potentially benefit MERCOSUR producers, if this were also to facilitate the sale of merchandise such as seeds and oleaginous fruit, coffee, meat or fruit, among others. This serves to underscore Argentina's interest in having an Agreement that encompasses the realm of agricultural products, as well as the EU's reluctance to do so, in line with forecasts carried out by general and partial balance studies (GLOBE y CAPRI, respectively) (Burrel, et al, 2011).
- Declining Stars: These have fallen in importance in terms of total trade, slipping from 41.6% to 16.8% between 2002-2006 and 2007-2009, respectively. In this case, pulp and waste paper, crude petroleum oils, ores and concentrates of base metals, and automobiles stand out.

- Retreats: Finally it is important to note the loss of relative importance of these products, where market share is lost in stagnant sectors, as for example in the case of leather and aluminum. Efforts by MERCOSUR should not be directed towards these sectors for none other than social reasons, in particular if it affects job creation or if it is concentrated in a region and will produce a harsh impact on the local economy. Therefore, more than focusing on access to markets, MERCOSUR should try to encourage cooperation in order to facilitate the transfer of experiences of industry restructuring, as some countries have done with these sectors.

3. Conclusions

The analysis of competitiveness provides us with an important tool for obtaining the maximum benefit of bi-regional Association Agreements. In relation to dynamic sectors, it is recommended to actively promote the rising stars, as well to support sectors that form missed opportunities so that they are able to become rising stars through gains in market share. Among the political instruments that can be used to foster this transition are those which promote productive development via the adaptation of new technologies; research, development, and innovation; trade facilitation, etc. For these sectors, tools such as those created by the EU can be utilized, for example, AL-INVEST, @LIS, etc., as well as knowledge transfers of sectorial policies. In the case of stagnant sectors, priority should be given to the declining stars, with an eye on facilitating their restructuring so that through innovation they are able to turn themselves into sectors in which there is growing demand. Finally, sectors in retreat must be supported for social reasons, although whenever possible reorganization of these sectors should be encouraged with compensation for costs generated. For these sectors, the Association Agreement presents the opportunity to strengthen national capacities, starting with the Agreements made in the pillars of cooperation and political dialogue.

Diagram 1. Policy orientation within the framework of bi-regional relations between the EU and MERCOSUR



Source: Created by authors

As we have seen, bi-regional relations between the EU and Latin America/MERCOSUR have been, and continue to be, fraught with significant problems. Although these have been dealt with throughout the years, the current panorama remains bleak. The unusual situation that the Euro Zone now finds itself in is leading to decision making that is relegating everything that doesn't directly involve the management of the debt crisis and reduction of the public deficit to the back burner. Therefore, in this wholly unfavorable context, there exists the possibility of getting attention in a series of aspects that are decisive for the tightening of relations between the two regions. Specifically, this includes the advancement of the talks needed to bring about an Association Agreement, where the principal disputes are those related to the negotiation of trade issues.

The most contentious issues are those concerning aspects of trade such as access to markets, particularly pertaining to agricultural products, which is an area that would have to be dealt with carefully in order to prevent relations from breaking down. In the case of being unable to reach a serious agreement on this issue, it may be possible to deepen other avenues of economic cooperation on the basis of the analysis of the competitiveness matrix. This is to say, the notion of signing a treaty does not have to be scrapped altogether just because concurrence on trade terms cannot be reached, as this issue can be supplemented with other sectorial agreements. With the same pragmatism applied to relations with Colombia and Peru[19], relations with MERCOSUR should be sealed by finding a middle ground. The failure of this latest round of talks will make it very difficult to tackle the negotiation process yet another time.

Although the signing of a free trade agreement (the pillar that deals with trade in the Association Agreement) is a central issue in strengthening relations, one cannot overlook the importance of other transversal instruments that the EU uses and MERCOSUR fails to make sufficient use of, or, in some cases, does not participate in, as for example in the Latin American Investment Facility –MIAL/LAIF. Here is a concrete example of where MERCOSUR could contribute to promoting the trade of the rising stars and reversing the loss of market share of those products deemed missed opportunities.

It is essential for the sectors designated as rising stars to be the targets of progressive cooperation policies geared towards productive excellence and the facilitation of trade, especially if export products have a large market share at their final destination. These products represent nearly a third of the EU's exports and 43% of MERCOSUR's sales to Europe. This is the case for some European merchandise linked to machinery and transport equipment (machinery for working with stone, wood and glass, pumps and compressors), as well as chemical products and related items (medicinal products, manufactured fertilizers, nitrogenous compounds, disinfectants and insecticides). In the case of MERCOSUR, these star products include foodstuffs (animal feed, fruit, and preserved meats), as well as some minerals (iron) and tobacco, taking advantage of market niches that fall outside the protection of the CAP. Beyond these items with little added value, there are also the aerospace and chemicals industries which also deserve some attention.

Following along the same lines as what was mentioned earlier, it is crucial to develop policies for those sectors deemed missed opportunities (51% of the EU's exports and 31% of MERCOSUR's in reciprocal trade), leaning towards policies which stimulate productivity and, in particular, the facilitation of trade. This is the case for a multitude of

[19] Given the difficulties which exist in the negotiations over an Association Agreement with the Andean Community of Nations, the EU has endorsed an agreement dealing exclusively with trade with Peru and Colombia. As such, Bolivia and Ecuador have been excluded, as have issues related to political dialogue and cooperation.

European products related to machinery and transport equipment, and foodstuff items for MERCOSUR. Nonetheless, it is necessary to mention that we are referring to sectors which are strongly protected; the automobile industry by the larger MERCOSUR countries, and foodstuffs (meat, corn, vegetable oils) by the EU. Given this situation and the desire to reduce impediments to trade, which is not always possible if the Free Trade Agreement does not progress, another possibility might include the creation of joint ventures, thereby taking advantage of some of the EU's cross-sectional cooperation instruments, for example the previously mentioned AL-INVEST.

The tools of economic cooperation between the EU and MERCOSUR must contribute to the restructuring of trade relations pertaining to those products where international commerce is losing dynamism and European products are becoming more and more important (declining stars), with the aim of enhancing quality, introducing design, differentiating products, etc. Thus it is necessary to facilitate the creation of mixed capital businesses and investment in research, development and innovation. These types of products are relatively unimportant in the EU's trade with MERCOSUR, representing around 5.3%, and only slightly more in the case of MERCOSUR's trade with the EU (16.8%), for example in products such as pulp and paper waste, base metals and automobiles. Likewise, it is essential to maintain support for the commercialization of retreats, if only considered necessary for social reasons, that is to say, in function of possible negative effects in terms of job losses in a particular region. These items make up around 10% of trade between the two blocs, consisting primarily of some manufactures with little added value such as leather, as well as electronic devices, combustion engines, and paper in the case of the EU. However, support should be gradual, and focused on sectors where the EU has a high market share in MERCOSUR and which represents a significant percentage of the EU's exports to the region. In a similar sense, there are new issues that need to be incorporated into the agenda, spanning from questions tied to environmental conservation, where Latin America has requested scientific and technological assistance from developed countries; to global economic governance, where the EU could be an important advocate of the Financial Transaction Tax (FTT)[20], the creation of the Migration Observatory, and of the Bi-regional Center for Conflict Prevention, keeping in mind that Brazil continues to have a greater and greater presence, not only as a regional actor but also as a global one.

All in all, there are many incentives and mutual interests that merit the deepening of relations between MERCOSUR and the EU, which should not be lost as a result of the difficulties surrounding disputes over access to markets, included in the economic-trade pillar of the Association Agreement. Nor should obstacles such as the shifting political priorities in Europe as a result of the economic and financial crises in the Euro Zone, or new alliances among emerging powers such as Brazil and/or Argentina, prevent the strengthening of beneficial ties between the blocs. Furthermore, the countries of MERCOSUR mustn't miss the opportunities presented by the EU's numerous

[20] Proposal for a council directive pertaining to a common tax system on financial transactions, thereby modifying Directive 2008/7/CE, COM(2011)594. It is currently awaiting a first reading in the European Parliament (consultation procedure).

cooperation resources, as has been the case in terms of very little or no participation on their part.

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