

From West to East: Mercosur and Singapore agree on FTA

Mercosur-Singapore Free Trade Agreement (MCSFTA), concluded in Asunción, Paraguay, on the 20th of July 2022

Among the Mercosur countries, the FTA reveals Brazil's clear interest in expanding economic and trade relations with key players in Asia, a highly dynamic trading area

Legal & Economic Context

On the 20th of July 2022, the South American bloc Mercosur and Singapore reached the end of negotiations leading to a trade agreement. Before defining a date on which the parties should sign the agreement, it will follow a regular revision process of its text. When signed, the provisions should enter into force as soon as all the countries ratify it and notify properly.

After more than 30 years, Mercosur is still one of the landmarks in the quest for regional integration in the Latin America and Caribbean region. In 1991 the Treaty of Asunción created and formed the basis for the general framework of trade regulation among the four countries of the South American bloc: Argentina, Brazil, Paraguay and Uruguay.¹ The initial objective of the regional bloc was to create a common market, particularly by eliminating all tariff and non-tariff barriers, establishing a free movement of labour and capital, and adopting a common external tariff, with a concept of open regionalism.

However, such a goal is still a dream of the political leaders of the member states. The Mercosur, over the last 30 years, has been limited to a customs union, littered with exceptions, and a relatively unstable framework of how to manage, on one side, the transition to full implementation of the customs union, and, to create a sustainable process of its enlargement, on the other side.

On, Mercosur's 30th birthday, celebrated in March 2021, "[...] there [was] not much to celebrate beyond its mere survival."² Mercosur's evolution is not linear. "A first decade of rapid progress in integration was followed by two more of backsliding and protectionism. Intra-zone trade was about 25% in 1997, today it is just 14%. While Mercosur has struggled to stick to its rules, the Common External Tariff is littered with exceptions."³

¹ Patricia Luiza Kegel and Mohamed Amal, 'MERCOSUR and Its Current Relationship to the European Union. Prospects and Challenges in a Changing World. ZEI Discussion Paper C209, 2012' <https://www.researchgate.net/publication/277103930_MERCOSUR_and_its_Current_Relationship_to_the_European_Union_Prospects_and_Challenges_in_a_Changing_World_ZEI_Discussion_Paper_C209_2012> accessed 6 September 2022.

² 'Can Mercosur Reverse Decades of Backsliding? | The Economist' (25 March 2021) <<https://www.economist.com/the-americas/2021/03/25/can-mercotur-reverse-decades-of-backsliding>> accessed 7 September 2022.

³ *ibid.*

After having reached its peak in terms of regional integration in 1998, its economic dimension was severely affected by two major trends that have had negative impacts on its dynamic⁴: the first major factor is related to the different macroeconomic crises that affected all the member states, causing a context of high uncertainty.

The second factor of instability is related to the own commodity boom that has operated as a strong mechanism to drive more individual integration of the countries with China and other Asian economies. China became the major trade partner of Argentina and Brazil. Such an "Asian dependency" process occurred before the regional bloc consolidated a customs union and a robust system of deepening integration mechanisms.

The changing pattern of global trade affected the Mercosur's international negotiation significantly⁵ and imposed a trend towards deeper integration with minor economies in Asia and Africa while hoping for a happy end to the negotiations with the European Union.

In 2019, the European Union and the Mercosur signed a free trade agreement - FTA (not yet ratified) after almost 20 years of negotiations. This agreement represents a landmark in the international integration of the regional bloc, which has a comprehensive scope and should significantly impact the own set-up of the Mercosur for several reasons.

First, such an agreement represents a milestone in the history of Mercosur since it reflects a mature growth of the regional bloc in terms of achieving a long-standing negotiation process and coming to an output that reflects, to a large extent, the common interests of all members' states.

That is also interesting because it is the first time two regional blocs agreed to create a free trade area: an inter-regional bloc agreement. Likewise, the two blocs represent major regional actors and key regional growth drivers (in Europe and Latin America).

Lastly, it is an agreement that has been reached in a period of great uncertainty in the multilateral system and the corresponding drawbacks in the own globalisation process.

While the development of the regional bloc has been relatively stagnant for almost 20 years, recent events have shown a light of hope, particularly considering the agreement with the EU and, recently, the end of negotiation with Singapore. The new arrangements bring about a fundamental question in the pattern of international integration of the Mercosur: does this process suggest a trend toward more integration with the East? Or does it suggest a kind of

⁴ Sandra Polónia Rios, 'Treinta Años Del Mercosur: Hora de Madurar' in Enrique Iglesias and others (eds), *Reflexiones sobre los treinta años del Mercosur* (2021) <www.kas.de/uruguay> accessed 6 September 2022.

⁵ Patrícia Luiza Kegel and Mohamed Amal, 'Perspectivas Das Negociações Entre o Mercosul e a União Europeia Em Um Contexto de Paralisia Do Sistema Multilateral e Da Nova Geografia Econômica Global' (2013) 33 *Brazilian Journal of Political Economy* 341 <<http://www.scielo.br/j/rep/a/49h7Pm5XymVhZMDsWTM7xZC/?lang=pt>> accessed 6 September 2022.

momentum in the international integration of the individual member states? In other words, is the Mercosur going East while waiting for the FTA with the EU ratification?

Trade between Mercosur countries and Singapore is relatively small. And trade between Brazil and Singapore is predominant compared to the other Mercosur members. Only 2% of the Mercosur export to extra zone countries goes to Singapore. Brazil holds about 98% of all Mercosur's export to the Asian country. In addition, before 2009, the balance of trade recorded a deficit, since 2009 Mercosur held a trade surplus that reached the amount of US\$ 4.7 billion in 2021, according to the Mercosur official Statistics service.⁶

On the one hand, the trade pattern between the two regions is an inter-industry trade, where Mercosur exports mainly commodities, such as meat, ferroalloys and iron ore. On the other hand, Mercosur members import insecticides, integrated circuits, medicines and ships from the Asian country.

In South America, Mercosur is the primary destination of Foreign Direct Investment (FDI), and data from United Nations Conference on Trade and Development (UNCTAD) points out that Singapore holds the 24th position in the list of the origin of FDI in Brazil. Besides, both countries have shown positive results in their investment by each in the other country.⁷

In 2020, Singapore invested the equivalent of US\$8.02 billion, standing for a relative share of 2% of total FDI inflows in Brazil. Although the volume of FDI is relatively low, the involvement of several Singaporean companies in Brazil - 128, according to the Brazilian Central Bank (Bacen) - has been growing significantly in recent years.⁸

However, despite Singapore's still modest share in Mercosur's trade relations and FDI flows, the FTA is an imperative step toward strengthening the bloc's integration in Southeast Asia. Besides, the agreement with Singapore is the first - signed - with a Southeast Asian country.

Facts

When looking at the Latin American economic blocs, Mercosur is far less active in the international scene when it comes to trade agreements' activity.

The EU-Mercosur FTA, for instance, took two decades to conclude in 2019. Yet, its entry into force is uncertain. However, the conclusion of the agreement stands for a milestone in the

⁶ 'SECEM (Sistema de Estadísticas de Comercio Exterior Del MERCOSUR)' <<https://estadisticas.mercosur.int/>> accessed 6 September 2022.

⁷ 'Investment Statistics and Trends | UNCTAD' <<https://unctad.org/topic/investment/investment-statistics-and-trends>> accessed 6 September 2022.

⁸ 'Direct Investment Report' <<https://www.bcb.gov.br/en/publications/directinvestmentreport>> accessed 6 September 2022.

history of Mercosur. The agreement is unique as it brings together the two regional blocs to create a free trade area: an inter-regional bloc agreement.

The long-lasting but fruitful negotiations with the EU might have motivated Mercosur to pursue further trade negotiations more promptly. In the case of Singapore, it all lasts less than 5 years. The preceded negotiations went ahead quickly, starting in late 2017. At that point, Mercosur's Brazilian pro tempore presidency sent a proposal to Singapore, inviting an exploratory dialogue toward a trade agreement. An exploratory meeting and the announcement of negotiations followed in 2018. After the 2019 first discussion round was held in person, negotiations switched to virtual meetings due to Covid-19 until 2022, when it concluded in Asunción, Paraguay.

Singapore, on the contrary, has been extremely active in building international partnerships and setting up better trade conditions. Singapore has signed an FTA with the bloc making up Chile, Colombia, Mexico, and Peru in January 2022, the Pacific Alliance-Singapore Free Trade Agreement, or simply PASFTA. It results from under 5 years of negotiations and overcoming the Pacific Alliance discussions with Australia, Canada, Japan, and New Zealand. On top of everything already conducted by Singapore so far in 2022. Singapore ESG, a statutory board under the Ministry of Trade and Industry and ProColombia, a government agency, signed a Memorandum of Understanding to enhance trade, energy, and tech collaboration. Besides that, Singapore has also signed digital economy pacts with New Zealand, Australia, and Chile, aiming to ease the trade routines' digitalisation and for Singapore companies to engage in cross-border business activities.

Analysis

The Mercosur-Singapore FTA follows the model of contemporary trade agreements and their trends, including provisions for specific treatment of investments. In the case of Brazil, those aligned with the Brazilian Investment Facilitation Agreement. The structure designed in the chapter also tries to stimulate the attraction and maintenance of investment flows. The goal is likewise to offer support to hesitant foreign investors.

The e-commerce chapter sets fundamental principles to help the development of a free, accessible, transparent, safe, and efficient trade platform.

Within the Intellectual Property (IP) domain, the FTA provisions endorse international standards previously in place at both ends and in alignment with the Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS) and the Paris Convention for the Protection of Industrial Property. Besides the traditional topics that an IP chapter covers, it

integrates the protection of genetic resources and traditional knowledge, which greatly interests Brazil, a megadiverse country. In addition, an annexe to this chapter has provisions to promote technology transfer.

If the IP system in both countries in a broader context meets international standards, it works differently on each side. While at the South American end, Brazil launched a national IP strategy in 2019 to cope with the country's key IP challenges,⁹ Singapore did it back in 2013 and has recently done it again, with the Singapore IP Strategy (SIPS) 2030 that "consists of three main focus areas, each addressing a different aspect of Singapore's economy – i.e., supporting international activities, growing local enterprises, and building a high-calibre workforce".¹⁰ In both cases, the strategies' expectation indicates the country's competitiveness enhancement, enforcement of registrations and resolution of IP-related disputes.

Moreover, amongst the world's most streamlined and robust intellectual property protection regimes, it is Singapore; which National Intellectual Property Office (IPOS) is considered one of the most respected, dynamic, and innovative IPOS. Singapore pursues a position as an ASIAN international hub for IP assets, the reason it recognises IP as a way to achieve development.¹¹ The Brazilian IPOS, on the contrary, suffer from a lack of financial independence, insufficient personnel and, consequently, a considerable backlog, especially in the case of patent applications.

Another key chapter is the one about trade in goods. Through the agreement, Mercosur and Singapore will work toward the abolition of import tariffs for all goods exported by Mercosur countries to Singapore as soon as the agreement is enforceable. In return, the South American counterparties also will offer tariffs liberalisation for Singapore once the FTA measures and provisions are in place in all countries.

From an institutional perspective, the closing of the FTA with Singapore also represents a successful foreign policy achievement in the middle of multiple negotiations going on at the moment. In that context, Brazil leads the bloc negotiations with Canada and Lebanon, and Uruguay coordinates the talks with South Korea. Before that, we find such success only if we look back to 2019 when the EU and Mercosur closed a trade deal. Unfortunately, the ratification process has never started and together with the European Free Trade Association (EFTA) agreement, they are currently under legal review. In the exploratory scenarios, there is much in the course which shows Mercosur's commitment to enlarging its foreign alliance. We can name

⁹ BRAZIL (GIPI), *Estratégia Nacional de Propriedade Intelectual (ENPI)* (2020) accessed 6 September 2022.

¹⁰ 'IPOS | Singapore IP Strategy 2030' <<https://www.ipos.gov.sg/manage-ip/singapore-ip-strategy-2030>> accessed 6 September 2022.

¹¹ Daniela Ferreira de Matos, 'Estudo de Impacto: Acordo de Livre Comércio Mercosul-Singapura' (2022) <[https://www.gov.br/produtividade-e-comercio-exterior/pt->](https://www.gov.br/produtividade-e-comercio-exterior/pt-) accessed 6 September 2022.

negotiations with distinct potential trade partners, including Central America, the Caribbean, El Salvador, Vietnam, Indonesia, and the Pacific Alliance.¹²

We also see the Mercosur-Singapore FTA as a positive and strong sign of an official agenda with the Asia-Pacific. We could not say it before Singapore, because the FTA between India and Mercosur is an extremely limited deal with almost no real implications. We see, however, that it is only the beginning. Mercosur needs to build an agenda with South Korea, but there is no hope now that the two sides will find a way out of the impasse. There is no Mercosur agenda with Japan or with China either.

Mercosur shall follow Uruguay's path and build a bloc agenda with China. However, they can try to use the FTA with Singapore as a gateway to ASEAN, especially in China. If we consider that there is much Chinese and Asian business in Singapore, this FTA can revert in new ASEAN investment in the Mercosur region.

Singapore is a port city, and tariffs never played a role against accessibility to the country, which has always been considerable open. That is also why there are two perspectives to consider when analysing the Mercosur-Singapore FTA. One side refers to the real impacts of the trade deal, which can be related to the trade flows increasing more in services than in goods. The other side is the symbolic impact it can produce. In our opinion, the latter is particularly related to a chance to access Southeast Asia and is the most relevant impact.

Practical Significance

The Mercosur-Singapore FTA is an overarching agreement that targets trade conditions and market access improvement through decreasing tariffs and creating opportunities for firms.

In the case of Brazil, it should favour the FDI attraction, create new prospects for Brazilian exportations and path the way to cooperation, namely on trade facilitation and customs. All Mercosur exportations will enjoy a better position within the competitive market due to the deal on tariffs.

Brazil's Foreign Trade Secretariat (SECEX) estimates that Mercosur-Singapore FTA can generate positive outcomes for Brazilian GDP, exports and imports and investments, as well as a decrease in prices. The study also indicates that the existence of the FTA, in comparison to a scenario without the agreement, can lead to an increase of R\$ 28.1 billion in Brazilian GDP, accounting for values accumulated between 2022 and 2041. SECEX offers an estimated R\$11.1

¹² Secretaria del Mercosur, *Informe Semestral Del Mercosur* (32nd edn, 2022) <<https://www.mercosur.int/en/documento/32a-edicion-del-informe-semestral-junio-2022/>> accessed 6 September 2022.

billion in investments, R\$21.2 billion in Brazilian exports and R\$27.9 billion in imports, totalling an increase of R\$49.1 billion in trade between Brazil and Singapore.¹³

Still, according to SECEX, a value-added index for Agriculture is expected by 0.03% and that for the extractive industry by 0.02%. There also would be an increase of 4.41% in the transformation Industry, 4.85% in the services sector, and 2.47% in the agricultural sector. The FTA should also affect different sectors in diverse ways. However, the effects of the FTA follow the Brazilian economic trends, featuring positive outcomes at the level of products and exports. The prospects show a growth in the sectoral product in 55 of the 65 sectors.¹⁴

In a context where UNCTAD estimates that Singapore's stock of foreign investment amounts to US\$625 billion, the flows of FDI between both sides are also supposed to benefit from the FTA too.¹⁵

Technological inputs, machinery, and all sort of equipment that can be useful for the local firms in Brazil and South America, in general, will be available at better prices. That can increase productivity and decrease prices while making a product more competitive.

In the short run, the FTA with Singapore is less effective in enlarging the Mercosur trade position. That is due to the region's political and economic instability, adding more uncertainty in the global context of bilateral trade negotiations.

Nevertheless, the agreement is likely to represent another landmark in the future of the regional bloc. While the FTA with the EU opens a new stage in the Mercosur international integration, the agreement with Singapore can provide added advantages for Mercosur to strengthen its position and explore new trade opportunities with other large trade partners.

The question then is how such a Singapore-Mercosur agreement can influence the Mercosur as a regional bloc of integration.

The agreement is expected to be implemented gradually and in a more long run horizon. However, the agreement will likely imply important short-run implications in different areas, particularly in bilateral direct investment and increased business opportunities for small and middle-sized companies in Asian countries.

While we understand that the effects are expected to be positive, the impacts' assessments and analysis are difficult to foresee until we have a perspective of its ratification and implementation. However, we can expect some important implications from the agreement.

¹³ Matos.

¹⁴ *ibid*; *Free Trade Agreement Between Mercosur-Singapore: Informative Summary* (2022).

¹⁵ United Nations Conference on Trade and Development, *World Investment Report 2022* (2022).

First, we do not expect a significant increase in bilateral trade between the two regions. Singapore is a relatively small and open economy. The elimination of tariff barriers is not expected to imply significant changes in the volume and pattern of bilateral trade.

Second, from a long-term perspective, such an agreement can open new opportunities for other trade agreements with larger economies, like Indonesia or China.

Such an agreement can strengthen negotiations of the Mercosur vis-à-vis other regional blocs, like the EU. Finally, we believe that the commitments of the Mercosur with important economic global economies can provide a great opportunity to turn the regional bloc into a sustainable and stable global integration framework.

To conclude, we see the Mercosur-Singapore FTA as a major event in the path of the Mercosur's member states to a long-standing trade integration with Asian countries. This process started during the commodity boom and evolved significantly after the 2008's financial crisis, creating a kind of Asian dependency, replacing traditional partners, like the USA and the EU, as the major trade and investment partners. The implications of such an agreement reinforce the process of moving East and exploring the great business opportunities in Asia. However, we see several problems that may limit the potential impacts of such an arrangement. First, it seems Mercosur going East does not necessarily reflect a strategic choice of the regional bloc. This important move seems to point to a short-run opportunity for trade negotiation rather than a strategic positioning of the member states as a regional bloc.

Second, Singapore is a small and highly open economy. It is likely to expect the country to benefit from the advantages of a larger economic bloc by exporting more technology-intensive goods. How much the agreement can promote investment flows to the Mercosur is difficult to foresee. Singapore's relative share in the world outward FDI (OFDI) is small, and its strategic interests are more oriented toward deepening its integration in southeast Asia.

Finally, the advantages of signing an FTA with Singapore can imply significant changes in Mercosur's trade and investment patterns when the regional bloc can set up a strategic trade policy by building alliances with large economies. Going East means creating mechanisms of cooperation with those economies to access regional markets and new sources of competitive advantages.

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