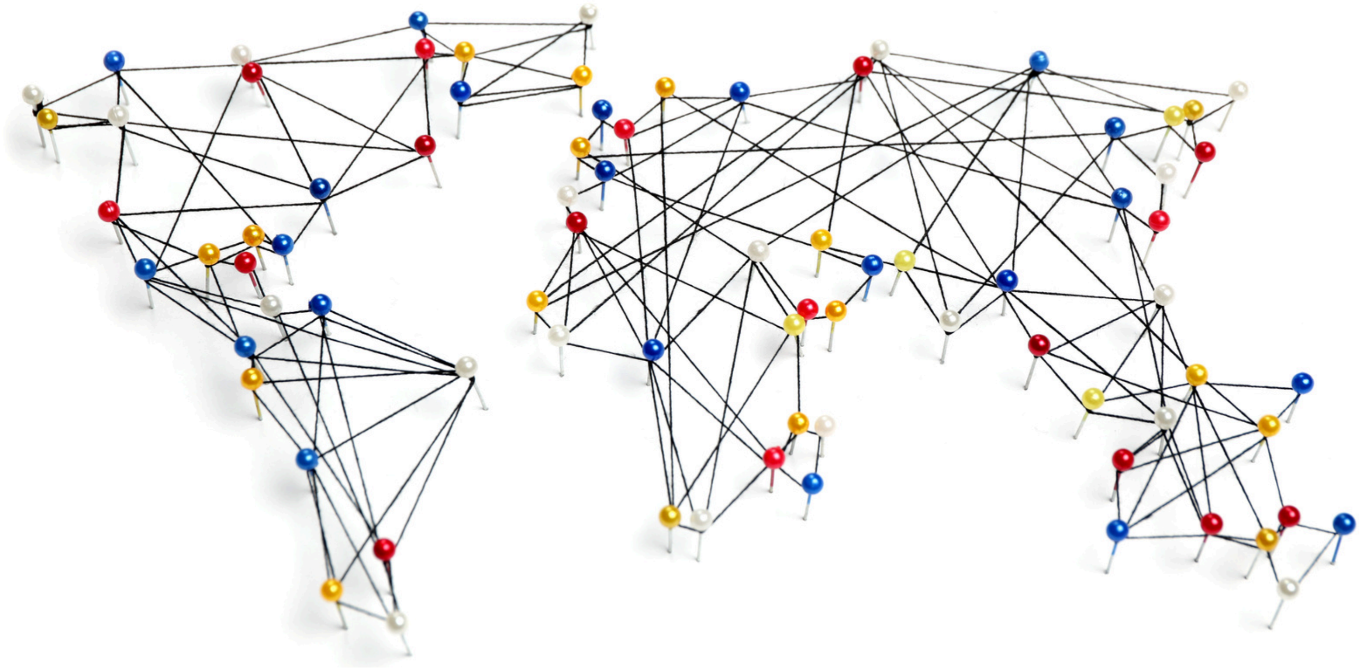
ABCI NOTE



ABCI NOTE WINTER 2025

ABCI Chairman

Dear reader:

We are happy to introduce the Winter 2025 ABCI Newsletter, with a new design to commence the ABCI Institute's journey into its third decade of promoting research and information on international trade.

This edition features a new session, "Expert's Take", and to inaugurate it we invited diplomat Henrique Choer Moraes, who led the Brazilian team at the EU-Mercosur negotiation, to write a short piece. The recently approved Agreement is also the subject of Vera Kanas text. Chiara Pappalardo exposes the crisis facing the EU's automotive industry. Luiza Nonato surveys the use of Trade Remedies in Brazil during the second year of Lula III. Our ABCI chairman, Aluisio de Lima-Campos, discusses the upcoming U.S. Trade Policy and its likely impacts. Finally, Sergio Goldbaum links the views on the future of the Multilateral Trade System that were discussed at our ABCI XXth Symposium.

The content of this newsletter can also be read as individual posts on our ABCI Substack.

Please share this newsletter and the ABCI Substack website on your social media channels.

ABCI wishes you all a happy 2025.

NEW DEVELOPMENTS REGARDING THE RELATIONSHIP BETWEEN TRADE AND ENVIRONMENT IN THE AGREEMENT BETWEEN MERCOSUR AND THE EUROPEAN UNION TRADE AGREEMENT

Vera Kanas

Despite the increasing unilateralism that characterizes our current global landscape, there are still successful examples of agreements between nations—or more precisely, between economic blocs—in the field of trade. This is the case of the conclusion of the Partnership Agreement between Mercosur and the European Union, announced in December 2024, which marks a transformative milestone in international trade relations.

Since the supposed closing of the Agreement negotiations in 2019, several interesting developments have taken place. The one we consider the most important is the regulation of the relationship between Trade and Environment.

The parties negotiated an Annex to the Chapter about Trade and Sustainable Development, under which the blocs undertake to reinforce their environmental commitments and to avoid the adoption of unnecessary barriers to trade. The Annex includes provisions regarding multilateral environmental and labor regimes, the relationship between trade, investment, sustainable development, trade and women's empowerment, and cooperation.

It is worth noting that the EU has committed to using data from Mercosur authorities in assessing the compatibility of imports from Mercosur with compliance requirements established by EU legislation. The EU acknowledges the quality of data produced by Mercosur institutions for the implementation of European regulations.

Furthermore, the parties recognized that environmental measures affecting trade must be consistent with WTO Agreements and that they must not constitute a disguised restriction on trade, and they must be based on technical and scientific information.

Finally, we highlight the innovative mechanism that prevents unilateral measures by the Parties from disrupting the balance set in the Agreement, recognizing that such measures could undermine negotiated trade concessions and distort the agreed outcomes. An arbitration process would determine whether there has been an erosion of commitments and, if so, the extent of such an impact—regardless of whether a formal breach of the Agreement has occurred. If the arbitration concludes that trade has been restricted, the Party imposing the restriction must offer trade compensation (market access concessions) to the other Party. If no agreement is reached on compensation, the affected Party will have the right to impose retaliation (suspension of benefits under the Agreement) in an amount determined through arbitration, with the goal of restoring the balance of the Agreement.

The provisions and instruments above will ensure that, for example, an EU legislation issued for environmental purposes, such as the EU Deforestation Regulation, which is based on a legitimate concern but that includes a trade measure that imposes a severe or disproportional burden on exporting countries of agricultural products like Brazil, does not nullify or impair a market access concession granted under the trade agreement.

THE EU AUTOMOTIVE INDUSTRY IN TRANSITION

Chiara Pappalardo

The automotive industry in Europe is facing significant headwinds. Production slumped between 2019 and 2022 before it bounced back again marginally in 2023. However, the number of newly registered EU cars is still lower than before the pandemic in 2019. The sector is weighed on by weak economic growth, high energy costs, disruption in key supply chains, geopolitical risks, and industrial policies of third countries, such as the United States Inflation Reduction Act and China's extensive government interventions. Worryingly, the share of battery-electric and plug-in electric vehicles in European carmakers' output is very low and has declined in recent months. In August 2024, registrations of electric cars dropped by 43.9% compared to the same month in 2023, driven by an astonishing 68.8% decline in Germany, considered the bloc's industrial powerhouse.

The challenges associated with electric vehicles (EVs) include high costs and inadequate charging infrastructure. The average selling price of an EV in Europe is approximately €65,000, roughly double that of more traditional models. European incumbent companies are struggling to make profitable and affordable EVs, mainly due to the high cost of batteries. Only one of the world's top 15 battery-electric vehicles is made in the EU. New companies from the battery and tech sectors have entered the market and leapfrogged the incumbents, especially as EVs are more uncomplicated to assemble than internal combustion engine vehicles. In this context, China has emerged as a global EV manufacturing hub. Vis-à-vis the EU, China is the main source of car imports, increasing by nearly 40% from 2022 to 2023. The country also dominates the production of almost every raw material and component (batteries, chips) used to make EVs. Meanwhile, Chinese investment in the EU along the EV value chain has been rising for the past few years.

A complicating factor for European automakers is EU Regulation 2023/851, which sets stricter standards for carbon dioxide (CO_2) emissions from new passenger cars and light commercial vehicles. While the regulation bans the sale of petrol and diesel cars by 2035, subsidies for EVs were reduced in certain regions, with the European market increasingly having to rely on favorable company car taxation schemes. The law also imposes strict requirements on automakers. If the average CO_2 emissions of a manufacturer's fleet exceed its specific emission target in a given year, the manufacturer must pay – for each of its new vehicles registered in that year – an excess emissions premium of €95 per g/km of target exceedance.

As a result of policy, industrial and economic trends, many EU factories are closing, raising questions of timing, social equity, and workers' rights. The EU green growth agenda is becoming increasingly unpopular with voters. However, few would disagree that the EU automotive industry is too big to fall behind global competition, employing 13.8 million people (directly and indirectly) and representing 8.5% of total EU manufacturing employment. In Slovakia, Romania, Sweden, Czechia, Hungary and Germany it represents more than 10% of total manufacturing employment. The automotive sector also has major upstream and downstream linkages and comprises a complex network of cross-border supply chains, including a large number of specialized small and medium-sized enterprises. A case in point is Italy, which has a wide network of distributors and manufacturers and is a major exporter of auto parts.

How can the EU automotive industry move forward and stay competitive? Elected representatives and industry experts are taking a hard look at these questions. In a recent report, former president of the European Central Bank, Mario Draghi, suggested lowering energy and labor costs and increasing automation in the sector. He recommended developing a specific EU industrial action plan covering all value chain stages for the automotive industry. Furthermore, he advises supporting new essential projects of common European interest in innovative areas (such as affordable electric or autonomous vehicles and circularity in the value chain) and developing recharging and refueling infrastructure.

For their part, EU automotive industry representatives have urged the EU institutions to take urgent relief measures while political leaders have asked companies like Volkswagen and Stellantis to negotiate with labor unions and strike deals to prevent or defer planned layoffs.

Finally, the EU has taken steps to stave off competition on the trade side. In October 2023, the European Commission initiated anti-subsidy investigations into EU imports of battery electric vehicles from China, arguing that these imports were being subsidized and thereby detrimental to the EU industry. Provisional countervailing duties (ranging from 17.4% to 36.3%) entered into force on 5 July 2024. The Member States supported the definitive measures on 4 October 2024.

The future of the EU automotive industry is all but certain, yet one thing is clear: the road ahead is bumpy at best.

THE USE OF TRADE REMEDIES IN BRAZIL: INSIGHTS FROM LULA'S THIRD TERM (2023-2024)

Luiza Nonato

The use of trade remedies during the first half of Lula's third term saw a notable increase in investigations, encompassing initiations, sunset reviews, and other related procedures.

According to Figure 1, the Brazilian authority conducted 69 investigations in 2024, including 40 initiations, 27 sunset reviews, one redetermination, and one countervailing duty investigation. This is a significant increase from the previous year when it conducted 29 investigations, including seven initiations, 15 sunset reviews, two anti-circumvention reviews, and one countervailing duty investigation. Currently, 145 trade defense measures are in force.

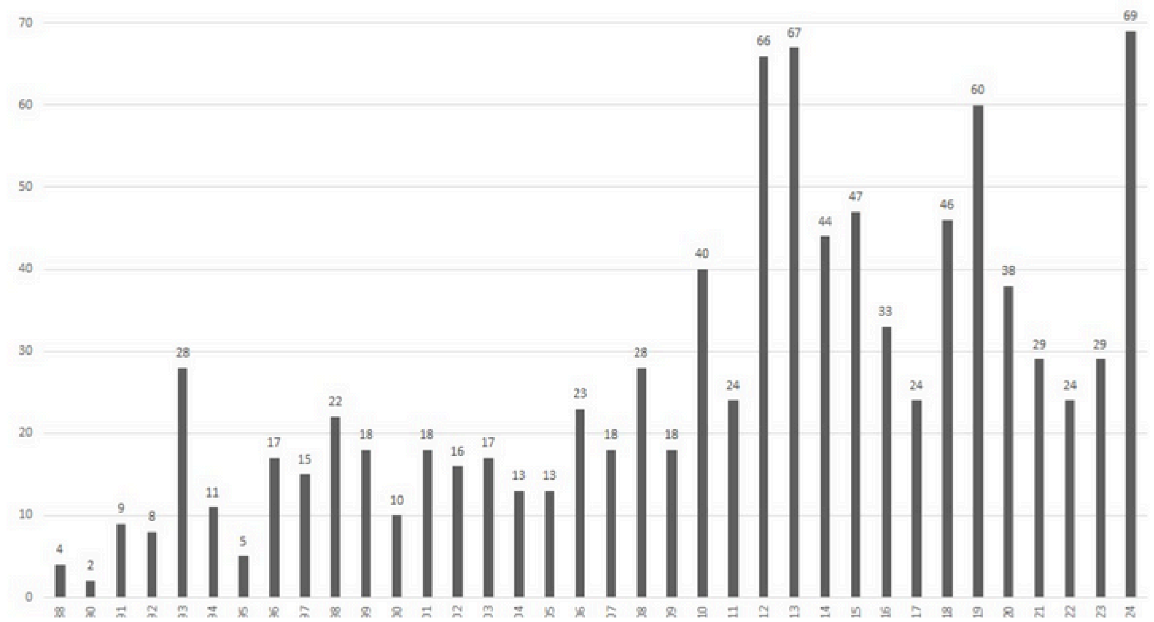


Figure 1: Brazil: Trade defense measures investigations, 1988-2024. It includes anti-dumping (initial investigations and sunset reviews), countervailing measures and safeguards) — source: Ministry of Development, Industry and Trade.

TThis data reveals three significant trends:

The sharp increase in trade defense activity, from 29 investigations in 2023 to 69 in 2024, underscores a growing tendency among Brazilian industrial sectors to leverage trade remedies to address unfair trade. This may also be a strategic reaction to growing external competition, indicating a more protectionist-reliant stance in a progressively complex global trade environment.

The rise in the number of investigation openings, which increased more than fivefold from 7 in 2023 to 40 in 2024, indicates a shift towards addressing potentially new cases of dumping or subsidization, reflecting heightened import trends and their impacts on local markets.

Aligned with the overall increase in trade defense measures, the rising number of sunset reviews (15 in 2023 and 27 in 2024) suggests a continued effort to reassess the necessity of maintaining existing measures, ensuring their alignment with evolving trade dynamics.

For reference, the data used is available <u>here</u>.

UPCOMING U.S. TRADE POLICY AND LIKELY IMPACTS

Aluisio de Lima Campos

As we approach January 20, here is what can be expected for U.S. trade policy based on official announcements and comments by Trump and his team, which, as of now, are just appointments still subject to approval by Congress.

The Trade Team

First, Trump's selections for the leading positions in trade policy include Howard Lutnick for Secretary of Commerce, who has been tasked with leading the U.S. trade and tariff agenda, with direct oversight of the Office of the United States Trade Representative (USTR), and Jamieson Greer, an experienced trade lawyer, to be the U.S. Trade Representative and focused on implementing tariff policies and defending American manufacturing, agriculture, and services, as well as opening up export markets. Robert Lighthizer, who served as USTR in Trump's first administration (when recently appointed USTR Greer was his Chief of Staff), has been asked to "run US trade policy." Although not officially announced for a formal position, Lighthizer's role suggests he will continue to influence trade policy in some capacity. Scott Bessent has been picked to lead the Treasury Department. Bessent is known for his background in hedge fund management (including a long association with George Soros' fund management firm) and his support for tariffs as a negotiating tool. These selections reflect Trump's emphasis on trade policy, mainly on tariffs and rebalancing trade deficits. However, the exact roles and the extent of their influence can be subject to change based on the administration's final structure and any congressional confirmations required.

The Policy

As it looks right now, trade policy will focus on tariffs. Trump has historically favored tariffs as a tool for trade negotiations and economic policy. There are indications that his administration might pursue a strategy involving 'universal' tariffs, targeting countries like China, Canada, and Mexico. Some reports suggest these tariffs might be more selective than previously proposed, but Trump called those reports "fake news" in his January 7 Mar-a-Lago press conference.

Trump's preference for bilateral agreements over multilateral ones is expected to persist. His administration has shown a willingness to use tariffs as leverage to push for negotiations that favor U.S. economic interests, as seen with the renegotiation of NAFTA into the USMCA. This approach aims to ensure economic gains for the U.S., focusing on job creation and reducing trade deficits. Such a policy also suggests that the upcoming trade team will not give the WTO and international trade rules much attention.

Trump has utilized national security justifications for imposing tariffs, notably on steel and aluminum from various countries under Section 232 of the Trade Expansion Act. This intertwining of trade with national security will probably continue, potentially expanding to other sectors or countries considered to pose security risks. He is invoking national security to pursue control of the Panama Canal and the purchase of Greenland.

Global Trade Relations and Economic Impacts

Global trade relations will likely suffer from aggressive tariffs and trade threats. It could increase tension with trading partners, possibly resulting in retaliatory measures. This might disrupt international supply chains and have domestic inflationary effects due to increased costs for consumers and businesses, especially those highly dependent on imports. However, this approach might also be used strategically to negotiate better trade terms or to encourage domestic production.

On the economic impact of this trade policy, while tariffs might protect some domestic industries, they've historically led to higher costs for U.S. businesses and consumers, potentially impacting overall economic efficiency and job markets. The policy's success in reducing trade deficits or boosting domestic employment has been debated, with previous efforts showing mixed results. The impact on prices, however, is almost assured in the short term. The only expectation is by how much, as reflected by ongoing increases in U.S. Treasury yields.

Financial markets are experiencing a mixed reaction to Donald Trump's announced trade policy, with enthusiasm and caution evident across different sectors and markets. After Trump's election victory, U.S. stock markets initially surged, with the S&P 500 and other major indices hitting record highs. This was mainly due to expectations of pro-business policies, tax cuts, and deregulation. However, there has been a negative impact on stocks of import-dependent businesses and increasing caution by investors concerning sectors like technology, which might face higher tariffs or regulatory changes.

In his upcoming term, Trump's trade policy would likely emphasize protectionism, focusing on tariffs to negotiate better trade deals, protect national industries, and address trade deficits. However, the exact implementation, scope, and impact would hinge on various factors, including global economic conditions and the responses of U.S. trade partners.

XXTH ABCI SYMPOSIUM: VIEWS ON THE FUTURE OF THE MULTILATERAL TRADE SYSTEM

Sergio Goldbaum

The future of the multilateral trade system was one of the major themes in the XXth ABCI Symposium, which was held on 2025 November 21-22, featuring **Dmitry Grozoubinsky** (*Why Politicians Lie About Trade*'s author), Prof **Uri Dadush** (Maryland Univ; *Geopolitics, Trade Blocks, and the Fragmentation of the World Commerce*'s author), the Brazilian Secretary of Trade, Tatiana Prazeres, Amb **Alan WM Wolff** (Peterson Institute for International Economics; *Revitalizing the World Trade System*'s author), and Prof **Padideh Ala'i** (American Univ).

Grouzoubinky stressed the issues of policy preferences and trade-offs: the US and other developed countries' policy choices seem to reveal that they currently prefer increased predictability and an increased attitude toward long-term investment rather than international stability, lower prices for consumers and a "more efficient distribution of where we make goods and services and how we connect those goods and services with those that want to buy them." In answering a question about Trump's tariffs, he said that what politicians present as no-choice policies are seldom intentional choices and that high tariffs can not consistently achieve two opposing objectives: increase tariff revenues and, at the same time, create jobs in America.

Uri Dadush reinforced the main takeaways from his book. In particular, the prospects of de-globalization are somewhat exaggerated, that despite the protectionist wave, trade is “as free as before the global financial crisis,” that regional trade agreements help facilitate international trade but are not enough, and that a multilateral perspective is still critical. Trade fragmentation and the erosion of the existing global trade rules will prevail in the next four years. Still, economic interest will make trade openness prevail in the long run, so WTO should be preserved. The China-US trade war is still the main question to be addressed, but the impact of China’s subsidies on commerce has been overstated.

Tatiana Prazeres elaborated on the meaning of trade fragmentation for Brazil's interests. For her, trade fragmentation could mean Brazil navigating a more complex global landscape with more restrictive, distorted trade practices. All that with a weaker WTO. So, Brazil may face pressure "to align itself with specific blocs or find that access to certain markets." On the other hand, she believes Brazil is "well-placed to position itself as a reliable trading partner as countries seek to diversify and develop more resilient partnerships." She also discussed the re-emergence of industrial policy, the impact of digitalization on trade, and the growing interaction between trade policy and environmental policy.

Amb Alan Wolff's primary concern is Donald Trump's intention to apply 10% and 20% tariffs to all imports and 60% to US imports from China and its foreseeable consequences. Among them are whether the developed countries will follow Trump's tariffs, the possibility of Chinese retaliation, and whether the WTO will resist the gradual disintegration of the rule-based open trading system.

Prof Padideh Ala'i agrees with Amb Wolff on the challenges to the multilateral trade system ahead and shares with Prof Dadush that the system is at “a tipping point.” However, she is not sure about the shape of trade fragmentation. She underscores the role of the WTO in allowing a peaceful resolution of trade disputes. She sees open plurilateral agreements as one of the ways forward despite the resistance of a few countries (India and South Africa). Most importantly, she worries about the isolationist trend in the US under Trump, comparing it to China's approach to building economic relationships with many countries worldwide.

In closing the event, panelists reiterated their long-term confidence in the multilateral trade system's resilience. They also reinforced the need to preserve and adapt its institutions to the new international environment.

The complete recordings of both panels are available on the ABCI website.

EXPERT'S TAKE

Henrique Choer*

MERCOSUR AND THE EUROPEAN UNION CONCLUDE NEGOTIATION OF PARTNERSHIP AGREEMENT

On December 6, 2024, the leaders of MERCOSUR and the European Union announced, in Montevideo, the conclusion of negotiations of the MERCOSUR-European Union Partnership Agreement. The Agreement will bring together two of the largest economic blocs in the world. MERCOSUR and the EU gather approximately 718 million people and a GDP of close to US$ 22 trillion.

Following the efforts of more than two decades of negotiations, the outcome achieved by the two regions is transformative from both economic and political perspectives, in addition to strengthening MERCOSUR as a platform for the international integration of its Member States. In a global context of growing challenges to the rule of law, social justice, and the peaceful settlement of conflicts, the Agreement represents the association between two regions that share common values and interests, such as the defense of democracy, multilateralism, and the promotion of human rights.

The Agreement incorporates innovative and balanced commitments that are in line with the challenges of the current international economic context. Among these commitments, it is worth highlighting (i) provisions that reconcile trade and sustainable development in a collaborative and balanced manner; (ii) an innovative mechanism for rebalancing concessions conceived to provide comfort to MERCOSUR exporters in the event that internal EU measures negatively impact the ability to effectively take advantage of the benefits obtained through the Agreement; (iii) government procurement disciplines that safeguard the policy space for health programs, inter alia.

The agreement's texts are currently being legally scrubbed before they can be translated into the EU's 23 official languages. Once they have overcome these stages, they will be ready for signature.

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