

Master Thesis:**Understanding the Roadblocks to the EU- Mercosur Trade Negotiations:
A Comparative Analysis of the Two Periods of EU-Mercosur Interregional
Trade Agreement Negotiations 1999 - 2004 and 2010 - 2016**

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*To Rob, Caroline, my brother, Karen and Leon
who were there for me every step of the way*

Introduction

1.1 Overview

The European Union (EU) and Mercosur have long expressed an official interest in creating an association agreement between the two blocs. This goal was partially formalized in 1995 with the signing of the Inter-regional Framework Agreement, with talks officially underway in 1999 following the re-launching of negotiations at the EU-Latin America Summit in Rio de Janeiro. Despite a continued (albeit inconsistent) formal interest in reaching an interregional trade deal, an association agreement has failed to materialize after well over a decade of negotiations and political dialogue between the two regional actors. Why has a trade agreement been so elusive? In the context of this overarching research question, this thesis paper sets out to analyze key developments in the two EU-Mercosur negotiation periods: 1999 to 2004 and 2010 to 2016. Five variables are defined and examined within both negotiation periods: ***Institutional Capacity, Political Will, Special/Sectoral interests, economic shocks and simultaneous trade negotiations***. These variables form the basis for a comparative analysis of the two trade negotiation periods in Chapter 3, thereby providing a comprehensive overview of endogenous and exogenous factors preventing an interregional trade deal. The goal is that an analysis of these variables will help provide an up-to-date comprehensive overview of the negotiation successes and pitfalls, as well a methodology which may be used to analyze future prospects for an EU-Mercosur Association Agreement.

1.2 EU-Mercosur trade negotiations in the Literature

Like much of the analysis of the EU-Mercosur trade negotiations, this paper will draw from the literature on interregionalism. By interregionalism this paper refers to one of many foreign trade policy (FTP) tools “which states or state-like entities choose over other instruments” like bilateralism and plurilateralism. (Meissner 2015; Aggarwal and Fogarty 2004; Elsig 2007). I will adopt Söderbaum and Langenhove’s (2005) simple definition of interregionalism as “*the condition or process by which two regions interact as regions.*”

The EU officially favors interregional trade models and it has actively, though unevenly through time and space, promoted its unique brand of interregional trade. Many scholars have touted EU’s

interregional trade preferences as a paradigm-changing form of “normative” or “civilian” power (Manners, 2002). Along the same vein, much of the literature has called EU’s international relations approach a form of “soft power” which favors strategies such as diplomacy, persuasion, and negotiation to produce its desired outcomes while exporting European values (Doctor, 2015). Doidge (2007) observes that when there are strong differences in levels of regional integration between EU and other negotiating blocs, the EU predominantly uses capacity-building forms of interregionalism. This tendency to use capacity-building measures to help strengthen less integrated regional counterparts is apparent in the EU-Mercosur negotiations as Mercosur received considerable funding in the area of “development cooperation” between 2007-2013, including \$50 million in funding¹ to extend Mercosur’s scope (70%), enhance role of civil society in Mercosur (20%), and supporting Mercosur institutions (10%) (Grieger, 2014).

However, it has also been called into question whether EU’s interregional model is in fact fundamentally different than other forms of region-to-region FTP (Grugel, 2004). Scholars have documented how economic recessions as well as competition from US or China have put a lot of pressure on the EU to drop the normative component of its interregional trade policy (García, 2015; Messerlin, 2013) or even to drop interregionalism in favor of other FTP tools such as bilateralism or plurilateralism instead of interregionalism (García 2015; Meissner 2015). Hence the creation of a Strategic Partnership between Brazil and Europe in 2007, a surprising bilateral act that angered several leaders of Mercosur member-states--most notably Argentina--while at the same time sending a strong message from the EU to Brazil signaling the importance of Brazil’s emerging economy to Europe’s strategic economic interests (Meissner, 2014).

Research on intra-regional impediments to an EU-Mercosur trade deal often centers on issues of regional “integration”² or the closely related concept of regional “cohesion”³, and has been especially directed towards shortcomings in the Mercosur bloc. Scholarly articles comparing regional models (Grugel, 2004; Doctor, 2007) point to disparities between the EU and Mercosur regional models, often isolating the institutional and political deficiencies of Mercosur as the main barriers to a trade deal (Doctor 2007). Mercosur did see some early successes in institution building with the creation of a Parlasur in 2002 and a dispute settlement mechanism following the

¹ Data taken from the European Parliamentary Research Service briefing *EU-Latin American Relations* (26/03/2014)

² List the regional intergration EU-Mercosur articles

³ Meissner (2014) defines cohesion using a series 12 indicators

Protocol of Olivos in 2004 (see Salvio, Cabral 2004), but institutional progress has since staggered and bloc negotiations have consistently revealed the predominance of state-centered actors and interests. Deficiencies in democratic processes within Mercosur have also been seen as an impediment in reaching a trade accord. Mercosur has been criticized for functioning largely as a top-down, state-centric negotiating partner, led by elite technocrats, lacking in participation from civil society, the private sector, and the citizens of nation-states; this of course harms the legitimacy of any trade agreement (Doctor, 2007) and has prompted the EU to invest in the promotion of more bottom-up processes within Mercosur governance.

In addition to deficiencies in institutions and democratic processes, a principle factor affecting integration/cohesion--and by extension, a successful regional trade agreement--has been policy divergence between member states of both regional blocs. Several prominent Latin American leaders, including heads of state Luis Lula of Brazil and Cristina Kirschner of Argentina, presented political opposition to the liberalization of their economies and pushed back against many of the neoliberal trade models offered to Mercosur by the EU and other trade entities. Apart from ideological factors, policy divergence often stemmed from special interests and specific sectors within nation-states of both regional blocs. From the European side, a key obstacle to an EU-Mercosur trade agreement has been the protectionist stance of the agricultural lobby in France and The Netherlands and the refusal to compromise on Agricultural subsidies outlined in the EU's Common Agricultural Policy (CAP) (see Revell, Sanders, Sanders 2014; Tomazini 2013) as well as Argentina's unwillingness to offer concessions in the services and industrial sectors (Tomazini 2013).

Regional asymmetries of political power and lack of interstate integration in terms of economic benefits constitute further important obstacles to reaching an inter-regional agreement. On the one hand, political and economic power asymmetries are endemic to Mercosur due Brazil's disproportionate size, population and GDP relative to the other Mercosur states. Brazil is by far the largest member, accounting for 67,3% of the total GDP of Mercosur⁴. During early negotiation stages, Mercosur was often characterized as a platform for Brazilian political and economic interests (Grugel, 2004). Trade statistics have confirmed that Brazil has in many periods benefited disproportionately from intra-regional trade compared to smaller Mercosur countries such as

⁴ <http://blogs.worldbank.org/opendata/what-are-trade-blocs-and-how-do-two-latin-america-s-largest-compare>

Uruguay and Paraguay, and those members have aired many grievances on the matter (Tomazini 2013). Mercosur's ability to function as an interregional unit has been dependent on Brazil's state interests. At times Brazil's interests have been favorable towards a deeper Mercosur integration, yet in other instances, as detailed by Messner (2015), Brazil has preferred to act independently of Mercosur.

Another factor that has worked simultaneously in favor and against EU-Mercosur negotiations are the concurrent trade negotiations; the FTAA and WTO Doha Round as well as the major economic pressures arising from Chinese FTP in the Western hemisphere⁵ are therefore important pieces of the puzzle in analyzing the EU and Mercosur FTP decisions. Meissner (2015), for instance, argues that EU's shift towards bilateral negotiations in 2006 (while the EU-Mercosur negotiations were on hiatus) was triggered mainly by exogenous factors—most notably, US and Chinese interest in the Brazilian market—as opposed to endogenous factors such as changes in Europe's FTP.

As many authors are quick to point out, the literature on interregionalism and regionalism—both with the EU-Mercosur context, and otherwise—has been fragmented and inconsistent (Doctor, 2016). Another important gap in the literature relates to the causal link between regional integration and interregional trade is unclear. While literature has attempted to connect regional integration's effect on interregional trade outcomes, the reverse scenario has not been studied as extensively. In light of this issue, Doctor's 2016 article examines the reverse situation: what is the impact of interregional trade negotiations on the regional integration? His findings suggest that interregional trade negotiations have little influence on deepening regional integration. Furthermore, the vast majority of literature examining the failure in negotiations between the EU and Mercosur has mainly focused on two factors: the reluctance to liberalize trade for agricultural products on behalf of the EU, and, on behalf of Mercosur, the unwillingness to liberalize the industrial and services sector.

The literature on the EU-Mercosur Negotiations has therefore looked at several dynamic pieces of the trade negotiation puzzle on both an inter and intra-regional scale. While each factor is important in its own right, the goal of this thesis paper is to provide a more comprehensive and systematic overview of the causes behind the failure of trade negotiations.

⁵ see Peters, Enrique (2015) *China's Role in Latin America: Can it be a Win-Win?* Atlantic Council, Adrienne Arsht Latin America Center.

1.3 Research Question and Structure

This thesis focuses on understanding the impediments to an association agreement⁶. The central research question for this paper is therefore:

- *Why have the EU and Mercosur repeatedly failed to produce a trade agreement since the establishment of the 1999 EU-Mercosur Interregional Framework for Cooperation Agreement?*

The trade negotiations will be compared across two periods using five key variables affecting trade negotiation. Subsequently, this paper uses Putnam's (1988) two-level game model of negotiations and conflict resolution to answer the overarching research question.

The main research question encompasses several sub-questions. Chapter I, focusing on the 1999-2004 negotiation period, is dedicated to answering the following sub-questions:

- *What were the setbacks and the successes of the EU-Mercosur negotiations during the first period based on the five variables of interest?*
- *Why has inter-regional trade been a preferred trade policy instrument for the EU and Mercosur countries?*
- *Why would Mercosur be interested in an inter-regional trade negotiation with the EU?*

Chapter 2 focuses on the second negotiation period (2010-2016), employing a similar approach:

- *What were the setbacks and the successes of the EU-Mercosur negotiations during the first period based on the five variables of interest?*
- *Why did negotiation talk resume and under what circumstances?*

The following Chapter 3 offers a comparative analysis of the two negotiation periods, comparing the variables across time and incorporating them in the Two Level Game theory model to explain their overall failure.

⁶ The discussion of the potential benefits of an agreement is not the focus of this paper; however, to the extent it relates to the research question, I will discuss how regional blocs and sub-regional

- *What variables have changed or stayed the same between the earlier negotiation period and the current one?*
- *What social-political-economic conditions make a trade deal more or less feasible at this moment than at the previous occasions?*

1.4 Dimensions of the Comparative Analysis

As to the time-frame of the negotiations for the purpose of this thesis, I will be analyzing the development of negotiations on a theme-by-theme basis roughly following the chronology of events. The rationale for a chronological overview is to adequately situate isolated events in the EU-Mercosur within their broader inter, intra-regional, and global contexts while the issue-by-issue examination allows for closer scrutiny of specific issues, prompting the comparative analysis in Chapter 3. Highlighting both the major important advances and major derailments in the two negotiation periods requires a multi-dimensional analysis: country-specific, sector-specific and region-specific as well as interregional-specific analysis method is employed.

The primary unit of investigation of this paper is the region, namely the Mercosur and EU regional blocs although the “y” or outcome variable is the establishment (or absence thereof) of an association agreement. This paper therefore identifies issues which exist between blocs as well as issues endogenous to each bloc (but only if they can be shown to have had a causal impact on the interregional trade negotiations⁷). Finally, just as interregional developments are affected by intra-regional developments, intra-regional developments are affected by nation-specific stances on trade policy. Several cases covered in this thesis will show how country-specific issues (e.g. The Argentinian service sector) can affect regional cohesion and, by extension, interregional trade negotiations.

Putnam’s Two-level Game model allows for an interregional and intra-regional analysis of the five variable. This model will be used as a tool for explaining the causal effects of the variables on the results of the trade negotiations.

⁷ That is to say, there are many regional issues beyond the scope of this thesis paper; likewise, there are also several interregional issues (i.e., EU development funding in Mercosur countries) that will not be covered here.

Variables: Uses and limitations

The five following variables will be used for this comparative analysis. It is important to consider that these variables are not binary; instead they occur on a spectrum. In addition, (as outlined in the limitations' section) these variables are all interdependent and interrelated to varying degrees. The causal impact of each variable on other variables is beyond the scope of this thesis. Nor will the variables be weighted or quantified. This paper operates under the assumption that all it takes is a deficiency in one of the variables to prevent a trade agreement. Therefore, the following variables will be analyzed using the lens of Putnam's Two-Level Game Theory which allows for analysis on both an inter and intraregional level.

1. ***Political Will:*** Political will refers to the willingness of leaders of member-states to advance or complete a trade deal. This variable refers to ideological opposition to the trade deal adopted by leaders of nation-states and other high-ranking officials. This variable most significantly refers to whether a country's leader and other high-ranking representatives favor more protectionist macroeconomic trade policies or liberal (neoliberal) policies. Political will can be identified through policy briefs, speeches and positions of representatives of member-states.
2. ***Regional Institutional Capacity:*** This variable refers specifically to the existence and capacity of supra-national institutions to conduct trade negotiations, as well as the ability (or lack of ability) of these institutions to conduct simultaneous negotiations. Defining this variable requires looking at the evolution of regional trade institutions, examining institutional mechanisms and their quality.
3. ***Special and Sectoral Interests:*** This variable refers specifically to the impact of intra-regional special interests which have affected the trade deal. (This variable does not encompass ideological factors so much as protectionist positions in specific economic sectors, although certainly the two are related). Essentially, the special and sectoral interests' variable will cover the contentious trade items and provisions which have produced gridlock.

4. ***Simultaneous trade negotiations:*** Finally, the analysis would be incomplete without an explanation of how competing and simultaneous trade interests have affected EU-Mercosur inter regional trade negotiations. The most important simultaneous negotiations are FTAA, Doha and China's foreign policy towards Latin America.
5. ***Economic shocks:*** This variable refers to exogenous economic shocks - such as the global depression of 2008 and 2009 - that have set back trade deals.

Analyzing these aforementioned variables can provide unique insight into the roadblocks as well as the successes within the negotiation period. The variables are analyzed using two-level game model with the aim of providing a clear and comprehensive view of the negotiations' failures. There are, however, some limitations to this theoretical model. For one, many of the aforementioned variables are interrelated, inextricably linked and overlapping. Regardless, it helps to view each in isolation in order to understand the various dimensions of trade negotiation shortcomings.

Another limitation is that many of the variables can (and do) have an effect on one another. Methodically describing and quantifying the causal links between these factors is beyond the scope of this paper.

Sources for this Thesis Paper

This is a document based mostly on the political and historic data available regarding the EU-Mercosur negotiations. Therefore, in order to carry out the research, the information was gathered from both the open digital sources such as the Internal Mercosur publications through Mercosur Press, as well as third-person interviews conducted with Mercosur officials in both periods (see Doctor, 2007 and 2015; Meissner, 2014; Tomazini 2013). In order to provide a detailed description of the development of negotiations, official government positions will be examined. Such information was collected from the EU records, records/summaries of major summits, and media sources (see SICE summaries of each round of negotiations, SICE is the Foreign Trade Information System of the Organization of American States which contains the official records of each round of negotiations). Analysis from organizations like the Inter-American Development Bank (IDB) and the Center for Strategic and International Studies (CSIS) were also equally important data sources for this section of the thesis .

Chapter 1: Negotiation period 1999 – 2004

The period of 1999 – 2004 comprises of 15 rounds of negotiations, mainly taking place in the framework of the EU-Mercosur Bi-Regional Negotiations Committee (BCN). The first part of this chapter briefly describes the main framework and functionality of Mercosur and the EU, in order to later examine the five variables and answer the underlying question of why the EU and Mercosur States decided to start such a project.

Interegionalism surged as a phenomenon in International relations during the 1990's. According to Doctor (2007), interregional negotiations were seen as a response to accomplish deeper integration into the global economy, as well as to diminish the negative impacts of globalization, and last but not the least, to cooperate into a better multilateral order. Mercosur was launched in 1991 with the Treaty of Asunción. At the beginning the block was composed by four countries: Argentina, Brazil, Paraguay and Uruguay. Chile joined in 1996 as an associate member, followed by Bolivia in 1997. The goal of the Mercosur treaty was creating a customs union for its members. Three other countries joined Mercosur as associate members in the early 2000's, namely Peru in 2003, and later on Colombia, followed by Ecuador in 2004. The last member to join was Venezuela in 2012, which was nevertheless suspended as a member state in 2016 for failing to incorporate important rules regarding human rights and trade into the national laws (Paraguasu, 2017). The purpose of creating a customs union was aimed at reducing the political instability in the region, resulting after many years of totalitarian governments and dictatorships. In order to understand the following analysis in this chapter, it is important to first explain the underlying structure of Mercosur.

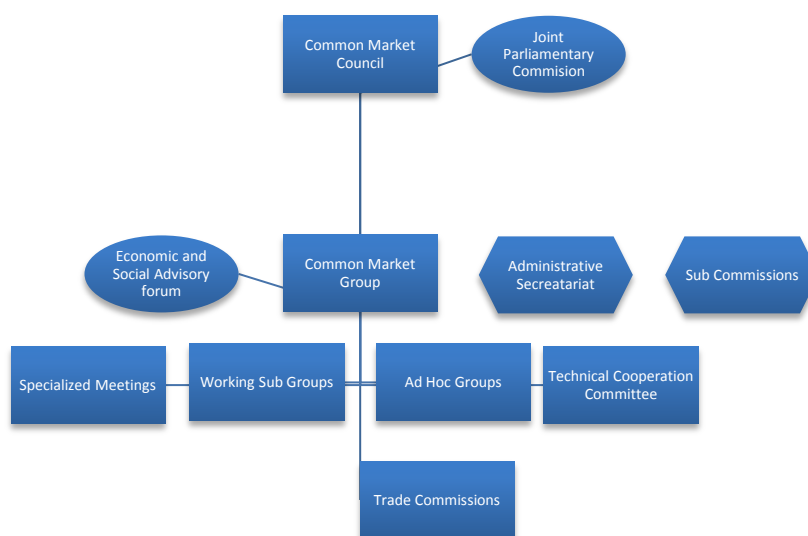


Figure 1. Mercosur institutional structure (Malamud, 2003)

Malamud (2003) describes Mercosur as a hidden source of Presidentialism success experience, where setting up a regional union did not require the use of supranational institutions to be successful, or at least not active one. As it can be observed from Figure 1, Mercosur did establish a supranational structure, but did not grant it an actual autonomy to function. The different Mercosur bodies are mainly comprised by member states public officials and nationally appointed technicians with low levels of responsibility (Ibid), therefore, in Malamud's view, Mercosur is a positive case of an institution which manages to work without the existence of decision-making bodies to solve controversies and where such issues can be solved on a purely intergovernmentalist mechanism-basis. This thesis widely opposes Malamud's argument; this opposition will be later discussed through the 5 different variables, the fact that Mercosur does not have functioning institutions, and is highly reliable on the current president (in particular the Brazilian and Argentinian cases), which has created several constraints regarding political will towards achieving an agreement, as well as in the power the single voice negotiators have been able to achieve when negotiating with the European Commissioners. In summary, Mercosur has no functioning supranational organs, and the relations between members states are mainly determined by the current governments, resulting in high levels of dependency on the relationship between the member states. Furthermore it is also relevant to mention that Mercosur is by nature an intergovernmental body, and it does not function as other international organizations, which hold a tripartite division of the functions. This aspect, as discussed in the following paragraphs, has been an important roadblock in the negotiations between both blocks.

In 1995, Mercosur and the EU signed the Inter-Regional Framework for Co-Operation Agreement (IFCA). The EU had been a constant supporter of Mercosur's integration; the EU's offer of technical assistance to Mercosur in order to aid the completion of the common market through IFCA serves as a proof of such support. One might interpret the EU's support as efforts to help Mercosur achieve its goal of becoming a similar union to that of the EU. However, after closer examination of political discourses and comprehensive study of the negotiation development, it becomes clear that the EU's vision differed greatly from that of member states in terms of the end goals, hence it is possible to suggest that this negotiation did not consider everyone's interests equally from the starting point.

Based on the existing literature and official documents (as listed in the introduction), the following chapter will showcase the reasons behind the failure in the negotiations for the period of 1999 – 2004 through the lense of five variables previously explained in the chapter.

1. Political Will:

This thesis suggests there was in fact an obvious lack of political will on both sides of the negotiations. It can be mainly observed through two key aspects during the above-mentioned period of negotiations: namely, time delays and lack of determination. The first aspect is quite noticeable in the time frame between the signing of the EU – Mercosur Inter-Regional Framework Co-operative Agreement in 1995 and the actual launch of the negotiations in 1999: *“After much dithering, the European Council of Ministers gave the EC go-ahead to begin trade negotiations in 1999”* (Doctor M. , 2015). In order to understand the political will, or lack of it during the first period of negotiations, is it important to look back in time, long before the official negotiations were launched in 1999 (Torrent, 2013). The birth of the EU – Mercosur negotiations could be examined using the concept of *“Path dependence”*: a term commonly used in political science to state that *“Where we are today is a result of what has happened in the past.”* (Margolis). The project (the negotiations) seems to have been doomed from the beginning; a project, launched by a Brazilian Diplomat, Ambassador Jório Dauster, and representatives of two Iberian countries, was very unlikely to go through considering France’s opposition (Albuquerque & Lohbauer, 2013), as one of the big four⁸ countries. According to Guilhon (2013), the main reason why Brazil took part in the signing of the 1995 Framework Agreement was to show the United States that Brazil had more options. Problems arose with the political will’s reinforcement through declarations such as the one of the commissioner for Agriculture of the European Union stating that: *“The European Union has a Common Agricultural Policy. Don’t think that the European Union will change its CAP to make a trade agreement with Mercosur”*⁹. Some other aspects, which demonstrate the lack of political will, is *the absence of President Cardoso during the formal signing of the treaty, because of a trip to China, and who ended up being represented by Planning Minister Jose Serra* (Albuquerque & Lohbauer, 2013), a minister well known for his stance opposed to Mercosur¹⁰. This episode is worthy of consideration, because at that time, China represented a very small fraction of Brazilian exports in comparison with the EU, therefore, reading between the lines it can be interpreted as a silent statement of Brazil’s lack of trust in the scope of the association between the EU and Mercosur.

⁸⁸ *The big four represent Germany, France, UK and Italy. There is a saying the EU which can translate at the Big two (Germany and France) and all the rest* (Albuquerque & Lohbauer, 2013)

⁹ One of the authors attended the seminar representing the Brazilian Minister of Planning and Budget (Albuquerque & Lohbauer, 2013)

¹⁰ <http://plus55.com/politics/2016/06/game-over-mercotur>

Another expression of political will is the lack of determination observed in the structuring of the Association Agreement. This comprehensive agreement (the so-called “umbrella agreement”) can only be concluded once all chapters are negotiated and finalized (Tomazini, 2013). During the First Meeting of the EU- Mercosur Biregional Negotiations Committee, it was agreed that the negotiations “*should constitute a single undertaking to the implemented Parties as an indivisible whole*” (SICE, 2000). Nevertheless, “*No deadline was set, in order to reduce commitment*” (Onuki, 2013). It is well known that the negotiations mostly focused on areas not constituting a real loss for any of the parties. The evidence provided by the OAS (Organization of American States) suggest that the most complicated topics were being pushed for the next round of negotiations, as it will be discussed in the second chapter of this thesis. It is a prevalent pattern at the time when this thesis was written (2017).

The global and local economic and political contexts also played an important role in the political motivations behind this agreement. During the early stages of negotiations there was a time when both parties - the EU and Mercosur - would seek international visibility, and the EU wanted to challenge the United States; a way to demonstrate such intention was through developing closer relationship with Latin America (Onuki, 2013). This was also a period when both parties expressed very positive outlook about the results. As stated in the work programme and agenda of the 1st Meeting of the EU- Mercosur Bi-Regional Negotiations Committee, the information exchange period for the negotiations on trade issues ranged from June 2000 to mid-2001. This round did not produce expected results, and, as we head towards the 24th negotiation round in September of 2017, trade issues are still part of the discussion. When examining the negotiations, the recurrent answer to why negotiations have failed usually is the following: “*The reluctance of the EU towards trade liberalization of agricultural products, plus how sensitive Mercosur is regarding the liberalization of the industrial and services sector, in addition to a lack of offers in the area of government procurement by Mercosur*” (*Ibid*). However, as this section has tried to illustrate, a variety of other reasons behind the failure should not be excluded from the evaluation of all failure catalysts. One of such catalysts - lack of political will - is a key aspect, and one last demonstration of this is the view of the *former president of the MEBF, actively involved into the negotiations, who stated that the “lack of political will would made the entrepreneurs loose their motivation for greater engagement after 2004.”* (Tomazini, 2008)

The following section will examine the issue of institutional capacity, focusing mainly on the Mercosur case.

2. *Regional Institutional Capacity*

Here, it is essential to understand why the EU and Mercosur decided to engage in negotiations in the first place. At the time when the negotiations were launched, the EU widely engaged in promoting its values and securing a place in the international arena. By supporting Mercosur, they were promoting their way of doing things. At the same time Mercosur, which lacked and still lacks resources, hoped that support from the EU would make the project stronger and help acquire funding to fuel its new institutions. From the very beginning of negotiations, regional institutional capacity at the Mercosur level has been a problem when it came to signing an agreement. Mercosur's institutional capacity is poor and very divergent among different member states. It is very hard to have the different players on the Mercosur side speak with a single voice when their views and needs are so different within the regional block.

The literature (Doctor M. , 2015) indicates there is a debate among scholars regarding the impact of inter-regionalism in the definition of Mercosur. While some authors (Phillips, 2003 and Doctor, 2015) believe the association agreement with the EU is what has kept Mercosur together in the first place, other scholars view it in a complete opposite way, arguing that the agreement has in the end posed much more pressure on the Mercosur at a regional level, creating greater disparities within the member states: *"Mercosur's external agenda, it was argued, had forced policy makers into talking issues and formulating common positions before they were ready to do so"* (Doctor M. , 2015). The development of Mercosur nevertheless indicates that even though international agreements might represent some kind of glue, this certainly is not sufficient to encourage member states to give any power whatsoever to supranational institutions, nor has it changed the strong influence of the member states' ruling governments at given times.

Institutional capacity certainly is a key factor when it comes to Mercosur's role on the roadblocks to a successful negotiation is the intergovernmental logic to preserve the national autonomy. This certainly has limited the scope of Mercosur's bodies (Doctor M. , *Prospects for Deepening Mercosur integration: Economic asymmetry and institutional deficits*, 2013), undermining the power of their international negotiators. As mentioned in the first paragraph of this chapter, Mercosur's

supranational bodies are mainly member states' nationally-appointed officers and technicians with low level of responsibilities. Same rule of thumb applies to the negotiators at the negotiation rounds: while the European Union is represented by highly specialized technical experts, Mercosur employs high level officials and politicians whose expertise is inferior to the EU team capacity. These negotiators also have to face the difficulty of not having a single voice, and hence, as it was already mentioned, Mercosur's largest players, namely Brazil and Argentina, have failed to coordinate their policies with third countries:

Argentina's and Brazil's import coverage by Temporary Trade Barriers during the period 1990-2013
(Bown, 2016)

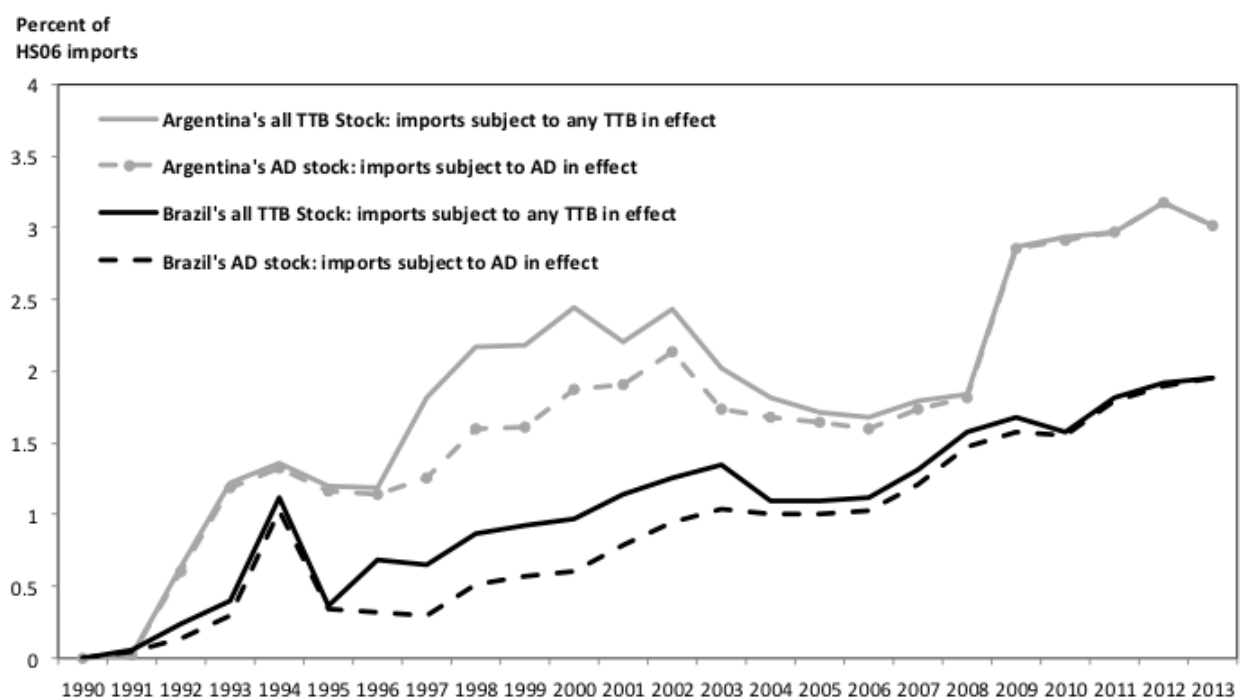


Figure 2: Bown and Tovar (2016, Figure 2) at Bown, 2016

As it can be observed in Figure 2, and according to Bown et al's (2016) analysis of the Temporary Trade Barriers (TTBs) both Brazil and Argentina have been applying since 1990, there is a clear increase in them. In the words of Bown, "However, there are both level differences and inter-temporal differences as to when each country added significant new TTBs. These are the first evidence of an uncoordinated application of the TTB policies by the two countries. (Bown et al,

2016), which in turn mean that the lack of a supranational institution controlling this situations is not only necessary but a must when coming to an EU – Mercosur agreement.

3. *Special and Sectoral Interests*

This section refers to what is commonly known as the “popular” reasons why the negotiations have not been fruitful, and therefore deserves a brief mention only. Tomazini (2013) points out the divergent positions within the business sectors of both blocs. Back in 1998, business representatives from both the EU and Mercosur created the Mercosur European Business Forum aimed at “preparing joint recommendations to the decision makers on how to eliminate trade restrictions, giving the business community a single voice in the negotiations”. Nevertheless this was not the case in practice. Guilhon et al. (2013) elaborate on this point arguing that since 2002 “*a large range of internal resistance from member countries and from European Economic groups who would never be willing to deal with lowering barriers to a number of agricultural products*” (p.21). Since the agri-sector is one of the most well-known roadblocks to the negotiation, and therefore it is certainly an area that cannot be left out from the discussion.

4. *Simultaneous trade negotiations*

At the dawn of the first period of negotiations, the formation of the WTO created an environment of optimism about the globalization of trade. This was also the time when negotiations for the FTAA and Mercosur were taking place. Moreover, FTAA negotiations were happening almost at the same time as negotiations with the EU. Evidently the EU was being used as a bargaining tool during the negotiations with the American counterparts, “*After the relative success of the 2001 Summit of the America’s in Quebec, which reintroduced the FTAA negotiating process, the EU also reacted quickly by resuming negotiations with Mercosur, until the definitive burial of the FTAA in 2004, from which time it advanced no further*”. (Albuquerque & Lohbauer, 2013). The year 2005 saw the weakening of the Free Trade of the Americas, which directly affected negotiations (Onuki, 2013), because Mercosur no longer had a motivation to keep driving the dialogue with the European Union, as it will be later described in the Regional Cohesion section of this paper. The influence of the simultaneous Doha round affected the EU-Mercosur’s negotiations, since sensitive topics for both Mercosur and the EU were being discussed, (i.e tariff concessions to the industry). According to Tomazini (2013), this

had a negative impact on the bloc to bloc negotiations because such sensitive topics were not given deserved attention.

5. *Economic shocks*

While in the 1990's the relations between Mercosur and the EU seemed quite optimistic, the beginning of the year 2000 had a negative effect on the Latin American Bloc. The most important shocks during this period are the 1997- 1998 currency devaluations in South East Asia (Carranza, 2010), which greatly affected the Brazilian economy, and the Argentinian crisis in 2001 (Bown, 2016). Because of the crisis in Brazil, in 1999 the country announced that all negotiations with Argentina would be ceased, in addition to threatening to end Mercosur. The history of Mercosur during this period was greatly affected by the environment. In this case (as well as in other instances) the disputes between the two larger economies of the bloc (the two countries together make up to 80% of Mercosur's GDP), were solved by presidential diplomacy, which takes us back to Malamud's (2003) thesis that Mercosur intergovernmentalism is a case of hidden success for a trade bloc. Nevertheless, this is not the case, as Mercosur's structural cracks keep posing a problem for its regional future partner, the EU, as the internal disputes of the countries and the anarchic behavior of the member states prevail as a liability to the negotiations.¹¹ This topic will be further discussed in the following section; hence, as mentioned in the introduction, the different variables interact with each other and can overlap, such as the economic shocks and regional cohesion.

6. *Regional Cohesion:*

According to Onuki (2013), apart from the French agricultural protectionism and the integration of Eastern European countries, an important factor behind the unwillingness of the EU to make more generous offers were the inconsistencies within the interests of two major powers in Mercosur: Argentina and Brazil. Argentina and Brazil's divergent interests - for instance, their expectations regarding the desired model of integration did not coincide with what the member countries were looking to achieve from their membership in Mercosur. The lack of regional cohesion within Mercosur could be traced back to its origins: why did the countries join Mercosur in the first place?

¹¹ For further details on the effect of economic crisis for Mercosur please refer to Carranza (2010).

Under Menem, Argentina considered Mercosur merely as a tool to become closer to the United States, while for Brazil it was a way to expand its international credibility. Nevertheless, it seems that member states did not foresee the difficulties and resources necessary in order to accomplish successful regional cooperation, namely, common policies, viable supranational organizations, the assumption that some sovereignty will be lost. Onuki (2013) points out that the reason why Mercosur was created was the context of uncertainty in Latin America during the 90's. These were times where many countries had recently come back to democracy and were looking forward to re-joining the international arena. The main problem with this kind of behavior was that the Mercosur project itself did not have a purpose per se, and that member states decided to join by default. The result of it was a project defined by internal crisis of each member state, which in turn paralyzed external negotiations, such as with the EU.

The 1999 -2004 period is marked by 25 rounds of negotiations. This first part of the negotiations ended in 2004, due to a disagreement on the trade pillars, and did not reopen until the year 2010, which will be focus of the following chapter of this thesis.

Chapter 2: Negotiation period 2010 – 2016

After a long period of standstill in the negotiations, they were finally resumed at the EU-LAC summit on May 4th, 2010. Peña (2013) sheds some light as to why the negotiations resumed, defined mainly by the Spanish Presidency. After re-launch, the first round of negotiations was held between June 29^t and July 2nd in Buenos Aires. Several other meetings took place the coming years (9 of them to be more precise), and the negotiations are still an ongoing process – the last round took place in July of 2017. In 2014, former Brazilian President Dilma Rousseff announced that the process would soon come to a successful conclusion, nevertheless once again this was not the case and several rounds of negotiations later there is still no agreement. As this chapter will explain, many of the situations already presented in the last chapter repeat themselves in the second negotiation period, namely a lack of political will and the absence of monetary resources on the Mercosur's side to carry out the negotiation process smoothly. However, this period is marked by some important changes taking place at the presidential level, namely the election of president Macri in Argentina and Venezuela being permanently suspended from the bloc. Concurrently, on the other side we see a very politically unstable Brazil. Once again it is facing a political turmoil due to the newly elected president being formerly charged for corruption, and all these prior disruptions in the political arena can only induce further delays in the negotiation process. As it was previously mentioned in chapter 1, Mercosur is heavily reliable on the political agenda and the currently elected presidents because of its intergovernmental nature.

1. Political Will

On the political will front, first and foremost it is important to highlight how much the negotiations between both blocs depend substantially on the political will of the parties. Arana (2017) points out how important it was to re-start the negotiations and the fact that it was time for Spain to hold the presidency of the EU. As it is of common knowledge, the Spanish have the largest interest in the Latin American region as they have important investments in it, with companies such as ENDESA and Telefonica. But as it was the case during the first round of negotiations, once again the process faces difficulties; A clear example of the lack of political will once negotiations were restarted is the fact that in the early 2010, the discussion did not focus on sensitive topics, but rather on the areas where disagreement was unlikely, mainly international matters, such as foreign aid to Haiti (Onuki, 2013). During the last round of negotiations carried out in July 2017, topics such as subsidies kept

being postponed for the September 2017 round: *“The EU explained its proposal on subsidies and responded to some Mercosur questions. Mercosur remained reluctant to include provisions on subsidies in the agreement. Discussions will continue at the next round. (Commission, 2017).”*

2. Regional Institutional Capacity

In this dimension, the story of the first round of negotiations also seems to repeat itself. Bouzas (in: Carbone, 2015) believes an endemic problem for Argentina in this matter is the *“tradition of conflict and instability of the Argentinian Society, which by definition puts the country in a cyclic path”*¹². He claims the Argentinian political culture really influences the way how the Argentinian actors see the world surrounding them. Their view is one of conflict and because of that their actions also result in conflict, which in turn does not make them attractive as partners (ibid).

Mercosur as a project has also failed to evolve and this (as it happened in the period 1999 – 2004) still relies on the strong inter-governmental approach that Latin American heads of states have towards regional integration. It is illustrated by the fact that even though MERCOSUR installed a parliament in 2006, all decisions had to be made through unanimity, leaving the parliament with little competence and representation. MERCOSUR’s ultimate objective was to move from a customs union into a common market. In order to do so, following the European Union’s experience, this would imply creating an operative regional institution, whose role would be decision making and dispute settlement (Malamud, 2002), but its dispute settlement institutions have only been called 15 times in a timeframe of 20 years (Malamud, 2012). In comparison, the EU Court of Justice makes a 100 rulings every year (Malamud et al., 2007). Hence, MERCOSUR’s dispute settlement body is really inferior to that of the EU.

Malamud (2012) believes that the key precondition to the existence of regional integration is the will from sovereign states to voluntarily transfer parcels of sovereignty to a supranational institution, in his words; *“unlike Europe, the pooling of sovereignty has never been regarded as either a means or an end, and national sovereignty has always been more valued than any potential gains from integration”* (Malamud, 2012, pp.18). Therefore, regional integration in Latin America, as perceived by the EU, is not possible. According to Malamud, Latin America’s “regionalism” is just a tactic to maximize the foreign policy objectives of the contracting governments (Ibid), where small

¹² Translated from Spanish by thesis author.

states are searching for visibility and redistribution and in the case of large states it could be the search for recognition in the international arena, as it is with Brazil. Latin American regional integration is condemned to fail when states are not willing to transfer sovereignty; hence the problems rely on compliance and implementation, and the only way to ensure both of those is to have an effective supranational mechanism to enforce and monitor the agreements between the member states.

During the current round of negotiations (namely XXVIII), the lack of institutional capacity could represent a breaking point in the negotiations. Not having assigned functions makes supranational institutions such as Mercosur too volatile to the ruling governments in its member states; a good example of this is the current Venezuelan crisis, which has Venezuela suspended from the bloc due to not following the rules. This, of course, creates further instability and less trust on the EU side to complete the agreement within the two years Argentina expects it to be completed. Mercosur in the end is just an extrapolation of the strong presidential governments in the region, making Latin America's political culture an important roadblock upon the completion of any agreement, "*... the reluctance to allow any supranational decision-making powers is the main shortcoming hampering deeper integration.*" (Doctor M. , 2015)

3. Special and Sectoral Interests

During the second period of negotiations, Argentina adopted a strong protectionist stance (Tomazini, 2013; Messerlin, 2013). Even though Brazil represented a much better "partner" for the EU, especially during the Doha Round where Brazil was the one pushing towards concessions on the side of the emerging and developing countries, the failure of the negotiations in 2008 and the ensuing economic crisis brought difficulties to their relationship. Since then Brazil also shifted more towards defensive interest for both domestic reasons and due to the international pressure for an anti-trade approach coming from Argentina and Venezuela (Messerlin, 2013). Additionally, there is the issue of the EU deciding to sign a strategic partnership agreement with Brazil, which in the first place according to Doctor (2015) has been the leading member to insist on a strict intergovernmentalism and can therefore be directly blamed for the lack of improvement in the Mercosur project. As it was discussed earlier, the intergovernmentalist nature of Mercosur and the lack of supranational institutions have been and will continue to be an impediment for an

effective agreement. Looking through the same lens of special and sectorial interests, the fact that the EU went ahead with the SPA with Brazil, only created further distrust within the block. The issue with agricultural sector is still strong, *“frequent declarations in EU member countries with strong agricultural interest indicate that, still, is it necessary to overcome many resistances...in order to reach an agreement”* (Peña, 2013).

4. Simultaneous trade negotiations

During this period of negotiations Brazil focused on positioning itself as a leader among the world's poorest countries. This, as argued by Onuki (2013), reduced the significance of more powerful negotiations with major powers, and in turn lowered the disposition Brazil could have had to allocate resources to Mercosur. This is directly connected to the regional institutional capacity, which as mentioned earlier is relatively weak compared to that of the EU. Another important aspect certainly has been the non-completion of the Doha Round, an agreement which just as the EU-Mercosur one must be agreed upon in all aspects before getting approval. While this thesis will not focus on the reasons why the Doha Round has not been completed, nevertheless it is important to mention the failure of the Doha Round to close. Hence, as Messerlin (2013) explains, this (failed Doha Round) has left room for “mega PTA's” between large Asian economies, as well as for the Trans Pacific Partnership (TTP) which was secretly discussed among participating nations for 5 years, and it is now in the process of being approved by each national congress. More importantly, it gives the EU a motive to focus on a different geographical area for its agreements, therefore it comes as no surprise that shortly after Messerlin's (ibid) publication the European Union started negotiations for a Free Trade Agreement with Japan in March 2013, and nowadays in addition to the Free Trade Agreement, a Strategic Partnership with Japan is also being negotiated. (European Commission, 2016).

In 2012, the Council gave the European Commission a mandate for negotiating a PTA with Japan, reading between the lines, this clearly suggested a change of approach by the top EU policy makers (Messerlin, 2013) moving towards larger economies such China. As it can be seen in Figure 3 below, Brazil was far from being attractive trade partner for the EU at the time of the second period of Mercosur negotiations.

	EU Market Expansion (% of EU GDP)		Regulatory quality	
	2010	2030	a	B
EU	100	100	5 to 100	5 to 100
Brazil	12,9	23,5	126	58
Japan	33,9	36,1	20	6
China	36,2	168,6	91	27

Figure 3. * In the table “a” and “b” refer to country rankings, the higher the country’s rank, the poorer is its regulatory performance. “a” is the ease of doing business; “b” is the Overall Index, from the Global Competitiveness index.

Sources: Adapted from Messerlin (2013)

The growing interest in Asia is also seen on the Mercosur’s side. In 2012, Wen Jibiao proposed the idea of a Mercosur – China Preferential Trade Agreement. China has moved extremely fast up in the rank as trading partner with Brazil, up from 12th to 1st in terms of exports, while ranking 2nd in terms of imports (ECLA, 2011). In general, China gained an important position in Latin American economies in a very short period of time (8 years). This rapid change was also accompanied by a rise in commodity prices driven by China, as 60% of Latin American exports to China are natural resources (The Economist, 2012), which made China extremely attractive to the Brazilian market. In contrast to the European Union’s vague definition of a Strategic Partnership, China offers a more concrete description. Chinese Prime Minister, Wen Jiabao defines cooperation in the framework of a Strategic Partnership as follows: “Long-term and stable, transcending both differences and ideology and social systems, and the impact of individual events. Furthermore, it should take place on an equal footing and be mutually beneficial” (Gaens et al., 2009 in Schmidt, 2010). Apart from being more concrete, this definition also acknowledges cooperation between equals, which could interest Latin America.

Just like the European Union, China has deployed a soft power strategy to gain a place in Latin America because it needs Latin America in order to further develop. China positions Latin America as part of their foreign policy objective “Zho Chu Qu” or “going outwards”. In order to further develop, the Asian giant pursues to increase their foreign investment. Such strategy represents a

major difference with the European Union's approach, because the EU does not have the same economic urgency, and therefore not the same degree of interest neither in Latin America, nor Mercosur. According to Cejas (2011), China sees Latin America as a potential consumer: Brazil, Argentina and Mexico represent an important market of 352,1 million people (World bank, 2012). During the visit of the Chinese Prime Minister Wen Jiabao in June of 2012 to Brazil, Uruguay, Argentina and Chile, he expressed the interest of Chinese investors to actively engage in financing concrete infrastructure projects in these countries - for instance, the construction of a US\$900 million solar park in Chile, financing ports in Uruguay and the modernization of the Belgrano Cargas, a railway network in Argentina (The Economist, 2012). Last, but not least, even though Latin America holds closer political and cultural ties with the European Union and in particular with Spain, the normative and less flexible stance the EU has embraced during the last decades has made Latin American governments take a step back. But the key to its soft power lies in the fact that China is expected to have a sustained economic growth in the upcoming years, which in turn represents important opportunities for the Latin American economies, as the trends have already shown in the past years.

5. Economic shocks

The 2008 bubble burst in the U.S. had an extensive impact on the EU's economy. Countries such as Greece and Spain had to deal with tremendous public deficits. Later in 2010, the EU had to for the first time ever ask for a loan from the International Monetary Fund in order to pay its debts. This makes it difficult to believe that determined interest groups would be willing to weaken their strong position towards trade liberalization (Albuquerque & Lohbauer, 2013): *"In the EU, the economic and monetary crisis has captured the full attention of the top decision makers, leaving trade a frozen issue on a sidetrack"* (Messerlin, 2013). *"The economic crisis made the EU to open its markets in priority to economies that fulfilled three conditions: Very large, well regulated and well connected with the rest of the World"* (Messerlin, 2013). Mercosur clearly does not fulfill these conditions and in that sense it makes it hard to believe there will be a consensus in the short term, albeit the political discourse does indicate otherwise.

6. Regional Cohesion

As it happened with the other variables, Regional Cohesion at the Mercosur level prevails in a disadvantaged position. The two main economies of Mercosur still remain Brazil and Argentina, between them accounting for 2.3 trillion USD (The total for the bloc is 2.8 trillion). The main issue is lack of policy coordination: better coordination would substantially improve their negotiating position with third parties. An example of the trade disputes between both economies was the 2011 case when Argentina cancelled automatic licensing for hundreds of imports, creating delays at the ports and contributing to a 15% decline in Brazilian exports (Carranza, 2010).

Chapter 3: Comparative Analysis of the Two Negotiation Periods

The following chapter aims to compare the variable's analysis presented in the previous sections, in order to predict the outcome of the EU Mercosur negotiations, which are still taking place at the time of this research - the next round will be held in September of 2017. When looking at the six categories from the previous chapters, one of the main variables that stands out is the lack of political will to further strengthen Mercosur on the Latin American side, as well as the absence of such will to negotiate on the EU's side. Onuki (2013) sheds some light as to why this happened: *"Actors calculate the costs and benefits, with each side seeking their best outcome... the greatest challenge for a process of integration is the willingness of the countries involved to accept the costs that inevitably arise in the short term, and to have the patience to wait for the benefits...The calculation involves not just material gains but also political risks and the benefits that can be difficult to measure"*. In the case of Mercosur, member states do not feel it is worth to reinforce the project. According to Peña (2013), political will and strategic vision are necessary components for a stable strategic association with a focus on economic integration. Whereas in the first round of negotiations the motivations behind the EU to sign an agreement with Mercosur were to counterbalance the power the US was projecting in the region, during the second round the EU was motivated by the Spanish Presidency which started in 2009. Here, we can find evidence in statements from newspapers of the time, for example in the Argentinian newspaper El Clarin (in Arana, 2017) who published the opinion of a Member of the European Parliament stating: *" ... If with the Spanish presidency there is not progress with Latin America, forget about it"*. In addition, the sub secretariat of economic integration of Mercosur at the time, Eduardo Sigal, also agreed that the

Spanish presidency was a key factor in the improvement of the relationship between both blocs (Ibid).

Other authors have also pointed out the need for a more comprehensive view of the EU – Mercosur Relations, and have tried to explain the reasons behind the lack of political will observed in the relationship between both regions, in spite of the longstanding economic and political ties. Arana (2017) is one of such scholars, offering a similar view to the statement of this thesis, but with a different argument. According to her, the EU has been more responsive rather than a strategic actor when analyzing its relationship with Mercosur. Her research highlights factors such as counterbalancing the US, EU aspirations, the commonly known political and economic ties between both blocs, the EU's desire to expand their model abroad, suggesting those are not sufficient to explain why the relationship formed in the first place. The argument in her case is that the relationship in fact lacks political will, because it was not in the EU's interest, but because Mercosur demanded it. The opposing arguments described in this thesis show that counterbalancing the US was indeed a reason why the EU and Mercosur embarked on the project, as it coincides with the terms under which the negotiations stalled.

Another important variable to take into account is the level of regional cohesion in the Mercosur region. One mistake on the European side when deciding to go-ahead with the agreement with Mercosur was the assumption that the Mercosur countries had a shared political culture and therefore were an easy target to implement the EU's normative power: “ *... there was a strong and oversimplified assumption in Brussels that Mercosur elites shared the same cultural codes and political objectives as their European Counterparts* (Grugel, 2007 in Doctor M. , 2015). As the Mercosur countries share close cultural and historical ties with some of the EU countries (Spain and Portugal in particular), the two regional blocs were in many ways “natural” partners.

The two periods of negotiations do not show significant changes in the analysis of the variables, even though the context is different and the situations do change over time. Ultimately, patterns that led to stalling in the negotiations remain, such as the lack of cohesion of Mercosur, the lack of political will reflected in the negotiations' briefs, with key negotiation areas getting delayed for further rounds. The comparison also showed evidence that the factor economic shock factor is too much related to the regional cohesion and for further studies should be studied in such framework.

Conclusions

When examining the reasons behind the failure of the negotiations, the common knowledge suggests that the deadlock has been caused because of the agricultural products. The entire array of products Mercosur is interested in exporting to the EU are among the 30% of products where the EU exhibits some kind of defensive practice (Albuquerque & Lohbauer, 2013). Another commonly known reason for the failure of the negotiations is the unwillingness of Mercosur member states to be more flexible on negotiation terms. The thesis objective was to explore the roadblocks of the agreement from a more comprehensive perspective in order to showcase the real constraints. The analysis leads to conclude that both aspects mentioned above are only the tip of the iceberg and allow us to reflect on two important issues. First one is an important reason behind the failure of the negotiations, which has not received enough attention by the literature. It is the lack of political will as well as the reasons where this lack of political will comes from. In the case of Mercosur, as it has no “functioning” supranational institutions, political will certainly has a stronger power, which in turn makes the progress of negotiations depend greatly on the elected presidents in the Mercosur member states.

Furthermore, the influence of the geopolitical and economical context has also played a significant role. An example of this was the timing of the first round of negotiations in 2001 during the Fifth Meeting of the Negotiation Committee when the EU agreed to reduce tariffs, but Brazil had already severely suffered from the Real's devaluation, on top of Argentina overcoming the effects of the economic crisis (Onuki, 2013). The impact of the TTP for the EU-Mercosur PTA also deserves a further investigation; if Messerlin's (2013) hypothesis is right, it would suggest that this PTA could have a future in the short run, if the US would re-join before January 2018, hence, in order to protect itself against the TTP, Brazil would or should push for an EU-Mercosur PTA. But on the other hand, because the US has so far dropped out, it could result in the negotiations getting extended for another few years.

After the round of negotiations held at the beginning of October 2016, the future outlook seems more promising, as there is now hope for the agreement to be finally reached after one or two years in light of, among other aspects, the new Argentinian President who has a much more pro – business view of the economy.

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