CEI Centre for International Economy

GLOBAL REPORT

SEPTEMBER 2019

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WORLD

TRADE TENSIONS CONTINUE

During August, China and the United States repeatedly expressed their willingness to reach an agreement to put an end to ongoing trade tensions. However, in the same month they also announced new protectionist measures.

As part of the plan to affect imports for US$ 300 billion announced in July (see Global Report - CEI, August 2019), the U.S. published the list of products to which an additional 10% tariff will be applied in two stages. On 23 August, China announced as retaliation a 10% tariff on imports from the U.S. for US$ 75 billion, which will also be carried out in two steps, between September and December of the current year. In response to these measures, the U.S. reported a further increase from 10% to 15% to the additional tariffs announced in July 2019 and one from 25% to 30% for products that were affected in 2018. In the technological field, the United States extended the authorization to sell supplies or technology to the Chinese telecommunications company Huawei for 90 days, until 18 November.

According to a study by the Peterson Institute for International Economics, if these latter measures are taken into account, U.S. exports to China will be subject to a trade weighted average tariff of 25.9%, compared to the 6.7% rate on imports from the rest of the world. It is worth mentioning that before the onset of tensions, the tariff rate faced by the U.S. was 8%. In the case of reverse trade flows, the U.S. retaliation measures will cover 96.8% of imports from China with a trade weighted average tariff of 24.3% (which stood at 3.1% at the beginning of the trade tensions). Besides, according to the annual survey of the U.S. China Business Council, these trade tensions have damaged 80% of the U.S. companies that do business with China, while 30% agree that they receive an unequal treatment vis à vis Chinese companies.

G7 SUMMIT IN BIARRITZ

The G7 met on 25 and 26 August in Biarritz, France. Within the framework of this meeting, the U.S. and the EU sought to bring together their positions on trade issues. While German Chancellor Angela Merkel stated they could start a broad trade negotiation, but without including agriculture –as demanded by France–, Trump considered that an agreement with the EU is possible so as not to apply additional tariffs to car imports in the context of an investigation on national security threats.

In their brief statement, the G7 leaders signalled their commitment to open and fair trade and to the stability of the global economy. They also expressed their desire to reform the WTO in order to improve its effectiveness with regard to intellectual property protection, to resolve trade disputes more quickly and to eliminate unfair trade practices. According to statements by French President Emmanuel Macron, the latter point is to indicate that multilateral trade rules are needed to deal with certain trade practices of China that they consider unfair.

EUROPE

BREXIT: UNCERTAIN FUTURE WITHIN DAYS OF DEPARTURE DATE

A little over a month after coming to office, Boris Johnson is facing serious difficulties to fulfil his campaign promises of securing a deal or no-deal Brexit on 31 October.

During the G7 summit in Biarritz (see World) Johnson spoke with the EU authorities and published a letter stating his intention to leave with a deal, only if the EU agrees to remove any safeguard on the border with the Republic of Ireland. Otherwise, an exit without agreement would be the most probable outcome.

However, after conservative MP Phillip Lee withdrew his support to the Prime Minister, the members of the British parliament managed to pass a bill giving them the final word on the exit process. Thus, Johnson must reach an agreement with the EU before 19 October or request a new extension to continue negotiating the exit conditions.

At the same time, the leader of the House of Commons, the conservative Jacob Rees-Mogg, has affirmed that the government will try to approve a call for early elections by mid-October. Analysts point out that this could be part of Johnson's strategy of forcing an electoral call that results in a clear and sufficient majority to gain political support in order to carry out a no-deal withdrawal.

While these political ups and downs occur, the UK government is seeking to advance in the conclusion of "continuity agreements" with the countries that trade with the island –in August the agreement with South Korea was confirmed as well as the ratification by the Chilean Senate of another continuity agreement–. Brussels is also working on its contingency measures, as it considers that a "hard" Brexit is the most likely possibility.

ITALY FORMS NEW GOVERNMENT ALLIANCE

After several days of tension within the ruling coalition formed by the Northern League and the Five Star Movement (M5S), the Vice-President of the Council of Ministers Matteo Salvini requested a vote of censure against his own government. This pushed Prime Minister Giuseppe Conte to submit his resignation before the Senate on 20 August and prompted the President of the Republic, Sergio Mattarella, to initiate consultations to explore the possibility of forming an alternative government and avoiding the call for early elections. The result of this troubled August agenda ended in the formation of an alliance between the Democratic Party, the Free and Equal Party and the M5S, a change that reduces representativeness to the benches of Eurosceptic leaders and opens the possibility for the new Italian government to adopt a pro-European imprint.

The reactivation of the economy is one of the great challenges the new ruling alliance will have to address. Although the financial markets have reacted positively to these political changes, one of the pressing issues that should be resolved is the deficit in the public budget that brings about a conflict with the EU requirements. In this regard, in August, one of the main issues under discussion was the way to avoid a further increase in VAT on goods and services scheduled for 2020 and 2021 –the reduced rate would rise from 10% to 13% and the ordinary from 22% to 26.5%–. Even though this measure would strengthen the government coffers, it could also contribute to slowing the country's economy.

ADVANCES IN THE EU-MEXICO AGREEMENT RENEGOTIATION

The Head of the Delegation of the European Union in Mexico, Klaus Rudischhauser, announced in August that the negotiation for the renewal of the Economic Partnership Agreement in force between the parties is expected to be concluded before the end of 2019. The only chapter still pending is the one related to public procurement, which would allow companies from the signatory countries to participate in the tenders of the European and Mexican local administrations. The renovated agreement would also incorporate as a new feature the liberalization of the farming sector.

SOUTH AND CENTRAL AMERICA

MERCOSUR AND EFTA FINALIZE NEGOTIATIONS FOR AN FTA

Mercosur concluded the negotiations for the free trade agreement with the European EFTA bloc, made up of Switzerland, Iceland, Norway and Liechtenstein. These countries, with a population of 14 million people, are among those with the highest purchasing power in the world and their combined GDP exceeds a trillion dollars. They have a prominent participation in the global trade in goods and services, which would strengthen the bilateral exchange between the two blocs, currently amounting to US$ 7 billion annually.

With regard to market access, the agreement grants preferential treatment to 97% of Mercosur's exportable offer. In addition, Switzerland and Norway have granted several bilateral quotas to the bloc, as well as 0% intra-quota tariffs for some of the WTO's consolidated tariff-rate quotas on agriculture. The agreement also covers regulatory issues, in terms of services, investment, public procurement, non-tariff measures, intellectual property and sustainable agriculture, among others.

THE UK GRANTS FUNDS FOR THE DEVELOPMENT OF BRAZIL

Brazil and the United Kingdom have signed a memorandum of understanding whereby the former will receive 100 million reals from the United Kingdom Prosperity Fund, designed to boost economic growth in developing countries. In particular, the resources will be allocated to the integration of SMEs to global value chains, to the improvement of operational efficiency in the ports, to Brazil's process to enter the OECD, to intellectual property provisions and to regulatory matters. Likewise, the fund will invest about 400 million reals in different sectors of Brazil, for projects related to trade facilitation, business environment, energy, smart cities, green finance and health.

NORWAY AND GERMANY REDUCE FINANCIAL SUPPORT TO AMAZON RAINFOREST

In a context of claims to Bolsonaro's administration for fires in the Amazon rainforest, Germany announced a budget cut for projects in that area. Norway followed suit, suspending its economic participation in the Amazon Fund. This fund has been collecting donations since 2008 to finance sustainable development projects in the Brazilian Amazon, and Norway has historically been its largest contributor.

BRAZIL PREPARES ITS PRIVATIZATION PROGRAMME

The Brazilian government announced that nine more state-owned companies would be included in its "destatisation" programme, including the postal service –Latin America's largest logistics company– and the Port of Santos, the most important in Brazil. If the announcement is materialised, the country is expected to raise 2 trillion reals, part of which would be used to finance public education for children.

In addition, public-private partnerships will be held in areas such as street lighting, prisons, sewage and solid waste; and the possibility of concessions of national parks is being analysed.

CHILE STRENGTHENS TRADE TIES WITH INDIA

Chile and India have strengthened their trade ties within the framework of August's G7 summit. On the one hand, they signed a cooperation agreement whereby the Indian pharmaceutical companies will be able to participate in the bidding for the purchase of medicines made by Chile through the Supply Centre of the National Health Service System. On the other hand, both parties highlighted their willingness to extend the partial scope agreement that they currently have in force to one of free trade.

NORTH AMERICA

THE U.S. CONSIDERS RETALIATION AGAINST FRANCE'S DIGITAL SERVICES TAX

In August, the United States Trade Representative (USTR) called Google, Facebook and Amazon to testify within the framework of the investigation carried out under section 301 of the U.S. Trade Act regarding the 3% tax on digital services imposed by France last month. The companies warned that this Digital Services Tax (DST) would affect their operations and the additional costs would be transferred to consumers.

The French DST seeks to tax the multinational technological companies until the OECD and the G20 agree on a common policy on the matter (see Global Report - CEI, August 2019). Due to the fact that most of the affected companies would be North American, Donald Trump's government does not rule out implementing retaliations in the form of tariffs on French wine.

In turn, several European countries are considering implementing some type of DST since, among other reasons, said companies do not declare their revenues in the country of origin of the economic activity, but rather they do so in other countries with lower tax requirements.

NEW TRADE AGREEMENT BETWEEN THE U.S. AND JAPAN

Within the framework of the G7 summit, U.S. President Donald Trump and Japanese Prime Minister Shinzo Abe agreed on the signing of a trade agreement next September during the General Assembly of the United Nations.

According to information released to the press, the agreement would tackle issues related to agricultural, industrial and digital commerce, with the exception of the automotive sector. Through the White House Twitter account, it was stated that Japan would buy the maize that the U.S. has ceased to export to China due to the current trade tensions. Abe, in turn, remarked that the maize purchases would make it possible to solve the shortfall resulting from pests in Japan's crop fields.

The agreement –reached after a little more than five months of negotiations– seeks to enable the U.S. to have the same trade conditions with Japan as the members of the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP), from which the U.S. withdrew in December 2018.

The conclusion of the negotiations for the agreement takes place in parallel with the entry into force of a protocol on tax treaties. According to Steve Mnuchin, United States Secretary of the Treasury, this will significantly reduce taxes on interests, royalties, some direct dividends and capital gains, favouring investment flows between the countries in question.

CANADA EXPANDS ITS AIR TRANSPORT AGREEMENT WITH CHILE

Canada and Chile have expanded their air transport agreement, which will give airlines more flexibility to operate passenger and cargo services with stops at a third country, if the final destination is one of the two countries in the deal. In a news release, Canada highlighted that the measures will help the air industry increase its access to international markets. Canada and Chile have had a free trade agreement in force since 1997, which was updated last February.

MEXICO CLOSES OVERSEAS TRADE OFFICES

The Mexican government has decided to close its trade representations in China, Japan, Belgium, Uruguay, Canada and France and use the embassies to promote business and investment. The government bases this decision on its austerity policy, although it guarantees that the closing of the trade representations overseas does not pose any risk to commercial or investment flows.

ASIA AND AFRICA

MOUNTING TENSIONS BETWEEN JAPAN AND SOUTH KOREA

Amidst the growing trade dispute between Japan and South Korea, both countries decided to implement restrictions to their bilateral trade. On the one hand, Japan excluded South Korea from its "white list" of 27 trading partners to which it applies minimum restrictions for the exports of sensitive products that could be used in the arms industry. The measure has been in force since 28 August and is framed within a safety measure in exports control. On the other hand, this country considered that the measure was ill-founded and removed Japan from its list of trusted trading partners, being this a category that grants exporting preferential treatment, as of September. In addition, South Korea officially announced on 22 August it will not renew the General Security of Military Information Agreement (GSOMIA) with Japan.

Said measures take place in a context of conflict between both countries which results from the South Korean Supreme Court ordering some Japanese companies, including Nippon Steel and Mitsubishi Heavy Industries Ltd., to compensate the victims of unpaid forced labour during the Japanese colonization between 1910 and 1945. Japan alleges that the issue is already regulated by the 1965 bilateral agreement. These tensions give rise to uncertainty in the negotiations of the Regional Comprehensive Economic Partnership (RCEP) and in those of the People's Republic of China, Japan and South Korea Free Trade Agreement.

ISRAEL AND SOUTH KOREA CONCLUDE NEGOTIATIONS FOR AN FTA

After almost three years, South Korea and Israel concluded the negotiations for the signing of a free trade agreement. Once it becomes effective, most Israeli exports to the South Korean market will be exempt from tariffs, including machinery and electrical equipment, mechanical devices, fertilizers, medical equipment, cosmetics, plastics, metals, fruit juices and wines. At the same time, duties on products from South Korea imported into Israel, such as automobiles and autoparts, refrigerators, medical equipment, electronic components, toys, plastics and chemicals, will be reduced.

Israel described the agreement as "historic" and it was the first signed with a country from East Asia. South Korea leads the production of memory components and is second in that of semiconductors. Likewise, it is the major shipbuilder in the world and its automotive industry is considered one of the best globally.

SOUTH KOREA RATIFIES FTA WITH CENTRAL AMERICA

South Korea ratified in August its Free Trade Agreement with the Central American Common Market (CACM), bloc of five Central American countries –Costa Rica, El Salvador, Honduras, Nicaragua and Panama–. These Central American countries must now conclude their own legislative approval so that the agreement becomes effective –except for Nicaragua and Costa Rica, where this is a fact already and the agreement will be operative as of October–.

Guatemala, another member of the bloc, was finally not included in the agreement although it had participated in the first rounds of negotiations. Nevertheless, President Jimmy Morales assured that he will seek his country's adherence in 2019. The National Coffee Association (Anacafé, for its name in Spanish) is one of the sectors actively demanding an FTA with South Korea.

Ministry of Foreign Affairs and Worship
Argentine Republic

Closing date of this issue: 30 August 2019