MERCOSUR-SOUTH KOREA TRADE AGREEMENT:
A FRAMEWORK FOR AN INNOVATIVE PROPOSAL

Denise Gregory
Nicolás Albertoni
Kisu Kwon
Misook Park
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Study Group on Regulatory Innovations

FINAL REPORT

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Denise Gregory
Nicolás Albertoni
Kisu Kwon
Misook Park

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I. Introduction
Although Mercosur and South Korea present a weak trade flow and investment integration, they show an excellent complementarity potential to increase both. The Mercosur-South Korea Free Trade Agreement (FTA) is an ambitious trade deal and the first being negotiated by Mercosur with an Asian country. Negotiations were launched in May 2018, and its seventh round took place virtually in September 2021. So far, some of its Chapters have already been closed: Trade Competence, Sustainable Development, Dispute Resolution, and Cooperation (still open the indication of sectors). Negotiations are slow regarding Chapters on Market Access for Goods and Services, Rules of Origin, Sanitary and Phytosanitary System (SPS), Technical Barriers to Trade (TBT), and Government Procurement.

The FTA Agreement has found resistance from the Korean agricultural and Mercosur manufacturing sectors. The pressure on the Argentine side led the government to decide in April 2020 to withdraw from the ongoing Mercosur negotiations to liberalize trade in goods, including the FTA with Korea. Nevertheless, Argentina may join the agreement later, based on what the other three bloc members will have negotiated. When extended to trade in goods, the scenario of different speeds in preferential agreements creates non-trivial problems for managing the common trade policy and the free circulation of goods within Mercosur.

It is crucial to advance negotiations in those areas in which Korea and Mercosur are most sensitive, including mechanisms that will allow a considerable reduction in tariff and non-tariff barriers.
This Project offers a unique opportunity for the International Intelligence Unit from Fundação Getulio Vargas and The Korea Foundation to contribute to a more innovative agreement regarding (i) joint initiatives in technical cooperation, (ii) local payment currency systems, (iii) disciplines on non-tariff barriers, (iv) normative coherence and harmonization, (v) support programs for raising the SMEs utilization of the FTA, and (vi) a regular business forum. Our Regulatory Innovations Study Group brought Mercosur and South Korea experts to review the literature, meet and debate virtually with trade experts from the academic, private, and public sectors to gather and propose a set of policy-oriented recommendations for Mercosur and Korea FTA government negotiators.

Section II summarizes the key steps and advancement of the FTA negotiations so far. In Section III, we present data on the bilateral trade in goods and a short analysis of both sides’ offensive and defensive interests and the main sectors affected by protectionist measures implemented by Korea toward Mercosur and vice versa. In Section IV, we analyze the literature review to outline the perceptions on the FTA from the sensitive sectors of Mercosur and Korea. Moreover, we identify the potential to cooperate in non-sensitive areas. Section V points out some countries’ positions, divergences, and challenges to conclude FTA. It incorporates contributions from the interviews with trade experts from both sides. In Session VI, the Group makes recommendations to the negotiators on regulatory innovations and novelty aspects.
II. Mercosur-South Korea FTA Background
In 2005, Mercosur and the Republic of Korea initiated a joint study to explore the feasibility of a Mercosur-Korea free trade agreement. The first meeting for that study group took place in Asunción, Paraguay, in May 2005. The second meeting was in August 2005 in Seoul, Korea.

In March 2017, Mercosur and Korea completed their exploratory conversations with a solid commitment to negotiating a trade agreement in the future. As a report from the SICE (OAS Foreign Trade Information System) highlights, “The Chief Negotiators of Mercosur and the Vice-minister of Trade and Investment of the Republic of Korea met in Buenos Aires, Argentina, on December 10, 2017, and agreed on the importance of quickly initiating negotiations for a Trade Agreement between Mercosur and Korea.”


As SICE outlines “The first round of negotiations took place in Montevideo, Uruguay on September 11-14, 2018. The second round of negotiations concluded in Seoul, on April 6, 2019. The third round was held in Montevideo, Uruguay, on July 8-12, 2019. The fourth round of negotiations ended, on October 4, 2019, in Busan, Korea. The fifth round of negotiations took place in Montevideo, Uruguay on February 10-14, 2020. On March 3, 2020, Mercosur and Korea met in Seoul to review the status of the negotiations for the signing of a Mercosur-Korea trade agreement.”

Finally, in August/September 2021, the 7th Round of Mercosur and Korea negotiations were held in virtual meetings by the Market Access Groups on issues related to Goods, Trade in Services, E-commerce and Investments, Rules of Origin, Sanitary and Phytosanitary Measures, Institutional Affairs, Intellectual Property Rights, Trade Defense, Government Procurement, and Technical Barriers.

**TABLE 1: Summary of key steps in the negotiations of the agreement**

<table>
<thead>
<tr>
<th>Date</th>
<th>Key steps</th>
</tr>
</thead>
<tbody>
<tr>
<td>04-05 May 2005</td>
<td>Asunción, Paraguay. Results of the first meeting for a joint study on Mercosur-Korea trade agreement</td>
</tr>
<tr>
<td>17-18 August 2005</td>
<td>Seoul, Korea. Second meeting for a joint study on Mercosur-Korea trade agreement</td>
</tr>
<tr>
<td>02 March 2017</td>
<td>Buenos Aires, Argentina. Mercosur and Korea conclude exploratory talks for a trade agreement</td>
</tr>
<tr>
<td>10 March 2017</td>
<td>Mercosur and Korea agree on beginning trade talks</td>
</tr>
<tr>
<td>25 May 2018</td>
<td>Seoul, South Korea. Mercosur and South Korea launch trade negotiations</td>
</tr>
<tr>
<td>11-14 September 2018</td>
<td>Montevideo, Uruguay. The first round of trade negotiations</td>
</tr>
<tr>
<td>01-06 April 2019</td>
<td>Seoul, South Korea. The second round of trade negotiations</td>
</tr>
<tr>
<td>08-12 July 2019</td>
<td>Montevideo, Uruguay. The third round of trade negotiations</td>
</tr>
<tr>
<td>04 October 2019</td>
<td>Busan, Korea. The fourth round of trade negotiations</td>
</tr>
<tr>
<td>11 February 2020</td>
<td>Montevideo, Uruguay. The fifth round of trade negotiations</td>
</tr>
<tr>
<td>03 March 2020</td>
<td>Seoul, Korea. Mercosur-Korea meeting</td>
</tr>
<tr>
<td>31 May-04 June 2021</td>
<td>The sixth round of trade negotiations (virtual)</td>
</tr>
<tr>
<td>30 August -09 September 2021</td>
<td>The seventh-round of trade negotiations (virtual)</td>
</tr>
</tbody>
</table>

Source: SICE (2021) based on Mercosur, Ministry of Foreign Affairs and Trade of Korea; Ministry of Trade, Industry and Energy, Korea; Ministerio de Relaciones Exteriores y Culto, Argentina; Ministério das Relações Exteriores, Brazil; Ministerio de Relaciones Exteriores, Paraguay.
III. Trade Policy Data of the Relationship between Mercosur and Korea
While Korea exports to Mercosur mainly manufactured goods, such as electrical articles, wireless communication apparatus, electron tubes, and computers, Mercosur exports mostly primary products or low value-added primary processed goods to Korea, such as minerals, soybean oil, flours derived from the extraction of soybean oil and cereals.

Mercosur’s offensive interests rely on increasing export opportunities to the Korean market by removing or significantly reducing its import tariffs and adding new or expanding current TRQs (tariff rate quotas) for agricultural products. It has a strong comparative advantage. The latter include beef, poultry, ethanol, cereals, rice, and ores. Mercosur’s defensive interests have been negotiating long phase-in periods for tariff cuts for Korean industrial goods, such as electrical machinery, vehicles, and car parts, and escalating its protected industries’ exposure to competition. In addition, a sensitive issue in the negotiations with South Korea is sanitary and phytosanitary measures. The country is known for its highly complex and discretionary sanitary and phytosanitary measures regime, and Mercosur demands advancement concerning those disciplines beyond those of WTO SPS.

In the manufacturing sector, Korea has offensive interests. Its manufactured goods, such as motors and electronics, are competitive globally. Electrical machinery and equipment, machinery, mechanical appliances, vehicles, and plastics are Korea’s leading exports to Mercosur. Korean exporters argue that the Mercosur market’s high tariffs are the major obstacle to trade. Nonetheless, they are firmly to support an FTA with Mercosur.

The Mercosur-Korea FTA has also been seen as a strategic instrument to revitalize Mercosur’s internal convergence and foster its integration into global value chains through ambitious modern and preferential trade deals.
Meanwhile, Korea maintains a defensive stance on opening agricultural markets. Even though Korea imports a large share of agricultural products, certain domestically produced items are directly linked to the survival of Korean farmers. Those items cannot entirely depend on imports. In addition, the Korean government is committed to protecting food security for future generations.

The Mercosur-Korea FTA has also been seen as a strategic instrument to revitalize Mercosur’s internal convergence and foster its integration into global value chains through ambitious modern and preferential trade deals.

Figures 1 and 2 show the exports trend from Korea to Mercosur and vice versa. First, it is possible to identify that exports from Korea to Brazil represent, on average, 84% of total exports to Mercosur between 2009-2020, with Argentina accounting for 10%, Uruguay and Paraguay for 2% each.

**FIGURE 1: Exports trend from Korea to Mercosur**

![Graph showing exports trend from Korea to Mercosur](source)


**FIGURE 2: Mercosur’s exports to Korea**

![Graph showing Mercosur’s exports to Korea](source)

In terms of bilateral trade, Tables 2 and 3 show the main sector’s exports from Korea to Mercosur and vice versa.

**TABLE 2: Top 5 Sectors in Korea’s exports to Mercosur between 2018-2020**

<table>
<thead>
<tr>
<th>Sector</th>
<th>Average in total exports from 2018 to 2020</th>
</tr>
</thead>
<tbody>
<tr>
<td>Electrical machinery and equipment and parts thereof (product code 85)</td>
<td>32%</td>
</tr>
<tr>
<td>Machinery, mechanical appliances, nuclear reactors, boilers (product code 84)</td>
<td>14%</td>
</tr>
<tr>
<td>Vehicles other than railway or tramway rolling stock (product code 87)</td>
<td>17%</td>
</tr>
<tr>
<td>Plastics and articles thereof (product code 39)</td>
<td>7%</td>
</tr>
<tr>
<td>Pharmaceutical products (product code 30)</td>
<td>3%</td>
</tr>
</tbody>
</table>


**TABLE 3: Top 5 Sectors in Mercosur’s exports to Korea between 2018-2020**

<table>
<thead>
<tr>
<th>Sector</th>
<th>Average in total exports from 2018-2020</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cereals (product code 10)</td>
<td>19%</td>
</tr>
<tr>
<td>Ores, slag, and ash (product code 26)</td>
<td>17%</td>
</tr>
<tr>
<td>Residues and waste from the food industries (product code 23)</td>
<td>15%</td>
</tr>
<tr>
<td>Beverages, spirits, and vinegar (product code 30)</td>
<td>7%</td>
</tr>
<tr>
<td>Mineral fuels, mineral oils, and products of their distillation (product code 27)</td>
<td>5%</td>
</tr>
</tbody>
</table>


The following two charts show the trade policy measures implemented between Korea and Mercosur. **As expected, Korea’s measures toward Mercosur (3 liberalizing and 3 protectionist measures on average between 2009 and 2021) were fewer than Mercosur’s measures in Korea (34 liberalizing and 38 protectionist measures on average between 2009 and 2021).**
Tables 4 and 5 show the main sectors impacted by policy measures implemented by Mercosur toward Korea and vice versa. The first table shows that the main sectors impacted by protectionist measures implemented by Mercosur in Korea were motor vehicles and electric motors, among others. At the same time, Mercosur countries have also implemented liberalizing measures, which positively impacted Korean sectors such as instruments & control equipment, other special-purpose machinery, among others.
The following table shows that the main sectors impacted by protectionist measures implemented by Korea toward Mercosur were food products, prepared & preserved fish, among others. At the same time, Korea has also implemented liberalizing measures, which positively impacted Mercosur sectors, such as prepared & preserved fish, cereals, and basic organism chemicals, among others.

### TABLE 4: Trade Policies and Sectors Impacted by Measures Implemented from Mercosur Toward Korea

<table>
<thead>
<tr>
<th>Sector</th>
<th>Interventions</th>
<th>Sector</th>
<th>Interventions</th>
</tr>
</thead>
<tbody>
<tr>
<td>Motor vehicles, trailers &amp; semi-trailers; parts</td>
<td>81</td>
<td>Instruments &amp; control equipment, except optical instruments</td>
<td>138</td>
</tr>
<tr>
<td>Electric motors, generators &amp; transformers; parts</td>
<td>63</td>
<td>Other general-purpose machinery &amp; parts</td>
<td>115</td>
</tr>
<tr>
<td>Other fabricated metal products</td>
<td>58</td>
<td>Other general-purpose machinery &amp; parts</td>
<td>99</td>
</tr>
<tr>
<td>Other general-purpose machinery &amp; parts</td>
<td>57</td>
<td>Other electrical equipment &amp; parts</td>
<td>91</td>
</tr>
<tr>
<td>Other special-purpose machinery &amp; parts</td>
<td>49</td>
<td>Pumps, compressors, hydraulic &amp; pneumatic power engines; parts</td>
<td>91</td>
</tr>
</tbody>
</table>

Source: Global Trade Alert, 2021.
* Until October 2021

### TABLE 5: Trade Policies and Sectors Impacted by Measures Implemented from Korea Towards Mercosur

<table>
<thead>
<tr>
<th>Sector</th>
<th>Interventions</th>
<th>Sector</th>
<th>Interventions</th>
</tr>
</thead>
<tbody>
<tr>
<td>Food products n.e.c.</td>
<td>5</td>
<td>Prepared &amp; preserved fish, crustaceans, molluscs</td>
<td>11</td>
</tr>
<tr>
<td>Prepared &amp; preserved fish, crustaceans, molluscs</td>
<td>5</td>
<td>Cereals</td>
<td>10</td>
</tr>
<tr>
<td>Basic organic chemicals</td>
<td>4</td>
<td>Basic organic chemicals</td>
<td>6</td>
</tr>
<tr>
<td>Other electrical equipment &amp; parts</td>
<td>3</td>
<td>Oilseeds &amp; oleaginous fruits</td>
<td>6</td>
</tr>
<tr>
<td>Petroleum oils &amp; oils of bituminous materials, other than crude</td>
<td>3</td>
<td>Sugar &amp; molasses</td>
<td>5</td>
</tr>
</tbody>
</table>

Source: Global Trade Alert, 2021.
* Until October 2021
IV. Mercosur and Korea’s perception of the FTA
Sensitive sectors’ position on FTA

The feasibility of a Mercosur-Korea FTA was discussed for more than 20 years. Nevertheless, the positions of major economic sectors have changed little in the past years. The agriculture of Korea and the industrial sector of Mercosur are reluctant to open their market to other parties.

Barbieri and Pedrozo (2009) evaluated the agriculture of Korea and the manufacturing sector of Mercosur as the main obstacles to the FTA. While agricultural products are where Mercosur countries have their best comparative advantage, Korea applies a high tariff on them. Even if Korea needs foreign agricultural products, at the same time, it is forced to defend and maintain a food security policy for the next generation. Accordingly, the study argues that it will be difficult for Mercosur to obtain advantageous concessions from Korea in the agricultural sector. Another obstacle is a lack of coordination among Mercosur countries to apply its Common External Tariffs (CET). Although Mercosur adopts the CET, general exceptions are allowed for capital assets and goods related to technology and telecommunication. The members of Mercosur can modify the applications of the CET and have temporary exception lists. This measure is to protect each country’s sensitive manufacturing sector.

Considering the protective stance of Korean agriculture and Mercosur’s manufacturing sector, Barbieri and Pedrozo (2009) propose a Preferential Trade Agreement (PTA) – a limited market opening, rather than a FTA. It suggests that a PTA is the first integration step, and the parties ultimately will negotiate an FTA in long-term interest.

Nowadays, Argentina still makes a similar argument, where it wants to exclude its sensitive manufacturing sector from extensive market opening. A PTA, however, is not a feasible option, since Korea and the agricultural sector of Mercosur insist on a comprehensive market-opening agreement. The National Confederation of Agriculture of Brazil (CNA) suggests that only a broad and ambitious agreement would result in concrete gains for exporters of agricultural products in Brazil. CNA (2020) argues that a limited agreement would not contemplate Brazil’s potential to benefit from the South Korean market.
Korea’s Industry

In August 2021, the Ministry of Trade, Industry, and Energy of Korea held a video conference to update the Korea-Mercosur FTA negotiations and seek industry feedback. The conference was attended by fifteen industry associations, such as the Automobile Industry Association, Petrochemical Association, Fine Chemical Industry Promotion Association, Steel Association, Semiconductor Association, Display Association, Machinery Industry Promotion Association, Machine Tool Industry Association, Bio Association, and Electronic Information and Communication Industry Promotion Association. Participants at the conference discussed the necessity of concluding a Korea-Mercosur FTA and exchanged views on a wide range of topics, including promising areas for Korea-Mercosur cooperation and difficulties in entering the Mercosur market. Those industry associations agreed that an early conclusion of the Korea-Mercosur FTA was necessary given the growth potential of the Mercosur and expressed their hope that Korean companies would expand their business into Mercosur in the future. They also mentioned that the Korea-Mercosur FTA is expected to not only enhance price competitiveness through tariff cuts but also introduce a unified rule of origin, eliminate non-tariff barriers, and raise the level of regional norms, such as intellectual property, and strengthen the protection of Korean corporate rights.

The Korean Institute for International Economic Policy (KIEP) conducted a survey asking Korean companies for their opinions on the conclusion of an FTA (Kim et al., 2011). The respondents were 48 exporters to the Mercosur market. The Korean companies responded that the rise of competing countries (22.8%), high tariffs (17.1%), and complicated customs procedures (14.6%) were obstacles in exports to Mercosur. 80.4% of the firms supported the Korea-Mercosur FTA in order to tackle those obstacles, 59.1% expected tariff reduction or elimination, and 28.8% hoped to simplify customs procedures.

Korea’s Agriculture

Trade negotiations are governed by the ‘give and take’ principle. It is essential to give one in order to get one. As Korea depends on trade, it has deliberately opened its market through FTAs. The agricultural sector views itself as the one to give up, while the manufacturing sector rewards. Several studies support this opinion, which is why the Korean agricultural sector is sensitive to market opening.

The Korea Rural Economic Institute (KREI) did research titled “The Impact of Free Trade Agreements (FTAs) with Latin American Countries on the Agricultural Sector” prepared by the Ministry of Agriculture, Food and Rural Affairs. The study states that if the Korea-Mercosur trade agreement went into effect, the domestic agricultural sector would suffer an impact of up to 2.1 billion dollars over 15 years (Farmers Newspaper, 2018).
According to “The impact of 9 FTAs on the industry for the last five years”, a report proposed by the Ministry of Trade, Industry and Energy submitted to Seo Sam-seok, a member of Parliament, the agricultural and fishery lost 390 million dollars production, while the increase in production in the manufacturing sector reached 55 billion dollars. This analysis results from part of the FTAs that entered into force in Korea as of June 2021. The damage to the agricultural and fishery sectors is expected to be significantly greater if all the 17 FTAs have entered into force are targeted (Farmers newspaper, 2021).

Using the dynamic analysis method, KREI assessed the impact of 14 FTAs on the domestic agricultural sector. Han et al. (2017) indicate that agricultural production decreased by an average of 0.4% per year between 2004 and 2015. The sectors with the most considerable losses were livestock and fruit.

KREI analyzed the increase in imports and exports in agricultural and livestock products during the ten years of the Korea-EU FTA. Kim et al. (2021) found that imports from the EU increased by 132% in 10 years since the Korea-EU FTA was implemented in July 2011. On the other hand, Korea’s exports to the EU increased by only 65.7%.

Mercosur’s Industry

As Korea is a strategic market and a vital partner for trade and investments, the Brazilian National Confederation of Industry (CNI) conducted a study (2020), selecting Korea as one of its ten priority markets for the Brazilian industrial sector. Nevertheless, CNI reiterates its sensibilities about an FTA with Korea. A 2020 impact analysis (using the Global Trade Analysis Project model - GTAP) found that a broad Agreement would harm 51 sectors (25 in the industrial sector, 18 in the services sector, and 8 in the agricultural sector) while benefiting just 11 sectors. They reported losses in capital goods, electronics, auto parts, and textiles. Since Korea’s agricultural sector is highly protected, Mercosur’s major market gain would be limited to a few products such as grains.

In April 2020, the Argentine Industrial Union and the CNI Brazil issued a Joint Declaration requesting the Mercosur governments to carry out consultations with the private sector before the conclusion of negotiations to address issues of concern to the industrial sector, which include:

- the private sector’s lack of knowledge about the content of offers that had already been exchanged;
- the knowledge that the previously traded proposals (Chapter on Market Access of Goods) had covered 90% of the tariff universe and the trade value, leaving little room for dealing with sensitivities issues;
- the high concentration of production in a few and large Korean companies in sectors such as electronics, steel, chemicals, and automobiles, gave those companies better conditions for international competition.
Mercosur’s Agriculture

The agricultural sector of Mercosur is widely regarded as one of the major beneficiaries of the bloc’s Trade Agreement with South Korea. Rural associations from all participating countries expect an agreement to reduce Korean protectionist measures and boost Mercosur exports to Korea. The Federation of Rural Associations from Mercosur’s (FARM) response to Argentina’s withdrawal from the FTA negotiations showed this favorable position. The FARM lamented the decision and urged the Argentinian government to return to the negotiating table, recognizing the agreement’s importance to the overall sector.

The study conducted by the Brazilian National Confederation of Agriculture and Livestock (CNA) may help to understand better the expected impact of the trade agreement in the sector. According to CNA (2020), Korea is a large importer of agricultural products, while Brazil is the world’s third-largest agricultural exporter. However, despite such complementarity, the Brazilian exporters face some challenges in the Korean market. In addition to the high competition from other countries’ goods, some domestic policies, such as production subsidies and high tariffs, can make it difficult to export several products.

CNA (2020) argues that Korea is more protectionist in the agricultural sector. Agricultural tariff reductions were slower than other sectors when analyzing Korea’s FTA with China, the USA, the EU, New Zealand, and Australia. Quotas, special tariff reductions, and exclusion of products happened occasionally. The average tariff for agricultural products is about six times higher than in mining and industry.

According to CNA (2020), at least 31 Brazilian goods from 11 agricultural sectors face tariff peaks in South Korea, with rates of 41.7%, equal to or higher than three times the average Korean tariff (13.9%). High tariffs significantly impact the mining industry, malt, starches, inulin, and wheat gluten, followed by cereals and vegetables, plants, roots, and edible tubers sectors. South Korea applies a tariff of over 800% to some of these items. Furthermore, “Brazilian agricultural exports are also affected by non-tariff barriers, such as: sanitary and phytosanitary barriers (as in the case of fruits), the lack of an international export certificate (as in the case of live animals and fruit), the South Korean policies to encourage and support domestic production (as in the case of cereals), or the specificities and consumption preferences (as in the case of vegetable oils) and also impact the trade as a whole.” (CNA, 2020). Finally, they mention that Korea benefits from FTAs with agro-exporting countries (The United States, The European Union, ASEAN, Australia, and New Zealand). These are the same countries that compete with Brazil and impact trade.

They conclude that a comprehensive FTA with Korea will benefit Brazil by opening markets and/or increasing the exports of sugar and ethanol, soy and its derivatives, coffee, dairy, fish, peanuts, fiber and textile products, meats, cereals, and flours. Furthermore, Korea may increase Brazilian agricultural competitiveness by supplying
fertilizers and machinery, given that it is the seventh-largest exporter of machinery for the production of dairy products.

Ribeiro (2021) from The Institute for Applied Economic Research (IPEA) also analyzed the impact of Mercosur-Korea FTA on the Brazilian economy (using the GTAP model). The study reports that Brazil’s GDP may gain by 0.49%, investment by 1.16%, and real wage by 0.32%. Both Brazil and Korea may grow due to the FTA, although Korea would profit more. Korean exports to Brazil would increase by 250%, while Brazil’s export to Korea would rise by 49%. The gain of Brazil mostly would come from the agricultural sector, while the manufacturing sector could expect to lose jobs and trade balance. The employment in the manufacturing sector would fall by 0.21%, and the trade deficit in this sector would increase by USD 2.3 billion. In detail, there would be a drop in production in textiles, motor vehicles and parts, and electronic equipment, reflecting the Korean’s strong competitive advantage in these activities. In addition, some sectors, such as iron and steel, metal products, rubber and plastic, coal and petroleum products, and beverages and tobacco, would have to reduce their employment level without loss of production.

**Brazil currently imposes higher tariff and non-tariff barriers to industrial goods than Korea. Since Korea is expected to increase its industrial goods exports to Brazil, Korea’s gain will be more meaningful.** The industrial sector is hostile to the Mercosur-Korea FTA since the gain of the Brazilian industrial sector is unclear, and losses are expected in the vehicles & parts and electronic equipment, where Korea has a remarkably competitive position in the world market.

The Brazilian Ministry of Economy’s Secretary of Foreign Trade (SECEX) released the paper “Mercosur Free Trade Agreement Impact Study - South Korea” in August 2021. It highlighted that the negotiations with South Korea are part of a broader Asia agenda since the continent has the highest economic and population growth rates globally. “The economic importance of the region and the level of integration of the Asian economies make Brazil’s trade strategy for the continent imperative.” (SECEX, 2021). SECEX estimates that negotiations with South Korea, Indonesia, Vietnam, and Singapore will increase the Brazilian GDP by R$ 502 billion cumulatively through 2040, in addition to a positive impact on investments, trade and wage bills and a reduction of prices. As Ribeiro’s simulation study (2021), SECEX emphasizes that the Mercosur-Korea FTA will benefit the Brazilian economy considerably, with positive impact on all macroeconomic variables and positive sectoral effects. In this study, most sectors show an increase in production, exports, and total imports. Also, “a more detailed examination of the free trade agreements signed by South Korea demonstrated that, given the high rates of relief agreed, often above 90% in terms of tariff lines and trade volume, there was a willingness to significantly reduce these tariff barriers.” (Ribeiro, 2021).
Expectation for Cooperation in non-sensitive areas

The main purpose of an FTA is to reduce or eliminate tariff and non-tariff barriers to trade, and the Mercosur-Korea FTA can incorporate issues other than those. Using the agreement as a channel for economic cooperation, Korea extends the purpose of FTA. Korea’s FTA includes a chapter on economic or technical cooperation, a non-conventional FTA issue. Korea now has 17 FTAs with 57 countries in force, and 12 of them have a chapter on “Cooperation,” “Economic Cooperation,” or “Technical Cooperation.” Usually, FTAs with developing countries have those chapters. We can get ideas from the FTAs signed by Korea and by Mercosur. Table 6 provides examples of those chapters in the FTAs of Korea with ASEAN, Australia, Israel, and Colombia, indicating specified sectors and areas of mutual interests for development. Likewise, Mercosur-EU FTA covers cooperation in economic and non-economic issues, regarding dialogue and exchange of information, small and medium-sized companies, and sustainable development. Therefore, Mercosur and Korea shall identify the sectors/areas with a high demand for cooperation and profit from each other’s partnership. Recommendation #1 in Session VI of this report will further discuss the Cooperation issue and identify sectors of mutual interest.

Although there are chapters on cooperation in most FTAs, not all cooperative projects are implemented. We found that including specific conditions in the text of the FTA agreement can help the projects to take place. Establishing a committee for a specific sector, setting a contact point in each country, or specifying the cooperation plan for SMEs (such as capacity building, training, and technical assistance, exchanging experiences, and R&D) are examples of those conditions.

Kwon et al. (2017) surveyed 54 confederations of industries or public entities related to industries from Mercosur to ascertain their interest in collaborating with Korean business firms. 83% of them presented high interest in cooperation with foreign companies, and 49% showed interest in cooperation with Korean firms, with expectations to enter a new market, develop new products, conduct joint R&D, and learn new technology. However, they were concerned that they might face challenges finding proper partners. They considered the FTA a good measure to overcome those challenges and facilitate inter-firm cooperation between Korea and Mercosur. Accordingly, the study suggests the Mercosur-Korea FTA includes a chapter on inter-firm cooperation, outlining various measures for identifying cooperation partners and providing financial or institutional support for cooperation.
Korea’s FTAs

**Korea-ASEAN FTA:** chap 3. Economic cooperation
1) Customs procedures, trade, and investment promotion, SMEs, human resources management and development, tourism, science and technology
2) Capacity building programs and technical assistance

**Korea-Australia FTA:** chap 16. Cooperation
1) Agriculture, Fisheries and Forestry
2) Energy and Mineral Resources

**Korea-Israel FTA:** chap 17. Technical cooperation
1) Aerospace, medicine and medical supplies, information security, cyber security, virtual reality, big data, renewable energy, Information Technology (IT) and Biotechnology (BT), agriculture and food, Artificial Intelligence (AI), healthcare
2) Venture start-up cooperation

**Korea-Colombia FTA:** chap 17. Cooperation
1) Agriculture, fisheries and Aquaculture, forestry, maritime transport, information and communication technology, energy and mineral resources, tourism
2) Small and medium-sized enterprises, Industrial and commercial cooperation, Science and technology, and Culture

EU-Mercosur FTA

**Dialogue chapter** to establish dialogues and exchange information. Subcommittees will be established for each of the following subjects
1) Animal welfare matters
2) Agricultural biotechnology
3) Combating antimicrobial resistance
4) Scientific matters related to food safety, animal and plant health

**SME chapter**
1) A website containing information regarding the Agreement to give practical and detailed information to SMEs
2) SME coordinators to carry out the tasks to fulfill SMEs’ needs

**Sustainable Development Chapter**
Sub-committee to facilitate and monitor the effective implementation of this chapter
1) Labor
2) Environment
3) Climate Change
4) Biodiversity
5) Sustainable management of forest, fisheries, and aquaculture
6) “Precautionary Principle”
7) Responsible management of Supply Chain

Source: Text of each FTA.

Urrego-Sandoval and Ramon’s (2021) study on Pacific Alliance (PA) and South Korea cooperation suggests a future collaboration. Korea is seeking to become an associate member of the PA, including signing an FTA with the countries’ members. Since the PA member’s position on the FTA with Korea is similar to that of Mercosur, the suggestions for Korea-PA cooperation may also use for the Mercosur-Korea FTA. Chile, Colombia,
and Peru have bilaterally signed FTAs with South Korea (the FTA with Mexico is not concluded yet). The perceptions in those countries about the FTAs outcomes are very positive, particularly from the agricultural sector (with a profound impact on trade gains and investments).

Nevertheless, the industrial sector has been concerned about inter-industry trade disparities in value. Korea exports high value-added products to the PA bloc and imports commodities from the bloc, similarly to the Korean-Mercosur economic relation. The research underlines the economic cooperation among institutions from Korea (Trade and Promotion Agency - KOTRA, KOICA, Korea Eximbank) and from the PA (ProChile, ProColombia, universities, and think tanks). This cooperation provides information and guidance to facilitate loans to SMEs, better understand consumer preferences and trade barriers and support firms and joint ventures with their operations.

Overall, “the study recommends cooperation in specific sectors in order: a) to upgrade the “old Agreements” to integrate digital economy elements, e-commerce, 5G, investment provisions, sustainable development opportunities, labor and financial services, government procurement, new SPS protocols; b) to debate the positive outcomes from trade preferences; c) to support investment opportunities in non-traditional sectors, such as Information and Communication Technologies (TICs) and clean energy; d) to enhance scientific and technological cooperation, R&D activities to facilitate technology transfer; and e) to finance infrastructure of the Pacific region, transport and logistics” (Urrego-Sandoval and Ramon, 2021).

CNI opposes FTA with Korea, although it favors collaboration on non-controversial issues. The CNI’s Agenda for South Korea (2020) proposes actions to improve the business environment, simplify bureaucratic procedures, and facilitate trade in the following six areas: (1) Intellectual Property: CNI suggests signing a permanent agreement between Brazil’s The National Industrial Property Institute (INPI) and Korea’s Korea Intellectual Property Office (KIPO) to cooperate in sharing information to fast-track patent examination (PPH - Patent Prosecution Highway). (2) Customs: CNI proposes signing the Agreement of Mutual Recognition between the Authorized Economic Operator programs (AEO). (3) Air Service: CNI suggests expanding the scope of the present agreement. (4) CNI proposes an agreement in cooperation and facilitation of investments. (5) Trade Barriers: CNI suggests identifying and removing barriers to trade, such as the barriers to Brazilian beef imposed by Korea in 2012. (6) WTO Reform: CNI proposes negotiating with joint proposals for the modernization and strengthening of the WTO and alternatives for the proper functioning of the WTO Dispute Settlement System.

Ribeiro (2021) simulated Mercosur-Korea FTA. The study shows that a large part of gains would come by reducing non-tariff barriers, especially in Brazil and Mercosur. An agreement involving only tariff reductions would still have positive results but is less effective. He highlights that both Brazil and Korea would
experiment significant gains of exports – total and bilateral – in a great number of sectors. However, the FTA would reinforce the current sectoral pattern of bilateral trade. Accordingly, he suggests that it is crucial to reduce non-tariff barriers and enhance cooperation to exchange technology and skills to diversify bilateral trade and maximize the positive effects. Ribeiro (2021) also argues that the service sector should be included in the FTA. Since the service sector does not face import tariffs, the gains reported in this study would come almost entirely from deducing non-tariff barriers. Moreover, the data show that Brazil would have a lot to gain in this sector.

Due to the COVID-19, health care has become an important cooperation agenda between countries. Melo and Papageorgiou (2021) introduce inter-regional cooperation cases to counter the pandemic among the EU, ASEAN, African Union, and Mercosur. It evaluates that the COVID-19 crisis tested multilateral and regional cooperation and revealed a lack of coordination and delay in their responses. Inter-regional cooperation was generally superficial and slow, and countries adopted unilateral measures without considering counterparts’ needs. The study presented good examples of coordinated responses in obtaining medical supplies or offering financial assistance. The Team Europe Initiative donated COVID-19 tests to African countries, the COVID-19 ASEAN Response Fund mutual assistance with China, and the Mercosur COVID-19 emergency fund. Mercosur-Korea FTA can incorporate suitable measures to respond to future pandemics, but the measure should not be unilateral.

Chile, Colombia, and Peru have bilaterally signed FTAs with South Korea (the FTA with Mexico is not concluded yet). The perceptions in those countries about the FTAs outcomes are very positive, particularly from the agricultural sector (with a profound impact on trade gains and investments).
V. Countries Positions, Divergences and Challenges
The Study Group conducted four on-line interviews with three trade experts from Mercosur (one each from Argentina, Paraguay, and Uruguay) and one from South Korea (under the Chatham House Rule). The experts could share their reflections, experiences, and recommendations.

The interviews were aimed to develop a broader understanding of the FTA’s implementation, benefits and impacts and/or of a specific chapter/area covered by the agreement. The main topics of the interviews were:

- The effectiveness of the FTA in reaching its various objectives;
- The main effects of the implementation of various areas of the FTA;
- The impact of the FTA on various stakeholder groups; and,
- Unintended side effects and desired improvements for the FTA.

(See Annex I for the full interviews questionnaire)

There is a clear consensus from the interviews that Mercosur is not working properly internally, which slows down the negotiations. Moreover, the Mercosur-Korea FTA is not a priority for either side, and the COVID-19 pandemic is a major concern.
The common perception is that Mercosur is an example of an economic integration project that has stagnated. Deep integration combined with high levels of murky protectionism, even between members, has not served these member countries well and has limited the success of free trade agreements with other countries. Apart from the lack of consensus on Mercosur’s main trade goals, the heterogeneity in the structure of each member’s economies added even more complexity to the negotiations. According to one interviewee, “Paraguay is part of any regional integration even before that regional integration is created,” since, in his perspective, Paraguay is a landlocked country. The country also favors Mercosur trade negotiations with third parties, where asymmetries are considered, given that the country has little negotiating power in bilateral agreements. In contrast to Paraguay and Uruguay, which want more openness in broader sectors, Brazil and Argentina are more protectionist.

It is worth pointing out that Mercosur as a bloc is more than just a commercial agreement, as shown by its normative framework. Its principles are based on a complex shared history of its members, with broader ambitions of forming a seamless customs union similar to the European Union, safeguarding democracy, and coordinating broader policy. The challenge for the organization, which is not limited to Mercosur but plagues many of the region’s multilateral bodies, is to use this framework to drive development rather than the obstacle to free trade genuinely among its members and then becoming a formidable market. A 30-year-old institution is not easily dismantled or reformed, but Mercosur must evolve with the times to stay relevant. The bloc’s leaders need to identify and attempt to implement a clear, predictable plan of action to promote the export sectors of member countries and their integration in global value chains and maintain the confidence of international investors (Albertoni, 2019).

It seems clear that Mercosur countries need to seek PTAs beyond Mercosur. However, to do so, it is necessary that the bloc modernizes and each country simultaneously undertakes tough domestic reforms.

Unilateral trade liberalization in Brazil is one of its main domestic reforms that could create a more favorable context for domestic industrial production (Oliveira et al., 2018). As for Argentina, O’Farrell et al. (2018) state that there were at least three main reform mechanisms in the last decade: compensation (“to potential losers from liberalization”), transformation (“to support firms and workers to transit from a ‘restructuring process’ as a consequence of trade liberalization to dynamic firms”), and concertation (“of jobs, through which government took a gradual stance in the liberalization of cell phones and the special promotion regime”). However, there was “low incidence in minimizing resistance to liberalization from potential losers or gaining support from potential winners. The reasons for that are multifold and specific to each of them.”

Some interviewees highlight the political misalignment that Mercosur is going through this year when the bloc completes 30 years. Important divergences had
arisen opposing the member countries. Argentina opposed Brazil’s proposal to reduce the CET and also opposed Uruguay’s request to enable negotiation with third parties, allowing freedom of action for individual member states to negotiate trade agreements bilaterally without losing the advantages already provided by the bloc. This reform would allow small sub-groups within Mercosur to negotiate faster than the bloc as a whole.

Albertoni (2019) features four key steps for reforming Mercosur: (1) signing an agreement in which the members ratify the consolidation, deepening into the existing free trade area, and committing to addressing all the exceptions that have previously been used to restrict market access; (2) amending the bloc’s founding language and processes to allow the customs union and its members greater flexibility in negotiating international agreements with other countries or blocs. In conducting individual trade policy, members will transition to a PTA rather than a customs union. In recent years, bloc-wide negotiations have been plagued by delays in the process between the signing of agreements and their ratification; (3) considering ‘flexible clauses’ as the requirement for two-member countries to ratify the agreement (one of which must be Uruguay or Paraguay). To protect the smaller members, a similar mechanism to the one in the revised Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP, formerly TPP); and, (4) as for bilateral negotiations and negotiations between subgroups, each country should be free to negotiate with countries outside of Mercosur in a balanced and transparent framework. Chapter 32 of the new trade agreement between the United States, Mexico and Canada (USMCA) serves as a helpful guideline. It established that if one of the three partners wishes to start a commercial agreement with a country outside the bloc, it must notify the other two USMCA members three months before beginning the negotiations.

Another key element for Mercosur countries is to take their relations with China into account to explain some current trade policy dynamics. Wise (2020) talks about a “Southern Cone Style of Developmentalism” with China: “The onset of the China boom in 2003 saw both Brazil and Argentina with newly elected leftist executives, Lula and Nestor Kirchner. Although the political economy literature is laced with references to this period as “post-neoliberal,” there are important nuances in the market reforms embraced by the two countries in the 1990s. These differences shaped the varying content and emphases of the developmental programs that both administrations rolled out in the early 2000s”.

**On the relevance of the Mercosur-Korea FTA, there is a clear consensus from both sides on the importance of its conclusion.** The interviewees attributed new topics in the agenda as one factor for the delay in the FTA negotiations, which shows new issues under negotiation. However, some of them highlight difficulties in agreeing due to the great sensibilities in domestic markets, mainly related to compromises in reducing non-tariff measures or advancing in the Services Chapter.
VI. Policy Recommendations
A Chapter for technical cooperation in sectors with mutual interest and a fund for the projects

Cooperation projects should be developed in the sectors with mutual interest

As appointed in Session IV, Korea uses its FTAs as a channel for economic cooperation. The agreements generally include a chapter of economic or technical cooperation, a non-conventional FTA issue. Mercosur countries are concerned that the FTA with Korea might have a harmful effect on their manufacturing sector. In contrast, the Korean agricultural sector worries about the competitiveness loss of its products in the domestic market due to cheaper products from Mercosur. These worries arise from the idea that FTA is about to reduce trade barriers. It may cause an inflow of cheaper foreign products, although this is a conventional aspect of FTA.

On the other hand, Mercosur countries welcome Korean investment in the manufacturing sector or its advanced technology. Korea has a national system of advanced innovation, where a strong partnership between companies, universities, and government favors innovation. For example, joint projects to accelerate the digital transformation of the production sector or cooperation in health care will be accepted gladly by both Korea and Mercosur. The FTA can cover those non-conventional issues, and those sectors of mutual interests can be included in the Cooperation chapter. Then, which sectors have a high demand for cooperation that should be addressed in the cooperation chapter?

Some of the trade experts interviewed by our study group indicated the following sectors where Mercosur and Korea can cooperate: high-tech electronics, digital work, telecommunications, automotive sector (taking advantage of the manufacturing of Korean automotive plants or auto parts already integrated into Mercosur), among others. The FTA may look at innovations beyond trade and tariffs in areas where Korea shows great expertise (as investments) and where the links between the private technological sectors of Korea and Mercosur are increasingly connected (ex: Samsung R&D Center in Mercosur).

The Economic Commission for Latin American and the Caribbean - ECLAC (2021) reports that Latin America and the Caribbean countries face significant challenges in economic recovery from the pandemic. The old economic model and the Foreign Direct Investment (FDI) into the region depended on commodity price cycles before the pandemic, which limited productivity growth of the economy, and the
growth was not sustainable. ECLAC suggests that the region has to transform its economy in order to guarantee a sustained increase in GDP and productivity over time. ECLAC underlines that a profound transformation is necessary for eight sectors: (1) the transition to renewable energy; (2) sustainable electromobility in cities; (3) the inclusive digital revolution; (4) health manufacturing industry; (5) bioeconomy; (6) the care economy; (7) the circular economy; and (8) sustainable tourism. ECLAC asserts that FDI can be an important channel for transforming and developing those sectors.

The Organization of Economic and Cooperation Development (OECD) reports that Latin America and the Caribbean face some challenges: low potential growth, limited fiscal space, and higher demands for better public services and well-being standards. OECD (2020) suggests that digital transformation is an important tool to address these challenges. International partnerships are also essential, especially in the COVID-19 crisis. It stresses the role of digital technologies in three sectors: (1) the digital revolution is necessary to raise firms’ productivity, particularly for micro and small companies; (2) a digital transformation improves well-being for families, workers, and students by providing them with a better chance of learning; and (3) digital technologies can upgrade the quality of public service by making the service more credible, efficient, inclusive, and innovative. Particularly, public health and education are essential sectors of public service. As ECLAC (2021) emphasized the role of FDI, OECD (2020) stresses international and innovative partnerships.

Both ECLAC (2021) and OECD (2020) underline the transformation of the economy to sustainable productivity growth and inclusive development. Furthermore, the international partnership is suggested as a key channel.

Korea also shows a great interest in those sectors. Recently, the Korean government published “The Korean New Deal,” a national strategy for a great economic transformation. Korea faces the challenges of slower GDP growth and increasing income inequality. COVID-19 changed the world economic structure and accelerated the transition towards a digital economy and a green economy. The Korean New Deal was introduced to overcome the economic recession and raise productivity over time. The plan underlines the transition towards a digital economy and a low-carbon, environmentally friendly economy. The transition will create new industries and jobs. The plan depicts 28 projects for the transformation, and many of them are similar to what OECD (2020) and ECLAC (2021) suggested for Latin America and the Caribbean. Thus, we can recommend those common sectors from The Korean New Deal, OECD (2020), and ECLAC (2021) as those where Korea and Mercosur have a high demand for the development and international partnership. Accordingly, we suggest the Korea-Mercosur FTA includes the following sectors in the “Technical Cooperation” chapter:
• Expanding the integration of 5G and AI into industries
• Making a smart government that utilizes 5G and AI
• Advancing cyber security
• Creating technology-based education infrastructure for grades 1-12
• Strengthening the online education system of universities and job training institutions
• Building smart medical and care infrastructures with digital technology
• Promoting remote working in SMEs

• Supporting online activities of microbusinesses
• Adding digital innovation to urban spaces and industrial complexes
• Turning public facilities into zero-energy building
• Restoring the terrestrial, marine, and urban ecosystems
• Building a smart grid for more efficient energy management
• Promoting renewable energy use
• Expanding the supply of electronic and hydrogen vehicles
• Laying the foundation for green innovation via R&D and financial sectors

Both ECLAC (2021) and OECD (2020) underline the transformation of the economy to sustainable productivity growth and inclusive development
A Fund from Mercosur and Korea to ensure the continuity of technical cooperation

Many of Korea’s FTAs include cooperation chapters and corresponding sectors, but not all of them generate follow-up projects. One suggestion for the projects to be materialized is to raise funds to support technical cooperation.

The Korea-Israel FTA is a good example where R&D funds from both parties facilitate projects to be generated. Korea and Israel started FTA negotiations in May 2016 and concluded them in August 2019, after six rounds of negotiations. Both countries signed the FTA in May 2021. Israel signed 12 FTAs, and Korea was the first Asian country to sign. Korea-Israel FTA includes a chapter for technical cooperation that specifies cooperation in advanced technology: aerospace, medicine, medical supplies, information security, cyber security, virtual reality, big data, renewable energy, IT and BT, agriculture and food, AI, and healthcare. It also underlines cooperation in venture start-ups. Those are the sectors where both countries have technology or production capacity with high demand for development.

It is not the first time Korea and Israel have established an alliance. In 1999, they signed an agreement on industrial technology cooperation. They founded a joint R&D fund – The Korea-Israel Industrial R&D Foundation (KORIL-RDF), to finance joint projects since 2001. For the past 20 years, 65million USD was raised, and the fund financed 181 joint research projects. Before signing the FTA, each country disbursed 2 million USD annually for the fund. As the two countries signed the FTA, they revised the old agreement and vowed to increase the contribution to 4 million USD from each side. The key success factors of the industrial, technological cooperation between Korea and Israel can be attributed to the selection of specific sectors with mutual interest and the constitution of and the increase of the contributions for the bilateral fund.

Korea-Mercosur FTA has already included a chapter for technical cooperation. Nonetheless, for the chapter to generate tangible projects, it should include sectors where both parties have a strong interest and set up a joint R&D bilateral fund to ensure the continuity of cooperation.
A regular business forum for industries and consumer groups with a long-term financial support

A regular business forum should be run with industries and consumer groups to generate business opportunities and inform consumers about the benefit of the Mercosur-Korea FTA. The manufacturing sector of Mercosur and the agriculture of Korea are unwilling to open their markets, and their stance has changed little since the beginning of the FTA talks. While the manufacturing sector of Mercosur is concerned, they welcome investment from Korea. The problem is that they are unsure whether a trade agreement accompanies investment from Korea.

Korean companies are interested in the Mercosur market, but they face some challenges for investors. According to the interview with Korean firms in Mercosur, one of the big challenges is finding proper business partners (Kim et al., 2011). They asked the Korean government to provide them with a platform where Korean and Mercosur business sectors could exchange information. It will help them find adequate partners for investment in Mercosur. Both Korea and Mercosur demand cooperation, but they do not have sufficient channels.

There were several forums between Korea and Mercosur where investment opportunity was discussed, such as Korea-Brazil Forum between 2005 and 2010, Korea-Brazil 21st Century Commission between 1996 and 1999, and Korea-Mercosur Forum for Industrial Cooperation in 2019. However, they were run temporarily and had insufficient attention from the business sectors. The business sectors did not have the leading role in the forums. Korea-Brazil Forum and Korea-Brazil 21st Century Commission included the issues of industrial cooperation between Korea and Mercosur, but the participation of business sectors was small. Only four of the 32 participants at the 4th Korea-Brazil Forum in 2009 were from the business sector. In the fourth meeting of the Korea-Brazil 21st Century Commission in 1999, 4 were businesspersons out of 28 participants. The governments and researchers led both forums. The Korea-Mercosur Forum for Industrial Cooperation was held in Brazil and Argentina in 2019, and business sectors from Brazil and Argentina were the main participants. However, the Forum was held only once. In this sense, previous forums’ weak and negative points should be improved for future forums.
TABLE 7: Business forums between Korea and Mercosur

<table>
<thead>
<tr>
<th>Title</th>
<th>Periods</th>
<th>Hosts</th>
<th>Participants</th>
</tr>
</thead>
</table>
| Korea-Brazil Forum                              | 2005~2010     | • Korea Foundation  
• Ministry of Foreign Affairs of Brazil                          | • 32 people in the 4th forum in 2009  
• 14 government officials,  
10 researchers,  
4 businesspersons, 2 bankers,  
2 lawyers                                                                 |
| Korea-Brazil 21st Century Commission            | 1996~1999     | • Established by the Presidential Summit of 1996                      | • 28 people in the 4th forum in 1999  
• 16 government officials,  
8 researchers, 4 businesspersons                                            |
| Korea-Mercosur Forum for Industrial Cooperation | 2019          | • Ministry of Trade, Industry, and Energy of Korea  
• Korea Trade and Investment Promotion Agency                             | • Government officials from Korea, Brazil, and Argentina  
• Business sectors from Brazil and Argentina                                |

Consumer groups were not involved in any of the forums mentioned above. We must listen to what they say and raise the consumer group’s knowledge about the agreement. While we hear the industry’s worries in the FTA negotiations, we do not hear much of the voice from the consumer groups. While the FTA may bring harsh conditions for producers of Mercosur and Korea, the consumers in both regions can benefit from cheaper products. Since the industry is much more cohesive than the consumers, the industry’s opinion stands out. The consumers may not be aware of the benefits they can enjoy from the FTA, and they are not organized as a group to claim any benefit, as the industry does. Korean consumers may not be aware of the diversity of products from Mercosur they may have access to in the future or how much their quality is superior to the products currently on sale in Korea, and vice versa. If the business sectors and consumer groups were represented in the same forum, then the agricultural sector of Mercosur could promote their products directly to Korean consumers, for example.

Most of the forums did not last long. One reason is that there was no long-term financial support to maintain them. Korea-Brazil 21st Century Commission agreed to establish a fund in the fourth meeting in 1999. The plan was to raise 2 million USD and increase it to 10 million USD in 5 years. Korea and Brazil were about to contribute 50 percent each, and the fund was expected to be used for joint projects between them. However, the commission has not been held since 2000, and the fund was not established.

Accordingly, we suggest a regular forum where business sectors will play a leading role and consumer groups are involved. In addition, a fund should be raised by both Korea and Mercosur to assure the forum’s long-term operation.
Raising the firms (mostly SMEs) utilization of the Mercosur-Korea FTA

When countries sign an FTA and the agreement is in force, some exporting or importing companies do not benefit from the tariff reduction. They have to verify whether their products satisfy the rules of origin as specified in the FTA. As of 2010, 5 FTAs were in force in Korea, with Chile, Singapore, EFTA, ASEAN’s 10 countries, and India. Not many companies, however, enjoyed the FTAs’ trade benefits. The Korean trade authority and researchers conducted surveys with manufacturing and trading companies to determine the reasons for such low utilization of the FTAs. Cheong (2008) reported that only 21% of firms utilized FTAs in their business in applying preferential tariffs, and he said the ratio was 19% in the survey from KOTRA. Cheong and Cho (2010) conducted another survey to identify the obstacles preventing the trading firms from utilizing the FTAs’ preferential tariffs. The firms replied that the significant barriers were the lack of information on the FTAs, difficulties in satisfying the rules of origin, low tariff preferential margins, and the lack of importers’ business culture in utilizing FTAs. At that time, information on FTAs was provided on the websites, but usually only the copy or a summary of the texts of the Agreements. Cheong (2014) described that Korean firms instead wanted manuals for utilizing FTAs and descriptive explanations in a more simplified language. He also mentioned that Korean firms needed training courses for education and interpreting the texts of the FTAs. Cheong (2014) explained that the rules of the origin chapter was the most burdensome for companies. Many of them did not know that they had to verify that their products satisfied the rule of origins to apply the preferential tariff of the FTAs.

The Korean government prepared a comprehensive program to support trading companies using the FTAs to solve the business sector’s obstacles easily. It included consulting service, training courses, regular hearing of the business opinion, and integrated support centers. The detailed contents of the program are described in the following table.
The Korean government established the FTA Utilization Support Center, especially to support small and medium-sized companies. Eighteen centers are located in major cities in Korea, and 15 centers are placed in foreign countries, namely China, Vietnam, India, Indonesia, Thailand, Philippines, the United Kingdom, and Mexico. The domestic centers provide consulting services, training courses, seminars, services related to the rules of origin, among others. The main tasks of those overseas centers are the promotion of FTA utilization and consulting for Korean and foreign firms.

The Korean government measures the proportion of products that receive the preferential tariff rates among the products subject to the application of preferential tariffs by FTAs. Those statistics are provided with the name of “FTA utilization ratio.” In 2020, the FTA utilization ratio of Korean exporting firms was 74.7%. It has increased dramatically since 2010, considering that the FTA utilization ratio was as low as around 20%. In 2020, the FTA utilization of Korean importing firms was 82.3%. We can conclude that the government support program greatly raised FTA utilization.

Korea’s 17 FTAs with 57 countries are in force. Korea learned that trade does not automatically increase just because FTAs are signed. Companies, specifically small and medium-sized, need support to use the FTAs. We recommend that Korea shares with Mercosur its experience in raising the utilization of FTAs. Mercosur members can establish similar supporting programs to help small and medium-sized companies participate more in global trade using FTAs. Moreover, the supportive measures will contribute to increased trade under Mercosur-Korea FTA.

### TABLE 8: Korea’s support program for FTA utilization

<table>
<thead>
<tr>
<th>Business demand survey</th>
<th>Regular and special meetings and surveys for industrial agencies, representative companies</th>
</tr>
</thead>
<tbody>
<tr>
<td>FTA business information</td>
<td>FTA homepage for tariff, rules of origin</td>
</tr>
<tr>
<td></td>
<td>Seminars, workshops</td>
</tr>
<tr>
<td></td>
<td>Guide books, pocketbooks, brochures</td>
</tr>
<tr>
<td>FTA expert, consulting</td>
<td>Cyberlearning system on FTAs</td>
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<tr>
<td></td>
<td>FTA class in universities and graduate schools</td>
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<tr>
<td></td>
<td>Courses for FTA consultants and experts</td>
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<tr>
<td>Direct assistance for business</td>
<td>FTA business consulting</td>
</tr>
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<td></td>
<td>FTA call center</td>
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<tr>
<td></td>
<td>Local FTA Assistance Centers</td>
</tr>
<tr>
<td>FTA system maintenance</td>
<td>Integrated Business Rules of Origin Center</td>
</tr>
<tr>
<td></td>
<td>Integrated FTA Info Center</td>
</tr>
</tbody>
</table>

Source: Cheong (2010).
Introduction of a Local Currency Trade Settlement Arrangement - LCTSA in the Mercosur - Korea FTA

Trade between Korea and Mercosur has grown rapidly in quantity over the past 30 years. However, bilateral trade has structural problems that are very vulnerable to economic fluctuations due to the poor number of traded items. Structural problems of bilateral trade are first attributed to the trade structure specialized in inter-industry trade. In other words, due to the trade structure in which Korea exports industrial products and Mercosur exports primary products, bilateral trade is inevitably weak and volatile.

Another reported problem is that the trade participation of small and medium-sized enterprises is insignificant, as demonstrated in Figures 5 and 6. Latin America is the most distant market for Korean companies, geographically and psychologically. Due to these distance barriers, Latin America is thus the market with the lowest participation of Korean SMEs by region. In particular, among Latin American countries, Mercosur (especially Brazil and Uruguay) is the market with the lowest participation of Korean SMEs. As such, Mercosur companies feel the same about the Korean market.

![FIGURE 5: The export share of Korean SMEs by region](source: KOSIS)

![FIGURE 6: The export share of Korean SMEs by country in Latin America](source: KOSIS)

Another important issue is the high exchange rate volatility. According to a survey by KOTRA in 2020, Korean companies cited exchange rate fluctuations as the biggest challenge in doing business in Brazil. Such high exchange rate volatility is a huge barrier for investment and import/export companies. In particular, it is an even more significant business barrier for SMEs lacking preparation for dealing with foreign exchange risk.

POLICY RECOMMENDATIONS
Above all, we defend that the participation of SMEs, which are one of the leading players of trade, must be expanded to increase trade between Korea and Mercosur. It is thus necessary to reduce transaction costs through foreign exchange risk reduction. In order to achieve this objective, we suggest introducing a local currency trade settlement arrangement (LCTSA) between Korea and Mercosur. Fortunately, they have already been independently operating a trade settlement system in their currencies to revitalize trade by reducing foreign exchange risk. Nevertheless, it will be necessary to review actively the introduction of the bilateral arrangement by sharing the experiences of operating the local currency trade settlement system introduced by both parties.

**Mercosur’s experience**

At the Mercosur level, the Local Currency Payment System (SML) was launched on October 3, 2008, when Argentina and Brazil started using their currencies for trade transactions between the two countries. With the introduction of SML between Argentina and Paraguay on June 22, 2021, SML is being used in all trade transactions among Mercosur members.

Mercosur member countries have introduced SML for the following three purposes. First, member countries want to expand trade by reducing transaction costs, which are expected to be reduced by 3-4% due to the simplification of trade settlement procedures. Transactions among member countries will be greatly revitalized as foreign exchange risk is eliminated and the possibility of default on settlement is lowered. Second, member countries expect trade revitalization of SMEs, which have been avoiding trade transactions, and will thus benefit from reducing trade transaction costs and resolving difficulties in foreign exchange transactions. Finally, progress in the financial integration of Mercosur is expected. As exporters and
importers become more familiar with using member currencies instead of the dollar, and as the liquidity and efficiency of the real-peso exchange rate market are improved, it is expected that financial integration will ultimately be sped up by introducing a single currency of Mercosur.

**FIGURE 8: Mercosur’s local currency payment system model**

![Diagram showing the local currency payment system model](source: Brazilian Central Bank and Central Bank of Argentina)

The characteristics of SML operation are as follows. It is a cross-border system integrated with Central Banks (CBs-payment platforms). Transactions begin with value transfers of local banks and end with compensations between those CBs. CBs do not assume mutual or credit risk with financial institutions. It is optional and complementary to existing payment systems. Traditional trade documents are maintained except the Export Registration, which must be filled in local currency. It is not a risk hedging mechanism, since it eliminates the foreign exchange risk for exporters.

Since its introduction, Mercosur’s SML has received great attention as a fresh alternative. It focuses on the simplicity and speed of system operation and the expansion of exports of SMEs. Although it has been more than ten years since the introduction of SML, it is evaluated that its operational performance is insufficient due to factors such as the absence of incentives for SMEs to participate and the lack of awareness and understanding of SML by companies.

**POLICY RECOMMENDATIONS**
Korea’s Experience

Since the global financial crisis in 2009, major emerging market countries have pushed actively ahead with the internationalization of their currencies by promoting local currency settlement of intra-regional trades.

Korea has also pushed ahead with enhancing the Korean Won use in current account transactions. As part of this, Korea introduced the Currency Swap-Financed Trade Settlement Facility with China in 2012 for the first time. This facility supporting trade settlement using the proceeds of the Korea-China currency swap arrangement intends to revitalize bilateral trade settlement in local currencies via the provision of backstops in the form of the counterparty currencies by the two central banks.

Under this scheme, the Bank of Korea (BOK) lends its Renminbi (RMB) currency swap proceeds to banks in Korea, supporting Korean firms’ RMB payments to settle their trade with China.

1. The BOK and the PBOC activate the currency swap and place their respective currencies in each other’s accounts (the BOK places KRW and the PBOC, RMB).

2. An importer in Korea imports goods from an exporter in China on the settlement in RMB and applies for an RMB loan from a bank in Korea.

3. The bank in Korea submits an application to the BOK for an RMB currency swap-financed loan. The BOK reviews the application and transfers the RMB funds to the Korean bank’s account via its agent bank in China (correspondent bank).
4. The bank in Korea signs an RMB loan contract with the importer.

5. The bank in Korea instructs its corresponding bank in China to transfer the RMB funds to the exporter’s account in China.

6. The corresponding bank in China makes the RMB payment to the exporter.

7. The importer in Korea repays the RMB loan at maturity.

8. The bank in Korea collects the importer’s RMB loan and transfers the RMB funds to the BOK’s account with the PBOC through its corresponding bank in China.

Source: Bank of Korea (2012).

The People’s Bank of China (PBOC) also lends its KRW currency swap proceeds to banks in China to support Chinese firms’ KRW payments to settle their trade with Korea.

**FIGURE 10: From perspective of importer in China**

1. The BOK and the PBOC activate the currency swap and place their respective currencies in each other’s accounts (the BOK places KRW and the PBOC, RMB).

2. An importer in China imports goods from an exporter in Korea on the settlement in KRW and applies for a KRW loan from a bank in China.

3. The bank in China submits an application to the PBOC for a KRW currency swap-financed loan. The PBOC reviews the application and transfers the KRW funds to the Chinese bank’s agent account in Korea (corresponding bank).
4. The bank in China signs a KRW loan contract with the importer in China.

5. The bank in China instructs its corresponding bank in Korea to transfer the KRW funds to the account of the exporter in Korea.

6. The corresponding bank in Korea makes KRW payments to the exporter.

7. The importer in China repays the KRW loan at maturity.

8. The bank in China collects the importer’s KRW loan and transfers the KRW funds to the PBOC’s account with the BOK through its corresponding bank in Korea.

Source: Bank of Korea (2012).

Among countries with a currency swap agreement, Korea operates a trade settlement system in its currency only with emerging countries. On the other hand, it has a currency swap agreement with developed countries, which are key currency countries, purely responding to the financial crisis. In August 2021, Korea signed a currency swap agreement with Turkey and introduced a local currency trade settlement arrangement.

As of September 2021, Korea has more than 198.2 billion USD in currency swap contracts. These figures exclude Canada, where no limits have been set in advance. Korea has bilateral currency swaps with the following nine countries: 60 billion USD with the US; 59 billion USD with China; 10.6 billion USD with Switzerland; 10 billion USD with Indonesia; 8.1 billion USD with Australia; 5.4 billion USD with the UAE; 4.7 billion USD with Malaysia; no pre-arranged cap with Canada; 2 billion USD with Turkey. Korea is also a member of the Chiang Mai Initiative Multilateralization (CMIM), a multilateral currency swap arranged among the ASEAN+3 members (13 countries), allowing Korea to swap 38.4 billion USD in case of a financial crisis.

As seen above, both Korea and Mercosur have a trade settlement system in their currency to promote their exports. The two arrangements aim to reduce foreign exchange risk, and transaction costs for companies to alleviate external vulnerabilities due to decreased dependence on major reserve currencies and promote trade. However, the two arrangements have different characteristics regarding the purpose and method of operation.

First, Korea’s local currency trade settlement is derived from the currency swap agreement. Korea introduced trade settlements in its currency to improve the utilization of currency swap funds. On the other hand, Mercosur introduced the system from the outset focus purely on local currency trade settlement, regardless of currency swaps.

Second, Korea is using currency swap funds to promote trade settlement in its currency since it is difficult to activate trade settlement in its currency only just
through the strength of the original market. Conversely, Mercosur operates a trade settlement system in its currency based on the voluntary participation of importers and exporters engaged in trade transactions. In other words, with no special incentives or subsidies for importers and exporters, the system is operated purely on the strength of the market.

### Specific Recommendation

Although trade between Korea and Mercosur has increased significantly over the past 30 years, traded items are not diverse, and trade is vulnerable to economic fluctuation. In this situation, the role of companies is important to expand bilateral trade. In particular, it is necessary to encourage the participation of SMEs to revitalize stagnating trade. However, as analyzed earlier, SMEs on both sides are reluctant to export due to high exchange rate risk and transaction costs.

Therefore, it is necessary to introduce the local currency trade settlement arrangement (LCTSA) to stimulate trade between the two sides, especially to expand the exports of SMEs. With the introduction of LCTSA, it is possible to expect the effect of reducing transaction costs and foreign exchange risk, as well as reducing the psychological distance. For the rapid introduction of LCTSA, it is necessary to be included in the Mercosur-Korea ongoing FTA negotiations agenda.
Inclusion of sector-specific disciplines on non-tariff barriers to trade

One of the most sensitive issues for Mercosur in the FTA negotiations with South Korea is its complex sanitary and phytosanitary regime. According to SECEX’s (2021) analysis of the Korean non-tariff barriers to trade in goods, especially technical barriers, sanitary and phytosanitary measures, those measures might harm the bilateral trade flow between Brazil and South Korea by adding costs for Brazilian exporters. The Disciplines on Market Access of Goods, SPS, and TBT negotiations seek to strengthen trade while maintaining a high level of human, animal and plant health safety, as well as reducing transaction costs. Nevertheless, if the criteria are too tight or arbitrary, they may become barriers to trade. The differences and divergences between regulatory policies create impediments to trade. The central idea is to reach a consensus around good practices and transparency between national regulatory bodies. And they shall have as basic guidelines, recommendations, and good international practices, considering technical, scientific, and technological advances.

The parties shall cooperate and exchange information on procedures for assessing conformity, use of relevant international standards, technical regulations, regulatory issues, transparency, marking/labeling, measures to simplify import, and approval of licensing and certification requirements. The parties shall also cooperate to promote mutual understanding of one another’s technical regulations, standards, and conformity assessment procedures. Particularly, the SPS chapter provisions seek to reduce the time needed for approving establishments for products of animal origins (“pre-listing”), and recognizing disease-free areas to minimize losses to producers in the event of outbreaks of animal diseases. As with other modern FTA Agreements, the Mercosur-Korea FTA shall exceed obligations in the WTO TBT and SPS Agreements on transparency, information exchange customs/trade facilitation, and regulatory coherence.

As a reference, the European Union-Korea FTA Chapter on Market Access for Goods contains a novelty aspect: the inclusion of four sector-specific disciplines on non-tariff barriers and monitoring working groups.

1. On pharmaceutical products and medical devices, it establishes stronger transparency rules for the Korean regulatory system, especially pricing and reimbursement rules for drugs. It also requires the parties to provide access to tribunals that review pricing and reimbursement decisions upon applicants’ request, adopt or maintain measures to ensure ethical business practices among manufacturers and suppliers of drugs and medical devices, and establish a working group on pharmaceutical products and medical devices.
2. On electronics, it emphasizes the importance of relying on international standards (specifically, those issued by the International Organization for Standards and the International Electrotechnical Commission) to minimize duplicative requirements. It also eliminates the requirement for conformity assessment procedures for many goods, removing European producers’ substantial cost and time burden.

3. On motor vehicles and parts, it states that Korea must accept international standards for all major technical regulations (e.g., UN-ECE for core safety standards), thereby removing a significant barrier for EU exporters of these goods. Additionally, it stipulates inter alia that the parties shall not introduce any new regulatory measures that impair market access for motor vehicles and parts. It also establishes a working group for monitoring.

4. On chemicals, it emphasizes the importance of transparency concerning laws and regulations for the chemical sector and cooperation in Good Laboratory Practices and Test Guidelines to harmonize chemical assessment and management. It also establishes a working group on chemicals.

As indicated in Table 4 of the present study, based on Global Trade Alert - GPA (2021), Mercosur’s main sectors affected by protectionist measures toward Korea in the last decade were motor vehicles, electric motors, metal products, machinery & parts. For example, products related to electronics (such as electric motors, electronic valves, and other electronic equipment) were affected by around 200 protectionist measures; followed by motor vehicles (81 protectionist measures); basic organic chemicals (68 protectionist measures); and pharmaceutical products (44 protectionist measures).

Table 5 shows the main sectors affected by protectionist measures implemented by Korea toward Mercosur. These sectors were food products (5 measures), prepared & preserved fish (5 measures), basic organic chemicals (4 measures), electrical equipment & parts (3 measures), and petroleum oils (3 measures).

Likewise, the EU-Korea FTA and the Mercosur-Korea FTA Disciplines on Market Access for Goods should include the sectors most affected by non-tariff protectionist measures. Both countries have a strong interest in expanding and facilitating trade. They should negotiate detailed disciplines for those sectors aiming at regulatory coherence, simplification/harmonization of procedures, and reduction and/or elimination of real non-tariff barriers to trade.


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ANNEX I
Interview Questions with Trade Negotiations Experts

The purpose of this questionnaire is to have a broader understanding of the Mercosur-Korea Trade Agreement, its obstacles, and expectations. Besides, it aims to gather possible recommendations on Regulatory innovations and novelty aspects, focusing on themes such as normative harmonization, trade facilitation schemes, TBT, and SPS, government procurement, technical cooperation, the role of the small and medium companies (and how they can engage in the global value chains), local currency payment systems, among others.

The specific question addressed to Mercosur Interviewers:
1) Considering that Mercosur countries have different standpoints towards the market opening, how does that affect Mercosur-Korea FTA negotiations?

2) EU-Mercosur FTA is not signed yet due to environmental issues. Can the delay affect Mercosur-Korea FTA negotiations? If so, what strategy could be taken to proceed with those negotiations?

General questions addressed to all interviewers:
1) Could you point out some possible impacts of the agreement on stakeholder groups?

2) In which sectors or areas do you think Mercosur and Korea could cooperate most? Could you suggest appropriate mechanisms?

3) What measures and actions could you recommend to alleviate the resistance to the Mercosur-Korea FTA from the agricultural sector of Korea and the manufacturing sector of Mercosur?

4) Most FTAs include “Economic and Technical Cooperation chapters”, as well as a Dialogue chapter for the exchange of information, knowledge, and good practices in some sectors and issues. Which ones would be more relevant?

5) Could you point out any unintended side effects of the Mercosur-Korea Agreement?

6) Which relevant subjects are not being discussed but should be?

7) Could you highlight any innovation or novelty aspect/ clause from any other FTA?

8) Could you recommend any literature/reports or other potential interviewees we should consult?