ESTIMATED EFFECTS OF THE EU-MERCOSUR FTA

REPORT

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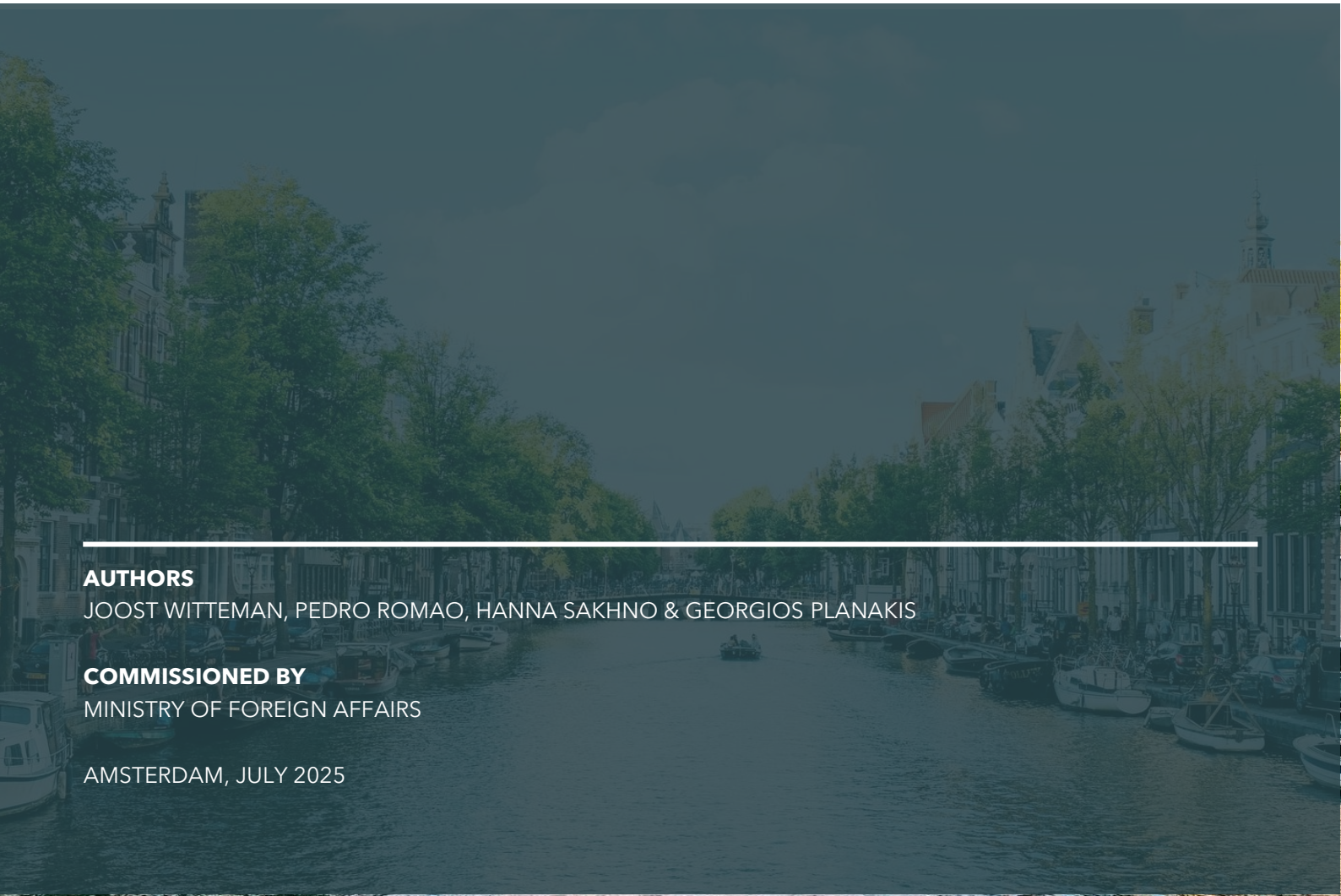

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Findings

We estimate welfare gains from trade of around +0.02 percent of real GDP for the Netherlands as a result of the proposed EU-Mercosur trade agreement.

Our assignment and methodology

SEO has been asked to estimate the expected effects of the EU-Mercosur agreement on the Dutch economy. On December 6 2024 the European Commission and the Mercosur-countries (Brazil, Argentina, Paraguay and Uruguay) finalized negotiations on the EU-Mercosur Agreement. As such, EU Member States will respond to the draft agreement, with the aim of ratification in the near term. To support the Dutch policy debate, we have been asked by the Dutch Ministry of Foreign Affairs to estimate the expected effects of the Mercosur Agreement in terms of trade and GDP.

Our estimates follow from a structural gravity model. This framework is a standard model in trade economics. For instance, it has been used to assess the effects of European integration[1], as well as to estimate the effects of trade agreements for the Netherlands, the EU internal market on the Dutch economy, as well as EU enlargement.[2] The gravity model framework allows us to take into account both trade creation and diversion, as well as price variations that result from changing trade patterns. This means that we cannot only estimate trade effects, but also equilibrium effects such as income, price, and welfare changes.

Trade effects

The Mercosur-EU FTA is estimated to result in an increase in trade.[3] For the Netherlands, we estimate an increase in exports of around +0.18 percent and an increase in imports of also around +0.21 percent. For the remaining EU26, effects are estimated to be somewhat larger, namely +0.43 percent for exports and +0.47 percent for imports. For Mercosur-economies, the export growth is estimated to be between +2.09 and +5.36 percent depending on the country, and the import growth between +1.27 and +5.29 percent, again depending on the country. In EUR-terms, the effects are largest for the largest countries. For the Netherlands, exports are estimated to increase by +1.1 bln. and imports by +1.2 bln. Estimated trade changes for the EU26 are +12.3 bln. for exports and +12.2 bln. for imports. Brazil total exports are estimated to increase by +9.3 bln. and imports by +9.7 bln. Argentina's exports and imports increase by around 1/5th of this and the increases for Paraguay and Uruguay are even smaller. Overall, Brazil is the primary driver of the increase in trade as a result of the Mercosur agreement.

The largest trade changes are associated with manufacturing and services. We estimate Dutch manufacturing and services exports to increase by between +0.4 and +0.5 bln. each, as will their imports. For the remaining EU26, the increase in manufacturing trade approaches +9 bln., both when looking at exports and imports. In services trade,

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1 See e.g., Head, K. & Mayer, T. (2021). The United States of Europe: A Gravity Model Evaluation of the Four Freedoms. *Journal of Economic Perspectives* 35/2, 23-48.

2 See e.g. Freeman, D., Meijerink, G., & Teulings, R. (2022). Trade Benefits of the EU and the Internal Market. The Hague, The Netherlands: CPB Netherlands Bureau for Economic Policy Analysis. Witteman, J., A. Kuczynski, N. Verheuvel, N. Oomes, T. Belt, E. Hoole, M. De Groot, E. van den Burg & B. Sangers (2023). Expected Economic Effects of the EU FTAs with Chile, Mexico and New Zealand. SEO Amsterdam Economics. Oomes, N., Appelman, R., & Witteman, J. (2017). Impact of the EU-Ukraine Free trade Agreement on the Dutch Economy. SEO Amsterdam Economics.

3 We interpret model results as medium to long-term changes after the Mercosur Agreement is fully implemented.

exports are estimated to increase by +2.2 bln and imports by +2.0 bln. In value terms, for the Mercosur economies Brazil dominates the total effects. Manufacturing imports by Brazil are estimated to increase by +7.0 bln. and manufacturing exports by +6.7 bln. For comparison, Argentina (the next largest economy) only has effects of around +1.6 bln. In services, effects for Mercosur economies other than Brazil are negligible. Effects in agriculture are smaller. For instance, we estimate that Brazil's exports increase (in real terms) by EUR +0.6 bln. and its imports by EUR +0.5 bln. Dutch exports are estimated to increase by EUR +0.2 bln. and imports by EUR + 0.3 bln.

Welfare effects

What do these changes in trade imply for welfare? Welfare is the economic measure of how better or worse countries are as a result of policy changes, in this case the EU-Mercosur Agreement. In the case of trade agreements, welfare changes are a net measurement. This net measurement is a composite of effects on both the producer and on the consumer side of the economy. On the producer side, the opening of new markets induces both competitive opportunities, but also pressures. The effect this has on incomes depends on which of the two effects dominates. On the consumer side, new trade opportunities typically result in access to a greater product variety at lower prices. As a result, the differentials in changes in nominal incomes and the price levels characterizes the welfare effects. These welfare effects are measured in the same units as real GDP.

Overall, we estimate welfare gains from trade due to an EU-Mercosur Agreement at between +0.09 and +0.52 percent of GDP for the Mercosur countries, and at +0.02 percent of GDP of the Netherlands (see Table S.1). Within certain industry groups, the effects are more pronounced. For instance in agriculture, the welfare effects are estimated to be between +0.69 and +1.15 percent of real GDP for the Mercosur countries, and around +0.06 percent of real GDP for the Netherlands. The estimated effects for manufacturing typically are smaller than those for agriculture and the estimated effects for services are in turn typically smaller than those for manufacturing. The overall effect on the economy as a whole is a weighted average, so that as a result the overall effect typically is biased in the direction of the effect for the services industry as that industry typically is rather large. This also accounts for, for instance, the difference in the estimated welfare effect for the Netherlands vs. the EU26: the latter has a larger share of services, so therefore the drift towards the services estimate is stronger for the EU26 than for the Netherlands.

Table S.1 Summary of welfare effects (in % of real GDP)

Region	Country	%Δ Welfare			
		Total	Agri	Manuf	Serv
MERCOSUR	**Argentina**	+0.52	+1.15	+0.34	+2.25*
	Brazil	+0.09	+0.69	+0.16	+0.04
	Paraguay	+0.12	+0.87	+0.10	+0.00
	Uruguay	+0.33	+0.79	+0.18	+6.88*
EU	**Netherlands**	+0.02	+0.06	+0.02	+0.01
	EU26	+0.00	+0.07	+0.01	+0.00

Source: SEO Amsterdam Economics. * Less precisely estimated due to lesser data quality, probably underestimating the existing services production and trade.

Whilst we have not formally estimated distributional effects, the analysis suggest that some groups may benefit more than others from the EU – Mercosur Agreement. Underlying the welfare effect in Table S.1 are changes in nominal incomes and prices. For the Netherlands, we estimate a small negative impact on nominal incomes earned, primarily in agriculture, but also a decrease in the aggregate price level that more than offsets the

decrease in nominal incomes – so that real income / welfare increases. A reasonable interpretation of this is that consumers will benefit from the EU – Mercosur Agreement due to a lower price level, but that for some producers of agricultural output the decrease in nominal incomes need not always be fully offset by the lower price level for consumption. For producers in manufacturing and services, we generally estimate an increase in nominal incomes.

Table of Contents

1 Introduction

This report estimates the economic effects of the EU-Mercosur trade agreement using a gravity model of international trade.

1.1 Background and our assignment

We have been asked to estimate the expected effects of the EU-Mercosur Free Trade Agreement (FTA) on the Dutch economy. On December 6, 2024, the European Commission and the four Mercosur countries (Brazil, Argentina, Paraguay, and Uruguay) concluded negotiations on EU–Mercosur Agreement, finalizing the deal after 25 years of discussion. The European Commission is currently finalizing the legal text through a process of legal review and translation. Once completed, the agreement will be submitted to the Council of the European Union for approval, followed by consideration by the European Parliament. Member States are expected to deliberate on the agreement in the coming months, with a view toward provisional application or full ratification depending on political consensus.

The EU-Mercosur Agreements is an extensive agreements. It covers both goods and services and includes chapters on sustainable development, intellectual property, public procurement, and sanitary and phytosanitary measures. The agreement also contains provisions to reduce non-tariff barriers and improve regulatory cooperation. A central feature of the agreement is the gradual elimination of tariffs on over 90 percent of goods traded between the two regions. For the EU, this includes improved market access for industrial products (notably cars, machinery, and chemicals), while Mercosur countries gain preferential access for agricultural exports such as beef, poultry, sugar, and ethanol. Tariff phase-outs are staggered over multiple years to protect sensitive sectors and for some of these industries (such as for some of the sensitive EU agricultural products) quotas manage the volume of exports and imports that may benefit from the reduced tariff rates.

To support the Dutch policy debate, we have been asked by the Dutch Ministry of Foreign Affairs to estimate the expected effects of the EU-Mercosur FTA in terms of trade and GDP.

1.2 Methodology

Our estimates follow from a General Equilibrium (GE) Structural One-Sector Armington-CES Gravity Model. This framework is the workhorse model in trade economics. For instance, it has been used to assess the effects of European integration[4], as well as to estimate the effects of trade agreements, the EU internal market on the Dutch economy, as well as EU enlargement (both by CPB[5] and by us[6]). For a detailed exposition of the gravity model of international trade, see, e.g., Anderson (2011), Head & Mayer (2014) or Yotov, Piermartini & Larch (2016).

The GE gravity model of international trade relates bilateral trade to country-level characteristics ("GDP") and bilateral trade costs ("distance"). As a shorthand, the gravity model typically implies that nominal bilateral trade is increasing with the size of either trading partners' economy ("GDP") but decreasing with bilateral trade costs (resulting from, for example, countries being far away from each other; or "distance" resulting from other trade

4 See e.g., Head, K. & Mayer, T. (2021). The United States of Europe: A Gravity Model Evaluation of the Four Freedoms. *Journal of Economic Perspectives* 35/2, 23-48.

5 See e.g., Freeman, D., Meijerink, G., & Teulings, R. (2022). Trade Benefits of the EU and the Internal Market. The Hague, The Netherlands: CPB Netherlands Bureau for Economic Policy Analysis.

6 See e.g., Oomes, N., Appelman, R., & Witteman, J. (2017). Impact of the EU-Ukraine Free trade Agreement on the Dutch Economy. SEO Amsterdam Economics.

barriers). FTAs have the potential to reduce bilateral trade costs (i.e., reducing the "distance" between countries). Our gravity model then first estimates the trade cost reduction as a result of the FTA, and then estimates the resulting change in trade.

Our gravity model accounts for both trade creation and trade diversion in response to the introduction of the FTA. For example, a reduction in bilateral trade costs between the EU and Brazil could spur bilateral trade between the EU and Brazil (trade creation). However, some of this increase in bilateral trade may reduce trade between the EU and other trading partners as it becomes more favorable to trade with Brazil relative to other trading partners (trade diversion). Our gravity model corrects for this by counterbalancing trade creation with a trade diversion effect.

The balance of trade creation and trade diversion implies welfare effects. Welfare effects are measured in terms of real GDP. Our gravity model estimates such welfare changes subject to several assumptions, including that there is no (immediate) reallocation of factors of production, consumers consider goods imperfect substitutes, and industries are separable (no spillovers between industries or countries). Whilst gravity models then yield consistent estimates of welfare effects, these effects typically are smaller than the effects estimated by models that include, for example, reallocation of factors of production, capital investments, sectoral spillovers, or multi-period dynamic estimations.

To consistently estimate trade creation, trade diversion, and welfare effects, the gravity model requires data on both bilateral trade as well as domestic output. Data on domestic output is needed to fully account for trade diversion, as not all output is exported. We employ a novel dataset of disaggregated bilateral and within-country trade flows from the United States International Trade Commission (USITC) – in particular ITPD-S (released December 2024). We also employ the Dynamic Gravity Dataset (DGD) with country- and country-pair characteristics from USITC. ITPD-S contains data on different industries, including agriculture, manufacturing, and services.

We estimate the effects of the FTAs as follows. First, for every industry in our dataset, we estimate the effect of past FTAs – comparable to the EU-Mercosur Agreement - on bilateral trade. Our data on FTAs is from the World Bank's Deep Trade Agreements (DTA) dataset. We use the recently released 2024 version. The DTA dataset provides data on 400 FTAs, disaggregated into 52 provisions (topics covered by trade agreements – e.g. agreements on sanitary and phytosanitary measures). We construct an FTA-index to capture differences in trade agreement depth. Secondly, we construct an indicator that expresses to what extent FTAs address similar issues as the Mercosur agreement is expected to address.[7] Together, this gives us an estimate of the average effect of Mercosur-style agreements on bilateral trade flows, but not yet corrected for the effects of trade diversion and welfare (partial equilibrium). In the second stage of the estimation, we solve for general equilibrium and market clearing conditions to dynamically compute total changes in trade and welfare. These so called *counterfactuals* represent scenarios in which the trade agreement is fully implemented by all countries. Given our dataset, our counterfactuals reflect global trade costs variations and not directly simulated changes in tariffs for individual products, industries, and/or countries. The estimated effects then illustrate what trade would look like in a given year if the counterfactual policies had been in place. We estimate effects based on the last year available in our dataset. This shows what trade would have been if the Mercosur Agreement had already been in force in the last year in our dataset. We interpret this as an estimate of the structural effect the Mercosur Agreement could have on trade after it will been fully implemented and markets have adjusted over het medium- to long-term.

7 The classification is due to Timini and Viani (2023) who have pursued a similar methodology was we pursue here.

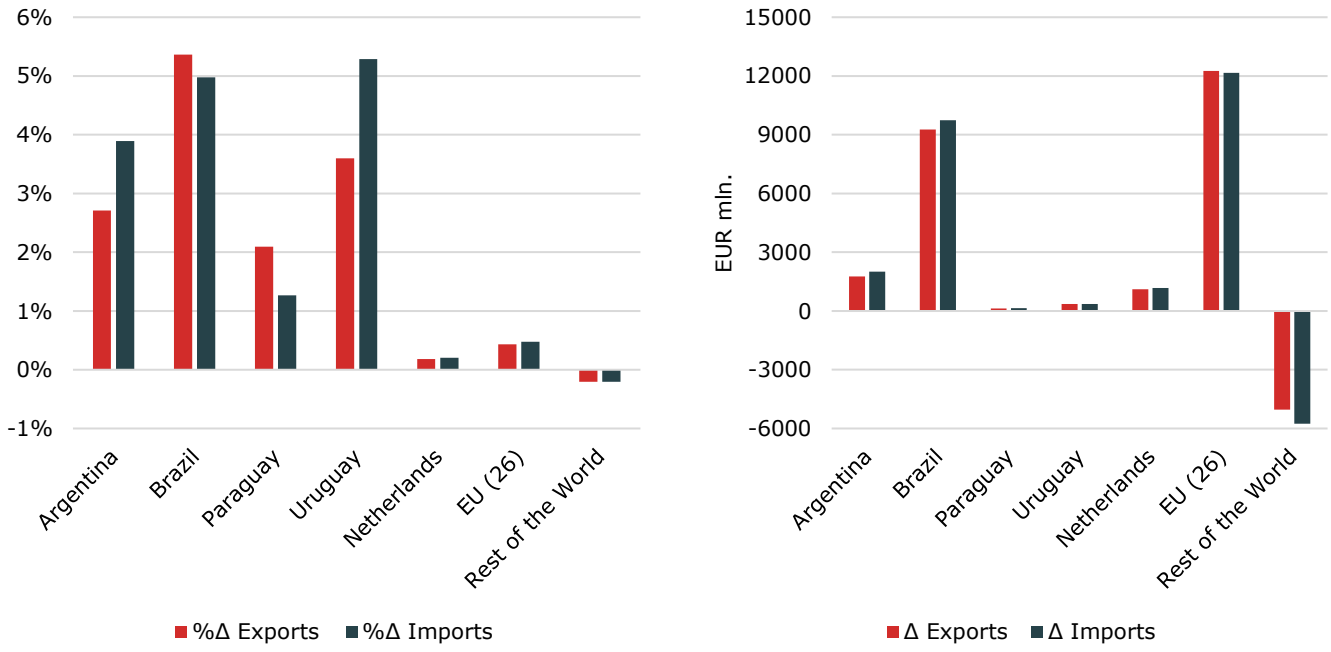
2 Model estimates

Gravity model estimates suggest gains-from-trade effects of between +0.09 and +0.52 percent of real GDP for the Mercosur countries, and at +0.02 percent of real GDP of the Netherlands.

2.1 Trade effects

Figure 2.1 shows the estimated effects on (real)[8] exports and imports for the Mercosur economies, the Netherlands and the (other) EU26, and the rest of the world. For Mercosur economies, exports are estimated to increase by between +2.1 percent (Paraguay) and +5.4 percent (Brazil). The growth of imports is estimated to be in a similar range, namely between +1.3 percent (again Paraguay) and +5.3 percent (Uruguay). Figures for the Netherlands and the EU are more modest. Dutch exports are estimated to increase by +0.2 percent and imports by +0.2 percent too. For the other EU26, export growth is estimated to be +0.4 percent and import growth is estimated to be +0.5 percent. For the rest of the world, a small decrease in overall trade volume is estimated on account of the increased trade between the EU and the Mercosur countries (meaning that other countries will be trading less with these two economic blocks).

Figure 2.1 Effects on total imports and exports (%Δ left and Δ right)



Source: SEO Amsterdam Economics.

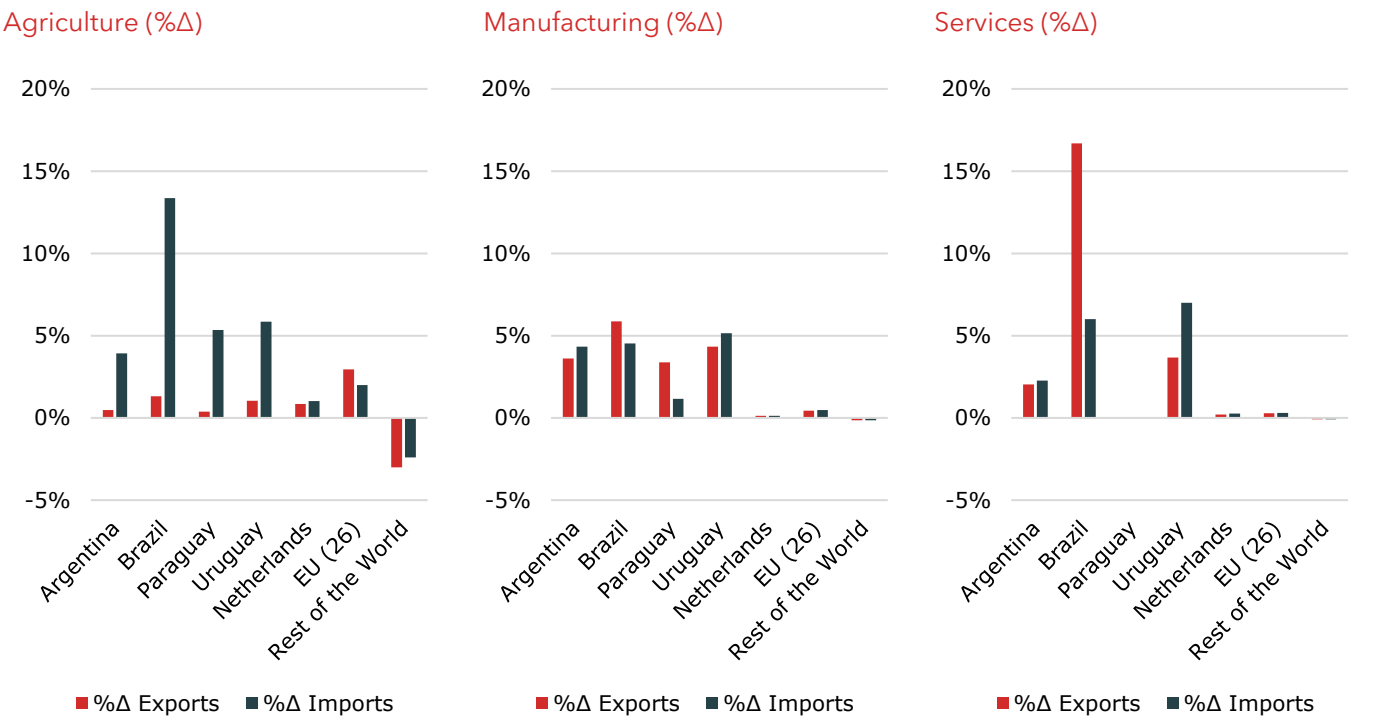
Next to percentage changes, Figure 2.1 also reports changes in EUR-terms. For the Netherlands, this shows that exports are estimated to increase by +1.1 bln. and imports by +1.2 bln. Note that this is the overall effect of changes in exports and imports – i.e. after that a part of the increase in bilateral trade with Mercosur economies is offset by changes in trade with other economies (Appendix A contains a detailed table showing the decomposition).

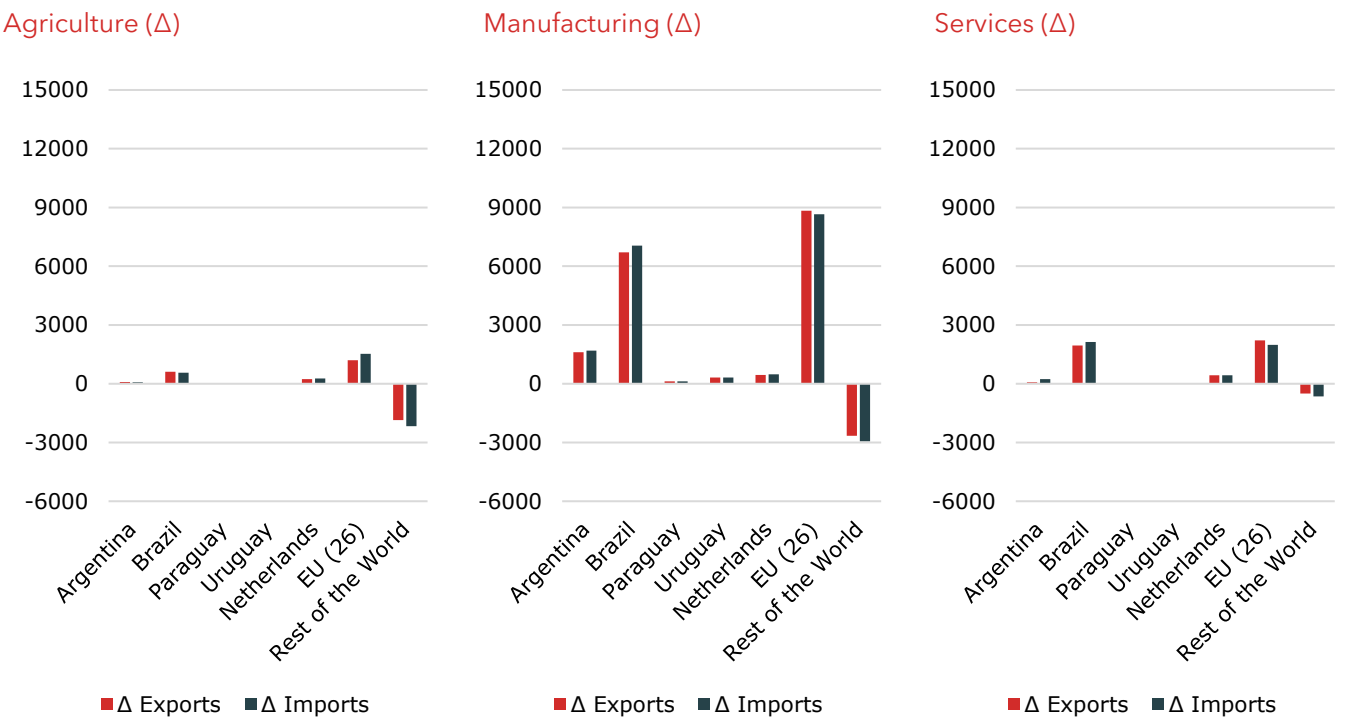
8 The model yields export changes in nominal terms. To extract the real effects, we re- and deflate the changes in exports and imports to the old price index.

Estimated trade changes for the EU26 are +12.3 bln. for exports and +12.2 bln. for imports. The fact that these estimated changes for the EU26 are larger than those for the Netherlands is on account of a 'size effect' (the EU is a larger economy than the Netherlands). A similar dynamic is visible on the Mercosur-side, where the effects (in USD terms) are largest for Brazil. Brazil total exports are estimated to increase by +9.3 bln. and imports by +9.7 bln. Argentina's exports and imports increase by around 1/5th of this and the increases for Paraguay and Uruguay are even smaller. Overall, Brazil is then the primary driver of the increase in trade as a result of the Mercosur agreement. Relatedly, the effects for Mercosur are relatively large compared to the effects for the Netherlands and the EU26 (see also the left panel in Figure 2.1). This should be intuitive: the Mercosur economies gain increased access to one of the largest and richest markets in the world, whereas this effect is relatively smaller for EU economies (i.e. the Mercosur economies constitute a smaller part of the global economy).

Figure 2.2 disaggregates the results from Figure 2.1 into three broad industries: agriculture, manufacturing, and services. In agriculture, we estimate increases in exports for Mercosur countries of between +0.4 percent (Paraguay) and +1.3 percent (Brazil). For the Netherlands and the EU26, we estimate increases in exports of +0.8 and +2.9 percent respectively. Exports of the rest of the world are estimated to be decreasing. On the import side, we see large percentage increases in Mercosur imports in agriculture, but these large growth rates are the result of the fact that current imports are relatively modest. For manufacturing, we estimate export increases for Mercosur countries between 3.4 percent (Paraguay) and 5.9 percent (Brazil) and import changes of between 1.2 percent (Paraguay) and 5.2 percent (Uruguay). Effects for the Netherlands and the EU26 are around 0.1 and 0.5 percent respectively, both for exports and imports. There is a small effect (<0.1 percent) on trade in the rest of the world. For services trade, we again see clear denominator effects. Brazil's estimated increase in services trade is large, but that is mainly the result of a relatively low base. In the case of the Netherlands and the EU26 with larger existing services exports, effects are less pronounced and in the range of 0.2 and 0.3 percet in exports and imports.

Figure 2.2 Effects on total imports and exports (%Δ top and Δ bottom)





Source: SEO Amsterdam Economics.

The bottom row of Figure 2.2 shows changes in exports and imports again in EUR-terms. Generally, measured in EUR-terms the changes in trade are largest for manufacturing, followed by services and agriculture. In part, this is due to a volume effect: the overall trade value in manufacturing is larger than the overall trade value in for instance agriculture. As a result, the EUR-value of changes in exports and imports commonly also is larger. Figure 2.2 highlights that in value terms, the effects of the Mercosur agreement are estimated to be largest for manufacturing and services. A second observation is that the largest economies account for the largest effects in value term (in particular the EU26 and Brazil). This holds both for agriculture and manufacturing, as well as for services. In agriculture, we estimate that Brazil's exports increase (in real terms) by EUR +0.6 bln. and its imports by EUR +0.6 bln. Dutch exports are estimated to increase by EUR +0.2 bln. and imports by EUR +0.3 bln.. Quantitatively, effects in manufacturing and services are (significantly) larger. We estimate Dutch manufacturing exports to increase by +0.5 bln., as will imports. The same goes for services, with both exports and imports increasing by +0.4 bln. The overall effect on the trade balance as a result of changing trade with both Mercosur and non-Mercosur economies is a small decrease. For the remaining EU26, the increase in manufacturing trade approaches 9 bln., both when looking at exports and imports. In services trade, exports are estimated to increase by 2.2 bln and imports by 2 bln. In value terms, for the Mercosur economies Brazil dominates the total effects. Manufacturing imports by Brazil are estimated to increase by 7.1 bln. and manufacturing exports by 6.7 bln. For comparison, Argentina (the next largest economy) only has effects of around 1.6 bln. In services, effects for Mercosur economies other than Brazil are negligible.

Underlying these total changes are nuanced substitution effects that are illustrated in more detail in Appendix A. As an example, as Mercosur economies directs more of their trade towards Europe, this reduces (at least in the context of our model) exports to other destinations. The resulting unmet demand in these locations can then be serviced by other exporters, including Europe and the Netherlands. As a result, only looking the increase in trade between Europe and Mercosur economies would distort the estimated trade impact of the Mercosur agreement, as it would fail to account for trade diversion and substitution.

2.2 Welfare effects

What do these changes in trade imply for welfare? Welfare is the economic measure of how better or worse countries are as a result of policy changes, in this case the EU-Mercosur agreement. In the case of trade agreements, welfare changes are a net measurement. This net measurement is a composite of effects on both the producer and on the consumer side of the economy. On the producer side, the opening of new markets induces both competitive opportunities, but also pressures. The effect this has on incomes depends on which of the two effects dominates. On the consumer side, new trade opportunities typically result in access to a greater product variety at lower prices. As a result, the differentials in changes in nominal income and the price levels characterizes the welfare effects. These welfare effects are measured in the same units as real GDP.

Overall, we estimate welfare gains from trade due to a Mercosur agreement at between +0.12 and +0.52 percent of GDP for the Mercosur countries, and at +0.02 percent of GDP of the Netherlands (see Table 2.1). Within certain industry groups, the effects are more pronounced. For instance in agriculture, the welfare effects are estimated to be between +0.7 and +1.2 percent of real GDP for the Mercosur countries, and around +0.06 percent of real GDP for the Netherlands. The estimated effects for manufacturing typically are smaller than those for agriculture and the estimated effects for services are in turn typically smaller than those for manufacturing. The overall effect on the economy as a whole is a weighted average, so that as a result the overall effect typically is biased in the direction of the effect for the services industry as that industry typically is rather large. This also accounts for, for instance, the difference in the estimated welfare effect for the Netherlands vs. the EU26: the latter has a larger share of services, so therefore the drift towards the services estimate is stronger for the EU26 than for the Netherlands.

Table 2.1 Summary of welfare effects (in % of real GDP).

Region	Country	%Δ Welfare			
		Total	Agri	Manuf	Serv
MERCOSUR	Argentina	+0.52	+1.15	+0.34	+2.25*
	Brazil	+0.09	+0.69	+0.16	+0.04
	Paraguay	+0.12	+0.87	+0.10	+0.00
	Uruguay	+0.33	+0.79	+0.18	+6.88*
EU	Netherlands	+0.02	+0.06	+0.02	+0.01
	EU26	+0.00	+0.07	+0.01	+0.00

Source: SEO Amsterdam Economics. * Less precisely estimated due to lesser data quality, probably underestimating the existing services production and trade.

Underlying the welfare changes are nominal income effects on the production side ('competitiveness') and the overall price level. Table 2.2 and Table 2.3 provide a disaggregation.

Table 2.2 shows the equilibrium effects in terms of nominal incomes. The interpretation of Table 2.2 requires some care, but can broadly be interpreted as the pressure that domestic producers face due to the policy shock. If they are positive, domestic producers can capitalize on new trade opportunities effectively rising wages in response to a surge in demand, whereas if they are negative, producers face rising competitive pressures and have to adjust by lowering wages gradually. A second interpretation is that on a macrolevel, the benefits for producers also affect the incomes of the consumers that work in these industries. The nominal income effects in Table 2.2 thus both reflect the price effects put on producers, as well as the results this has for the incomes earned as a result.

Table 2.2 suggests various changes in nominal incomes. For Argentina, Paraguay and Uruguay, the model suggests that the Mercosur agreement would generally have positive nominal income effects, both in the aggregate and per industry. After the Mercosur agreement these countries can more easily sell to the European market, and the additional demand that this causes boosts nominal incomes. For Brazil and the EU, effects appear more heterogenous. For Brazilian manufacturing and services, it appears the case that the additional supply by EU countries puts pressure on Brazilian producers in these industries. EU producers are more efficient in these industries, so that price pressures increase. This reduces nominal incomes. A similar picture appears to hold for EU agriculture: more productive / lower cost Brazilian production puts price pressure on domestic producers. The picture for the Netherlands matches the European picture: nominal incomes decrease in agriculture after the EU-Mercosur Agreement, but increase in manufacturing and services. Like before, the overall effect on the economy is a weighted average of the share of the respective industries in the total economy.

Table 2.2 Nominal income effects

Region	Country	%Δ Nominal incomes			
		Total	Agri	Manuf	Serv
MERCOSUR	Argentina	+0.22	+0.61	+0.09	+1.98*
	Brazil	-0.32	+0.81	-0.07	-0.44
	Paraguay	+0.08	+0.68	+0.02	+0.00
	Uruguay	+0.27	+0.66	+0.18	+3.54*
EU	Netherlands	-0.01	-0.46	+0.01	+0.01
	EU26	+0.02	-0.42	+0.01	+0.03

Source: SEO Amsterdam Economics. * Less precisely estimated due to lesser data quality, probably underestimating the existing services production and trade.

Table 2.3 shows the other component of the welfare effect, namely the overall change in the (domestic) price level. This effective price level reflects how easily countries can buy from producers with high technology levels and low production costs. The overall price level thus captures the effective price level of the overall consumption basket (both domestic and imported). These overall price level changes largely mirror the story above. Higher supply of EU manufacturing and services production to the Mercosur countries lowers the aggregate price level in these countries. In the EU, the supply of more Mercosur agricultural output reduces the overall price level for such products. As a result, consumers can expect to pay lower prices for agricultural output. Again, the overall effect on the economy is a weighted average of the share of the respective industries in the total economy. For the Netherlands, we see a decrease in the price level for agricultural and manufacturing output. This can be the result of cheaper imports from Mercosur economies, to the benefit of Dutch consumers.[9] On the other hand, for the EU26 we see a small increase in the price level due to higher aggregate prices for services (increased demand from Mercosur economies boosting the price level).

Table 2.3 Price level effects

Region	Country	%Δ Price level			
		Total	Agri	Manuf	Serv
MERCOSUR	Argentina	-0.16	+0.51	-0.24	-1.60*
	Brazil	-0.38	+0.69	-0.22	-0.47

[9] The Mercosur economies export a variety of agricultural products such as fruits and vegetables, soybeans, meat and meat products, etc. The same holds for manufacturing output, including for instance woods and articles of wood, and hides, skins and leathers. See Sakhno, Witteman & Romao (2025). EU-Argentina and Netherlands-Argentina Trade Profile. SEO Amsterdam Economics; Sakhno, Witteman & Romao (2025). EU-Brazil and Netherlands-Brazil Trade Profile. SEO Amsterdam Economics; Sakhno, Witteman & Romao (2025). EU-Uruguay and Netherlands-Uruguay Trade Profile. SEO Amsterdam Economics; and Sakhno, Witteman & Romao (2025). EU-Paraguay and Netherlands-Paraguay Trade Profile. SEO Amsterdam Economics.

	Paraguay	+0.04	+0.59	-0.08	+0.00
	Uruguay	+0.00	+0.52	+0.01	-4.03*
EU	**Netherlands**	-0.03	-0.54	-0.01	+0.00
	EU26	+0.01	-0.49	+0.00	+0.02

Source: SEO Amsterdam Economics. * Less precisely estimated due to lesser data quality, probably underestimating the existing services production and trade.

With respect to the positive welfare effects reported in Table 2.1, a comparison of Table 2.2 and Table 2.3 sheds light on the source of the welfare gains. The welfare effect for the total economy is a weighted average of the welfare effects for the various industries considered and the welfare effect by industry (as it is for the total economy) is the net effect of income and price effects. Consider the Netherlands, by Table 2.2 and Table 2.3 the nominal incomes for manufacturing increases, whilst the price level decreases. In turn, we get a positive welfare contribution. For services, we largely observe increases in nominal incomes. The story for agriculture is more nuanced. Table 2.2 suggests a decrease in nominal incomes in the agriculture industry. The logical interpretation is that increased competitive pressures from Mercosur competitors put pressure on incomes earned in the agricultural industry. Table 2.3, however, shows that the price level also decreases. This increases real incomes as the same consumption bundle can be achieved at lower prices. The key question for welfare then becomes the comparison between the decrease in nominal incomes and the decrease in the price level. The latter effect dominates, so in turn, a positive welfare effect results in Table 2.1. The interpretation of this welfare effect requires some care. Our model is at the country level so that effect from the demand and supply sides are equally relevant for the country as a whole. In reality, producers and consumers will benefit unequally (everybody consumes agricultural output, but not everybody produces it). Our model does not capture such distributional effects, but it is reasonable to assume that Dutch consumer will generally be net beneficiaries, whilst some Dutch agricultural producers will face pressures on their incomes that are not fully compensated by the fact that these producers will also be consumers paying lower prices. Producers in manufacturing and services can generally expect to benefit too.

2.3 Prior studies

How do our estimates relate to prior studies for the Netherlands? Wageningen Social and Economic Research has also estimated the effects of the Mercosur agreement on the Dutch economy.[10]

In the aggregate, Wageningen's most recent estimates show that the Dutch economy stands to gain around +0.02 percent in (real GDP). Wageningen furthermore states that the bilateral trade balance with Mercosur economies will worsen for agricultural products (except for dairy), but that there will be a substantial growth in trade in manufacturing and services. Wageningen also signals that as a result, there will be small but negative effects on nominal incomes earned in agriculture.

Wageningen's findings are generally in line with the results that we report here. We also estimate welfare gains of 0.02 percent of real GDP and also show that trade growth is especially large in manufacturing and services. Regarding agriculture, we also report a somewhat worsening trade balance. We do note however, that the Wageningen report mainly shows changes in bilateral trade between the Netherlands / EU and the Mercosur block. The results that we have reported are broader than this, in that they also account for changes in trade between the Netherlands / EU and other economies. Quantitatively, the effects that we estimate on total trade sometimes are somewhat smaller than those reported by Wageningen, even though they point towards a qualitatively similar dynamic. Regarding the observation by Wageningen that earned nominal incomes in agriculture may decrease

10 https://www.wur.nl/nl/publicatie-details.htm?publicationId=571025cb-5259-4937-a924-53bbc505dc9d

somewhat, we also report that nominal incomes in agriculture could decrease somewhat. However, in addition, we also estimate that the aggregate price level for agricultural products decreases more so that the welfare contribution is positive. We have also commented that this net welfare gain also will have distributional effects that we have not estimated. A reasonable interpretation of the combination of our estimates and those by Wageningen is that Dutch agricultural producers will lose some nominal income, but that the Dutch economy as a whole stands to gain welfare due to lower prices. Next to agriculture, our report also suggests income and price changes for manufacturing and services. These appear to be unambiguously positive.

Appendix A Additional results

Appendix A.1 Detailed trade substitution

In order to better assess the effects on trade, Table A.1 shows the substitution patterns in trade in changes in real USD rather than percentage changes. Table A.1 has four panels: one for the total changes, and three for changes in agriculture, manufacturing, and services. Each panel can be read both across the rows, as it can across the columns. Reading it by row corresponds to reading from the exporter perspective, whereas reading from the column represents the importer perspective. For instance, the first row of the table shows Argentina's exports to the countries labelled in the columns. Note that this also includes Argentina's 'exports' to Argentina – i.e. non-exported Argentinian output. The last two columns show the total change in exports (excluding non-exported domestic output) and the total effect (including non-exported domestic output). There are also similar rows for the imports side.

Table A.1 highlights several dynamics in changing patterns in international trade.

First, looking at the changes in total trade, Brazil and the EU26 are the largest drivers in trade changes. In the top panel, we see Brazil's exports increase by around USD 10 bln. and its imports by around USD 11 bln. The changes in exports and imports by Argentina, Paraguay and Urugay are smaller. Within the Mercosur block, the country with the second largest increases in exports and imports is Argentina, which increases exports by around USD 2 bln. and imports by USD 2.3 bln. If we're looking at the Netherlands and the EU, we see that changes are largely associated with trade with Brazil.

Second, swings in EU-Mercosur trade changes are partially offset by swings in 'within-country trade' (i.e. non-exported output) and in trade with the rest of the world. The increase in Brazil's exports of around USD 10.3 bln. is a net effect of an increase of USD 12.3 bln. in exports to the Netherlands and the EU26, that is partially offset by a decrease in exports to other destinations. This reflects that exports that formerly went to other destinations are redirected towards Europe. A similar pattern is visible with respect to intracountry trade flows that for Brazil decrease by around USD 9 bln. This reflects the fact that goods that formerly were not exported (for instance due to prohibitively high trade costs), are now exported (so not consumed at home). The resulting net effect for Brazil is an increase in real trade of USD 1.5 bln. Similar dynamics are visible for all other countries in the model.

Third, in real value terms, the largest effects are seen in manufacturing and to a lesser extent in services. This is partially the result of the fact that these industries for most countries account for the bulk of GDP and trade. Such a large 'base' means that in value terms there is more value to redirect towards new trading partners.

Looking within industries, most of the dynamics mentioned above hold as well: Brazil is the country that drives most of the effects and domestic and rest of the world substitution is very important. Agriculture provides a clear illustration. In agriculture, Brazil is estimated to increase exports to the Netherlands and the EU26 by USD 3.4 bln. However, Table 2.1 also highlights that total Brazilian exports only increase by USD 0.7 bln., in large part due to a decrease in exports to the rest of the world. Conversely, we see that the EU26 and the Netherlands are importing less from the rest of the world (USD -0.5 bln. and -1.7 bln. respectively) because of the inflow of Brazilian. However, given that some of these Brazilian exports to Europe are redirected from other (previous) export destination, we also see an increase in Dutch and European exports to the rest of the world. The fact that Brazil moves produce out of other export destinations in order to serve the European markets, reveals an opportunity for

Dutch and European exports to grow in these markets. This dynamic is less visible in for instance services, where the main driver of export growth by Dutch and EU economies is in Mercosur economies (in particular in Brazil).

Table A.1 Disaggregated real trade effects (exports and imports)

Region	Exporter \ Importer	MERCOSUR				EU		Rest of the World	Total Δ Exports (EUR)	Total Δ (EUR)
		Argentina	Brazil	Paraguay	Uruguay	Netherlands	EU26			
	Total									
MERCOSUR	Argentina	- 1.411	- 276	- 40	- 6	540	2.660	- 1.115	*1.763*	*352*
MERCOSUR	Brazil	- 153	- 7.980	- 4	14	1.856	9.119	- 1.560	*9.273*	*1.293*
MERCOSUR	Paraguay	- 6	- 23	- 102	-	16	196	- 57	*125*	*23*
MERCOSUR	Uruguay	- 15	- 43	- 9	- 286	167	438	- 184	*354*	*68*
EU	Netherlands	242	893	18	19	- 934	- 88	24	*1.108*	*174*
EU	EU (26)	2.868	12.528	221	322	- 825	- 10.413	- 2.863	*12.251*	*1.838*
	Rest of the World	- 923	- 3.332	- 47	15	- 575	- 169	5.016	*- 5.031*	*- 15*
	Total Δ Imports (USD)	2.013	9.747	139	363	1.179	12.156	- 5.755		
	Total Δ (USD)	602	1.767	38	78	245	1.743	- 739		
	Agriculture									
MERCOSUR	Argentina	21	25	1	-	203	517	- 663	*83*	*104*
MERCOSUR	Brazil	- 3	- 155	- 2	- 2	583	2.433	- 2.394	*615*	*461*
MERCOSUR	Paraguay	- 3	4	3	-	8	52	- 51	*10*	*13*
MERCOSUR	Uruguay	-	1	-	- 6	46	63	- 88	*22*	*16*
EU	Netherlands	2	67	1	2	- 223	13	152	*236*	*13*
EU	EU (26)	44	370	13	15	- 119	- 1.140	880	*1.203*	*63*
	Rest of the World	38	99	3	5	- 459	- 1.550	1.833	*- 1.863*	*- 30*
	Total Δ Imports (USD)	*79*	*565*	*16*	*21*	*263*	*1.528*	*- 2.165*		
	Total Δ (USD)	*100*	*411*	*19*	*14*	*39*	*388*	*- 332*		
	Manufacturing									
MERCOSUR	Argentina	- 1.431	- 301	- 41	- 6	309	1.963	- 311	*1.613*	*182*
MERCOSUR	Brazil	- 150	- 6.236	- 2	16	744	5.368	731	*6.708*	*472*
MERCOSUR	Paraguay	- 4	- 27	- 104	-	8	144	- 6	*115*	*11*
MERCOSUR	Uruguay	- 15	- 44	- 9	- 280	120	365	- 96	*322*	*42*
EU	Netherlands	122	581	17	14	- 380	- 171	- 117	*447*	*66*
EU	EU (26)	2.313	9.762	208	283	- 592	- 7.743	- 3.139	*8.835*	*1.091*
	Rest of the World	- 576	- 2.919	- 50	10	- 109	981	2.677	*- 2.663*	*13*
	Total Δ Imports (USD)	*1.691*	*7.053*	*123*	*317*	*480*	*8.650*	*- 2.937*		
	Total Δ (USD)	*260*	*817*	*19*	*38*	*99*	*906*	*- 261*		
	Services									
MERCOSUR	Argentina	- 2	-	-	-	29	180	- 141	*67*	*65*
MERCOSUR	Brazil	-	- 1.590	-	-	529	1.318	103	*1.950*	*360*
MERCOSUR	Paraguay	-	-	-	-	-	-	-	-	-
MERCOSUR	Uruguay	-	-	-	-	1	9	-	*10*	*10*
EU	Netherlands	118	245	-	3	- 330	71	- 11	*426*	*96*
EU	EU (26)	511	2.397	-	23	- 114	- 1.529	- 604	*2.213*	*684*
	Rest of the World	- 385	- 513	-	-	- 7	400	506	*- 505*	*2*
	Total Δ Imports (USD)	*244*	*2.129*	*-*	*26*	*437*	*1.978*	*- 653*		
	Total Δ (USD)	*242*	*539*	*-*	*26*	*106*	*449*	*- 146*		

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