Trade Facilitation is Still a Worthwhile Objective

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Trade facilitation is vital to the future of international trade. Although tariffs have been reduced throughout the world in recent decades, there still remains significant barriers to trade – these barriers could be reduced by investing in trade facilitation. Many countries, especially developing countries, have not taken advantage of these tariff decreases and of the resulting increased international trade. Investment in trade facilitation would be both cost effective and allow developing countries to engage in more trade, especially in the emerging global supply chain system. The Trade Facilitation Agreement negotiated by the World Trade Organization in December 2013 & July 2014 failed to gain the consensus required. However, even after this setback, trade facilitation is still a worthwhile objective and would be considerably beneficial to international trade.
Trade facilitation is vital to the future of international trade. Although tariffs have been reduced throughout the world in the recent decades, there still remains significant barriers to trade – these barriers could be reduced by investing in trade facilitation. The Trade Facilitation Agreement (TFA) negotiated by the World Trade Organization (WTO) in December 2013 & July 2014 failed to gain the consensus required. The WTO inability to reach consensus on the Trade Facilitation Agreement is both a negative mark on the WTO and detrimental to international trade. However, even after this setback, trade facilitation is still a worthwhile objective and would be considerably beneficial to international trade.

Over the recent decades tariffs have decreased throughout the world, expanding international trade. However, many countries, especially developing countries, have not taken advantage of the opportunities of this increased international trade. Often they are hampered by their lack of infrastructure (port facilities, rail, and road networks), lack of streamlined customs procedures (and modern equipment often necessary for this), and a plethora of bureaucratic rules and regulations that make importing or exporting difficult and time consuming. By investing in these trade facilities, it is believed that costs and time for cargo spent in transit would be greatly reduced and consequently, trade would be increased. Developing countries and their trading partners would all benefit from this.

Traditionally, companies produce a product in their home country, then export it to another country to be sold. However, many people believe the future of industry involves a different model of production: the global supply chain. In this process, materials cross the borders several times, as they are refined, made into parts, and then assembled as a final product. This system is highly dependant upon efficient customs and border-crossing procedures. It is only practical cost-effective if these procedures are in place.

This paper will examine trade facilitation and the movement to formalize a plan to advance trade facilitation. This paper has four main sections: WTO & Trade Facilitation; What is Trade Facilitation & Why is it important?; Global Supply Chain; and Cost Effectiveness of Trade Facilitation.
WTO & Trade Facilitation

In December 2013, members of the World Trade Organization (WTO) took part in negotiations in Bali, Indonesia, at the organization's ninth ministerial meeting (Wilkinson, 2014, p. 2). These negotiations were slightly different than prior WTO talks – which are normally based on “single undertaking”, where all issues are negotiated and adopted together (Babu, 2014, p. 12). Instead, at Bali negotiators focused on some of the 'low hanging fruit', issues that were seen as possible to come to an agreement on. This was in part a result of the lack of any substantial agreement since the Doha Round in 2001; instead of negotiating everything, it was decided to focus on a few issues that could be completed (Wilkinson, 2014, p. 3).

Indeed, the WTO had not completed a major trade agreement since it replaced the General Agreement on Trade and Tariffs (GATT) in 1995 (Koopmann, 2014, p. 2). Although the Doha Round, the fourth ministerial conference in Doha, Qatar in November 2001, had raised many hopes – none of these hopes have been realized. As a result, faith in the Doha package of objectives, in the WTO itself, and even multilateral negotiations - have all been waning.

The past decade has been rough for the world trade organization – specifically for the efforts of trade negotiators to reach a package agreement, even while trade jurists have performed their task of adjudicating disputes with admirable skill and speed. Doha Round negotiations are on the verge of catastrophic failure. the multilateral trading system will be dealt a near fatal blow if nothing results from 12 years of hard negotiations. Prospects for resurrecting the WTO as the premier forum for trade negotiations will be crippled if the work of the Doha Round is cast aside. In short, the year 2013 is shaping up as the “make or break” year for multilateral trade negotiations. (Hufbauer, 2013, p. 9)

The three issues negotiated at Bali were trade facilitation, agriculture, and treatment of Least Developed Countries (LDCs) (Wilkinson, 2014, p. 3). The latter two resulted in an impasse; however the former culminated in an Agreement on Trade Facilitation (“TFA”) (WTO, 2013a, p.1). This was considered to be a very important milestone: “the first multilateral trade agreement successfully negotiated in 18 years and the first such accord
concluded by the WTO” (Neufield, 2014b, p. 3). The terms of the TFA stated the members would establish a Preparatory Committee to draw up a protocol and then it would be submitted to members for ratification: “The General Council shall meet no later than 31 July 2014 to annex to the Agreement notifications of Category A commitments, to adopt the Protocol drawn up by the Preparatory Committee, and to open the Protocol for acceptance until 31 July 2015.” (WTO, 2013a, p. 1)

However, the General Council was not able to form a consensus before the 31 July deadline (WTO, 2014a). As WTO Director-General Roberto Azevedo explained:

> On the one side we have the firm conviction, shared by many, that the decisions that ministers reached in Bali cannot be changed or amended in any way — and that those decisions have to be fully respected. And on the other side of the debate we have some who believe that those decisions leave unresolved concerns that need to be addressed in ways that, in the view of others, change the balance of what was agreed in Bali. (WTO, 2014a)

India blocked the agreement, insisting on linking it to domestic food security concerns; if there was no agreement on food security, then there would be no consensus on trade facilitation (Babu, 2014, p. 2; Hoekman, 2014, p. 3). This was somewhat of a change for India, since in December the Indian minister touted the importance of the “landmark” agreement; however, a new government took power in India between December and July (Babu, 2014, p.1). Agreement in the WTO is based on consensus, not voting, so India’s refusal to consent to the TFA amounted to a veto (Babu, 2014, p.2; Although WTO rules allow for a formal vote to be taken as an alternative to consensus, this has never been done and it is unlikely this optional procedure will be utilized for the TFA). After the failure to meet the July 2014 deadline, it remains to be seen what will happen with the TFA (Hoekman, 2014, p. 3).

What is Trade Facilitation and why is it important?

Trade Facilitation (TF) is a term that, although often used, has varying definitions. Trade Facilitation is “loosely speaking cutting red tape at the
The WTO defines it as: “Removing obstacles to the movement of goods across borders (e.g. simplification of customs procedures)” (WTO Glossary, "trade facilitation"). In its narrow sense, it means making the process of crossing borders smoother and more straightforward. “[T]rade facilitation is 'the simplification and harmonization of international trade procedures', where international trade procedures are the 'activities, practices and formalities involved in collecting, presenting, communicating and processing data required for the movement of goods in international trade’” (Persson, 2012, p. 13; Engman, 2005, p. 6). In its broader sense, the term also includes improvement to the trade infrastructure, such as port facilities, roads, rails, etc.

In a similar definition, the Doha Ministerial Declaration (WTO 2001) formally refers to trade facilitation as 'expediting the movement, release and clearance of goods, including goods in transit'. Hence, loosely speaking, trade facilitation refers to reforms aimed at making it easier for traders to move goods across borders, with a specific focus on lowering transaction costs associated with cross-border trade procedures. (Persson, 2012, pp. 13-14, cit. WTO 2001)

Although tariffs have decreased dramatically, there still remain significant non-tariff barriers (NTBs) to trade. And unlike tariffs, these NTBs normally do not have an objective of raising revenue or furthering a public policy; instead, they are more often simply dead-weight that slows (or prevents) trade. TF has gained traction and relative importance in recent years because “... when tariffs and other non-tariff barriers to trade have been gradually dismantled over the years, this has increased the relative costs of having inefficient trade procedures” (Persson, 2012, p. 12). In other words, as tariffs have decreased, the relative costs of inefficient trade procedures escalate and become more obvious. Many believe that further increasing international trade will require addressing these NTBs: “when measured in tariff-equivalent terms, the 'border effect' of tariff and non-tariff barriers approaches 100 percent. The problem is that responsible policy officials are not rising to the challenge by energetically dismantling barriers that impede trade and investment flows” (Hufbauer, 2013, p. 9).
TF benefits all trading partners, however the effect on LDCs can be the most dramatic. “Trade facilitation initiatives, with the aim of lowering trade transactions costs, can enhance trade competitiveness, and expand trade flows, while at the same time playing an important role in supporting a positive business climate” (Helble, 2009, p. 1). Landlocked countries, who are dependant upon the borders of their neighbours, can also benefit greatly from TF. (Neufield, 2014a, p. 9).

Another obstacle to trade is the delays in shipping: “each additional day that a product is delayed prior to being shipped reduces trade by more than 1 percent. They show that the effect is even larger for time-sensitive agricultural and manufacturing products.” (Königer, 2011, p.14, cit Diankov et al, 2010)

TF would address the time, as well as the costs, involved in shipping, thus making importing/exporting more profitable and, therefore, a more attractive endeavour for businesses.

Global supply chains

As international trade has increased, global supply chains have increased in importance, yet their full potential is far from realized. “A large share of 21st century trade requires integrated global supply chains that move intermediate and finished goods around the world. Intermediate goods account for 60 percent of global commerce” (Hufbauer, 2013, p.11). In global supply chains “goods cross borders multiple times, initially as inputs and ultimately as final products” (Lee, 2014, p. 4). For example, raw materials are imported and processed into parts, and then these parts are shipped to a different country where they are assembled into a finished product which is then sent to yet a different country to be sold to consumers. The costs associated with crossing borders hampers the flow of goods required by such a global production network (Lee, 2014, p. 4). Furthermore, some global manufacturers may spend more on logistics than on the manufacturing itself (Elms, 2013, p.163).

Going forward, this form of production will become more integral to and common-place in international trade: “Such 'supply-chain trade', which is
about making things internationally, as distinct from traditional trade in the form of selling goods and services internationally, is the most dynamic segment of international commerce” (Koopman, 2014, p.2). As this type of production is utilized more frequently, it will become more important to streamline the border crossing process; or perhaps to explain it another way, until the border crossing process is streamlined, such global production will be limited and under-utilized.

As goods cross borders many times, first as inputs and then as final products, fast and efficient customs and port procedures are essential. Unduly complex processes and documentation raise costs and cause delays, and ultimately, businesses, economies and consumers bear the cost. Conversely, a country where inputs can be imported and goods and services can be exported within quick and reliable time frames is a more attractive location for foreign firms seeking to invest. (OECD, 2013, p. 1)

Since tariffs have been significantly reduced world-wide, there is probably more fertile ground in focusing on trade facilitation, instead of solely on tariffs. “Also, there are several empirical analysis results showing that the gains in global trade from smoother border procedures could be higher than the gains from tariff reduction” (Lee, 4). The increase of such trade facilities can greatly benefit developing countries: “The improvement in such logistics performance has been empirically shown to have the greatest positive effects in expanding trade for developing countries” (Lee, 5). The future growth of international trade is correlated to further developing global supply chains - which require greater trade facilitation.

Cost effectiveness of Trade Facilitation

Proponents have long argued that investment by developed countries into the trade facilitation of developing countries would yield an increase in overall trade, worth the initial investment. Indeed, some recent studies have examined this in depth and have supported this conclusion: “These results indicate that aid for trade, in particular if highly targeted, can have a significant impact on the costs of trading” (Königer, 2011, p.11). This study concluded that an increase in aid of $2.89 million would yield a 1.2% decrease
of costs; it further calculated that a 1.5% reduction in costs would increase trade from 3 to 8.75\%.³

Other studies have examined the potential global impact: “If countries improved these factors [border administration, telecommunications, and transport infrastructure] more modestly, halfway to the region’s best practices, world GDP could increase by $1.5 trillion or 2.6 percent, and world exports of goods could increase by $1.0 trillion or 0.4 percent” (Hufbauer, 2013, p. 13).

Another study revealed investment into TF can greatly increase trade: “...based on aid from 2007 data of US$ 117 million, a 1% increase in aid (US$ 11.7 million) could generate a trade increase of about US$ 818 million. This yields a ‘rate of return’ on every additional dollar of aid of about US$ 697” (Helble, 2009, p.18). The largest share of aid for trade is focused on improving infrastructure.⁴

TF can also lower costs of trade, which not surprisingly are normally higher in LDCs. “Average trade costs in LDCs are considerably higher than in non-LDCs (1,805 versus 1,260 US$ for cost to export [a 20ft dry-cargo container weighing 10 tons] and 2,246 versus 1,453 US$ for cost to import, respectively)” (Königer, 2011, 15; for the sample container description: see cit 6 on p. 5).

However, for aid to be effective, it must be focused and significant: “...we argue that very low aid flows are too marginal to show any influence on the cost of trading. Accordingly, our hypothesis is that aid flows only become effective when they reach a certain (threshold) level. [. . .] It seems that – on average – only larger development projects are successful in reducing trade costs” (Königer, 2011, p. 16).

Although often a large initial investment is required, once the changes are made the annual expenses may be modest: “Measures that entail a significant upfront investment to introduce are not necessarily costly to operate once set up — the best example is a single window mechanism for submission of documentation” (OECD, 2013, p. 3). In Costa Rica, the creation of such a single window had a significant impact on the time required to get through the border; the single window system “helped reduce clearance time for dairy products from 10 to 1.5 hours, and for agrochemicals from 27.5 to 2.2 hours”
Such drastic reductions in time spent in border-crossing can have substantial implications on businesses considering trading internationally, such as global supply chains but also small businesses that may not normally take part in international trade.

Most exporters are large enterprises; Small and Medium size Enterprises (SMEs) are often reluctant to export/import. “Only the most productive firms are able to make profit withstanding the additional costs associated with exporting. Less productive ones cannot do so and only produce for the domestic market” (Li, 2009, p. 1). However, SMEs are an important employer and this tends to increase as nations develop: “SMEs contribute up to 45 percent of the World’s employment on average; and up to 33 percent of employment in developing countries” (Duval, 2014, p. 2).

One study examined the affect of trade facilitation upon SMEs in Asia, and found that improving trade facilitation increased the likelihood of an SME partaking in international trade, specifically “increasing policy predictability and enhancing IT services are the most effective. SMEs appear to be less responsive to improvement in transportation infrastructure than large enterprises” (Li, 2009, p. 2). For SMEs, it is important to understand what the costs and procedures are before they begin to trade internationally; when these cannot be discerned or accurately predicted, SMEs are reluctant to engage in international trade. By advancing TF, international trade would become more attractive to SMEs.

The OECD calculated the possible trade cost reductions of the Bali TFA, based on either a limited implementation or a full implementation: 11.7-14.1% for low income countries; 12.6-15.1% for lower middle income countries; and 12.1-12.9% for upper middle income countries (OECD, 2014b, p. 2). The Peterson Institute for International Economics estimated the impact of trade facilitation (albeit, prior to the December 2013 drafting of the TFA) at over one trillion USD worth of increased exports globally, over 20 million jobs created, and an almost 1 trillion USD increase in GDP (Hufbauer, 2013, p. 7).

“In addition, compared with other types of liberalization, trade facilitation is a relatively easy subject to agree on because it will (in general) not lead to reduced government revenue – it may in fact increase it” (Persson, 2012, p. 12). TF reduces costs, increases the predictability of procedures, and reduces time spent crossing borders – all of which leads to increased trade.
Conclusion

Many business and political leaders see the failure to generate anything concrete from the Doha Round, or the Bali Accords, as a major setback to the WTO; however, there is still strong support for the WTO (Fung, 2014, p. 2). It is clear, from the different focus of negotiations at Bali, forsaking the single-undertaking method, that the WTO yearns to realize a new agreement - even if only to complete something, anything, since the 1994 agreement that created the WTO. From the possible areas negotiated at Bali, TF is still the most likely field where consensus could be gathered. If the WTO were able to convert the TFA from a defeat into a victory, it would restore faith in the WTO and in the multilateral negotiation system. Furthermore, and perhaps more importantly, it would have a beneficial impact upon global trade, especially for developing countries.

It is unclear what will happen to the TFA since the July deadline was missed. However, most of the countries still support, at least in theory, the TFA. If India could be convinced, or bargained with, then it is certainly conceivable that consensus could be gained and a new path created to finalize the TFA. The likelihood and possible mechanics of arranging an amicable resolution with India is outside the scope of this paper; however, certainly such a resolution is theoretically possible, even if it may be difficult.

Of course, the WTO Trade Facilitation Agreement is not the only avenue available for the furtherance of trade facilitation. Countries already negotiate TF between themselves, frequently between a donor nation and a LDC. Heretofore, there have been numerous aid for trade programs; if these programs were expanded and focused on appropriate TF objectives, then a significant positive impact could be obtained, both for the developing country and for the trading partner. By increasing TF in LDCs, these countries would become more competitive in both international trade and as partners in the growing global supply chain; moreover, international trade would enlarge.
Endnotes

1 But see: Kharel, 3: “Improvement in the competence of the local logistics industry in LLDCs [Land-Locked Developing Countries] is found to have the biggest impact on LLDC exports. A particularly interesting finding is that improving the efficiency of clearance at the customs/border in LLDCs is more important than doing the same in transit countries as far as boosting LLDC exports is concerned. But non-customs-related aspects of trade facilitation in transit countries, such as ease and affordability of arranging international shipments and transport and information technology infrastructure, remain important areas needing reform to help increase LLDC exports.”

2 Although the paper speculated reducing shipping time would reduce costs as well, it was not proven in the calculations of their data sample. “Overall, the aid variables’ main objective is to make trade more cost-efficient. Reducing the time for trading is one (important) channel by which trade costs can be lowered. However, we cannot observe this correlation in our results.”

3 “Assuming similar elasticities for our trade cost measures, for Trade Facilitation we find that reducing trade costs by 1.5 percent leads to an increase in trade volumes in the range of 3 to 8.75 percent. Taking into account that these aid flows are very specific and in volume rather exiguous, their impact can be considered substantial.” Königer, 12.

4 “… infrastructure is the largest category of aid for trade: infrastructure projects account for about 54% of the global aid for trade portfolio.” Hoekman, 2010, 14.

5 Hufbauer, 7. Specifically: 1.043 trillion US dollar increase in exports; 20.6 million jobs created; 960 billion US dollar GDP increase. “These payoffs are broad estimates and represent permanent annual static gains for the world economy.”
References


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