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SOME REASONS NOT TO NEGOTIATE EXPORT TAXES AND RESTRICTIONS IN THE WTO NAMA NEGOTIATIONS

This Analysis briefly examines some of the economic and policy reasons behind the application of export taxes and export restrictions in developing countries. The elements enumerated in this note provide arguments against negotiations aimed at further restricting the use of this type of policy tools, as currently being proposed by developed countries in the WTO NAMA negotiations.

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SOME REASONS NOT TO NEGOTIATE EXPORT TAXES AND RESTRICTIONS IN THE WTO NAMA NEGOTIATIONS

I. INTRODUCTION

1. The use of export restrictive measures as a trade policy-instrument dates as far back as 1275 when England imposed export duties on wool and hides.[1] By 1660, England applied export taxes on more than 200 products.[2] During the 18th and 19th centuries, export taxes were introduced in colonies in Asia, Africa and Latin America primarily for revenue raising purposes. Discriminatory taxes and rebates on exports from the colonies were also used to favour exports to the colonizing countries.

2. Today, export taxes continue to be a common policy instrument in many developing countries. Export taxes are usually instruments implemented as part of policies aimed at fostering the industrialisation and diversification of developing countries or are applied for revenue raising purposes.

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[1] Devarajan, S., Go, D., Schiff, M. and Suthiwart-Narueput, S., 1996, "The Whys and Why Nots of Export Taxation, the World Bank.
[2] Ibid.

3. Nevertheless, the use of export taxes and other export restrictions could be curtailed under the WTO NAMA negotiations[3]. In fact, notwithstanding the importance of these instruments for several developing countries, export restrictions have recently been the subject of proposals that aim at restricting or prohibiting their use. These proposals, submitted by developed countries, neglect the motivations behind the use of export restrictions and, if adopted, could further restrict the policy options that poor countries have to implement their developmental strategies. This note succinctly enumerates some of the reasons why export taxes are used and why their prohibition would be a mistake from a developmental point of view.

II. THE PROPOSED PROHIBITION OF EXPORT TAXES AND RESTRICTIONS

4. Recent proposals by developed countries, submitted separately by Japan[4] and by the European Communities[5], concur in so far as they request WTO Members to consider restricting, or completely banning, the use of export taxes and restrictions. While the EC proposal targets more specifically a reduction, restriction or even prohibition of export taxes, the Japanese proposal concentrates mostly on new legal provisions to enhance transparency in the application of export restrictions.

5. According to the EC, export taxes artificially transfer gains from trade between WTO members to the countries imposing them and provide an unfair advantage to the producers of the country where export taxes are applied when these producers export to third countries. Finally, according to the EC, most countries applying these measures have set prohibitive levels of taxes (15% or more).

6. Hence, the EC proposal calls for a complete elimination of export taxes over a period of time, with the exception of few measures falling within a negotiated positive list, which would be authorized but subject to a maximum (bound) level. Developing countries currently have the right to apply export taxes, so this restriction or prohibition of export taxes would consist of new measures, proposed in the form of a new "*WTO Agreement on Export taxes*". Under the EC proposal, the provisions and exceptions of GATT XII, VIII, XX and XXI would remain available.

7. Since existing WTO Agreements already impose restrictions in the use of most export restrictions (e.g. general prohibition of quantitative restrictions with circumscribed exceptions and obligation to apply quantitative restrictions in a non-discriminatory manner), the Japanese proposal concentrates more specifically on how to enforce such

[3] Non-Agricultural Market Access (NAMA) negotiations were mandated by the WTO Doha Ministerial Declaration (2001) and aim at reducing or eliminating tariffs and non-tariff barriers applied to non-agricultural products.
[4] Communications from Japan: "*Enhancement of disciplines for quantitative export restrictions on natural resources such as minerals*" (JOB(06)/14, 1 February 2006)"*Text-based contribution for negotiation on enhanced disciplines on export restrictive measures*" (JOB(06)/29, 24 February 2006), "*Text-based contribution for negotiation on enhanced transparency on export restrictions*" (JOB(06)/29/Rev.1, 20 March 2006), "*Progress report: Proposal for enhanced transparency on export restrictions*" (JOB(06)/21/Rev.1, 12 April 2006), and "*Modification history of the text for enhanced transparency on export restrictions*" (JOB(06)/29/Rev.2, 18 April 2006).
[5] Communications from the EC: "*Activity report on export taxes to the NGMA*" (JOB(05)/321, 08 December 2005), and "*Negotiating proposal on export taxes*" (TN/MA/W/11/Add.6, 27 April 2006).

provisions. Therefore it aims at introducing new detailed procedural requirements to enhance the transparency in the creation and management of export restrictions (publication and notification of new measures, obligation to provide specific information, data and statistics). The stringency of the new provisions would be tantamount to those of the existing Import Licensing Agreement.

III. WHY DO DEVELOPING COUNTRIES NEED EXPORT TAXES?

8. As trade policy instruments, export restrictions take various forms: export taxes, export bans, export quotas and licenses, regulated exports and supervised exports. However, export taxes and export quotas and licenses have been the most commonly used export restriction instruments. In general, it is argued that export taxes are the preferred instrument among the various instruments for export restrictions because export taxes are transparent and easy to administer compared to, for instance, export quotas and licenses, which require cumbersome quota and license administration and may lead to an inefficient allocation of rents owing to the activity of local pressure groups.

9. As far as product coverage is concerned, agricultural products, fishery products, mineral and metal products, and leather, hides and skin products are the products on which export taxes are most frequently imposed.[6] The main arguments in favour of the use of export taxes by developing countries are:

A. The terms of trade argument

10. In simple terms, 'terms of trade' refers to the purchasing power of a country. A decrease in a country's export price relative to its import price implies deterioration in the country's terms of trade. Export earnings are important for financing imports. A country whose terms-of-trade has deteriorated for a prolonged period would have difficulties in financing its imports, particularly when its reserves are low and it has limited access to international finance. Such has been consistently the case for most developing countries.

11. A large number of developing countries export primary commodities (both agricultural and non-agricultural) for which the long-term prices have been falling sharply since the 1980s. In the 1980-92 period, the World Bank's index for non-oil commodity prices fell by almost 50 per cent.[7] The price fall has not been any gentler since the turn of the new millennium. During the 1997 – 2001 period, the UNCTAD combined price index of all commodities in US dollars fell by 53 per cent in real terms.[8] In other words, commodities lost more than half of their purchasing power in comparison with manufactured goods in only four years.

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[6] Piermartini, R., 2004, "The Role of Export Taxes in the Field of Primary Commodities," World Trade Organization

[7] see, Devarajan et al., Op. Cit.

[8] UNCTAD, 2003, "Economic Development in Africa: Trade Performance and Commodity Dependence", United Nations, Geneva.

Box 1: How damaging is a terms of trade deterioration for economic growth?

"A major explanation for the poor economic performance of the region [Africa] in the past two and a half decades is the significant loss of resources due to adverse terms of trade. World Bank estimates suggest that the cumulative loss resulting from adverse terms of trade over a period of almost three decades (1970–1997) for African non-oil-exporting countries (excluding South Africa) amounted to 119 per cent of the combined GDP of these countries in 1997, 51 per cent of cumulative net resource flows, and 68 per cent of net resource transfers to the region (World Bank, 2000: 21–22). Research carried out by the UNCTAD secretariat indicates that if SSA terms of trade had remained at 1980 levels, the share of the subcontinent
in world exports would have been double its current level."

Source: UNCTAD, 2003, "*Economic Development in Africa: Trade Performance and Commodity Dependence*", United Nations, Geneva.

12. The tenet of the terms-of-trade argument for export restriction is that export taxes and other forms of export restrictions could improve the terms of trade of a country when the country has a market power on the commodity, i.e., the ability to influence the world prices of a particular commodity. Let us see the dynamics of such a restriction by a large country by using an export tax as an example.

13. A large country, i.e. one with sufficient market power in a particular commodity, has the ability to influence the world price of the commodity. An export tax on the commodity imposed by that country has the effect of creating a wedge between the domestic and the international prices of the commodity. The export tax would increase the world price of the commodity, while maintaining domestic prices unaltered. If the demand for the commodity is perfectly inelastic, i.e. consumers in importing countries do not react to the increased price by reducing their consumption, the incidence of the export tax would be entirely borne by consumers in the importing countries. Producers in the exporting country would continue to benefit from the same price for their commodities while the government of the exporting country gains from the tax revenue.

14. When the demand, however, is not perfectly inelastic but slops downward, as is often the case, the export tax is expected to increase the world price of the commodity, but not by the full extent of the tax. Part of the tax incidence is borne by domestic producers. This is because when demand for the commodity is not perfectly inelastic, consumers would cut their consumption in response to the higher price caused by the export tax. As a result, the domestic supply of the commodity would increase while the price in the domestic market would fall.

15. In both cases, an export tax on a commodity can improve the terms of trade of the imposing country as it increases the prices for its exports. As can be seen from BOX 1, adverse terms-of-trade is a serious concern in many developing countries and has been among the major source of low economic development. The use of export taxes by large countries is thus a desirable objective for these countries. In fact, as indicated by Bhagwati, unexploited market power on the world market is a distortion from the

viewpoint of the exporting country.[9] Even the presence of strategic considerations such as the retaliation by importing countries, or free-riding by other smaller exporters does not entirely wipe-out the terms of trade gains for a large country to impose the export tax. Hence, strategic responses by importing and other exporting countries to the export tax levied by the large country do not affect the basic desirability of the export tax but its optimal level.

16. The terms-of-trade argument is not applicable for countries that lack the market power to influence the world prices. If a small economy imposes an export tax, the incidence of the tax would entirely fall on domestic producers. However, since the tax will have no effect on the world market, the country will not see any improvement in its terms of trade.

B. The Economic Diversification Argument

17. Economic diversification has been the core economic development objective for many developing countries. In fact, one of the factors which explain the economic vulnerability that plagues many developing countries is their reliance on only one, or a very small number of, export product and export market. The economy and trade of a large number of developing countries are indeed dependent on few primary products (agriculture, forestry products, leather, hides and skins, fish and fishery products and mineral resources). Economic diversification is regarded as the first-best solution to many of the economic ills that mire a large number of developing countries.

18. Economic diversification can take two forms: horizontal and vertical. Horizontal diversification refers to a shift from traditional commodities (i.e. with low demand elasticity and price) to dynamic commodities (i.e. one with high demand elasticity hence high price); for example, a shift from the production of coffee to cut-flowers or fruits and vegetables. Horizontal diversification also refers to a sectoral shift, e.g. from mining to a service sector such as tourism and so forth.

19. Vertical diversification refers to downstream movement along the value chains of commodity production through value-addition. It implies adding value on primary product through the various stages of processing and /or distribution.

20. The important question is: how would export restrictions, in this case export taxes, be useful for achieving horizontal and vertical diversifications?

21. A country, regardless of its market power, can provide an incentive for both vertical and horizontal diversification by imposing export a tax on its traditional exports and by concomitantly exempting products towards which it seeks to diversify from any export tax . For example, by imposing a tax on raw coffee, a coffee producing country may discourage the export of coffee in its primary form (raw) and encourage diversification towards more processed forms of coffee or the diversification away from it, in favour of new sectors.

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[9] As cited in , Devarajan et al., Op. Cit.

22. The use of export restrictions, particularly export bans and export taxes, for the purpose of encouraging vertical diversification has been common in most developing countries. There are mainly two versions of arguments for this:

1. *The "infant Industry" argument or the Input Subsidization argument*

23. Export restrictions have been often pursued under the "infant industry" argument. The infant industry argument states that temporary protection and subsidization of a newly established manufacturing industry could enable the development of a comparative advantage in that industry. In this context, export restrictions such as export taxes that lower the domestic price of raw materials would provide a cost-advantage in the form of subsidized input to the domestic industry.

24. The relevance of a shift towards a high value added segment of the value chains of commodity production has been even more pronounced today. However, the feasibility of resource-based industrialization has long been a subject of academic controversy.

25. The economic activities of resource-rich developing countries have been mostly concentrated on the low-value end of activities, often producing primary commodities through growing cash crops or extracting mineral resources. While the processing, packaging, labeling and distribution activities are monopolized by developed countries' parastatals.

26. A number studies showed that firms operating in the high-value added segment of the commodity value-chain made lucrative profits while the income that primary producers obtain is hardly enough for meeting their basic subsistence needs. Hence, diversification into a high value added segment of the value chain of commodity production has often been regarded as the optimal development objective that developing countries need to attain.

2. *Countervailing Tariff Escalations*

27. In addition to serving as "indirect input subsidy" to domestic industries, export taxes could be regarded as countervails to a tariff escalation in importing countries. A tariff escalation by importing countries reduces the competitiveness of processed or semi-processed articles imported from abroad. For instances, if Côte D'Ivoire manages to raise the world price of cocoa through the use of an export tax or through other export restriction instruments, Japan (whose tariff escalates from 0% for raw cocoa beans to 32% for chocolate) would have to buy the raw cocoa at a higher price from the international market. At the same time, the tax would lead to a fall of cocoa price in the domestic market thereby indirectly subsidizing the chocolate industry in Côte d'Ivoire. In this case, the export tax could be used to countervail the unfair advantage that the Japanese chocolate industry would obtain from the tariff escalation.

C. The Tariff Revenue Argument

28. This is a straight forward argument. Export taxes, particularly on agricultural goods, have been used as a major source of government revenue since colonial times.[10] This is mainly attributed to the low tax-base in most developing countries and the relative administrative simplicity and the political feasibility of export tax as compared to other options such as income, consumption and land taxes.

29. Despite the decline in its contribution to the total tax revenue in developing countries, export tax remains a significant source of government fiscal revenue in a number of developing countries. In countries such as Burundi, Sri Lanka, Mexico, Ethiopia and Guinea export taxes account for more than 20 per cent of government revenue.[11] The contribution of export taxes to total government revenue is also high in Cameroon, Ghana, Syria and Costa Rica [12].

D. Countervailing Monopsony Power

30. An important question that one may ask is: What are the relevant factors that determine developing countries terms of trade? In other words, what is the share of the final prices of primary commodities that goes to producers in developing countries; and how soon changes in final prices of commodities in the world market pass-though to producers? These are important questions to consider because they put the discussion in export restrictions and export taxes in the context of imperfect competition, which is the real context for most primary commodities of export interest to developing countries.

31. The markets for primary commodities have been increasingly dominated by a handful of multilateral buyers. This phenomenon, known as "market concentration", has come to be the norm rather than the exception in almost all major commodity markets. The increasing concentration in buyer-power and the oligopsonistic nature of primary commodity markets are easy to explain for internationally agricultural primary commodities. For example, four multinationals (Kraft, Procter & Gamble, Sara Lee, and Nestlé) dominate the coffee market. In the early 1990s the coffee earnings of exporting countries were around US$10-12 billion out of the retail sale of around US$30 billion, i.e., around 30 per cent of the retail sales were appropriated by the coffee-producing countries.[13] In 2002, retail sales exceeded US$70 billion, but the earnings of the coffee-producing countries fell by around 50 per cent to about US$5.5 billion.

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[10] Khan, H. M., 2001, "Agricultural taxation in developing countries: a survey of issues and policy," Agricultural Economics 24(2001): 315-328.
[11] Devarajan et al., 1996, Op. Cit, P. 7.
[12] Khan, H. M., 2001, Op. Cit, p. 19.
[13] Action Aid, 2005, "Power hungry: six reasons to regulate global food corporations," http://www.actionaid.org.uk/_content/documents/power_hungry.pdf.

32. The question: what could explain this "disconnection" between the prices or earnings that go to producing countries and the prices that final consumers pay? The answer is the market structure.

33. A handful of multinational corporations that dominate the markets for most primary commodities use their "oligopsony" power to purchase primary commodities from producing countries at a lower price and use their "oligopoly" power to sell the commodities at a higher price. A number of studies that utilized the "value chain" analysis have consistently shown the proportionality of profits to market power in the value-chains of trade in commodities. Developing countries that face a single or few buyers for primary commodity exports have seen dwindling shares in final sales value and hence a loss of producer's surplus due to falls in prices and quantity exported which would not have been faced had the market been competitive. The abolition of state marketing boards wiped-out the countervailing force against the oligopsonic power of single or few multilateral buyers. Therefore, export restrictions such as export taxes levied by the producing countries could be one possible corrective measure.[14] Export taxes would further reduce the volume of export, but offers a way by which exporting countries can appropriate a part of the profits of the monopsonists and/or oligpsonists.[15]

IV. THE MAJOR ARGUMENTS AGAINST EXPORT RESTRICTIONS

34. The use of export restrictions as trade policy instruments has become a polemic terrain of academic and policy debates. Much of the objection to export restrictions is ascribed to their efficiency and distributional impacts. The opponents of export taxes argue that export taxes levied by a large country, by leading to a fall in domestic prices and increase in world prices of the taxed goods, unfairly punish producers and consumers of the importing countries; while favouring domestic consumers, including local processors that use the taxed product as an input in their production, in the producing country. When levied by a country with no or little market power, the effect of export taxes is to benefit local consumers and processors at the expense of local producers. In general, export restrictions that lower domestic prices are equivalent to taxes on producers and subsidies to consumers.

35. In addition, by restricting trade in low cost goods and resulting into higher prices of the goods in international markets, it is argued that export taxes lead to production and consumption inefficiencies.

36. The possible negative environmental effects of export taxes are also sometimes brought up by the opponents of export restrictions. It is argued, sometimes backed by empirical evidence, that by lowering the domestic price of raw materials such as logs, iron ore, etc., export restrictions encourage reckless use of resources in a way that damages the environment. In addition, in so far as it reduces domestic prices,

[14] See, Deardorff, V. Alan and Rajaraman, Indira, 2005, "Can Export Taxation Counter Monopsony Power," Discussion Paper no. 541, Gerald R. Ford School of Public Policy, the University of Michigan.
[15] Ibid.

domestic producers will have little incentive to invest in environmentally safe technologies and practices.

V. CONCLUSION

37. While it is true that the use of export taxes has slightly faded away over the recent years, either because of unilateral reforms or because of commitments undertaken in the context of regional or bilateral trade agreements, they remain useful instruments in many cases for developing countries.

38. Moreover, it is also true that export restrictions and taxes alone are certainly not sufficient to trigger diversification. Nor are they always the best policy instrument for all policy objectives of developing countries. However, there are a number of cases where targeted export restrictions on primary commodities, for instance, by countries which have market power, could be not only desirable, but very effective in implementing development and industrial policies.

39. Yet, developing countries may find it useful to defend their policy space or policy discretion regarding policy instruments that are available to them, including export restrictions. Seen under this light, the proposals by Japan and the EC that aim at restricting or disciplining the use of export subsidies tampers with the policy space and capacity to implement development strategies of developing countries.

40. In fact, the complete prohibition at the multilateral level of export taxes would constitute an additional policy constraint, which should not be seen in isolation of other constraints, such as the removal of tariffs, the prohibition of certain subsidies and the effects of several other WTO rules being negotiated. Accepting further restrictions on the use of yet another policy instrument, i.e. export taxes, will certainly not assist developing countries in reducing their economic vulnerability and better integrating their economies to the multilateral trading system.

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