THE OUTCOME OF CLOSER ECONOMIC LINKS WITH THE EEC FOR LDCS' EXPORTS PREVIOUSLY DUMPED IN WORLD MARKETS

AN EMPIRICAL INVESTIGATION[1]

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1. Import duties on export goods

COMMERCIAL policy specialists are sometimes bewildered when analysing the tariffs of many semi-industrialized countries, by the existence of high rates of customs duties on precisely those goods for which these countries are *a priori* expected to have a comparative advantage in production. Conventional trade theory does not count on the presence of *import* duties on those foreign goods which directly compete with exportables.[2] In practice, however, this is a very common case, as will be shown later.

There are a series of answers to the paradox, which are of non-theoretical nature:

1. Internal transport or storage costs may be high enough to prevent arbitrage inside the country, specially if the latter is big and the merchandise concerned is bulky or deteriorates rapidly. Thus it is perfectly possible that some regions of the country export the same good which other regions import from third countries. This has sometimes been called border trade. A typical case is the oil trade between Canada and the United States, the oil being shipped in opposite directions on the east and west coasts.[3]

2. The tariff position considered may cover quite heterogeneous products, so that the duty really applies only to some of the goods of the category, while others are being exported at international prices and with no imports taking place. Here we recognize the existence of intra-industry trade in differentiated products, due to the existence of economies of scale brought about by long runs operated in particular industries (e.g. chemicals). Partly (but not completely), the problem can be overcome by taking tariffs on highly disaggregated products.

3. The duty may be a historical curiosity or more generally speaking redundant.

However, it is clear that there is a fourth possibility of high relevance

[1] I am indebted to Pham Thuy for her help in the computation of statistical material.

[2] This does not imply that an *export* tax exists. But the latter may be charged at the border on the domestic good which *leaves* the country.

[3] Other intra-industry trade in functionally homogeneous products must be excluded here, such as trade in seasonal products or entrepot trade, because it would be irrational in these cases to impose import duties. For a comprehensive review of the theory of intra-industry trade, see [5].

when explaining the trade of semi-industrialized countries, namely the existence of price discrimination. To illustrate its practical importance, we have included an Appendix with the cases registered by the GATT Committee on Anti-Dumping Practices from mid 1970 till the end of 1975 and reported by GATT members, which either opened an investigation or which took provisional action against the country accused of practising dumping. From the table it clearly appears that there has been an absolute increase in the number of investigations opened against semi-industrialized countries' products. This is also true in relative terms when compared to dumping practices of developed countries. To illustrate the quantitative importance of the trade covered, two figures for each tariff position have been included: world imports originating in the country being investigated and the export market share of the country in total world export trade. The year selected was the one in which the opening of the case took place.

Contrary to the usual assumption of perfect competition in the domestic markets considered, monopoly may prevail. If the local producer is competitive at given world prices and thus can export, the imposition of an import duty allows him to practice discrimination. Domestic consumers will pay a price higher than the world price charged on exports. Of course, the duty stands there in order to prevent the shifting back of exports to the home country at world prices.[1] Finally one important feature of the economics of dumping should be stressed before proceeding to consider preferential trading: the total quantity produced, as well as the allocation of resources in the home country, is *not* affected by the introduction of the tariff, whenever the local monopolist can export the good under Free Trade.[2] Of course, one must assume that the sector studied is sufficiently small so that the relative price of factors of production is not altered by the introduction of discriminating prices and by the subsequent distortion of relative domestic prices.

This is so because under a profit-maximizing behaviour of the firm the volume produced is uniquely determined by equalizing marginal costs to the given world price.[3] From the normative point of view, the exploitation of a dumping situation, via the introduction of a prohibitive tariff, *only* implies (1) a redistribution of income inside the country from consumers to producers, which is considered neutral, assuming that 1 dollar is 1 dollar

[1] The tariff is prohibitive. Transport costs may also help to prevent the shifting back, specially in the case of bulky commodities.

[2] There is no Customs revenue collected by the Treasury because the duty is prohibitive. Moreover, it is misleading to think of the domestic price in terms of a tariff-inclusive price, because there may be 'a lot of water' in the tariff.

[3] We shall see later that a real distortion is introduced by the tariff whenever it allows the dumper to export at world prices not covering its own costs.

for everybody; (2) the appearance of the conventional net loss zone supported by consumers, through the rising of domestic prices over and above the world price. From the international viewpoint there is no distortion whenever the minimum average total cost of the domestic supplier is less than the given world price. In this case, as economists have held for a long time, it is not rational for foreign countries to introduce anti-dumping or other countervailing duties. Only if export prices do not cover average total costs is there ground to accuse the dumper of unfair competition, as most of the national legislations and even article VI of GATT imply. As is well known, the spirit of most of the existing legislation is that there is such a thing as a 'normal' value of the product, which inevitably leads to the conclusion that any other price far below the latter is 'abnormal', thus 'unfair'. The idea is probably that what is sold at these prices does not cover costs. However, one may have serious doubts on the real importance of this case for these reasons: When analysing the Appendix, which gives us a rough idea of the real world situation, it appears that in most cases we can expect the countries concerned have a true comparative advantage in the production of the goods they actually export. They are thus efficient world producers. There is also some indirect evidence supporting our opinion in the report of the Working Party of GATT, adopted recently.[1] Developing countries stressed that their domestic prices are not a reasonable measure of the 'normal value' of the product and that these should not be used for price comparisons to prove the existence of dumping. According to their view, only export prices applied to third countries should be investigated. Furthermore one developing country said that balance-of-payments difficulties explained the need for high domestic prices. Both statements probably point to the fact that tariffs, which were introduced after the Second World War for infant-industry reasons, have succeeded in stimulating the substitution of imports, as a first stage, and the development of exports later. However, the tariff has not yet been reduced, allowing dumping in the cases where imperfect competition prevails in the domestic market. Of course, developing countries are caught between two fires when they reply to the accusation of dumping: on the one hand they wish to prove that they are competitive in the products they export. On the other hand, they wish to try to convince developed countries that their domestic prices are not the 'normal' ones, which means of course that they are higher. A neoclassical economist might sympathize with this last idea, in so far as a tariff-inclusive price has nothing to do with the 'normal' price or, for that matter, the 'natural price' concept put forward by the first Classical economists.

[1] Document L/4239, 21 November 1975, reproduced in GATT's *Basic Instruments and Special Documents*, supplement no. 22.

2. Customs Union theory and monopolistic price discrimination: explaining Customs Union formation

Joining a Customs Union or a Free-Trade Area allows the monopolist who practises dumping in a semi-industrialized country to reach the newly available markets at fixed prices that he cannot influence but which are higher than world market prices. He cannot monopolize his own domestic market any more because the rules of the Free-Trade Area or of the Customs Union imply that the country eliminates its tariffs on trade originating in the region. Thus two effects may be expected to follow simultaneously in the country: a positive consumption effect brought about by the reduction of the domestic price and a negative export-trade diversion effect brought about by the opening of access to a high-cost area. There is no import-trade diversion, because the pre-existing tariff in the semi-industrialized country was prohibitive. Note that total exports do not necessarily increase since the additional production may be absorbed by additional local consumption.

The practical implication of these observations is that they help to explain Customs Union or Free-Trade Area formation[1] *in that the conclusion of such kind of agreements may be a way to convince the local producer to drop monopolistic practices and stop asking for protection, while making consumers happier; it is also an intelligent form of selling to the big trading bloc some discriminatory tariff concessions (which will be perceived as reverse preferences) against other direct preferences.*[2]

Casual investigation by Victoria Curzon and Robert Middleton on EFTA shows that surprisingly few dumping cases were investigated during the first decade of existence of this association. In fact, this is not surprising, taking into consideration that the elimination of tariffs in the area allows for price discrimination based only on non-tariff barriers or transport costs.[3] However, one should not conclude that the situation has improved from the welfare point of view. In fact what has happened is that the *inefficient* monopolist, who would have disappeared as a result of multilateral tariff reduction negotiations, has survived by extending its area of discrimination, although sharing its privilege with the other producers of the Free-Trade Area.

[1] There is no difference between adopting one or the other formula, as long as in the latter case it is the small semi-industrialized country which adopts the big-country tariff.

[2] The theory of Customs Union formation was elaborated in the last decade by the late H. Johnson and other authors. It tries to explain better the actual behaviour of governments, and may be seen as a direct consequence of the scepticism brought about by the general theory of the second best, developed in the late 1950s; see [6].

[3] See V. Curzon [1], pp. 137–40; R. Middleton [8], pp. 86–8. Price discrimination could, however, survive in the area if we allow for the existence of shifting effects 'à la' Shibata, see [11].

3. A glance at some relevant statistics

In order to cast some light on to the presumed dumping situation, we have reproduced below Table I which shows GATT duties of six Mediterranean countries for eight selected categories of products. These countries have all concluded partial preferential arrangements with the European

TABLE I

Range of GATT rates of Customs duties

Chapters of the Brussels Nomenclature	*Spain*	*Israel*	*Morocco*	*Tunisia*	*Turkey*	*Egypt*
07.02. Frozen battered onion rings	6%					
16.04. Tinned sardines			120–50			
20. Preparations of vegetables, fruit, or other parts of plants		35–55		60	50–75	
29.16. Citric acid		10+0.15 IL/kg				
39. Artificial resins and plastic materials	20–50	20–50				
60/61/65. Knitted and crocheted goods, articles of apparel and clothing accessories of textile fabric, headgear and parts thereof	15–50 (mostly 30–50)	Mostly 25–60	35–80	20–50	70–100	50–160
64. Footwear	15–25					
87–02. Road vehicles	50–70					40–70

Source: *National Tariff Schedules; International Customs Journal*, International Customs Tariff Bureau, Brussels, 1975–6.

Economic Community in the late 1960s and early 1970s.[1] Moreover, as a second stage of the process and in the framework of what has been called the Mediterranean Policy of the EEC, some of them have already signed Free-Trade Area agreements with the Community (Israel, 1975; Morocco, 1976; Tunisia, 1976). We have indicated the extreme values of the range of *ad valorem* taxes applied to the goods covered by each of the categories of the Brussels Tariff Nomenclature. No figure was included when some duties of the corresponding category were zero, as justified on p. 127, n. 1, nor when there were specific duties or non-tariff barriers instead of *ad valorem* taxes. There was also no point in including the range of duties when the corresponding export figures included in Table II were not available. This table was set up by selecting first the Standard International Trade Classification (SITC) categories, at the 3- or 4-digit-level

[1] Turkey concluded an association agreement with the EEC in 1963, which should lead to the creation of a common Customs Union after an interim period of twenty-two years. Thus *de facto* only partial preferential trading prevails up to the present.

TABLE II

Column 1: Total exports in value (millions $) 1970
Column 2: Export market share in OECD import trade, 1970 (in %)
Column 3: Total imports in value (millions $) 1970

	Spain			*Israel*			*Morocco*			*Tunisia*			*Turkey*			*Egypt*		
	1	2	3	1	2	3	1	2	3	1	2	3	1	2	3	1	2	3
Frozen battered onion rings	183.893	12	10.505															
Tinned sardines							58.050	8	—									
Preparation of vegetables fruit, or other parts of plants				40.118	3.14	—				3.444	0.27	—	5.564	0.43	—			
Citric acid				*4.652*	*0.27*	—												
Artificial resins, plastic materials	10.729	0.37	78.784	3.045	0.10	17.764												
Knitted and crocheted goods, articles of apparel and clothing accessories of textile fabric, head-gear and parts thereof	47.051	0.99	13.258	51.275	1.08	2.241	4.085	0.10	—	1.000	0.02	1.132	4.175	0.08	—	10.163	0.21	—
Footwear	104.361	7.12	—															
Road vehicles	34.799	0.33	36.751													2.305	—	28.770

Sources: *Yearbook of International Trade Statistics 1970–1971*, United Nations, New York, 1973.
Statistical Papers, series M, no. 34, Standard International Trade Classification, Revised, United Nations, New York, 1961.

of aggregation, which correspond exactly to the Brussels Nomenclature tariff positions chosen. For each Mediterranean country three figures have been considered: total exports by value, export shares of the concerned country in total OECD import trade and total imports of these countries from the OECD area. The last figure has been included in order to give some notion of the heterogeneity of the particular SITC class.

The first two figures give a rough idea of the importance of this export trade. From the statistics analysed it appears that, notwithstanding the fact that some of the duties may be redundant,[1] there must be some price discrimination, given the importance of most of the duties. Of course, the lower the Mediterranean country import figure is, the higher the probability of existence of dumping. Thus plastic materials both in Spain and in Israel must be regarded with caution.

Road vehicles in Spain may be an industry where dumping may appear because oligopolistic market structures prevail in this sector. On the other hand, clothing in the six countries considered should be dropped from this study as apparently atomistic market conditions prevail in all these cases. An interesting case is footwear in Spain because it seems to be *a priori* an awkward example of potential dumping due to the well-known existence of thousands of small production units. However, as spelled out in the appendix to the article, Spain has been accused of practising dumping in the past in this field (women's footwear, 1970).

Middle-of-the-road cases are canned products (vegetables and fruits) in Israel, Tunisia and Turkey, where the existence of large government intervention (such as export government bodies or nation-wide co-operative organizations) allows for the existence of cartel conditions. When we look at factual cases (see Appendix), we see that in these last years, dumping investigations were opened on green olives packed in glass coming from Spain, and on apple juice concentrates originating in Greece. For instance, the import duty rate applied by this last country on the same product is 42 per cent. And the same happens for other products in which both countries play a leading role in world trade (i.e. steel reinforcing bars and ceramic floor tiles, both mentioned in the Appendix).

However, the clearest examples of dumping by Mediterranean countries, where the high domestic tariff played a crucial role, are the cases of tinned sardines of Morocco and of onion products from Spain. Here we have two products where both countries play an important role in world trade and where the product selected was homogeneous, while imports into the two countries were small, due to the presence of customs duties on both commodities in the two Mediterranean countries considered.

[1] Note that because the export figure may correspond to duty-free goods, ranges of tariffs starting at zero have been excluded from Table I.

From this rapid survey of the actual situation, we can state that price discrimination, due to the combined existence of monopoly conditions and protective import duties, is a relevant issue when examining trade relations of semi-industrialized countries with developed countries. The issue will probably come to the forefront of future negotiations between Spain, Portugal, and Greece on the one hand, and the European Economic Community on the other, for the entry of the former into the EEC. The model presented may be of some use to explain the interests of the different partners involved in these negotiations.

To illustrate the relevance of the observations presented above, plastic materials in Israel (chapter 39) in Table I have been selected as a case study. This country is supposed to eliminate its import duties on this tariff position by 1985 under the Free-Trade agreement signed in May 1975 with the EEC. The prevailing rates of the Common External Tariff of the EEC lie between 7 and 18.4 per cent.[1] Positive consumption effects to be reaped by Israeli local users are to be small due to the fact that plastic materials are mostly intermediate products, with low demand price elasticities. On the other hand, important redistribution effects may take place, considering the fact that local gross production amounted to more than 47 million dollars in 1970.[2] But for the country as a whole the net outcome of free access to the plastic materials market to the EEC may be low or even negative in view of the inefficient and artificial development of this branch of industry.

4. Some final remarks

The object of this paper was to show that a dumping situation exploited by the producers of a small country in a free-trade environment promotes mainly a redistribution of income in this country but not a distortion in the allocation of resources. When the country decides to join a trading club by signing a free-trade arrangement with it, covering the sector in which dumping takes place, the first effect tends to disappear, while a *real* distortion emerges from the new situation, brought about by export trade diversion from third countries towards the partner country implying a waste of resources since production is artificially extended.

As shown, there is some empirical evidence that semi-industrialized

[1] These tariffs already take into account Kennedy Round developments although the final reductions applied were less than the scheduled ones, due to their conditional acceptance against the elimination of the well-known American Selling Price regulation by the U.S.

[2] This figure includes also synthetic rubber as well as man-made fibres, which are mainly covered by chapters 40, 51, and 56 of the Brussels Nomenclature. See *The Growth of World Industry, 1971 edition*, vol. i, General Industrial Statistics, 1961–70, United Nations, New York, 1973. When man-made fibres are added to the general export figure for plastic materials included in Table I, the Israel total amounts to more than $20 millions.

countries around the Mediterranean are practising (maybe involuntarily) dumping in neighbouring developed countries, by letting up-dated high-level tariffs subsist in sectors where they have acquired, in the process of industrialization, comparative advantage. Their progressive economic association with the EEC is eliminating this highly visible and irritating distortion by supressing redundant tariffs, but at the same time these countries are undoing a part of the progress made since the beginning of industrialization by fostering production at a cost no longer competitive at the world level.

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APPENDIX

Investigations opened on alleged dumping practised by semi-industrialized countries; exports concerned and country's export market share in world trade

Year	*Product*	*Products' origin*	*Exports of the given year (value in millions \$)*	*Export market share in world imports* (*in* %)
1970	Files and rasps	Portugal	1.493	0.06
1970	Fertilizers	Greece	4.491	0.34
1970	Women's footwear	Spain	104.361	6.36
1970	Glass sheet	Taiwan	N.A.	N.A.
1970	Pig-iron	Brazil	23.786	2.09
1970	Gelatine explosives	Yugoslavia	2.841	1.70
1971	Steel pipes	Spain	6.948	0.74
1971	Ammonium nitrate fertilizers	Yugoslavia	1.877	0.39
1971	Eggs, chicken in the shell	Mexico	N.A.	N.A.
1971	Sulphur	Mexico	15.820	6.73
1971	Monochrome and colour television	Taiwan	N.A.	N.A.
1971	Bicycle tyres and tubes	Taiwan	N.A.	N.A.
1971	Apple-juice concentrate	Greece	24.731	2.38
1971	Carpets of coconut fibre and thread	India	25.843	2.48
1971	Wire	India	0.276	0.05
1971	Yarns of acrylic fibres	Taiwan	N.A.	N.A.
1971	Yarns of acrylic fibres	South Korea	9.023	N.A.
1971	Wood chipboard	Portugal	4.012	0.79
1972	Steel-wire rope	Taiwan	N.A.	N.A.
1972	Vinyl film printed	Brazil	1.612	0.14
1972	Iron for reinforced concrete and steel sheets	Spain	6.223	0.56
1973	Complex ternary fertilizers	Yugoslavia	N.A.	N.A.
1973	Vacuum vessels	Hong Kong	13.476	0.34
1973	Maleic anhydrine	Spain	N.A.	N.A.

Year	Product	Products' origin	*Exports of the given year (value in millions $)*	*Export market share in world imports (in %)*
1973	Steel files	India	0.022	0.005
1973	Steel files	Portugal	1.066	0.23
1973	Liquid sprayers	South Korea	N.A.	N.A.
1973	Deformed steel reinforcing bars	Mexico	N.A.	N.A.
1973	Picker sticks (for textile machines)	Mexico	0.215	0.03
1973	Vinyl film printed	Argentina	2.631	0.18
1973	Tile, ceramic glazed wall	Philippines	3.960	0.51
1973	Egg products	Israel	2.087	0.47
1973	Egg products	Yugoslavia	0.407	0.09
1973	Green olives, packed in glass	Spain	91.361	5.45
1973	Ternary compound fertilizers	Yugoslavia	N.A.	N.A.
1973	Acrylic-fibre socks	South Korea	26.439	1.45
1973	Acrylic-fibre socks	Taiwan	N.A.	N.A.
1973	Saccharin and its salts	South Korea	N.A.	N.A.
1973	Self-adhesive photo albums	South Korea	20.926	0.94
1973	Transit car seats	Brazil	20.680	0.19
1974	Polypropylene and polyethylene rope	South Korea	N.A.	N.A.
1974	Colour TV sets	Singapore	37.406	1.59
1974	Frozen battered onion rings	Spain	183.393	10.72
1974	Ramin dowels and mouldings	Singapore	4.427	0.37
1974	Ramin dowels and mouldings	Malaysia	14.742	1.25
1974	Plywood paper overlaid or printed	Singapore	59.878	4.573
1974	Plywood paper overlaid or printed	Taiwan	N.A.	N.A.
1974	Louvred doors	Taiwan	N.A.	N.A.
1974	Tinned sardines	Morocco	58.050	7.21
1975	Playing cards	Hong Kong	10.479	0.48
1975	Fibreglass fishing-rods	Taiwan	N.A.	N.A.
1975	Fibreglass fishing-rods	South Korea	N.A.	N.A.

Year	*Product*	*Products' origin*	*Exports of the given year (value in millions \$)*	*Export market share in world imports (in %)*
1975	Oil and air filters	Israel	N.A.	N.A.
1975	Hardboard	Philippines	48.629	1.75
1975	Acrylic sheet	Taiwan	N.A.	N.A.
1975	Citric acid	Israel	4.652	0.21
1975	Citric acid	Mexico	N.A.	N.A.
1975	Slide projectors	Singapore	2.358	0.11
1975	Files and rasps	India	6.296	0.19
1975	Natural rubber (latex) balloons	Mexico	N.A.	N.A.
1975	Battery post and terminal cleaning brushes	Hong Kong	59.466	1.66
1975	Wooden clothes-pins	Hong Kong	5.790	0.49
1975	Wood panels	Brazil	18.349	1.56
1975	Steel reinforcing bars	Spain	66.245	8.05
1975	Ladies raincoats	Hong Kong	104.728	6.34
1975	Portland hydraulic cement	Mexico	N.A.	N.A.
1975	Multi-metal lithographic plates	Mexico	N.A.	N.A.
1975	Monosodium glutamate	South Korea	N.A.	N.A.
1975	Ceramic floor tiles	Spain	64.351	3.92

Sources: *GATT, Committee on Anti-Dumping Practices*; *United Nations, Yearbook of International Trade Statistics*, 1972–3, 1975 (vol. II).
N.A. = not available.