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Contents

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EDITORIAL *by Vitor Gaspar and Jozef Konings*

At the G20 Summit, in London, last April, world leaders reiterated their commitment to free trade and the WTO. World trade growth has underpinned rising prosperity for half a century. But it is now falling, for the first time in 25 years, reflecting shrinking global demand and the withdrawal of trade credit. Hence, world leaders showed that they know how important it is to resist protectionism in the midst of a global slump.

The fact that trade protection hurts the economy of the country that imposes it is one of the oldest but still most startling insights economics has to offer. The idea lies at the roots of Economics itself. Adam Smith's *The Wealth of Nations,* which gave birth to economics, already contained the argument for free trade: "*It is the maxim of every prudent master of a family, never to attempt to make at home what it will cost him more to make than to buy. (…) What is prudence in the conduct of every private family can scarce be folly in that of a great kingdom. If a foreign country can supply us with a commodity cheaper than we ourselves can make it, better buy it of them with some part of the produce of our own industry, employed in a way in which we have some advantage.*[1]" The current issue of the BEPA monthly is entirely devoted to trade and trade policy. In the first article ***Kevin O' Rourke*** compares the Great Depression with the current global crisis. The paper strikingly shows the similarity in terms of magnitude of the economic downturn in terms of the collapse of industrial output and world trade, in the early stages of the recession. However, because of faster and better policy intervention it is likely that the depth and duration of the global downturn will be much shorter now than in the 1930s. The decisive aspects relate to the conduct of monetary and fiscal policy, a clear focus on long run adjustment and sustainable growth and an active pursuit of multilateral solutions, justified by strong international linkages and spill-over effects. ***Damien Neven*** and ***Georges Siotis*** also start with drawing the parallels between the global crisis and the Great Depression. Their emphasis is on the importance of avoiding fragmentation of the Single Market. They stress the importance of the EU's rule-based system. Such rules must be strong and resilient – credibly supporting the commitment to an open market economy with free competition – but also flexible in the face of unforeseen developments. There is clearly a tension between strength and flexibility, between commitment and mutability. Such conundrum must be used so that European integration emerges stronger and deeper from the process.

The same challenge is also at the heart of the application of the WTO rules as documented in the contribution of ***Willy Alfaro***. Pending the conclusion of the Doha Round, the "do no harm" principle, i.e. the commitment

by the G20 economies not to use new trade restrictions and trade-distorting subsidies is of particular importance to all countries, in particular to developing countries, whose economies are generally more trade dependent and therefore more vulnerable to the impact of new trade barriers. However, there has been a marked increase in protectionist pressures globally since September 2008, driven by demands to protect domestic jobs and businesses. The downward trend of anti-dumping investigations registered since 2001 has come to an end: the number of investigations increased by 27% in 2008 compared to 2007 and this increase looks set to continue in 2009. Likewise, safeguard actions appear also to be increasing, although less than anti-dumping actions. The contribution by ***Chad Bown*** also starts from the observation that there is a strong link between an *increase* in use of policies such as antidumping and safeguards during economic downturns associated with recessions and exchange rate shocks. He illustrates the recent surge in antidumping measures world wide and the increased use also by developing countries, like China of these type of measures.

How antidumping actions can affect economic performance of firms is documented in the contribution of ***Hylke Vandenbussche***. She shows that typically the least efficient firms receive antidumping protection. While it triggers them to restructure, they are not able to close the efficiency gap with firms that do not receive protection, which sheds a different light on the effectiveness of antidumping measures in protecting domestic firms. Furthermore, the effects of antidumping protection on domestic firms depend on firms' initial conditions in terms of productivity and on their exporting status. Not taking the interests of exporters into account when deciding to protect a particular industry is bound to have detrimental long run effects which need to be considered before deciding to impose protection.

The last three contributions tune in on the magnitude of collapsing trade that is observed in the current crisis. ***Gaspar Frontini*** and ***Nuno Sousa*** document the drastic collapse in trade and explain this by the collapse in global demand, the globalization of the supply chain and the fall in trade finance. They argue that it is key to avoid protectionistic responses and to continue further with multilateral trade liberalisation. Also ***Alyson Ma*** and ***Ari Van Assche*** tune in on the collapsing exports in China and argue that the true export content in China's GDP is smaller than believed due to the large role played by processing trade and hence traditional measures tend to overstate the dependence of China on foreign trade. At the same time, the collapse in Chinese GDP and processing trade due to the crisis is likely going to spill-over to the rest of South-East Asia, where most of processing trade is done.

Finally, ***Alina Ujupan*** reviews some evidence which suggests that the contraction in economic activity is slowing. This evidence is still insufficient to conclude that a recovery is about to emerge. Clearly, many risks remain. We cannot know for certain that policies will work. However, in contrast to the Great Depression, monetary and fiscal policy has reacted in a timely and forceful manner, and on a scale unprecedented in recent memory. Competent authorities have acted in order to avoid or mitigate the consequences of systemic failures. Last but not least multilateral cooperation, at the level of the G-20 has acted as a catalyst for the political will to resist protectionism, safeguard an open world trade system and co-ordinate the global answer to the economic crisis.

ENDNOTE

[1] *The Wealth of Nations*, Book IV, Chapter II, pagraph 11, page 357 of the Liberty Fund Edition.

1 Protectionism and the Great Depression

*By Kevin O'Rourke**

Comparisons between the Great Depression and the worldwide economic crisis which began in 2008 can no longer be regarded as fanciful. World industrial output has been falling as rapidly since April 2008 as at the onset of the crash 80 years ago (see Figure 1). What is true for the world is also true for the four major European economies (Figure 2). German and British output is falling at roughly the same rate as that experienced 80 years ago, while French and Italian output are also falling extremely rapidly. Indeed, these two countries are well 'ahead of schedule', in that they only saw their industrial output start to fall with a lag last time around. Finally, Figure 3 shows that the volume of world trade is falling far more rapidly now than it did during the Great Depression.

There should be no doubt about the matter. It is the duration of the current downturn that, so far, distinguishes it from the Great Depression, not its amplitude. What is now crucial is that policymakers act decisively to limit the downturn to a year or so, preventing the economy to continue to contract at present rates for several years. Whether they will succeed remains to be seen, and will largely depend on the political will to do what is economically necessary.

In this context it is worth considering the lessons to be learnt from the Great Depression for the inter-relationships between trade policy and the sort of economic cataclysm the world is currently undergoing. For example, it is often stated that the wave of protectionism which followed the passing of the Smoot-Hawley Act[1] in June 1930 led to the Depression of 1929 becoming Great. Modern scholarship, however, has conclusively debunked this version of history, showing instead that the roots of the Great Depression lay in flawed macroeconomic policymaking. In turn, the scale of the downturn probably made widespread protectionism inevitable. While protectionism during the 1930s may not have been as economically damaging in the short run as is sometimes thought (and may indeed have benefited some individual countries), it was immensely damaging both geopolitically, and in terms of the longer run prospects for the international economy. It is thus crucial that governments and central banks avoid the sorts of mistakes which were made during the 1930s.

At the time of the Depression, observers such as Keynes put the blame squarely on excessively tight monetary policy. The U.S. Federal Reserve raised interest rates in 1928 in an attempt to halt runaway stock markets, and this lowered investment and aggregate demand. This contractionary impulse was then spread internationally, as other countries were forced to follow suit because of their commitment to the gold standard. It is important to stress that this monetary interpretation of the Depression is not just Keynesian, since it was given a major intellectual boost by Milton Friedman and Anna Schwartz, writing about the U.S. experience in the 1960s (Friedman and Schwartz 1963). More recent scholarship (e.g. Temin 1989, Eichengreen 1992) has retained the monetary interpretation of the Great Depression, but has regarded it as an international phenomenon rather than a primarily American one, and as being due to a variety of structural factors, notably the gold standard, rather than to isolated policy mistakes.[2] In particular, not only did the gold standard spread the initial contractionary impulse; it also implied that policy makers were unable to combat the Depression effectively. They could not lower interest rates when this was required in order to combat unemployment, since this would have led to their currencies depreciating. Furthermore, expansionary fiscal policies were also regarded as dangerous. The consequences of adherence to gold could be clearly seen in 1931, when several countries raised interest rates as their currencies were attacked, thus prolonging the Depression. It was only when countries left the gold standard that they were able to adopt appropriate monetary policies, and started to recover. This happened in 1931 in Britain, and in 1933 in the United States. A small 'gold bloc' centred on France resisted until 1936, and experienced the longest Depression of all.

In these circumstances, it is hardly surprising that countries resorted to wholesale protectionism. With export markets gone in any event, because of falling demand and protectionism elsewhere, the perceived opportunity costs of protecting one's

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home market seemed much smaller than usual. Indeed, in some countries such as Ireland, protectionism led to the development of import-substituting industry which cushioned the labour-market impact of the Depression during the 1930s, albeit at a ruinous long-run price which was fully realised during the 1950s (Neary and Ó Gráda 1991, O'Rourke 1991). Clemens and Williamson (2004) find that, during the interwar period, tariffs were positively related to growth in the core economies (France, Germany, the UK and U.S.) and less developed countries, but negatively related to growth in the European periphery and the frontier societies of the New World other than the U.S. They also find that those countries which had been hit hardest by the Crash grew faster in the late 1930s if they had higher tariffs, ceteris paribus. This is contrary to the common view that tariffs were a disaster during this period.

This does not imply, of course, that the protectionism of the 1930s was a benign phenomenon: on the contrary. Protectionism is a classically beggar-thy-neighbour policy, diverting demand from one country to another. If everyone attempts to do this, on average they will not end up better off, and in the process the benefits of trade are lost. Protectionism also helped to fuel the international tensions of the period. For example, in Japan the Smoot-Hawley tariff and British imperial protectionism undermined the political position of the more liberal elements, and strengthened the hand of those who claimed that imperialism, rather than trade, was the right way to ensure adequate supplies of primary products. Across the world, the Depression and interwar protectionism helped create new import-substituting industries which relied upon protection for their survival, and which therefore lobbied to retain protection in the aftermath of the crisis. The result was that interwar deglobalization was not a temporary phenomenon, but one which triggered a disintegration of the world economy which would last much of the rest of the century (Findlay and O'Rourke 2007).

As we contemplate a 21st century which will be more multipolar than ever before and in which resource scarcity will inevitably become a major theme in international economic relations the last thing that the world needs is an outbreak of global protectionism which might end up being locked into place for decades. The lesson of the interwar period is that macroeconomic policies which do not succeed in combating unemployment effectively make protectionism much more likely (Eichengreen and Irwin 2009). If we want to avoid such a risky scenario, we need to stop our own Depression in its tracks, now.

The April 2009 World Economic Outlook of the International Monetary Fund makes it clear how demanding this task will be. The world economy is in the grips of a vicious circle involving negative feedbacks between the financial sector and the real economy. The credit crunch is disrupting the flow of credit to viable businesses, economic activity is contracting, firms are closing, and workers are being laid off. This in turn is widening the holes in the banks which need to be filled. In order to arrest this downward spiral, governments need to act far more decisively than they have done to date to solve the banking crisis, and prop up faltering aggregate demand.

Fixing the banks will require a lot more public money than has been committed to date, and this is not going to be popular. However, governments need to realise that the longer they procrastinate, the worse the problems will become. Nor can governments simply sit back and hope that exports will lift their economies out of recession – a classic route to recovery in many of the severest recessions of recent decades. The fact that this recession is global means that if we all wait for exports to miraculously recover, we could be waiting a long time. With investment and consumption both suffering, governments need to become 'spenders of last resort', as the IMF puts it, with a particular onus on those governments who still have the fiscal capacity to play this role. And, of course, central banks need to cut interest rates to zero or thereabouts, and engage in quantitative easing. The good news is that while in some countries governments have tended to be much somewhat cautious, at least policy has been moving in the right direction during this crisis, albeit too slowly. This is a major difference with the Great Depression experience (Eichengreen and O'Rourke 2009). Unfortunately, fiscal fragmentation and conservative ideology mean that the European response to the crisis is likely to lag well behind what is required. Whether this will lead to a rejection of Europe, or to a belief that what is required is a stronger and more united Europe, remains to be seen.

ENDNOTES

[1] Officially the **Tariff Act of 1930** was an act signed into law on June 17, 1930, that raised U.S. tariffs on over 20,000 imported goods to record levels. In the United States 1,028 economists signed a petition against this legislation, and after it was passed, many countries retaliated with their own increased tariffs on U.S. goods, and American exports and imports were reduced by more than half.

[2] In turn, this interpretation is largely accepted by authors such as Bernanke (2000), whose analysis is essentially complementary to that of Eichengreen and Temin, providing evidence of additional channels through which contractionary monetary policy depressed the economy.

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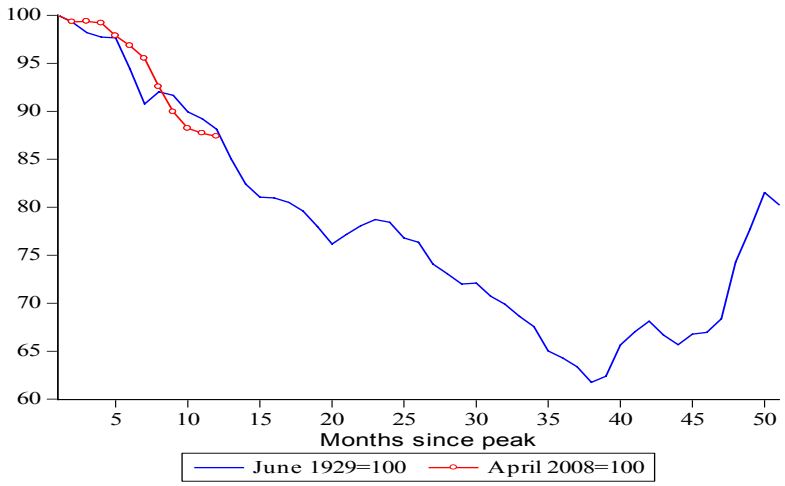
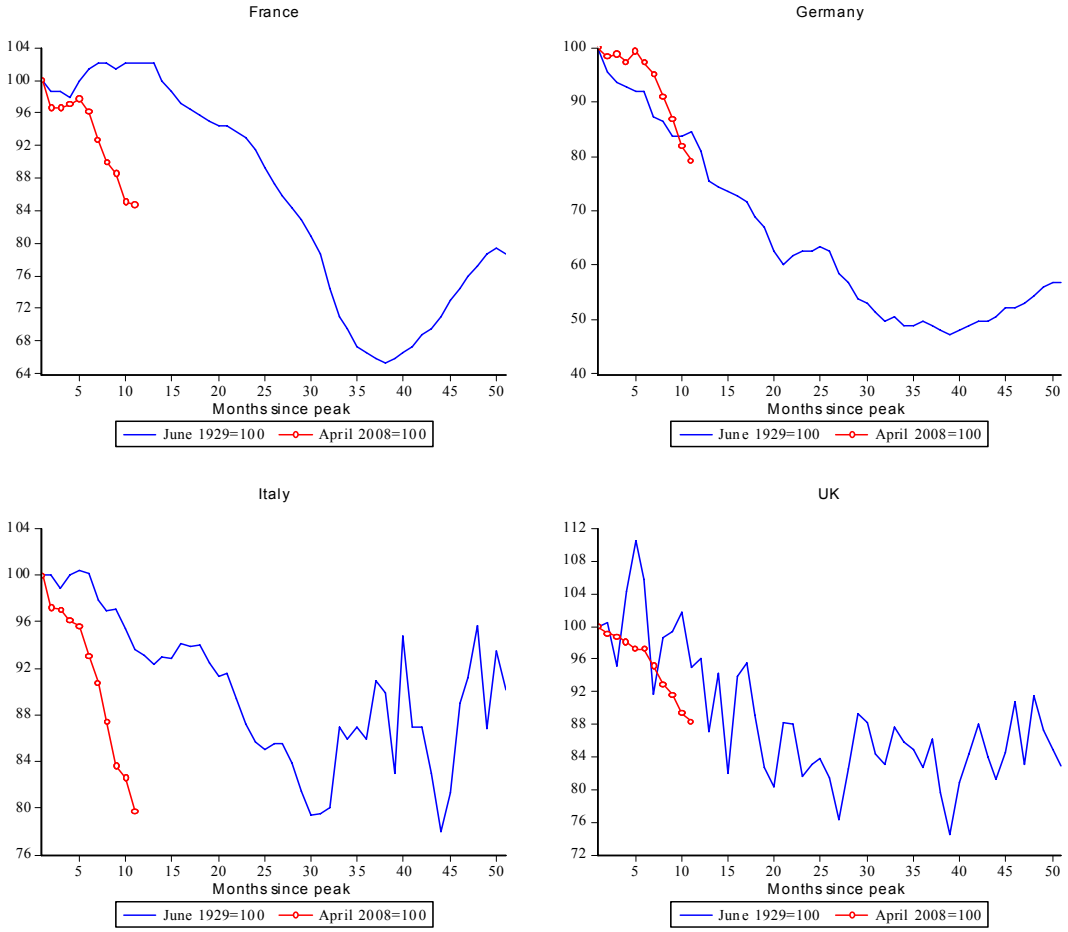
Figure 1: World Industrial Output during the Depressions of 1929 & 2008



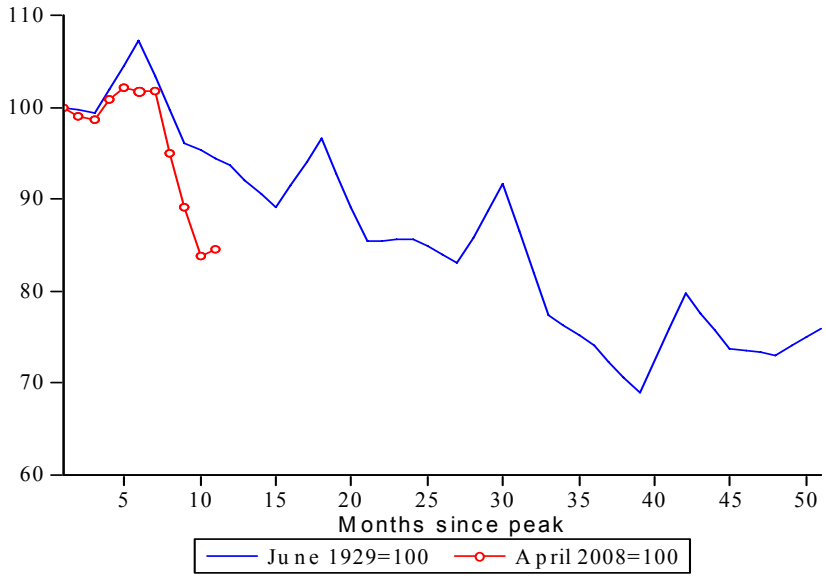
***Source*: Eichengreen and O'Rourke (2009).**

Figure 2: Industrial Output, Now vs Then (the European 'Big 4')



***Source*: Eichengreen and O'Rourke (2009).**

Figure 3: The Volume of World Trade, Now vs Then



***Source*: Eichengreen and O'Rourke (2009).**

2 The Two Faces of Flexibility

*By Damien Neven and Georges Siotis**

The parallels drawn between the current situation and the Great Depression indicate that the drop in headline economic indicators is of similar magnitude, as shown in the contribution of O'Rourke.

The bottom line is that the period ranging from mid-2008 to today looks terribly similar to the unfolding of the events during the 1929-1931 period. The drop in international trade appears as even more pronounced than what the world witnessed during the 1930's (see figures of O'Rourke).

For policy makers, the challenge is not to avoid a massive contraction (the latter has already occurred), but to avoid a "Slide to the Abyss", to use the expression coined by the great financial historian Charles P. Kindleberger (1986). In short, to avoid the policy mistakes that converted a necessary adjustment into a slump that ended, for most of the World, with the onset of WWII.

Despite this depressingly gloomy outlook, there is ground for optimism. The policy response, informed by experience and further developments in economics, has been drastically different. Economists can take comfort in the fact that the toolbox that they put at the disposal of policy makers did contain the right instruments to fight the slump (although they were, admittedly, buried under a thick blanket of ideological considerations). Both monetary and fiscal policies have reacted aggressively to sustain aggregate demand. So far, the simple, but time proven recipe consisting of supporting demand and output without interfering with competitive price setting has been upheld.

Even the collapse in world trade is not as worrying as headline figures suggest. The reduction in trade barriers and transport costs coupled with a more favourable environment towards FDI that have characterised past decades have led to unprecedented degree of specialisation. Goods sold to final consumers are often produced by combining intermediates inputs originating in numerous locations, as the distinct steps of the vertical chain have been scattered worldwide according to the pattern of comparative advantage. These massive efficiency gains, delivering affordable children clothes and toys as well as better medical equipment, have materialised thanks to the often maligned process of globalisation.

In practical terms, regional specialisation means that a 1€ reduction in final goods consumption leads to a much larger drop in observed international trade, since the same input crosses borders many times. In addition, the recent drop in the price of many primary commodities, a welcome development in most cases, leads to a ceteris paribus fall in international trade measured in value terms. Last, despite the harshness of the current adjustment, there has been no wholesale surge in protectionism. Overall, a close look at the data suggests that the link goes from collapsing final demand into reduced trade, not the other way around (Francois and Woerz (2009)).

Despite the absence of a 1930's like erection of trade barriers and vigorous macro policies, the danger of "murky protectionism" (a term christened by Evenett & Baldwin (2009) is very real, as the severity of the current slump has boldened advocates of intervention aimed at supporting ailing industries. Existing rules allow for WTO compatible measures that would result in effective protection. For instance, tariffs can be legally raised for many goods as there is "headroom" (reflecting the fact that current tariffs are below maximum WTO compatible levels). In addition, there always exists scope for improper use of anti-dumping. Many "grey area" measures, such as discriminatory public procurement, are not easily tackled in a multilateral framework functioning along inter-governmental rules, not least because of the potential for long drawn out litigation. Last, the ethereal "moral suasion" that public authorities can (and do) exercise results in favouring domestic agents with iron-clad regularity.

The EU is firmly committed to WTO multilateral rules and the Treaties explicitly prohibit any discrimination on the base of origin for intra-EU transactions. At the same time, in times of economic distress, citizens legitimately and

* DG COMP

understandably turn to the State for action. Even within the rule-based EU system where States have willingly shared sovereignty to achieve welfare enhancing goals, States remain the principal custodians of their citizens' well-being. Active public intervention may even be efficiency enhancing if markets are slow to adapt (the State acting as a bridge or cushion) and/or in the presence of a systemic market failure (financial markets freezing because trust and confidence have evaporated) compounded by informational asymmetries.

Thus, it should come as no surprise that many hopes are pinned on hard nosed public intervention to sustain domestic economic activity and employment. However, initiatives borne out of the need to act quickly may be counterproductive. Individual members will naturally fail to consider the consequences of their actions on others and they might clash with EU rules, meant to ensure a level playing field and the achievement of benefits from coordination. EU rules have been developed over time and have a proven track record. Invoking the uniqueness of the current situation is not, in itself, a convincing argument to suspend these time-hardened rules informed by economic principles.

Yet, EU rules are only useful insofar they are effectively applied. To the extent that rules are excessively restrictive and rigid, they are bound to snap under stress. At the opposite, if rule enforcement becomes too soft (or too "flexible"), the very same rules become toothless.

The EU's rule-based system has adapted to the circumstances deriving from dysfunctional financial markets and the market failures resulting thereof. For its part, EU competition policy has coped with this hitherto novel situation, both actively and, in a conscious manner, "passively".

The Commission, adopted in December 2008 a "temporary framework for State aid measures to support access to finance in the current financial and economic crisis" (the "temporary framework" or TF) in response to the growing effects of the crisis on the real economy. The adaptation of rules contained in the TF target the specificities and the expected temporary nature of credit tightening. In addition to specific initiatives related to "Green Products", the TF focuses on the provision of finance to the real economy and the new measures explicitly aim to tackle the current dysfunctional nature of credit markets. In particular, the Commission has recognised that interest rate reductions by Central Banks are not adequately reflected into medium and long term interbank rates. The Temporary Framework therefore allows Member States to grant loans whose interest rate consists of the sum of the central bank overnight rate plus a premium equal to pre-crisis spreads between interbank rates and overnight rates, plus a credit risk premium corresponding to the risk profile of the recipient with premia calibrated on those observed pre crisis (as stipulated by the Commission Communication on the revision of the method for setting the reference and discount rates). This allows States to provide loans that have been constructed on the basis of pre-crisis conditions in credit markets. On trade finance, the conditions to invoke the escape clause have been relaxed in the TF. As a result, two schemes allowing State provision for short term export credit insurance in the OECD area have been adopted.

On the "passive front", many control instruments devised in the context of the quiet financial waters associated with the Great Moderation have not been up-dated to take into account of the circumstances derived from the current turmoil and, in particular, the sharp increase in the perception of counterparty risk. This is the case for both direct finance (lending) and financial guarantees, whose associated "safe harbour" thresholds have been left untouched following Lehman Brother's demise. *De facto*, this allows Member States to financially support firms on the basis of pre-crisis conditions.

The downside of this desirable flexibility introduced in the EU's rule-based system is that Member States may fall prey to the temptation to use this leeway to engage in actions that violate the Treaties' spirit. This flexibility could be used to pursue blatantly nationalistic objectives. It is hoped that, for the sake of the European project, our leaders will have enough moral clout and vision to put these temptations at bay.

ENDNOTES

[1] Official Journal C 16, 22.1.2009, p. 1.

[2] Available at: http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=CELEX:52008XC0119(01):EN:NOT

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3 The Global Economic Crisis and Trade-related Developments

*By Willy Alfaro**

Overview

Since the beginning of the year, the economic situation has continued to worsen around the world. According to the latest IMF forecast the global economy is expected to contract by 1.3% in 2009, the first such fall in sixty years, and the outlook for recovery to start in 2010 is still very unclear. The volume of world merchandise trade is projected to contract sharply in 2009 by 9%, due to the collapse in global demand and shortages of trade finance that have created supply-side constraints to export growth in many developing countries. In such circumstances, it is important that governments avoid policies that unduly restrict international trade. So far, there is no indication of an imminent descent into high intensity protectionism, involving widespread resort to trade restriction and retaliation. The multilateral trade rules built over the past sixty years continue to provide a strong defence against that happening. The danger today is of an incremental build-up of restrictions that could slowly strangle international trade and undercut the effectiveness of policies to boost aggregate demand and restore sustained growth globally.

Many governments around the world are facing increased pressure to take protectionist actions. So far, most WTO Members appear to have largely successfully kept these pressures under control, although more recently some slippage has occurred. There have been increases in tariffs, new non-tariff measures, and more resort to anti-dumping actions. The financial and fiscal stimulus packages that have been introduced to tackle the crisis clearly favour the restoration of trade growth globally, and they are to be welcomed, but some of them contain elements – such as state aids, other subsidies, and "buy local" conditions – that favour domestic goods and services at the expense of imports.

One factor helping to contain protectionist pressures so far has been greater public scrutiny of trade policies. National policy debates highlight the need to avoid adverse trade effects and to respect WTO obligations. In some countries, proposals to introduce new trade restrictions have been amended or rejected after scrutiny highlighted their disadvantages these could present for the domestic and global economy. For instance, the recent action of the U.S. Administration in making clear that the "buy American" provisions will be administered "in a manner consistent with United States' obligations under international agreements" was important in reducing potential market restricting effects of the legislation. Some governments have gone further and introduced measures to liberalize and facilitate trade.

The incidence of new trade measures taken in response to the current crisis is not out of line, so far, with what happened during previous downturns in economic activity. However, trade policy risks are still increasing. The main risk is that governments will cede ground to protectionist pressures, even if only gradually, as long as the global economic situation continues to deteriorate. As a result, world trade could contract further, undermining confidence in an early and sustained recovery in global economic activity.

The second risk is that measures taken "temporarily" to try to protect jobs and business now from the effects of the crisis will create a legacy of uncompetitive industries and sectoral over-capacity that will continue to generate protectionist demands even after economic activity picks up again. The failure of trade restrictions and subsidies to provide effective industrial support in the 1970s and 1980s, and the long-term costs imposed on world trade, needs to be recalled.

There is an implicit contradiction in using measures that restrict trade, and therefore that tax production and incomes, while at the same time the main thrust of policies to overcome the economic crisis is geared to expanding aggregate demand. In the context of the global economic crisis, completing the Doha Round is the surest way of safeguarding the individual trade interests and the multilateral trading system against the threat of a return to protectionism. This would also represent a much needed global stimulus package.

Pending the conclusion of the Doha Round, the

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"do no harm" principle, i.e. the commitment by the G20 economies not to use new trade restrictions and trade-distorting subsidies is of particular importance to all countries, in particular to developing countries, whose economies are generally more trade dependent and therefore more vulnerable to the impact of new trade barriers. The G20 leaders clearly recognized the importance of international trade in general, and the multilateral trading system in particular, in terms of boosting aggregate demand and restoring sustained growth globally.

One of the most important steps that the WTO has taken in the context of the global crisis is to monitor new trade and trade-related measures adopted by countries. The WTO monitoring reports are issued quarterly on the basis of information provided by WTO Members and Observers and other relevant public and official sources.[1]

Trade policies

There has been a marked increase in protectionist pressures globally since September 2008, driven by demands to protect domestic jobs and businesses. Coverage by the press of the threat of protectionism has drawn attention to how these pressures are being dealt with in national trade policymaking processes.

In a number of cases, proposals for potentially protectionist legislation have been successfully resisted, or amended, before being executed. In some other cases, however, governments have moved to relax legal, institutional or policy limitations on the extent to which potentially trade-restricting or distorting measures can be taken. The economic crisis has also called attention to standing legislation in the area of trade in agriculture that automatically or semi-automatically increases support to farmers whenever agricultural prices fall.

Some governments have taken trade liberalization and facilitation measures in the past six months, involving the reduction or elimination of import tariffs and export taxes and the expansion of trade finance facilities. The purpose of these measures is no doubt various, but each one is an example of trade policies contributing positively to help reverse the contraction of global trade and to stimulate aggregate demand by reducing consumer prices and producer costs. On the other hand, the WTO Secretariat found, in its latest monitoring report, a number of new import and export restrictions, trade-related subsidies and trade remedy actions that have been taken since September. So far there has been no general trend in the direction of widespread protectionism, but a pattern is beginning to emerge of increases in import licensing, import tariffs and surcharges, and trade remedies to support industries that have faced difficulties early on in this crisis. Many of these measures have been imposed only recently, or are still in the process of being implemented, so that their trade effects are not yet entirely clear.

WTO rules act as a check on the degree to which these measures can restrict trade flows, but the current crisis is highlighting the extent to which those rules and the individual market access schedules of WTO Members provide substantial room for trade restriction and distortion to increase and will continue to do so at least until the Doha Round is completed.

Reports of various kinds of non-tariff measures affecting trade, such as standards and technical regulations, are also rising. It would appear for the time being that this is due less to an increase in the number of new measures than to changes in the way in which existing measures are being applied and administered.

There has been an increase in state aids and potentially trade-distorting subsidies in some countries to support manufacturing industries, notably the steel and automobile industries, including direct funding, special loans and guarantees. Similar measures have been used by some countries to provide support to their financial services industries. Using public finance in this way provides the governments that can afford it with an alternative to using border trade restrictions to protect their economies against foreign competition, but is not an option open to the vast majority of developing countries whose fiscal situation is being placed under even more stress than usual by the economic crisis.

These measures can prolong the operations of uncompetitive or insolvent firms. This denies market share to more efficient producers including foreign suppliers. In some cases, the provision of state aids and subsidies is subject to specific conditions that can restrict trade. In other cases, governments are taking a direct management role in firms in exchange for financial participation by the State.

It is important to recall the experience of the 1970s

and early 1980s when governments, faced with very difficult global economic conditions, resorted heavily to trade restrictions and subsidies to support ailing industries and sectors such as textiles and clothing, shipbuilding and steel. This slowed down structural adjustment and the correction of problems of global over-capacity. It led subsequently to the introduction of new and chronic forms of protectionist measures to manage trade flows, some of them beyond the reach of GATT trade rules, so as to support strategic sectors and national champions that were no longer competitive internationally but in which too much had been invested to allow them to be abandoned easily.

In industries that today are globally integrated such as automobiles, where production takes place internationally and mergers and acquisitions have diluted the meaning of many "national" brands, it has become more difficult and more costly to try to target national problems of over-capacity or inefficiency by using trade restrictions or subsidies. Some governments are choosing instead to give assistance to the automobile industry by channelling tax incentives or subsidies to consumers rather than to producers. As long as this kind of support is provided without restricting consumers' choice to buy domestic or foreign cars, these measures can result in both domestic production and imports of automobiles rising.

The downward trend in anti-dumping investigations registered since 2001 has come to an end, and an upward trend, which could accelerate rapidly, has started. The number of investigations increased by 27%in 2008 compared to 2007. However, the total of 208 new initiations in 2008 is still well short of the peak of 366 in 2001. The increase in initiations of anti-dumping investigations looks set to continue in 2009; a preliminary search through available sources gives an estimate of 53 new initiations up until 222009.

Between 1 July and 31 December 2008, the main users of anti-dumping, measured by investigations initiated, were India, Brazil, Argentina, China, Turkey, and the European Union, while the main targets of anti-dumping investigations were China, the European Union and the United States.

There is no significant trend discernible for countervailing duty actions in 2008, although there have already been five initiations of new investigations between January and 222009 (compared with six initiations for the period 1 July -31 December 2008).

An argument for not being anxious about these trends is that trade remedy instruments were designed to be used precisely when their domestic industry is suffering injury. However, the ability of the restrictions to alleviate injury is curtailed when many Members are resorting to similar measures. Whatever relief is obtained from temporarily halting imports in one domestic industry can be offset by the pain of restricted foreign demand for goods produced in others. Since trade remedies deliberately aim to restrict trade, the threat of retaliation is likely to be significant.

Safeguard actions appear also to be increasing, although less than anti-dumping actions. The total number of safeguard actions initiated in 2008 was 11, up from eight in 2007, but lower than 13 in 2006 and far less than the peak of 34 initiations in 2002. There have been 13 initiations already in 2009 (until 22), indicating a likelihood of increased use of safeguard measures. Historical data shows that an increase in safeguard actions usually occurs only about a year after a major shock affects an industry or economy. Safeguard action may therefore increase in the latter half of 2009.

Fiscal stimulus and financial support programmes

Most G20 countries and some other governments have announced substantial fiscal stimulus programmes with the aim of boosting domestic demand.[2] Fiscal stimulus and financial support programmes are evidently to be welcomed in current circumstances from a trade perspective. Both are aimed at reversing the fall in global aggregate demand and restoring credit markets to good health.

Although the key objectives of these programmes remain paramount – to prevent systemic failure of global financial markets and to counter global recession by boosting aggregate demand – their potential trade effects should be considered. For the sake of the effectiveness of the programmes themselves, openness to trade can play an important role in providing value-for-money and, as long as GDP remains significantly below its potential and resources are unemployed on a large scale, the inefficiency in resource allocation created by restricting trade is all the more counter-

productive. Trade restrictions act as a tax on incomes and production and therefore run counter to the main objective of these programmes which is to boost real aggregate demand. Given their size, many of the programmes have the potential to impact seriously and negatively on foreign producers who specialize in activities that are the target of government support in other countries. The details of many of these programmes are still unclear. Some elements of those that have been announced have already raised concerns about their potential trade-restricting or distorting effects. Whatever those effects may be, the willingness of the governments concerned to provide detailed information on the implementation of the programmes in a transparent way to their trading partners is to be welcomed. Doubts will continue to exist about the trade-damaging nature of other programmes where little is known publicly about their scope or how they are to be implemented.

International trade can be harnessed by these fiscal stimulus programmes to deliver a bigger boost to aggregate demand globally than will be the case if steps are taken to restrict the effects of the stimulus inside national borders. Governments nonetheless often face strong pressure to introduce a domestic-bias into the design of their programmes and prevent the stimulus funded by domestic taxes from "leaking out" as spending on foreign goods and services. This concern can be lessened to the extent that different national programmes are coordinated in terms of size and timing. Leakage into higher imports will then be compensated for, at least partially, by increased exports generated by the stimulus programmes of other countries.[3]

Some of the stimulus programmes announced to date include conditions on how funding is to be spent that aim to reduce the leakage into imports and concentrate the stimulus effects on domestic firms and job creation.[4] Restricting imports by attaching conditions to stimulus programmes taxes producers and income and reduces the net impact of each programme on domestic and global aggregate demand.

Trade Finance

The drying up of global liquidity combined with a general re-assessment of risks by commercial banks led in the second half of 2008 to a rise in the cost of trade finance instruments such as letters of credit, and in some cases, to serious gaps between demand and supply. Survey-based data point to a market gap in developing countries – i.e unmet demand for trade financing – of between U.S.$100 billion and U.S.$300 billion on an annual and roll-over basis.[5] In some countries foreign exchange has also become scarce. The situation, which was not expected to improve much in the first quarter of 2009, has in fact continued to deteriorate, mainly for North-South and South-South trade.

In cooperation with other multilateral and regional organizations, the WTO has been helping to mobilize various actors to shoulder some of the risk from the private sector and to encourage co-financing between the providers of trade finance. A two-track approach is being followed to: (i) find collective short-term solutions, notably by mobilizing government-backed export credit agencies and international financial institutions operating mostly on commercial terms; and (ii) develop measures allowing for better interaction between private and public sector players in the short and medium-term, all of which aim at removing the obstacles to risk co-sharing and co-financing by various institutions.

Conclusion

The WTO's monitoring of trade measures is a useful mechanism for increasing transparency and providing Members and Observer Governments with an opportunity to exert collective peer-pressure to resist protectionist tendencies. This has been widely recognized by the G20 leaders at the London Summit last April and other Governments. It is at times of great difficulties, when protectionist temptations flourish, that the value of the multilateral trading system is all the more apparent. Governments are looking to the WTO system of global trade rules for predictability, transparency and as a provider of confidence for economic operators. While some may already start seeing the bottom of the economic crisis, we have not yet seen its full social impact which will inevitably trigger political pressures on the trade front. It is therefore important that the monitoring mechanism remains on alert. The successful conclusion of the Doha Round will provide the best insurance policy against the resurgence of protectionism and isolationism. This will greatly contribute to the expansion of aggregate demand and thus help economic recovery.

ENDNOTES

[1] The inclusion of any measure in the monitoring reports implies no judgement by the WTO Secretariat on whether or not such measure is protectionist in nature. Moreover, the reports do not make any judgement on the consistency of listed measures with WTO rules.

[2] The IMF has recommended a global fiscal stimulus target of 2% of aggregate GDP each year for 2009-2010, but it appears that target has not yet been met by the G20 countries for 2009 and under current conditions there will be a withdrawal of discretionary fiscal stimulus in 2010.

[3] This reasoning underpins the European Economic Recovery Programme adopted at the end of 2008.

[4] One condition of this kind is "Buy National" requirements. These raise concerns for trade and the trading system because they threaten to cut foreign suppliers off from markets that they could otherwise hope to compete in, either by reserving the market completely for domestic suppliers or by introducing new administrative complexities that make procurement practices less transparent and accessible for foreign suppliers. They can also provoke retaliation by other countries.

[5] Based on estimates of experts met at the WTO, March 2009.

4 The Global Resort to Antidumping, Safeguards and Other Trade Defense Instruments Amidst the Financial Crisis

*By Chad Bown**

WTO member countries use import-restricting "trade defense" policy instruments during both good and bad macroeconomic times. Nevertheless, economic evidence from historical data finds a strong link between an *increase* in use of policies such as antidumping and safeguards during economic downturns associated with recessions and exchange rate shocks (Knetter and Prusa, 2003). During the current financial crisis, there is concern for a substantial increase in the use of trade defense instruments beyond what normally occurs in the ongoing process of globalization to mitigate the adjustment process. With the global spread of the financial crisis, newly available data tracking the global use of these trade defense instruments does indicate a marked increase in WTO members' combined resort to these instruments beginning in 2008 that continues into the first quarter 2009. The resort to these instruments is widespread across a number of countries, including almost all of the WTO membership included in the Group of Twenty (G-20). However, since the onset of the crisis the use of these instruments has been most pronounced in the area of "South-South" trade – i.e., developing country importers initiating and imposing new protectionist measures primarily affecting developing country exporters – with the vast majority of the product-level actions targeting exports from China. The increased resort to import-restricting trade defense instrument is of concern given the substantial economic research literature documenting the multitude of their adverse economic affects including welfare losses to consuming industries, anti-competitive effects, and an increased possibility of retaliation and spiraling 1930s style protectionism.[1]

The effort to track, assess, and examine the impact of the spread of protectionism is complicated by both the adoption of use of "traditional" trade defense instruments of antidumping (AD) and global safeguards (SG) to new countries, and that many other countries are also adopting and implementing use of other "new" instruments such as countervailing duties (CVD) under "anti-subsidy" laws and China-specific transitional safeguards (CSG). The least well known of these four instruments because of its newness is the CSG, to which WTO members negotiated access beginning in 2001 as part of China's agreement to accede to the WTO agreement and which is in place until 2014. Furthermore, some of these trade defense instruments apply to specific foreign countries while others are to be applied on a more nondiscriminatory most-favored-nation (MFN) basis across foreign sources.[2] In the presence of multiple trade defense instruments which can be "substitutes" to each other for providing the same access to import protection, one way to normalize the data to assess the frequency of their *combined* use over time is to examine *non-redundant* requests for new protection undertaken within an economy at the *product* level.[3]

As figure 1 indicates, WTO members initiated 36 new product-level investigations requesting imposition of new import restrictions under national trade defense laws in 1Q 2009.[4] This is an increase of 18.2 per cent compared to the same period in 2008 and also continues an upward trend. The total number of new import-restricting investigations launched in 2008 was 29.9 per cent higher than the number of new investigations initiated during 2007. It is worth pointing out, however, that the year 2007 was the low point for new trade defense initiations since the 1995 establishment of the WTO.

Based on the historical data on the use of these trade policies and especially in the case of the antidumping which is the dominant trade defense instrument in use around the world, the vast majority of new investigations and requests for import protection are highly likely to ultimately result in the imposition of new "definitive" import restrictions in the form of tariffs, price undertakings, or quantitative restrictions. While the rates of imposed final measures in developed economies like the U.S. and EC may have been in recent years in the range of 50-60 per cent of

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initiations, the rate is much higher in many developing countries including some of the countries that are the major new sources of the current rise in initiated investigations (e.g., India, Turkey), where it is not uncommon to find 80-95 per cent of the initiations resulting in the imposition of new measures.

Figure 2 tracks the imposition of new measures at the product level across the same sample of WTO members illustrated in figure 1. The imposition of definitive measures typically occurs with a 12 month lag from the period of initiation, which explains why the 2Q 2008 low point of newly imposed definitive measures lags 1 year from the 2Q 2007 low point for the newly initiated investigations.

An important implication of the 2008-2009 increase in new investigations (figure 1) is the high likelihood that they will result in a 2009-2010 surge in newly imposed definitive import restricting measures. WTO members did impose 21 new *product-level* definitive import restrictions in 1Q 2009 under national trade defense laws, an increase of 10.0 per cent compared to 1Q 2008, and the annualized rate translates to the frequency of new import restrictions in 2009 to be 18.8 per cent higher than the rate at which definitive new measures were imposed in 2008. However, this annualized figure will certainly under-predict the *actual* increase in imposed measures in 2Q through 4Q of 2009. The increase in the rate of imposed measures is expected to be much *larger* than 18.8 per cent higher than the number imposed in 2008, given the sharp increase in newly initiated investigations in 2Q through 4Q of 2008 (see again figure 1).

Table 1 documents the relative frequency of the users of these trade policy instruments in 1Q 2007 through 1Q 2009. Most striking is that since the onset of the crisis – or roughly between 1Q 2008 and 1Q 2009, developing countries initiated 73 per cent of all new investigations. This use has been dominated by India (20 per cent), Argentina (13 per cent), Turkey (9 per cent), China, Brazil, and Colombia (5 per cent each). Developed economies initiated only 23 per cent of the new investigations during this time, although most of those derive from initiations by the United States (9 per cent) and the European Union (7 per cent).

Table 2 illustrates the product-level requests by sector for new import restrictions under these trade defense instruments between 1Q 2007 and 1Q 2009. For the developed economy users, the industries most frequently resorting to these instruments are chemicals, iron and steel, and machinery, with 65 per cent of the developed economy initiations since 1Q 2008 occurring in just one of these three sectors. As these are the historically dominant sectoral users of trade defense instruments, the predominance of their use during the crisis is not in itself surprising. However, it does raise the possibility of abuse for anti-competitive concerns (Messerlin 1992; Veugelers and Vandenbussche, 1999), especially given the recent wave of M&A activity in the steel sector and the desire to segment markets. Developing country firms have also initiated a number of new requests for import protection under trade defense instruments since 1Q 2008 in the steel, chemicals, and machinery sectors (45 per cent of total developing country initiations). The other two sectors with a high number of new investigations in developing countries are textiles and apparel and plastics and rubber, which combine for another 27 per cent of the total developing economy activity under these instruments during the crisis.

Table 3 illustrates the frequency with which exporters in various countries have been *targeted* by country-specific trade defense instruments such as AD, CVD and CSG. Given the economies that are using these trade policies and the sectors that are being targeted for new import restrictions thus far, it is not surprising that the exporters targeted by these actions are primarily located in other developing countries. The frequency with which developing countries as a whole have been targeted in country-specific trade defense investigations is roughly ¾ both in 2007 and during the more recent period of global crisis between 2008 and 1Q2009.

Nevertheless, the use of country-specific trade defense instruments such as AD, CVD and CSG documented in table 3 illustrates the overall is intensively targeting exports from China, which have faced roughly 40 per cent of all investigations during this period and more than 40 per cent of the definitive measures being imposed. However, the WTO membership's use of trade defense instruments to target China's exports is not new as it simply continues a trend dating back to China's

WTO accession in 2001 and even earlier (Bown, forthcoming b). Explanations for the increasing intensity of use of these instruments against China's exports since 2001 include: China's export increase during this period; China receipt of MFN treatment in WTO members' tariff schedules since 2001 which constrains to trade defense instruments WTO members' abilities to impose potentially WTO-consistent import protection against China; China continues to be treated as a "non-market economy" (NME) in many countries' antidumping procedures which gives AD authorities more discretion than is available vis-à-vis other exporters to calculate dumping margins; and many WTO members do not feel as though China's state-owned enterprises (SOEs) and the government's use of other explicit and implicit subsidies have been sufficiently curtailed since its 2001 accession.[5] Whether the global crisis *increases* the intensity of use of these instruments against China relative to other exporters is, however, an issue of concern that will require continued monitoring and in depth analysis as more data becomes available.

ENDNOTES

[1] For surveys see Blonigen and Prusa (2003) for antidumping, and Bown and Crowley (2005) for safeguards. See also Vandensbussche and Zanardi (2008) and Messerlin and Reed (1995).

[2] In principle these trade defense instruments do require different forms of evidence before they can be applied. AD requires evidence of less-than fair value pricing (dumping) and injury to the domestic industry from the dumped imports; CVD requires evidence of foreign subsidization and injury, SG requires evidence of injury caused by increasing imports, and CSG requires evidence of injury caused by increasing imports from China. Nevertheless, economic research such as Bown (2004) and Bown and McCulloch (2003) has shown that these instruments can be applied in ways that have similar effects on trade flows.

[3] By an initiation or measure being defined at the product level, for example, we mean that Argentina's two 1Q 2009 antidumping investigation of "Electric food processors" from Brazil and from China are treated as one product-level investigation. Furthermore, to ensure product-level initiations are not redundant across policy instruments, a WTO member's simultaneous AD and CVD investigations (measures) over the same product are treated as one investigation (measure). For example, the US's 1Q 2009 simultaneous AD and CVD investigations of "Polyethylene retail carrier bags" from Vietnam are treated as one product-level investigation.

[4] Most of this activity is antidumping, however, the use of other instruments has been increasing recently. As described in the *Global Antidumping Database*, these figures are based on original source, nationally provided data for AD and CVD. The data reported in the text and figures is based on that collected for 20 AD- (18 CVD-) using countries, and while this does not comprehensively cover the global use of the instrument, historically these countries represented 90 per cent of AD (93 per cent of CVD) initiations by all WTO members during 1995-2007. The data collected on countries' use of SG and CSG is comprehensive and obtained from the WTO in addition to national government sources.

[5] Consider India's activity in 1Q 2009 for example: it initiated 3 antidumping investigations, 3 China-specific safeguard investigations, 2 global safeguard investigations, and its first ever countervailing duty investigation, also one in which it targeted China.

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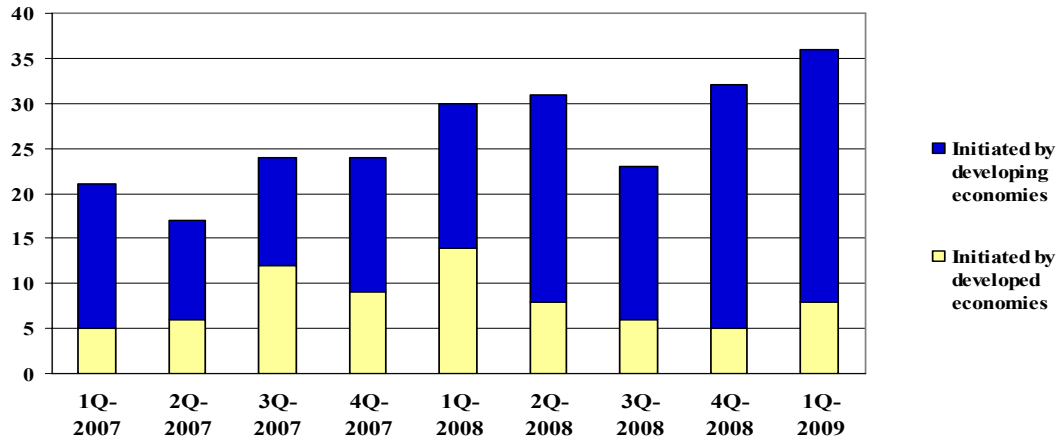
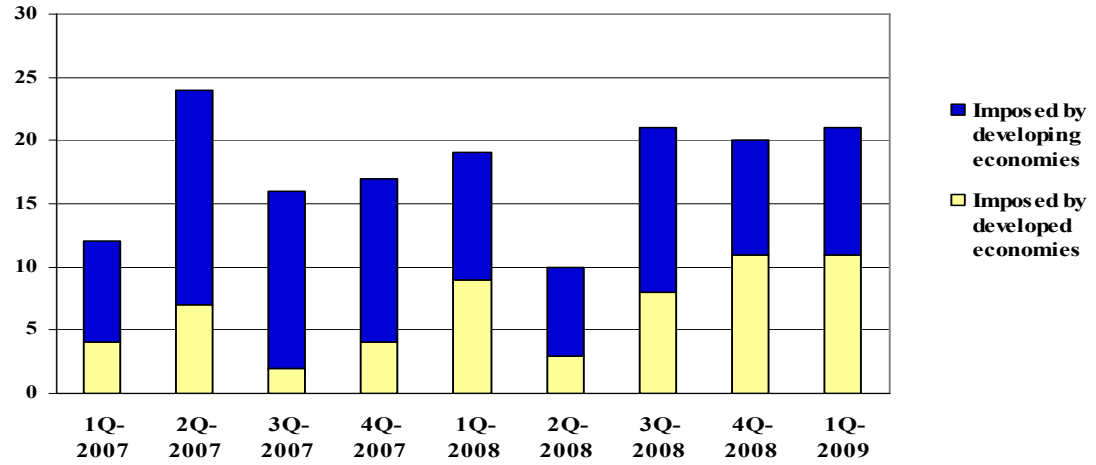
Figure 1: Newly Initiated Import-Restricting Trade Defense Investigations, 1Q 2007 - 1Q 2009



Source: Compiled by the author from the Global Antidumping Database. These are non-redundant AD, CVD, SG, CSG at the product level. See definition in footnote 4.

Figure 2: Newly Imposed Import-Restrictions under Trade Defense Instruments, 1Q 2007 - 1Q 2009



Source: Compiled by the author from the Global Antidumping Database. These are non-redundant AD, CVD, SG, CSG at the product level. See definition in footnote 4.

Table 1: Country Use of Trade Defense Instruments at the Product Level, 1Q 2007 - 1Q 2009

Countries	Initiations 2007 Total	Initiations 2008 Total	Initiations 1Q 2009 Total	Measures 2007 Total	Measures 2008 Total	Measures 1Q 2009 Total
USA	14	12	2	3	12	4
European Union	6	10	1	8	9	1
Canada	1	3	1	1	3	1
Australia	3	4	1	2	0	3
New Zealand	2	0	0	1	1	0
South Korea	6	3	0	0	6	2
Taiwan	0	0	0	1	0	0
Israel	0	1	3	1	0	0
Argentina	6	11	8	6	4	2
Brazil	10	8	0	11	5	1
India	14	21	9	11	11	4
Turkey	6	12	1	4	10	2
China	1	6	2	6	1	0
South Africa	5	2	1	2	2	0
Pakistan	0	3	1	2	0	0
Colombia	1	6	1	7	0	1
Mexico	3	1	1	0	0	0
Peru	2	0	1	1	0	0
Venezuela	0	0	0	0	0	0
Ukraine	5	4	2	0	5	0
Others	1	9	1	2	1	0
Developed countries total	32	33	8	17	31	11
Developing countries total	54	83	28	52	39	10
Total	86	116	36	69	70	21

***Source**: Compiled by the author from the Global Antidumping Database. These are non-redundant AD, CVD, SG, CSG at the product level. See definition in footnote 4.*

Table 2: Developed and Developing Economy Trade Defense Initiations by Sector, 1Q 2007 - 1Q 2009

Sectors	Developed Economies 2007 Total	Developed Economies 2008 Total	Developed Economies 1Q 2009 Total	Developing Economies 2007 Total	Developing Economies 2008 Total	Developing Economies 1Q 2009 Total
Agriculture	2	1	0	0	1	2
Chemicals	10	8	0	17	18	8
Iron and steel	8	11	1	5	12	2
Machinery	1	5	1	8	7	3
Materials	1	0	2	4	9	1
Misc. manufactures	0	1	1	3	4	0
Other metals	0	3	0	2	5	3
Plastics and rubber	4	0	1	5	10	1
Textiles	1	1	0	7	13	6
Vehicles	0	1	0	1	2	1
Wood	5	2	2	2	2	1
Total	32	33	8	54	83	28

***Source**: Compiled by the author from the Global Antidumping Database. These are non-redundant AD, CVD, SG, and CSG at the product level. See definition in footnote 4.*

Table 3: Exporters Targeted by Global Use of Trade Defense Instruments, 1Q 2007 - 1Q 2009

	Initiations			Measures		
Exporting (affected) country	2007 Total	2008 Total	1Q 2009 Total	2007 Total	2008 Total	1Q 2009 Total
Total	162	211	49	104	119	36
Developing country exporters (percent of total)	110 (0.68)	155 (0.73)	33 (0.67)	71 (0.68)	81 (0.68)	29 (0.81)
Developed country exporters	52	56	16	33	38	7
China (percent of total)	65 (0.40)	84 (0.40)	19 (0.39)	46 (0.44)	49 (0.41)	16 (0.44)
South Korea	12	9	2	5	7	2
European Union	9	14	6	4	8	1
Thailand	8	11	2	5	1	3
USA	8	10	2	4	6	1
Taiwan	7	8	1	7	7	2
Malaysia	5	10	0	4	2	3
Indonesia	6	10	3	3	4	2
India	5	9	0	4	3	2
Japan	4	3	0	5	2	0
Russia	6	2	0	0	5	0
UAE	3	0	0	0	1	1
Brazil	2	3	4	2	2	0
Turkey	3	3	0	0	3	0
Others	19	35	10	15	19	3

***Source**: Compiled by the author from the Global Antidumping Database. These are exporting country-specific use of trade defense instruments (i.e., AD, CVD, and CSG) used by the same policy-imposing countries described in footnote 4. However, to be able to focus on the issue of export targets, this table does not normalize trade defense instruments under the "product-specific" and "non-redundant" definitions but simply reports the counts of AD, CVD and CSG use.*

5 Antidumping protection: Good for Bad Firms but Bad for Good Firms

*By Hylke Vandenbussche**

Introduction

While for the past twenty years the world has seen a drastic fall in tariff barriers, trade protection is still around – albeit in a different form. As shown in Figure 1, the fall in tariffs has coincided with a spectacular increase in the number of antidumping measures, which have become the most frequently used instrument of trade protection.[1] The downward trend in the number of antidumping measures that started in 2003 has been reverted since the beginning of the global financial and economic crisis. Despite the political commitment made not to increase protectionism at the G20 Summit in November 2008 and more recently in April 2009, antidumping measures and investigations have increased rapidly in 2008 and this seems to continue in 2009.[2] This paper draws mainly on work of Konings and Vandenbussche (2008, 2009) to discuss how antidumping protection has an impact on European companies and shows how such protection can be detrimental for the more efficient firms, due to the global nature of the more efficient firms and their global supply chain.

Antidumping measures, which mainly impose import duties, are allowed under the WTO agreement when there is unfair trade. In the context of the EU antidumping legislation, if a company exports a product to the EU at a price lower than the price it normally charges on its own home market, it is said to be "dumping" the product. If in addition, the price charged in the EU is also lower than the one charged by EU companies selling the same product, EU firms are said to be "injured" and an investigation can be opened, the latter usually initiated by a number of companies or associations. However, current antidumping rules are not well equipped to distinguish between "fair" and "unfair" trade. When foreign producers produce goods more cheaply, their prices are bound to be lower, especially when they export to a large market like the U.S. or the EU where they are likely to face more competition than in their own domestic markets. What appears to be unfair trade may well be an indication of foreign comparative advantage. This would then imply that it is the less efficient firms that have an interest in filing for and receiving protection so to get sheltered from international competitive pressure.

Antidumping protects inefficient domestic firms

Table 1 shows the average efficiency level, measured by total factor productivity[3], of European firms that apply and receive antidumping protection and compares it with a comparable control group of European firms that never apply for antidumping protection. The numbers refer to a sample of about 4000 European firms that are followed between 1993 and 2003. These refer to companies that were involved in European antidumping cases for the years 1996, 1997 and 1998 as well as a control group of companies with similar characteristics in terms of size, capital stock and sales, but were never involved in antidumping cases. It further compares two similar time frames, one referring to the period before protection and one referring to the period during which firms that applied and received Antidumping protection is in place (usually 5 years). It is clear that firms that never apply and hence never receive antidumping protection have on average the highest efficiency score, measured by total factor productivity. In contrast, firms receiving antidumping protection tend to have lower efficiency before protection (1.32 versus 2.23). So, this confirms the notion that it is the least efficient firms that typically are involved in antidumping cases and suggests that use of antidumping measures may have little to do with "unfair" practices by foreign firms.

Furthermore, Table 1 indicates that both protected firms and unprotected ones experience a productivity increase during the antidumping protection period, but it seems that on average the increase in efficiency is higher for protected firms (17% versus 4%). This may suggest some positive effect of antidumping protection, however, it is clear from the second column that this productivity increase is never sufficient to close the

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productivity gap with unprotected firms (1.55 versus 2.32). While on the one hand this result points to the fact that lowly efficient firms seem to start restructuring in order to be able to cope better with international competition once protection comes off, on the other hand these restructuring efforts may not be sufficient after all given that the productivity gap cannot be closed. In the absence of protection, some firms that received antidumping protection likely would have exited. The resources freed by their exit would be reallocated towards more efficient sectors in the economy, resulting in a larger productivity increase.

Antidumping: good for bad firms, but bad for good firms!

While the average firm's efficiency seems to be different between the group of protected and unprotected firms, also within the group of protected firms there may exist important differences *between* firm responses. A specific feature of antidumping protection is that it applies to *all* European firms producing the product that is being investigated, even though that some firms producing it have not filed for protection. Furthermore, not all firms that receive protection have the same level of initial productivity, where it is measured as the distance relative to the best performing firm in the sector (i.e. the one with the highest productivity), illustrated in Figure 2. The initial productivity distribution of protected firms is skewed to the left meaning that the majority of protected firms have a relatively low productivity level prior to the protection. But at the same time the productivity distribution of protected firms has also a thin right hand tail which implies that a small number of the protected firms have a high initial productivity. This begs the question whether antidumping protection affects all protected firms in a similar way or whether firms respond heterogeneously to trade protection?

Accounting for these initial conditions in a regression analysis framework reveals that there is substantial firm heterogeneity in firms' responses to antidumping protection. While antidumping protection appears to raise the productivity of the lowly efficient firms it reduces the productivity of the highly efficient ones. This result suggests that antidumping protection is "Good for Bad Firms but Bad for Good firms!"

Several explanations can account for this. A first explanation is that the threat of exit is higher with the least efficient firms and therefore once they receive temporary protection they have a higher incentive to restructure before being exposed to international competition. But this does not explain why the most efficient firms lose out when they face protection. A more likely explanation is related to the global nature of the firm, i.e. the extent to which firms are active in international trade. A stylized fact is that typically the most efficient firms are the ones that are also able to be active in international markets, due to the sunk costs (transaction costs) involved with international trade. In particular, antidumping protection may adversely affect those exporters that outsource part of their production to the countries targeted by the antidumping protection. Outsourcing entails a fixed cost which only more efficient firms can cover. Since exporters tend to be more efficient than non-exporters, exporters may engage more in outsourcing than non-exporters. Imagine a French exporting firm that outsources bicycle assembly to China for the purpose of importing these bicycles into France, while performing activities such as branding, labeling and other types of distribution activities in France. French exporters that outsource their bicycle production face more expensive imports since they have to incur the antidumping duty imposed on bicycle imports from China. Current antidumping law does not automatically exempt outsourcers from paying an import duty, not even when the majority of the value added is created domestically. This puts outsourcers at a serious disadvantage over domestic bicycle producers which do not have to pay the import duty and hence this may negatively affect the domestic demand and exports of these global firms. In addition, this may undermine the competitiveness of firms exporting domestic varieties that are refrained from setting a lower price in extra-EU export markets in order not to be accused of dumping practices by others. Furthermore, exporters may experience reduced market access abroad if domestic trade protection results in retaliatory action whereby trade partners protect themselves in turn.[4]

Table 2, based on a recent paper by Konings and Vandenbussche (2009), shows that exports of products that receive antidumping protection tend

indeed to decline during protection, compared to a control group of products that do not receive protection. Also recent case evidence[5] in the EU suggests that the international orientation of firms or the lack thereof is what divides firms within the same domestic import-competing industry over the desirability of antidumping policy. A recent EU antidumping case on leather shoe imports from China, divided the European shoe producers over the desirability of protection. "Globalized" EU shoe producers argued that they were harmed by the antidumping protection since they outsourced the assembly of their shoes to China which made them subject to an antidumping duty upon imports of the shoes in Europe despite the fact that well over 50% of the value added of the shoes was created inside the EU through activities such as research, design, logistics, development and marketing making the shoe a European shoe and not a Chinese one.

Conclusion

This note pointed out that typically the least efficient firms receive antidumping protection and that it helps them to restructure. However, they are not able to close the efficiency gap with firms that do not receive protection, which sheds a different light on the effectiveness of antidumping measures in protecting domestic firms. Furthermore, the effects of antidumping protection on domestic firms depend on firms' initial conditions in terms of productivity and on their exporting status. Not taking the interests of exporters into account when deciding to protect a particular industry is bound to have detrimental long run effects which need to be considered before deciding to impose protection.

ENDNOTES

[1] e.g. Blonigen, Bruce and Prusa, Thomas J., "Antidumping," *Handbook of International Economics*, edited by E. Kwan Choi and James Harrigan, (Malden, MA, Blackwell Publishing), 2003, pp. 251-284.

[2] See the contribution by Chad Bown and by Willy Alfaro in this issue

[3] This table is taken from Konings and Vandenbussche (2009). We measure efficiency by total factor productivity and report an index of total factor productivity. This is a sophisticated way to measure productivity that relates a firm's input factors to its output.

[4] E.g. Prusa (2001). Retaliation is also singled out as a motive for AD law *adoption* by Vandenbussche and Zanardi (2008).

[5] Swedish National Board of Trade (2007).

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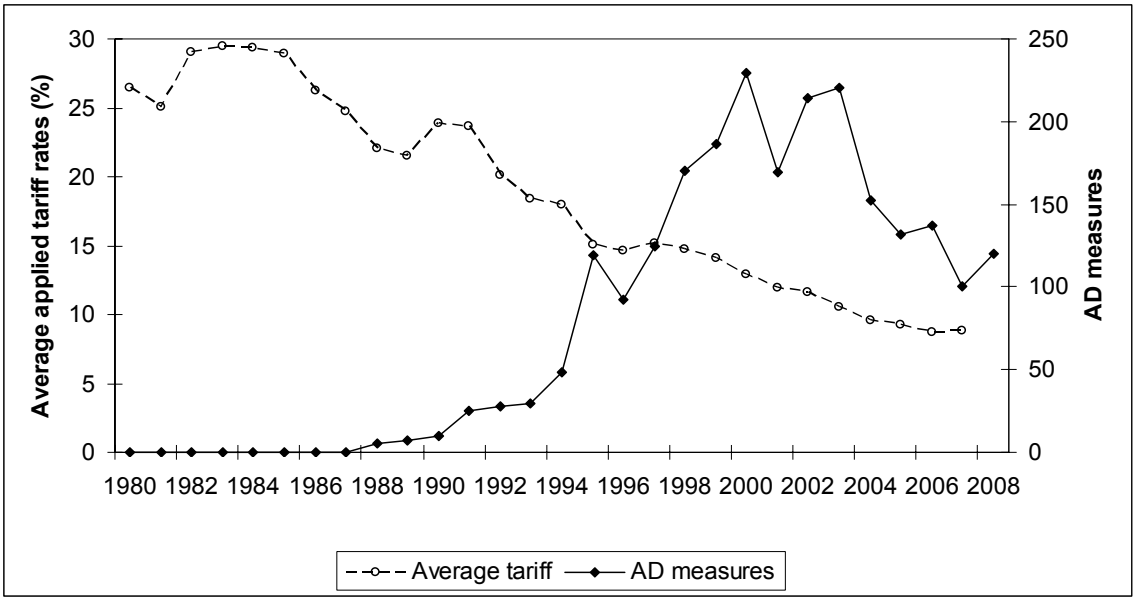
Vandenbussche, H., Zanardi, M., 2008. What Explains The Proliferation of Antidumping Laws?, Economic Policy, January, pp.93-138.

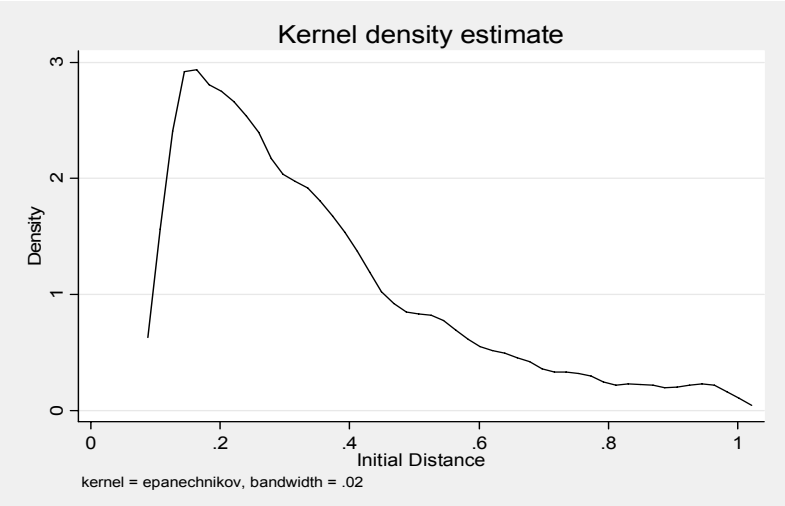
Prusa, T., 2001. On the Spread and Impact of Antidumping. Canadian Journal of Economics 34(3), 591--611

Figure 1: Evolution of Tariffs and Antidumping Measures



Source: The tariff data for 1980-2007 from UNCTAD TRAINS (WITS, 2009) which runs to 2007. The AD data are from WTO data, and the Bown database

Figure 2: Frequency of Good firms and Bad firms



Source: Konings and Vandenbussche (2008), Journal of International Economics

Table 1: Comparing Average Total Factor Productivity Across Firms

	Productivity *Before* Antidumping Protection	Productivity *After* Antidumping protection	Percentage change in average productivity
Unprotected firms	2.23 (2.55)	2.32 (2.63)	4%
Protected firms	1.32 (1.05)	1.55 (8.65)	17%

***Source**: Konings and Vandenbussche, 2008, Journal of international Economics; standard deviations in brackets.*

Table 2: Evolution of Extra EU Exports during AD protection

	Extra-EU Exports			
	Volume		Prices	
AD-EFFECT	-0.369*** (0.1215)	-	0.003 (0.052)	-
AD-EFFECT x year1		-0.506*** (0.235)		0.021 (0.099)
AD-EFFECT x year 2		-0.344* (0.215)		-0.137* (0.092)
AD-EFFECT x year 3		-0.298* (0.220)		-0.034 (0.094)
AD-EFFECT x year 4		-0.243 (0.211)		0.0006 (0.092)
AD-EFFECT x year 5		-0.177 (0.211)		-0.064 (0.081)
Year Dummies	Yes	Yes	Yes	Yes
Fixed Effects	Yes	Yes	Yes	Yes
# observations	724	724	724	724

***Source**: Konings and Vandenbussche (2009); ***/* denotes statistically significant at the 5%/10% level.*

6 Global downturn, trade and trade policy

*By Gaspar Frontini and Nuno Sousa**

Over the last months the world has plunged into the most severe recession since World War II as the effects of the crisis in the developed countries' financial sector rippled through the real economy. The initial hopes that the recent dynamism of emerging economies would cushion the downturn in the advanced world have proven to be too optimistic and the outlook for the global economy quickly deteriorated in only a matter of months. In the meantime, we have witnessed an even more pronounced decline in world trade. Since October, we have been through the greatest slump in trade values and volumes of the last decades (Fig. 1 and 2).

Why was the trade decline so dramatic?

In hindsight, the scale of the collapse of global trade can be explained by the sharp demand shock that followed the worsening of financial conditions worldwide, the pronounced downward correction of commodity and energy prices (that depressed further trade values) and the current level of global economic integration. In particular, the emergence of complex international production sharing networks over the past decades contributed to exacerbate the decline in trade of recent months. In a world of internationally fragmented production and where an important part of global trade (around 55% of trade in goods) involves the exchange of intermediary inputs, a fall in demand for a final good in one country stops a series of trade transactions down the supply chain magnifying the trade impact of the global economic slump.[1] Furthermore, the disruption of credit markets also led to a shortfall of trade finance that underpins the vast majority of trade transactions. The World Bank estimates the reduction of the supply of trade finance to be between $100 and $300 billion, which is thought to have been responsible for around 10% of the contraction in trade observed since the beginning of the crisis.[2]

What can trade policy do?

Whilst the scale of the slump in global trade is worrying, it should be seen primarily as a reflection of the high degree of economic integration that has been achieved over the last decades (combined with a sudden and pronounced economic downturn). However, this is true as long as the contraction in economic activity does not lead to the (re)introduction of barriers to trade and investment.

Global crises, notably the great depression of the 1930s, have been fertile ground for the emergence of protectionist policies. The scale of the current crisis and its social costs (namely in terms of employment and income losses), and the speed and extent of the contagion across the world provide enough reasons for concerns about a possible resurgence of protectionism. The anti-globalisation rhetoric can be expected to strengthen further if citizens increasingly associate openness with an additional layer of uncertainty that makes economies vulnerable and more difficult to manage. The destabilisation of emerging and developing economies, which are highly dependent on foreign markets and financing, may also contribute to erode support for open trade. Furthermore, "beggar thy neighbour" protectionist measures may also resurge, based on claims that they are necessary to minimise leakages from fiscal stimulus programmes (by discouraging imports) and that exports should be promoted to offset the impact of the slumping domestic demand.

However, a 1930s-style global race towards protectionism has been averted so far for several reasons. First, the existence of a WTO-led multilateral system of trade rules legally restrains to an important extent the use of blunt protectionist measures. Second, the global economy has changed fundamentally over the past decades and there is a clear and generalised awareness that there is more to loose than to gain from a retreat from trade. The emergence of international production chains, by making the economic costs of protectionism more immediately apparent, has contributed to increase the resistance to the raising of new trade barriers. Third, the political pro-trade response led by the G20 has been coordinated, unwavering and timely.

The objective for trade policy was clear from the start: keeping markets open and trade and

* DG TRADE and CDT

investment flowing. However, there was also an awareness that a passive stance would not be sufficient and that policymakers needed to send clear signals of their commitment to free trade. In the two summits since the beginning of the crisis, the G20 nations proved able to show the necessary leadership in this respect.

Firstly, the G20 pledged to continue to put all efforts to conclude the DDA signalling a firm commitment to further multilateral trade liberalisation, which would provide an important boost to the world economy. Estimates vary, but the most recent and most comprehensive study (which is based on the package on the negotiation table in December 2008) finds world GDP gains of $167bn on an annual basis, if the fully fledged DDA deal were implemented.[3] Overall, Doha has the potential to deliver more than the Uruguay Round, especially if an ambitious outcome on trade facilitation and services liberalization is achieved. Moreover, there is also a clear appreciation of the fact that the value of the DDA as an insurance policy against protectionism has increased with this crisis. In addition, to the gains from further market access, a DDA deal would also crucially reduce the policy space for protectionism that exists under the current trade rules (by consolidating bound and applied tariffs). A recent study makes this point very clear by showing that an increase of all applied tariffs to current bound levels would reduce global welfare by as much as $350 bn. If (in a more realistic scenario) all countries were to raise their tariffs to the highest level they have applied since 1995, the loss in terms of global output would be $134 bn. Global trade flows would fall by 7.7% and 3.2% under each scenario.[4]

In addition, at the Washington summit in November 2008, the G20 also agreed to prevent an immediate protectionism resurgence by committing to a self-imposed standstill in terms of *new barriers to investment or to trade in goods and services, new export restrictions or WTO inconsistent measures to stimulate exports.* At the London summit, the G20 reinforced this commitment in several ways: it extended the standstill pledge until the end of 2010 and added four important new elements, notably: i) a pledge for the quick rectification of any new trade restrictive measures, ii) an explicit reference to the need to minimise any negative impact on trade and investment of domestic initiatives taken in the framework of the fiscal stimulus packages and financial rescue plans, iii) a commitment to notify promptly any new measures to the WTO and iv) an explicit mandate to the WTO to monitor and to report publicly on the evolution of the situation on a quarterly basis.

Finally, the G20 also provided a decisive push to tackle the trade finance crunch that is affecting businesses in the developed and developing world by agreeing at the London Summit to make $250 billion available over the next two years to support the financing of international transactions of goods.

How serious is the situation so far?

Despite the rapid G20-led response the danger of a protectionist backlash is not yet behind us. Firstly, it will crucially depend on a number of factors about which nothing can yet be said for sure most notably the length and depth of the recession and the overall magnitude of the contraction of global trade. Secondly, while it is true that so far none of the large trading nations has yet resorted to across the board measures to hamper trade and investment, there has been a gradual build up of diverse trade restrictions. Direct border barriers (including tariffs, tighter licensing requirements, and outright import bans) have been limited to some countries (Russia, Ukraine, Argentina to name a few of the largest). But, a number of less obvious restrictions to trade can be identified across several countries. The fiscal stimulus packages, which are the back bone of the macroeconomic response to the crisis in most countries, have opened the door to a wide range of more subtle forms of protectionism including targeted subsidies and other discriminatory initiatives such as public procurement provisions that favour local production (the "buy American" clause adopted by the U.S. is a good example of such initiatives). There have also been reports of increasing use of standards and technical regulations - including sanitary and phytosanitary (SPS) measures - in ways that can be trade distortive.

Such measures are particularly difficult to restrain because they fall through the existing loopholes of the WTO legal framework. And, it is unlikely that there will be in the near future the political momentum for going further in terms of more stringent international rules on issues such as government procurement and subsidies.

Therefore, the G20 self-restraint commitment on new protectionist measures is likely to continue to be the main mechanism available to catalyse peer pressure and avert an escalation of such initiatives. However, the G20 protectionism standstill is based on a political (not legal) commitment. For it to be effective, it will require mutual vigilance and the close monitoring of all measures with trade impact. The WTO has been given the task to carry out such monitoring but this will not be feasible without all parties being fully cooperative and transparent. It is fundamental that all countries factor in their G20 trade commitments in their policymaking decisions (in fields as diverse as competition, environmental, consumer, and employment polices) at the earliest possible stage. As far as the EU is concerned, adopting a leading role based on a full commitment to the G20 protectionism standstill is the best possible option. Not least, because within the existing WTO trade rules, the EU has less policy space for manoeuvre, notably in comparison to many developing and emerging economies that could raise tariffs without breaching their WTO commitments.

Conclusion

For many years we have been used to seeing trade and FDI growing faster than income. The declines in trade flows we are now witnessing are (for the moment at least) no more than a symmetric trade response to a sharp and synchronised fall in income (triggered by a global shock originated in the financial sector). This trade response is amplified due to the globalisation of the supply chain and the collapse in trade credit. Therefore, the situation should not be seen as roll back of globalisation but rather as evidence of how much integration has been achieved over the past decades. Trade was not at the origin of the crisis, and therefore the contribution of trade policy to its solution has limits. Nonetheless, trade policy has an important role to play not least because of the real risk of a protectionist escalation as the crisis lingers and unemployment rises. In this context, keeping trade flowing and open markets and avoiding trap of protectionism must be remain central policy objectives. Moreover, if further multilateral trade liberalisation is achieved it would provide a much needed contribution to the counter-cyclical macroeconomic response to overcome the present downturn.

ENDNOTES

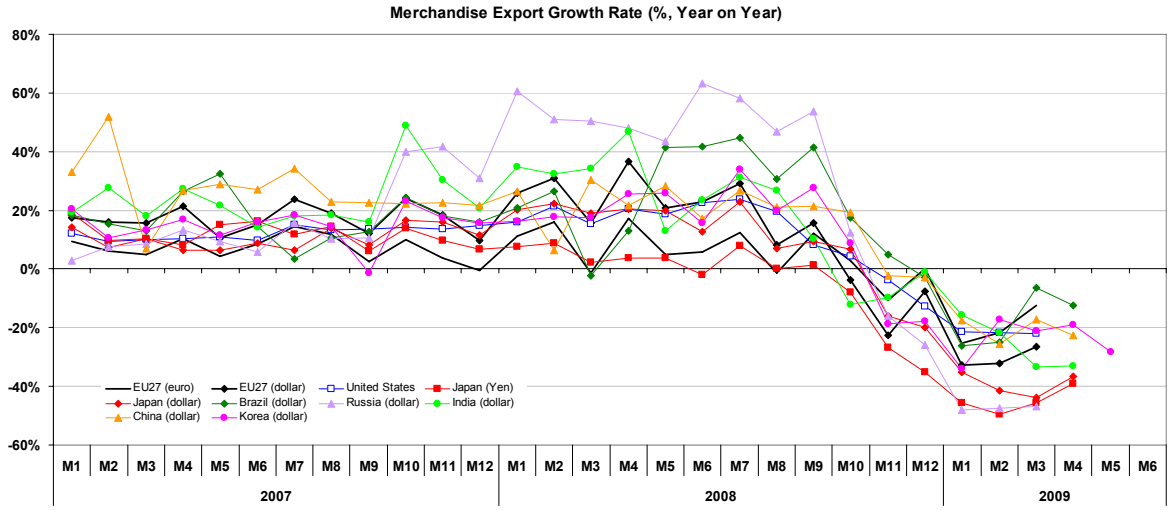
[1] Internal researched based on a CGE simulation to quantify this mechanism showed that a reduction in 0.5 percentage points in GDP growth is associated with a reduction in the growth rate of EU exports (imports) that can vary between 6-10 percentage points.

[2] See note by the Secretariat of the WTO working group on Trade, Debt and Finance (WT/WGTDF/W/44) of 23 March 2009.

[3] "Economic impact of potential outcome of the DDA", Lionel Fontagné and Yvan Decreux , CEPII working paper N° 2009-01, May 2009.

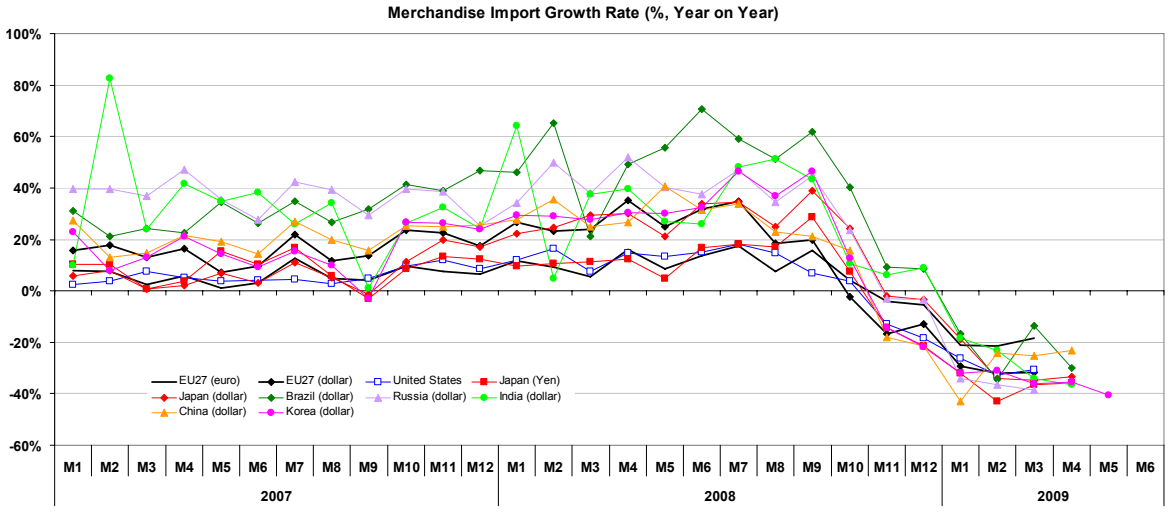
[4] "The potential cost of a failed Doha Round", Antoine Bouet and David Laborde, International Food Policy Research Institute Issue Brief no.56, December 2008.

Figure 1



Sources: Eursotat, National sources

Figure 2



Sources: Eursotat, National sources

7 When China Sneezes, Asia Catches a Cold: the Effects of China's Export Decline in the Realm of the Global Economic Crisis

*By Alyson C. Ma and Ari Van Assche**

Introduction

The recent global economic crisis has hit China's exports hard. With advanced economies' markets in turmoil and consumer confidence at an all-time low, the demand for China's exports has in the past year experienced a massive contraction. In the first quarter of 2009, China's exports were down 20.1% compared to a year earlier, from US$304 billion to US$243 billion. The reason why this is considered a worrisome trend for the Chinese economy is that exports represented 42% of China's gross domestic product (GDP) in 2007, which is a much higher figure than that observed in other large economies such as the European Union, the United States and Japan (where exports represent 12%, 12% and 18%, respectively, of GDP).[1] Some observers thus fear that, because China is so export-dependent, the Chinese economy may be exceptionally vulnerable to changes in external demand, especially in this time of worldwide crisis. This has led to the call for China (among other Asian countries) to rebalance its growth away from exports and toward domestic demand in order to return to pre-crisis growth rates, including calls for a stronger Chinese Yuan.

This recent decline in Chinese exports thus leads to two main questions that will be addressed in this contribution. First, how closely is the Chinese economy tied to the business cycle of advanced economies and therefore vulnerable to the current economic crisis? Second, how does the decline in China's exports affect its East Asian neighbors?

Processing Trade and China's Export Dependence

We start with addressing the first question by discussing China's export-to-GDP ratio. In particular, the export-to-GDP ratio can be a very misleading indicator of China's dependence on exports as GDP is measured in value-added terms, while exports depict the gross value of the goods that leave China's borders (Anderson, 2007). To see how this may create biased estimates when evaluating China's export dependence, consider the example of the iPod, which Apple assembles in China and exports to the rest of the world. In 2006, the export value for a 30GB video model was about US$150. However, Linden et al. (2007) estimate that only US$4 was produced in China, with the large brunt of value added being created in and imported from the United States, Japan, and Korea. If China's iPod export value is converted to value-added terms by removing its import content, only 2.6% of the iPod's gross export value remains.

This difference between gross export value and the domestic content share of exports (which is in value-added terms) is highly relevant for understanding China's export dependence since a large portion of China's exports (not only the iPod) heavily relies on imported inputs. Due to China's aggressive export promotion policies since the mid-eighties, China has effectively created a dualistic trading system.[2] Under its ordinary trade regime, exports rely mainly on local inputs and imports are primarily for domestic consumption. Koopman et al. (2008) estimate that in 2006 the domestic content share of ordinary exports was 88.7%. Conversely, under the processing trade regime, firms import their inputs duty free for processing and re-export. The same authors estimate that in 2006 the domestic content share of processing exports was much lower at 18.1%.

Over the years, the importance of processing trade has grown in China's overall trade as many firms offshored their labor-intensive assembly plants to China. As it is shown in Figure 1, between 1988 and 2006 the share of processing exports in China's total exports has risen from 30% to 53%, while the share of processing imports in total imports has increased from 27% to 38%. Overall, this implies that the aggregate domestic content share in China's exports is much lower than for most other countries, amounting to only 50.8% in 2006 (Koopman et al., 2008). In other words, approximately half of China's total export value is the value of the imported inputs that are embodied in the products that are exported.

Once we take into account the low domestic

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content share of its exports, China's export dependence is more limited than the export-to-GDP ratio would suggest. Indeed, if only the domestic content share of its exports is considered, China's export-to-GDP ratio drops to 21%, which is just slightly higher than Japan's 18%.[3] China is thus less vulnerable to shocks in external demand than is generally thought. In fact, Anderson (2007) and He and Zhang (2008) argue that the discussion about whether China is decoupling from the global cycle is rather mute. The Chinese economy is, and always has been, effectively decoupled from business cycles in advanced economies in terms of GDP.

While it is still too early to determine if China's economic growth will be resilient against the sharp contraction in export demand, there are some recent indications that China may indeed be able to escape the crisis relatively unscathed (Economist, 2009). In the first quarter of 2009, China's GDP growth accelerated to an annualized rate of over 6%, up from around 1% in the previous quarter. Furthermore, big banks such as Morgan Stanley, Royal Bank of Scotland and Barklays all have recently revised up their forecasts for China's GDP growth this year from 5-6% to 7-8%. These higher forecasts are partially fueled by China's large fiscal stimulus package, but also reflect China's remarkable buoyancy to the global economic downturn.

Processing Trade and Business Cycle Pass-Through

While processing trade makes China more decoupled from external demand shocks, it may make the other East Asian countries' exposure to the downturn considerably larger than often thought. This is the second issue we address in this note. Since more than 80% of China's processing export value corresponds to import content, China transfers a large portion of its external demand shocks to the countries from which it intensively imports its processing inputs.

China imports its processing inputs more intensively from its East Asian neighbors than from the rest of the world.[4] As it can be seen in the first column of Table 1, with the exception of Vietnam and Indonesia, more than 44% of China's imports from major East Asian economies were processing imports in 2006. This share is significantly higher than for countries outside of East Asia. For example, only 28.4% and 18.4% of China's imports from the United States and the EU-19[5] where processing imports. As a result, we should expect that the recent decline in China's exports should go hand-in-hand with a particularly severe drop in China's imports from East Asian economies.

From the most recent trade data, we indeed find preliminary evidence that the recent economic downturn is hitting most severely China's imports from East Asia.[6] Compared to the previous year, China's imports from its major East Asian trading partners (except for Vietnam) all have declined between 25% and 61% in the first quarter of 2009 (see Table 2). In contrast, China's imports from the United States and the EU-19 have dropped only 19.5% and 15.6% respectively. Furthermore, as it is shown in Figure 2, the percentage drop in China's imports is largest for the East Asian countries where China most intensively sources its processing inputs.

Conclusion

A particular characteristic of China's trading regime is the large role played by processing trade. This feature is important to keep in mind since it provides a more nuanced picture of China's role in the world economy than is often portrayed by the media. China's dramatic exports rise is largely driven by the fact that many foreign firms have offshored *a slice of their value chain* – labor-intensive final assembly – to China for export purposes. Many of these assembly plants heavily rely on imported inputs from East Asian economies, while they create relatively limited value added in China.

In this research note, we have used this insight to dispel the widely held misconception that China's economy is excessively export-dependent and therefore particularly vulnerable to a drop in export demand in the realm of the current economic crisis. The argument that China should rebalance its growth away from exports to domestic demand in order to return to pre-crisis growth rates therefore seems largely overblown. The growth of China's economy is already mostly domestic demand-led.

At the same time, this note helps to dismiss the notion that soaring trade between China and its East Asian neighbors protects East Asia against a downturn in Western economies. Because of China's heavy reliance on East Asian inputs for its exports, it effectively passes on negative export

demand shocks to the East Asian economies by reducing its demand for their processing imports. Indeed, by using recent trade data, we provide preliminary evidence of this business cycle pass-through during the current economic crisis. Compared to the previous year, China's imports have in the first quarter of 2009 declined most for the East Asian countries where it most intensively sources its processing inputs.

ENDNOTES

[1] The EU export figure does not include internal trade between individual member states.

[2] See Van Assche (2009) for a more detailed explanation of China's dualistic trading regime.

[3] We assume that the domestic content share of China's exports is the same in 2007 as in 2006.

[4] See Zhang (2008) for a similar argument.

[5] The EU-19 countries are: Austria, Belgium, Czech Republic, Denmark, Finland, France, Germany, Greece, Hungary, Ireland, Italy, Luxemburg, Poland, Portugal, Slovakia, Spain, Sweden, The Netherlands, United Kingdom.

[6] The most recent data by trading regime (ordinary versus processing trade) are not available.

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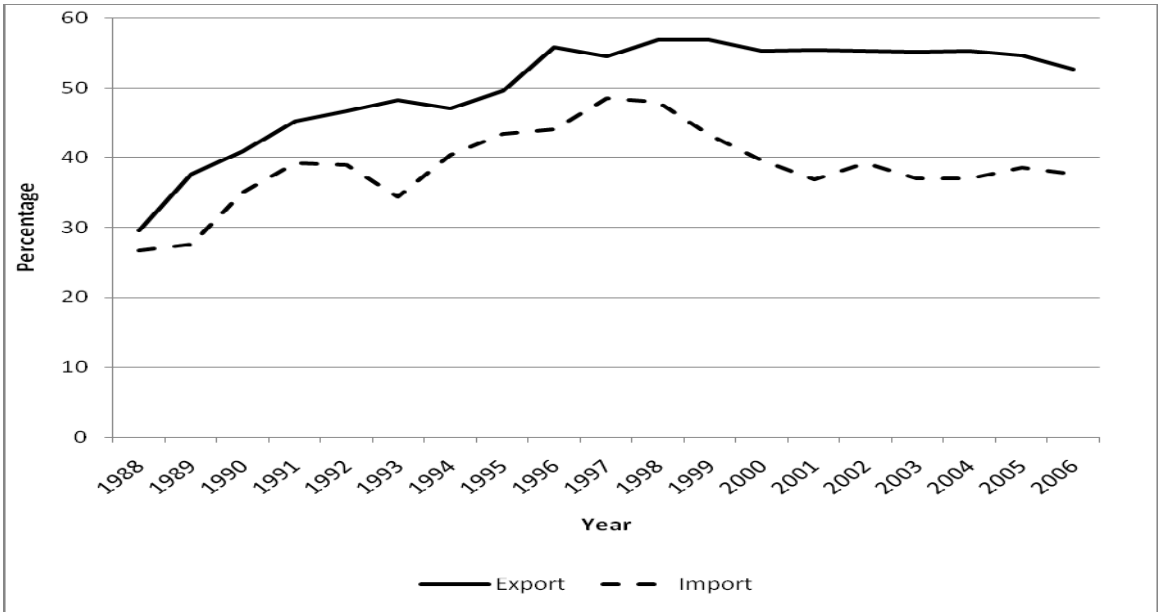
Figure 1: Proportion of total trade represented by processing trade, 1988-2006



Source: Authors' calculations using China's Customs Statistics.

Table 1: Share of exports and imports that are used in processing trade, by country of destination/origin, China 2006

Country	Processing imports as share of China's total imports (%)	Processing exports as share of China's total exports (%)
East Asia	53.6	60.7
Hong Kong	63.0	73.4
Japan	44.2	57.7
South Korea	54.0	45.3
Singapore	47.9	65.2
Taiwan	70.3	54.0
Malaysia	47.9	55.7
Thailand	50.6	41.9
Philippines	58.1	41.1
Vietnam	15.3	24.2
Indonesia	32.9	25.5
West	22.3	59.07
United States	28.4	63.3
EU-19	18.4	54.3
All Countries	37.6	52.7

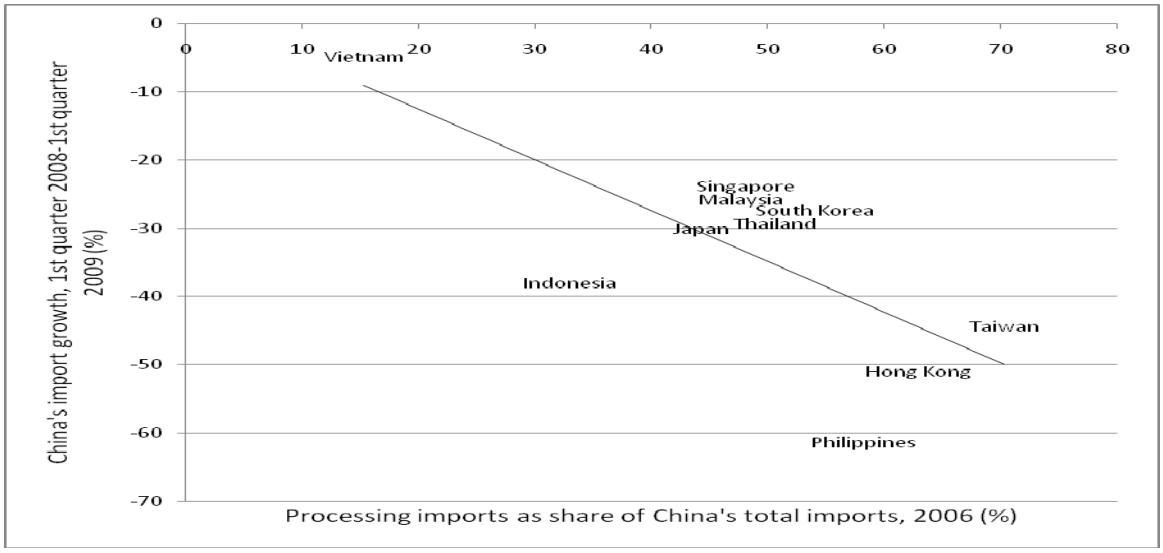
Source: Authors' calculations using China's Customs Statistics.

Table 2: China's trade in the first quarter of 2008 and the first quarter of 2009, by region and selected countries

	Exports (US$Mill.)		Imports (US$Mill.)		Growth rate	
	1st quarter 2008	1st quarter 2009	1st quarter 2008	1st quarter 2009	Exports	Imports
East Asia	114,000	87,100	118,000	77,500	-23.9	-34.2
Hong Kong	42,400	31,600	3,220	1,580	-25.6	-50.9
Japan	26,000	21,600	34,200	23,900	-16.9	-30.0
South Korea	16,100	11,300	26,400	19,200	-29.4	-27.4
Singapore	6,940	5,770	4,370	3,280	-16.9	-25.0
Taiwan	5,700	3,720	25,800	14,400	-34.6	-44.4
Malaysia	4,730	3,610	7,360	5,500	-23.7	-25.3
Thailand	3,500	2,580	6,220	4,400	-26.1	-29.3
Philippines	1,910	1,700	5,710	2,210	-10.7	-61.3
Vietnam	3,180	2,190	787	750	-31.1	-4.8
Indonesia	3,450	2,600	3,630	2,250	-24.7	-38.0
West	114,000	92,400	49,000	40,600	-19.13	-17.15
United States	53,300	45,400	19,800	16,000	-15.0	-19.5
EU-19	62,000	48,100	29,200	24,600	-22.5	-15.6
TOTAL	304,000	243,000	261,000	304,000	-20.1	-31.0

***Source**: Authors' calculations using China's Customs Statistics.*

Figure 2: Processing Import Share and First Quarter Import Growth



***Source**: Authors' calculations using China's Customs Statistics.*

8 Facts and figures that matter

By Alina-Stefania Ujupan

Is the decline in economic growth bottoming out? Some recent evidence

While the fall in world economic activity is expected to continue in the course of 2009[1] (Figure 1), recent (mostly qualitative) indicators suggest that decline is slowing. The evidence is suggestive but decidedly inconclusive. The OECD composite leading indicators for April 2009 point to a slowing of the pace of deterioration in most of the OECD economies with stronger signals of a possible trough in Canada, France, Italy and the United Kingdom. Moreover, the latest estimate from the €-COIN coincident indicator for the euro area shown in Figure 2, which summarizes information from a large set of data suggests that GDP growth has already reached its trough in the first quarter of 2009 even if economic growth continues to be very weak.

The collapse in GDP growth is a major determinant of movements in the flow of exports and imports of goods and services internationally. In February 2009, the euro area current account was in deficit equivalent to 1.2% of GDP, reflecting primarily developments in the trade balance (Figure 3). However, coincident with the mitigation in the decline in GDP growth are early signs that the fall in trade is also slowing down.[2] Since trade flows are endogenous, dependent primarily on movements in relative GDP, a stabilization in international trade is indicative that the decline in GDP is bottoming out. Indeed, the evidence suggests that while still negative, export and import growth has stabilized in the first quarter of 2009. But caution remains important as recently released provisional data from the German Federal Statistical Office indicate that German exports were 4.8% lower in April than in March.

Survey data suggest that most confidence indicators appear to have troughed in March and have begun to recover in April 2009. Economic sentiment reached 67.2 points from a 64.7 low in March. Industrial and service confidence reached -35.0 and -24.3 points, respectively, from -37.8 and -25.4 in March (Figure 4). Consumer confidence rose by 2.4 points, reaching -31.3 points in April 2009. Employment expectations varied in the manufacturing and services sector and still remain low (Figure 5). Nevertheless, most confidence indicators point to persistently weak conditions remaining far below the prior crisis levels and it is uncertain whether the small improvements already recorded will be sustained in coming months.

An additional indication that can signal improving world output growth is the recent recovery in the price of oil. It has often been suggested that there is a strong relationship between the evolution of the price of oil and current and prospective economic growth. The demand for oil is a "derived" demand dependent upon output growth, while the supply of oil markets is virtually fixed in the short run. Therefore, shocks that raise the demand for oil have an immediate impact on its price. It is reported that at the May 28 OPEC meeting Ministers decided to maintain the current levels of oil supply on the grounds that signs of an emerging economic recovery could push oil prices upwards. Oil prices have been up rising since April 2009, from a historic low in February 2009 of $44/ barrel (Figure 6). According to a recent study by McKinsey[3], despite current uncertainties, there is potential for a new spike in the oil price between 2010 and 2013.

As noted in the beginning of this short note, the evidence is suggestive but not conclusive regarding the outlook for economic growth. The signs as yet are too few to be able to determine in a more confident manner whether the trough has been reached or passed. It is possible that output growth could remain flat at some very low level over coming quarters, or, less likely, that it might resume its decline. It is also possible that a W-shaped pattern emerges. It is, therefore, necessary to observe carefully recent developments taking into consideration the risks inherent in making judgements on the basis of insufficient data.

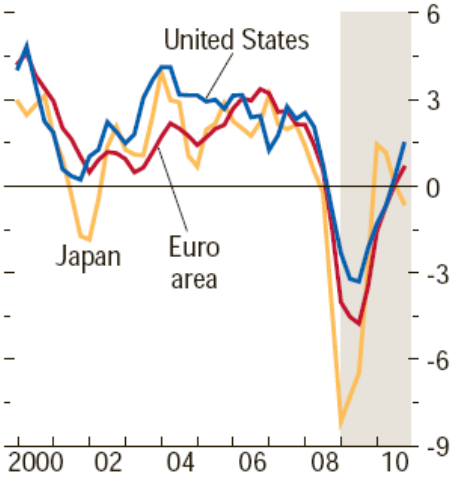
ENDNOTES

[1] IMF, World Economic Outlook, April 2009 (http://www.imf.org/external/pubs/ft/weo/2009/01/index.htm) and OECD Economic Outlook, March 2009 (http://www.oecd.org/document/59/0,3343,en_2649_34109_42234619_1_1_1_37443,00.html).

[2] http://www.trade.cec.eu.int/intra/info/analysis/financial_crisis_updates.cfm

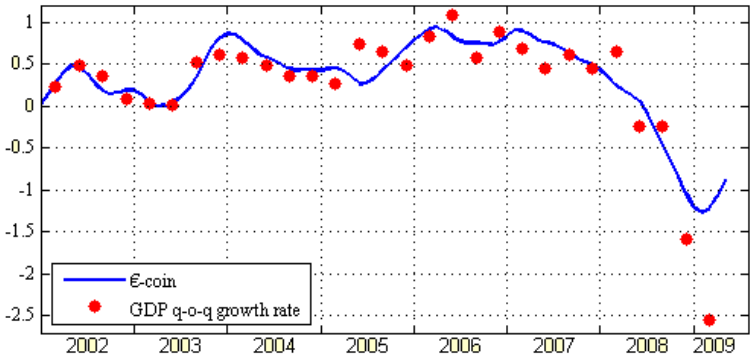
[3] Nyquist, Scott and Jaeson Rosenfield, 2009, 'Why energy demand will rebound' The McKinsey Quarterly, May.

Figure 1: Global outlook: Real GDP



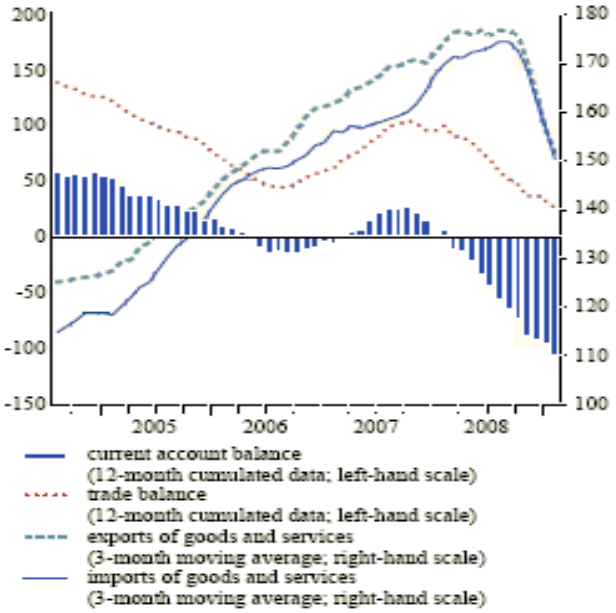
***Source**: IMF, World Economic Outlook April; Haver Analytics; and World Economic Outlook (WEO) database.*

Figure 2: Euro area GDP trend growth



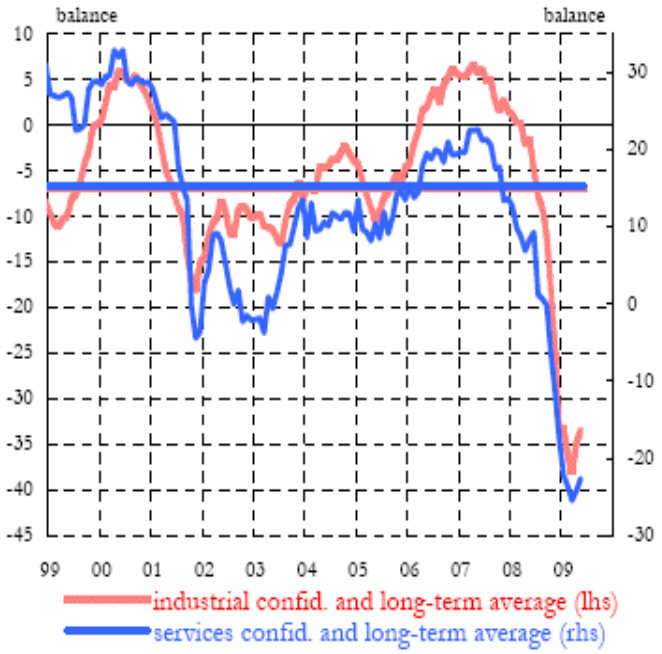
***Source**: CEPR, €-coin (http://eurocoin.cepr.org/)*

Figure 3: The Euro area current account and trade balances (EUR billions, monthly data, seasonly adjusted)



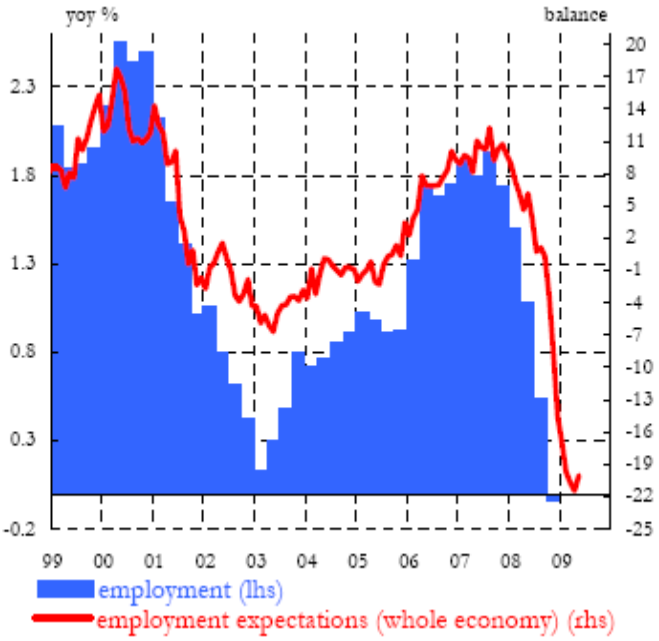
***Source**: ECB, Monthly Bulletin, May 2009.*

Figure 4: Industrial and services confidence



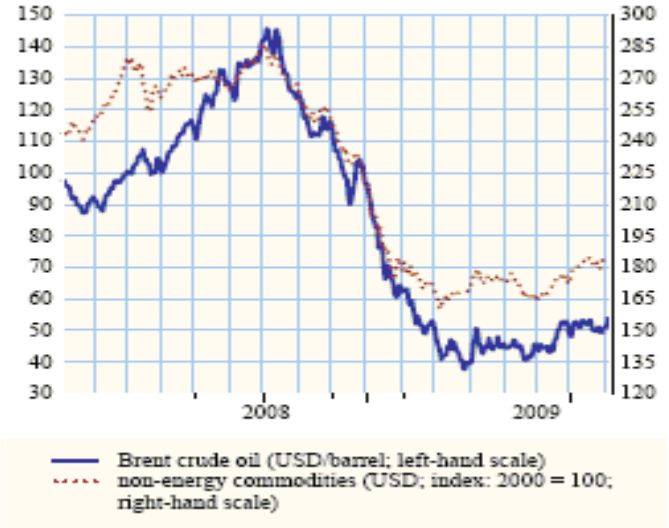
***Source*: DG Ecfin, Key Indicators for the Euro area**

Figure 5: Employment and employment expectations (manufacturing and services)



***Source*: DG Ecfin, Key Indicators for the Euro area**

Figure 6: Main development in commodity markets



***Source*: ECB Monthly Bulletin, May 2009, Bloomberg and HWWI.**