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Annex 2 and 3 of the Draft NAMA Text of July 2007: Implications for Bangladesh

By

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Background

On 17 July 2007, prior to the meeting of the WTO-TNC on July 26, 2007, the Chairman of the WTO Negotiating Group on Non-Agricultural Market Access (NAMA), Ambassador Don Stephenson of Canada, circulated a draft text on NAMA modalities titled *Chairman's Introduction to the Draft NAMA Modalities*. In the draft modalities the NAMA Chairman came up with a number of suggestions towards further liberalization of industrial tariffs.

As the Chairman noted, the NAMA text was drafted on the basis of his understanding of the various perspectives articulated during the NAMA negotiations. Although, during their deliberations in the TNC a number of countries have expressed their opposition to the idea that the draft be considered as a working document, there is a high likelihood that the draft modalities will serve at least as an important *reference point* for negotiations during the third quarter of the year 2007. It is thus important that Bangladesh and other developing countries closely examines this document to understand the possible consequences of the proposed NAMA modalities, and firms up their stance with respect to the proposals in the draft modalities.

This brief paper has been prepared with the aforesaid task in mind. The analysis particularly focuses on the possible implications of Annex 2 and Annex 3 of the NAMA modalities for Bangladesh which relates to the slower pace of implementation of the reduction commitments by the EU and the USA for certain selected items (23 items for EU in Annex-2 and 16 items in the USA in Annex-3 of the Draft Modalities). The analysis remains preliminary, however, and will need to be further extended and developed to understand the full impact of the NAMA modalities for Bangladesh.

The NAMA Draft Modalities

There is by now a general consensus that a *Swiss type* formula will be adopted for tariff reduction under the NAMA, with varying coefficients for the developing and developed country members of the WTO in light of the principle of non-reciprocity in commitments by these two groups of countries. LDCs have not been asked to undertake reductions commitments; however, the expectation is that they will bind their industrial tariff lines[1]. In this connection the NAMA text states, "Individual LDCs shall determine the extent and level of tariff binding commitments in accordance with their individual development objectives". Para 14, Draft NAMA Modalities, 17 July 2007).

Reduction of tariffs to be implemented by the developed and Non-LDC developing country members of the WTO, as suggested in the draft NAMA modalities, is likely to have adverse impact on LDCs such as Bangladesh, through *preference erosion* in those tariff reducing countries that provide preferential treatment to the LDC exports[2].

The draft modalities have suggested that the coefficient in the *Swiss formula*, to be used for tariff reduction purposes, would be 8 – 9 for industrial countries, whilst for the developing country members the coefficient will be between 19 and 23. [3] One of the major implications of these Swiss coefficients is that reductions will be much steeper for products with higher tariffs *(tariff peaks)*. As is known, apparels, Bangladesh's major export item, face tariff peaks (high tariffs) in both the US and the EU markets. Accordingly, Bangladesh will need to closely study the impact of all proposals with regard to NAMA negotiations.

[1] Most, including Bangladesh, have already bound their agricultural tariff lines.
[2] Rahman M. and Shadat W. B. (2006), "NAMA Negotiations in the WTO and Preference Erosion: Concerns of Bangladesh and Other Asia-Pacific LDCs", South Asia Economic Journal, Vol. 7(2).
[3] It is to be noted in this context that the developed countries wanted a coefficient of 10, while the developing countries sought a coefficient of no less than 30.

As is known, tariff reductions under the current negotiations are to take place from bound rates. It is to be noted in this connection that according to the US Trade Policy Review (2006), US's *Applied MFN tariffs* are at the bound rates 'to offer predictability to the US tariff regime[4]'. For the EU tariff rates have also been bound at applied rates[5] (for 98.2% of products, including apparels[6]). Accordingly, for all practical purposes, the reductions in both EU and the USA, under the NAMA negotiations, will begin from the applied rates.

As was stated above, in developed country markets where LDCs such as Bangladesh currently enjoy *Duty Free* access, any reduction in MFN tariffs will lead to erosion of preferences with consequent implications for price competitiveness. Also, similar impact is likely to be observed in the developing countries where LDCs receive preferential treatment through membership in the various RTAs. In some of the developing countries the proposed coefficient of 19-23 could result in tariffs coming down to below the applied rate, at least for some items. Consequently, margin of preference for LDCs such as Bangladesh, which are members of RTAs, could also be reduced i.e.; there could also be preference erosion of LDCs in developing countries as a result of NAMA negotiations.

The NAMA Chair has proposed Annex 2[7] and Annex 3[8] in the NAMA draft on modalities with a view to mitigating the adverse affect of preference erosion for the LDCs, and also developing countries. The idea is to slow down the pace of reduction in the preferential margins and to provide producers in these countries same breathing space to adjust. Instead of reductions of tariffs in 5 installments, the Chair has proposed reductions in 7 installments for selected items in the EU (Annex 2) and the USA (Annex 3). Annex 2 of the Draft Modalities contains 23 items at HS 8 digit level whilst Annex 3 has 16 items at the HS 8 digit level (The two lists are presented in Annexures 1 and 2 in this text in pgs 19-20). In both cases the selected items are predominantly apparels, but also include a few other items. The analysis below ascertains to what extent the proposed Annex 2 and Annex 3 will impact on Bangladesh's market access in the EU and the US market respectively.

Implications of Annex 2 and 3 for Bangladesh

Table 1: Estimates of Final Tariff Rate and Per Year Reduction Rate Applying the Swiss Formula with a Coefficient of 9

Tariff Rate (%)	Coefficient	New Tariff Rate (%)	Tariff Reduction	Per Year Tariff Reduction (5 installment)	Per Year Tariff Reduction (7 installment)
12	9	5.14	6.86	1.37	0.98

Source: Estimates based on NAMA Draft Modalities and TARIC database.

The analysis presented in Table 1 and Table 2 of the present text shows that with a *Swiss coefficient* of 9, the higher the rate of tariff the deeper will be the tariff reduction[9], and consequently, the average annual tariff cuts will be higher in those cases. As was stated above, tariffs on apparels generally face *tariff peaks* in developed countries, so that the depth of tariff cuts will be significant for apparel products. The estimates presented in Table 1 of this document shows that with a current base tariff of 12% for apparels in the EU, the tariffs will come down to 5.14% i.e.; the reduction will be to the tune of 6.86%. If the reduction is carried out in 5 installments the average yearly tariff cut would be 1.4%; to compare, if it is done in 7 installments the average yearly tariff cut will be about 1.0%. Although, the tariff cut itself will be deep enough, the difference between the annual rates of

[4] *Para 9; WT/TPR/S/160/Rev.1*
[5] *World Tariff Profiles 2006*
[6] *Para 11; WT/TPR/S/177/Rev.1*
[7] *See Annexure 1 for the detailed list of Annex 2 of the Draft NAMA Modalities for the EC*
[8] *See Annexure 2 for the detailed list of Annex 3 of the Draft NAMA Modalities for the USA*
[9] As would be expected under the Swiss formula.

reduction under the two regimes (5 installments and 7 installments) are not significant, only to the tune of 0.39% each year. Since LDCs including Bangladesh, receive preferential treatment in the EU a slower pace of reduction is likely to result in slower pace of preference erosion.

Text Table 2: Estimates of Final Tariff Rate and Per Year Reduction Rate Applying the Swiss Formula with a Coefficient of 9

Tariff Rate (%)	Coefficient	New Tariff Rate (%)	Tariff Reduction	Per Year Tariff Reduction (5 installment)	Per Year Tariff Reduction (7 installment)
8	9	4.24	3.76	0.75	0.54
16	9	5.76	10.24	2.05	1.46
32	9	7.02	24.98	5.00	3.57

Source: Estimates based on NAMA Draft Modalities and USITC.

The situation in the United States of America (USA) is somewhat different, since tariffs on items in Annex-3 vary widely, between 8 – 32%. As Table 2 of this text shows, the tariff peak of 32% will come down sharply to 7.0% i.e.; by about 25%. Thus, if carried out in 5 installments this will mean an average yearly tariff cut of 5.0%, whereas if done in 7 installments the average yearly cut will be about 3.6%, a difference of 1.4% each year is observed.
Bangladesh does not receive duty-free access to the US market. Thus, in contrast to trade with the EU, where slower pace of reduction will benefit Bangladesh, in the US a slower pace will be to the detriment of Bangladesh's interest. Thus, it is to Bangladesh's advantage to have faster reduction in tariff in the US market. Indeed, slower reduction is going to be advantage for AGOA and CBI LDCs which do enjoy duty-free access to US market.

As is quite evident from Table 1 of the text, the annual reduction in the tariff (1.4% as against 1.0%) in the EU, under the proposed NAMA modality (between the implementation period of 5 years and 7 years) is rather insignificant. Indeed this cannot and will not compensate for the significant preference erosion that Bangladesh will have to face ultimately[10]. The extension of the tariff reduction schedule by a mere couple of years is thus not going to help the LDCs to address the consequences of preference erosion in the EU. Consequently, the proposed protracted implementation of the tariff reduction schedule can be hardly termed as a *compensatory mechanism* in view of any likely *preference erosion*. In this context, other effective measures (immediate DFQF market access for all products from all LDCs in all markets, more specifically in the US, a global preference erosion fund, additional support under Aid for Trade etc.) must be considered on an urgent basis.

The Extent of the Impact

As is known, in the EU Bangladesh receives Zero tariff market access under the EU's EBA (Everything But Arms) initiative. Annex Table 1 in the text reveals that for most of the items in Annex-2 of NAMA the MFN tariff is at the level of 12%. Accordingly, any reduction in the MFN applied rate as a result of application of the *Swiss coefficient* proposed in the NAMA draft will lead to considerable preference erosion. As Annex Table A shows, Bangladesh exported 14 of these 23 items in 2006. However, in only 9 of these Bangladesh had any significant export in 2006. Export of the other five items was insignificant (these are the shaded items in text Table-3). A slower pace of reduction of the proposed items may be of some benefit to Bangladesh, since this will slow down the pace of preference erosion. But as was earlier stated, this will not matter much as a compensatory mechanism.

As a matter of fact, the actual consequence in terms of preference erosion for Bangladesh in the EU market will depend on whether the list in Annex-2 of the NAMA Draft included items that are entering the EU market by making use of the GSP facilities or not. If any of the 9 items (mentioned

[10] First from 12% to 5.14% under the current negotiations and to (near) zero percentage through future negotiations.

above with significant export from Bangladesh to the EU market) was not being able to enjoy GSP facilities (because of inability to comply with the EU Rules of Origin), then it would be better for Bangladesh to have such items excluded from Annex 2 of the draft text. Similarly, in pushing for items to be included in Annex 2 of the draft text (during subsequent negotiations), Bangladesh will need to see whether such items are actually being able to enter the EU market at ‘zero’ tariff by utilizing the EC GSP facilities. Only if for those selected items the GSP utilization rate was found to be high, will it make sense to ask for inclusion of such items in Annex 2[11].

It is seen from Table 3 that the GSP utilization rates for the 9 items of Bangladesh’s (considerable) export interest in Annex-2 of the NAMA draft vary across the various items. For some items the utilization rate is high, ranging between 85% and 100% (for five items). However, for the other three items the GSP utilization rate varies between 26% and 68% (Table-3). For the latter group of items, some of the exports in each tariff line enjoyed GSP facilities, but most did not (resulting in low GSP utilization rate). Indeed, if these three items, along with the four items noted above (where Bangladesh exports are negligible) are replaced by items for which Bangladesh’s GSP utilization rate was higher, Bangladesh would stand to gain from a protracted time line for tariff reduction in the EU. The strategy for Bangladesh thus should be to pursue negotiations along this line. It should be noted in this context that the EC is thinking of changing the RoO. Impact of any such possible change on Bangladesh’s GSP utilization rate should also be closely studied for the purpose of strategizing in the context of NAMA negotiations.

Table 3: Bangladesh GSP Utilization Performance in EU(27) for Items in NAMA (Annex 2)

(Million USD)

Products	***GSP Zero (a)***	***Total Exports (b)***	***GSP Utilization Rate (%) (a/b)***
03037998 – frozen salt water fish(excl.//3.79-87)	*0.23*	*0.27*	*85.53*
03042019 – frozen fillets of freshwater//salmon)	*0.06*	*0.06*	*100.00*
03042094 – frozen fillets of saltwater//renadier)	*0.00*	*0.01*	*0.00*
03061350 – frozen shrimps of the genus//water	*59.31*	*118.87*	*49.89*
03061380 – frozen shrimps and prawns//"penaeus")	*68.98*	*102.22*	*67.49*
57011090 – carpets and other textil//byweight)	*0.00*	*0.01*	*0.00*
61051000 - men"s or boys" shirts o//thervests)	*183.51*	*215.86*	*85.01*
61091000 - t-shirts, singlets and other//rocheted	*1218.14*	*1413.96*	*86.15*
61101290 - jerseys, pullovers, cardigan//rticles)	*18.85*	*19.08*	*98.79*
61102099 - women"s or girls" jerseys,//stcoats)	*386.38*	*424.31*	*91.06*
61103099 - women"s or girls" jerseys,//stcoats)	*559.50*	*639.39*	*87.51*
62034235 - men"s or boys" trouser//underpants)	*190.39*	*360.06*	*52.88*
62052000 - men"s or boys" shirts o//thervests)	*62.05*	*232.85*	*26.65*
62142000 - shawls, scarves, mufflers//crocheted)	*0.01*	*0.01*	*100.00*
Total (14 HSC)	***2747.42***	***3526.97***	***77.90***

Source: Estimated from EuroStat Database (based on Annex Table-G).

On the other hand, Bangladesh currently does not receive GSP preferential treatment for most of its exports to the US market (including apparels). Indeed, in 2005 only about 1.07% of Bangladesh’s export (in value terms) to the US was under preferential treatment[12]. In 2006 Bangladesh exported all the 16 items listed in Annex-3 of the NAMA modalities. Indeed, all these items belonged to wovenwear and knitwear. As a matter of fact, none of these items are covered under the US GSP Scheme for LDCs. Reduction of tariffs on these items will allow Bangladesh to enter the US market at reduced tariff. Accordingly, the suggested protracted implementation of tariff reduction in the NAMA modalities for the 16 items proposed in Annex 3 will not help Bangladesh’s export to the US; rather this will harm Bangladesh’s market access because of the slower pace of reduction. Indeed a more prolonged reduction of tariffs on these items will help AGOA and CBI beneficiary LDCs which currently enjoy ‘zero’ tariff market access for apparel products in the US market – their

[11] This exercise will need to be done by analyzing the GSP utilization scenario of Bangladesh in the EU market at HS 8 digit disaggregate level.

[12] In 2005 Bangladesh exported 602 items at HS 8 digit level to the USA. Of these only 125 received ‘zero’ duty under the GSP facility accounting for 20.7% of Bangladesh’s export (no. of tariff lines) to US market in 2005

preference erosion will be slowed down. In contrast, slower pace of implementation of tariff liberalization will mean that Bangladesh will need to continue exporting the 16 items in Annex-3 at relatively higher MFN duties (compared to a situation whereby tariff would be reduced at normal pace i.e.; in 5 installments).

As was stated above Bangladesh exported 14 of the 23 items listed in Annex-2 (for EU) of the NAMA Draft Modalities. Evidence suggests that those 14 items do indeed include a number of items of major export interest of Bangladesh. This is clearly seen from Annex Table A of this document (Pg. 9). Exports of these 14 items was worth USD 3536.9 million or 53.6% of Bangladesh's total export to the EU market in 2006. As will be evident from this table, the MFN tariffs on these items are quite high – about 12% for almost all products. Application of the *Swiss formula,* with a coefficient 9, would reduce this tariff to the tune of 5.1% (a reduction of 6.9%) as was stated earlier.
Annex Table B indicates that of the stated 14 items in Annex 2 of the NAMA text, only 8 belongs to Bangladesh's top 30 export items to the EU in 2006. These 8 items account for 53.3% of Bangladesh's total export to the EU[13]. The table shows that a number of articles of export interest to Bangladesh is not included in NAMA Annex 2. These are: HS 62046239 (Rank 5), 62034231 (Rank 6), 61102091 (Rank 9), 62046231 (Rank 10) etc. Thus, Bangladesh's interest will be to ensure inclusion of as many items of her top export interest (listed in Annex Table B of this document) as possible in the list presented in Annex 2 of the draft NAMA modalities.

As may be seen in Annex Table C, total export of the 23 items in Annex 2 from all LDCs was USD 6265.2 million (of which Bangladesh's export was USD 3536.9 million or 56.5% of the total LDC export). It is clearly evident from the table that although the LDC list includes some items of Bangladesh's export interest, there are others which cater to the interest of other LDCs. To reiterate, in case of possible revision of this list, Bangladesh should try to include those items from the list in Annex Table B of the present text which are of high interest to it, but are not at present included in Annex 2 of the NAMA draft. In doing so, as was stated earlier, the GSP utilization status ought to be closely studied.

The part of the NAMA draft pertaining to the US market (in its Annex Table 3) contains 16 items. As indicated in Annex Table D of the present text, in 2006 Bangladesh exported all the 16 items to the US, these 16 items accounted for about USD 1757.9 million or 50.3% of Bangladesh's total export to the US for that year. The MFN tariff rates of these items, as is seen from the table, vary between 7.4% and 32.0% (however, most of the tariff lines varied between 16% and 32%). Here also an application of the *Swiss coefficient* of 9 will result in substantial cut in the MFN tariff duties (as was stated earlier, for 16% MFN rate the tariffs will come down to 5.8%, or a reduction of 10.2 points; for MFN rate of 32% tariffs will come down to 7.0%, or a reduction of 25.0 points).

Annex Table E indicates that of these 16 items in Annex 2 of the NAMA text, only 11 items belong to Bangladesh's top 30 items of export to the USA. These 11 items accounted for 48.5% of Bangladesh's export to USA in 2006. As was mentioned earlier, since Bangladesh doesn't enjoy GSP facilities for apparels in the US market, any protracted reduction of the MFN duties (in 7 installments instead of 5) will have negative impact on Bangladesh's market access to the extent of the difference originating from the normal pace and the slower pace of tariff reduction. Accordingly, it should be in the interest of Bangladesh to have as small a number of items of export interest as possible included in the list in Annex 3 of the NAMA modalities.

Annex Table F shows that the 16 items that are listed in Annex-2 accounted for about 19.9% of LDC export to the USA in 2006. The table shows that the US list (in Annex 3) includes many items of export interest to Bangladesh in the US market. Out of the top 30 items of export interest to Bangladesh the NAMA Annex 3 table includes 11 items (accounting for 48.8% of Bangladesh's export in 2006). It will be to Bangladesh's interest to get at least some of these items excluded from this list to ensure faster pace of reduction of MFN tariff.

[13] Indeed the other 6 items account for less than 0.5% of Bangladesh's total export to the EU in 2006.

Conclusion - Bangladesh Strategy in view of Annex 2 and Annex 3 of the NAMA Draft

In the case of the EU market, Bangladesh’s interest will be *to have* as many tariff lines of export interest included in Annex 2, provided Bangladesh is able to utilize GSP facility for these items. In the case of the US market Bangladesh’s interest is *not to have* items of her export interest included in Annex 3.

It is to be noted that if the US provides ‘zero’ tariff market access to Bangladesh (for apparels or for all products) this scenario will be reversed. In this case, as is true for the EU, Bangladesh’s strategy will be to have as many items of her export interest as possible included in Annex 3 of the NAMA draft. Although this seems quite unlikely at this point of time, Bangladesh should remain alerted to this possibility.