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A CASE STUDY OF IMPACT ON A DEVELOPING COUNTRY

Rajesh Mehta
Pooja Agarwal

RIS-DP # 59/2003

Research and Information System
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WTO NON-AGRICULTURE MARKET ACCESS MODALITIES

A CASE STUDY OF IMPACT ON A DEVELOPING COUNTRY*

by

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Summary

The Cancun Draft Ministerial Text outlines the broad agenda for the ministerial consideration. For Non Agriculture Market Access it lays emphasis on the revised draft proposal submitted by Chairman of Negotiating Group on Market Access (NGMA). As a modality of negotiation it talks about 'non-linear formula' approach. The formula proposed in the NGMA Chairman's draft would cause 51.8 percent decline in India's current bindings. In this paper an attempt has been made to study the implications of this formula on Indian Industrial tariffs as India gets integrated with world trade. It also provides comparative analysis of the recently submitted controversial US-EC-Canada proposal that would seriously hurt India and other developing countries. It will lead to 76 per cent decline in India's average tariff, while tariff cuts by Canada will be 39 per cent, by EC - 32 per cent and by US - 36 per cent. So with this proposal of Canada-EC-US, developed countries tariffs are not falling substantially whereas developing countries have to make significant reductions.

WTO NON-AGRICULTURE MARKET ACCESS PROPOSALS
A CASE STUDY OF IMPACT ON A DEVELOPING COUNTRY

The 146 member nations of the World Trade Organisation (WTO) are destined to meet within few weeks for its fifth ministerial conference. A draft[1] on Cancun ministerial text has been prepared which will be discussed and probably adopted. India being the part of the WTO membership has to take care of its development strategy and trade policies. The promises of Doha Declaration have to be kept. Apart from many other topics like agriculture, services and TRIPs etc. the fate of market access for non-agriculture products will also be decided.

The draft Cancun ministerial text, recently circulated by the chairman of General Council of WTO, recommits to complete the work programme of Doha Declaration by 1 January 2005. Besides other areas, this draft has adopted the framework for modalities for negotiations on non-agricultural products set out by Negotiating Group on Market Access (NGMA). It has also asked the negotiating group to conclude its work on establishing modalities by some date that has to be decided. It has further stressed that negotiating group should ensure that the negotiations are concluded by that date.

In this paper an attempt have been made to assess the implications of millennium round of WTO negotiations on Indian industrial tariffs. Section I provides the background of these negotiations with a review of Doha mandate on market access of non-agriculture products. In Section II we have presented the current position of modalities for negotiations. In case there is an agreement on these modalities the road map for negotiations will be very clear i.e. almost finalised. Then follows its implications that we have estimated by taking India as our case study. Section III contains the implications of these negotiations on Indian industrial tariffs. Section IV concludes the entire scenario.

I. Background: Doha Declaration

The fourth ministerial conference of WTO was held in Doha, Qatar in November 2001. The ministerial declaration contained the mandate on number of issues. As a part of this mandate (paragraph16) it was decided that the negotiations on market access for non-agriculture goods should be conducted. Paragraph 16 says that, "We agree to negotiations which shall aim, by modalities to be agreed, to reduce or as appropriate eliminate tariffs, including the reduction or elimination of tariff peaks, high tariffs, and tariff escalation, as well as non-tariff barriers, in particular on products of export interest to developing countries. Product coverage shall be comprehensive and without *a priori* exclusions. The negotiations shall take fully into account the special needs and interests of developing and least-developed country participants, including through less than full reciprocity in reduction commitments. To this end, the modalities to be agreed will include appropriate studies and capacity-building measures to assist least-developed countries to participate effectively in the negotiations" cf, WTO, *Ministerial Declaration*, WT/MIN (01)/DEC/W/1, Nov. 14, 2001, Doha, 9-14, November 2001.

This Doha is a cause of concern for India and other developing countries in variety of ways. Those are as follows:

(1) The declaration highlights reduction and elimination of tariffs, tariff peaks, high tariffs, tariff escalation and non-tariff barriers. India has to be very careful about elimination of tariffs. It is sometimes said that elimination of tariffs by developed countries may give a higher market access to India and developing countries, because most of the developed countries are members of mega-trading blocs (with preferential and free tariffs). Elimination of tariffs, it may be pointed out will not provide preferential market to member countries of Regional Trading Associations (RTAs) for intra-regional trade. Hence non-member countries like India can get market access of member countries of mega-trading blocs.

(2) The Declaration also talks about reduction in and elimination of high and peak tariffs. The definition of high and peak tariffs has not been made very clear in modalities before negotiations start. Peak tariff in the literature is defined at a specified level, i.e., 10 per cent, 12 per cent or 15 per cent[2]. The level of the peak tariffs cannot be assumed as being the same for all member countries - developed countries, developing countries and LDCs. In fact, there is a case that it must be linked to average tariff.[3]

(3) The ministerial declaration also mentions reduction or elimination of tariff escalation as well as of non-tariff barriers. In this context, it should be remembered that the Uruguay Round negotiations led to increase in tariff escalation of developed countries; particularly for the products in which India and other developing countries have an export interest[4].

(4) The declaration does not mention the modalities of the negotiations. It merely states that the modalities have to be decided, and goes on to add that the decisions should take into consideration the appropriate studies and capacity building measures to assist LDCs.

(5) The Doha declaration does not mention anything about the base rate (the tariff rate for starting negotiations) as the basis of negotiations.

(6) The Doha Declaration also says that a member country cannot *a priori* exclude an item/product for negotiations. In other words, India and other developing countries cannot keep any item in the unbound list on an unilateral basis.

(7) There is no mention of "credit for autonomous liberalization".

(8) The declaration does not make any reference to an increase in transparency and predictability through a significant expansion of the scope of tariff bindings and through simplifying members' tariffs. A large number of developed countries are defining tariffs in the form of specific and compound duties, which have been found to be relatively high. It is very difficult to put them in the negotiations without knowing *ad valorem* equivalence and the other implications of such duties.

(9) The declaration talks about reduction or elimination of non-tariff barriers, in particular on products of export interest to developing countries. However, it does not talk about different types of non-tariff barriers be it hardcore or soft. Different issues relating to NTBs, namely identification, examination, linkage with other areas of Doha declaration, modalities, etc., remained untouched.

(10) In the negotiation process it is expected that there will be mounting pressure on India and other developing countries to reduce/eliminate its tariffs. A number of studies do however suggest[5] that developing countries should give emphasis on the following aspects:

- <u>Elimination of Tariffs:</u> Developing countries should completely reject the issue of elimination of tariffs as one of the core objects of the Doha declaration. Elimination of tariffs will lead to very high reductions by developing countries as compared to that of developed countries and a further reduction (or even complete elimination) in industrial tariffs of developed countries would not lead to a substantial increase in market access for countries like India. It will not be consistent with development dimension of the present Round. It will also be not consistent with the principle of 'less than full reciprocity'. Elimination of low/nuisance tariff should not be considered as equivalent to high or deeper reduction by developed countries.

- Reduction of Tariffs: Developing countries should not concentrate on reduction in the average tariff but their concerns should be on other aspects like peak tariffs, tariff escalation, 'credit for autonomous liberalisation', non-*ad valorem* duties, etc.

- Non-*Ad valorem* Duties: A large number of developed countries are used to the practice of imposing specific and complex duties rather than *ad valorem* duties. The total number of commodities for which custom duties are given in the form of specific duties, is very large for developed countries' for instance EU (1780 tariff lines), US (1455 tariff lines). In most cases, non-*ad valorem* duties[6] consist of one single specific tariff. However, many are mixed and complex, consisting of several specific and *ad valorem* tariffs associated with a condition of relationships between them. There are many variants of specific duties in the schedules of different countries. Some of these variants are very complex[7].

It has been noticed that the developed countries have imposed specific duties on a large number of commodities as compared to the number of commodities by developing countries. Although most of the countries believe that the specific duties should be replaced by *ad valorem* rates, no decision was made in the UR. In fact, a significant number of UR bound rates had been committed in the form of specific duties. It has been noticed that these specific duties conceal the fact that the countries are indirectly imposing high tariffs[8] without explicitly mentioning them in different forums[9].

The specific duties are not suitable for analytical and comparative purposes, and require more common *ad valorem* tariffs. Hence these specific duties should be converted to *ad valorem* equivalence[10] (AVEs). A study by UNCTAD (1999-2000) has computed *ad valorem* equivalence of specific duties for 18,000 commodities (of different countries) for the year 1996. It shows that the *ad valorem* equivalence of a large number of products, whose customs duties are defined in the form of specific tariffs in national custom tariff schedules, is very high.

The custom tariff database of the US for August 1999[11] also proves the above-mentioned observation. In this database, the US defines specific duties for around 600 industrial commodities (national lines) and provides the corresponding *ad valorem* equivalent rates of most of the specific duties. It shows that the average tariff rate of commodities with non-*ad valorem* duties is almost three times higher than the average tariff rate of the commodities whose custom duties is defined in form of *ad valorem* rates. In this context, it is worth highlighting that *ad valorem* equivalence of bound rates is still not available in the literature.

- <u>Tariff Peaks</u>: Even if the tariffs are reduced by developed countries, tariff peaks seem to be the major hurdle in the market access for certain sectors, where the developing countries have good export potential.

  In most of the literature[12], a cut-off point has generally been carried out for the identification of commodities with peak tariffs. The level of cut-off point is generally taken as 12 per cent (and sometimes 10 per cent or 15 per cent). All those commodities, whose tariff rate is more than 12 per cent *ad valorem* rate, are called commodities with peak tariffs. In the existing literature the selection of a cut-off point is arbitrary and has no relationship with average tariff. Further it does not make any distinction between different groups of countries.

  Besides, a number of attempts have been made to identify the commodities with peak tariffs. Notably the study by UNCTAD[13] concludes that, "both frequency and levels of tariff peak rates remain a matter of concern. Over 10 per cent of tariff universe of the Quad countries, corresponding to an aggregate 4,000-tariff line, will continue to exceed 12 per cent *ad valorem*. All four countries maintain high variance in tariff rates. One fifth of the peak tariffs of the US, one quarter of those in EU and Japan, and about one tenth of those of Canada exceed 30 per cent. In the four **<u>selected developing countries, tariff peaks are more frequent but reach less extreme rates</u>** than in the major developed countries" (emphasis added). Mehta and Mohanty (2001) also prove this point using detailed data of five developed countries.

- Tariff Escalation: Tariff structures of many countries have traditionally displayed significant escalation favouring domestic processors for a large number of commodities. It was expected that tariff commitments in the UR would provide for gradual reduction of escalation by applying relatively higher cuts to finished goods. However, rapidly rising tariffs have been noticed from low rates for raw material to higher rates for intermediate goods and sometime peak tariffs for finished products. A number of studies[14] have confirmed that tariff escalation has continued after the UR for a large number of sectors, particularly, fish & fish products, textile & textile products, leather & rubber products, footwear and to some extent wood & wood products. Basically, the results conform that tariff escalation is still a major constraint for export industries of India and developing countries.

- Non-Tariff Barriers: The developed countries have an impressive array of new measures of protection and government interventions. These have been imposed through different instruments, including non-tariff barriers (NTBs). The agreements of the UR have changed the intensity of different types of NTBs. Some measures of NTBs have lost their importance. However, a significant increase has been noticed in some other measures of NTBs.

  The non-tariff barriers continue to affect the growth of world trade and the UR could not tackle these issues successfully. On the one hand the importing countries generally term them as NTBs, the imposing countries insist that 'these instruments are policy objectives'. Developing countries should emphasise a coherent approach for dealing with such issues and participate actively in setting up new (and clear) rules and provisions.

In short, the priorities of developing countries should be focussed on Peak Tariffs, Tariff Escalation and NTBs to get market access, and to see that it is consistent with development dimension and "less than full reciprocity".

II. The Present Sate of Negotiation on Modalities

The preparations for the fifth session of the WTO ministerial conference are expediting. The chairman of the general council of WTO has circulated a revised draft of Cancun Ministerial Text[15]. This draft adopts the framework for establishing modalities in market access for non-agriculture products as submitted by the chairman of the Negotiating Group on Market Access (NGMA).The NGMA was created in WTO to initiate negotiations on market access for Non-agriculture products, such negotiations could be concluded by Jan. 1, 2005. The Fifth Ministerial Conference in Cancun will take stock of these negotiations and recommend appropriately.

II.1 WTO-NGMA Formula[16]

As part of negotiations a number of meetings of NGMA have been held and many proposals[17], particularly relating to Modalities, have been submitted by member countries.

The different modalities can be categorised into following five broad categories.

1. Request and offer
2. Formulae
3. Sector by sector
4. Zero for Zero
5. Mixed

A list of formulas submitted by some members to NGMA is given in WTO[18]. Based on different submissions, the chairman of NGMA has prepared a document 'Draft Elements of Modalities for Negotiations on Non-Agricultural Products', WTO, *TN/MA/W/35*/Rev.1 19 August 2003.

The major components of the NGMA Chairman Draft (NGMA-CD) are:

II.1.1 Formula

The application of the formula will be based on the following elements:

- base rate: tariff reduction or elimination on all non-agricultural products[19] from the bound rates after full implementation of current concessions[20]. However, for unbound items, the basis for commencing the tariff reductions shall be two times the MFN applied rate[21];

- the base year for MFN applied tariff rates shall be 2001;
- non-*ad valorem* duties shall be converted to *ad valorem* equivalents;
- HS nomenclature: negotiations to commence on the basis of Harmonized System (HS) 1996, and negotiations to be finalized in HS2002 nomenclature;[22] and
- for import data, the years 1999-2001, hereinafter "reference period", shall be used in order to mitigate yearly fluctuations.

All non-agricultural tariffs shall be reduced on a line-by-line basis using the following formula[23] applied to the base rates outlined in above paragraph:

$$t_1 = \frac{B \times t_a \times t_0}{B \times t_a + t_0}$$

where,

t_1 is the final rate, to be bound in *ad valorem* terms

t_0 is the base rate

t_a is the average of the base rates

B is a coefficient with a unique value to be determined by the participants (member countries of the WTO).

II.1.2. Sector-by-Sector/Zero-by-Zero Approach

The NGMA-CD has also proposed a sectoral elimination approach, in addition to the application of formula, for seven sectors: Electronics & Electrical goods; Fish & Fish products; Footwear; Leather goods; Motor Vehicle parts & components; Stones, Gems, & Precious Metals; and Textiles & Clothing.

II.1.3 Supplementary Modalities

In addition to the above two approaches the NGMA-CD proposes that member countries should adopt other procedures for ***additional tariff reduction and elimination***.

II.1.4 Non-Tariff Barriers

The Chairman summarises some elements for reductions or elimination of non-tariff barriers.[24] The above components do not summarise elements of 'special & differential treatments', 'newly acceded members' and 'appropriate study and capacity building', given in Appendix II.

Keeping the priorities of developing countries, the following paragraphs give some pointed observations on NGMA-CD modalities:

The core modality is based on formula. The formula proposed in NGMA-CD is a modified version of Swiss Formula. Swiss formula does not incorporate the structure and average level of tariff rates of individual member countries, while the NGMA-CD proposed formula takes cares of average tariffs of member countries. However, this formula (like Swiss formula) also depends upon the (***magic***) value of coefficient B. In Tokyo Round, the value of B was taken as 14 (and 16 in some cases). In this modified formula of NGMA-CD we cannot take B=14 or 16; because it will not lead to deeper reduction as per guidelines of the Doha declaration. The draft proposal is silent on the value of coefficient B.

The zero-by-zero approach for tariff elimination of seven sectors, i.e. Electronics & Electrical goods; Fish & Fish products; Footwear; Leather goods; Motor Vehicle parts & components; Stones, Gems, & Precious Metals; and Textiles & Clothing; is similar to information technology agreement (ITA). Although the NGMA-CD talks about S&D treatment for implementation period in these sectors, but it adds very specifically that approach will be applicable to all the products of these sectors, even for developing countries. In other words, India and other developing countries have to eliminate tariffs on all lines of these sectors. These sectors constitute a major share of developing countries trade. As mentioned earlier, it is not easy for developing countries to accept the elimination of all tariff lines even in an extended time frame.

The NGMA-CD is completely silent on tariff escalation of non-agricultural products. The formula does indirectly capture it. In case the NGMA-CD formula is used, the rate of the tariff escalation may declined as compared to as that of Uruguay Round[25]. However, the 'supplementary modalities' of NGMA-CD may lead to increase in tariff escalation. This may not meet the priorities of developing countries. In this context the draft proposal for market access for agricultural[26] is very clear. The proposal says that "for developed countries…… where the tariff on a processed product is higher than the tariff for the product in its primary form, the rate of tariff reduction for the processed product shall be equivalent to that for the product in its primary form multiplied, at a minimum, by a factor of 1.3". In other words, the proposal for market access for agriculture suggest that the binding rate of finished products should be reduced by more than 30 per cent as compared to that of raw-materials, if the pre-millennium round tariff of the final product is higher than that of the raw material.

The NGMA-CD proposal is very clear that all items whose duties are defined in the form of specific and complex form should be included in negotiations. It says "… Non-*ad valorem* duties shall be converted to *ad valorem* equivalents (AVEs) according to the procedures…" The NGMA-CD proposal also mentions the formula for working out *ad-valorem* equivalence of specific duties using simple methods. However, it is well known how some of these specific duties are defined and it is very difficult to calculate *ad-valorem* equivalence of these duties[27]. The NGMA-CD proposes that in such case of "Non-*ad valorem* tariffs for which AVEs cannot be calculated by the Secretariat because of the technical nature of the duties concerned shall be assumed to have an AVE equivalent to the tariff average (t_a) as used in the formula". India and developing countries should keep to close watch on this, because it has been noticed that the *ad valorem* equivalence of specific duties, indeed, is relatively very high as compared to those commodities whose duties are defined in the form of *ad-valorem* rates.

NGMA-CD is still not clear about coverage of NTBs to be dealt. It is probably not very clear about how to deal with non-tariff barriers. It is still talking about (i) identification and examination of various types of NTBs, (ii) categorisation, (iii) collection of information and (iv) inter linkage with other bodies of WTO. It says that modalities could include request/offer, horizontal or vertical approaches. Developing countries should ask for clear interpretation of such steps towards NTBs.

The NGMA-CD proposal says that "for developing countries …" up to 5 per cent of tariff lines may remain unbound provided that no more than 1 percent (1 per cent of the total value of a member's imports) could be taken in one HS chapter. Both these conditions of 5 per cent tariff lines and 1 per cent import value is very strict.

II.2 WTO-NGMA Possible Options[28]

After submitting above-mentioned draft the NGMA received various proposals for amendments to this draft. As a result some adjustments were proposed by the chairman in the form of possible options to the draft elements. These adjustments include capping the average value ($t_{a)}$ of the base rates at a certain level to be determined by the participants. And while calculating this average value both the bound rates and applied rates have to be given equal weightage. The countries that have less than 35 percent binding coverage are expected to bind all non-agricultural lines and bind the tariffs at a level not to exceed 27.5 percent. For developing countries longer implementation period is granted. Few more amendments are suggested in this paper relating to newly acceded members and non- tariff barriers.

II.3 EC-US-CANADA Proposal[29]

Another proposal came in the form of, " Joint paper by Canada, European Communities and United States on Non-Agricultural Market Access: Modalities, 11 August 2003". This paper proposes a Swiss formula approach with a single coefficient to be applied on a line by line basis. Less than full reciprocity will be achieved by reducing the formula cut by another factor (X) which will be based on credits given for binding coverage over and above 95 percent and narrowing the margins between bound and applied tariffs. For further flexibility less than formula cuts would be permitted for sensitive lines. Less than comprehensive bindings of all tariff lines will be allowed for least developed and IDA-only members.

These three proposals have been the topic of varied discussions for quite some time in the international scene. The EC-US-CANADA proposal has been strongly condemned by developing countries, as it does not seem to serve their interests. In the following section we have tried to estimate the resultant tariffs for India on the basis of above three formulae:

1. NGMA Chairman Draft (CD) Formula
2. NGMA Chairman 'Possible Options'
3. EC-US-CANADA Proposal

III. Impact of Formulae on India

III.1 NGMA-CD formula

(a) ***Methodology***

The NGMA-CD formula contains following variables:

1. t_0 - the base rate of all tariff lines of India
2. t_a - the average of the base rates
3. B - a coefficient with a unique value to be determined by the participants

The tariff cutting exercise will start from the Uruguay Round bound rates that are base rates. These rates are collected for non-agricultural commodities defined in HS-1996 at 6-digit level. These products do not include those tariff lines, which fall under sectoral elimination. With all these rates the simple average i.e. t_a was found out. Then we arbitrarily chose the values of B that were 0.25,0.5,1.0,1.5,2.0. After fitting these values in the formula for different scenarios of B consequential were the post-millennium round rates. The results are presented in Table I.

(b) ***Proposed Bound Rates***

India's average tariff rate for base year (2001) comes to 44.5 per cent for all non-agricultural products. Range of base tariffs is 0 to 70 per cent except for two items. Most of items in base year have rate of 25%, 40% and 70%. In case B = 1, proposed average bound rate in post-millennium development round comes to 21.2 per cent (excluding seven sectors). This will lead to a reduction of 51.8 per cent.

In case B = 1.0, bound rate of a large number of items will be 21.1 per cent (1698 items), 27.2 per cent (720 items), and 16.0 per cent (395 items). The range of India's proposed tariffs will be 0 to 27.2 per cent. Two items with mega-tariffs of 150 per cent (type of alcohol) and 300 per cent (passenger goods), in base year, will be 34.3 per cent and 38.7 per cent, respectively.

The increase in B (>1) does not lead to significant difference in reduction of tariffs; while decline in B below 1(i.e. B<1) reduces post-millennium bound tariffs significantly.

Table I: India: Proposed Bound Rate (%) in Millennium Development Round based on NGMA Chairman Draft Proposal, under Alternate Scenario of B (Excluding commodities of seven sector)							
	Base rate*	**B=0.25**	**B=0.5**	**B=1**	**B=1.5**	**B=2**	**No. of Tariff Lines**
	0.00	0.00	0.00	0.00	0.00	0.00	67
	3.00	2.36	2.64	2.81	2.87	2.90	7
	5.00	3.45	4.08	4.49	4.65	4.73	10
	10.00	5.27	6.90	8.17	8.70	8.99	28
	12.50	5.89	8.00	9.76	10.53	10.96	1
	13.30	6.06	8.32	10.24	11.09	11.57	2
	20.00	7.15	10.53	13.80	15.39	16.33	15
	25.00	7.70	11.77	16.01	18.19	19.52	395
	26.70	7.85	12.14	16.69	19.07	20.54	1
	30.00	8.12	12.78	17.92	20.70	22.44	9
	32.50	8.29	13.21	18.78	21.86	23.81	3
	34.00	8.38	13.45	19.27	22.53	24.60	1
	35.00	8.44	13.60	19.59	22.96	25.12	8
	36.00	8.50	13.75	19.90	23.39	25.63	1
	37.70	8.59	13.99	20.41	24.09	26.48	1
	38.90	8.65	14.15	20.76	24.58	27.07	1
	40.00	8.70	14.30	21.07	25.01	27.60	1698
	46.70	8.98	15.07	22.79	27.48	30.63	1
	50.00	9.10	15.40	23.54	28.59	32.01	72
	55.00	9.25	15.84	24.60	30.15	33.99	1
	70.00	9.60	16.88	27.21	34.17	39.18	720
	150.00	10.36	19.38	34.32	46.19	55.86	1
	300.00	10.73	20.71	38.75	54.60	68.64	1
Average (%)	***43.97***	***8.53***	***14.14***	***21.19***	***25.49***	***28.41***	**3044**

*Final Bound Rate or Two times MFN Applied Tariff Rate in 2001 (for unbound items).
Note: The analysis is carried out for 3044 commodities on the basis of 6-digit HS Level. The range of proposed bound rates is found out after excluding seven sectors under 'Sectoral Elimination' Approach. Although the average value (44.5%) is used while calculating the proposed rates, was based on all commodities.

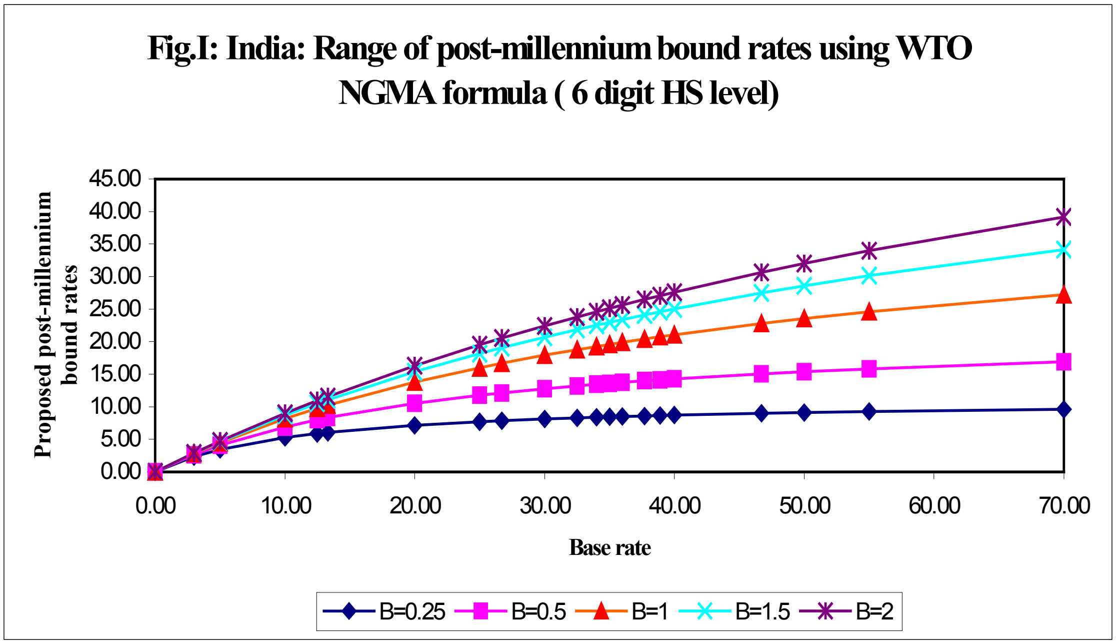

Fig.I: India: Range of post-millennium bound rates using WTO NGMA formula (6 digit HS level)
Proposed post-millennium bound rates
Base rate
B=0.25
B=0.5
B=1
B=1.5
B=2

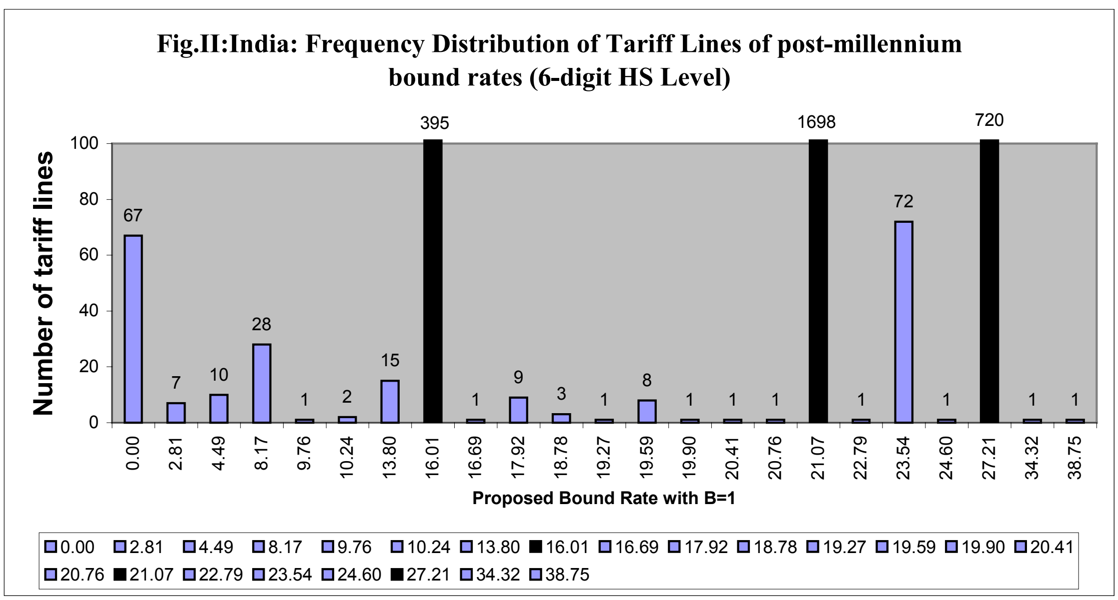

Fig.II:India: Frequency Distribution of Tariff Lines of post-millennium bound rates (6-digit HS Level)
Number of tariff lines
Proposed Bound Rate with B=1
395
1698
720
67
7
10
28
15
72

(c) Sectoral Tariff Elimination

We have defined seven sectors as per Table II. Our results show that tariff rates of all the items under 'fish and fish products', 'leather products', can be significantly cut. There are some items in textile sector (324 out of 2220) where tariff cut cannot be made significant, or eliminated. Out of 3251 items of seven sectors of India (at 8-digit), 2833 can be easily reduced or eliminated (Table III).

Table II: A Definition of Seven Sectors

Special sectors	**HS Chapters**
Fish and fish products	3,15,16
Leather goods	42
Textiles and clothing	50-63
Footwear	64
Stones, gems and precious metals	71
Electronics and electrical goods	85
Motor vehicles parts and components	87

Table III: Number of Iitems (at 8-digit HS-96) in which India can Eliminate Tariffs.

Sectors	**Total No. of Lines**	**Bound Items-Significant Cut**	**Bound Items-Inadequate Rate**	**Bound Items – Sufficient Rate**	**Unbound Items-High Binding Rate**	**Unbound Items-Significant Cut**	**Sensitive Items, where elimination can be problem**
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)=(4)+(5)+(6)
Fish and fish products	134	6				128	-
Leather goods	54					54	-
Textiles and clothing	2220	1024	4	302	18	872	324
Footwear	62				1	61	1
Stones, gems and precious metals	88	50			1	37	1
Electronics and electrical goods	555	329	4	38 (125)*	3	56	45
Motor vehicles parts and components	138	65			47	26	47
Total	3251	1474	8	465	70	1234	418

* We have excluded 125 commodities which fall under ITA agreement and whose binding is already fixed at zero

Source: RIS Study, *Indian Industrial Tariffs: Towards WTO Development Round Negotiations*, 2003

Above table has been prepared specially for these seven sectors after conducting an analysis all non-agriculture products that amounted to 9467 items by categorizing them in five groups*

(1) **<u>Group I: Bound Item – Significant Cut</u>** *<u>Identification of items where bound rates are very high and India could bring them down</u>*. *<u>These commodities are selected on the basis of various criteria:</u>*

(a) The commodities with low price elasticity, i.e. lower than the average value (1.29).

(b) Then, we have taken into consideration those commodities for which difference between tariff rates and bound rates are less than or equal to – 5 per cent points during the year 2000-01.

(c) The recommendations of apex industrial bodies, industrialists, department, etc. regarding the reduction of bound levels for certain commodities,

(d) Commodities with a very high share (value) of exports during the year 2000-01 and with a positive growth rate of exports for the last five years,

(e) Commodities with very high share (value) of exports during the year 2000-01 and with a negative growth rate of exports for the last five years but with a zero share value of imports during the year 2000-01,

(f) Commodities with very high share (value) of exports during the year 2000-01 and with a negative growth rate of exports for the last five years but with a very low share value of imports for the same year and with a negative growth rate of imports for last two years,

(g) Then, the rest of the commodities with a zero share (value) of imports during the year 2000-01 irrespective of their export share,

(h) Commodities with a low import share (value) during the year 2000-01, a negative rate of growth of imports for the last two years and a positive rate of growth of exports for the last five years irrespective of their export share,

(i) Commodities with a low import share during the year 2000-01 and with a growth rate of imports less than 10 per cent,

(j) Commodities whose imports are not increasing

(k) Commodities with low import share.

In case of textile items, following two additional criteria have been used.

(l) This contains items of the textile industry, i.e. items under Section XI of the ITC HS classification for which the committed level of the final bound rate is to be achieved by 1st March 2005. This identifies the items with bound rates that are high and could be brought down. Items of the textile industry are identified seperately, because the WTO committed level has to be achieved by 1st March 2005, and that level can be significantly lower than the present level of the MFN Tariff Rate. Further, there will not be a significant time difference between the: (i) implementation period of the present level of committed rate, i.e. 1st March 2005, and (ii) initiation of the process of implementation of the millennium round.

(m) As mentioned earlier, industrial items of the textile industry have been recently renegotiated, and the binding rates have been generally defined in the form of mixed duties, i.e. "a*d valorem* percentage, or Rs. A per unit whichever is higher".

Given the nature of these duties, i.e. mixed duties, we have not applied a large number of the criteria mentioned above, in identification of 'sensitive items'.

(2) **Group II: Bound Items – Inadequate Rate** *List of tariff lines where the existing bound levels are considered inadequate and effort can be made to see that these are raised suitably.* The various criteria used for identification of commodities in this list are as follows:

(a) On the basis of recommendations of the apex industrial bodies regarding increase in tariff rates.

(b) Commodities reserved exclusively for the small scale industries. In this case we have not taken into consideration those commodities, which were "Free" during 1998 to 2001.

(c) Commodities for which imports have increased in recent times, i.e. 2001-02 as per reports from various sources, economic dailies, G.O.I, particularly for those for which the QRs were removed in April 2001.

(d) Commodities on which anti-dumping duties are imposed but are not categorised above.

(e) Commodities on which safeguard duties are imposed.

(f) Recommendations of Ministry of Chemicals and Fertilizers, Department of Fertilizers, Government of India.

The criteria stated here were not applied to commodities of the textile industry, for which the import duty is defined in the form of “mixed duty” [30].

(3) **Group III: Bound Items Sufficient Rate** *Tariff lines where the existing levels of binding rates are considered just sufficient to provide the adequate protection.*

This list consists of all the bound lines, which are not included above two mentioned list, excluding items of textile industry and information technology.

(4) **Group IV: Unbound Item – High Binding Rate** *Tariff lines, which due to domestic sensitivities, cannot be bound or need to be bound at high levels.*

All the criteria used for the identification of items are used here also for unbound items. Along with those criteria, all the unbound lines for which QRs were removed in April 2001, with very high import values for the period April 2001-August 2001 and with very high growth rates of imports calculated for the periods April 2000-August 2000 and April 2001-August 2001 are shifted here. It also includes some fertilisers of the canalised route.

(5) **Group V: Unbound Item – Significant Cut** *Tariff lines of low trade interest, which may be bound at low levels.*

This list includes the unbound items, which are not included before.

(d) Additional Provisions for Developing Countries: Number of items under 5 percent Lines and 5 percent imports.

Table IV shows that there are 3.5 per cent of our tariff lines, which may not require significant cut or should remain unbound. These items belong to above-mentioned **Group II** (Bound Items – Inadequate Rate), **Group III** (Bound Items – Sufficient Rate), and **Group IV** (Unbound Item – High Binding Rate).

Table IV: India's number of Items which should be either Unbound or Highly Bound (at 8-digit HS Level)	
(a) All commodities	
	No. of lines
Group II	30
Group III	563
Group IV	167
TOTAL	**760**
Total No. of all lines	**9467**
% Share of all lines	**8.03**
(b) All Items (excluding special seven sectors)	
	No. of lines
Group II	22
Group III	98
Group IV	97
TOTAL	**217**
Total No. of lines	**6216**
% Share of all lines	**3.49**

Group II contains the items whose present level of bound rates is not considered adequate because of the imposition of safeguard and anti-dumping duties, "highly sensitive imports", small-scale industry or strategic industry of importance to Indian economy. **Group III** contains items where the final bound levels are considered adequate or sufficient. **Group IV** contains unbound items, which could not be bound in the Uruguay Round, and need to be bound at a higher level/unbound. The recommendations for identification of commodities in this category is based on number of criteria, i.e. "small scale industry", "toy industry", recommendations by apex and industry bodies, government department highly sensitive to imports, strategic industries.

III.2 NGMA Possible Options

This formula talks about capping the average tariff value to a certain extent. This can cause serious harm to India since levels of India's tariff rates are significantly high. Secondly, the procedure for calculation of average tariff value to be used in the formula is not very clear. Although we did some simulations on the basis of this new method and our results show that the value of base rate comes to 32 percent. And using this average value in the formula we have found that the tariff cuts have increased significantly. Like for instance with B=1 the estimated post millennium average comes down to 17.7 percent. Formerly (in NGMA CD proposal) this value stood at 21.9 percent. The detailed results are given in Table V.

Table V: India: Proposed Bound Rate (%) in Millennium Development Round based on NGMA Chairman 'Possible Options', under Alternate Scenario of B (Excluding commodities of seven sector)

Base rate	B=0.25	B=0.5	B=1	B=1.5	B=2	NO. of TL
0	0.0	0.0	0.0	0.0	0.0	67
3	2.2	2.5	2.7	2.8	2.9	7
5	3.1	3.8	4.3	4.5	4.6	10
10	4.4	6.2	7.6	8.3	8.6	28
12.5	4.9	7.0	9.0	9.9	10.5	1
13.3	5.0	7.3	9.4	10.4	11.0	2
20	5.7	8.9	12.3	14.1	15.2	15
25	6.1	9.8	14.0	16.4	18.0	395
26.7	6.2	10.0	14.6	17.2	18.8	1
30	6.3	10.4	15.5	18.5	20.4	9
32.5	6.4	10.7	16.1	19.4	21.6	3
34	6.5	10.9	16.5	19.9	22.2	1
35	6.5	11.0	16.7	20.2	22.6	8
36	6.5	11.1	16.9	20.6	23.0	1
37.7	6.6	11.2	17.3	21.1	23.7	1
38.9	6.6	11.3	17.6	21.5	24.2	1
40	6.7	11.4	17.8	21.8	24.6	1698
46.7	6.8	11.9	19.0	23.7	27.0	1
50	6.9	12.1	19.5	24.5	28.1	72
55	7.0	12.4	20.2	25.6	29.6	1
70	7.2	13.0	22.0	28.5	33.4	720
150	7.6	14.5	26.4	36.4	44.9	1
300	7.8	15.2	28.9	41.4	52.7	1
Average 32%	6.5	11.2	17.7	22.0	25.1	3044

* Final Bound Rate or Two times MFN Applied Tariff Rate in 2001 (for unbound items).

Note: The analysis is carried out for 3044 commodities on the basis of 6-digit HS Level. The range of proposed bound rates is found out after excluding seven sectors under 'Sectoral Elimination' Approach. Although the average value (32%) used while calculating the proposed rates, was based on all commodities.

III.3 EC-US-CANADA Formula

So far developed countries have been dictating the terms of international trade. This time also the proposal submitted by EC, US and Canada does not take into consideration the needs of developing countries. Although the value of coefficient to be applied in the formula is not clear but still we have conducted the tariff cutting exercise by taking this value as 15 (close to the value used in Tokyo round). Thereby it is seen that post millennium average tariff falls down by 76 percent. That is from 44 percent (base rate) the tariff falls down to 10.6 percent. On the other hand after some quick simulations based on bound rates of these three nations it is found that with the same value of coefficient B, Canada is giving only 39 percent cut in its average tariffs, EC 32 percent and US 36 percent. So with the same value developed countries tariffs are not falling substantially whereas developing countries have to suffer more. Thus this formula cannot serve the interests of developing countries with same value of coefficient.

Table VI: India: Proposed Bound Rate (%) in Millennium Development Round based on EC-US-CANADA Proposal, with B=15

Base rate (%)	Post Millennium bound rate (%) with B=15
0	0.0
3	2.5
5	3.8
10	6.0
12.5	6.8
13.3	7.0
20	8.6
25	9.4
26.7	9.6
30	10.0
32.5	10.3
34	10.4
35	10.5
36	10.6
37.7	10.7
38.9	10.8
40	10.9
46.7	11.4
50	11.5
55	11.8
70	12.4
150	13.6
300	14.3
Average	**10.7**

Note: The analysis is carried out for all non-agriculture commodities on the basis of 6-digit HS Level using B=15. The range of proposed bound rates is found out after excluding seven sectors.

IV. Summary and Concluding Remarks

Market Access for the non-agriculture products is one of the principal agenda items in the WTO negotiations. The basic mandate in the Doha declaration under the category 'tariff and trade of industrial products' is both broad and comprehensive. The developing countries should concentrate on reduction in peak tariffs and tariff escalations. It should also demand that all the countries should define their binding rates in the form of *ad valorem* rates, because it has been noticed that *ad valorem* equivalence of non-*ad valorem* duties are very high.

After the adoption of Doha agenda a number of proposals relating to 'modalities' were submitted by member countries to NGMA. The Chairman of NGMA submitted a draft proposal of modalities after a series of formal and informal consultations. The core modality/formula submitted by NGMA-CD takes into account most of the concerns of the developing countries, i.e. (i) tariff peaks, (ii) tariff escalation, and (iii) *non-ad valorem* duties. The NGMA-CD formula can take care of (i) reduction of tariffs, (ii) peak and high tariff and (iii) structure of pre-development round binding rates. In other words, if the average tariff of a country is low the declining rate of peak tariff will be substantial. This NGMA-CD formula is sensitive to co-efficient value of B. In case B=1, India's average applied rate will decline by around 51.8 per cent. The rate of decline of India's average MFN applied rate will be 81 percent, 67 percent and 35 percent, for B=0.25, 0.5 and 1.0 respectively. Keeping this factor in view India and developing countries should adopt this proposal with B=1. India and other developing countries should be very careful about NGMA chairman's 'possible option'. It talks about capping the value of average tariff, which is against the interests of developing countries like India. Similarly, India and developing countries should completely reject Canada-EC-US formula.

It is not easy for developing countries to completely accept the tariff elimination in seven sectors, even in an extended framework. Keeping in view the prevailing level of development and their infrastructure in the developing countries, it needs to be appreciated that tariff is an important instrument for making domestic and trade policies. On the domestic front tariff elimination, it may be recalled, will lead to substantial reduction in customs revenue that is the main form of revenue receipt for the developing countries. The developing countries therefore, should be given full advantage of "less than full reciprocity". It should be either (i) 'Zero-for-A', where A is a positive number (say 5 percent) for developing countries; or (ii) the coverage of lines in identified seven sectors should be 75 per cent of lines for developing countries, or (iii) ‘Seven-for-Four’, where developing countries should eliminate tariffs for any four sectors. The thrust could be to grade the product tariff according to the developing countries’ capabilities.

Notes

1 "*Preparations for the fifth session of ministerial conference, Draft Cancun Ministerial Text, Revision*", JOB (03)/150/Rev.1, WTO, 24 August 2003.

2 See for example WTO (2001), *US Trade Policy* Review, Geneva.

3 See, Mehta (2001), *WTO, Liberalisation and Industrial Sector: The Case of Market Access*, RIS Occasional Paper No. 63.

4 See, Mehta (2003), *Indian Industrial Tariffs: Towards, WTO Development Round Negotiations*, RIS.

5 UNCTAD (1999-2000), The Post-UR Tariff Environment for Developing Countries: Tariff Peaks and Tariff Escalation, TD/B/COM/1/14/Rev/1, 14, September. Mehta (2001), ibid; Mehta (2003), ibid, UNCTAD (2003), Back to Basics: Market Access Issues in the Doha Agenda, UNCTAD/DITC/TAB/Misc.9, and Bacchetta, M. and B. Bora (2003), Industrial Tariff Liberalization and the Doha Development Agenda, WTO Discussion Paper.

6 Amount of value per unit of imported commodity.

7 See, for example, UNCTAD, CDROM *TRAINS* Winter 1998 and Mehta, R. and S.K. Mohanty (2001), *WTO and Industrial Tariff: An Empirical Analysis for India*, Reprint, RIS.

8 See Mehta and Mohanty (2001), *ibid*. UNCTAD, *ibid*.

9 See Mehta and Mohanty (2001), *ibid*, UNCTAD *ibid*.

10 See Mehta and Mohanty (2001), *ibid.*

11 Mehta R. (2001), *ibid*.

12 See, UNCTAD (1999-2000), *ibid* and UN, *Market Access since UR, Implications, Opportunities and Challenges,* Report prepared by UNCTAD and WTO, May 1998.

13 See UNCTAD (1999-2000), *ibid* for instance.

14 UNCTAD, *ibid* and Mehta (2001) *ibid* in the recent past.

15 "Preparations for the Fifth Session of the Ministerial Conference, Draft Cancun Ministerial Text, Revision", JOB(03)/150/Rev.1, WTO , 2003.

16 "Draft elements of modalities for negotiations on non-agriculture products", TN/MA/W/35,Rev.1, WTO 19 August 2003.

17 A number of proposals have been submitted by different countries. Among these proposals three submissions have been made by India.

18 "Formula approaches to tariff negotiations, Note by the Secretariat, Revision, TN/MA/S/3/Rev.2", WTO, 11 April 2003.

19 All products not covered by the WTO Agreement on Agriculture.

20 Credit may be given for autonomous liberalization provided that the items were bound on an MFN basis in the WTO since the conclusion of Uruguay Round. Thus, in the following cases, credit will accrue by using the base rate that was in place before the autonomous liberalization took place, and the formula reduction would be applied to this higher basis. In the case of items that were not previously bound, two times the MFN applied rate or the new bound rate, which ever is higher, for the year the liberalization took place would be the basis. It is noted that in the cases of the Ministerial Declaration on the Expansion of Trade in Information Technology Products, further initiatives in the Pharmaceutical zero-for-zero sector, and certain other individual initiatives, the bound rate was reduced to zero and through the application of the formula, credits would not be relevant. Thus, for the remaining items, credit could be given for the tariff lines noted in the following WTO documents which have been given legal effect through certifications: European Communities (WT/Let/178), Hungary (WT/Let/441), India (WT/Let/374), Korea (WT/Let/302), Pakistan (WT/Let/424), Sri Lanka (WT/Let/398), and the United States (WT/Let/182).

21 When the MFN applied rate in the base year is less than 2.5 percent, 5 percent shall be used as the basis.

22 If Members so desire, they may commence with HS2002 nomenclature if the corresponding concordance tables are provided.

23 All numbers used in the formula will be calculated to one significant decimal point.

24 Para 13 of "Draft elements of modalities for negotiations on non-agricultural products", TN/MA/W/35, WTO,16 May 2003.

25 Uruguay Round led to increases in tariff escalation particularly for products in which developing countries have export potential. See, Mehta and Mohanty (2001) and UNCTAD (1999/2000), among others.

[26] WTO (2003), *Negotiations on Agriculture First Draft of Modalities for the Further Commitments*, Committee on Agriculture, TN/AG/W/1/Rev.1, 18 March 2003.

[27] See for example UNCTAD, *TRAINS,,* Winter 1998; and Mehta and Mohanty (2001).

[28] "TN/MA/W/35: "POSSIBLE OPTIONS", JOB (03)/155,WTO (2003).

[29] "Non-agricultural Market Access: Modalities, Joint Paper by Canada, European communities and United States", WTO (2003).

[30] This is because the specific duty of "mixed rate" will take care of high import price.

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