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What Impact will the Outcome of the Hong Kong Ministerial Have on the Textiles and Clothing Sector?

in:

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By Esther Busser

1. Introduction

From 13-18 December, the 6th WTO Ministerial took place in Hong Kong. Although, in general, not much was accomplished, some substantive decisions were made in the area of Non Agricultural Market Acess (NAMA), which includes the textiles and clothing sector.

The NAMA negotiations can affect the textiles and clothing industry twofold. First of all, the negotiations in NAMA focus on tariff reductions. A reduction of domestic tariffs means that the domestic market is less protected against imports from other countries. Since the elimination of quotas at the beginning of 2005, many countries are already facing cheap textiles and clothing imports, especially from China, which harm domestic markets. A drastic reduction in applied tariffs would increase such imports, especially now that the EU and US have reached an agreement with the Chinese government to limit Chinese imports into the US and EU.

Secondly, many developing countries receive preferential access to developed countries' markets such as the EU and US. Tariffs on textiles and clothing are relatively high in developed countries; developing countries have a large benefit from the preferences they receive. A sharp reduction in the overall tariffs of developed countries will reduce the preference margin that many developing countries enjoy. Their advantage compared to other non-preference receiving countries will be reduced and market share might be lost.

2. Tariff Reduction Formula

The use of a Swiss formula for tariff reductions was agreed upon in Hong Kong. With a Swiss formula there is a greater reduction of higher tariffs than of lower tariffs, i.e. developing countries, which generally have much higher tariffs than developed countries, will have to reduce their tariffs to a larger extent (non-linear) than developed countries. In the previous Uruguay Round an average reduction was applied, whereby countries had to reduce their tariffs by a certain average. But they were flexible in terms of reducing certain tariff lines to a large extent and keeping others, which were more sensitive, higher.

This Swiss formula not only reduces high tariffs on a larger scale (with an aim to harmonise tariffs) but also applies the formula on a line-by-line basis, for all tariff lines. There are two types of Swiss formulae, and WTO Members still have to decide on which formula to use. The first one is a simple Swiss formula, and the second one is a Swiss type formula. Examples of the Swiss type formula are the ABI (Argentina, Brazil, India formula) and the Caribbean formula. The basis of the Swiss type formula is the average tariff of members, and which is more advantageous for developing countries, as they generally have rather high average tariff levels. The ABI formula would result in using multiple country specific coefficients. The Caribbean proposal goes a step further than the ABI proposal in that it also assigns credits to countries for specific situations such as dependence on preferences, dependence on tax revenue, limited export base, etc.

Simple Swiss: final bound tariff = ([initial bound tariff] x [coefficient]) / ([initial bound tariff] + [coefficient])

ABI: final bound tariff = ([initial bound tariff] x [tm x [coefficient]) / ([initial bound tariff] + [tm x [coefficient]), where tm is the national average bound rate.

Caribbean: final bound tariff = ([initial bound tariff] x [tm x [coefficient + C]) / ([initial tariff] + [tm x [coefficient + C]), where tm is the national average bound rate and C is the credit.

The value of C will be the sum of the values of relevant factors for each developing country such as: substantial tariff binding coverage, autonomous liberalisation, revenue dependence, need to maintain and strengthen domestic industries, policy space for development of potential industries and for general industrial development, adjustment costs for loss of preferences, existing degree of openness and vulnerability to external shocks, economic vulnerability.

For example, a bound tariff of 30% under a simple Swiss formula would result in a bound tariff of 15% after applying a coefficient of 30. A coefficient of 6 would lead to a tariff of 5% for a bound tariff of 30%.

The basis for tariff reductions shall be the bound tariff level. Countries with unbound tariffs in textiles and clothing will have to bind their tariffs and then apply the reduction formula (explained below).

The coming months will be used to determine which of the two types of formula is going to be used and, once a formula has been chosen, which coefficients shall be applied. The higher the coefficient, the lower the cuts, and the higher the final bound tariff. If, for example, the coefficient is 10 then the final bound tariff after formula cut will show a range of tariffs for a specific country with maximum tariffs of 10%. If the coefficient is 30 then the range of tariffs will show a maximum of 30%. It should be noted that the Swiss formula factually results in substantial cuts, even when using a relatively high coefficient.

A number of proposals were tabled based on the simple Swiss formula, either with one coefficient or with two coefficients. In the case of two coefficients there was a proposal by Pakistan for a coefficient of 6 for developed countries and a coefficient of 30 for developing countries. The EU proposed a coefficient of 10 for developed countries and 15 for developing countries. The US requests the two coefficients to be “within sight of each other”. No concrete proposals for coefficients have been made with respect to the ABI formula.

Both types of the Swiss formula will bring about sharp tariff cuts, but, in comparison to the simple Swiss formula, the ABI or Caribbean formula would not entail such drastic cuts for developing countries. On the other hand, there is the issue of preference erosion for a number of developing countries if a major reduction of the developed countries’ tariffs takes place. With respect to preference erosion an ABI formula would be less preferable than a simple Swiss formula, as it would lead to more preference erosion due to greater tariff cuts in developed countries, as they have low average bound tariffs.

3. Tariff Binding

As already mentioned above, tariff reductions will be carried out on the basis of the bound tariff. Countries that have bound less than 35% of their tariffs (the so-called paragraph 6 countries[1]) are required to bind 100% of their tariffs, but will not be asked to reduce their tariffs. Also LDCs are excluded from tariff reduction, but they are requested to bind their tariffs substantially.

1 Paragraph 6 countries with binding levels lower than 35% of their tariff lines are : Cameroon (0.1%), Congo (3.2%), Côte d’Ivoire (22.9%), Cuba (20.4%), Ghana (1.2%), Kenya (1.6%), Macao (15.6%), Mauritius (5.3%), Nigeria (6.9%), Sri Lanka (28.3%), Suriname (15.1%) and Zimbabwe (9.0%).

Many developing countries still have a large number of unbound tariff lines (e.g. Bahrain, Fiji, India, Malaysia, Pakistan, Philippines, Singapore, Thailand and Tunisia). In order to apply the tariff reduction formula, unbound tariffs have to be bound first. The negotiations, therefore, focus on the method of binding.

It was decided in Hong Kong to bind unbound tariffs by adding a non-linear mark-up to the applied tariff. This will then be the base rate for tariff cuts. The non-linear mark-up will consist of adding a number of percentage points to the applied tariff - either a constant number of percentage points, or a different number of percentage points depending on the level of the currently applied rate (the lower the applied rate the higher the mark-up, and the higher the applied rate the lower the mark-up). Most discussions have focused on a constant mark-up with proposals concerning the number for the mark-up, ranging from 5 to 30 percentage points. An applied tariff of 15% will thus receive a mark-up of, for example, 15% to get a bound rate of 30%. This tariff of 30% will then be reduced by applying the tariff reduction formula. With a coefficient of 10 in a simple Swiss formula, the new bound rate will be 7.5%.

4. Flexibilities for Developing Countries

Paragraph 8 of the "July framework"[2] provides for flexibilities for developing countries, which is the third key issue in NAMA negotiations. These flexibilities are:

"We agree that developing-country participants shall have longer implementation periods for tariff reductions. In addition, they shall be given the following flexibility:

a) applying less than formula cuts for up to [10] percent of the tariff lines provided that the cuts are no less than half the formula cuts and that these tariff lines do not exceed [10] percent of the total value of a Member's imports; or

b) keeping, as an exception, tariff lines unbound, or not applying formula cuts for up to [5] percent of tariff lines provided they do not exceed [5] percent of the total value of a Member's imports.

We furthermore agree that this flexibility could not be used to exclude entire HS Chapters."

2 This refers to the framework for further negotiations that was adopted at the WTO General Council in July 2004.

Developing countries can, thus, exempt up to 5% of their tariff lines from the tariff reduction formula, or identify up to 10% of the tariff lines for less than formula cuts.

A number of countries (Argentina, Brazil, Venezuela, China, Egypt, India, Indonesia, Namibia, Pakistan, Philippines and South Africa) had submitted a communication on paragraph 8 flexibilities at the end of last year (TN/MA/W/65), demanding that developing countries should be able to retain the right to revise the percentages (of tariff lines exempt from full tariff reduction, or subject to reduced tariff reduction) upwards to enable countries to manage the adjustment of sensitive sectors and to prevent social disruption caused by job losses and closure of enterprises that would be the result of further liberalisation. The Hong Kong Declaration does not elaborate further on the flexibilities.

It will be important to first look at how these flexibilities could deal with the concerns regarding job losses arising from the application of the formula in textiles and clothing, and then to determine if there is a need for an extension of these flexibilities (both the percentages and the value limitations could be too restrictive to offer enough flexibility).

5. Sectoral Negotiations

The NAMA negotiations framework also provides for sectoral negotiations. The aim of such negotiations is not only a more ambitious tariff reduction than a formula cut, but also an elimination or a harmonisation of all tariffs in a sector. A number of sectors have been identified for negotiations on tariff elimination or harmonisation. These are bicycles, chemicals, electronics/electrical equipment, fish, footwear, forest products, gems and jewellery, pharmaceuticals and medical equipment, raw materials and sporting goods, textiles, apparel and auto/autoparts.

The sectoral negotiations on textiles and clothing have not really started yet. They also differ from the other sectoral initiatives in that they might aim at tariff reductions that are lower than the tariff formula reductions in order to shield the sector from further disruption after last year's elimination of quotas. A number of developing countries are looking into this sectoral initiative, including Turkey, Tunisia, Mauritius, Jordan, Dominican Republic, North African countries and others. The coming weeks will bring about more clarity as to if and how this initiative will be taken forward.

6. Non-Tariff Barriers

Discussions regarding NAMA not only focus on tariff reduction but also on Non-Tariff Barriers (NTBs), such as technical requirements. A large number of NTBs have been identified by countries, but no agreement has been reached with regard to these NTBs. Some of the NTBs are dealt with in other negotiating groups, and some are dealt with bilaterally. SA 8000[3] is considered to be a NTB and is included in the list.

The US has tabled a proposal on labelling requirements in textiles, clothing and footwear. The aim of the proposal is to examine administrative and other practices that are used to implement labelling programmes in textiles, clothing and footwear industries, with an aim at identifying efficient methods for provision of the information.

7. Other Issues

Some general language on the need to address preference erosion and the situation of small and vulnerable countries is included in the Hong Kong Declaration. As indicated above, preference erosion will be substantial in the case of textiles and clothing if a Swiss formula is applied.

Another important issue is the impact of tariff reduction on tariff revenue. A number of countries depend quite substantially on tariff revenue for their government expenses.

8. The Linkage Between Agriculture and NAMA Negotiations

The Hong Kong Declaration includes a paragraph (para 24) on the link between NAMA and Agriculture with regard to market access for developing countries, stating that ambition on market access should be comparable in both areas of negotiations.

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3 The SA 8000 "standard" is a code of conduct with a "verification" system administered by the US-based NGO, Social Accountability International (SAI). Supplying companies can ask organisations authorised by SAI to issue them a certificate that indicates compliance with the SA 8000 standard. The supplier can then use this certificate to assure sourcing companies that its working conditions are consistent with the SAI code.

Whether full modalities for NAMA can be set by the end of April will depend mainly on the progress made in Agriculture, and, particularly, if an agreement can be reached among the major players – the US, EU, Brazil and India. Both Brazil and India are likely to cede substantially with respect to NAMA (as discussed further below) if Agriculture can be resolved. Overall, many commentators believe that a large number of developing countries might agree to a NAMA agreement provided they benefit from Agriculture. For example, Brazil already showed some flexibility with regard to the EU on NAMA in making a proposal that was then removed from the agenda anew. Many developing countries appear sanguine about NAMA impacts as they fall into categories that will enable them to limit the impacts for the time being (i.e. LDCs, or the "paragraph 6" countries that have bound less than 35% of their tariffs, both are exempt from tariff reductions). However, there remain a number of countries that will be more or less greatly affected, depending on the structure of their tariffs and the difference between bound and applied tariffs. If the industries that are prone to be affected by tariff reductions are highly labour intensive, a significant unemployment rate would, likely, be the result. Other countries will be affected due to preference erosion (primarily LDCs and ACP countries)

9. Negotiating Timelines

NAMA negotiating (days and) weeks are scheduled for March and April. Modalities are aimed for by 30 April 2006. The main issues that remain to be discussed and require a solution prior to the end of April are the coefficients of the formula, and the choice between a simple Swiss and a Swiss type formula, the flexibilities and the mark-up for binding of tariffs. It is very likely that developing countries shall continue to support a Swiss type formula. In the end, however, they may well be willing to give it up in exchange for a high coefficient in a simple Swiss formula. Especially for Brazil, a simple Swiss formula with a high coefficient would be less harmful than for other countries, as there is a big difference between its applied and bound tariffs. Therefore, considerable cuts will not have such a major impact, as these will mainly be cuts in bound tariffs but not (or only minor) cuts in applied tariffs. Other developing countries will, however, face severe cuts in applied rates. Members are also supposed to look at ways of dealing with preference erosion and small and vulnerable economies. And, finally, Members will have to set up methods and timelines for dealing with sectoral negotiations and NTBs. Decisions on these issues are expected by the end of July 2006. Depending on the outcome of the discussion on coefficients there might be more movement in the area of sectoral negotiations (i.e. if low tariff reductions are the result of the formula, it makes it more likely that the overall NAMA negotiations will be followed up by sectorals).

10. How Can Trade Unions Get Involved?

There are several processes for involvement: national, regional and international. The ICFTU lobby and policy work on trade is organised around the TILS network (Trade, Investment and Labour Standards) which also includes the Global Union Federations (GUFs) such as the International Textile, Garment and Leather Workers' Federation (ITGLWF). The trade union's positions are discussed within this network with regard to a broad range of issues, including manufacturing trade and trade of textiles and clothing. In particular, the current round of negotiations (Doha Round) with an aim to lower tariffs in manufacturing substantially, as well as the end of quotas in textiles and clothing, have brought many concerns in connection with the current trade rules. Position papers are part of the work on trade, in particular with regard to the ongoing negotiations and the different elements therein as an outcome of TILS. At the regional level there are both the ICFTU regional office for Africa (ICFTU-AFRO) as well as the ITGLWF regional office. At the national level it is up to the national centre or the textiles and clothing workers' union to, first of all, estimate the impact of possible scenarios that are under negotiation on employment, to identify an ideal scenario for the country, to lobby the government, in particular the trade minister for inclusion of the conclusions of the trade union assessment in the decision-making process. This can be done either through consultations (inside strategy) or through an outside strategy, such as using demonstrations, actions etc. At the same time, it is important to link up with other trade unions in the region that have similar positions. There is an important role here for the regional office. And, finally, it is important that the actions and lobby work that take place at the national level are brought back into the multilateral decision-making process in the WTO in Geneva, where negotiators come together. The national trade unions' concerns and demands have to be heard at the national level and the international level, and the government has to be held responsible for decisions it takes at the international level that will affect the employment situation in each country.