Appropriate Use of Trade Defence Instruments

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[This document reflects the views of the author only]

There is community and international agreement that some types of government subsidies and of private market behaviour damage economic welfare and perhaps other interests such as perceptions of fairness. The instruments currently available to the Community do not match these problems well, and the least well matched is the most used. The results are that anti-competitive behaviour is not identified and that there is potential for interventions that reduce competition, lower economic welfare, and damage development. The remedy is to move to a system that attacks the problems directly.

Has globalisation transformed trade relations and the role of TDI? Or have attitudes to it changed?

High import penetration and globalisation of production were well established by the time current TDI were first used extensively, in the 1980s, and in the industries where they are most used. There may be more industries, and a higher share of more economies, which are very dependent on imports or exports, but cross-national production and intra-company trade are not new. The problem of deciding what is a national industry and where the national interest lies between two firms, both with national production, national employment, foreign production, and exports, but one foreign owned, was an issue of the 1970s. If there is a change, it is that the gradual increase in the number of companies and people for whom trading is normal has reached a point where they are more likely to be surprised by a trade barrier than by a new traded product. As noted in the setting out of the Issues, outsourcing has become more widespread across companies and activities, and this suggests that there is more acceptance that it is fair to use alternative production locations which are more favourable.

Trade defence instruments identify two targets, trade which is considered unfair, whether because of the exporter's strategy or his government's assistance, and injury caused to producers. Only trade flows which are found to be both unfair and damaging to Community industry are targeted,[i] and the Community's 'lesser duty' rule means that the extent of the injury limits the duty. The injury calculation is difficult to apply and subject to controversy. Nevertheless, as it would be blatantly protectionist to propose that the fact that an industry is suffering injury is in itself a reason to restrict imports, the substantial arguments about TDI are about what is 'unfair'. Have Community views on what is 'fair' changed, such that the coverage or application of TDI need to adjust? The declining use of AD by the Community is cited by Evenett, Vermulst, 2005, as a sign of changing attitudes by member countries.

The growth in public lobbying against AD, in particular in cases in 2005 and 2006 against China, may reflect not only that consumer groups and users of imports are

more aware of their potential losses from TDI, but also that they now judge that public opinion has moved away from equating producer interests with the national or Community interest. That is, it has become politically acceptable to lobby against producer groups. If this change is happening, it suggests that the way in which the Community interest is interpreted may need to evolve.

The very clear identification of the products which are affected by a TDI and the fact that the instrument deals with an existing import means that the normal assumption in analysing trade policy, that consumers have less focused interests than producers because they cannot visualise the benefits of a potential liberalisation of trade, does not hold. This would, however, have been true at any time in the history of TDI, and it might seem that industrial users of a product would be better able to organise against controls on it than consumers plus retail interests. The change could be the result of a combination of greater concentration and organisation in retail markets and growing concern for the interests of consumers relative to employees. The demographic reduction in the ratios of workforces to total populations could be having an effect.

The use of TDI, in theory and in practice (Issue set 1)

The economic argument for anti-dumping is that firms with market power, or attempting to secure market power, can use pricing strategies to acquire market dominance. As in any non-competitive situation, this will have damaging consequences for efficiency and welfare. The best way to deal with this is through removing or controlling the market power, but anti-monopoly or regulatory approaches are not normally regarded as feasible at the international level, so AD is suggested as a substitute. There is also the argument (which would also apply to government subsidies) that non-competitive pricing strategies create unpredictable and therefore unfair environments for normal firms. The simple retort, that low prices are good, whether for other firms using the output or consumers, so we should not worry about why they are low, is not sufficient if countries want to keep a competitive business environment with clear and stable incentives for investment.

But it remains true that if anti-competitive distortions do not exist, low prices are good. One problem with TDI as currently used is that they do not depend on identifying distortions. AD deals with a symptom, a price that appears to be lower than conventional pricing or cost calculations would suggest; countervailing duties, which do depend on the identification of a subsidy, are rarely used.[ii] AD investigations do not look at the nature of the market, as competition investigations do. In some cases, where a firm has a large presence in the Community, competition law has been used on foreign firms. One way in which globalisation may be influencing what is possible and desirable is to increase the potential for that solution. There remain, however, cases where there may be anti-competitive behaviour that takes place entirely outside the community, but produces effects on exports to it (the fact that some countries' competition legislation excludes anti-competitive behaviour directed at exports aggravates the problem).

But there is no reason to believe that an instrument that looks at only one symptom of market power identifies either all or only uncompetitive practices. The fact that TDI rose in the 1980s when tariffs were coming down (so protected home markets were less protected) and government intervention was declining, does not suggest an easy relationship between the conventionally identified elements of 'unfairness' and TDI. The dependence of AD, in particular, on companies within the Community agreeing on a problem and in some cases then on companies in the exporting countries

reaching an undertaking on prices creates obvious opportunities for encouraging anti-competitive collusion, so AD may be damaging, not merely ineffective.

The problem with the various methods for comparing prices and costs is not just that they may depend on inadequate data or an arbitrary choice of methods, but that they do not take account of the range of legitimate pricing strategies, including evidence on price leaders; on pricing to market, rather than on the basis of own costs; or on the different customs in different industries for short or long term pricing, etc. They also do not look at characteristics of the market (in either the exporting or the importing country) that could indicate market power or a predatory pricing policy. It would be possible, as has been suggested,[iii] to have, in addition to the WTO-required AD analysis, an investigation to look for anti-competitive behaviour, in the same way as the Community investigations currently have to show injury, before calculating and imposing an AD duty which would be a 'least' duty on the basis of the three calculations.

TDI, multinationals, and outsourcing (Issue set 2, excluding 6th and 8th bullets)

To exclude related firms from the group whose interests are to be represented (the group for which the minimum 25% of the industry/50% of those expressing views must be applied) assumes[iv] that they have different objectives or company strategies from other firms. There are problems with this approach. As such firms become responsible for an increasing share of trade, unrelated firms are an increasingly unrepresentative set. It is not clear why related firms' interests must be different or that the differences will be relevant to the finding of a problem, or why it is assumed that the behaviour and potential for collusion of non-related firms need not be examined. This is a separate question from that of using intra-firm prices.

It is not clear what an 'EU firm' is. The Community interest (see below) could be in activities in the EU, so the links of a foreign-owned firm with production in the EU would certainly be of interest, but this might also mean an interest in related stages of production in other countries. It would not be possible simply to include the interests of overseas production by an EU firm without calling into question whether the interests of workers for an EU branch of a foreign firm should be included, and how to weight these. More fundamentally, the interest of the Community is in the income of its residents and/or its citizens, and only in the activities of firms insofar as they contribute to this through efficient production and the income that remains in or returns to the country. These reasons also make it odd to exclude the views of firms with foreign associates.

If EU firms, however defined, do choose to operate in another country, then it is only if the application of the rules in an AD investigation produces a perverse result, either by wrongly finding dumping or by creating uncertainty, that it will discourage such investment. If the rules are badly applied, and discourage any investment in an efficient producer, this will damage welfare in the EU through loss of potential efficient imports. It may also, at the limit, divert investment from other countries to the EU, if the EU applies the rules more badly than other countries, but as this investment will be in a second-best location, it will not compensate for the loss of welfare from investing in the original country.

In competition policy, it is the nature and activities of a company that may be a problem for efficiency or welfare. To translate this into an investigation of all the exporters from a country is valid only if the dumping is assumed to stem from some national action (for example government action to close the domestic market to provide a platform for export). If there is such a strategy (leaving to one side the fact

that much of recent trade analysis suggests that such protection is not likely to produce an efficient industry able to provide a sustained threat to any other country), then, as in the case of subsidies, it would be more consistent to identify the strategy, and agree instruments to change it.

Different interests and different Community objectives (Issue set 2, 8th bullet, and set 3, 1st and 2nd bullets)

The question of identifying and balancing different interests should not be different from any other Community policy choice (which doesn't mean that it is easy, of course). There are at least three ways of defining interests: 1) as the AD and countervailing Articles do (and as the summary of issues for this seminar does), by the various commercial interests: producers, users, and consumers; 2) by the different country interpretations of interests, as is implicitly done in the requirement that the Advisory Committee of member countries approve definitive duties; and 3) from economic principles, in terms of welfare maximisation (including if possible consideration of long-term results of market structure).

The first, as interpreted in the AD and subsidies procedures, gives special status to producers, because their views must be recorded, while the consultation of consumers depends on consumer groups' taking the initiative, although it also gives 'special consideration' to restoring competition, and thus to the original objectives of anti-dumping and anti-subsidy action. This approach embodies a view that existing production and existing jobs have a higher value than the potential production and employment that could follow, possibly in a completely different industry, from an adjustment to a more efficient distribution of production (effectively weighted at 0, with no formal procedure for assessing alternative futures). There is also the problem that the exclusion of related firms from the initial assessment reduces the weight given to producers in the EU with overseas interests. A consistent commercial interest approach should include these as well.[v] Including users of intermediate products and consumers goes part of the way to looking at economic welfare, but the focus on existing producers and their employees can only measure very short-term interests. The existence of discretion, at the level of the Advisory Committee, leads to a risk that lobbying will override the stated criteria.

The economic argument rejects the idea that any Community interest is a simple algebraic sum of positive and negative effects on interest groups. It would not give any special weight to producers or those currently employed by them, except as inputs to national economic welfare, measured principally by total income, and thus consumer interest, but it would try to give real weight to the arguments about the risks of anti-competitive strategies, whether dumping or subsidies. This method would therefore look at the net effects on existing and possible replacement production, including the potential contributions of both more efficient production within the EU and production outside the EU, and would analyse and attempt to quantify the medium or long term effects on competitiveness[vi]. This means looking at the interests of future consumers as well as present.

A problem with both the first and the third approaches is that they assume that there is agreement in the EU on the criteria for a decision. The apparently consistent support or opposition of some countries for AD measures in the Advisory Committee[vii] (and the existence of reform proposals from some) suggests lack of agreement on the principles of Community TDI. Some of the differences may reflect interest groups, if producers of a particular good are in some countries, and users or consumers in others.[viii] But the groupings are too consistent for that to be the only explanation.[ix] It may be partly disagreement about the type of approach to

Community interest (total welfare or interest group), but is also about the types of effect which are considered good or bad, for example preferences for flexibility or stability of production, prices, or employment. There may be more or less concern for predictable prices. These differences also have to be resolved in other EU policies, but the discretion allowed in TDI brings to the fore the role of national preferences in each decision.

Any of these views of interests could, and arguably should, take account of economic interests interpreted more broadly, for example to include the likely responses of the exporters or countries against whom action is taken, or even the possibility that policy action in this area may affect other international policy interactions.[x] A national welfare interest approach could accommodate this, but the current listing of interest groups to be consulted does not explicitly include others involved in international regulation or negotiations, or those at risk of other countries' TDI. The role of the Advisory Committee gives the possibility of taking these into account, but the legal ruling that it needs to give reasons for overruling a Commission recommendation could limit its ability to introduce new interests and, as Stevenson (2005) notes, treating countries differently for reasons unrelated to the dumping could be considered discriminatory.

Development, environmental, and social interests (Issue set 3, 3rd, 4th, and 5th bullets)

If TDI were operating to remove obstacles to the efficiency of the economic system, as the rationale for action against subsidies and against anti-competitive action by industries would suggest, then it would be odd to ask if they could damage development.[xi] That the question can be asked adds support to the view that the current system of looking at prices, not at industrial structure, is penalising normal economic behaviour by firms, not anti-competitive actions or market power. The EU's interests in promoting development may provide an additional argument for reforming a system which is economically wrong and disruptive to a rule-based international trading system. Exempting developing countries from actions under the existing system (or reducing its effects on them through some form of differential treatment) would help development, provided the change applied to all developing countries. If it discriminated by only excluding some developing countries from the application of TDI, it would, like any discriminatory preference, be distorting and create the risk of long-term inefficiencies.

To apply unilaterally the EU's views on environmental or labour standards (even if it were possible to identify a Community consensus) to other countries would be a clear breach of the international system. If there is international consensus on any standard, whether environmental, labour or other, it should be embodied in an international convention or, if it is trade-related, in the WTO, with agreed enforcement mechanisms. As long as there is not international agreement, then the differences are part of the different conditions of production on which comparative advantage is based.

Improving the technical efficiency of TDI through internal action (Issue set 4)

The fundamental fault, that most trade defence actions are not designed to deal directly with the problem of unfair competition (so there is no way of guaranteeing that they are limited to goods 'unfairly' traded, even if there were agreement on what this meant), should probably be tackled before devoting major efforts to reforming how they are applied. The Stevenson (2005) paper has made some useful suggestions on improving their application, and increased transparency at all the

stages could make serious errors of judgment about likely effects or interests less likely. There are technical problems: for example, the measurement of injury, especially when there are other factors damaging the industry; the very limited time allowance for exchange rate changes; and zeroing. Here, examination by experts on pricing and markets might help. It would be possible, as suggested p. 3, to add evidence on market power to the AD investigation. Clearly a system that affects a small share of EU production and trade, but requires a third of DG Trade staff to administer, needs reform.

Improving TDI through international action (Issue set 2, 6th bullet)

As noted in the Issues paper, other countries also use TDI in ways that do not improve economic efficiency or international equity. It seems possible that some of the increase in the use of AD has been because of the existence of an international agreement, with well-publicised discussion of the rules. The number of countries with their own AD regimes increased in the 1990s, and helping countries to establish WTO-consistent regimes has been part of international technical assistance to trade. It is inevitable that once such a measure exists, countries will each press it to its limits. If this risk of overuse or abuse is increasing awareness of the potentially damaging effects of badly applied TDI, it may lead to more interest in the possible reforms. Even if it is just creating a fear of 'tit for tat' action, it may be reducing the use of AD as the risks of retaliation lead to an uneasy truce. This could increase the prospect of reform (an analogy has been drawn with the tariff wars of the 1930s; this could be extended to hope for a response similar to the formation of GATT). As long as the current system remains, however, there is a risk to European interests if actions which are tackling real anti-competitive behaviour might be countered by actions against normal business pricing choices.

There is a clear Community interest in a functioning international system that tries to reduce negative effects from one country's actions on another and that provides ways of countering the effects and, when necessary, negotiating changes in the rules. The regime on subsidies provides this. In contrast, the AD regime does not require identification of excessive protection or faults in the competition regime of the exporter's country. It could be argued that the EU has tried to negotiate lower tariffs and an international competition regime. These, however, were not presented as an alternative to AD. It remains the case that the AD regime provides for unilateral identification of a negative effect without evidence of an internationally agreed policy failure by the exporting country. That the EU has not achieved its aims by negotiation would not normally be considered a sufficient excuse for unilateral action.

Continuing to press for multilateral agreements that mitigate the conditions which produce anti-competitive behaviour is clearly one avenue, especially if it were made clear that these would eventually be a substitute for, not an addition to, the existing AD regime. Increasing the controls on government subsidies and lowering tariffs to increase the competitiveness in foreign (and EU) markets are the most immediate means.

Finding areas of agreement on international standards for anti-competitive regimes will be more long-term. Although there is agreement on anti-trust policy within the Community, countries still have different attitudes to and restrictions on some types of competitive behaviour, including elements central to AD determination, the conditions under which producers may sell below cost or their normal prices. Nevertheless, the difficult process of developing a Community competition regime gives the advantage of experience in trying to extend this to other countries. Agreement could start with restricting the practice of exempting anti-competitive

behaviour which only affects exports from normal controls. If this cannot be done multilaterally in the short run, it could be done either as part of regional trade agreements or through separate competition agreements, on the precedent of bilateral investment treaties. Regions or pairs of countries could agree to recognise that their competition regimes provided sufficient control such that additional action through AD was no longer necessary, and agree not to use it. It is surprising that, except for the EU itself, the only regional agreement that has renounced AD is that between Australia and New Zealand.

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[i] The suggestion in Stevenson 2005, annex 1 p. 3, that the objective is *either* [emphasis added] to remedy market distortions…..or to address the serious deterioration….' is therefore seriously misleading. This report has useful suggestions for some practical improvements, but is much more conservative in identifying problems than most external studies of the Community's TDI.

[ii] As discussed in Stevenson (2005).

[iii] For example, Wooton, Zanardi, 2002

[iv] There is a test of whether 'there are grounds for believing or suspecting that the effect…is such as to cause the producer concerned to behave differently from non-related producers' only for distantly related producers. Direct subsidiaries or owners are assumed to behave differently.

[v] Including these is not sufficient to ensure that a solution that improves competitiveness because of the possibility that firms use TDI to segment markets. 'The observed sectoral pattern of antidumping reflects the increasing privatization of trade policy by firms that enjoy enough initial oligopolistic power to fully use the pro-collusive bias embedded in antidumping regulations'. (Messerlin p. 35 in Bhattasali et al 2004)

[vi] Although TDI are normally considered in the context of microeconomics, with attention to their effects on specific products, there is some evidence that extensive use of AD can have measurable macroeconomic effects, lowering total imports, and acting to damage economic welfare, like any interest in protection (Vandenbussche, Zanardi, 2006).

[vii] Analysed by Evenett, Vermulst, 2004.

[viii] Research in the US has identified effects from the relative strength of lobby groups (Blonigen and Prusa in Choi Harrigan, 2003)

[ix] The UK, for example, opposed AD when it was first included in GATT (Blonigen and Prusa in Choi, Harrigan, 2003), and Sweden was not a regular user before it joined the Community.

[x] Stevenson 2005 suggests the corollary of this, that if investigations find that market conditions in the exporting country are a problem, the EU could use this information to target in other negotiations.

[xi] Even those who would argue that some current rules on subsidies restrict developmentally desirable interventions would argue for changing the rules on subsidies, not on the ability of countries to take countervailing action against them.