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Unlocking the Potential of Global Value Chains through Reform of Rules of Origin

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Overview

1. Global value chains today
2. RTAs are here to stay
3. Preferential RoO are a *double-edged sword*
4. Need for reform and modernization of preferential RoO and how they are managed
5. Some remarks concerning LDCs in the context of GVCs & RoO



Global Value Chains today

- ❖ **GVCs** => trade in intermediate goods and services in fragmented and internationally dispersed production processes
- ❖ About **60% of global trade** consists in trade in intermediate goods and services.
- ❖ For example: The share of value added in Eurozone exports stood at **21% of the total exports** in 2011.
- ❖ **Similar trend** in all major economies
- ❖ GVCs are typically coordinated by **TNCs** – about **80%** of global trade

GVCs are on the rise; **but ...**

❖ **However**, participation in GVCs is heterogeneous and uneven, across and within countries.

❖ **Low-Income Developing Countries (LIDCs) are under-represented** in GVCs, even though their integration has risen in the past two decades – **from 6% to about 11%** of the world total (OECD & WBG 2015).

GVCs are on the rise; **but ...**

- ❖ **Sub-Saharan African countries**, for example, still find themselves **at the start** of their integration process into GVCs.
- ❖ The depth of their integration has **barely increased** since the mid 1990s.
- ❖ Neither the **diversity** nor the **quality** of their exports have been improving.
- ❖ Mainly **commodity exports** (Céline Allard et al. 2016)

GVCs are on the rise; **but ...**

- ❖ GVCs can lead developing countries to **building productive capacity** where local firms have a significant share in value added.
- ❖ **But** technology dissemination, skill building and upgrading are not automatic! They require significant investment (OEC, WTO, UNCTAD 2013).
- ❖ Also, more exports **do not necessarily mean value-added** exports



GVCs are on the rise; but... (**some conclusions**)

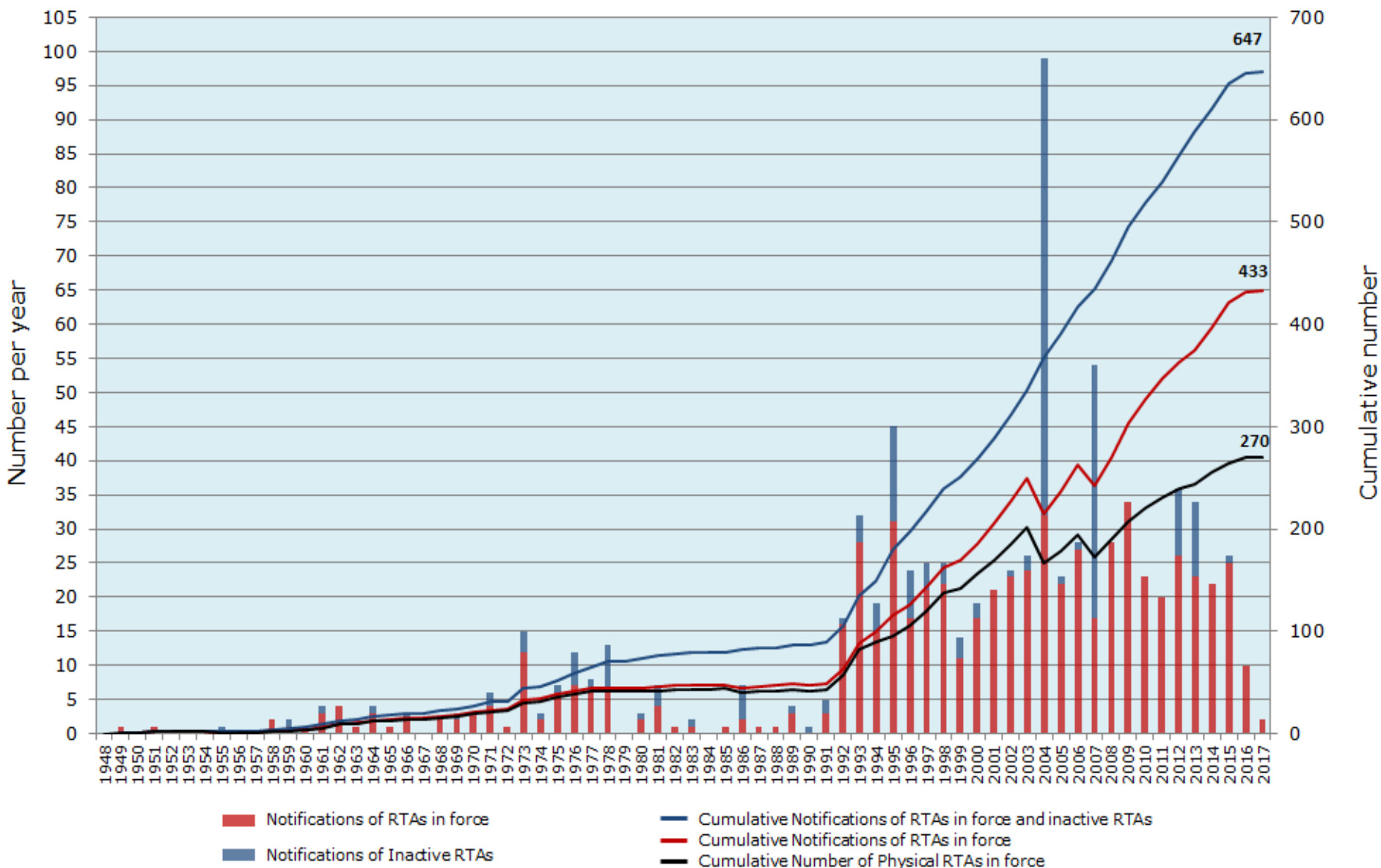
❖ ... Therefore, the crucial issue particularly for developing countries is to devise means of **deepening their production capacities** and get a bigger share of **value added**. E.g. thru:

- ❖ skilling the labour force
- ❖ structural transformation in industry
- ❖ increasing production in different service sectors
- ❖ Investing in energy production and strategic infrastructure
- ❖ Strategically investing in agriculture

RTAs – an overview

- ❖ GVCs operate within **multilateral, plurilateral, regional** and **bilateral** trade regimes.
- ❖ In the past two decades, Regional Trade Agreements (of two or more parties) have **proliferated**.
- ❖ And that's because they offer some **benefits** (*economic, political, cultural, etc.*) - *cf., the graph below*

Evolution of Regional Trade Agreements in the world, 1948-2017



Note: Notifications of RTAs: goods, services & accessions to an RTA are counted separately. Physical RTAs: goods, services & accessions to an RTA are counted together. The cumulative lines show the number of notifications/physical RTAs that were in force for a given year.
 Source: WTO Secretariat.



RTAs – an overview

❖ “Economic benefits” are always part of the core reasons for the formation of RTAs – Cf:

❖ **GATT XXIV:4** – “... closer integration... to **facilitate trade** between constituent territories....”

❖ The **Enabling Clause** - the decision on *Differential and More Favourable Treatment, Reciprocity and Fuller Participation of Developing Countries* of 28th November 1979 (L/4903)

❖ RTAs which are formed for a good cause, and which are the main legal basis for trade preferences (*except GSP regimes, which are unilateral concessions*) can cause economic harm to some countries due to **Rules of Origin**

Preferential RoO are a double-edged sword

❖ In the first place, pref. RoO are mainly used to prevent **trade deflection** (with its general negative economic consequences) and also ensure that the benefits of a preferential arrangement go to the rightful beneficiaries.

❖ However, they can in effect act as trade barriers by imposing exorbitant (*unintended/intended*) costs on producers and exporters.

Preferential RoO are a double-edged sword

- ❖ This is mainly due “**how stringent /restrictive, or not**” a RoO is with regard to an existing value chain in which it is expected to operate (which Inama 2017 calls the “**substance**” – in a different context, though).
- ❖ In an FTA, for instance, if the parties agree on “the substance”, it is easier to agree on the “**form**” – i.e., the various methodologies such as *CTH*, *specific processing*, etc.

Preferential RoO are a double-edged sword

- ❖ Very restrictive RoO can lead to economically **sub-optimal functioning of GVCs** by deterring the use of cheaper parts and materials from third countries.
- ❖ Moreover, strict and diverse RoO affect the ability especially of LDCs to fully benefit from intended enhance market access through FTAs or unilateral trade regimes (GSP/GSP+)

The road to reform and modernization of preferential RoO

- ❖ Need for implementation the Nairobi WTO **Decision on preferential RoO for LDCs**
- ❖ Minding the principle that these RoO should be **transparent** and **simple**, and contribute to **facilitating market access**.
- ❖ It calls for, for instance:
 - ❖ allowing use of non-orig.materials up to 75% of final value
 - ❖ expansion of cumulation
 - ❖ implementation flexibilities and transparency

- ❖ Weakness: Most of its provisions give much leeway concerning implementation
- ❖ Moreover, some of its provisions are of *best-endeavor* nature – the likes of “to the extent possible”, “where appropriate”, etc.

The road to reform and modernization of preferential RoO

- ❖ In the context of GVCs, there are also understandable calls to include the **service component** in rules of origin.
- ❖ Advanced **IT solutions** (e.g. thru better origin databases) have potential to solve some implementation challenges.
- ❖ **Self-certification** as opposed to certification by authorized bodies needs to be encouraged.



The road to reform and modernization of preferential RoO

- ❖ Ultimately, reform is needed with respect to the **pref. RoO themselves** and **how they are implemented**.
- ❖ **Harmonization** of rules and methods as opposed to fragmentation is desirable.
- ❖ **WCO** and **WTO** have an important role to play.
- ❖ The same to member countries, private sector, academia and other stakeholders



Some remarks concerning LDCs in the context of GVCs & RoO

- ❖ Expand production capacities, utilize national and regional value chains and gainfully integrate into GVCs.
- ❖ Address seriously supply chain issues and press for the relevant RoO reforms.



Thank you for your attention!

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