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*Policy Brief*

# *WHY TRADE FACILITATION MATTERS NOW MORE THAN EVER*

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On February 22, 2017, the World Trade Organization's (WTO) Trade Facilitation Agreement (TFA) entered into force. The TFA was concluded at the WTO Bali Ministerial Conference in 2013. Since then, countries have been working on implementing the agreement in their domestic markets to reach the two-thirds requirement for implementation.[1] As of March 2017, 113 members (or 69 percent of WTO members) have ratified the agreement—including 19 Latin American and Caribbean (LAC) countries—and another 93 countries have notified the WTO of their timeline for each TFA provision, giving a comprehensive picture of the state of the agreement.

This implementation of the TFA is a positive reminder that countries around the globe are still committed to improving the international trading system and promoting free trade. It also demonstrates the ability of countries to agree on a single set of standards for all countries, developed and developing alike. Unlike past agreements, the TFA does not water down its requirements to accommodate less developed countries. Instead, it allows these countries to implement the provisions on their own timeline and gives them access to technical assistance and capacity building resources to ensure full compliance with the TFA's standards. Finally, the TFA agreement provides a critical update to the rules that govern the transit of goods. International trade has evolved significantly since the WTO wrote its rules on customs, shipments, and technical barriers to trade. The TFA effectively catches up to the new realities of trade where faster, cheaper, and more efficient shipping and processing is required.

## International Trade: A Changing Landscape

Over the past 20 years, the international community has made significant progress in dismantling barriers to trade. Applied tariffs were reduced (or eliminated where possible), quotas were removed, and free trade agreements (FTAs) proliferated. This led to shifting patterns of global trade and a new regulatory architecture. Between 2000 and 2008, world exports grew more than 10 percent a year on average. At the same time, developing countries started to engage more in global commerce, and trade among developing countries (i.e., South-South) and between developing and developed countries (i.e., North-South) steadily increased. In 1990, South-South trade accounted for just 5 percent of global trade; today it accounts for roughly 20 percent.

During this period, countries negotiated bilateral and plurilateral FTAs, creating a complex network of agreements. The FTAs brought down barriers to trade by streamlining procedures and expanded trade by opening new markets and allowing goods and services to move efficiently across borders. However, the onset of the global financial crisis represented a major setback for the global trading system. Between 2008 and 2009, international trade flows dropped precipitously. Although trade recovered in the immediate post-crisis years (early 2009 to mid-2011), it has remained stagnant ever since and, most recently, has contracted. Anemic demand from developed countries, weak growth in developing countries' imports, and lower commodity prices resulted in feeble growth in world trade. Additionally, the barriers to trade have changed. With relatively low tariffs levels and so many FTAs, the real impediments to trade are non-tariff and technical barriers. This means that countries need to find new ways to stimulate trade and economic growth. One of the most pragmatic and effective ways to do this is through the implementation of trade facilitation initiatives.

[1] The TFA stipulates that 110 of the 164 WTO members must ratify the agreement before the full TFA can be implemented.

## Why Trade Facilitation? Why Now?

The result of the Brexit referendum in June 2016, the decision by the United States not to ratify the Trans-Pacific Partnership, and recent calls to renegotiate or outright dismantle the North American Free Trade Area have halted the trend toward larger and larger preferential trade agreements. It is difficult to predict how the global trade architecture will evolve in the next few years. We could witness a resurgence of mega-agreements; a new wave of regionalism lead by China; a further proliferation of bilateral agreements worldwide; or a growing number of trade frictions that could damage the international trade system enshrined in the WTO. In this context, part of the appeal of trade facilitation is that it does not require formal negotiations—unlike free trade agreements—and is therefore more politically feasible in the current climate. Trade facilitation provisions directly target the barriers impeding trade, such as lack of transparency, duplication of documentation requirements, and the absence of automatic data submission procedures. In that sense, trade facilitation can act as a tool or "technology" at the multinational, regional, and national levels to (1) improve the efficiency of the existing regulatory trade architecture; (2) address new structural changes in trade; (3) complement investments in commercial infrastructure; (4) absorb new disruptive technologies in trade; and (5) maintain the momentum of trade liberalization.

## Improving the Efficiency of the Existing Regulatory Trade Architecture

### *Multilateral initiatives*

Despite the complex network of FTAs and the fact that international trade is increasingly organized within global value chains, there has been little effort to coordinate the global regulatory architecture. The WTO's TFA is the first multilateral agreement to do so, and it was long overdue. The TFA will dramatically improve the regulatory architecture through the harmonization and standardization of global best practices that govern the movement, release, and clearance of goods. This will create more transparency and predictability at the border, which will help producers tap into global value chains and participate more in trade. The payoffs from these reforms are significant. The WTO estimates that the TFA can reduce total trade costs by more than 14 percent for low-income countries and more than 13 percent for upper middle-income countries. Latin American countries could see trade costs reduced by between 12 percent and 23 percent. The TFA would also reduce the time it takes to import by over a day and the time it takes to export by almost two days.

The international community knows the potential payoffs and is helping move the trade facilitation agenda forward. For example, the World Customs Organization is assisting WTO member countries in implementing the TFA by providing guidelines for governments that include key steps required for accession and compliance. It is also providing technical support and capacity building and sharing national best practices to help expedite implementation. Similarly, the Global Alliance for Trade Facilitation[2] is working to engage the private sector and promote business awareness and engagement on trade facilitation. The alliance has partnered with companies and local trade associations to discuss and implement reforms. The group also provides technical and financial assistance to support capacity-building efforts.

[2] GATF is public-private partnership organized by the Word Economic Forum, the International Chamber of Commerce, the Center for International Private Enterprises, with the governments of Canada, Germany, the United Kingdom, and the United States.

## *Regional initiatives*

Throughout Latin America, trade facilitation has become a priority and regional associations are helping countries implement programs designed to improve the cross-border movement of goods. This is particularly important for the LAC region, where burdensome procedures, high costs, and delays are some of the biggest obstacles to trade. Currently, it takes an average 3.5 days for goods to clear customs in LAC, compared to just three days in East Asia and the Pacific, and less than a day in OECD countries.[3]

To address these issues, initiatives like the Pacific Alliance are focusing on implementing trade facilitation measures to better connect with the rest of the world. The Pacific Alliance agreement contains rules to increase transparency and improve procedures for the transit of goods. The agreement also contains an innovative provision that commits countries to create an interoperable electronic single window (RED VUCE, as is known by its Spanish acronym). Firms will be able to use an electronic, single entry point to carry out all the administrative procedures required by the various government offices to obtain authorization to import, export, or trans-ship commercial merchandise. This eliminates the need to deliver physical documentation to multiple offices for approval, thereby improving the end-to-end efficiency and security of supply chains.

In addition, members have agreed to make all necessary information available online and have simplified customs procedures to expedite the release of goods, including the mutual recognition of national authorized economic operator (AEO) programs.

These programs have already contributed significantly to reducing costs and transit times. In a survey conducted by the Inter-American Development Bank (IDB) on AEO certified companies in LAC, 91 percent reported that their supply chain security had improved significantly, while 72 percent said their relations with customs agencies had improved, and 65 percent reported that the physical inspection of their cargo and dispatch times had declined.[4] In Peru alone, the single window program has reduced customs clearance times by 15 percent compared to 2012, generating $9 million in savings for importers and exporters.

In Central America, the General Secretariat of Central American Economic Integration is working on integrating trade and transportation networks across Belize, Costa Rica, the Dominican Republic, El Salvador, Guatemala, Honduras, Nicaragua, and Panama. In 2015, the executive committee approved the Trade Facilitation Strategy and Regional Competitiveness plan, focused on coordinated border management. Part of this includes a Central American digital trade platform and border integration measures such as early transmission of documents for cargo, only carrying out immigration controls in the country of departure, an electronic system for documentation, and the implementation of new technology to expedite border crossings.

In South America, the Union of South American Nations Council of Infrastructure and Planning is modernizing and optimizing border crossings and border management as a way to promote development in the region. Their latest strategic action plan (2012-2022) prioritizes facilitation and

[3] http://www.doingbusiness.org/data/exploretopics/trading-across-borders
[4] The IDB conducted a survey in 2013 and 2014. The surveys have not been published online but the data has been presented in multiple fora, including this blog and this presentation.

optimization of border crossings. Similarly, the Caribbean community has incorporated trade facilitation measures into their latest strategic plan.

### *National initiatives*

Numerous countries in the region are modernizing customs procedures, implement single window programs, and improve border management. These initiatives will help those countries that have not already implemented the TFA to incorporate the alliance's key provisions.

LAC is progressing well in terms of implementing the WTO TFA provisions. Twenty countries have ratified the agreement,[5] while another eight have notified the WTO of the provisions they will implement, what—if any—assistance they need, and their timeline for implementation.[6]

### *Public-private partnerships*

Many government-led regional initiatives are working with the private sector to implement their trade facilitation agenda. For example, the Pacific Alliance created a business council to promote the RED VUCE and harmonize technical standards and mutual recognition, with the goal of making the alliance a homogeneous regulatory zone. The Americas Business Dialogue is another public-private partnership helping the region implement the WTO TFA. The group has been helping countries implement provisions such as advance rulings, duties and charges, release and clearance of goods, and formalities related to import, export and transit, as well as policies for low value shipments applicable regardless of country of origin. Similarly, the Asia-Pacific Economic Cooperation Business Advisory Council is strengthening the connectivity of supply chains and improving business mobility in Asia and the Pacific. One example is a business travel card, which allows pre-cleared business travelers to enter participating member economies, thus eliminating the need for individual visas.

## Addressing New Structural Changes in Trade

### *Growth of global value chains in international trade*

One of the biggest changes to the international trading system is the growth of global value chains. Gone are the days when a good is wholly produced by one firm in one country. Instead, companies specialize in the production of one piece or process of a good that is traded across multiple borders and assembled in stages. Nowadays, intermediate products comprise 60 percent of global trade, 30 percent of which is between affiliates of the same multinational corporations.[7] A well-known example is North America automobiles, which cross the United States border eight times during production, integrating materials from Mexico and Canada along the way.

The prominence of global value chains in global trade means that transportation logistics are essential to a country's competitiveness. High costs of border crossings can increase the cost of final goods by 15 percent, and every additional day at the border can reduce trade by 1 percent. Therefore, improved border crossings depend on trade facilitation more now more than ever.

[5] They are Belize, Brazil, Chile, Dominica, Dominican Republic, El Salvador, Guyana, Grenada, Honduras, Jamaica, Mexico, Nicaragua, Panama, Paraguay, Peru, Saint Kitts & Nevis, Saint Lucia, Saint Vincent & the Grenadines, Trinidad & Tobago, and Uruguay.

[6] This includes Antigua & Barbuda, Argentina, Barbados, Colombia, Costa Rica, Ecuador, Guatemala, and Suriname.

[7] http://voxeu.org/article/trade-facilitation-matters

### *Increase in South-South trade*

Another key structural change has been the increase in South-South trade. Over the past 15 years, trade between emerging and developing countries as a share of total trade has doubled from 20 to 40 percent, and South-South trade has increased from 5 percent to nearly 20 percent of world trade. However, inefficient border management has impeded their participation in global value chains. For example, in Latin America, there are on average 15 to 30 agencies involved in border crossings transactions. Roughly 75 percent of delays at the border are due to inefficient processes, whereas the remaining 25 percent are due to inadequate physical infrastructure.

Trade facilitation can address these inefficiencies and help countries improve transit times and reduce costs. In fact, research by the OECD shows that improving the availability of trade-related information, simplifying and harmonizing documents, streamlining procedures, and using automated processes can reduce trade costs in low-income countries by nearly 15 percent.[8]

### *Increase in electronic commerce*

The final structural change affecting global trade is the increase in electronic commerce. E-commerce has been growing steadily, doubling worldwide between 2013 and 2017 alone, from $1.1 billion to $2.4 billion.[9] In Latin America, e-commerce is forecasted to increase by more than 30 percent during that same period. This presents new trade facilitation challenges. More trade conducted online means an increasing number of small shipments and more products passing through customs individually rather than as parts of larger cargo shipments from single large companies.

This new landscape calls for more flexibility and simplified procedures for low-value products, an area in which trade facilitation measures can have a substantial impact. For example, countries can expedite customs treatment for small or express shipments and remove limitations on express treatment for goods beyond a particular value or weight. Countries would also benefit from streamlining documentation to ensure the timely release of goods. These measures would allow small shipments to transit through borders faster, something that is increasingly important in the "just-in-time" world of electronic commerce.

## Complementing Investments in Commercial Infrastructure

Historically, Latin American countries have focused investment on upgrading their physical—or "hard"—infrastructure, including the roads, railways, waterways and ports that physically make up the transportation networks that connect countries throughout the region. More recently, countries have been realizing the importance of investing in the "soft" infrastructure of trade: the policies and regulations that govern the movement of goods within countries and across borders. Soft infrastructure consists mainly of trade facilitation measures that harmonize and standardize trade procedures such as customs and border management. While hard infrastructure physically connects the region, soft infrastructure deepens integration by facilitating cross-border trade.

[8] Evdokia Moïsé, Silvia Sorescu OECD Trade Facilitation Indicators *The Potential Impact of Trade Facilitation on Developing Countries' Trade 04 Mar 2013*

[9] Kati Suominen, "Fueling the Online Trade Revolution: A News Customs Security Framework to Secure and Facilitate Small Business E-Commerce," April 2015, Report of the CSIS Europe Program. https://csis-prod.s3.amazonaws.com/s3fs-public/legacy_files/files/publication/150421_Suominen_FuelingOnlineTradeRev_Web.pdf

Research has shown that to unlock the full potential of infrastructure investment and policy reform, governments must simultaneously invest in hard and soft infrastructure. A 2011 study by the IDB[10] found that when governments invest equally in hardware and software, intra-regional exports nearly double. Sixty percent of those payoffs are generated by investments in hard infrastructure, while 40 percent can be attributed to investments in soft infrastructure. This implies not only that investments in infrastructure are profitable, but also that the returns on investment are distributed evenly between the software and hardware of trade.

Countries should therefore implement trade facilitation measures that streamline processes, harmonize rules, and strengthen institutions. These measures are relatively low-cost compared to investments in physical infrastructure and have high upside benefits in the form of lower transaction costs. OECD research shows that streamlining trade procedures can reduce transaction costs by 5 percent. Similarly, a new study by the IDB[11] shows that exports in Uruguay could increase by 6 percent if cargo was able to clear customs within one day.

## Absorbing New Disruptive Technologies in Trade

Technology has played a big role in transforming the nature of global trade. Advances in the internet and computing, robotics, and 3-D printing have had an impact on what and how we trade. The Internet of Things—the networked connection of physical objects—for example, is changing transportation and supply chain logistics by capturing data from and providing information to various supply chain entities. cloud computing allows for nearly unlimited computing power and storage, while technologies like geospatial information systems and automatic identification and data capture enable precise monitoring of goods as they move through the logistics chain, which makes supply chains significantly more connected, secure, and efficient.

These technologies can simplify trade procedures at every level of the supply chain, and trade facilitation measures can help boost their impact by absorbing and disseminating new technologies with the potential to positively affect trade. For example, digital platforms for business allow actors in the supply chain to interact through single virtual platforms. These platforms connect individual sellers with millions of potential buyers, provide better access to information, and introduce greater flexibility into the whole supply chain. ConnectAmericas[12] is an example of a business-networking platform that helps small and medium-sized enterprises in Latin America grow their businesses internationally by connecting clients, investors, and suppliers.

Remote monitoring is another disruptive technology that enables trade and complements trade facilitation efforts. Technologies such as radio-frequency identification—electronic security seals on shipping containers—allow actors to monitor physical goods in transit, can prevent spoilage of products (e.g., agricultural or medicinal products with short shelf lives), and make the supply chain more secure by, for example, sending alerts if cargo is tampered with. Trade facilitation measures such as the harmonization of standards on data collection and storage, cooperation between customs agencies for exchange of information, or programs related to the freedom of transit (e.g., interoperable single windows) could use these technologies to improve trade logistics.

[10] https://publications.iadb.org/bitstream/handle/11319/1376/Investing%20in%20Integration%20%20%20.pdf?sequence= 1
[11] http://www.iadb.org/en/topics/trade/out-of-the-border-labyrinth,20206.html
[12] https://connectamericas.com/home

A final category of trade-enabling technology that can improve the distribution of goods by making transportation more efficient. This is done, for example, using geographic information system, real-time operating systems, and cloud computing. These technologies can automate route planning and generate delivery plans specifically tailored and updated to meet the constraints imposed by physical infrastructure, planning, and order requirements. All this is can be achieved automatically and in real time, introducing greater control and flexibility into transportation and logistics and dramatically cutting travel times and reducing costs.

## Maintaining the Momentum of Trade Liberalization

A big advantage to implementing a trade facilitation agenda is that it contributes to trade liberalization without requiring formal trade negotiations. It also allows countries to participate in multiple initiatives simultaneously without creating overlapping or contradictory rules, as often happens when countries are a party to multiple FTAs. Indeed, many Latin American countries are doing just that. For example, almost all of the 21 LAC countries that are part of the WTO's TFA are also involved in regional and national trade facilitation initiatives.

At the regional level, the Asia-Pacific Economic Cooperation—whose members include Chile, Mexico and Peru—launched the Trade Facilitation Action Plan to coordinate the groups' trade facilitation work and reduce transaction costs by 10 percent. The plan focused on domestic regulatory reforms, providing more secure trade, improving mobility for businesspersons, and increasing the use of electronic filling. Recent iterations of the plan focus on assisting countries to implement the WTO TFA. The cooperation's Committee on Trade and Investment also does a great deal of work on improving supply chain connectivity and regulatory coherence and cooperation.

In Latin America, the Pacific Alliance has prioritized trade facilitation. Member countries are required to make all necessary information available online, simplify customs procedures to expedite the release of goods (in particular for express delivery shipments), and automate procedures. Government organizations of member countries are working with the business community to promote closer cooperation between customs officials and the private sector. More recently, the Pacific Alliance and the Common Market of the South have been cooperating on trade and integration by developing an action plan to strengthen dialogue on issues like trade facilitation, including customs cooperation, simplification and digitization of origin certification, and greater mobility for people.

Important bilateral initiatives are also taking place in Latin America. In March 2016, Argentina and the U.S. signed a bilateral Trade and Investment Framework Agreement that includes cooperation on regulatory issues, technical capacity building, and the facilitation and expansion of bilateral trade. The previous year, Brazil and the U.S. signed a trade facilitation memorandum of intent that commits both countries to improving their economic and trade relations. The MOI enjoys strong support from the private sector, which is advocating for closer cooperation with the government to increase technical border management and reduce the cost of doing business.

These initiatives are significant because they show these countries are willing to engage important trade partners outside the region on contemporary trade topics. In the past, Argentina and Brazil had withdrawn from multilateral initiatives and extra-regional bilateral partnerships, focusing instead on intra-regional integration. The signing of bilateral partnership agreements with one of their most important trade partners demonstrates an understanding of the importance of cooperation on regulatory issues for reducing unnecessary costs and stimulating trade.

## The Impact of Trade Facilitation Measures in LAC

A significant amount of empirical work has attempted to estimate the gains from trade facilitation. While results vary, there is consensus that trade facilitation reduces trade costs and boost exports. The WTO estimates[13] that ratification of the TFA would boost global trade by up to $1 trillion and reduce total trade costs by 14 percent for low-income countries, 15 percent for lower middle-income countries, and 13 percent for upper-middle income countries. A 2015 study by the OECD[14] found that the implementation of the TFA could reduce worldwide trade costs by between 13 and 17 percent; global exports could increase by $33 to $100 billion per year and global GDP could get a boost of $67 billion once the TFA enters into force.

New research by the IDB[15] provides a microanalysis of the payoffs of trade facilitation. The study looks at various trade facilitation measures—border delays in Peru, risk management in Uruguay, single windows in Costa Rica, AEO programs in Mexico, and the regional transit of goods in El Salvador—and finds that they have a positive and significant impact on trade. One of the main mechanisms through which these measures affect trade is by increasing the number of shipments. This means that the application of trade facilitation allows companies to receive inputs (intermediate goods) when needed and respond faster to the demands of buyers, thereby introducing greater flexibility into their production and exports. This increases the participation of these companies in trade in general, and in global value chains in particular.

These are exciting times for international trade, as the composition and direction of trade flows is evolving and technological advances are improving the way we exchange goods. Yet in Latin America and around the world, regulatory misalignment and cumbersome administrative procedures remain barriers to trade and impose unnecessary costs. There is, therefore, no better time than now to enact new, targeted policies to facilitate trade. Indeed, governments seem to be catching on to this realization, as the subject has become more prominent in policy discussions, the design of government strategies, and the funding priorities of regional organizations. LAC still has a long way to go, but the region is making inroads by participating in multilateral initiatives, regional cooperation, and unilateral domestic reforms. Countries should build on this momentum and continue to focus their attention on trade facilitation initiatives that reduce trade costs and propel Latin American trade and integration forward.

[13] https://www.wto.org/english/res_e/publications_e/wtr15_e.htm
[14] http://www.oecd.org/tad/tradedev/WTO-TF-Implementation-Policy-Brief_EN_2015_06.pdf
[15] http://www.iadb.org/en/topics/trade/out-of-the-border-labyrinth,20206.html

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