THE DEVELOPMENT RELEVANCE OF TRADE PREFERENCES: 
AN ANALYSIS ON SWITZERLAND

Sangeeta Khorana*

ABSTRACT

Developing countries continue to place preferences as a centrepiece in their negotiating agenda. However, economists are increasingly questioning the feasibility of preferences, from a development perspective. This paper evaluates the efficiency of preferences as means to enhance market access for developing countries’ products and identifies the constraints to an effective utilisation of preferences by the beneficiaries’ countries and products in Switzerland. It suggests feasible changes to the design of preferences, from both a development objective and the perspective of the trading system, so that preferences can be used as a development instrument by Switzerland to help developing countries integrate into the multilateral trading system.

Keywords: Special and differential treatment, trade preferences, multilateral negotiations

JEL Classification: F13, F15, O19

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Department of Economics, School of Management and Business, University of Wales, Aberystwyth, SY23 3DD. United Kingdom.
1. Introduction

Developing countries have traditionally sought special and differential treatment (SDT) in the General Agreement on Tariffs and Trade (GATT) and the World Trade Organisation (WTO) to increase the development relevance of the trading system (Hudec, 1987; Jackson, 1997; Michaopoulos, 2000; Finger, 2001; Hoekman, 2005). Trade preferences within the generalised system of preferences (GSP) framework are seen as an essential element of the SDT to integrate developing countries and least developed countries (LDCs) into the world trading system (Brenton, 2003).

Despite the apparent popularity of preference schemes among beneficiary countries, an intense controversy has been going on among trade economists regarding the costs and benefits of allowing preferences within the SDT framework (Patterson 1965; Baldwin and Murray, 1977; Brown, 1987, 1989; MacPhee and Oguledo, 1991; Nilsson, 2002; Panagariya, 2002a, b; Rose, 2002; Özden and Reinhardt, 2002; Cline, 2004; Brenton and Ikezuki, 2005). Literature review on the utilisation of non-reciprocal tariff preferences by the beneficiary countries shows that preferences have not been able to generate substantial export flows from the beneficiary countries (OECD, 2004). Studies show that market access for agricultural products within the GSP framework has remained elusive (Panagariya, 2002a, b; Özden and Reinhardt, 2002; OECD, 2004). For instance, the analysis of the utilisation of the non-reciprocal schemes in the main preference allowing countries, i.e., European Union (EU) and the United States (U.S.) shows that in the EU these schemes have failed to generate significant impact on the growth of beneficiary countries’ exports (Panagariya, 1999, 2002b; UNCTAD, 2003; Gallezot, 2003; Brenton and Ikezuki, 2005). Similarly, preferences allowed to developing countries by the U.S. have also been ineffectively utilised (UNCTAD, 2003; Bouët, et al., 2005). Studies show that the overall gains in export volumes and earnings from GSP preferences allowed by the EU and the U.S. are highly concentrated in a few higher income developing countries (Sapir and Lundburg, 1984; Karsenty and Laird, 1986; MacPhee and Oguledo, 1991;
Brenton and Ikezuki, 2005; OECD, 2005). As a result the overall impact of non-reciprocal trade preferences on market access has been modest from a development perspective.

None of the existing studies, however, assesses the efficiency of preferences as market access instruments in Switzerland which is the eleventh largest importer of agricultural and food products (WTO, 2004b). Based on the methodology used in the existing studies on the EU and the U.S. (WTO, 2001; UNCTAD, 2003; Brenton and Ikezuki, 2005), this paper evaluates the efficiency of preferences in Switzerland with estimations of utilisation ratios, potential coverage and utility rates of preferences. It analyses the extent to which developing countries’ agricultural products gain preferential access into the Swiss markets under the existing GSP framework. The relevance of research is substantiated by the analysis of trade data for 1972-2002, which shows that despite an increase in agricultural imports of Switzerland, the share of developing countries has declined from 26 % to 13 %, while Switzerland’s imports from the EU have grown five-fold between 1992-2002 (Swiss Federal Customs, 2003).

The structure of the paper is as follows:
Section 2 gives the historical background and traces the evolution of the GSP scheme under the SDT framework.
Section 3 presents an overview on the preferential framework in Switzerland and highlights the main features of the existing GSP scheme.
Section 4 estimates the utilisation rate of preferences, its utility rate and the potential coverage of products under the GSP framework.
Section 5 identifies the main constraints to preference utilisation by developing countries.
Section 6 concludes and suggests feasible changes to the design of preferences, from both a development objective and the perspective of the trading system, so that preferences can be used as a development instrument in the multilateral trading system.
2. Evolution and the original motivation of the SDT

The concept of preferences traces its roots to the Havana Conference (November 1947) when “most of the less developed countries of the world demanded freedom to promote industrialisation by restricting trade” (Wilcox, 1949). Developing countries submitted more than 800 amendments in Havana reflecting their demands on commodity price controls, quantitative restrictions for the balance of payments and longer deadlines for commitments, among demands for other exceptions. As a result of these demands, Article XVIII of the GATT 1947 allowed developing economies to use domestic policy to develop particular sectors and to safeguard their balance of payments. At the same time it also allowed industrialised countries to continue special access for colonies or other associated countries (defined in the agreement). The GATT, therefore, institutionalised the notion of “special and differential treatment” with provisions on non-reciprocity in trade negotiations between developed and developing countries.

During 1960s, the prices of primary commodities fluctuated widely and the exports of developed industrialised countries grew faster than the other countries of the world with the result that the terms of trade of developing countries worsened with developed countries. This “corroded developing countries’ confidence in the system” and led developing countries to demand an organisation to address their trade and development needs. As a result, the United Nations Conference on Trade and development (UNCTAD) was created in 1964 that emphasised the need to formulate “measures to impart stability in international commodity markets at remunerative levels as vital to less developed countries”.

During the Kennedy Round, negotiations (1964-1967) the contracting parties adopted Part IV on trade and development; as a result of which Articles XXXVI to XXXVIII were incorporated in the GATT (Part IV, GATT 1965). The Articles institutionalised the notion that developing countries were entitled to “special and differential treatment” in the GATT system and also incorporated provisions on non reciprocity in trade negotiations between developed and developing countries with the objective to reduce trade barriers.
for products from developing countries. The Committee on Trade and Development was also established during this time with the mandate to review the application of the provisions on SDT, carry out consultations with all the contracting parties in its application, consider extensions and suggest modifications, if any, to further the objectives of trade and development.

By the time the second meeting of the UNCTAD was held in 1968 all countries had accepted the importance of preferences for developing countries. The Generalised System of Preferences scheme was adopted through Resolution 21 (II) in 1968 with the objective “to allow the generalized, non-reciprocal, non-discriminatory system of preferences in favour of the developing countries, including special measures in favour of the least advanced among the developing countries to increase their export earnings; promote their industrialization; and, accelerate their rates of economic growth.” This agreement marked the outset of preferences for developing countries not as a theoretical issue like in the early 1960s or as a set of the later contending proposals, but as a framework that would provide the guidelines under which developed countries could allow preferential market access for developing countries (Santos, 2005). The EEC was the first to formulate a preference scheme in July 1971, followed by Japan (August, 1971), Norway (October, 1971), Denmark, Finland, Ireland, New Zealand, Sweden and the United Kingdom (January, 1972)³, Switzerland (March 1973), Austria (April, 1972), Canada (January 1974) and the United States (1976).

Since tariff discrimination was a violation of the most-favoured nation obligation of the GATT the legal authority for preferential tariff schemes needed a GATT waiver. The contracting parties approved the waiver in 1971 and the GSP scheme was authorised for an initial period of ten years. The authority for preferences was further extended for an indefinite period, with a permanent waiver to the MFN clause through the “Enabling Clause” in 1979 by the GATT contracting parties under the “Differential and More Favourable Treatment, Reciprocity and Fuller Participation of Developing Countries” (Decision of November 28, 1979). There were, however, no legal binding obligations for
developed countries to implement the GSP scheme and it was left to the discretion of the preference allowing countries to define the scope of preferences (Michalpoulos, 2000).

The WTO Uruguay Round also incorporated the SDT provisions in the multilateral agreements. The existing SDT measures have been classified by the WTO into six groups: increasing trade opportunities for developing countries; safeguarding the interests of developing countries; providing flexibility in the application of WTO rules; postpone the application of rules and commitments undertaken; providing transitional time periods; as well as allowing technical and special assistance to developing countries and LDCs (WTO, 2004a). The Agreement on Agriculture (AoA) incorporates the following two main dimensions of the SDT: market access and rule related (WTO, 1995).

The Doha Declaration reaffirmed that the “provisions for special and differential treatment are an integral part of the WTO agreement” [Para 13] and called for a review of the SDT schedules (WTO, 2002a). By the end of 2005, a total of 12 national GSP schemes were notified to the UNCTAD. These schemes allow non-reciprocal preferences at reduced or zero tariff rates over the MFN tariff rates for selected agricultural and industrial products originating in developing countries. The countries that allow non-reciprocal preferences under the GSP framework are the following: Australia, Bulgaria, Canada, the European Community, Japan, New Zealand, Norway, Poland, the Russian Federation, Switzerland, Turkey and the United States.

3. An overview on the preferential framework in Switzerland

Agricultural imports gain entry into the Swiss markets on MFN terms and under a complex arrangement of preferential agreements, i.e., the GSP scheme, free trade agreements (FTAs) and bilateral agreements. These are the following:

(i) The framework of the European Free Trade Association (EFTA);
(ii) Bilateral trade agreements with the EU; and,
(iii) Non-reciprocal trade preferences allowed to developing countries and the LDCs under the GSP scheme.
As part of the EFTA, Switzerland has signed FTAs with the following countries\(^9\): Bulgaria (RS 0.632.312.141), Croatia (RS 0.632.312.911), Chile, the Faeroe Islands (RS 0.632.313.141), Israel (RS 0.632.314.491), Jordan (RS 0.632.314.671), Former Yugoslav Republic of Macedonia {FYROM}(RS 0.632.315.201.1), Morocco (RS 0.632.315.491), Mexico (RS 0.632.315.631.1), Lebanon, the Palestinian Authority (RS 0.632.316.251), Romania (RS 0.632.316.631), Singapore (RS 0.632.316.891.11), and Turkey (RS 0.632.317.631). This agreement covers processed agricultural products and fish as well as other marine products.\(^{10}\) All non-agricultural products are duty-free, except fish oils and fats, and chemical based preparations for animal feed (HS 3824.9091 with an MFN *ad valorem* equivalent tariff of 19%).

Switzerland is also a part of the Declarations of Cooperation with Albania, Algeria, the Gulf Cooperation Council (GCC), Mercosur\(^{11}\), Serbia and Montenegro, and Ukraine within the EFTA framework. Negotiations for free trade agreement (FTAs) are also underway with Tunisia, Egypt, the SACU (South Africa, Botswana, Lesotho, Namibia, and Swaziland) and Canada. In addition, the possibility of negotiating free-trade agreements with South Korea and Thailand is currently under debate.

In addition, Switzerland has signed bilateral agreements with the European Community.\(^{12}\) The bilateral agreement on agriculture covers both agricultural and industrial products. The agreement provides for complete liberalisation of bilateral trade through full tariff and export subsidy elimination, liberalisation of cheese sector by 2007 and the harmonisation of Swiss and EU legislations on liquor\(^{13}\) (OFAG, 2003). It also provides duty-free access for meat, dairy and cut flowers imported under the present TRQ regime (WTO, 2004b).

There are also preferential tariff quotas notified for import of feathers, soft drinks, and tobacco from Turkey; and for olive oil from Jordan (Swiss Federal Customs, 2002).\(^{14}\) The preferential (duty-free) quota on cane sugar from developing countries (opened in 1997 in addition to WTO commitments) has been increased from 5,000 tonnes per year to 7,000...
tonnes from 1 April 2001.\textsuperscript{15} In March 2004, preferential quotas of combined 5,000 tonnes were also allowed on certain oilseeds and oil products from least developed countries.\textsuperscript{16}

3.1 Main features of the existing Swiss GSP scheme

Under the existing GSP scheme, Switzerland allows non-reciprocal trade preferences to developing countries and the LDCs in the form of exemption from and/or, a lower duty on notified agricultural and industrial products\textsuperscript{17}; an exception is textiles and clothing on which 50\% tariff reduction is granted (UNCTAD, 1999; Swiss Regulation RS 632.911). The LDCs, however, enjoy a higher level of preferences on agricultural products and the applied MFN tariffs for the LDCs are 55 - 75 \% lower than applicable for developing countries.\textsuperscript{18} A zero tariff initiative for all LDCs is proposed by 2007.

Graduation from the GSP scheme:
The graduation of the beneficiary countries from the GSP scheme is based on an assessment of the existing preferences and the level of the development of the beneficiary countries (Article 3, RS 632.91). The criterion for graduation provides that if the beneficiary country is classified by the World Bank as a “high-income country”\textsuperscript{19} then the most advanced beneficiary country should be removed from the list of the GSP beneficiary countries. The revision is undertaken periodically - in 1977 the list of beneficiaries was revised for the first time and Spain, Portugal were graduated from the list of GSP beneficiaries; at the same time Romania, Bulgaria and China were added to the list of developing countries eligible for GSP. During 1997 – 2000 Cyprus, Hong Kong, China, Mexico, the Republic of Korea, and Singapore were graduated out of the GSP scheme. During 2002 – 2003 Croatia, the Former Yugoslavia Republic of Macedonia (FYROM), Jordan, Morocco, Malta (following its EU accession), and the West Bank of Gaza Strip (following the signing of bilateral trade agreements) were graduated out of the GSP scheme. In 2004, the beneficiary countries that acceded to the EU were graduated out of the scheme. More recently, Tunisia was graduated out of the preference beneficiary list in May 2005. The graduation mechanism also provides for a
review of the beneficiary countries included in the list of LDCs. During April 2001 – March 2004, Bosnia and Herzegovina and Albania were added to the LDCs’ beneficiaries list and were granted tariff preferences. Similarly in April 2004, Senegal was graduated into the LDC list of beneficiaries (WTO, 2004b).

**Preferential rules of origin:**

The rules of origin for products imported under the GSP scheme state that products must be wholly obtained in the beneficiary country and transported directly to Switzerland; and should be accompanied by the documentary evidence of its origin. The proof on the origin of products that these comply with the rules of preferential origin (Form A) must be endorsed by an approved authority in the country of origin, either in English or French. This has to be accompanied by an invoice declaration, signed by the exporter. Processed agricultural products that claim the GSP benefits should have the proof of origin in the beneficiary country with a minimum local content of 50 % of the value-added for agricultural products. Cumulation between groups of developing countries is, however, not permitted.

**3.2 The scope and depth of preferences allowed under the Swiss GSP scheme**

The average MFN tariff (in AVE terms) notified on agricultural commodities is 36.2 % whereas the average preferential tariff for developing countries is 34.2 % (WTO, 2004b). The LDCs, however, enjoy a much lower MFN average of 24.1 % on agricultural products (Table 1 refers).

**Table 1 : GSP and MFN tariffs notified on agricultural imports: 2002**

<table>
<thead>
<tr>
<th>Imports under the scheme</th>
<th>Average tariffs</th>
<th>% imports allowed free</th>
</tr>
</thead>
<tbody>
<tr>
<td>Generalised System of Preferences (GSP)</td>
<td>34.2 %</td>
<td>31.9</td>
</tr>
<tr>
<td>Least-developed countries (LDCs)</td>
<td>24.1 %</td>
<td>45.8</td>
</tr>
<tr>
<td>MFN</td>
<td>36.2 %</td>
<td>15.9</td>
</tr>
</tbody>
</table>

*Source: WTO, 2004b, pp. 99*
The analyses of the Common Customs Tariff (CCT) shows that a total of 1609 MFN tariff lines were notified on agricultural products. Table 2 presents the break up on MFN and preferential tariffs during 2002. It shows that developing countries enjoyed preferential market access on 492 tariff lines.

Table 2: Tariff lines liberalised under Switzerland’s GSP preferences: 2002

<table>
<thead>
<tr>
<th>Total lines utilised</th>
<th>Total lines</th>
<th>Share of total (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>MFN duty free</td>
<td>774</td>
<td>48%</td>
</tr>
<tr>
<td>Total GSP preference</td>
<td>492</td>
<td>31%</td>
</tr>
<tr>
<td>Full preference</td>
<td>379</td>
<td>24%</td>
</tr>
<tr>
<td>Partial preference</td>
<td>113</td>
<td>7%</td>
</tr>
<tr>
<td>Dutiable lines (MFN)</td>
<td>343</td>
<td>21%</td>
</tr>
</tbody>
</table>

Main products with low or zero notified MFN tariffs

| Vegetables (HS 7), fruits mainly temperate and tropical (HS 8), prepared meat & fish products (HS 16), unprocessed tobacco (HS 23) |

Source: Own calculations based on the Swiss Common Customs Tariff

The calculations, in percent terms, shows that developing countries enjoyed preferences under the GSP scheme on 31 % of the total notified agricultural tariff lines, i.e., full preference on 24 % and a partial tariff reduction on 7 % on the total tariff lines notified on agricultural products. Of the remaining lines, 21 % of these were notified on products excluded from preferences and 48 % had zero MFN tariffs. This suggests that nearly half of the total agricultural products imported by Switzerland in 2002 did not enjoy or at most received only a partial reduction in duties under the preferential GSP framework. The analysis of the CCT reveals that products for which developing countries are the main producers, e.g., vegetables (HS 7), fresh fruits mostly tropical and temperate fruits (HS 8), prepared meat and fish products (HS 16), and tobacco (HS 23) have zero or low MFN tariffs.
4 The utilisation of preferences: empirical evaluation of agricultural imports under the Swiss GSP framework

4.1 Description of the data set and methodology

This section uses trade data, for a total of 114 developing countries and 53 LDCs that export under the GSP scheme, over 492 tariff lines on which preferences have been notified under the GSP scheme. It evaluates the efficiency of trade preferences with calculations on utilisation rates, potential coverage and utility rates. These ratios have been calculated at the 8-digit level for all the beneficiary countries and products. The total results have, however, been aggregated across products and countries at the 2-digit level for simplicity in presentation.

The main indicators are as follows:

**Utilisation rate**: is the ratio between imports actually receiving GSP preferences and agricultural imports covered under the preference scheme. Higher utilisation rates shows that preferences have been effectively used by the preference beneficiary countries. This is a measure of how much developing countries have been able to take advantage of preferences allowed under the GSP scheme.

**Utility rate**: is the ratio of agricultural imports actually receiving preference and all total dutiable agricultural imports (these include both, covered and not covered agricultural imports). A low value of utility rate means that a large part of dutiable imports (either covered or not) pay the MFN rate.

**Potential coverage**: is the ratio between imports that are covered by preferences and the total MFN dutiable agricultural imports. Higher percentage values of the potential coverage suggests broad coverage of products under the scheme.

4.2 Main findings

Table 3 contains total import data for Switzerland from the beneficiary developing countries.
<table>
<thead>
<tr>
<th>Year</th>
<th>Total imports</th>
<th>Total dutiable imports</th>
<th>Covered</th>
<th>Receiving preference</th>
<th>Potential coverage</th>
<th>Utilisation rate</th>
<th>Utility rate</th>
</tr>
</thead>
<tbody>
<tr>
<td>2001</td>
<td>1,200,386,947</td>
<td>751,125,819</td>
<td>449,261,128</td>
<td>322,508,979</td>
<td>37.43%</td>
<td>71.79%</td>
<td>26.87%</td>
</tr>
<tr>
<td>2002</td>
<td>1,103,012,119</td>
<td>689,531,098</td>
<td>413,481,021</td>
<td>283,586,592</td>
<td>37.49%</td>
<td>68.59%</td>
<td>25.71%</td>
</tr>
<tr>
<td>2003</td>
<td>1,151,776,323</td>
<td>729,715,342</td>
<td>422,060,986</td>
<td>277,446,712</td>
<td>36.64%</td>
<td>65.74%</td>
<td>24.09%</td>
</tr>
</tbody>
</table>

**Source:** Own calculations based on the Swiss Federal Customs data

During 2001 - 2003, the total imports from developing countries were 3,455.18 million CHF, out of this only 883.54 million CHF were eligible for GSP preferences. This suggests that only 25.57 % of the total imports from developing countries benefited for preferences under the GSP framework; the remaining 74.43 % of the total agricultural products imported from developing countries came under MFN tariffs.

In 2003, the total imports by Switzerland, as the preference-giving country, from GSP beneficiaries amounted to 1,151.76 million CHF, of which 422.06 million CHF were covered under their GSP scheme. However, only 277.45 million CHF out of the potential 422.06 million CHF actually received trade preferences, with the utilisation rate equal to 65.74 %. This means that the MFN rate of duty, rather than the preferential tariff, was levied on 144.6 million CHF potentially covered by trade preferences. This suggests that there is tremendous scope for improving the utilisation of the currently available trade preferences under the GSP scheme.

The analysis of the potential coverage ratios shows that low product coverage has been a persistent feature of the existing GSP scheme. In 2003, the product coverage was equivalent to only 36.64 %, a persistently low potential coverage over three decades and falling imports under the GSP scheme suggest that an increase in the existing product coverage under the GSP scheme can be considered. The analysis shows that a restrictive
coverage of products under the GSP scheme inflates the utilisation rate of preferences. The value of preferences allowed to developing countries under the GSP scheme is however, worth much less than it appears at the first glance on the utilisation rates of preferences.

During 2001 – 2003, the average utilisation of preferences by all the beneficiaries was 68.77%. The analysis shows the average utilisation rate was higher at 71.70% in 2001 but this has declined over 2001 - 2003. The decline of almost 6% in the utilisation rate of preferences is explained by lower participation by China in the GSP scheme and at the same time increasing imports from the EU under bilateral agreements.

Table 4 provides a breakdown of preferential agricultural imports from the top GSP trading countries (the main countries have been identified in terms of the total imports that receive preferential treatment) and the utilisation of preferences by the main trading partners.

Table 4: Average coverage and utilisation rates of preferences in Switzerland, by main developing countries: 2001 – 2003

<table>
<thead>
<tr>
<th>Countries</th>
<th>Total imports (MFN + GSP)</th>
<th>Total MFN dutiable imports</th>
<th>Covered</th>
<th>Receiving preference</th>
<th>Potential coverage</th>
<th>Utilisation rate</th>
<th>Utility rate</th>
</tr>
</thead>
<tbody>
<tr>
<td>South Africa</td>
<td>270,086,569</td>
<td>129,440,356</td>
<td>140,646,213</td>
<td>92,246,146</td>
<td>52.07%</td>
<td>65.59%</td>
<td>34.15%</td>
</tr>
<tr>
<td>Thailand</td>
<td>300,915,565</td>
<td>76,377,077</td>
<td>224,538,488</td>
<td>153,586,499</td>
<td>74.62%</td>
<td>68.40%</td>
<td>51.04%</td>
</tr>
<tr>
<td>Vietnam</td>
<td>94,054,546</td>
<td>65,666,972</td>
<td>28,387,574</td>
<td>19,486,711</td>
<td>30.18%</td>
<td>68.65%</td>
<td>20.72%</td>
</tr>
<tr>
<td>China</td>
<td>197,594,300</td>
<td>78,722,211</td>
<td>118,872,089</td>
<td>96,972,171</td>
<td>60.16%</td>
<td>81.58%</td>
<td>49.08%</td>
</tr>
<tr>
<td>Philippines</td>
<td>66,033,360</td>
<td>26,208,543</td>
<td>39,824,817</td>
<td>38,520,742</td>
<td>60.31%</td>
<td>96.73%</td>
<td>58.34%</td>
</tr>
<tr>
<td>Brazil</td>
<td>633,642,589</td>
<td>360,996,185</td>
<td>272,646,404</td>
<td>200,888,169</td>
<td>43.03%</td>
<td>73.68%</td>
<td>31.70%</td>
</tr>
<tr>
<td>Main trading partners</td>
<td>1,562,326,929</td>
<td>737,411,344</td>
<td>824,915,585</td>
<td>601,700,438</td>
<td>52.80%</td>
<td>72.94%</td>
<td>38.51%</td>
</tr>
</tbody>
</table>

| Total - All developing countries | 3,455,175,389 | 2,170,372,259 | 1,284,803,135 | 883,542,283 | 37.18% | 68.77% | 25.57% |

Source: Own calculations based on Swiss Federal Customs data
During 2001 - 2003, the average utilisation rate of preferences by the main GSP trading partners has been 72.94 % against the average utilisation of 68.77 % by all the beneficiary countries. This suggests that the main trading partners have utilised the scheme by an additional 4 % points compared to the other beneficiaries. In terms of the total volume of agricultural imports covered and receiving preferential treatment, Philippines shows an average utilisation rate of 96.73 %, other countries with high average utilisation of GSP preferences are China (81.58 %) and Brazil (73.68 %).

An important qualification that needs to be emphasised is that higher utilisation rates of the GSP scheme does not ensure that preferences will be utilised automatically by all the beneficiary countries. The utilisation of preferences is related to the existing conditions of the GSP scheme and the manner of operation of the scheme. For instance the products covered, the preference margin allowed, the rules of origin requirements, administrative costs to be borne by the exporters in the beneficiary countries, existing non-tariff measures like health and safety standards notified for imports, conditions for imports under the other preference schemes are important factors that determine the utilisation of the GSP scheme by the beneficiaries.

The utility rate by the main beneficiaries is 38.51 % against the average of 25.57 % during 2001 – 2003. A lower utility rate suggests that most imports come under the MFN tariffs. There is therefore, scope for an expansion of the existing product coverage under the GSP scheme if preferences have to be used a trade policy instrument for the development of the beneficiary countries.

Figure 1 presents the indicators for the 6 main GSP trading partner countries that participate in imports under the GSP scheme.
Figure: 1: Efficiency indicators of the GSP scheme

Brazil

China

Phillipines

Vietnam

Thailand

South Africa

Source: Own calculations based on the Swiss Federal Customs data
The analysis shows that Brazil has sustained high utilisation rates of GSP scheme because of large imports of meat and meat offal (HS 2) by Switzerland. Imports from China also show high utilisation of the scheme, but the utilisation of the GSP scheme has declined from 91% to 48% during 2001 – 2003; the main reason for this trend of the utilisation of preferences is the bird flu, which influenced the demand for poultry and, therefore, the imports from China adversely. Agricultural products imported from Philippines and Vietnam show sustained high utilisation of the GSP scheme. These countries are the main suppliers of seafood, i.e., products of meat and fish (HS 16), seed fruit equivalent and preparations of fruits and nuts mainly for use by the processing industry in Switzerland (HS 20) and fresh fruits (HS 8), respectively. South Africa has also utilised these preferences for fresh fruits (HS 8).

It emerges from the analysis that preferences do not fulfil the objective of enhancing market access for all the beneficiary developing countries into the Swiss markets. For those developing countries that are not relatively advanced, the value of preferences is negligible. The selective utilisation of preferences and skewed distribution of the benefits of additional market access benefits is can be interpreted to imply that preferences under the GSP framework underperform as a development tool. As a result, the feasibility of preferences from a development perspective is questionable since these do not help achieve the objective of the SDT to integrate developing countries into the world economy.

5 Main constraints to an effective preference utilisation

The analysis suggests the following main reasons for low utilisation ratios of preferences:

Firstly, the existing coverage of products under the GSP scheme is restrictive. The analysis shows that products in which developing countries have a comparative advantage and interest are excluded or at most these products are allowed a partial preference under the GSP framework. Most processed agricultural products are excluded from preferences or allowed a very small preference margin. The analysis shows that most processed products, like roasted cocoa paste,
cocoa butter and cocoa powder are imported under the bilateral preferential agreement from the EU\textsuperscript{23}; this hints at the possibility of re-export by the EU, which, however, cannot be substantiated due to lack of re-export figures. Besides, similar tariff preferences have been allowed under the bilateral agreement to all imports from the EU which further reduces the effective preference margins and, therefore, the incentive for developing countries to participate in the GSP scheme. A small preference margin, therefore, clearly excludes any incentive for the exporters in developing countries to utilise the GSP scheme and preferences, therefore, fail as means of enhancing market access for developing countries’ agricultural exports in Switzerland.

Secondly, the existing notified rules of origin requirement under the Swiss GSP\textsuperscript{24} are complicated and require the exporters in developing countries to incur high compliance costs. The existing rules need a minimum content of 50\% domestic input requirement and do not allow cumulation between developing countries. The administrative complexities, for instance, maintenance of complex accounting systems and expenses incurred to obtain the relevant customs certificate to prove conformity with the origin rules; and, information deficiencies in sourcing inputs and design production structures to ensure compatibility with the requirements specified by the preferential rules of origin, lead to an overall low utilisation of the GSP scheme. The Trade Policy Report on Switzerland also recognises the shortcoming that “the administrative costs of compliance with the specific rules of origin may exceed the benefit of the margin of tariff preference” (WTO, 2004b).

Thirdly, the cost argument is further enhanced by the specific structure of Swiss tariffs. Specific tariffs are levied by weight and the incidence per unit of specific tariffs is very high for low valued agricultural products. As a result, this discriminates against the low valued unprocessed agricultural products from developing countries and does not encourage participation in primary agricultural trade.

Finally there are additional factors that limit the utilisation of preferences by developing countries. These are issues relating to the beneficiaries’ limited capacity to satisfy the requirements for imports. Some of these are as listed below:
(a) Inability to comply with the mandatory health and safety standards as well as the labelling requirements;
(b) Lack of knowledge and expertise to design production structures to ensure compatibility with the standards for processed agricultural products;
(c) Inability to comply with the strict norms on traceability for most agricultural products;
(d) Supply side constraints and institutional weaknesses, i.e., unreliable business partners, unstable macro-political environment, corrupt bureaucracy;
(e) High costs for exporters to get access to standard trade facilitating measures like insurance and trade finance;
(f) Infrastructural bottlenecks and high costs of transportation;
(g) Consumers’ perception about the origin of products (e.g., demand for fair trade products).

6 Conclusions and the way forward

The results clearly show that the GSP scheme has not provided additional market access for all the beneficiary countries and products in Switzerland. The benefits of enhanced market access are selective and concentrated on a small group of developing countries. As a result, a disproportionate share of enhanced market access benefits accrue to a relatively small group of developing countries that are relatively better integrated into the multilateral trading system. This suggests that preferences allowed under the existing GSP scheme have underperformed from a developmental perspective.

The inability of preferences to enhance market access for developing countries and the continued underutilisation of preferences by all the beneficiaries suggests that there is a need to recast the existing GSP scheme of Switzerland. An important option is to strengthen the existing framework of preferential tariffs under the GSP framework. In the short run, it is recommended that the GSP framework can be strengthened by enhancing the existing preference margins and product coverage complemented with a simplification of the preferential rules of origin for agricultural products. In the long run, it is suggested that capacity building measures should be initiated so that these address the institutional weaknesses and the existing supply side constraints in the
beneficiary countries so that these countries’ exports are competitive to facilitate their integration into the world economy. The recommendations for the short and long run are as follows:

6.1 Allow higher preference margins and broader product coverage for developing countries’ products imported under preferences

An increase in preference margin is warranted to strengthen the framework of preferential tariffs from a development perspective. It is recommended that higher preference margins should be allowed on products in which developing countries are the main producers, e.g., cut flowers (HS 6), vegetables (HS 7), fresh fruits mainly tropical fruits (HS 8), cocoa (HS 18), and tobacco (HS 23) so that it provides an incentive for developing countries’ exporters to participate in the GSP scheme. Broader product coverage together with higher preference margins will provide the premium over the normal rate of return that will encourage participation by developing countries and lead to a higher utilisation of preferences. This will have positive effects through economies in scale and scope, which will stimulate further trade and growth in developing countries and lead to better integration of these countries in the world economy.

6.2 Simplify the existing rules of origin

It is suggested that the existing rules on cumulation for agricultural products should be simplified so that these allow developing countries to source the intermediate inputs from the best low cost providers. Cumulation should be allowed between developing countries or groups of these countries because this will enable the beneficiary countries to meet the high value-added requirement as a group of countries and contribute to a higher participation by these countries in the GSP scheme. It is also proposed that the existing domestic value-added requirement should be replaced by the import value requirement for the costing of the shares of domestic to imported inputs. The rationale for this suggestion is that the import value requirement is relatively easier to compute and the value of the imported inputs can be supported by the suppliers’ invoices. It is, therefore, suggested that the import value requirement on content can be substituted with the “value-added tariffs” approach in the long run. The UNCTAD (2003) has also proposed the value-added approach which excludes the preferential component under the GSP scheme so that
MFN duties are paid on the non-preferential component of the product. This approach will simplify the administration of the rules of origin, support a gradual integration of developing countries in the multilateral trading system, and enable a transition to single tariffs in future.

6.3 Initiate capacity building and technical assistance for the beneficiary countries

Capacity building measures and technical assistance are an important way forward to enhance the participation of developing countries and facilitate their integration into the world economy in the long run. Development assistance through capacity building can address the major trade-related costs, for instance infrastructural bottlenecks, institutional weakness and problems, that at present limit export growth in many small and low-income developing countries and their effective participation under the GSP scheme. Capacity building will support institutional capacity building in developing countries that will allow the beneficiary countries to benefit from increased trade opportunities and better access in general.

For instance, Swiss importers have undertaken capacity-building measures in Brazil, Argentina, South Africa and Paraguay, that helped these countries to become the main suppliers of high quality meat (HS 2) to Switzerland. The Swiss Import Promotion Programme (SIPPO) and individual supermarkets, e.g., Migros and Coop, in Kenya, Ethiopia, and Colombia for cut flowers, vegetables and fresh fruits have also undertaken other similar initiatives.

Since capacity-building measures involve huge investments, many importers may not invest large amounts for infrastructure development in developing countries that suffer from “natural” locational disadvantage. Federal government participation is, therefore, recommended through official involvement as well as incentive schemes for the importers. This will reflect the commitment of the Swiss Federal government to the developmental objectives and signal the continuity and certainty of preferences in future. In addition, customs officials and exporters in the beneficiary countries should be imparted training; this can be disseminated through conducting seminars on customs formalities at the national and regional level in the beneficiary countries. These seminars will provide useful information to the beneficiary countries’ customs officials and the exporters about the existing rules and regulations on the rules of origin under the
GSP scheme. In the long run, such measures will reduce the high administrative costs that, under the present system, are a disincentive to developing countries’ participation.

6.4 Change the structure of tariffs from specific to ad valorem basis

Another closely related issue that impacts developing countries’ competitiveness and consequently market access, mainly for primary agricultural products is the structure of tariffs. Switzerland has specific tariffs, which are levied on the quantity rather than value of the imports. Specific tariffs tend to discriminate against exports from low-income countries, whose producers often specialize in the lower price-quality segment of export markets. In this manner, specific tariffs bias against the imports of low value primary agricultural commodities that are mainly produced by developing countries. Statistics reveal that agricultural prices have been declining over 1990-2000 (IMF, 2003) and falling agricultural prices combined with specific tariffs become a market access barrier for developing countries exports. It is, therefore, recommended that Switzerland should change from specific tariffs to *ad valorem* tariffs in the long run.

To conclude, it is imperative to address the development objective of preferences at the multilateral level so that these are used as trade policy instruments for development. Changes in the design of preferences are needed to enhance the efficiency of the existing GSP scheme, from both a development objective and the perspective of the trading system in general. This will further the development objective of preferences and in this manner preferences can be used to further the development objective of preferences, allowed by Switzerland, so that these support the integration of developing countries into the multilateral trading system.
Endnotes:

1 GSP schemes allow non-reciprocal preferences at reduced or zero tariff rates over the MFN tariff rates for selected agricultural and industrial products originating in developing countries. The GSP schemes are at http://www.unctad.org/Templates/Page.asp?intItemID=2309&lang=1

2 There are has two lists of countries that are eligible for tariff preferences under the GSP framework. List I includes developing countries generally termed as APS countries (Allgemeines Zollpräferenzsystem) in the Swiss nomenclature. List II includes LDCs, referred to as the PMA countries (pays les moins avancés). The handbook on the Swiss GSP is at http://www.unctad.org/en/docs//poicdtsbm28r1.en.pdf.

3 Denmark, Ireland and the U.K. replaced their scheme upon joining the EEC with the EEC scheme in January 1974.

4 On market access, SDT allows preferential access under the GSP framework for developing countries’ products, complemented by less than full reciprocity in negotiating rounds. On rules, SDT includes providing technical assistance to lower income countries to help them implement disciplines, complemented with longer time periods as well as exemptions from WTO rules (Hoekman, Winters & Michalopoulos, 2004).

5 During 2001-2002, developing countries made 88 specific suggestions to strengthen SDT – important among these were proposals on improved preferential access to developed country markets, exemptions from specific WTO rules, binding requirements to provide technical and financial assistance to help developing countries implement multilateral rules and benefit from negotiated rights, and an expansion in aid to address the supply side constraints.

6 The details of the GSP schemes are available online at http://www.unctad.org/Templates/Page.asp?intItemID=2309&lang=1

7 The details of the different trade regimes are at http://www.wto.org/english/tratop_e/tpr_e/s141-3_e.doc

8 The European Free Trade Association (EFTA) is an inter-governmental organisation established in 1960. Its Member States are Iceland, Liechtenstein, Norway and Switzerland. The EFTA member states have concluded a number of free trade agreements with a number of countries worldwide as a member country of the EFTA. Free trade agreements concluded with third countries within the EFTA framework cover processed agricultural products and fish and other marine products as well as industrial products.

9 The relevant legislation refers in brackets.

10 Unprocessed agricultural products are not covered by the agreement. These are different rules of origin for reciprocal free trade agreements concluded within the context of bilateral agreements, these are available online at: http://www.zoll.admin.ch/f/gesetze/dokumente/d30/d30.php

11 Free-trade organization, founded in March 1991 as a result of the Asunción Treaty by Argentina, Brazil, Paraguay, and Uruguay, and formally inaugurated on 1 January 1995. Mercosur constitutes the world’s fourth-largest free-trade bloc after the European Economic Area, the North American Free Trade Agreement, and the Asia-Pacific Economic Cooperation Conference. In June 1996, Chile and Bolivia were admitted as associate members.

12 In 1972, Switzerland and the EU signed a free trade agreement for industrial products. In 1999, seven Bilateral Agreements were signed on free movement of persons, land and transport, air transport, agriculture, research, technical barriers to trade and government procurement. In 2004, Switzerland and the EU agreed on nine additional agreements, these deal with cooperation in the fields of justice, asylum and migration (Schengen/Dublin), taxation of savings, action to combat fraud, processed agricultural products, the environment, statistics, the media, pensions, education, vocational training and youth. Details are given at: http://www.zoll.admin.ch/f/gesetze/dokumente/d30/d30.php
Ordonnance sur les denrées alimentaires (RS 817.02), Annex 7 and 8.

Administration fédérale des douanes.

Ordonnance du 29 janvier 1997 fixant les droits de douane préférentiels en faveur des pays en voie de développement, RS 632.911, as amended.

Federal legislation RS 632.911 refers.

The list of products eligible for GSP benefits are listed at http://www.admin.ch/ch/d/sr/632_911/app1.html. The applied preferential and MFN tariffs are listed in the Zolltarif, this can be accessed online at http://xtares.admin.ch/tares.

The list of the products eligible for special preferences under the GSP scheme is available online at http://www.admin.ch/ch/d/sr/632_911/app3.html.

In 2004, the World Bank classified a high income country with per capita income of $ 10,066 or more per year.

There are specific rules of origin for agricultural products imported under the non reciprocal preferences within the GSP which are available on line at: http://www.unctad.org/en/docs/poitcdtsbm28r1.en.pdf.

Switzerland has specific tariffs that are levied by weight, litre.

The average potential coverage of products under the GSP scheme has been 32% during 1972 – 2002.

An example is cocoa (HS 18) that is allowed a preference margin of only 0.02 CHF/kg. During 2002, the total imports of cocoa by Switzerland were 287.68 million CHF. The share of developing in total cocoa imports was 60.53 million CHF, but out of this only 1.39 million CHF was imported under preferences and most of the cocoa imported came from the EU, despite the EU not being the main producers of cocoa.

The rules of origin have been notified to the WTO under Ordonnance relative aux règles d'origine régissant l'octroi de préférences tarifaires aux pays en développement, RS 946.39 in November, 1996, modified in 2004 to reflect the tariff initiative allowed for LDCs (WTO, 2004b; pp 54 refers).

REFERENCES


