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Restoring Market Access: The case of the EU's relaxation decision on origin requirements for selected Jordanian exports*

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Abstract

Rules of origin play a crucial role in preferential trade agreements, and they can also deny intended market access for preference receivers. This brief examines a relaxation by the EU (decision no.1/2016)¹ of the origin requirements for selected products from Jordan, which is intended to create 200,000 job opportunities for Syrian refugees. While the relaxation decision may have an effect on the refugee crisis in Jordan, further simplifications in RoO requirements are called for.

* See Brunelin, S., J. De Melo, A. Portugal-Perez (2018) "How Much Market Access? A Case study of Jordan's Exports to the EU" FERDI Working paper P211, February.

1. <https://publications.europa.eu/en/publication-detail/-/publication/a45b2513-6e7e-11e6-b213-01aa75ed71a1/language-en>

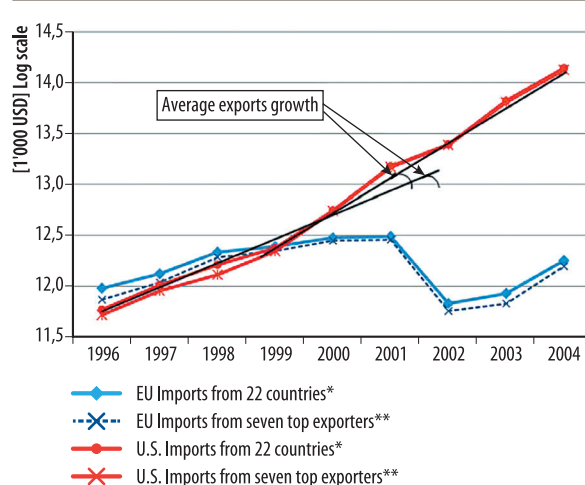
The value of preferential access schemes by the main purveyors of preferences, the EU and the US, has eroded over the years: a lowering of MFN tariffs, an extension of preferences by the EU and the US to more countries, unpredictability often compounded by complicated origin requirements to qualify for preferential access. Conconi *et al.* (2016) estimate that in the case of NAFTA, RoO on final goods reduced imports of intermediates from third-countries by about 30 percentage points. They conclude that even if external tariffs are unchanged, RoO embedded in FTAs may violate multilateral trade rules by increasing substantially the level of protection faced by non-members.

Against this trend, four changes in origin requirements have sought to restore market access. In 2001, under the Africa Growth Opportunity Act (AGOA), the US announced that certain AGOA beneficiaries would satisfy the origin requirement for apparel under the 'single transformation' rule (textiles → apparel) while the EU maintained a 'double transformation' rule (yarn → textiles → apparel) requirement for apparel under the Everything but Arms (EBA) (see figure 1a). Second, the EU adopted the 'single transformation rule for EBA (i.e. LDC) beneficiaries in 2011 (see figure 1b). For both the EU and the US, the (unadjusted) preferential margins for exports of apparel were quite similar (15%) for the US and 11% for the EU. Both figures show that an increase in apparel exports followed the move to a single transformation rule. Third, at the WTO ministerial in Nairobi in 2015, for non-reciprocal preferences for LDCs, WTO members have committed to allow that non-originating materials can make up to 75 percent of the final value of a product to qualify for preferential treatment.

Fourth, to alleviate the refugee crisis in Jordan, a EU decision (decision No.1/2016) provides relaxed origin requirements for a list of goods produced in Jordan for a ten year period until 31 December 2026. The hope is that this relaxation requirement will create up to 200,000 jobs for

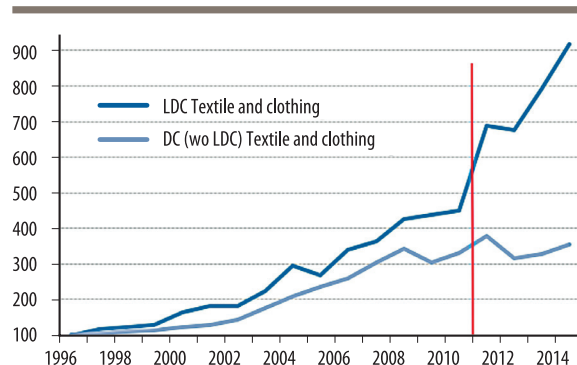
the Syrian refugees. The list of goods includes petroleum products, fertilisers, some chemical and plastic products, articles of leather, textiles, and apparel. Notably, manufacture from fabric is sufficient to confer origin to Jordanian apparel. This amounts to a temporary replacement of the double transformation rule by a single transformation rule for apparel.

Figure 1a. The move to the single transformation rule under AGOA (Exports of Apparel by 22 African countries to US under AGOA and to EU under EBA)



Source: Melo and Portugal-Perez (2014, figure 1a). Solid line indicates entry into effect of AGOA and dashed line entry into effect of single rule (for most beneficiaries)

Figure 1b. The move to the single transformation rule under EBA (EU Textile and clothing imports LDCs vs. other developing countries)



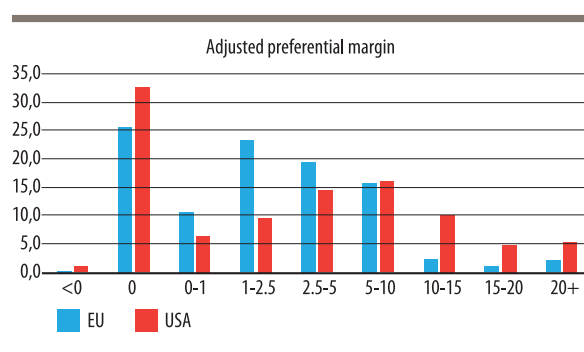
Source: Authors from COMTRADE- Base: 1996=100. Vertical line indicates entry into effect of single transformation rule.

In Brunelin *et al.* (2018), we assess this initiative by comparing Jordan's current utilization of EU-preferences under the EU-Jordan FTA (EUJFTA) with the utilization of preferences by Jordanian exports to the US under the Jordan-US Free Trade Area (JUSFTA), both FTAs going into effect over a 10- year period starting in the early 2000s. We conclude that the relaxation decision could help alleviate the refugee crisis in Jordan. From a broader perspective, simplification of RoO requirements may be the easiest way to restore preferential market access, especially for the EU and the US who have extended preferences to many trading partners.

EUJFTA and JUSFTA have a similar distribution of preferential margins

Adjusted preferential margins (sometimes called 'competition-adjusted margins') provide a first rough measure of potential market access because they exclude from preferences the trade-weighted preferences extended to other partners. This adjustment is important for the EU and the US, both purveyors of preferences to many trading partners. The distribution of these adjusted margins – which apply to all partners engaged in FTAs with the EU and the US – are shown in figure 2 at the most disaggregated (HS8) product level (the difference between unadjusted and adjusted margins for apparel are reported in table 1). Figure 2 shows a similar distribution of preferences for both countries. Between 25% and 30% of Jordanian exports to the EU and the US have no preferential margin, a reflection of zero MFN tariffs. Both the EU and the US only have 15 percent of their preferential margins for Jordanian imports in the 5-10% range. The EU has a lower share of tariff lines with preferential margins in the 10-15% range and beyond (around 2%-3% vs. 5% for the US). All in all, both the EU and the US still have non-negligible access to offer to Jordan.

Figure 2. Distribution of Adjusted Preferential tariffs for Jordanian products in (HS8) in 2016



Source: Brunelin *et al.* (2018, figure 1a)

Origin requirements to qualify for preferential access in apparel are stringent under EUJFTA

Effective market access however, must take into account the costs of complying with Rules of Origin (RoO) requirements and other compliance procedures (e.g. certification methods). A high Preference Utilization Rate (PUR) is a useful indicator to assess the intended effects of any FTA. Three factors are important in accounting for differences in PURs across sectors and across eligible countries:

- The depth of preferential access captured by the adjusted preferential margin.
 - The complexity of the RoO requirement
 - The size of the shipment because of the fixed costs of complying with the RoO requirements
- Table 1 summarizes the importance of these inter-related factors for PURs on apparel imports from Jordan under JUSFTA and EUJFTA. Preferences are higher under JUSFTA, especially when preferential access is measured correctly by the adjusted margin (a reflection of the fact that the EU extends preferences to a greater number of partners than the US). However, adjusted preferences under EUJFTA are still over 5 percent, which is relatively high, since the worldwide trade-weighted preference margin is barely over 1 percent (Carpenter and Lendle (2011))².

2. Excluding intra-european trade, WTO (2011) estimates that, for the 20 largest importers accounting for 90% of world trade, only 16% of their imports from partners qualify as preferential trade (on the assumption that all preferences are fully utilized).

For apparel, different RoO requirements are the most important difference between the two FTAs. In the case of JUSFTA, the single transformation rule applies [whereas for most other US FTAs a ‘triple transformation rule’ (cotton → yarn → textiles → apparel) applies]. Under EUJFTA – until the decision of August 2016 – Jordan’s requirement for access to the EU required a double transformation rule.

The disparity in PURs and import volumes is noteworthy as the markets for imports of apparel are of comparable size for the EU and the US and involve many common exporters of apparel. Imports of apparel under EUJFTA are negligible while they are from 100 to 300 times larger under JUSFTA. This pattern does not extend to other products at the HS8 level. Outside the apparel sector, comparing PURs at the product (HS8) level for EUJFTA and JUSFTA show similar patterns where, as expected, PURs are higher for products with higher adjusted preferential margins. For given preference margins, higher PURs are observed for products with larger traded volumes, an indication of the fixed costs associated with satisfying origin requirements (Cheraskin *et al.* (2011) and Keck and Lendle (2012)).

Table 1. Preferences, RoO requirements, utilization rates and import volumes in Apparel under EUJFTA and JUSFTA (2016)

	Knitted (HS61)	Non-knitted (HS62)	Knitted (HS61)	Non-knitted (HS62)
FTA	JUSFTA	JUSFTA	EUJFTA	EUJFTA
Preference margin (%) ^a	16.4 [14.0]	14.2 [11.8]	11.9 [6.4]	11.4 [6.1]
RoO (Transformation rule) ^b	Single	Single	Double	Double
Preference utilization rate (PUR)	100%	100%	0.01%	0.07%
Import volume (1,000\$)	930,000(\$)	322,000(\$)	31,294(€)	3,321(€)
Number of HS8 tariff lines	122	195	285	301

Notes: Source: Brunelin *et al.* (tables A2 and A3)

a. Adjusted margins (for preferences granted to other partners) in brackets. // b. See text for definition.

The complexity and heterogeneity of RoOs in apparel have contributed to disparate, and often low, preference utilization rates

To further illustrate the role of RoO requirements, table 2 reports the sharp differences in PURs for apparel imports across a selection of exporters engaged in preferential trade arrangements (mostly reciprocal) with the EU and the US. These PURs differ widely across partners, especially for the US. This disparity in PURs probably reflects Donner Abreu’s observation that no two RoO requirements for textiles and apparel are the same across the eleven preferential arrangements tallied (Donner Abreu, 2013, table 5.2).

Table 2. Utilization rates for Apparel (2016) Knitted (HS61) and non-knitted (HS62)

	EU		USA	
	HS61	HS62	HS61	HS62
Algeria	0.02	0.60	N.A.	N.A.
Egypt	0.93	0.89	0.99	0.98
Israel	0.60	0.39	0.97	0.97
Jordan*	0.01	0.07	1.00	1.00
Lebanon	0.91	0.80	0.00	0.51
Morocco	0.89	0.90	0.23	0.05
Syria	0.95	0.86		
Tunisia	0.93	0.90	0.00	0.00
Turkey	0.95	0.97	0.75	0.48

Notes: N.A. No trade flow. * For the USA, utilisation rates include FTA+GSP+ QIZ

Source Authors from Brunelin *et al.* (2018).

As a further check for the presence of a Jordan and/or apparel effect, using data for 2016 we regressed PURs on preference margins and import volumes at the HS8 level for all countries exporting under preferential schemes to the EU and US. Statistically significant estimates show that PURs are positively associated with preferential margins and, controlling for preferential margins, a higher average import volume is associated with a higher PUR, an indication of the presence of fixed costs. The interaction of a dummy variable for Jordan with a dummy variable for T&A is positive for the US and negative

for the EU, a reflection that the US only grants the single transformation rule in apparel for Jordan (and qualifying AGOA exporters) while other partners receiving US preferences have to meet the triple transformation rule. On the other hand, the negative coefficient for the EU dummy interacted with the T&A dummy captures the effects of the single transformation rule granted by the EU under EBA. Together, these results point towards the origin requirement in T&A having an independent effect on PURs for those products.

Further simplifications in RoO requirements are called for

The EU relaxation decision aims to create 200,000 job opportunities for Syrian refugees. This is an ambitious target. First, since beneficiaries must be located in designated special economic zones, this could be equivalent to a quota on exports under a capacity constraint eligible for preferential market access. Second, companies operating outside the designated areas will have to incur costs to move operations if they want to benefit from preferences and the

conflict in Syria has left the port of Aqaba in the South as the only viable option for Jordanian exports. Third, LDCs have access to the EU market under the single transformation rule since 2011. Looking ahead, further simplifications in origin requirements would help restore market access. For apparel, a uniform low value content rule (say 10% value-added across-the-board) perhaps combined with a change of tariff classification (CTC) at the subheading (HS6) level could be envisaged. In any case, for all products, eliminating RoO requirements for tariff lines with unadjusted preferential margins below 3%—which corresponds to the middle range of estimates of fixed costs for meeting origin requirements—should help, especially the small exporting firms. And progress at multilateralizing reciprocal RoO would be most welcome.

* This brief appeared as <https://voxeu.org/article/restoring-market-access-relaxing-rules-origin>. A version taking a broader perspective on Jordanian export performance under EUJFTA and JUSFTA appeared on the ERD forum.

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