CHAPTER 7

HOW AID FOR TRADE HELPS REDUCE THE BURDEN OF TRADE COSTS ON SMEs

Contributed by the International Trade Centre

Abstract: *Small and medium-sized enterprises (SMEs) represent the backbone of economic activity in both developed and developing country economies. SMEs tend to be less productive than large firms, and the productivity gap is particularly pronounced in developing countries. Evidence shows that SMEs that are integrated in global markets – whether directly or indirectly – are more productive than those that do not participate in trade. Integration into global and regional markets is thus likely to contribute to closing the productivity gap between SMEs and large enterprises, with positive repercussions on the inclusiveness of growth.*

SMEs suffer disproportionally from trade-related fixed costs, which create a bias in favour of large firms that find it easier to overcome fixed costs. A reduction of fixed costs to trade can therefore contribute to making trade more inclusive. Survey evidence reported in this chapter shows that costs related to access to information, access to trade finance or regulatory burdens are particularly important for private sector activity. In order to design effective solutions to reduce relevant costs, in particular those occurring at the border, collaboration between the public and the private sector is useful.

INTRODUCTION

Small and medium-sized enterprises (SMEs) are integral to economic development, particularly in LDCs, and are an essential component of inclusive, sustainable development. In most countries, SMEs represent well above 90% of all private enterprises and over 60% of employment. As such it is fair to say that they represent the backbone of economic activity in most economies. Not surprisingly, therefore, the health of an economy's SME sector is a good barometer of the well-being of a country's economy.

Evidence shows that SMEs are in general less productive than large firms and pay lower wages. But the size of the productivity gap between SMEs and large firms differs across countries and tends to be larger in the developing world. This productivity gap is likely to be a determinant of economic and social cohesion within an economy, which is likely to determine income distribution and the probability of SMEs to grow.

SMEs are by definition small, yet how small they are differs across countries, with the overwhelming bulk of firms being micro-firms in much of the developing world. Some countries, especially LDCs are characterised by a so-called missing middle, i.e. the absence of a healthy segment of middle-sized enterprises. This again may imply that large firms remain largely unchallenged by internal competitors, which may open the door to inefficiencies and non-competitive behaviour.

SMEs that are either indirectly or directly integrated into regional or global markets tend to be more productive and larger in size than SMEs that do not trade. The relationship between trade on the one hand and productivity and firm size on the other hand is multifaceted and multidirectional, with more productive firms finding it easier to trade, which in turn contributes to productivity increases. Lower trade costs can therefore contribute to higher integration of SMEs in regional and global markets and to productivity increases among SMEs, with positive effects on inclusive growth.

What is an SME?

The term SME encompasses a broad spectrum of definitions which vary across countries and regions. International organisations and financial institutions use their own guidelines for defining an SME. However, almost all definitions are based on some combination of the number of employees, turnover and assets. Regarding the maximum number of employees, the World Bank applies a cut-off value of 300 employees per firm, the Inter-American Development Bank a value of 100 employees and the Asian and African Development Banks a value of 50 employees.

Definitions also vary widely across countries and do not necessarily follow the expected pattern that richer countries allow for higher maximum numbers of employees. This is, for instance, reflected in the following Table 7.1 based on Gibson and van der Vaart (2008). It shows that In Viet Nam, companies with up to 300 employees qualify as small and medium sized, whereas in Norway firms with more than 100 employees are considered large.

TABLE 7.1 Maximum number of employees according to national SME definitions, selected countries.

Country (ordered by per capita GNI)	Maximum no. of employees to meet SME definition	Country (ordered by per capita GNI)	Maximum no. of employees to meet SME definition
Norway	100	**Viet Nam**	300
Switzerland	250	**Bangladesh**	100
Brazil	100	**Ghana**	100
Thailand	200	**Tanzania**	20
Moldova	250	**Malawi**	50
Egypt	50		

Source: Gibson and van der Vaart (2008).

How do SMEs perform?

The literature suggests that SMEs tend to be less productive than large companies, partly because they tend to be engaged in more labour-intensive sectors and do not benefit from economies of scale (Wymenga et al. 2011). This is especially true in developing countries, where advanced manufacturing techniques may not be used due to insufficient financing, a poor regulatory environment or other market failures. Lower productivity is born out in the statistics presented in Table 7.2, where the share of employment and the contribution to GDP are shown for a select number of countries. In most cases, the share of employment is higher than the share of GDP, implying the average productivity of an employee working for an SME is lower than that found for large firms. An exception is the United States, where employees working for SMEs appear to be as productive as those working for large firms.

TABLE 7.2 The importance of SMEs for trade and economic activity

Country	Share of firms (%)	Share of employment (%)	GDP Value Added (%)	Share of SMEs Exporting (%)
Brazil	99.9	77	61	11 (S)
Canada	99.7	60	-	-
Chile	98.9	80	25	15
China	99.0	73	60	40-60 (M)
Columbia	96.4	84	-	20
EU	99.8	70	61	-
India	95.0	80	40	32 (M)
Japan	99.0	72	52	14 (M)
Mexico	99.8	74	52	-
New Zealand	99.8	75	-	-
Sweden	96.3	60	57	24 (M)
Taiwan	96.3	80	-	56 (M)
US	99.9	50	50	31 (M)

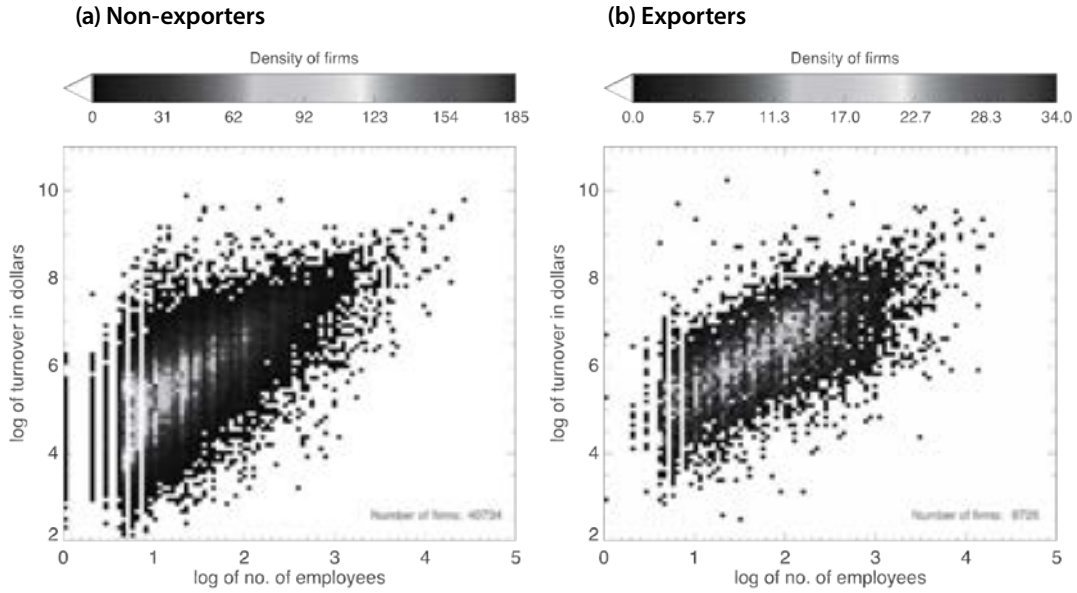
Note: SME share of firms, employment and GDP; fraction of SMEs engaged in export activities (M) and (S) denote data for manufacturing and services data only.

Source: OECD (2014).

The productivity differences between small and large firms tend to be more pronounced in developing countries than in industrialised countries. OECD-ECLAC (2013) reports that in Germany the productivity of small firms is around 70% of the productivity of large firms. In Argentina, in contrast, the productivity of small firms is less than 40% that of large firms, and in Brazil that percentage is below 30%. In some countries, the productivity gap between small and large companies is substantial. In India, for instance, enterprises with more than 200 employees are ten times more productive than enterprises with five to 49 employees (Abe et al., 2014). SME productivity also differs widely across Asian countries, with labour productivity in Indonesia being double that of India and Thailand being more than double that of Indonesia (Abe et al., 2014).

Smaller and less productive firms may find it harder to connect to global markets. The heat charts in Figure 7.1 below reveal that small firms with high turnover and high exports exist (notably in the services industry), but that it is much more frequent for exporters to have a size of around 100 employees (red dots are at a value of two on the horizontal axis). This evidence based on data from the World Bank's Enterprise Surveys is in line with findings from more sophisticated empirical studies showing that exporters tend to be larger in size and more productive than firms that do not trade (e.g. Bernard et al., 2007).

Figure 7.1 Firm level turnover versus number of employees: densities according to export status



Source: ITC calculations based on World Bank Enterprise Survey data.

Why trade-related fixed costs matter more for SMEs

The existence of trade-related fixed costs is likely to be one of the main reasons why smaller, less productive firms find it difficult to export. Indeed, in Melitz's (2003) seminal paper, trade-related fixed costs create a wedge between larger and smaller firms, as only the former manage to make profits while paying the fixed costs to export. Those firms that manage to export are more productive at the outset but become even more productive thanks to their ability to export.

The finding that fixed costs disproportionally affect SMEs is also reflected in case studies and business literature. Lattimore et al. (1998) cite evidence indicating that, in 1994-95, SMEs bore around 85 % of the regulatory compliance burden, while their share in GDP was only around 30%. Unlike large companies, most SMEs do not possess in-house trade or international departments with experts who know how to efficiently overcome relevant trade costs. SMEs tend to have limited resources and a lower threshold to absorbing risks, especially when operating in intensely competitive markets (OECD, 2006). In addition, the fact that SMEs tend to trade smaller quantities implies that fixed trade costs often make up a larger share of the unit cost of their goods and services when compared to rivals exporting larger volumes.

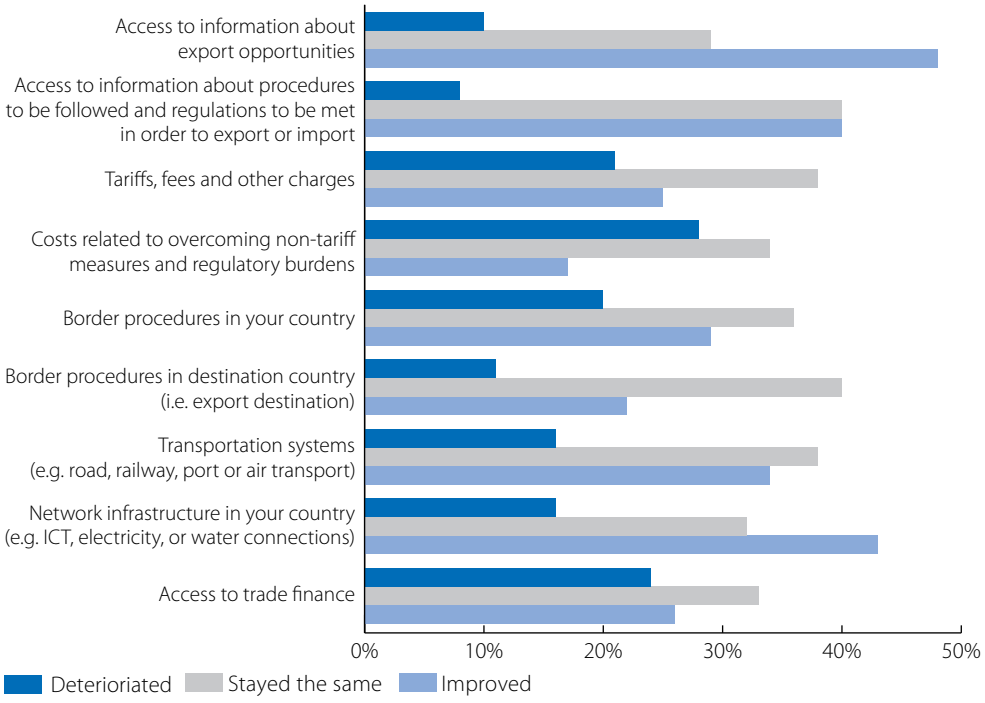
Trade-related fixed costs therefore greatly matter for SMEs and may hamper their opportunities to increase productivity through trade. SMEs are therefore likely to be among the main beneficiaries of efforts to address such costs in the context of aid for trade.

THE PRIVATE SECTOR VIEW ON TRADE COSTS

As part of the monitoring and evaluation exercise conducted under the Fifth Global Review of Aid for Trade, private companies were asked about their experience with trade costs and about their priorities for future trade costs reductions, notably in the area of border procedures. Responses were received from 521 firms, of which 103 were large firms (>250 employees), 94 medium sized (between 50 and 250 employees), 161 small (between 10 and 50 employees) and 158 were micro firms (less than 10 employees).

When asked about their experience with trade costs over the past five years, a relatively positive picture arises, in the sense that few respondents had observed a deterioration of the situation. The responses were similar for companies of different sizes.

Figure 7.2 How have the following aspects of trade costs evolved over the past five years?



Source: ITC Monitoring Survey (2015).

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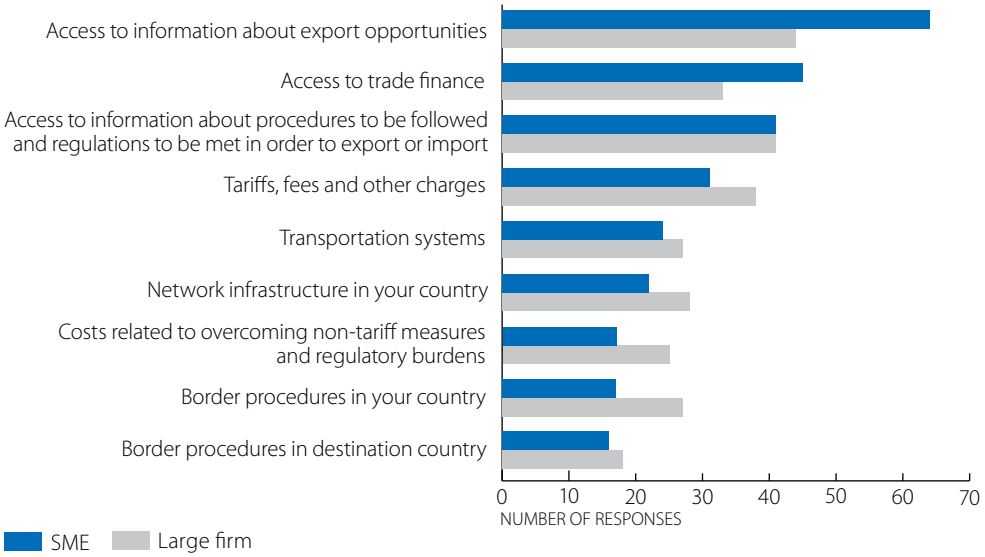
In this survey, a distinction was made between the costs firms have to incur to gain information on procedures and regulations and costs they have to incur to overcome non-tariff measures and regulatory burdens. The latter refers to costs to actually meet standards and regulations and costs incurred to prove that those standards and regulations are met, i.e. so-called certification costs.

Companies were also asked in which aspects of trade costs they would most value improvement. Respondents were asked to indicate the three factors of highest priority. Findings are reflected in Figure 7.3 and are grouped by respondents' size, with SMEs and large firms being reflected separately.

The following results are worth highlighting:

- The top priority for improvement for both large firms and SMEs is access to information about export opportunities. This reflects that exporters first need to be able to identify potential buyers before concerns about bottlenecks for the delivery of goods or services enter into the picture.
- The need for improvements in access to information on export opportunities has a significantly higher weight for SMEs (over 60% of responses) than for large firms (over 40%). More generally, the responses of large firms are relatively equally distributed across different aspects of trade costs, while the responses of SMEs are clearly concentrated around three top priorities.
- For SMEs, access to trade finance is the second most important priority for improvement and access to information about procedures and regulations is priority number three. For large firms, access to information about procedures and regulations weights second and improvements in tariffs fees and other charges weights third.

Figure 7.3 What are the three factors in which you would most value improvements: SMEs versus large firms



Note: SMEs are defined as firms with less than 250 employees. The chart reflects responses of 418 SMEs and 103 large firms.
Source: ITC Monitoring Survey (2015).

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- For both SMEs and large firms, costs related to access to information on processes and regulations are highlighted more frequently in the survey than costs to actually overcome regulatory burdens. This is in line with findings from more in-depth surveys on non-tariff measures conducted by the International Trade Centre [ITC] in recent years as described in the following section.

Exporters were also asked about the relevance of different aspects of border procedure facilitation for their performance. Questions and related explanations followed closely the terminology of the Trade Facilitation Agreement. Figure 7.4 illustrates the findings, again decomposed in findings for SMEs and findings for large firms. When it comes to border procedures, differences in views between SMEs and large firms are less apparent than in the case of the more general trade costs reported in Figure 7.4.

Large firms and SMEs identify the same four priorities when it comes to improvements in border procedures:

i. Publication and availability of information regarding clearance for exporting and importing is ranked first by SMEs and second by large firms.

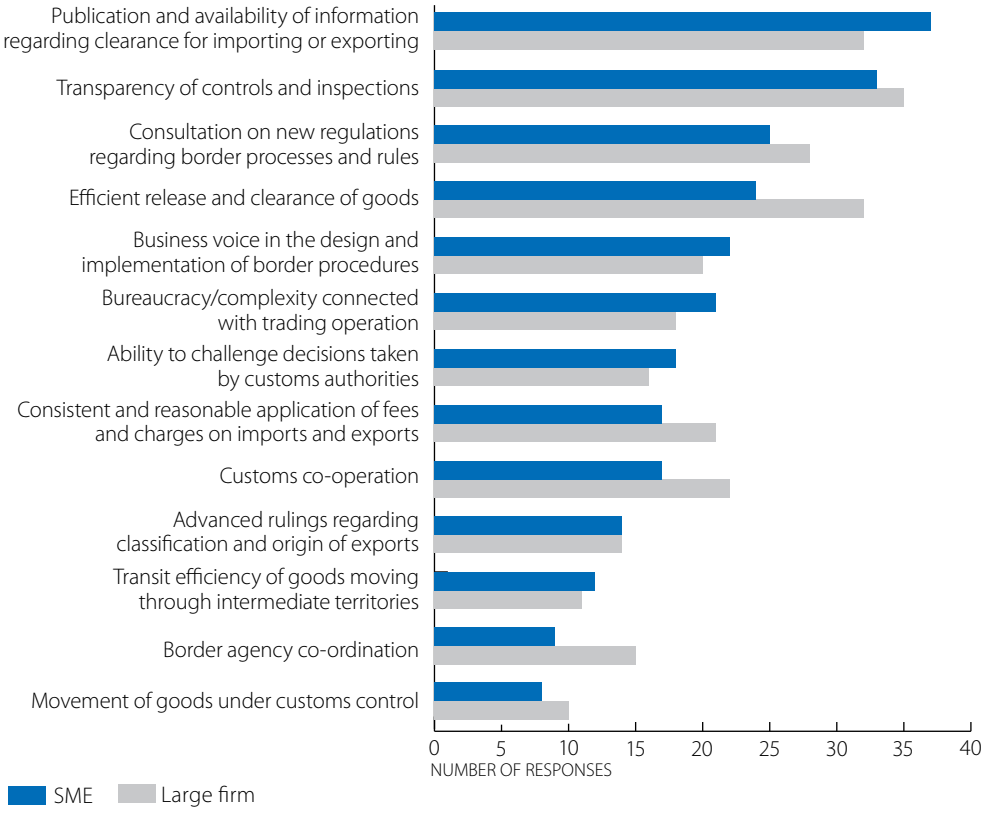
ii. Transparency of controls and inspections ranks second for SMEs and first for large firms.

iii. Consultations on new regulation regarding border processes and rules ranks third for SMEs and fourth for large firms

iv. The efficient release and clearance of goods ranks fourth for SMEs and second for large firms (with same number of responses for large firms as the option "publication and availability of information regarding clearance for exporting and importing").

It is also worth noting that strengthening the business voice in the design and implementation of border procedures ranks as a fifth priority for SMEs.

Figure 7.4 What are the three factors related to border procedures in which you would most value improvements?



Note: SMEs are defined as firms with less than 250 employees. The chart reflects responses of 418 SMEs and 103 large firms.
Source: ITC Monitoring Survey (2015).

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Non-tariff measures as obstacles to trade: a private-sector perspective

Recent decades have witnessed a significant reduction in tariff barriers to trade, notably thanks to different multilateral trade negotiation rounds and a multitude of regional and bilateral trade agreements. Trade barriers for manufactured goods, for instance, have decreased from an average of 40% at the end of the 1940s to an average of 4% in 2009 (Love and Lattimore, 2009).

Obstacles to trade, however, continue to exist but now take more frequently the form of non-tariff measures (NTMs). While some NTMs have been suspected of being of a protectionist nature, many of them are motivated by the increasing demand for protection of consumer health and safety and the environment, which translate into sanitary and phytosanitary measures, traceability requirements and other regulations. Some are also the consequence of the increased number of bilateral and plurilateral trade agreements, which, in the absence of a proper customs union, may lead to challenging rules of origin frameworks.

While NTMs are usually the same for all exporters, their impact can vary significantly across businesses. Compliance with regulations and certifications require specific suppliers and services (for instance, suppliers of non-toxic inputs and testing laboratories) that may not exist in close vicinity of some companies. In addition NTM-related costs often take the form of fixed costs and are therefore likely to affect SMEs disproportionally. It may even happen that standards increase the exports of large companies at the expense of exports of smaller companies, as shown by Anders and Caswell (2007) when assessing the effect of the adoption by the United States of the Hazard Analysis Critical Control Points (HACCP) standard on food imports.

TABLE 7.3 List of surveyed countries

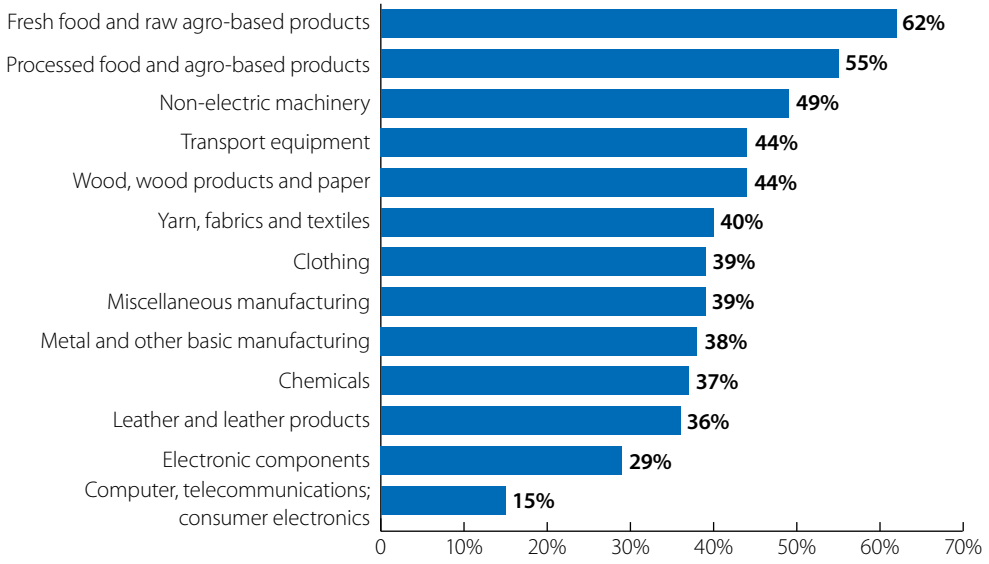
Sub-Saharan Africa	Middle East and North Africa	Asia	Latin America and Caribbean
Burkina Faso	Egypt	Bangladesh*	Colombia*
Côte d'Ivoire	Morocco	Cambodia	Jamaica
Guinea	State of Palestine	Indonesia	Paraguay
Kenya	Tunisia	Kazakhstan	Peru
Madagascar		Sri Lanka	Trinidad and Tobago
Malawi		Thailand*	Uruguay
Mauritius			
Rwanda			
Senegal			
Tanzania			

*Note: *Results for Colombia, Thailand and Bangladesh are not reflected in the analysis.*
Source: ITC (2015).

Assessing the trade effects of NTMs with traditional empirical methods and using trade statistics is notoriously difficult. To complement ongoing efforts in this direction, ITC has in recent years undertaken a series of comprehensive surveys to collect information about NTMs as perceived by companies in developing countries.

Information about NTMs has been classified based on the international taxonomy of NTMs jointly developed by a Multi-Agency Support Team (MAST) with minor adaptation to the context of a business survey. In addition to identifying the type of measure that is perceived as an obstacle, the survey identifies the institution that applies the problematic measure and whether the problem stems from the measure itself or from the procedure to demonstrate that the company complies with it. In the latter case, the NTM is classified as a procedural obstacle. The analysis below is based on data for 23 of the 26 countries for which data have been collected and processed (see Table 7.3). In total, 11 567 companies agreed to participate in phone screen interviews.

Figure 7.5 Exporters affected by Non-Tariff Measures-related obstacles, by sector



Source: How companies experience non-tariff measures – Survey-based evidence from developing countries, ITC (2015).

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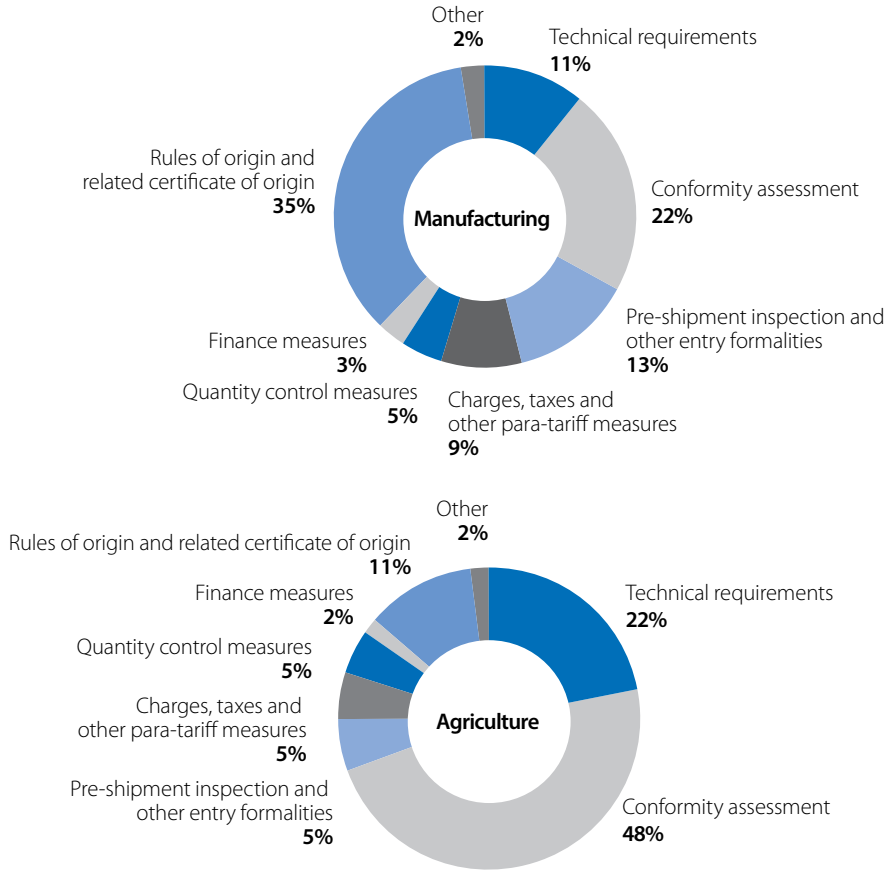
The evidence reported in Figure 7.5 suggests that fresh food and agriculture is the most affected sector on average in the 23 countries covered by the surveys, followed by the sector of processed food and agro-based products. Manufacturing sectors, notably electronic-related sectors, are less affected. The count of NTMs is based on the number of NTM cases reported by companies where issues related to different products or different measures reported by one single company have been considered as different NTM cases. When aggregating or averaging, individual countries have been given the same weight.

The type of burdensome NTMs also differs across sectors, as illustrated in Figure 7.6. Burdensome NTMs applied at the destination and reported by exporters of food and agro-based products primarily concern conformity assessments and technical requirements, while exporters of manufactured products are mostly affected by rules of origin.

Figure 7.6. Types of burdensome Non-Tariff Measures applied by partner countries by sector



Source: How companies experience non-tariff measures – Survey-based evidence from developing countries, ITC (2015).

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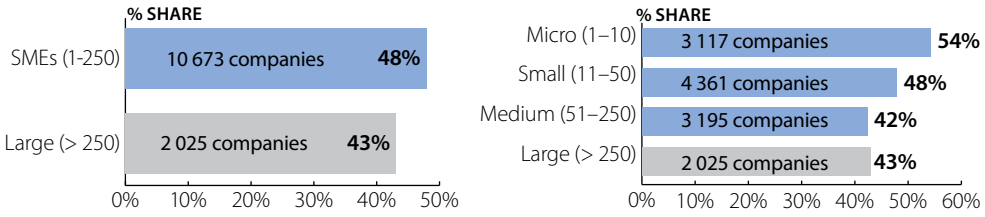
Figure 7.7 illustrates how the perceptions of NTMs differ according to firm size. The figure shows the percentage of firms of different size categories that reports at least one NTM as a trade obstacle. The left-hand panel illustrates that 48% of SMEs report that their business suffers from at least one NTM. This percentage stands at 42% for large firms. The higher figure for SMEs turns out to be mainly driven by micro and small firms as illustrated in the right-hand panel of the figure. A full 54% of micro-firms report they suffer from at least one NTM, and 48% of small firms do so.

Figure 7.7 Exporters affected by Non-Tariff Measure-related obstacles, by company size



Source: How companies experience non-tariff measures – Survey-based evidence from developing countries (a company is affected by NTMs if it reports at least one NTM-related obstacle), ITC (2015).

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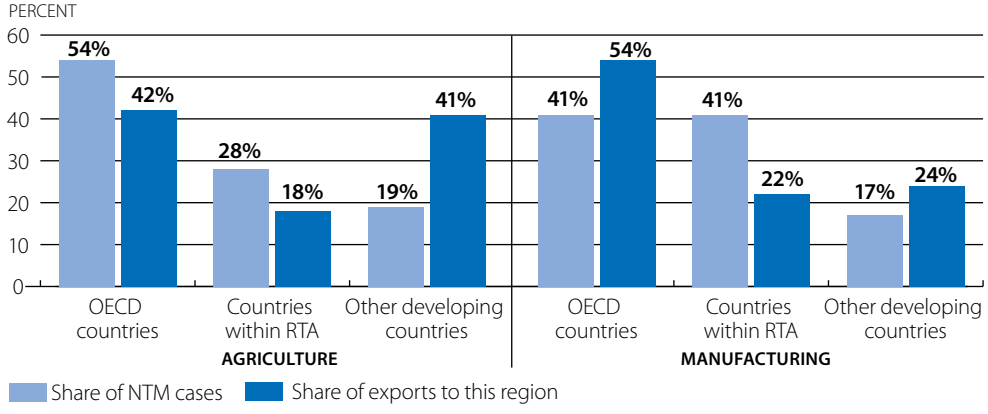
The survey responses of medium-sized firms, instead, are similar to those of large firms: 42% of medium-sized firms indicate that their business suffers from at least one NTM. In this context it needs to be highlighted, though, that the definition of medium sized applied in the chart does not necessarily correspond to what national definitions consider medium-sized. Indeed, in some of the survey countries – like Egypt, Malawi and Tanzania – companies with over 50 employees would be considered large.

Comparing the distribution of NTM cases by destination markets provides insights into the difficulty to comply with such measures in different markets. Figure 7.8 illustrates that the frequency of burdensome NTMs is highest for agricultural exports to OECD countries. This, however, partly reflects that OECD countries are also the main destinations of agricultural exports from the surveyed countries.

Figure 7.8 Share of cases of burdensome non-tariff measures versus share of exports across trading partners, by sector



Note: The bar chart plots for both the agriculture and the manufacturing sector the share of NTM cases for measures applied by partner countries against the estimated share of exports of the surveyed countries to their regional partners and the rest of the world (developing and OECD countries). Export shares are calculated excluding minerals and arms. Only NTMs reported by exporters are considered.

Source: How companies experience non-tariff measures – Survey-based evidence from developing countries (a company is affected by NTMs if it reports at least one NTM-related obstacle), ITC (2015).

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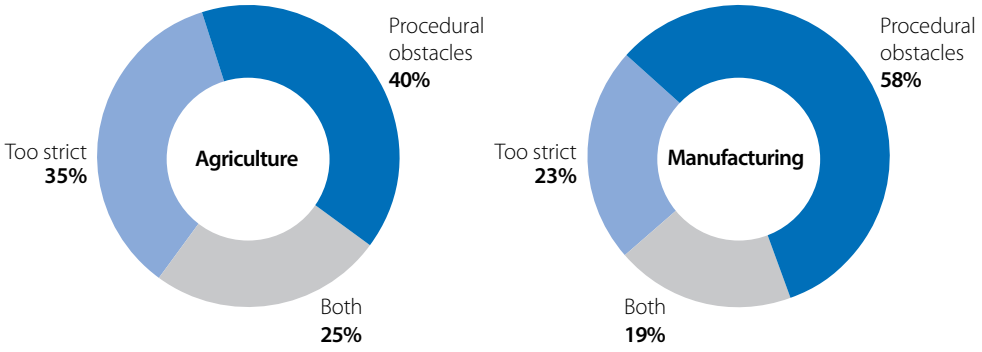
The most surprising finding in Figure 7.8 is probably the high incidence of burdensome NTMs among partners within RTAs. When taken proportionally to trade flows, NTMs are more frequently reported as a burden for exports to an RTA partner than for exports to an OECD partner. The difference is even more striking when comparing exports to RTA partner with exports to other developing partners. Trade with other developing partners is higher, but the incidence of burdensome NTMs is lower. These findings call for a deeper analysis of the design of NTM-related aspects of RTAs involving developing countries and of the implementation of those RTAs.

Implementation is indeed an issue as evidenced when looking into procedural aspects related to NTMs. When asked whether burdens from NTMs arise mainly because measures are too strict or because of procedural obstacles related to proving conformance with the NTM, procedural obstacles turn out to be more important than the design of NTMs. This is in particular the case in the manufacturing sector where 58% of firms report that NTM-related costs arise from procedural obstacles (Figure 7.9).

Figure 7.9 Reasons making Non-Tariff Measures burdensome for exporters, by sector



Note: The charts present the types of NTM-related obstacles faced by exporters of surveyed countries for agricultural and manufacturing products. It shows that 65% of NTMs on agriculture (left panel) and 77% of those on manufacturing products (right panel) are considered burdensome because of procedural obstacles.

Source: How companies experience non-tariff measures – Survey-based evidence from developing countries, ITC (2015).

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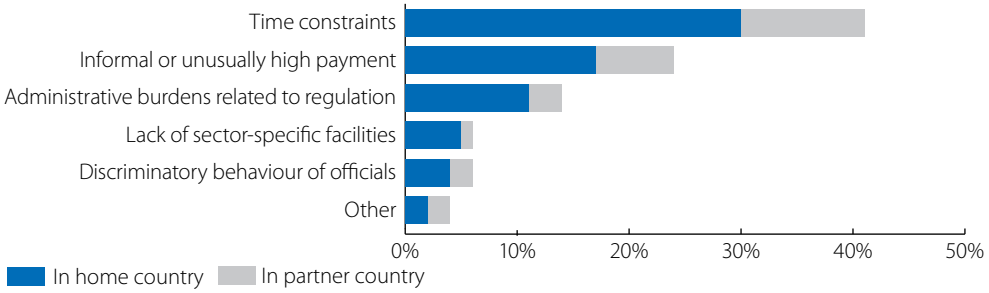
Survey answers make it possible to distinguish between NTM-related burdens originating within the exporting country and those originating in the partner country. Most procedural obstacles appear to originate in the exporting country as illustrated in Figure 7.10. Such obstacles are most frequently associated with time issues, payments and the administrative burden associated with NTMs.

Figure 7.10 Procedural obstacles related to Non-Tariff Measures



Note: The bar chart presents the types of procedural obstacles associated with the NTMs reported by surveyed countries' exporters (including both measures applied by the home country and those imposed by partner countries).

Source: How companies experience non-tariff measures – Survey-based evidence from developing countries, ITC technical paper (2015).

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ADDRESSING OBSTACLES TO TRADE FOR SMEs: FINDING THE BUYER

The discussion above has shown that exporters face a multi-stage challenge when trying to serve customers abroad. First of all, they need to be able to find buyers and to understand their demand. Indeed, access to information about export opportunities figures first as the most prominent factor in which exporters would value improvement. Only once hypothetical buyers have been identified, the challenge of actually delivering goods and services to those buyers becomes an issue.

The survey discussed below revealed that access to information about export opportunities is the factor in which enterprises most value improvement. This is in particular the case for small and medium-sized enterprises, as over 60% of SMEs indicated that improved access to information about export opportunities is their top priority.

Different private and public sector institutions have traditionally taken responsibility for providing access to export related information to producers. They will be referred to in the following as Trade Support Institutions. Their role is particularly important for pioneer exporters.

Trade Support Institutions: A myriad of different set-ups

Trade Support Institutions enable and encourage firms to engage with and survive in international markets. These institutions are typically export orientated, but as importation has become a key ingredient of successful trading the focus of TSIs has grown to cover all aspects of global trade including investment. The definition of TSIs covers many institutions which may differ immensely in function, form and funding. However, TSIs can be easily placed into one of three categories: general, sector-specific or function-specific (See Figure 7.11; Skidmore, 2013).

Figure 7.11 Description of Trade Support Institutions

Source: ITC (2013).

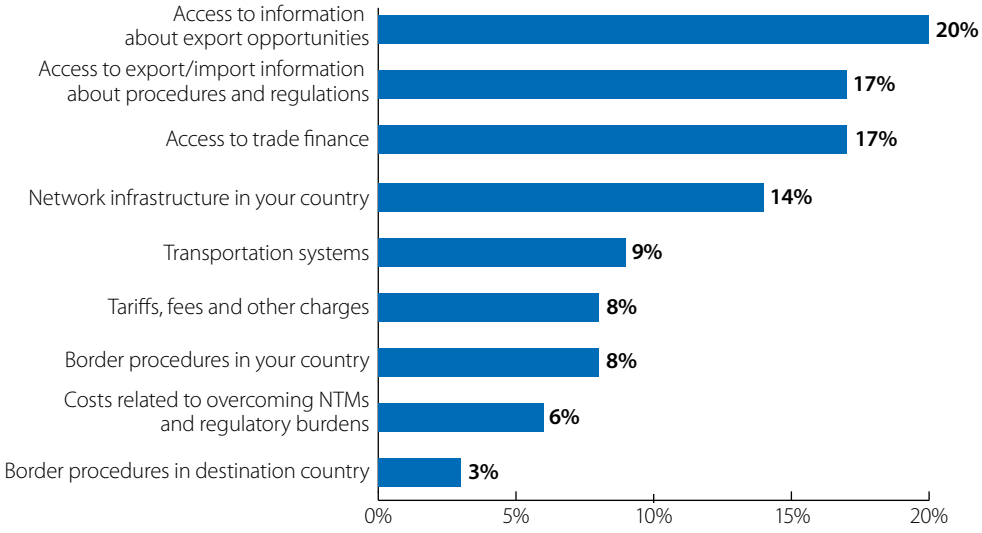
General TSIs include trade promotion organisations, investment promotion organisations, trade-related government ministries, chambers of commerce and economic development agencies. As such, they are some of the largest TSIs, with some of the widest mandates for promoting trade, and often derive their funding from public sources, even if the management of those funds are administered in partnership with the private sector. General TSIs are often portals for the latest market intelligence and also run technical assistance programmes. For example the International Trade Centre's Market Analysis Tools, which offers the latest information on standards and certification requirements, tariff and non-tariff measures, as well as trade flow data, helped to generate an additional USD 126 million dollars of exports in 2014 (See the aid-for-trade case story No. 54, "Market intelligence: ITC market analysis tools help generation of over USD 126 million dollars in goods and services exports").

Sector-specific bodies include exporter associations, trade associations, sector chambers and other sector-based bodies. They are typically smaller in size and scope than general TSIs but often provide highly specialised information and know-how on the sector concerned.

Finally, function-specific TSIs provide services which facilitate the actual process of exporting (or importing) for firms. Function-specific TSIs include export and credit financing bodies, standard and quality agencies, export packaging institutes, training institutions and trade and law arbitration bodies. In short, these TSIs may be seen as supplying services to the firm, or trust to foreign consumers and intermediaries, who may have little knowledge of the exporting firm or its product.

In a recent survey, carried out by the ITC for the Fifth Global Review of Aid for Trade, 24 TSIs were asked which three areas they would most value improvements in for their clients (Figure 7.12). The results show that access to information about export opportunities came top, followed by access to trade finance and access to information about procedures and regulations. In addition, TSIs were asked to identify the three most important articles in the Trade Facilitation Agreement (Figure 7.13). Publication and availability of information regarding clearance for import and export came first, with business voice and transparency coming second and third respectively.

Figure 7.12 Components of trade costs in which trade support institutions would most value improvements



Note: TSIs were asked ask to identify up to three factors they would most value improvements in.

Source: ITC Monitoring Survey (2015).

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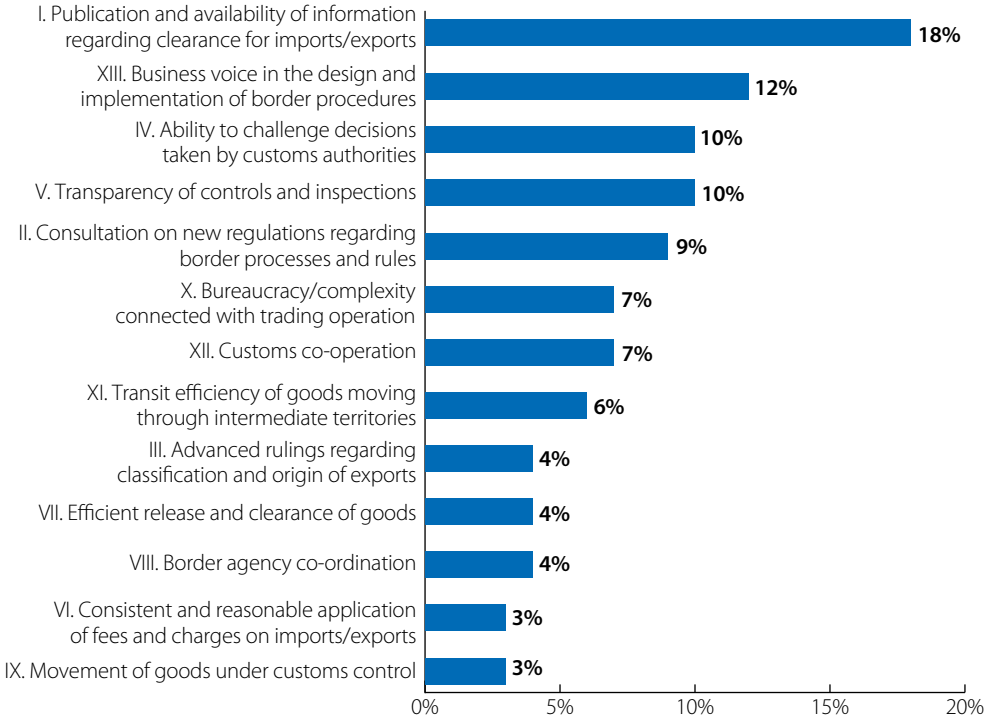
From these results, it is clear that TSIs are most concerned about market failures to do with lack of information. These findings are in line with those of a similar survey conducted by ITC among TSIs during its WTPO-conference in Dubai in October 2014. Since providing access to information is widely accepted as a public good, these results stress the importance of efforts by TSIs and technical assistance efforts trying to strengthen TSIs.

It is also striking that the answers provided by TSIs in this survey are very well aligned with the answers provided by private enterprises. This suggests that TSIs may well play a useful role as an intermediary between the private and the public sector, notably when it comes to contributing to the reduction of trade costs.

Figure 7.13 Factors related to border procedures in which trade support institutions would most value improvements



Note: TSIs were asked ask to identify up to three factors they would most value improvements in. Roman numerals indicate the relevant Trade Facilitation Agreement article.

Source: ITC Monitoring Survey (2015).

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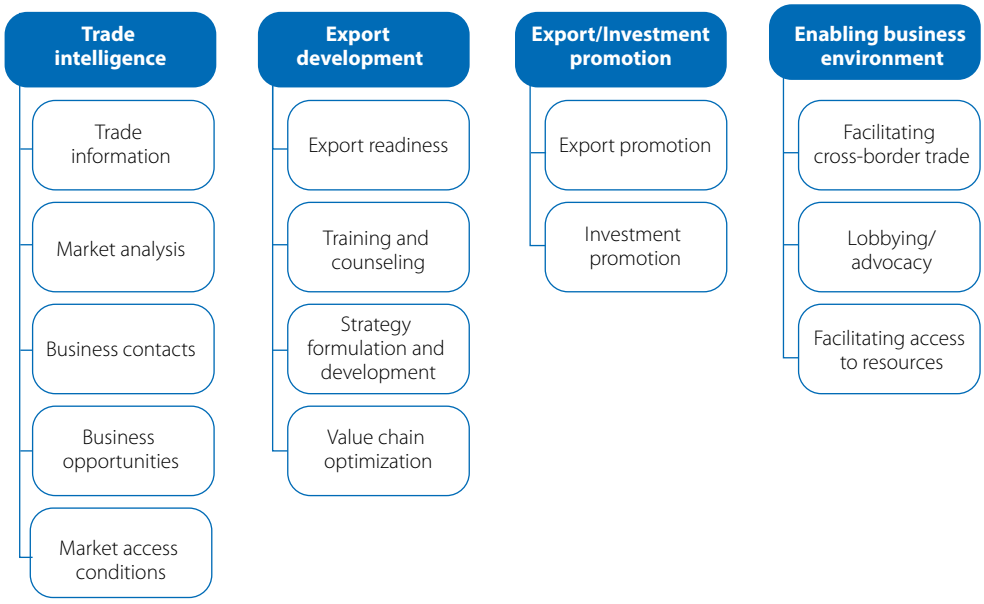
Providing access to information and assisting pioneer exporters

The economic justification for TSIs rests in the theory of asymmetric information, sunk costs for pioneer exporters and other market failures. Problems of asymmetric information arise from a firm's need to identify partners, suppliers and distributors. TSIs can help address this problem by facilitating forums and networks in which firms can easily identify suitable counterparts. Sunk costs in the context of pioneer exporters are costs associated with the gathering of foreign market information related to consumer preferences, business opportunities and quality and technical requirements, among other things. These activities require substantial investment, and the possibility of competitors acquiring this information directly or indirectly with little or no investment of their own acts as a deterrent to new entrants into export markets (see Roberts and Tybout, 1997). Therefore, TSIs often provide market intelligence as a public good, as well as providing a host of other services (see Figure 7.14 for an overview).

Since TSIs cover a wide range of institutions, it is difficult to assess their effectiveness. However, over the last decade, a number of studies have investigated the effectiveness of TSIs (e.g. Lederman, Olarreaga and Payton, 2006; Copeland, 2008; Lederman, Olarreaga and Payton 2009; Martincus et al. 2010). These studies tend to focus on a subset of trade support institutions, the so-called Trade Promotion Organisations (see Figure 7.11). A related branch of literature assesses the effect of foreign embassies and consulates (e.g. Rose 2005; Creusen and Lejour, 2013) on exports and finds significantly positive effects of the establishment of a first foreign mission in a country on bilateral trade.

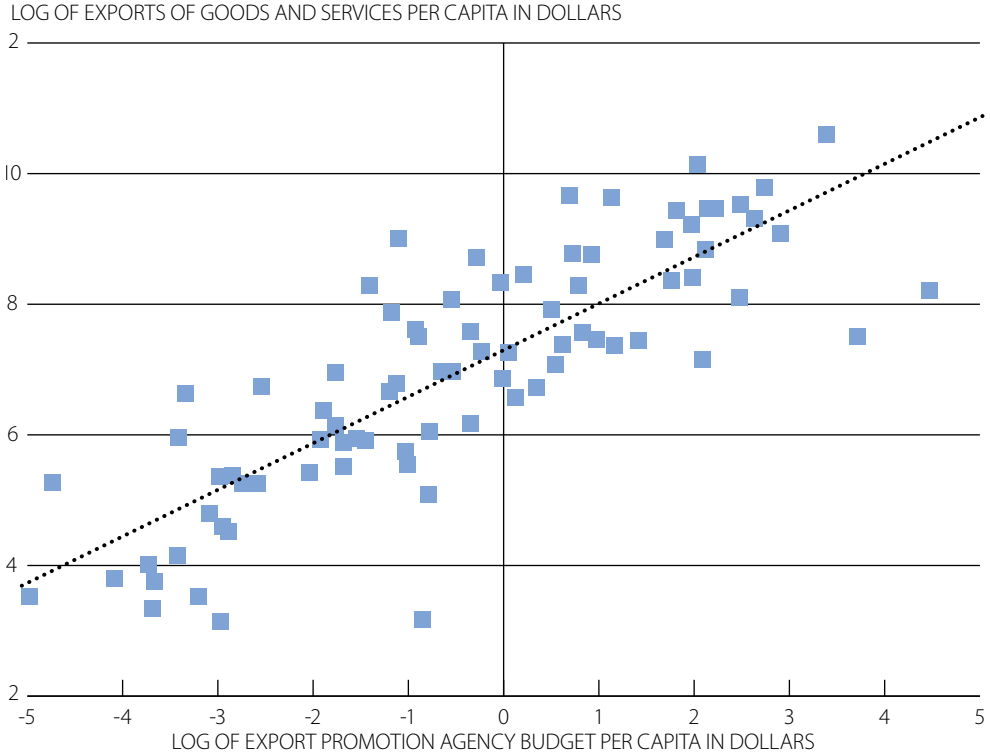
Figure 7.14 A list of services a Trade Support Institutions might offer



Source: http://www.intracen.org/itc/trade-support/developing-a-service-portfolio/

The study by Lederman, Olarreaga and Payton (2006) reveals a positive relation between the size of TPO budgets and exports (see Figure 7.15). Controlling for other effects that could drive the relation (e.g. per capita GDP), Lederman (2009) finds an inverted-U-shaped relationship between the size of TPO budgets and the marginal increase in exports. At the sample median, a USD 1 increase in TPO budgets is found to result in a USD 200 increase in exports.

Figure 7.15 Log of exports of goods and services per capita versus the log of TPO budgets per capita



Note: A simple linear trendline was used to indicate the positive reaction between the two variables.

Source: Lederman, Olarreaga and Payton (2006).

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A study of six Latin American countries between 2000-07 revealed that opening an export promotion agency office abroad translates into a an increase in exports that is approximately 5.5 times larger than enlisting a new embassy or consulate tasked with the same duty (IDB, 2010). The study also found that TPOs are far more effective when supporting the whole export process (see Figure 7.15).

Two challenges for TSIs that have been highlighted in the literature are the administrative set-up of the institutions and their decisions regarding firm level targeting.

The administrative structure of TPOs has been investigated in Lederman, Olarreaga and Payton (2006). TPOs, whose members share a large number of executive board positions with the private sector despite the organisations' public-sector funding, are associated with higher national exports than other combinations. In addition, a single and strong TPO seems to be more effective than multiple agencies with overlapping responsibilities (Lederman, Olarreaga and Payton 2006). The ITC's Assess, Improve and Measure (AIM) programme is designed to support TSIs, and in particular TPOs, to reform in order to boost their effectiveness (see the aid-for-trade case story No. 49, "Helping trade and investment support institutions AIM higher"). Over a five-year period, AIM will assist some 50 TSIs in better serving the needs of their clients.

Trade Support Institutions often have diverging approaches when it comes to what type of firm support is offered too. Some TSIs target small firms that are most in need of assistance, while others champion large firms to capture large profits. Small firms are typically responsible for the largest share of employment growth in most economies but often suffer from low productivity and poor product quality, among a host of other shortcomings. By contrast large firms are often the most productive. But they tend to be well financed, with ample resources and it can be considered questionable whether they are in need of public support.

A recent study on the long-term impact on exports of assistance from Tunisia's FAMEX matching-grant scheme by Fernandes and Mattoo (2014) points to a third way. When the firms which received assistance were divided into three categories – small (fewer than 20 employees), medium (20-99), and large (100 or more) – the results showed that after four years, exports of small firms declined by 65%, while exports of large firms were only 6% higher. However, the exports of medium-sized firms increased by 57%. This may be because medium-sized firms are often on the verge of breaking into foreign markets, requiring just a nudge to achieve their goal, which TSIs are well positioned to apply.

ADDRESSING OBSTACLES TO TRADE FOR SMEs: DELIVERING TO THE BUYER

Once potential markets have been identified, producers need to identify and assess what it requires to actually deliver to those markets. This implies assessing challenges related to organising transport and possibly to organising trade finance, two aspects that are being assessed in aid-for-trade surveys enquiring about trade costs.

In the following, the focus will be on challenges related to NTMs, admittedly only a subset – albeit an important one – of trade costs. Not all of the NTM-related trade costs captured by the surveys discussed fall under the standard concept of border costs. In order to adjust production processes to specific NTMs, costs falling on the producer, for instance, do not occur at the border. Yet they are costs that are incurred in order to trade, as they form part of a chain of challenges producers have to overcome to comply with NTMs abroad. Addressing such costs, therefore, forms an important component of trade-related technical assistance.

NTM-related challenges will be discussed following the order in which producers face these challenges when attempting to bring a good or services to a foreign market:

- They need to find out about requirements to be met in order to export to consumers abroad. This is an information challenge and has been highlighted in the survey responses as the third most important factor in which firms would value improvement.

- They need to adapt products and processes in order to comply with requirements, be they government imposed regulations or private standards.
- They need to demonstrate compliance, which typically implies that products need to be certified by recognised bodies and processes (e.g. inspection, testing and certification), and certification needs to be proven at the border, which may lead to procedural obstacles of the type highlighted in the survey evidence discussed in section 3.

At each stage of this process, exporters may face obstacles either with respect to their own capacity to handle the obstacle or with respect to the relevant institutional or policy environment. When it comes to NTMs, the relevant institutional environment is not only situated at the border but consists to a large extent of the technical infrastructure required to test and prove compliance with regulatory measures.

The nature of different types of obstacles is described below, together with the types of policies or interventions that exist to address these obstacles.

Access to information about product and service requirements

Important efforts exist at national and international levels to collect and disseminate information on NTMs. As mentioned previously, a major inter-agency initiative titled MAST has led to the creation of an international taxonomy of NTMs and has facilitated the publication of country-level data on non-tariff measures in the so-called TRAINS (Trade Analysis and Information System) database. This database contains information on relevant national legislations and is publicly accessible. In parallel, data are being collected and disseminated on firm level perceptions of NTMs. Those initiatives involve major and often costly data collection exercises. They are supported by the international donor community and contribute greatly on increasing transparency on the nature of NTMs.

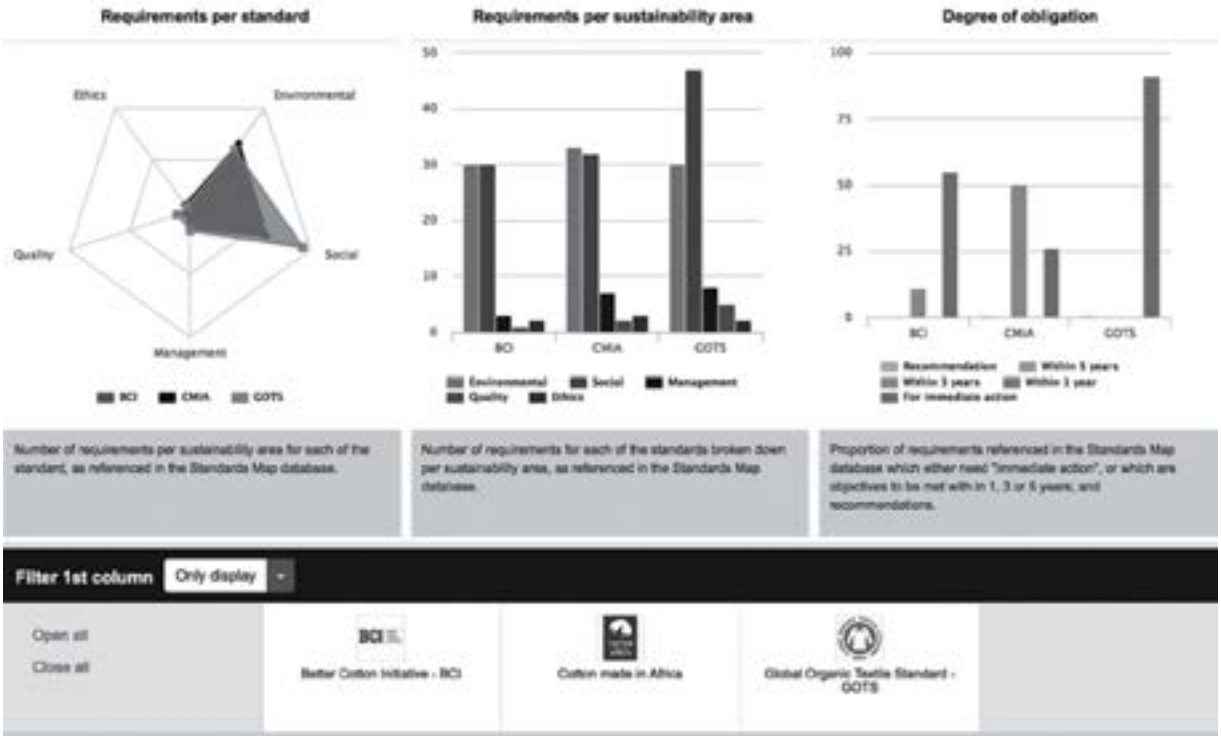
Figure 7.16 Voluntary sustainability standards: a snapshot

Source: ITC.

Similar exercises now also exist in the context of voluntary standards. NTMs are generally associated with compulsory regulations imposed by authorities in destination markets and by exporting countries. In addition to those official regulations, companies often have to comply with other standards if they want to reach markets. Voluntary standards are issued by governments, international private bodies (i.e. companies, NGOs, etc.) and sector associations. Complying with some voluntary standards may often be a *de facto* requirement to actually sell to some large retailers, while other standards cater to niche markets. Given the high number of private standards currently relevant for international trade, they can significantly add to the trade costs caused by national regulatory measures. Figure 7.16 provides a snapshot of a subset of voluntary standards, so-called voluntary sustainability standards and gives an impression of the incidence of voluntary standards

The role relatively straight-forward information tools can play in enhancing transparency in the jungle of voluntary standards illustrated in Figure 7.16 is explained here with reference to an ITC online tool – Standards Map (www.standardsmap.org) – that is dedicated to this transparency objective and provides information on over 160 voluntary sustainability standards (VSS). In addition to being a platform providing detailed information about standards, certification bodies, certification cost and countries where such standards operate and are recognised by companies and consumers, the tool also allows exporting companies to self-assess their performance in relation to various standards' requirements (see Figure 7.17). The Standards Map can also be used by buying and selling companies interested in comparing levels of VSS requirements of across several dimensions: the environment, social aspects, management, quality and ethics.

Figure 7.17 Comparison of cotton standards using ITC Standards Map



Source: ITC Standards Map, 2015.

In a context of multiple and increasing VSSs that are often similar on a range of criteria, brands, retailers and standard organisations can also use the Standards Map to facilitate the convergence of criteria. Thus, suppliers and buyers can take advantage of these VSS commonalities to drive more rationality and cost and time savings via joint audits and certifications.

Firm-level capacity to meet regulatory and standards-related requirements

Firms often need to build in-house capacity and/or to buy relevant equipment to meet regulatory or voluntary standards-related requirements. Such investments are costly and may also entail risks, notably the risk of building capacity in vain and not managing to export. Evidence exists that linking up to GVCs can reduce transaction costs and risks. Buyers within the chain often transmit know-how to suppliers and guarantee a certain level of sales if standards are met. Such assistance, however, does not come for free, as suppliers often end up accepting lower sales prices in return for reduced transaction costs (Iacovone et al., 2015).

Where private initiatives do not exist, technical assistance efforts are sometimes directed towards building relevant capacity. Such efforts often explicitly target SMEs and typically take the form of hands-on field projects directly working with SMEs. Numerous examples exist of aid-for-trade projects working directly with companies in developing countries to help them comply with NTMs and regulations. Frequently, such projects target the agricultural sector or the food processing industry, and in these cases the projects may take place under the umbrella of Standards and Trade Development Facility (SDTF).

With the Nigeria Export Promotion Council, the ITC implemented an STDF project to expand Nigeria's food exports of sesame seeds and shea nut butter through improved SPS capacity-building of private and public sector organisations and improved quality control along the supply chain.

Another project was financed by the European Development Fund and operated by the Horticultural Technical Center of Tamatave in Madagascar to develop the production of lychees and help them comply with European Union food safety regulations (see aid-for-trade case story No. 45, "Appui à la filière litchi de Madagascar"). This project started in 2001 and lasted for five years. Trade data reported by Madagascar reveal that lychee exports to Europe were strong throughout the duration of the project and then dropped. Exports started to rise again in 2010.

Yet another project, implemented by the ITC, focused on the cultivation of Sacha inchi, a native plant of Peru that can be used to produce comestible oil (see aid-for-trade case story No. 56, "US safety certificate could quintuple Peru's exports of indigenous food product"). The project, operated by the ITC trade and environment programme, was aimed at helping SMEs, as well as supporting biodiversity-based exports. Apart from providing technical support to producers, the ITC helped them prepare a submission to obtain Generally Recognized as Safe (GRAS) status from the US Food and Drug Administration. This status was obtained in 2014 and is expected to significantly increase demand for the product by US companies.

The need for commensurate technical infrastructure at the national level

In order to export producers need to demonstrate compliance, which typically implies that products need to be certified by recognised bodies, often laboratories, and processes (e.g. inspection, testing and certification). An accredited laboratory is one that is recognised as being competent. Accreditation of laboratories is carried out by authorised national bodies in various countries by examining laboratories' competence with respect to requirements given in ISO/IEC 17025 (the general requirements for the competence of calibration and testing laboratories). The compliance of a laboratory with ISO/IEC 17025 provides assurance of its competence.

Lack of acceptance or recognition of foreign test reports can represent a very serious barrier to trade. Whether the test report furnished by an exporter/manufacturer will be accepted overseas depends on each market and each regulator. This must be determined by the exporter/manufacturer prior to seeking entry to a particular market and forms part of the procedural obstacles captured in the NTM surveys.

Through Swiss-financed projects implemented by the ITC, laboratories for testing food and agricultural products in Tajikistan have be accredited to ISO/IEC 17025, and the Kyrgyz Centre of Accreditation (KCA) has become a signatory to the International Laboratory Accreditation Co-operation (ILAC) Mutual Recognition Arrangement (MRA). KCA is now a full member of ILAC in terms of accreditation of testing laboratories for compliance with ISO/IEC 17025. ILAC accreditation helps SMEs to reduce costs as it removes the need for repeated tests in another country by allowing selection of competent certification services that can save them both time and money.

While accreditation is sufficient for the recognition of competence at national level, MRAs are necessary to achieve recognition across borders. Mutual recognition agreements/arrangements (MRAs/MLAs) are formal agreements between accreditation bodies that acknowledge that the accreditation of laboratories and certification bodies granted by all parties to the particular agreement is equivalent. This is one of the areas in which international collaborative efforts can contribute to facilitating trade. Another area concerns collaboration on reducing procedural obstacles to trade as discussed below.

Addressing non-tariff barriers and procedural obstacles for more efficient cross-border processes

NTM business surveys discussed above highlight the relevance of procedural obstacles in the context of NTMs. Solutions to reduce such obstacles can be found through improved inter-agency co-ordination, simplified documents and procedures, enhanced transparency and predictability and by reducing charges and fees. Evidence suggests that these reforms are most impactful when designed, implemented and monitored in co-ordination with business through public-private mechanisms. It is important to include SMEs in the dialogue process for making the process inclusive and results comprehensive. Indeed, SMEs expressed the importance they attach to their voice being heard in the private sector survey.

It is not a coincidence that these principles and reforms are embedded in the WTO TFA. By imposing binding obligations on all WTO members to improve efficiency of border procedures, the TFA provides a unique opportunity to reduce trade transaction time and costs and increase SMEs' participation in global trade. Facilitating trade procedures, especially in developing and LDCs, will enhance SMEs' international competitiveness in regional and international markets and increase their integration in GVCs.

Promoting inter-agency co-ordination

The lack of co-ordination among agencies involved in the end-to-end trading process has been one of the most common causes of delays in administrative and compliance procedures. As traders need to work individually with a high number of different border agencies, their lack of co-ordination means applications and documents must be submitted and follow up ensured with each one separately. These human and financial resource-intensive procedures are costly for the government agencies as well as for traders, particularly SMEs, and result in increased international transaction costs.

Several measures that aim at improving border agencies co-ordination may be introduced. In addition to the establishment of a national trade facilitation committee (NTFC), the TFA drafters have included the requirement for co-operation among border regulatory agencies at a national level and co-ordination with neighbouring countries' border agencies to synchronise and harmonise activities with one another to facilitate completion of cross-border transactions. Co-ordination includes nominating a single-lead implementation agency, aligning procedures, formalities, working days and hours and developing and sharing common facilities (including joint border controls), also known as one-stop border posts.

Enhancing transparency and predictability

Lack of transparency and predictability on cross-border regulations and requirements leads to additional delays and costs for traders. The absence of updated information on trade processes, frequent changes in regulations or requirements different to what is published are common burdensome issues faced by SMEs. This becomes more pronounced in cases where enterprises operate in geographically-dispersed locations, without regular access to customs and border-control officials.

The TFA provides for more transparency and predictability for the benefit of traders. Exporting and importing businesses can obtain all trade-related information via multiple channels (e.g. print and online). Additionally, members are required to maintain enquiry points to enable traders to obtain documents and forms, understand procedures and get their queries answered. In this context it may be possible to gather spillovers from the international data collection efforts described above. The introduction of advance rulings, providing binding customs decisions prior to goods arrival at the border on tariff classification and origin, is a key tool in enhancing the predictability in customs procedures and ensuring uniform treatment of traded goods at the border.

Simplifying documents and procedures and reducing charges and fees

Complex documentation requirements and procedures involved in the trading process impose a significant burden on exporters. In some cases, traders and particularly SMEs lacking the human resources capacity have no other option than incurring the additional costs of hiring customs brokers to complete the complex requirements and reduce the occurrence of delays due to incorrect documentation. Furthermore, unusually high fees and charges and delays associated with receiving certificates and licenses is another common complaint by traders and prevents many SMEs from entering export markets. There is a perceived lack of transparency on the fees being charged and often informal payments are included in the final amounts.

These problems may be addressed by introducing a number of trade facilitation reforms. WTO members are required to establish a single-window system, a unique entry point through which traders may submit information and documents for all agencies involved in the trading process. These agencies co-ordinate with one another and submit their responses back through the same system and at the same time, and they must accept copies of certificates and licenses issued by other national agencies. This reform makes it easier for the traders to follow up with a single entity and reduces the likelihood of delays due to arranging and filing of duplicate information.

Members are further required to periodically review their trade procedures and documents with a view to decreasing complexity and applying them uniformly at all border locations. Governments should also aim at aligning national cross-border procedures to international standards for harmonisation and implication purposes. WTO members must also publish all fees and charges and establish mechanisms to periodically review them to reduce the number and diversity and limit them to the costs of services rendered. Additionally, with the introduction of electronic payments, the TFA aims to create an environment that increases the transparency on the fees being charged and reduces the occurrence of informal payments.

The ITC's recently launched Trade Obstacle Alert Mechanism illustrates how modern information technologies can be used to identify complexities in trade procedures and address them. The mechanism follows on from NTM surveys and consists of an online platform allowing companies to report obstacles they face in their trading operations. A national focal point is in charge of validating reports and directing them to the appropriate public body and sending the answer back to the company. The existence of an external entity ensures that requests are addressed in a timely manner. The mechanism is currently operational in Côte d'Ivoire and has already led to a reduction in the time and costs of trading.

CONCLUSIONS

Trade costs can take multiple forms and require different types of interventions to address them. Evidence obtained from private sector surveys and discussed in this chapter has led to the surprising finding that access to information and procedural obstacles represent among the most pressing obstacles to trade. This comes as a surprise in today's era of information technology and computerisation. Yet it also implies that addressing these obstacles is relatively straightforward and not overly costly.

The nature of the obstacles also suggests that addressing them may have strong impacts on SME integration in global markets. Access to information is more frequently mentioned as a priority obstacle by SMEs than by large firms. Indeed, the costs of information burdens may be relatively small in the view of most large enterprises but may be prohibitively large for SMEs.

Trade Support Institutions have traditionally played an important role in providing trade-related information, in particular information related to export opportunities. Given the relevance of informational obstacles, strengthening the capacity of TSIs to provide relevant and tailored information to their clients could become an important component of a future aid-for-trade agenda.

Modern technologies, in principle, also offer relatively cost-effective solutions to facilitating and streamlining border transition processes. The most suitable design of such solutions and their actual implementation may differ across countries. Strengthened communication and, where possible, collaboration between the private sector and the public sector can greatly contribute to finding the most suitable solutions and implementing them in a business-friendly way. The current international momentum arguably offers a unique opportunity for WTO member states to launch the relevant dialogues with the private sector in their countries and initiate the implementation processes of trade facilitation reforms.

In addition to the public sector, the private sector has an important role to play in the trade facilitation reforms implementation processes. Public-private dialogue (PPD) is particularly suited for identifying policy priorities, reducing regulatory costs and building consensus on the reforms needed. PPD helps to ensure reforms are demand-driven and in line with the needs and priorities of the main stakeholders, including SMEs. It is worth mentioning that private-sector involvement is required at all stages: needs assessment, priority identification, trade facilitation solution design, policy formulation and implementation and post-reform monitoring and evaluation.

Trade facilitation negotiators have chosen to retain this rationale by including a series of measures for involving private sector representatives in trade policy formulation. WTO members are obliged – and the private sector is expected to participate – to hold consultations before amending or introducing trade-related regulations, to provide the opportunity to comment on draft legislation, and to provide for a notice period between publication and entry into force of new or amended regulations in order to allow stakeholders to become acquainted with them. In addition to holding regular consultations between traders, government agencies and other stakeholders to achieve their common objectives, the Agreement includes a binding obligation for all WTO members to establish or maintain an NTFC, which aims to facilitate both domestic co-ordination and implementation of the provisions of the Agreement.

From the perspective of customs, SMEs are seldom a preferred client on account of the fact that their trade transactions are less frequent and their contributions lower. For this reason, they sometimes face specific difficulties and discriminations completing cross-border procedures. These discriminatory measures include, in certain countries, regulations that forbid SMEs to use the cross-border fast tracks or any other trade facilitation initiatives dedicated only to larger corporations. The TFA contributes to reducing discrimination towards SMEs, notably by forbidding the use of criteria that may be discriminatory towards SMEs (e.g. based on size of company or quantity of goods), which may prevent them from taking full benefit of all trade facilitation measures.

National efforts should also go in the direction of ensuring SMEs are fully included in the public-private dialogue mechanisms that are being set up under the auspices of the TFA. This would not only be fully in line with the spirit of the TFA but also with other policy initiatives at the global level, namely those taking place in the context of the B20 SME & Entrepreneurship Task Force, which was established in 2014.

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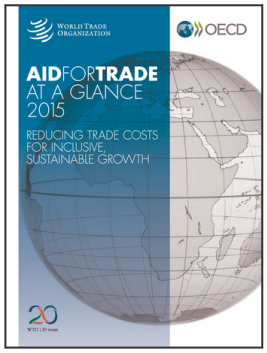

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