

## A STRATEGY FOR TRADE AND DEVELOPMENT

Development lies at the heart of trade; whether between nations or among local communities, trade has long been a way to enhance capabilities and spur growth. Countries that are more open to trade grow faster, have higher gross domestic product (GDP) per capita,<sup>1</sup> and have higher rates of job creation. Unlocking this potential requires approaches to trade that are win-win and balance the needs of importing and exporting countries. US trade preference programs are one example of a balanced, mutually beneficial approach to trade that promotes national security, jobs, and diplomacy.

Trade preference programs create greater opportunity for trade with developing countries, provided that certain standards on labor, intellectual property rights (IPR), and rule of law are met. They also promote labor standards, international human rights, and democratic values abroad, contributing to global security. For developing countries, the preference programs provide important access to the US market and promote a transparent business climate that is good for investors and local enterprises alike. Critically, the preference programs can help increase inclusive economic growth, reduce poverty, enhance food security, and support gender equality in developing countries. By raising their level of development and capacity to trade, developing countries that use the preference programs can grow to become important allies and build bridges to a more robust trading partnership with the US.

A strong commitment to maintaining trade preference programs can help ensure that the US remains at the forefront of global trade trends and that benefits continue to go to American consumers, producers, and small and medium-sized enterprises (SMEs). At the cornerstone of all US trade preference programs is the Generalized System of Preferences (GSP) program, which has been in place since 1974 and has been a pillar of US foreign policy for nearly a half a century. GSP covers 120 countries, and it provides the foundation for all other US trade preference programs, including those with the Caribbean nations, sub-Saharan Africa, and Haiti. All preference programs are linked to GSP; when GSP expired in 2013, small businesses faced administrative uncertainty under another preference program, the African Growth and Opportunity Act (AGOA), due to the interdependency of the preference programs.

For the US, trade preference programs support tens of thousands of jobs, supply US manufacturers with lower-priced inputs needed for establishing and expanding manufacturing within the US, and provide US consumers with a wider variety of consumer products at more affordable prices. The programs especially benefit US SMEs, who rely on duty savings from imported inputs to stay competitive, expand production, create jobs, and bring benefits to American workers. It is estimated that GSP saved US companies \$729 million in 2016, which translated into new jobs and expanded production in the US. GSP does not create competition with US manufacturing, and three-quarters of GSP imports are raw materials and intermediary inputs used by companies to manufacture finished goods in the United

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<sup>1</sup> Dollar, David, and Aart Kraay. 2004. "Trade, Growth, and Poverty." *The Economic Journal* 114: F22-49.

States. Further, a 2006 US Chamber of Commerce study highlights that approximately 80,000 jobs in the United States are associated with moving GSP imports from the docks to American farmers, producers, and end consumers.<sup>2</sup> A number of other US jobs are connected with trade preference programs, such as jobs in design, distribution, and IP-related sectors. These jobs keep the US competitive and put less pressure on other policy areas, such as foreign aid and immigration.

Despite its strengths, GSP has been plagued by short extensions and gaps in the program, which undermine the benefits to US stakeholders and constrain relationships with developing markets. This white paper will present four key recommendations for improving trade preference programs in order to make sure that they deliver to their full potential, yielding the greatest benefits possible to American SMEs and consumers as well as the poorest of the poor in developing countries: (1) Keep preference programs in place long enough for markets to develop and jobs to result; (2) Remove statutory prohibitions and cover products that are most central to development; (3) Better integrate trade preference programs with global supply chains; and (4) Establish a more comprehensive, coordinated approach on trade and development that is centered on rule of law and market development potential.

**Enhancing Trade Preference Programs as a Pillar of Trade and Development<sup>3</sup>**

<p>Increase Duration of Preference Programs to Ensure that Benefits Vest</p>	<ul style="list-style-type: none"> <li>• GSP has been prone to stops and starts. Increased duration would allow enough time for investment to take hold, as developing even the simplest supply chain can take a minimum of ten years.</li> <li>• A longer timeframe for preferences would provide predictability and certainty for US manufacturers and consumers, who rely upon the program’s cost savings, as well as investors who rely upon the inputs and reduction in commercial risk.</li> <li>• When GSP lapsed between 2013-2015, companies in California alone paid nearly \$200 million more in taxes (\$1.3 billion total for the US as a whole).<sup>4</sup></li> <li>• Increasing the duration of GSP would also help make all US trade preference programs work more efficiently – when GSP last expired, small businesses faced administrative hurdles under AGOA. Like GSP, AGOA directly creates US jobs, and estimates indicate that over 100,000 US jobs have resulted from AGOA alone.</li> </ul>
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<sup>2</sup> “Estimated Impacts of the US Generalized System of Preferences to US Industry and Consumers.” US Chamber of Commerce. 1 November 2006. Web. 23 May 2017.

<sup>3</sup> These recommendations reflect a trade and development initiative led by New Markets Lab (NML) that included representatives of U.S.-based non-governmental organizations (NGOs), members of the business community, economists, and trade experts. The fourth recommendation also draws upon work done by NML on trade, development, and rule of law.

<sup>4</sup> “GSP State Reports.” Coalition for GSP. Web. <http://renewgsptoday.com/gsp-state-reports/>.

<p>Cover Products Critical for Development</p>	<ul style="list-style-type: none"> <li>• Products like apparel, agriculture, and footwear are particularly central to development and global supply chains, as well as important avenues for women to participate in the formal labor force.</li> <li>• Removing statutory prohibitions and considering comprehensive product coverage, which would make it possible to conduct more tailored administrative reviews of product coverage under GSP, would allow US investors to sustainably manage supply chains and avoid becoming too centralized or dependent on one supplier.<sup>5</sup></li> <li>• Unlike other preference programs like the EU GSP+ and Everything But Arms, the US GSP program does not cover products that are most critical for development. Inclusion of these sectors would support growth for US SMEs and American consumers and enhance job creation.</li> </ul>
<p>Better Integrate Trade Preferences with Global Supply Chains</p>	<ul style="list-style-type: none"> <li>• Trade is increasingly critical for global supply chains, but not enough attention is paid to trade in intermediate goods, which are of increasing significance to both developing and developed countries.</li> <li>• Complex rules of origin (ROO) are critical to supply chain management and can place an undue burden on companies and customs officials alike. While the 35 percent ROO threshold in GSP could be maintained, providing more flexible cumulation rules, particularly among preference programs, and removing the cap on US inputs would enhance market development opportunities, including in regional markets.</li> <li>• Advanced developing economies are important links in the global supply chain, and preferences have been a step towards reciprocal two-way trade with many more advanced developing country trading partners.</li> <li>• Modernizing trade rules, such as labor provisions, in line with bipartisan principles and considering approaches like GSP+ would enhance the effectiveness of preferences to more fully reflect the realities of modern supply chains and create a bridge to more robust trading partnerships between the US and developing countries.</li> </ul>
<p>Build Bridge Between Trade Preferences, Rule of Law, and the Business Enabling Environment</p>	<ul style="list-style-type: none"> <li>• Trade preference programs should ultimately be part of a more comprehensive approach designed to deliver mutually beneficial, two-way trade and investment based on sound market principles and rule of law.</li> <li>• Preferences can act as a bridge to deeper trade engagement and a sound business enabling environment, particularly when coupled with trade capacity building and a “building block” approach to regulatory change and effective enforcement of laws.</li> </ul>

<sup>5</sup> For example, the 2015 H.R. 681 GSP Update Act allowed certain travel articles to be removed from statutory exclusion since they are no longer import-sensitive to US industries. Instead of amending tariff rates, the bill granted certain goods access to the annual GSP eligibility review process. A similar approach is reflected in the H.R.2735 bill introduced this year.

## THE IMPORTANCE OF TRADE PREFERENCE PROGRAMS IN THE US AND ABROAD

History and experience have proven that trade preference programs are beneficial, not only for the developing countries that receive preferences, but also for the developed countries that offer them. These programs are a win-win rather than a zero-sum game, and strengthening them has the potential to drive global economic prosperity, including for least developed countries (LDCs), which do not have the capacity to negotiate and implement more complex trade agreements.<sup>6</sup> For developing countries, preference programs play an important role in enhancing economic growth potential, alleviating hunger, improving labor conditions, and promoting gender equality. For the US, preferences can be a way to lower the cost of inputs and level the playing field in developing markets, enhancing opportunities in the US market and creating jobs. Preference programs like GSP also promote stronger labor conditions and international human rights, advance democratic values abroad, and maintain US national security interests in developing countries. Particularly when coupled with targeted capacity building and rule of law initiatives, trade preference programs act as a significant catalyst to equitable growth and become a bridge to sustainable two-way trade. With GSP set to expire at the end of 2017, it is time to look critically at how the program could best be shaped to meet these goals.

Global development cannot occur due to trade preference programs alone, however. In order to achieve balanced, sustainable, and inclusive growth and promote mutually beneficial, two-way trade and investment, it is important that trade preferences be complemented by a greater focus on rule of law, the business enabling environment, and capacity building and infrastructure development. Efforts to improve trade facilitation, which encompasses the rules and procedures that apply when a good crosses a border, could have a significant impact on improving the business enabling environment. According to the World Bank “every one dollar spent on trade facilitation in developing countries yields a return of 70 dollars,”<sup>7</sup> displaying the real economic impact that addressing supply-side constraints can have.

Trade preference programs are written into law by Congress and allow for duty-free exports from selected developing countries to the US market. These programs allow for both the US and beneficiary countries to benefit. Beneficiary countries gain greater access to the largest consumer market in the world, contributing to their growth, and American consumers and producers alike save in costs and gain from a more equal trade environment. In addition to the most longstanding and foundational trade preference program GSP, US trade preference programs include the African Growth and Opportunity Act (AGOA), the Caribbean Basin Trade Partnership Act (CBTPA), and the Haitian Hemispheric

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<sup>6</sup> Froman, Michael B.G. “U.S. Trade Preference Programs: Reducing Poverty and Hunger in Developing Nations through Economic Growth.” Office of the U.S. Trade Representative. June 2016.

<sup>7</sup> “Trade Facilitation.” *World Trade Organization*. WTO, [https://www.wto.org/english/news\\_e/brief\\_tradefa\\_e.htm](https://www.wto.org/english/news_e/brief_tradefa_e.htm).

Opportunity through Partnership for Encouragement Act (HOPE Act). There are 120 countries and territories that currently participate in the US GSP program, 17 eligible beneficiary countries within CBERA, and 38 eligible beneficiary countries within AGOA.<sup>8</sup> In 2015, those three programs comprised about \$212 billion worth of goods, of over \$2 trillion total US imports.

First supported by the United Nations Conference on Trade and Development (UNCTAD) in 1968 in response to multilateral interest, the underlying rationale for trade preference programs was that they could encourage export diversification in developing markets, spurring global trade growth and mitigating problems related to balance of payments challenges. Trade preference programs have also become imperative to supporting US economic and social interests domestically and abroad for a multitude of reasons, including the following:

- First, preference programs **support job creation and economic growth in the US**. As of 2015, AGOA alone had created approximately 100,000 jobs in the US by providing affordable inputs to American manufacturing companies.<sup>9</sup> GSP has also been central to creating – and keeping – US jobs. After GSP lapsed the last time (between 2013 and 2015), companies laid off employees, reduced workers’ hours, limited raises, and cut health and retirement contributions to compensate for higher costs and falling sales.<sup>10</sup> After its renewal, however, many companies were able to again transform the cost savings from the program into jobs and raises for American workers,<sup>11</sup> although the lapse did have a more lasting negative impact on smaller businesses.
- Second, preference programs **benefit America’s small businesses and consumers**. The Coalition for GSP conducted a survey on the impact of GSP on American businesses and found that GSP saved US companies \$729 million in 2016. It is of particular importance to the US – as the world’s largest consumer market – that trade remains open. Minimizing the costs of imports provides a great benefit to both American consumers, who may now purchase less expensive goods, and American producers, who may procure less expensive intermediate inputs for their final products. Again, the importance of keeping GSP in place is illustrated by the fact that Californian companies and consumers paid nearly \$200 million in additional taxes when the program last expired.

<sup>8</sup> United States Trade Representative (USTR). 2016. “US Trade Preference Programs: Reducing Poverty and Hunger in Developing Nations through Economic Growth.” Washington: USTR.

<sup>9</sup> AGOA Ambassadors Working Group Recommendations for the Re-Authorization of the African Growth and Opportunity Act (AGOA) available at <http://www.leadershipafricausa.org/pdf/activities/Focus%20on%20Africa/Press%20Release/African%20Ambassadors%20Recommendations%20For%20the%20Re-Authorization%20of%20AGOA.pdf>

<sup>10</sup> Coalition for GSP. “Lost Sales, Investments, and Jobs: Impact of GSP Expiration After One Year”. Sept. 16, 2014. Available <https://renewgsptoday.files.wordpress.com/2014/09/lost-sales-investments-and-jobs-impact-of-gsp-expiration-after-one-year.pdf>.

<sup>11</sup> See, e.g., Renew GSP Today. “It isn’t 1810.” Coalition for GSP, Sept 14, 2016, <https://renewgsptoday.com/>

- Third, preferences can be used as a tool to **promote labor standards, international human rights, and democratic values abroad**. Through trade preference programs, the US has been able to engage with foreign governments to adopt improved labor standards and strengthen rule of law. Labor standards are included in country eligibility requirements for preference programs, and they follow many of the International Labor Organization (ILO) Core Labor Standards. Specifically, under GSP, a condition for eligibility is that a beneficiary country “must have taken or is taking steps to afford internationally recognized worker rights, including:
  - a) The right of association,
  - b) The right to organize and bargain collectively,
  - c) A prohibition on the use of any form of forced or compulsory labor,
  - d) A minimum age for the employment of children, and a prohibition on the worst forms of child labor, and
  - e) Acceptable conditions of work with respect to minimum wages, hours of work and occupational safety and health.”

Since GSP was amended in 1984 to include labor rights in the eligibility criteria for beneficiary developing countries, treatment of labor in the GSP statute and its labor eligibility review process have been instrumental in addressing labor rights concerns in many developing economies. In Bangladesh, the withdrawal of GSP eligibility in 2013 and the ensuing launch of the GSP action plan resulted in a revision of the Bangladesh Labor Act and the registration of 200 new unions in the garment sector in two years.<sup>12</sup> In many other countries, the threat of withdrawing benefits alone has been sufficient to promote better labor standards and practices. For example, a labor rights petition filed by the AFL-CIO against Uganda led to the passage and enforcement of new laws, funding, and placement of labor inspectors.<sup>13</sup> In Guatemala, in response to US review of a petition containing evidence of the assassination of trade unionists and a repressive labor code, the Guatemalan government took rapid action to resolve a number of long-standing disputes and amend its labor code.<sup>14</sup>

Despite the usefulness of these provisions, bringing them in line with more recent bipartisan principles on labor and other standards, such as those contained in the May 10, 2007 agreement

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<sup>12</sup> United States Trade Representatives (USTR). 2015. “Standing Up for Workers: Promoting Labor Rights through Trade.” Washington: USTR Special Report. <https://ustr.gov/sites/default/files/USTR%20DOL%20Trade%20-%20Labor%20Report%20-%20Final.pdf>.

<sup>13</sup> The Trade Partnership. 2011. “The U.S. Generalized System of Preferences Program: An Update.” Washington. [http://tradepartnership.com/pdf\\_files/2011%20GSP%20Update.pdf](http://tradepartnership.com/pdf_files/2011%20GSP%20Update.pdf).

<sup>14</sup> Compa, Lance A., Vogt, Jeffrey S. 2001. “Labor Rights in the Generalized System of Preferences: A 20-Year Review.” Cornell: Comparative Labor Law & Policy Journal. <http://digitalcommons.ilr.cornell.edu/cgi/viewcontent.cgi?article=1172&context=articles>.



struck under the Bush Administration, would more fully reflect modern trade realities.<sup>15</sup> A complementary policy tool to consider might be a GSP+ program like the EU's, which applies a "carrot and stick" approach to enhance conditionality in trade preferences, improve labor and human rights standards, and expand market access to the products that matter most to development and global supply chains.

- Fourth, preference programs are vital to **maintaining US national security and economic interests** abroad. Increased trade encourages economic growth, which is closely linked to political stability, since political instability often emerges from economic stagnation. The programs have strengthened our ties with a number of countries, and they have proven to be a vital tool for engagement. Promoting security through programs like these is crucial to American business interests in a number of countries, and they encourage broader peace and stability as well. Further, by increasing US economic engagement in developing regions, the programs help check the influence of US competitors, including more advanced developing economies. Through trade preference programs, the US can use its positive trade relationships with developing countries to build closer, mutually beneficial ties.<sup>16</sup>

Trade preference programs are also essential to sustainable and inclusive growth in developing countries:

- First, preference programs address important social and economic goals, helping to **alleviate hunger, improve labor conditions**, and align with the UN Sustainable Development Goals (SDGs). According to the Office of the U.S. Trade Representative (USTR), US trade preference programs have helped "reduc[e] poverty in beneficiary countries by increasing and diversifying trade, encouraging inclusive economic growth, and creating new employment opportunities in certain sectors, such as textiles and apparel, that directly benefit the poor."<sup>17</sup>
- Second, preference programs work to **enhance gender equality** by expanding opportunities in sectors in which women work, and supporting sustainable development that benefits future generations. The impact of giving a woman a job is significant: it is estimated that one woman's job in the apparel sector supports up to 15 other people. US preference programs have led to job creation for impoverished women in sectors such as apparel in Africa, jewelry production in Asia, and agricultural production across the world. Around the world, women continue to be

<sup>15</sup> Bipartisan Agreement on Trade Policy, May 10, 2007.

<sup>16</sup> Day, Dan. 2014. "Free Trade Agreements and National Security: Five Key Issues." American Security Project (ASP) Discussion Paper. August. Washington: American Security Project Press.

<sup>17</sup> Froman, Michael B.G. "U.S. Trade Preference Programs: Reducing Poverty and Hunger in Developing Nations through Economic Growth." Office of the U.S. Trade Representative. June 2016.

underrepresented in formal labor pools.<sup>18</sup> In particular, preferences are crucial tools to help grow small businesses, including operations run by women entrepreneurs. Booz & Company estimates that raising female employment to male levels could increase a country's Gross Domestic Product (GDP) by as much as 34 percent. The World Bank's 2011 World Development Report highlighted that female-led households invest a higher percentage of income into food and education, to the benefit of the next generations. Making trade preference programs more inclusive and easier to use will enhance these benefits and help ensure that women and other marginalized groups are best positioned to gain from international trade.

- Trade preference programs, in conjunction with **capacity building programs from both the public and private sectors contribute to market infrastructure and strengthen economic rights**. On the public sector side, this includes projects to build trade infrastructure funded by agencies like the Millennium Challenge Corporation (MCC) and International Finance Corporation (IFC), which have been important avenues for improving trade-related infrastructure and the business-enabling environment. Such programs finance improved energy and transportation facilities, education for beneficiaries and service-providers, modernized property rights and land policy, and other areas essential to sustainable economic growth and an open investment climate.
- In the private sector, capacity building programs focus on a number of areas related to the trade preference programs, including **empowering girls and enhancing knowledge of women's economic rights**. Examples include Gap Inc.'s P.A.C.E. (Personal Advancement & Career Enhancement) Program, which provide technical training for women in the garment industry to help them advance at home and in the workplace. The Girl Effect, an independent non-profit that was developed and launched by Nike, Inc., uses the power of culture brands, technology, and mobile platforms to increase understanding and connectivity for and among girls to drive social change. Another example is the Women's Empowerment initiative of Business for Social Responsibility (BSR), which works with companies to design business practices and implement corporate strategies that increase access to resources and opportunities for women. These examples and many others highlight the importance of capacity building as a critical element to complement trade preference programs and other economic growth initiatives.

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<sup>18</sup> See Trump, Ivanka and Kim, Jim Yong. "Investment in Women Unleashes Global Gains." *Financial Times*. 24 April 2017. Web.



## GETTING THE GREATEST BENEFIT OUT OF TRADE PREFERENCE PROGRAMS

**W**hile the benefits of trade preference programs have been widespread, the programs could be better tailored to support more equitable growth and stability at home and abroad. Not only should trade preference programs be kept in place as long as possible, they should cover the products that matter most for sustainable growth and better link to global supply chains.

### KEEP TRADE PREFERENCES IN PLACE LONG ENOUGH FOR BENEFITS TO VEST

The benefits of trade preference programs do not happen automatically. They need to be kept in place long enough for the benefits – jobs, cost savings, and security and social gains – to vest. This will only happen if the preferences both have a long enough time horizon and if their renewal is a transparent process. For GSP, this means the frequent fits and starts that have become common to the program need to be reassessed.

Developing even the most straightforward supply chain can take a minimum of ten years, but value chains in a sector like agriculture will take even longer to develop. In the textiles and apparel sector, for example, investment is typically planned over ten-year periods, and returns on investment take two or more years.<sup>19</sup> Longer terms for preference programs are attractive to the business community in both the US and beneficiary markets, because they provide predictability and certainty for investors and businesses that rely upon the inputs that preference programs make available as well as help reduce commercial risk. Addressing issues in the business enabling environment, discussed below, such as non-tariff barriers and customs procedures, will also be an important aspect of developing efficient and inclusive global supply chains. However, most trade preference programs are not permanent, and important preference programs such as GSP continue to have relatively short terms with frequent renewal periods, which creates uncertainty for investors and hampers development of supply chains.

Trade relies upon predictability, and so preference programs must be reaffirmed and renewed in a timely manner. GSP is the foundation of all US trade preference programs, such as AGOA, CBTPA, and Haiti HOPE. When GSP expired in 2013, small businesses faced administrative uncertainties around claiming benefits under AGOA due to the interdependency of product designations in preference programs. Renewal of GSP for a time period of at least ten years would create greater certainty for US stakeholders and developing countries alike.

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<sup>19</sup> Mahoney, Brian. "Froman Pushes AGOA Renewal Before Presidential Summit." Law360, 30 Jul. 2014. Web. 13 Dec. 2014; Nijraini, John. "AGOA: The U.S.-Africa Trade Dilemma." Africa Renewal Online, Dec. 2014. Web. 13 Dec. 2014.

## COVER PRODUCTS THAT MATTER MOST TO DEVELOPMENT

Development is a two-way street, not a zero-sum game. Often the sectors that have the greatest impact on developing markets also play an important role in global supply chains to the benefit of US companies and workers. Yet, trade preference programs do not always cover the products that matter most to two-way development, like agricultural products or apparel and footwear. Comparing to trade preference programs such as the EU GSP+ and Everything But Arms (EBA), the US GSP has less expansive product coverage, and certain products excluded are still subject to tariff peaks. For example, some goods have a regressive duty structure resulting in a duty as high as 67.5 percent for some lower cost footwear products, which negatively impacts both low-income US consumers as well as footwear manufacturers in developing countries due to high start-up costs. The current structure of US preferences puts the US behind the EU, Canada, and other countries, which offer more under their trade programs and have established better mechanisms for enforcement of labor and human rights conditions. Under the US GSP program, 5,000 product lines out of a potential 7,200 are eligible for duty-free treatment. Many of the excluded products are those that are most important to developing countries - the 2,200 products lines excluded from the GSP program together account for over 30 percent of US import products. Other US trade preference programs, like AGOA, cover a select group of countries, with duty-free treatment on a wider range of products, including apparel, but even AGOA is limited in its coverage of some products with significant development potential, such as most agricultural goods.

Often, the products that are excluded from trade preference programs are those most significant to development, and their exclusion may be based on outdated trade considerations rather than present day economic or policy needs. To illustrate, certain products remain subject to tariff peaks and maintain rates such as 36.6 percent for agriculture, 57.4 percent for leather, textiles, and clothing, and 6.0 percent on other industrial products.<sup>20</sup> These rates stand in contrast to US tariffs overall; the U.S. average trade-weighted tariff was 1.5 percent in 2015.<sup>21</sup> When duty-free imports under trade agreements and trade preferences are excluded from the calculation, the trade-weighted tariff rate in 2015 was only 1.7 percent.<sup>22</sup> This large discrepancy between tariffs on certain products and the average tariff rate should indicate that the US has the ability to lower tariffs for products crucial to development without consequence. As a first step, Congress could remove the statutory prohibition against these products being included in GSP, and allow regulatory reviews to determine which products, if any, are still

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<sup>20</sup> Elliot, Kimberly Ann. 2015. "Trade Preferences for the Least Developed Countries: Opportunities not Panaceas." Think Piece for the E15 Expert Group on Trade, Finance, and Development. Geneva: International Centre for Trade and Sustainable Development and the World Economic Forum.

<sup>21</sup> World Bank. 2017. "World Development Indicators: Tariff Barriers." World Development Indicators. Web. Accessed April 2017. <http://wdi.worldbank.org/table/6.6#>

<sup>22</sup> Froman, Michael B.G. "U.S. Trade Preference Programs: Reducing Poverty and Hunger in Developing Nations through Economic Growth." Office of the U.S. Trade Representative. June 2016.

sensitive and should remain excluded from GSP.<sup>23</sup> To ensure that trade benefits support countries in need, Congress could consider whether there should be different levels of benefits for Least Developed Countries (LDCs) versus other GSP beneficiary countries. Such an approach has been done for travel goods and could be considered more broadly;<sup>24</sup> this would also be complementary of the GSP+ option discussed above.

Ensuring that all preference programs, including GSP, cover the products that matter most for development could help support growth for US SMEs and American consumers, as well as for developing countries. Including these products would also contribute to continuity in preference programs and US control over its foreign policy, since GSP benefits are covered under the legal standard of the WTO Enabling Clause and do not require a majority waiver at the WTO, which is always subject to the discretion of other countries. Because of the connection between GSP and all of the other preference programs, and also drawing lessons from Europe, this would help regions like Africa more reliably maintain preferential benefits.

Footwear is a sector in which the US needs to integrate more fully into global supply chains in order to compete, and trade preference programs can be instrumental. Adding footwear products would be extremely beneficial for US industry and job creation and could also help US companies diversify sustainable supply chains and avoid becoming too centralized or dependent upon any one sourcing country. Because of the capital-intensive nature of footwear capacity development, global footwear manufacturing is slow to respond to emerging economic pricing pressures and consumer trends. Even today, after several years of substantial supply chain repositioning, 93 percent of US footwear imports originate in just three countries: China, Vietnam, and Indonesia.<sup>25</sup> US footwear companies are actively looking for new and emerging production markets, and an enhanced GSP that includes duty-free footwear would help accelerate this trend, creating jobs and providing added value to the American footwear consumer while also allowing other countries in the global economy to develop this important sector.

While duty is not the sole determining factor that drives sourcing decisions for the US footwear industry, creating new duty saving opportunities within global supply chains would provide enhanced options for GSP partner countries and their potential customers. American footwear companies and their

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<sup>23</sup> As an example, the 2015 GSP Travel Goods Act removed certain travel articles from statutory exclusion after determination that they are no longer import-sensitive to US Industries. 13 tariff lines at the HS 8-digit level and 14 at the 10-digit level were designated as GSP-eligible.

<sup>24</sup> The 2015 H.R. 681 GSP Update Act allowed certain travel articles to be removed from statutory exclusion and considered under the annual GSP eligibility review process due to evolving import-sensitivity.

<sup>25</sup> See “US Imports For Consumption: All Footwear” Office of Textiles and Apparel, U.S. Department of Commerce <http://otexa.trade.gov/FLT/imports/cat10.htm>, and “2016 Footwear Production Power Rankings” Footwear Distributors and Retailers of America (FDRA), <http://fdra.org/wp-content/uploads/2017/05/FY-2016-Footwear-Power-Rankings.pdf>.

consumers paid close to \$3 billion in duties on imports in 2016. Addressing this heavy tariff burden would further encourage footwear companies to alter their sourcing strategies and pivot to a more diverse set of countries with footwear manufacturing capacity.

In addition to footwear, covering apparel products under trade preference programs would both benefit US beneficiaries and help maintain ongoing growth in developing economies, without harming US stakeholders or countries with existing preferential treatment for apparel. Textiles and apparel flow mainly from developing to developed countries, and a number of developing countries have found a niche in the apparel sector. This has been a sector of growth in Africa and Haiti, due to both inclusion in trade preference programs and more permissive rules of origin. For example, because African countries rely on a limited number of exports,<sup>26</sup> textile and apparel exports are particularly important to their development. Among the 29 African countries currently eligible for GSP and AGOA, 25 of them export apparel products to the United States. Apparel trade from Africa totaled \$956 million in 2016, which included many product categories in which African apparel exporters are specialized.

A 2013 study by Kimberly Elliott of the Center for Global Development found that preferential access could be granted more expansively without eroding the benefits of preferences that some developing countries rely upon.<sup>27</sup> The study found that benefits for African, Latin American, and Caribbean trading partners could be preserved, while also allowing for 50 percent of apparel exports from Bangladesh and 60 percent from Cambodia to receive duty-free quota-free (DFQF) access.<sup>28</sup> In other words, tariff lines could be added to GSP while still maintaining benefits for the important apparel industries – and the jobs they created – that have thrived due to trade preferences under AGOA, CAFTA, and NAFTA. Adding tariff lines to GSP would also ensure that these benefits remain in place on an ongoing basis and under more permanent legal authority at the WTO.

As part of a regulatory process, in order to fully assess the impact of trade preferences in key sectors and determine the appropriate level of coverage under GSP, an independent US ITC study could be conducted to specifically assess the impact on US consumers, workers, and industry in order to establish an economic basis for inclusion or exclusion of additional products. Not only is it important to assess the

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<sup>26</sup> United Nations Conference on Trade and Development (UNCTAD). 2015. “Key Statistics and Trends in International Trade 2014.” Geneva: United Nations Publication.

<sup>27</sup> Elliott analyzed the tariff lines (at the Harmonized Tariff System (HTS) 8-digit level) that had greatest market share for AGOA and Asian apparel producers. From this, she identified a competitive threshold, defined as a minimum percentage market share that determines the competitiveness of the country’s share of total trade according to specific tariff lines. Products that were most important to a preferential trade agreement would be safeguarded, or kept under preferences, and products that were competitive could be added to GSP. See Elliot, Kimberly Ann. 2013. “Getting to Yes on Expanded US Market Access for the Poorest Countries.” *Rethinking US Development Policy*. Center for Global Development.

<sup>28</sup> Elliot, Kimberly Ann. 2013. “Getting to Yes on Expanded US Market Access for the Poorest Countries.” *Rethinking US Development Policy*. Center for Global Development.

full implications of any changes to GSP, this should be considered in light of maintaining the effectiveness of other US preference programs as noted above.

The agricultural sector is also fundamental to development, both for the US and for developing countries, particularly those that have a large percentage of their populations earning less than US \$1.90 per day.<sup>29</sup> Notably, women make up on average 43 percent of the global agricultural labor force, ranging from 20 percent in Latin America to over 50 percent in Africa and Asia, and these percentages are increasing.<sup>30</sup> Strengthening agricultural markets is essential for enhancing food security, and thus critical for LDCs in particular.<sup>31</sup> In most countries, food security tends to rely upon both domestic production and imports. Emerging markets together make up 20 percent of US agricultural exports.<sup>32</sup> Efforts to strengthen agricultural markets will help create economies that are more food secure – and more politically secure – and also create new opportunities for US agricultural trade. The Organisation for Economic Co-operation and Development (OECD) and the World Trade Organization (WTO) have collectively identified that lower- and middle-income countries are not only exporting more high-value agricultural and food products, but their import demand has surged dramatically over the last decade.

Under the current trade preference programs, many important agricultural products are currently subject to tariff rate quota (TRQ) restrictions, which effectively prevent them from benefitting from preferential trade arrangements. Yet many TRQ allocations remain unclaimed, and the US often cannot meet domestic market demand. A TRQ provides a lower tariff rate for goods that enter under a specified quota, but that tariff rate spikes dramatically once the quota has been met. When dealing with TRQs, companies are faced with a certain threshold of trade that they may not exceed for fear of incurring large fees. So instead of investing and producing in such areas, firms have the incentive to invest and produce where there are no TRQs, or where TRQs are less likely to affect them. Although the US does not offer DFQF for LDCs, an incremental approach might include exempting LDCs from TRQ restrictions or to “remove quotas from processed product exports from LDCs to encourage linkages and job creation.”<sup>33</sup>

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<sup>29</sup> World Bank. 2015. “Poverty Line Update Frequently Asked Questions.” Brief. Web. Accessed 6 April 2017. <http://www.worldbank.org/en/topic/poverty/brief/global-poverty-line-faq>.

<sup>30</sup> Food and Agriculture Organization of the United Nations (FAO). 2011. “The gender gap in agriculture.” *The State of Food and Agriculture 2011*. Rome: FAO. <http://www.fao.org/docrep/013/i2050e/i2050e.pdf>.

<sup>31</sup> Christiaensen, Luc, Lionel Demery, and Jesper Kuhl. 2011. “The (evolving) role of agriculture in poverty reduction-- An empirical perspective.” *Journal of Development Economics* 96:2, p. 239-54.

<sup>32</sup> United States Department of Agriculture. February 2017. “Outlook for US Agricultural Trade 2017.” Issue AES 98. Web. Accessed at <https://www.ers.usda.gov/webdocs/publications/82591/aes-98.pdf?v=42788>

<sup>33</sup> Elliot, Kimberly Ann. 2015. “Trade Preferences for the Least Developed Countries: Opportunities not Panaceas.” Think Piece for the E15 Expert Group on Trade, Finance, and Development. Geneva: International Centre for Trade and Sustainable Development and the World Economic Forum.

## **BETTER INTEGRATE TRADE PREFERENCES INTO GLOBAL SUPPLY CHAINS**

Trade increasingly takes place through global supply chains that span national borders, creating opportunities for developed and developing markets alike. Although the majority of trade among countries is still comprised of unfinished goods and services, trade in intermediate goods is growing and warrants increased attention. As discussed above, one of the most critical considerations for development of global supply chains is the amount of time it takes for investment to take root and for supply chains to expand to include new countries.

In addition, rules of origin (ROOs) are used to determine how to classify a product for customs purposes, which is an important factor in determining whether a product is eligible to receive benefits under a preference program. While ROOs do help ensure that trade preferences are not bestowed upon non-beneficiary countries, complicated rules can place an undue burden on companies and customs officials alike, and may ultimately discourage the use of preference programs. At the most recent WTO Ministerial in Nairobi, a proposal was floated for a ROO threshold of 25 percent for LDCs. Analysis shows that the difference between a 25 percent and 35 percent value threshold (plus substantial transformation) is not significant, and GSP's ROO is more transparent than many maintained by other developed countries.

Maintaining the 35 percent value threshold under GSP while also providing for a more flexible cumulation rule would, however, enhance the effectiveness of the GSP program even more. For example, the Heritage Foundation notes that more expansive cumulation rules, such as allowing GSP countries to accumulate from all beneficiary countries within the program, can help increase trade among countries within and outside of preference programs, as well as help mitigate the negative effects of trade diversion.<sup>34</sup> This would allow the US to achieve some of its same policy goals and positively contribute to growth in developing markets, both domestic and regional. This would also better take into account the realities of modern supply chains and help address challenges faced by companies, particularly small businesses and women entrepreneurs. A more flexible cumulation rule extended to LDCs and developing countries alike could also support regional harmonization efforts, which is particularly critical for achieving economies of scale in markets in Africa and other parts of the world. In addition, the cap on US inputs is an outdated policy that should be removed.

Advanced developing countries play a particularly significant role in global supply chains, and their ongoing access through trade preference programs should be considered in light of their ability to facilitate efficient market development and ensure that trade preference programs spur inclusive growth and enhance critical regional market development. Advanced developing economies are strategic trading

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<sup>34</sup> Olson, Ryan. "To Avoid Trade Diversion, Congress should Liberalize Rules of Origin." Heritage Foundation. June 2015. <http://www.heritage.org/trade/report/avoid-trade-diversion-congress-should-liberalize-rules-origin>.



partners for the US, as these countries possess considerable consumption power and regional influence. In addition, the rationale for excluding some countries from GSP no longer exists and should be reconsidered based on current circumstances. Notably, more than three-quarters of GSP importers report that they are unable to source their products from the US,<sup>35</sup> and taking preferential benefits away from more advanced economies does not ensure that less developed economies will benefit. Instead, market share tends to drift to other more advanced developing economies, like China, when preferences are removed. Advanced developing countries like India and Brazil also still have large populations facing extreme poverty and income inequality. Trade preference programs are one critical tool that can help encourage both inclusive and sustainable growth and positive social and economic reforms.

Finally, market rules and legal standards, including for labor and human rights, play a particularly important role in global supply chains. Eligibility requirements in trade preference programs hold beneficiary developing countries accountable to improved standards for labor and human rights. However, the standards in GSP date back to 1984 and are out of line with modern supply chains. Updating these criteria consistent with the May 10 bipartisan agreement on trade policy would further enhance effective governance in developing countries and be a stepping stone to a more balanced trade relationship. In addition, consideration of a GSP+ scheme could enhance both the incentives and rewards for developing countries that make significant progress towards achieving governance, human rights, and labor standards.

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<sup>35</sup> Coalition for GSP. “Lost Sales, Investments, and Jobs: Impact of GSP Expiration After One Year”. Sept. 16, 2014. Available <https://renewsgptoday.files.wordpress.com/2014/09/lost-sales-investments-and-jobs-impact-of-gsp-expiration-after-one-year.pdf>.

## **BUILD BRIDGE BETWEEN TRADE PREFERENCES PROGRAMS AND INITIATIVES TO ENHANCE RULE OF LAW AND IMPROVE THE BUSINESS ENABLING ENVIRONMENT**

It is important that trade preferences are one element in a more comprehensive strategy of engagement between developed and developing country trading partners. Not only should trade preference programs be complemented by capacity building and infrastructure development programs as discussed above, they should ultimately be part of a more comprehensive policy designed to deliver mutually beneficial, two-way trade and investment based on sound market principles and rule of law.

Research and data suggest that trade preference programs are only one element in the larger set of trade policies that help promote development. Addressing supply-side constraints, including non-tariff measures, slow and expensive port transits, costly telecommunications, expensive and overly complicated trade paperwork, inefficient internal transport and logistics bottlenecks, and other challenges will be essential to ensuring both economic development and success in global markets and supply chains. Trade preference programs cannot address these supply side constraints, and duty benefits alone cannot substitute for regulatory reforms in the market. According to the World Bank and World Economic Forum, reducing business enabling environment challenges, such as eliminating non-tariff barriers to increase regulatory and compliance efficiency, streamlining customs procedures to reduce time and cost of import and export, and improving insurance and financial services to lower risk for businesses (which are often linked to laws and regulations), would increase world GDP six times more than through complete removal of tariffs.<sup>36</sup> The US Congress reflected this sentiment when it called for a review of the duty-focused approach in the most recent AGOA legislation.

Broadening the US approach on trade and development to strengthen focus on the business enabling environment and rule of law could help harness the potential of trade to build robust market systems, generate economic growth, and encourage private entrepreneurship.<sup>37</sup> In particular, reforms to improve market regulation, simplify administrative procedures, and promote the provision and maintenance of key infrastructure are essential to address the growing demand of citizens in developing countries for better market systems and establish a better environment for investment overall. It is estimated that increased public investment in infrastructure has helped countries deficient in natural resources, like Ethiopia and Rwanda, to achieve GDP growth as high as eight percent and improve the overall investment climate.<sup>38</sup> These improvements in the market are also directly linked to political stability and

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<sup>36</sup> World Economic Forum. “The Shifting Geography of Value Chains: Implications for Developing Countries and Trade Policy” 2012.

<sup>37</sup> Kuhlmann, Katrin. “Strengthening the Global Trade and Investment System for Sustainable Development.” International Centre for Trade and Sustainable Development and World Economic Forum. Nov 2015.

<sup>38</sup> African Economic Outlook. 2016. “Political and Economic Governance in Africa.” <http://www.africaneconomicoutlook.org/en/outlook/political-and-economic-governance-in-africa>.

global security. Ultimately, improvements in legal and regulatory systems, administrative procedures, and infrastructure are what attracts investment and creates jobs.

In addition, enhanced regional integration and the harmonization of trade policies encourage both North-South and South-South trade, improve the regional investment environment, and narrow income gaps. As a complement to trade preference programs, a rule of law-based approach focused on the building blocks of economic legal reform could enhance trade's use as a "tool for both poverty reduction and entrepreneurship."<sup>39</sup> Through such an approach, the US could regain its leadership role in international economic systems and improve working conditions and market opportunity worldwide.

- "Building blocks" for trade establish an open and transparent enabling environment for business and strengthen legal and regulatory systems and trade disciplines in areas such as trade facilitation, sanitary and phytosanitary (SPS) measures, technical barriers to trade (TBT), and services. A "building block approach," which could be approached either piece-by-piece or system-wide, would "support a range of economic opportunity for enterprises of all sizes and bolster the ability of all countries to participate in global markets. Implementation of the right legal and regulatory structures could also create predictability and transparency for investment, expand market potential, and reduce market risk."<sup>40</sup>
- The link between trade, capacity building, and agriculture is particularly pronounced. For agricultural trade, these "building blocks" are becoming increasingly important to farmers, companies, and consumers in the US and abroad, and they will impact both food security in developing nations (which has a direct link to global security and stability) and opportunities for enhanced two-way trade. Focus should be on incremental and integrated approaches to improve and harmonize global food standards, increase compliance with standards, reform customs systems, and improve coordination between government agencies, which would help transform markets in developing economies, support US exporters with securing access to growth markets, and improve food security and global stability. In addition to providing targeted technical assistance, the Farm Journal Foundation also suggests that dialogues designed to align developed country and beneficiary governments would support coordination on common objectives, such as food safety, and help improve development outcomes.<sup>41</sup>
- Scaling up training on how to navigate regulatory systems and use trade preference programs is also critical. For trade programs and policies, one tool is the US Commerce Department's innovative e-learning tool that helps developing countries identify their own economic

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<sup>39</sup> Kuhlmann, Katrin. "Strengthening the Global Trade and Investment System for Sustainable Development." International Centre for Trade and Sustainable Development and World Economic Forum. Nov 2015.

<sup>40</sup> Kuhlmann, Katrin. "Strengthening the Global Trade and Investment System for Sustainable Development." International Centre for Trade and Sustainable Development and World Economic Forum. Nov 2015.

<sup>41</sup> Bahalim, Ammad, and Joe Glauber. "Leveraging US Technical Assistance for Improved Development Outcomes." *Farm Journal Foundation*, February 2017.

opportunities and walk through how to best use trade interventions (including trade preference programs) to unlock market potential. Another model is the system of USAID Trade and Investment Hubs in place in sub-Saharan Africa to support enhanced two-way trade between the US and Africa.

- Capacity building, including through the Trade and Investment Hubs, has also been critical in expanding worker training and supply chain development, to the benefit of US companies in supply chains such as apparel and footwear. For example, with the assistance of the East Africa Trade and Investment Hub, East Africa is establishing itself as a reliable sourcing destination for global companies and source of US investment in apparel and footwear. Robust growth fueled by capacity-building efforts and business-enabling regulatory reforms is transforming East African countries from traditional aid recipients to dynamic trade partners in the global economy and is providing diverse sourcing outlets (and means for job creation and retention) for companies on both ends. These programs also link with improved labor and human rights standards, which raise working conditions around the globe and level the playing field for US businesses.
- Women's role in the global economy should receive greater focus as well. As Ivanka Trump and World Bank President Jim Yong Kim wrote in the *Financial Times*, "We know what works. We need to...offer programmes that train female entrepreneurs and help them access higher value markets. We need to develop new legal and regulatory frameworks to boost women's growth and productivity. The right skills training enhances women's capacity to manage their businesses. And mentorship opportunities and access to networks bring learning opportunities and connections to capital and markets."<sup>42</sup> Trade preference programs, coupled with initiatives focused on rule of law and an open, transparent, and equitable business enabling environment would directly address these gaps.

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<sup>42</sup> Trump, Ivanka and Kim, Jim Yong. "Investment in Women Unleashes Global Gains." *Financial Times*. 24 April 2017. Web.

## CONCLUSION

Over forty years after GSP was signed into law, the US and its allies in developing nations still have much to gain from trade preferences. Although these programs continue to be a work in progress, they are a crucial part of maintaining America's critical allies and ensuring that US economic and political interests are secured at home and abroad, in addition to their integral role in furthering international development. The data is clear that without these programs and developing country access to the US market, all parties would take a step back in development. The only way forward is to extend these programs with longer terms, enhance their coverage to products that matter most, streamline ROOs, and maintain benefits for more advanced developing economies. In addition, looking to the future, trade preference programs should become one prong in a broader trade and development policy focused on rule of law, global supply chains, and the business enabling environment, ensuring that markets around the world operate under principles of transparency, equity, and stability.

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