The Causes of Informal Trade: Importance of Trade Facilitation

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Two Questions

- 1. Which is more important in conducting trade facilitation reform: Integrity or Efficiency
- 2. Which is more important in conducting trade facilitation reform: Customs or Non-customs
- I will try to answer those questions based on economic analysis (not normative argument)
 - Economic analysis focuses on the elimination of informal trade

Mirror Comparison

- Trade statics is unique: More than two authorities collect data on the same economic transaction
 - Exporting country
 - Importing country
 - And possibly, transit country
- Import side tends to be larger than the export side because of transport costs.
 - Usually, IM-EX ratio is expected to be around 1.1 (land-locked countries' ratio tends to be higher).

Informal Trade Revealed by Mirror Comparison

- A certain type of informal trade can be revealed by mirror comparison.
- Informal trade in this study:
 - Trade that is properly recorded by one party but not by the other party.
 - We will call it recorded-unrecorded trade.
 - Unrecorded-unrecorded trade CANNOT be revealed by this method.
- Very low IM-EX ratio (import-side statistics is much smaller that export-side statistics) implies the existence of informal imports (trade that is properly recorded by the export country but not by the import country).

Bilateral Mirror Comparison

- Country A's total export to Country B to be compared against Country B's total import from Country A.
- Problem 1: There is a possibility that one of them simply mis-record the origin/destination of product.
 - E.g. goods from Japan to Mongolia via Korea.
- Problem 2: Bilateral mirror comparison tend to assume that the partners have correct trade statistics
 - E.g. Japan versus Mongolia
 - Is such an assumption relevant?

Aggregate IM-EX Ratio

- It is important to control the factor of origin/direction rerecording.
- Country A's import is compared against the Rest of the World (ROW)'s export to Country A.
- By using ROW, two factors are controlled:
 - Direction misrecording.
 - "Specificity" of partners.
- Note, however, that the land-locked status may affect the aggregate IM-EX ratio because of double/no-counting problem.
 - E.g. Goods from Japan to Mongolia via PRC

Ranking of Aggregate IM-EX (2010)

Bhutan	3.16	Viet Nam	1.01
Armenia	1.73	Georgia	0.99
Nepal	1.55	Sri Lanka	0.99
Japan	1.40	Hong Kong	0.96
Singapore	1.35	Samoa	0.88
India	1.34	Philippines	0.84
Rep. of Korea	1.32	Kazakhstan	0.73
China	1.31	Kiribati	0.71
Pakistan	1.30	Azerbaijan	0.65
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