

MichU
DeptE
ResSIE
D
#246

RESEARCH SEMINAR IN INTERNATIONAL ECONOMICS

Department of Economics
The University of Michigan
Ann Arbor, Michigan 48109-1220

SEMINAR DISCUSSION PAPER NO. 246

Dumping, Antidumping, and Emergency Protection*

by

Bernard M. Hoekman
GATT Secretariat

and

Michael P. Leidy
The University of Arizona

JAN 5 1990

The Sumner and
Laura Foster Library
The University of Michigan

July, 1989

Published in *Journal of World Trade*, October 1989

Many helpful suggestions were made by participants in seminars at The University of Michigan and the GATT. We are particularly grateful to Richard Blackhurst, Alice Enders, Marc Koulen, Robert Stern, and Frank Wolters for their comments on previous drafts. The views expressed are those of the authors and should not be attributed to the GATT Secretariat. Partial financial support from the Ford Foundation for a program of research on international trade policy at The University of Michigan is gratefully acknowledged.

Dumping, Antidumping, and Emergency Protection

by

Bernard M. Hoekman and Michael P. Leidy

I. Introduction

Loosely defined, dumping occurs when similar products are sold by a firm in an export market for less than what is charged in the home market. Alternatively, it may occur if the export price of the product is less than total average costs or marginal costs. Many important trading nations have legislation that allows them to impose antidumping (AD) duties if dumping is found to be occurring and to be injuring domestic industries. In this paper we focus in particular on the relationship that exists between AD and other policy instruments intended to deal with “excessive” import competition, especially safeguard laws modelled on Article XIX of the General Agreement on Tariffs and Trade (GATT).¹ The existence of AD law has several critical implications for the multilateral trading system. It is an inefficient instrument of contingent protection that can be used *de facto* — although not *de jure* — as a substitute for nondiscriminatory safeguards actions.² While there are coherent rationales for safeguards, none exists for AD. This does not mean, however, that AD is inconsequential.

It is well known that GATT-conform safeguard actions are rarely taken, and that multilateral agreement on improving safeguards procedures has been impossible to achieve in the last 15 years. In part this is due to the fact that alternative instruments such as AD exist. AD laws constitute an obstacle to the advancement of a liberal trading order,

¹In this article safeguards are actions taken to limit imports of a product from all sources in those cases where these imports have been found to harm domestic industries to such an extent that protection is deemed to be in the national interest. In what follows when we speak of Article XIX, emergency protection, or safeguard actions, this should be interpreted as temporary, nondiscriminatory actions under laws which are modelled on, or implement, the provisions of Article XIX of the GATT.

²The substitution relationship between AD and safeguards has been noted by Lloyd (1977) and UNCTAD (1984), among others, and is often implicit in the language used in the business press.

both directly and indirectly. Among the indirect influences one can point to the fact that the scope for an agreement on improved safeguard procedures, and the likely effectiveness of any such agreement in the ongoing Uruguay Round of multilateral trade negotiations, is diminished by the ready accessibility of national AD laws. Another indirect effect is that the availability of AD to import-competing firms, and the resulting credible threat of AD action facing foreign exporters, has contributed to the proliferation of voluntary export restraint agreements (VERs). As long as national AD laws create an environment in which AD actions, VERs, and market sharing arrangements proliferate, the level of intervention in trade is likely to be higher than otherwise, and the type of intervention more costly than necessary. In large part this is due to the fact that popular knowledge of both the level and the effects (costs) of these discriminatory trade policies is very limited.

Evidence of the attractiveness of AD procedures relative to other instruments of contingent protection is presented in Table 1. Clearly, AD is by far the most used instrument of contingent protection. Table 2 indicates that the U.S. and the EC in particular have been consistent users of AD, the number of instances where a protective action was undertaken remaining relatively constant since 1980.³ While most scholarly analyses focus on the interpretation and implementation of AD laws in various countries, and less on the effects of AD laws and the reasons they are used,⁴ we believe that it is of great importance to understand why AD procedures are apparently so popular and what the effects are of the ready accessibility of AD. This is desirable especially in the context of the ongoing Uruguay Round of negotiations. The fact that AD procedures can be used as a substitute for nondiscriminatory safeguards may restrict the types of agreement on safeguards that are possible. In particular, since AD actions are inherently discriminatory

³Statistics pertain to the number of final affirmative actions undertaken, both duties and undertakings (price or quantity agreements).

⁴This pertains especially to the legal and policy-related literature.

and currently in wide use, this suggests that the practical relevance of a nondiscriminatory safeguards agreement may not be very great, even if one can be negotiated.

Much in this article is at odds with the popular perception of AD laws. In large part this is because a systemic point of view is taken, which focuses on the economy-wide effects of AD. The hypothesis of this article is that a substantial proportion of AD actions are substitutes for safeguard actions, and that much of the remainder reflect rent-seeking behavior on the part of the domestic import-competing industry.⁵ While this is not a new thought, the importance and relevance of this hypothesis for the future of the multilateral trading system is often overlooked, especially by those who take a purely legal view of dumping and AD. Unfortunately, this appears to be the case for many policymakers involved. One of the justifications for writing what is largely a review article is to provide a contrasting view to those who see AD as a crucial — and GATT-sanctioned and thus legitimate — weapon in the arsenal of policies to protect a nation's industries from "excessive" foreign competition.

The plan of this paper is as follows. In Section II we discuss the circumstances under which dumping can occur, and conclude that the conditions under which dumping can occur are more extensive and varied than is commonly thought. Section III focuses on possible rationales for reacting against dumping. In Section IV we discuss the inferiority of AD as an instrument of protection, while Section V discusses possible reasons why resort to the AD instrument is nevertheless so common. In Section VI we turn to the implications of the existence of AD rules for the trading system in general and the Uruguay Round in particular. Various reforms are suggested that would improve upon the status quo, and that can be implemented unilaterally. Section VII closes with some concluding remarks.

⁵In general, of course, all AD petitions reflect rent-seeking behavior. The degree to which a "healthy" firm can abuse AD procedures by turning its legal department into a profit center that harasses foreign competition is constrained by the injury requirement. However, injury is not well defined in the context of AD, and examples exist of profitable firms obtaining import relief (Caine, 1981).

II. Rationales for Dumping

Dumping is defined in Article VI of the GATT as offering a product for sale in an export market at a price below “normal” value. Normal or “fair” value usually denotes the price charged by the exporting firm in its home market. In the absence of home market sales, the highest comparable price charged in third markets or the exporting firm’s estimated costs of production may be used to determine normal value.⁶ GATT rules allow actions against dumping if it can be shown that the dumping has caused or threatens material injury of domestic import-competing firms.

There are varying conceptions of dumping embodied in the GATT language and in national implementing legislation. While spatial price discrimination is sufficient, it is not necessary for dumping to occur. In U.S. law, for example, if prices charged by the exporter in its home market are below costs, products sold in the U.S. can be considered to be dumped, even if the prices charged are above those in the home market (so that technically reverse dumping may be taking place). In those cases where the home market is too small or nonexistent, the cost criterion will be used. In AD practice, cost-based investigations follow a so-called “constructed value” methodology. That is, “fully allocated costs of production” are calculated and summed with a fictive profit margin to arrive at a constructed value. This value is then compared to the export supply price. In what follows, we shall use the term “price-dumping” to refer to the price discrimination case, and “cost-dumping” to refer to the case where prices are less than cost, and home sales are small or nonexistent.⁷

⁶Under the cost criterion, economists generally would define dumping as selling below marginal costs. In practice, presumably in some part due to the nonobservability of marginal costs, average costs are usually taken as the criterion. However, marginal cost based dumping has been investigated. According to Caine (1981, p. 712) the U.S. ITC issues its first marginal-cost based cease and desist order in 1978 when an exporter was ordered not to sell in the U.S. at a price “below the reasonably anticipated marginal cost.”

⁷There are variants under both price- and cost-based procedures. If, for example, exports originate in nonmarket economies, constructed values often are calculated using the factor prices prevailing in developed economies.

The standard theoretical explanation of dumping postulates a static world without uncertainty where dumping will be rational and deliberate if three requirements are met.⁸ First, markets must be segmented, i.e., the exporter's home market must be sealed against secondary sales. This is because barriers to reimportation are needed if price differences are to be maintained. Without such barriers, price differentials across markets will tend to be eliminated by arbitrage. Second, the exporting firm requires market power in at least one market so as to be able to influence the price. Third, demand in the export market must be more elastic than at home. If these conditions are not met, the rational price-discriminating exporter will charge an export price at, or above, that set in the home market.

Once uncertainty is introduced into the trading environment, these standard conditions are no longer necessary for dumping to occur.⁹ Thus, market power is not necessary as it is quite possible for an exporter to act as a price taker at home and abroad, and yet have sales taking place at different prices *ex post*, after the resolution of uncertainty. Simple exchange-rate uncertainty can produce this outcome. If there is market power, different elasticities are not necessary for dumping to occur. Again, some source of randomness at the time the exporter's decisions are made can generate *ex post* dumping. As demonstrated by Blair and Cheng (1984), both managerial attitudes toward risk and demand uncertainty abroad may cause a price setting firm to choose a price in its export market below that in its home market, even if the price elasticities of demand across markets are identical.

In a world without uncertainty, dumping is always deliberate. Once uncertainty is introduced, however, dumping may be unintentional. For example, it is well known that

⁸See, for example, Viner (1923) or Corden (1974). These are necessary and sufficient conditions.

⁹For analyses of dumping in the context of uncertainty, see Bernhardt (1984), Blair and Cheng (1984), Hillman and Katz (1986), Katz, Paroush, and Kahana (1982), and Leidy and Hoekman (1988).

unexpected changes in exchange rates may lead a firm to dump even if it had no intention of doing so.¹⁰ Market structure and firm strategy may then become irrelevant as a determinant of dumping, and dumping can arise in any context. While market segmentation will be required for price differences to occur ex ante, in a setting where exchange rates fluctuate widely even this may no longer be necessary. However, in practice market segmentation will usually be the primary necessary condition for price-dumping to occur. The question then arises: is international market segmentation common? For many products and industries the answer is yes. Product differentiation, variations in tastes, trade policies and regulatory regimes, differing product standards, etc., all work to segment markets. The result is that the trading environment often will be quite conducive to acts of intentional and unintentional price-dumping.

As noted above, selling below average total cost can also constitute dumping, and it is not strictly necessary that prices charged in the export market be below those charged at home. In practice, the cost criterion is used primarily in cases where home market sales are too small to produce reliable information. The issues of market power and differing price elasticities then become irrelevant, as does the need for market segmentation. The cost-dumping case is important in practice, because many exporters produce exclusively or predominately for export, or sell only specific products for export. Often it may be in a firm's interest to sell below variable or even marginal costs for a while. Accepting losses in the short run may be a requirement to establish (or increase) market share, and/or to enable the firm to move down its learning curve, thus presumably increasing expected long-run profits. There may be economies of scale to exploit. Since

¹⁰The combination of random dumping (induced by exchange rate fluctuations) and the existence of AD laws has been modelled explicitly by Leidy and Hoekman (1988) in order to investigate the production decision of exporting firms in such an environment.

economies of scale are important in many industries, the existence of a cost-based definition of dumping further expands the potential applicability of AD.¹¹

The dual definition of dumping, the possibility of deliberate and unintentional dumping, and the relatively weak conditions necessary to produce an environment hospitable to both types of dumping, all suggest that its occurrence as defined by law will be frequent. And this means that antidumping policies have a much broader reach than is often realized. Petitioning for relief under AD laws is a popular intervention-seeking activity in part because instances of technical dumping are widespread. The import-competing firm's opportunity to use the AD laws to obtain (temporary) relief from foreign competition is in no way limited to instances of strategic (perhaps predatory) dumping, as is often suggested.

III. Rationales for Antidumping

The original theoretical rationale for AD law is due to Viner (1923). He argued that AD authority may be needed to protect domestic consumers from predatory (anti-competitive) dumping.¹² The fear was that a foreign firm (or cartel) might deliberately price products low enough to drive existing domestic firms out of business, then establish a monopoly. Once established, the monopolist could more than recoup its losses by exploiting the resulting market power. For this scenario to be plausible, however, the monopolist (cartel) must not only eliminate domestic competition, it must establish a global dominance. It is difficult to conceive of this occurring in most industries, and in practice cases of

¹¹In the long run, assuming entry is possible, one should observe average cost pricing in industries subject to scale economies, implying that dumping no longer should occur. For a theoretical analysis of dumping at less than marginal cost, see Davies and McGuinness (1982) and Ethier (1982).

¹²Viner distinguished three forms of dumping: sporadic, short run, and long run. Only the second form justifies a reaction in his view, as only this form of dumping can be construed as anti-competitive. Firms should be able to adjust to the first form, and the gains to consumers outweigh the losses to domestic producers in the last case.

successful predatory dumping remain undocumented.¹³ Even laboratory experimental work by Isaac and Smith (1985) has failed to produce any evidence of predatory pricing. In addition, if predation is intended, the multinational firm(s) involved must price low in all markets, and must take into account the possibility of retaliation by competitors (price war, for example) during the predation period. Further, even if all competitors worldwide were driven from the market, to be able to successfully exploit market power over time, barriers to entry in the post-predatory phase must be present.¹⁴ And such barriers to entry are rarely present without the support of a government regulatory agency. All of this calls into question the original theoretical justification for AD law.

Sometimes the conclusion is drawn that the appropriate procedure to combat anti-competitive behavior is through anti-trust laws.¹⁵ In the unlikely event that an anti-competitive outcome develops from a strategy of predatory dumping, this could be challenged under existing antitrust or competition laws, assuming that problems related to extraterritorial enforcement can be overcome.¹⁶ The issue of predation ultimately is an empirical one. The empirical work that has been done suggests that it is virtually never a consideration in AD cases. A number of investigations have shown that market shares of

¹³See, for example, Koller (1971). One qualification comes from Grey (1986, Chapter 2, footnote 41). He observes that recently “there are antidumping cases in which the margins appear to be so great, and the quantities so large, that it would be inappropriate to rule out predation.” He points to the case in 1985 when Japanese firms were allegedly dumping 64k D-RAM chips in the U.S.

¹⁴In the case of a cartel, another necessary requirement is that it remains stable. In practice, this requirement has often been difficult to meet for any substantial length of time.

¹⁵See, for example, Yarrow (1987) and Grey (1986).

¹⁶Indeed, even prior to the point when a monopoly position can be established the antitrust or competition laws may provide some relief to domestic firms. As Grey (1986) notes, the U.S. firm that initiated AD proceedings against Japanese manufactures of D-RAM chips in 1985 also filed an *antitrust* action.

affected exporters in the domestic market are often very low, sometimes less than one percent.¹⁷

In using the predation rationale for AD, purportedly the interests of consumers are being advanced, not those of import-competing firms. Yet in the absence of successful predation the imposition of AD duties can only harm domestic consumers. As AD actions cause exporters to recoil from the foreign market, competitive pressures are diminished and domestic prices move upward.¹⁸ It is rather paradoxical that vigilant and enthusiastic application of AD by policy officials tends to promote the result that it is supposed to combat under the predation justification: monopoly pricing.

Given the lack of documented attempts at international predatory behavior, let alone success stories, in practice AD can only be aimed at protecting the welfare of domestic producers. This is recognized by most observers, and is reflected in the wording and implementation of virtually all current AD legislation.¹⁹ AD is justified by governments by pointing out that it has been agreed internationally that dumping is an "unfair" trading practice. What is meant by unfair is unclear. Usually, unfair competition appears to imply that foreign firms benefit from an environment (usually due to government policies) that is not available to domestic import-competing firms. The implication is that foreign firms are "subsidized" in some fashion by their governments (or,

¹⁷Messerlin (1988), Tharakan, Caine (1981), UNCTAD (1984).

¹⁸Messerlin (1988) observes that in the first year after AD proceedings are initiated, imports of the allegedly dumped good declined by 18% on average. Further, "three or four years after the initiation, quantities still imported represented only two-thirds of the imports of the initiation year" (p. 11). And the impact on domestic prices is not limited to the dumped product. Messerlin finds that, in the first few years after the imposition of antidumping measures, the 'nondumping' exporters tend to align their prices, i.e., to increase them" (p. 18).

¹⁹EC legislation is an exception, but in practice its provisions that take into account the welfare of consumers have not had much effect. According to Messerlin (1988) the "teeth" of the community interest clause were rapidly removed with the introduction of a requirement that at least one domestic producer remain in existence. Of course, if only one (or a few) domestic firms exist there is likely to be a noncompetitive environment that may violate competition laws. But, this is not relevant in the context of AD.

that domestic firms are “taxed”).²⁰ This subsidization may occur through on- or off-budget means. For example, being allowed to have a monopoly position at home or being protected by a tariff or NTBs could be viewed as a form of off-budget aid. Often, this type of aid may be the cause of the market segmentation that allows dumping to occur. On-budget aid includes, of course, direct subsidies, and perhaps indirect subsidies of various sorts.²¹ Thus, when governments speak of unfair trade, they mean distorted trade. Whether there is a coherent rationale for addressing such disparities (distortions) facing firms of different nationalities will not be addressed in this article.

Regardless of the answer to this question, reacting against price dumping through AD is ill-conceived. AD is an inferior instrument to remedy an “unfair” practice because it does not address the source of the problem, which, in the context of dumping, must be those policies which artificially segment markets. The problem is to open up the foreign market, thereby eliminating the opportunity to dump. An AD duty can do little to achieve this end. Indeed, AD will only add distortions. As discussed in the next section, the mere existence of AD legislation distorts decision making. The threat of AD induces rent-seeking behavior on the part of import-competing firms, and leads exporting firms to alter production, allocation, and production-location decisions. Once an AD action has been taken the distortions change, but they do not disappear.

The same argument also applies to cost dumping. It can be argued that whether cost dumping is unfair depends on what allows it to occur. If it is part of the strategy of the firm and is financed by it, there does not seem to be much of a justification for invoking

²⁰The “taxation” rationale presumably drives recent EC AD actions against Hong Kong, even though Hong Kong is as close to a free market economy as one can imagine in practice.

²¹In principle, explicit subsidization should be addressed through countervailing duty investigations under auspices of the GATT and the GATT Subsidies Code (for signatories), and not by means of AD. However, the only substantial user of anti-subsidy investigations has been the United States. It is quite likely that AD procedures are being used to combat subsidization as well as import competition in general. Reasons include the need for investigation of sovereign practices and the greater uncertainty attached to anti-subsidy investigations.

AD.²² If it is due to direct or indirect government subsidization, anti-subsidy procedures should be used, not AD, assuming that there is a reason for intervening in the first place.²³

Insofar as the underlying problem is market segmentation due to government intervention, the best policy in general is to get the exporters home government to alter its policies. For example, it could use its anti-trust law to break a monopoly, or be induced to reduce the level of protection accorded to import-competing industries. While the political problem, of course, is how to induce the foreign government to follow this route, it is clear that AD does not have a useful role to play in this context.

To a large extent the issue of unfairness is really a red herring because dumping has simply been defined to be unfair. It appears clear that to a large degree the implicit rationale underlying AD policies is the same as that underlying safeguard legislation: to reduce competitive pressures in instances where imports are “disrupting markets.” In a substantial number of cases the root of the problem is a loss of competitive advantage.²⁴ A point to be emphasized here is that import-competing firms usually object to underselling, and not to price discrimination or selling below cost per se. Thus, de Jong (1968) has noted that “popular opinion refers to dumping when foreign producers are able to undersell the domestic supplier in his own market.” As described by de Jong, this notion was translated as “social” dumping in early discussions concerning AD legislation. While this term was not clearly defined, it was apparent that it referred to underselling by foreign firms in the domestic market. This was made possible by lower labor costs abroad (i.e., competitive advantage). In practice, underselling often lies at the source of a

²² Again, if there is an anti-competitive effect anti-trust laws may be invoked.

²³ Of course, some scholars may argue that the case for countervailing subsidies is not strong either.

²⁴ An exception being the case where cost dumping occurs as the result of explicit subsidization. However, in this context AD is a substitute for anti-subsidy (countervailing duty) investigations, and thus is being misused.

complaint, as what concerns importing-competing firms is not “unfairness” per se, but their inability, or unwillingness, to meet the price set by a foreign competitor. The concept of “social” dumping is not incorporated formally into AD legislation, this presumably being the *raison d’être* of emergency protection (safeguard) laws. However, the desire to address social dumping – i.e., import competition – certainly exists, and this is reflected in the use of existing AD legislation. But, as is discussed in the next section, AD is not the appropriate instrument to deal with problems of import competition.

In conclusion, AD policies are built on very weak theoretical foundations. The only possible rationale for AD is predatory pricing, something that is unlikely to occur and for which superior policy instruments exist. Furthermore, AD is incapable of addressing the underlying determinants of dumping (sources of “unfairness”) such as government sanctioned market segmentation.

IV. Inferiority of AD as an Instrument of Protection

A major effect of AD law is to make the world trading environment more uncertain for the exporting firm. This uncertainty leads exporters to recoil from export markets on the margin. To reduce the chance of facing AD procedures, firms will have a tendency to ship less product to the export market (thereby putting upward pressure on the export price), increase sales in the home market (putting downward pressure on the domestic price, assuming a home market exists), and, in addition, avoid underselling of import-competing producers. Thus, competitive pressure is likely to be reduced as a direct consequence of the existence of AD legislation.

There are a number of major incentive effects embodied in the existence of an AD threat. Some of these reduce, and others increase import competition. All of them act to distort the behavior of producers. A number of these distortions will be discussed briefly in this section. First, by adjusting domestic output the firm can trade off revenue in its home market against expected revenue earned abroad in the event of an AD action. Under plausible conditions it can be shown that in the case of price-based AD investigations a

firm will have an incentive to increase sales in the home market for any given level of total production (Leidy and Hoekman, 1988). By doing this, the ex post damage of an AD action —if it occurs — is reduced, as is the probability of an affirmative dumping finding. A second effect of the price-based AD law is that the expected marginal revenue in the foreign market declines for any given level of exports. This occurs since the marginal revenue of output allocated to the foreign market is zero in those states where the AD constraint becomes binding. When the AD constraint is binding, ex ante variations in the volume of product shipped abroad can have no effect on the revenue earned in that market ex post. The firm, therefore, has an incentive to reduce shipments to the foreign market for any given level of total production and domestic supply. Thus, the AD threat acts to reduce import competition. Observe, however, that the extent to which import competition declines is diminished to the extent that home-market sales are increased.

Under a cost-based AD investigation the exporting firm will not be able to change domestic sales to reduce the dumping margin. This is because long-run average total costs are given and this is usually the basis for the calculation of the dumping margin in such cases. Interestingly, according to Messerlin (1988), over 90% of recent EC cases against developing countries were cost-based. This statistic is consistent with the conclusion in Leidy and Hoekman (1988) that “there exists an incentive for import-competing firms to signal their preference for AD investigations that use an average-cost rule.” Cost-based AD is more pernicious than price-based dumping, both because the (potentially) affected exporter has fewer options at his disposal to avoid AD actions, and because they open the door to more ad hoc behavior on the part of investigating agencies.²⁵

A third effect of AD threats is that foreign producers will have an incentive to relocate productive facilities. The same factors apply here as in the case where foreign direct investment in the country imposing a tariff is motivated by locating behind the “tariff wall.” While causation is difficult to determine, one can point to the fact that

²⁵See footnote 30.

Japanese direct investment in the EC increased by 90% in the year following the introduction of legislation intended to deal with circumvention of AD duties through "screwdriver" or assembly operations (de Clercq, 1988). The result is likely to be less competition and more costly production, and thus higher prices for consumers (assuming the foreign producer is allowed to establish at all). Additionally, as noted by Webb (1987), AD also embodies incentives to shift production facilities from one foreign location to another. In general, the use of local content rules in conjunction with AD policies will increase efficiency costs even more. One of the more controversial recent developments on the AD-front has been an expansion of the law in certain countries to cover components (input dumping) and the establishment of minimum local content rules. An example is the EC "screwdriver-plant" regulation, which is now incorporated into the Community's basic AD instrument.

The result of these various incentive effects is that the existence of a AD threat will induce an exporting firm to react *ex ante*. *Ex post*, of course, if an AD action materializes, affected firms will be severely constrained. It has been calculated that three years after their imposition, AD measures on average reduce import volumes from the affected countries by about 40%.²⁶ But, AD actions are discriminatory, and thus will often not be effective once invoked. It is well known that selective protection is usually porous protection, in that incentives are created to circumvent the actions. Thus, the effect is trade diversion and incentives to relocate production. As AD duties and other measures such as undertakings apply to all the firms of a nation (regardless of the fact that some may not have been dumping) diversion should be understood as firms from unaffected nations taking up the slack. Interestingly, AD measures apply to all firms of a specific country because of the realization that otherwise diversion between firms of the

²⁶Messerlin (1988). See also UNCTAD (1984).

nation involved would certainly occur.²⁷ Because selective actions are ineffective, the incentive effects of AD threats can be considered to be inappropriate. Indeed, if the de facto rationale of AD is to protect import-competing firms, it is clear that imposing the constraint of having to demonstrate dumping simply distorts behavior of exporters for no good effect. A nondiscriminatory instrument would avoid these distortions, as well as the (gradual) cartelization of the world market that may occur as the system of bilateral measures is expanded to cover all producers.²⁸

This conclusion is strengthened once the link between AD investigations and the negotiation of VERs is taken into account. Because an AD action will hurt the affected exporter, a credible AD threat may be sufficient inducement to persuade exporters to agree to a VER. By doing so the exporter at least is able to capture some of the VER-generated quota rents, while the import-competing firms experience a (short-run) reduction in competition. The problems of VERs are well known, however. They include the fact that it is not a transparent form of protection and can easily lead to cartelization and monopoly pricing. But, of course, these "problems" will be perceived as advantages by import-competing firms.²⁹

The major effect of AD laws (threats) and measures is to raise prices in the importing market. This implies the creation of rents, paid by consumers. And in practice these rents can be quite large (Messerlin, 1988). It should also be noted that one outcome

²⁷On the ineffectiveness of discriminatory protection in general, see Baldwin (1982), Crandall (1987), de Melo and Messerlin (1988), and Yoffie (1983). In the specific context of AD, Messerlin (1988) found for the EC trade diversion effects (both intra- and extra-EC) were substantial.

²⁸See, for example, Hoekman (1988) and the references cited therein. It would also simplify substantially the administrative burden on exporters when faced with AD actions. Currently, involvement in an AD investigation is quite costly, both in terms of direct costs of legal counsel, and indirect costs of documenting the case, retaining links with importers, etc.

²⁹In this connection we can also note that AD is sometimes used as a device to monitor existing VERs or minimum price agreements. Steel provides an example. See UNCTAD (1984) and Koulen (1988).

of the price-fixing effect of AD laws is that firms will be inhibited from competing on price, and will shift to competing on quality. Even though AD protection is porous, it does foster a (short-run) reduction in competition, both through AD actions themselves and the threat of such actions. These are important substantive reasons for the preference firms show for AD. Of course, from an economy-wide perspective they also provide an important argument against AD. Nevertheless, the fact remains that selective actions often cannot be effective beyond the short run. This implies that procedural reasons must be just as important in explaining the revealed preference for AD as the substantive ones.

V. Further Explanations of the Revealed Preference for AD

In large part, widespread use of AD procedures in Australia, Canada, the EC, and the U.S. occurs because, in comparison to safeguards laws, access to AD procedures is easier, requirements more transparent, and the probability of an unexpected outcome lower. Also, while AD is a less efficient instrument than a nondiscriminatory action, it was demonstrated above that it will have some protective effect, especially in the short run.

In the European Community antidumping legislation is the most attractive (and sometimes the only) route for firms to take if they desire to obtain relief from import competition, as private parties do not have direct access to the safeguard law in the EC (Norall, 1987). One might expect, however, that, given a choice, safeguard procedures should be more attractive to firms hurt by import competition than AD. There is, after all, an extra burden of proof associated with AD: showing that dumping has occurred. Both procedures require that injury be demonstrated. But, as noted below, the material injury standard of AD procedures is less demanding than the serious injury standard required for safeguards (Article XIX) protection. Also, as argued above, it may not be much of a constraint to demonstrate that dumping has occurred as it can be expected to take place under a wide variety of circumstances. Further, to the extent that methods of determining

dumping margins by investigators are flexible, demonstration of dumping may even be possible in cases where home and foreign prices are identical.³⁰

Given that establishment of dumping often may not be much of a constraint, all the other procedural aspects of AD law are more likely to lead to a positive finding than those under safeguard procedures. The latter is subject to political discretion, as there is a need to take into account retaliation/compensation. GATT language, after all, allows for retaliation if emergency protection is imposed in those cases where compensation has not been offered, or is deemed to be insufficient. This is not the case under AD procedures since dumping has been defined to be countervailable as long as injury can be shown.³¹ But, the injury requirement of AD procedures is less stringent (easier to satisfy) than the one under safeguard procedures.³² Also, in the case of safeguard procedures, most countries require policymakers to take into account the effect of imposing protection on the economy as a whole. This will reduce the likelihood of an affirmative action. Related to this is the possibility that foreign policy considerations may inhibit action on the part of the policymaker. This is less likely to occur in the case of AD. The law stipulates the necessary conditions for an affirmative finding. If these are met, AD duties will be imposed (unless a VER is negotiated or the exporter makes an undertaking to remove the

³⁰In general, as AD legislation and procedures are quite complex, there exists a possibility that AD can be used/abused by investigating agencies to maximize the probability of an affirmative finding. Such an approach may be driven in part by broader political considerations. To the extent that such a possibility exists, it obviously will influence the attractiveness of initiating an AD case. Hindley (1988, 1989) has made a case that such a situation has prevailed in the EC context, in that EC investigation procedures in certain cases appeared to be biased in terms of both finding dumping and determining the dumping margin.

³¹Of course, AD does generate rents, so that there is an element of compensation. Also, one can expect retaliation in the sense of trading partners becoming more assiduous in applying their trade policy laws, or in developing them if these do not exist. This has happened to a certain extent, witness the intensive use of CVD actions in Chile, the first actions in Japan, and the recent implementation of an AD law in Mexico. See Stern, Jackson, and Hoekman (1989) on the first two, and GATT (1988) on the last.

³²See Caine (1981) and Jackson (1986). Article XIX speaks of "serious" injury, while AD language speaks of "material" injury. Neither is well-defined, but in national implementing language, serious injury is a more stringent criterion than material injury.

injury). If they are not met, a negative determination will follow. Furthermore, AD actions are permanent in the sense that there is no automatic degressivity of the measures imposed or time limits to these actions.

Finally, domestic import-competing firms may prefer AD laws because provisional measures are available. Even if the the investigation determines that no injury occurred, provisional measures may be sufficient to inhibit exporters. In the first place, these provisional measures may lead to substitution of demand away from the products under investigation. Once trading relationships have been severed, they may be difficult to re-establish. Also, risk averse importers may not want to be affiliated with producers that are "tainted," and that may be the target of other actions. Secondly, the existence of provisional measures tends to increase the pressure on exporters to agree to a VER.

VI. Implications for the Trading System and Suggestions for Improvement

From a normative perspective, AD actions are clearly an inefficient way to deal with problems of import competition. To a large degree, AD legislation and measures act as a system of selective safeguards. From a multilateral perspective the general problem is that the incentives facing firms are biased towards requesting, and receiving, discriminatory forms of protection. Thus, to alter the status quo requires that these incentives be changed. This can be done unilaterally or multilaterally. Safeguards and AD are presently being discussed multilaterally in the context of the Uruguay Round. As is well known, recurring negotiations on safeguards have never led to agreement. The problem, especially in the Tokyo Round, was that certain nations desired to be able to impose emergency protection (safeguards) on a unilaterally selective (discriminatory) basis. Even if this preference for unilateral selectivity has diminished, the value of a nondiscriminatory agreement for those countries against selective actions is uncertain, given that discriminatory procedures such as AD will continue to exist.

One could argue that AD legislation would have to be revoked for an agreement on safeguards to be meaningful. While this will go too far for many observers, it should be

remembered that the case against AD legislation is independent of the fact that AD can be used as a substitute for emergency protection. Even though from a theoretical perspective revocation of AD legislation arguably is the optimal policy to follow, in practice it is extremely difficult to repeal a law.³³ If one is forced to accept some form of AD law, it is necessary to consider alternative policies. There are three possibilities: (1) make use of AD more difficult and costly and limit its scope; (2) make safeguard procedures more "user friendly" and increase the probability of obtaining temporary, nondiscriminatory protection; and (3) do both at once. There are dangers attached to some of these options, in that the resulting outcome may be worse than the status quo. If, for example, only (2) is followed, import competing firms may find it easier to obtain protection and access to markets may worsen.

It appears likely that a number of countries will continue to broaden the scope of AD legislation. In the context of the safeguards discussions, this may be the worst possible outcome. Expansion of the scope of AD has been the trend in national practices/legislation. Examples include EC actions against "screwdriver" operations and input dumping, as well as the alterations to U.S. law such as anticircumvention and third-party dumping provisions.³⁴ The implication of these trends for the future are worrisome, to say the least, especially as regards the possibility of ever achieving effective multilateral discipline on measures of emergency protection. Another reason for concern is that developing countries have begun introducing and using AD laws (GATT, 1988). As argued by Messerlin (1988), the use of AD by these countries in conjunction with the fact that they are increasingly the target of AD actions jeopardizes the unilateral liberalization efforts that many of them are undertaking. It is unclear why these nations are enacting AD legislation, but a "demonstration effect" will be part of the answer.

³³Arguments for repealing AD legislation have been made periodically in the literature. Two examples are Barcelo (1979) and Caine (1981).

³⁴See, e.g., Norall (1987, 1989) on the EC, Horlick and Oliver (1989) on the U.S. Omnibus Trade and Competitiveness Act of 1988, and GATT (1988) in general.

In the remainder of this section the focus will be on two approaches to improve upon the status quo. One line of action is to make safeguard laws more attractive to use; another is to make AD actions focus more on economy-wide considerations. As there is not much wrong with most safeguard laws from an economic perspective, a major improvement would be to increase the use of safeguard procedures relative to AD and other forms of discriminatory protection (such as VERs). The underlying objective would be to reduce the incentive to invoke AD legislation. This requires that access to safeguard laws be made easier. As mentioned above, private parties in the EC have no direct access to the safeguard law. One possibility in increasing the relative attractiveness of safeguard procedures is to get rid of the compensation "requirement," as it is often argued that the need for compensating affected exporters (taking the possibility of retaliation into account) inhibits the use of safeguards. However, it may not be necessary to do away with compensation. One way to offer compensation without a drain on the government budget and without antagonizing other domestic industries is to implement a proposal made by Deardorff (1987). He suggests that the remedy in a safeguard case be a temporary global quota set at a level no less than some base year level of imports. Quotas would be allocated to all exporting countries and they would be transferable between countries. This should imply that there will be only one quota premium, equivalent to some MFN tariff, so that the ideal of nondiscrimination is approximated, and all nations receive some compensation (i.e., the quota rent). There is a substantial literature on how to improve Article XIX-type protection, but space considerations prohibit the lengthy treatment this subject deserves.³⁵

Turning to improvements of AD, a good approach would be to introduce more "safeguard-like" elements. Five suggestions to this effect are made below.

³⁵Recent contributions on this topic include Hoekman (1988), Jackson (1986), Sampson (1987), and Richardson (1988).

1. Incorporation of a national interest clause in AD procedures would be a major improvement. It would imply that before an affirmative finding can be made, a cost/benefit analysis should indicate that for the nation as a whole protection of an industry is worthwhile. A weaker version of this idea would be to allow consumer interests to have a greater voice in AD proceedings than is presently the case. If it were required that all users of the products (both final consumers, if any, and firms using the affected products as inputs) be offered a voice, the likelihood of affirmative actions might diminish.

2. Injury requirements could be made more stringent and more difficult to satisfy. Presently material injury is not defined clearly, and domestic laws allow for a number of injury indicators. The number of indicators could be decreased dramatically.³⁶ Another possibility would be to remove the provision that threat of injury can be sufficient for the imposition of an action. The potential for abuse of this language is obvious.

3. Remedies should be made degressive. For example, the AD duty could be decreased by a fixed proportion per year. There could also be time limits to actions and a prohibition for reapplying for assistance within a certain time frame. Furthermore, undertakings could be forbidden. These are often equivalent in effect to VERs, as the exporter will capture part of the rents generated by limiting exports. One effect of this is that exporters are less likely to complain about the AD action. This, in conjunction with the fact that protection is less visible implies that it will be less clear to consumers what is occurring. The resulting lack of transparency inhibits the implementation of less costly policies.

4. Another improvement would be to require participation by anti-trust bureaus in AD cases. These agencies should have the power to veto actions deemed likely to be harmful to competition. This procedure would be perfectly consistent with the predation argument for AD, of course, as presumably one is concerned with (emerging) monopoly.

³⁶The question of which indicator should be used is a separate one that should also be addressed. Some of the current ones have little economic justification as they often may be satisfied for industries that are highly profitable (Caine, 1981).

Nonacceptance of such a proposal could be taken to confirm the general belief of economists that AD is not really directed against predation.

5. An related possibility is not to look at likely effects but whether there is predatory intent. Again, given that the only possible theoretical rationale for AD is the predation argument, one could argue that use of AD should be limited to such cases. Of course, it will be quite difficult to establish the intent of the dumping firm. However, one could require that certain necessary conditions be met that are expected to be positively correlated with the possibility of predation. Market share and concentration ratios are obvious possibilities in this connection. For example, it could be required that firms that are dumping have $x\%$ of the global market, and that there exist at least a concentration ratio for the global industry of $y\%$.³⁷

VII. Concluding Remarks

In this paper we have argued that there is no compelling rationale for AD polices and that in practice AD is used as a way of reducing import competition. The consistent use that is made of AD (as illustrated in Table 2) and the trend that exists in terms of expanding its scope have implications for the trading system. In particular, AD offers a discriminatory form of protection that is often not transparent and distorts production, consumption, and trade. Its existence is likely to have implications for any Uruguay Round safeguards agreement, as in practice AD provides an alternative to safeguard-type temporary emergency protection. Various possibilities were identified in terms of improving the current situation, all of which can be implemented on a unilateral basis. However, the value of unilateral action will be limited from a global perspective, and multilateral agreement would be the preferred option. This is a negotiation problem, of course. As indicated above, the revealed preference of the major trading nations appears to be to expand the scope of AD legislation. Thus, to achieve any of the suggestions made

³⁷What these percentages might be is left open. As noted above, in practice market shares of countries facing AD investigations are often negligible.

above in a multilateral context will require active efforts on the part of those affected parties that recognize the social and systemic costs involved in carrying out AD actions.

References

- Baldwin, Robert E. 1982. "The Inefficacy of Trade Policy," Essays in International Finance No. 150, Princeton University.
- Barcelo, John J. 1979. "The Anti-dumping Law: Repeal it or Revise it," in Antidumping Law, 1 *Michigan Yearbook of International Legal Studies*.
- Bernhardt, Dan. 1984. "Dumping, Adjustment Costs and Uncertainty," *Journal of Economic Dynamics and Control*, vol. 8.
- Blair, Roger and Leonard Cheng. 1984. "On Dumping," *Southern Economic Journal*, pp. 857-65.
- Caine, Wesley K. 1981. "A Case for Repealing the Antidumping Provisions of the Tariff Act of 1930," *Law and Policy in International Business*, 13, 681.
- de Clercq, Willy. 1988. "Fair Practice, Not Protectionism," *Financial Times*, London, November 21.
- Corden, W. Max. 1974. *Trade Policy and Economic Welfare*, Oxford: Clarendon Press.
- Crandall, Robert. 1987. "The Effects of U.S. Protection for Autos and Steel," *Brookings Papers on Economic Activity*, No. 1, pp. 271-88.
- Dale, R. 1980. *Anti-dumping Law in a Liberal Trade Order*. London: MacMillan for the Trade Policy Research Centre.
- Davies, Stephen and Anthony McGuinness. 1982. "Dumping at less than Marginal Cost," *Journal of International Economics*, vol. 12.
- Deardorff, Alan. 1987. "Safeguards Policy and the Conservative Social Welfare Function," in Henryk Kierkowski (ed.), *Protection and Competition in International Trade*. Oxford: Basil Blackwell.
- Ethier, William. 1982. "Dumping," *Journal of Political Economy*, 90, 487-506.
- Finger, J. Michael and A. Olechowski (eds.). 1987. *The Uruguay Round: A Handbook for the Multilateral Trade Negotiations*. Washington: The World Bank.
- GATT. 1988. *Review of Developments in the Trading System*. Geneva: GATT.
- Grey, Rodney de C. 1986. "Trade Policy and the System of Contingency Protection in the Perspective of Competition Policy," mimeo.
- Hillman, Arye and Eliakim Katz. 1986. "Domestic Uncertainty and Foreign Dumping," *Canadian Journal of Economics*, August.
- Hindley, Brian. 1988. "Dumping and the Far East Trade of the European Community," *The World Economy*, London, December.
- —. 1989. "The Design of Fortress Europe," *Financial Times*, London, January 6.

- Hoekman, Bernard. 1988. "Services as the Quid Pro Quo for a Safeguards Code," *The World Economy*, 11, 203-215.
- Horlick, Gary and Geoffrey Oliver. 1989. "Antidumping and Countervailing Duty Law Provisions of the Omnibus Trade and Competitiveness Act of 1988," *Journal of World Trade*, 23, 5-49.
- Isaac, R. Mark and Vernon L. Smith. 1985. "In Search of Predatory Pricing," *Journal of Political Economy*, vol. 93, no. 2.
- Jackson, John H. 1986. "The Role of GATT in Monitoring and Promoting Adjustment: the Safeguards System," Research Seminar in International Economics Discussion Paper No. 170, The University of Michigan.
- de Jong, H. W. 1968. "The Significance of Dumping in International Trade," *Journal of World Trade Law*, 2, 162-188.
- Katz, Eliakim and J. Paroush and N. Kahana. 1982. "Price Uncertainty and the Price Discriminating Firm in International Trade," *International Economic Review*, June.
- Koller. 1971. "The Myth of Predatory Pricing: An Empirical Study," *Antitrust Law and Economics Review*, 105.
- Koulen, Mark. 1988. "Steel Export Restraint Arrangements and U.S. Anti-dumping and Countervailing Duty Laws," Geneva, mimeo.
- Leidy, Michael and Bernard Hoekman. 1988. "Production Effects of Price- and Cost-based Antidumping Laws under Flexible Exchange Rates," Research Seminar in International Economics, Seminar Discussion Paper No. 224, The University of Michigan.
- Lloyd, Peter. 1977. *Anti-dumping Actions and the GATT System*. Thames Essay No. 9. London: Trade Policy Research Centre.
- de Melo, Jaime and Patrick Messerlin. 1988. "Effects of European VERs on Japanese Autos," The World Bank, mimeo.
- Messerlin, Patrick. 1988. "Experiences of Developing Countries with Antidumping Laws," mimeo.
- Norall, Christopher. 1987. "New Trends in Anti-dumping Practice in Brussels," *The World Economy*, 9, pp. 97-111.
- Norall, Christopher. 1989. "The New Amendments to the EC's Basic Anti-Dumping Regulation," *Common Market Law Review*, 26, 83-101.
- Richardson, J. David. 1988. "Safeguards Issues in the Uruguay Round and Beyond," in Robert Baldwin and J. David Richardson (eds.), *Issues in the Uruguay Round*. Cambridge: National Bureau of Economic Research.
- Sampson, Gary. "Safeguards," in J. Michael Finger and A. Olechowski (eds.), *The Uruguay Round: A Handbook for the Multilateral Trade Negotiations*. Washington D.C.: The World Bank.

- Stern, Robert, John Jackson, and Bernard Hoekman. 1989. *An Assessment of the GATT Codes on Non-tariff Measures*. Thames Essay No. 57. London: Gower, for the Trade Policy Research Centre.
- Tharakan, P.K.M. 1988. "The Sector-Country Incidence of Anti-dumping and Countervailing Duty Cases in the European Community," in L. Mennes and J. Kol (eds.), *European Trade Policies and the Developing World*. Beckenham, Kent: Croom-Helm Ltd.
- UNCTAD. 1984. "Anti-dumping and Countervailing Duty Practices," TD/B/979, Geneva, mimeo.
- Viner, Jacob. 1923. *Dumping: A Problem in International Trade*. Chicago: University of Chicago Press.
- Webb, Michael. 1987. "Anti-Dumping Laws, Production Location and Prices," *Journal of International Economics*, vol. 22.
- Yarrow, George. 1987. "Economic Aspects of Anti-dumping Policies," *Oxford Review of Economic Policy*, 3, 66.
- Yoffie, David. 1983. *Power and Protectionism: Strategies of the Newly Industrializing Countries*. New York: Columbia University Press.

Table 1

Protective Actions Under Alternative Instruments, 1980-1985

Country/Bloc	AD		CVD		XIX	VER
	init.	impl.	init.	impl.	impl.	impl.
Australia	416	138	20	7	4	1
Canada	230	152	11	4	4	7
Chile	—	—	140	—	—	—
EC	280	122	7	3	10	58
Japan	1	—	1	—	—	6
United States	350	129	281	96	5	48
TOTAL	1,277	541	450	110	23	120

Notes:

CVD: countervailing duty

init.: initiated

impl.: implemented, i.e. protective action undertaken. This could be either a duty or an undertaking in the case of Anti-Dumping and Countervailing duties.

Source: Finger and Olechowski (1987), GATT (1988), and GATT *Basic Instruments and Selected Documents*, various years.

Table 2

Anti-Dumping Actions by Major Country/Bloc, 1980-87

Country/Bloc	Period ⁽¹⁾	Initiated	Provisional measure	Duty ⁽²⁾
Australia	1980-82	n.a.	n.a.	n.a.
	1982-84	141	55	88
	1984-86	117	57	43
	1987-87	40	17	4
Canada	1980-82	93	43	23
	1982-84	50	88	50
	1984-86	62	54	44
	1987-87	24	12	10
ED ⁽³⁾	1980-82	61	15	35
	1982-84	59	28	46
	1984-86	57	17	40
	1986-87	17	12	18
United States	1980-82	66	20	53
	1982-84	65	61	43
	1984-86	124	80	38
	1986-87	41	55	40

Notes:

(1) Periods are from June to July.

(2) Includes undertakings.

(3) Covers only actions against GATT Contracting Parties.

Source: GATT, *Basic Instruments and Selected Documents*, various years.