Chapter 4 EXPORTS AND IMPORTS

4.1. Which Products to Export?

The extent to which countries control the products allowed for export within countertrade deals differs considerably. There are very few countries which allow countertrade partners to take out any products they please. Clearly, if no restrictions are imposed, it can be expected that countertrade partners will adopt the easiest course of action of taking out a developing country's main established export items and selling them to established customers. This involves a simple replacement of the country's commercial sales and involves no benefit to the country whatsoever.

Therefore, nearly all countries which engage in countertrade impose some restrictions on the exports allowed. In the case of counterpurchase transactions and the various forms of bilateral agreements, it is usual to have an export list of permitted products from which the partner is allowed to make a selection within the confines of any requirements that may be stipulated related to quantities and values of the products in question. In the case of barter-style countertrade, the country may specify export products which are allowed or may adopt a case-by-case approach of considering individual proposals as they arise.

The disadvantage for a developing country of having a published export list for countertrade is that it might limit scope for flexibility, whereas the advantage is that interested parties, both inside and outside the country, are informed about the export possibilities and time is not wasted on proposing countertrade deals that stand no chance of being seriously considered.

An alternative to producing an export list is to specify those products not allowed for countertrade. In Malaysia, for example, there are three specific exclusions: logs and sawn logs, crude palm oil and tin ore and concentrate. Also, goods produced in the Malaysian Free Trade Zone and in the Licensed Manufacturing Warehouses are not allowed for countertrade. Other products may be suggested for countertrade but all proposals are subjected to very close scrutiny by the Malaysian authorities.

A further alternative, if the developing country wants to avoid publishing an export list, is to operate a consistent policy which comes to be known and understood by the trading community. In Zimbabwe, for example, most deals have involved tobacco, short fibre asbestos and, occasionally, low carbon ferro chrome. There have been very few cases when other products have been allowed.

Whether an export list for countertrade is published or not, there are a number of issues to be addressed. These mostly relate to the question of how the developing country can ensure that countertraded exports are additional to the existing level of commercial sales. Cynics will say that the whole idea of additionality is a bogus concept, but at least the attempt must be made to examine the issues in greater depth.

4.1.1. Additionality

Perhaps the most important countertrade issue, and the most contentious, is whether or not countertrade can lead to incremental exports - the argument of trade creation versus trade diversion.

The issue becomes complex when an effort is made to define "additional sales" and, further, when any attempt is made to prove additionality.

In the first place a distinction should be made between share of the cake and size of the cake. Policy-makers in most countries are primarily concerned with increasing their own country's share of any given market and, therefore, view additionality in purely national terms. Additional sales in this case can be achieved by taking market share away from a competitor, while the size of the total world market remains the same. An alternative approach is to view additionality in terms of increasing the total world market for the product in question, i.e. increasing the size of the cake. This might be achieved, for example, particularly within the context of South/South countertrade, by countries increasing consumption of commodities received in countertrade which they would not otherwise be able to afford to import under commercial terms.

The importance of this distinction between size and share of the cake will be returned to, but for the time being the goal of increasing market share may be taken as paramount.

For any particular country, there are four broad categories of potential incremental exports through countertrade.

		Examples
(i)	Traditional exports to new buyers in an established market	African country X is a major exporter of a particular mineral. It regularly supplies end-users in the USA. If a countertrade deal involved supply to other end-user companies in the USA which were not previously customers, it could be argued that the sales were additional.
(ii)	Traditional exports to a country which was not previously a market for the product	South American country Y is a major exporter of frozen chicken. If sales could be commenced to a new market it could be argued that the sales were additional. This would particularly apply if the sales were to an Eastern bloc country or a developing country, either of which might be unlikely to purchase the item in question by paying in foreign exchange.

(iii)	Traditional exports to a country which was previously a market but no longer has foreign exchange available to make purchases	Caribbean country Z used to sell bananas to a North African country but shortages of foreign exchange resulted in the trade being stopped. If banana exports were restarted within the context of a countertrade deal it could be argued that the exports were additional.
(iv)	Non-traditional exports to almost anywhere	Asian country A is a major exporter of tea but has only recently installed facilities for the production and export of tea bags. If tea bags could be exported within a countertrade deal it could be argued that the exports were additional.

Any country may select one or more of these categories. Malaysia, for example, allows exports of some of its traditional exports such as palm oil and rubber (in circumstances specifically agreed by the Ministry of Trade and Industry) and is also encouraging exports of non-traditional items such as rubber gloves and furniture.

4.1.2. Bulk Commodities Versus Non-Traditional Exports

Most of the traditional exports which are countertraded by developing countries are bulk commodities. There are many arguments about the relative merits of countertrading bulk commodities as opposed to non-traditional exports, some of which are examined in this sub-section.

The most important countertraded exports from developing countries have been bulk commodities including oil, minerals and soft commodities. An argument can be put forward that it is not in the long-term interests of developing countries to countertrade such commodities except in limited and specified circumstances. However, countertrade partners nearly always prefer to obtain bulk commodities. They offer a means of assembling a sufficient value for the countertrade, the obligations can be easily assigned to trading companies, the products are usually sold on a standardised basis, the opportunity for using futures markets exists in many cases, and the countertrade discount required is quite small.

The first problem for developing countries is that countertrade nearly always involves extra costs which the developing country itself usually ends up paying. Therefore, if a developing country has surplus stockpiles of commodities such as cocoa, rice, tobacco, minerals and so on, even if the stocks are difficult to sell, it may well be in the developing country's interests to incur the expense of continued storage, or to sell conventionally at a discount rather than engage in countertrade which involves extra costs and may disrupt the world market for the product in question.

In recognition of these dangers, many developing countries try to insist on additionality but there are many problems in achieving this for bulk commodities. Firstly, the world market position for most commodities is either static or declining. In a post-recession era some growth may be re-established, but in the current situation there is no real growth and, except in unusual circumstances, general over-supply. Occasionally it may be possible to open up a genuinely "new" market through countertrade in an Eastern bloc country or in another developing country, but such circumstances are unusual. Secondly, it is virtually impossible in many cases for the developing country to check on the destination of the countertraded product. A commodity such as rubber may change hands many times before it reaches its final user. Thirdly, an apparent new market may be no such thing. For example, an occasion is known when a Western machinery exporter seeking "new" markets for an export from a South American country managed to identify an exporter who was about to begin supplying a new customer in Europe. The transaction was redressed as a countertrade, the government of the South American country thought a new market had been opened up, but in fact a conventional method of trade had been replaced by a higher cost method.

In practice, the countertrading of bulk commodities usually either means that the developing country displaces its own commercial exports or that it is trying to "steal" market share away from competitors within a finite market. The latter situation may result in short-term benefit, but in the longer term it is likely that the competing country or countries will be forced to follow the same countertrade line, as is happening now with a number of Indonesia's competitors, thus resulting in a general free-for-all within the market. The consequence of countertrading a bulk commodity will very often be that the world market price of the product is depressed. Additional supply to an already over-supplied market leads to a reduction in price. Furthermore, the practice of selling countertraded goods to the final buyer at a discount also exerts downward pressure on the price in the market as a whole.

Countertrading bulk commodities can probably only be justified in a limited number of circumstances, for example, if the product is actually sold at the world price and the foreign partner is forced to absorb any extra countertrade costs. Another occasion might be if there is a desire to circumvent national or international rules, but this practice involves its own dangers and may also result in depressing the world price. Another is if a really genuine new market can be found, possibly in another developing country, which would definitely not have purchased the product except within a countertrade transaction; perhaps, also, if the countertrade is organised on a long-term basis whereby the developing country gains the security of a guaranteed outlet. And lastly, perhaps in a distress situation where a developing country has warehouses full of, for example, tobacco, which it is having great difficulty selling and desperately needs fertilisers for field application in a few weeks' time. In such a situation a trading company may be in a position to take the tobacco to pay for the fertiliser in a way that the developing country could definitely not organise for itself in the time available. However, very many countertrade transactions involving bulk commodities do not fall within the circumstances outlined above.

The occasions when developing countries stand to derive much greater benefit occur when they are able to trade 'non-traditional' exports which would otherwise be difficult to sell on the world market. Non-traditional in this context means exports from a particular country which are either new or recently established. Such products may be industrial goods or agricultural products (the latter group including unprocessed items such as fruits and vegetables as well as value-added products such as canned goods, dried fruit, cocoa products, fruit juices and numerous other products). If the developing country in question can sell the products for cash there will almost certainly be no benefit in countertrading, but if the developing country faces difficulties, perhaps because of lack of marketing expertise, then countertrade may offer a beneficial from of trade, particularly if new markets can be opened up. If, however, the products are difficult to sell simply because they are of inferior quality or too highly priced, then they will be useless for conventional trade or countertrade.

There are many difficulties involved in countertrading "non-traditional" products, which the countertrade intermediaries such as trading houses and banks would be the first to point out. Indeed, many developing countries already pay lip service to the idea of countertrading non-traditional exports, but the practical difficulties involved have resulted in relatively few transactions being completed. From the foreign trading partner's point of view the countertrading of non-traditional exports, compared with countertrading bulk commodities, requires even more imagination, ingenuity, effort and risk. In brief, the difficulties include the problem of amassing sufficient value for a countertrade transaction from non-traditional exports, the problem of identifying availability of supply, the problem of price competitiveness, the problem of entering more protected markets, and the problem of higher discounts (disagios) being required for such products.

From the developing country's point of view, countertrading of non-traditional exports offers much greater opportunities for entering genuinely new markets with less risk of depressing prices for the market as a whole. By using outside marketing expertise within a countertrade transaction, a developing country might be enabled to open up a market which could prove to be lucrative for years to come. One danger, however, for the developing country is the possibility of unwittingly encouraging marketing dependence. This might be avoided by including a marketing training component within the overall countertrade deal. It is also important that the developing country closely examines the net benefits of countertrading non-traditional exports. If, for example, the export item has a very high import content, then the benefits of countertrade might be very limited. Some countries, including Jamaica, have operated a system whereby the countertrade value is separated according to the local content and foreign exchange content of the exported product.

Lastly, developing countries must be prepared to give some promotional support (funds for advertising etc.) in appropriate cases to develop markets for non-traditional exports, particularly consumer products.

4.1.3. Weighting of Countertrade Export Values

One approach to the question of bulk commodities versus non-traditional exports in countertrade deals, which has been adopted by a few countries, is that extra "weight" is given to certain non-traditional products and a lower "weight" is given to bulk commodities or established export items. The rationale for this is that finding markets for bulk commodities and established export items will usually be quite easy for countertrade partners whereas the much more valuable exercise, from the developing country's point of view, of selling value-added and non-traditional exports is likely to be much more difficult. In recognition of this, and to give an incentive to take out the more "difficult" products, a weighting system may be introduced.

For example, if a foreign supplier has a countertrade obligation to take out $10 million from developing country X, the Government of X might allow the obligation to be fulfilled in the following way:

Product	Invoice Value $ million	Weight	Countertrade Value $ million
Palm oil	5.0	0.5	2.5
Cocoa products (not beans)	5.0	0.7	3.5
Frozen chicken	2.0	1.0	2.0
Furniture	1.0	1.5	1.5
Machine tools	0.25	2.0	0.5
	13.25		10.00

This system is really only applicable to the counterpurchase or similar types of countertrade.

As noted in Appendix 5, India has adopted a variant of this practice as part of its own counterpurchase scheme.

4.1.4. Destination of Exports

As well as controlling the actual products allowed for countertrade, developing countries can also attempt to control the destinations of those exports. A common approach is to allow a particular product to be countertraded on condition that it is destined for a particular market.

Different approaches are evident on policy matters related to export destinations. Some developing countries insist that their exports must be absorbed within the partner country and will not allow the products to be sold in third countries. This is the general approach adopted in many cases by Malaysia, although it sometimes allows a proportion of the export quantity to be shipped elsewhere.

A somewhat different approach is adopted by Zimbabwe which will allow some commodities to be countertraded with Eastern bloc countries and developing countries but will usually only countertrade with OECD countries on the basis that Zimbabwean exports are not destined for the partner countries, the argument being that if OECD countries want Zimbabwean exports they can pay for them in cash.

The great difficulty in implementing any policies related to export destinations is that the danger exists that export shipments will be redirected or re-exported. Many instances are known where this has happened, involving products exported under bilateral clearing agreements and other types of countertrade. Some developing countries have complained that their exports have been resold for foreign exchange on world markets, thus causing disruption to that developing country's own commercial sales and general disruption to the market.

Various measures can be taken by developing countries to try to protect themselves against these practices but the problem remains fairly intractable. If the countertraded exports are manufactured goods, they are likely to be more difficult to re-export. Also, some degree of protection is offered if exports are shipped directly to end-users. But in many cases the export items are standardised bulk commodities, such as rubber or palm oil, which are difficult to check and monitor. However, some measures can be taken by developing countries and these are outlined in section 10.3.

4.1.5. Concluding Remarks about Exports

Considerable difficulties exist in selecting and implementing a policy concerning the exports allowed for countertrade. The overriding aim must be to achieve incremental exports but the great problem in attempting to calculate "additional sales" is that it is impossible to know with certainty what products would have been sold in other circumstances and, therefore, additionality can only be estimated and never measured.

The broad guidelines suggested here are as follows. The clearest benefits from countertrade are likely to be gained from sales of non-traditional exports but it must be recognised that the countertrade costs are higher and the problems of organising deals are greater. The countertrading of bulk commodities and other traditional exports should be limited to those cases where particular benefits exist. Also, the benefits of short-term increases in market share should be measured against the possibilities of market destabilisation, particularly if, eventually, all suppliers of a given commodity adopt the same practices. The greatest benefits, in terms of achieving additional sales, are likely to be achieved by countertrading with other developing countries which would not otherwise have been able to afford to buy the products with cash; this is one of the major reasons why the fastest rate of growth in future countertrade will probably be in South/South deals. This provides a means of increasing the size, as opposed to the share, of the cake.

A sensible compromise in the debate about traditional and non-traditional exports may be to include both in the same deal. If, for example, a $5 million deal is being structured, it may make sense to allow the countertrade partner to take out $4 million in a bulk commodity such as rubber and $1 million in non-traditional exports such as rubber goods (gloves, etc.). This compromise offers the opportunity of making up a sufficient value for the deal with a bulk commodity while at the same time encouraging the market development of a "new" added value export. Also, as noted in section 4.1.3, this approach may be reinforced by adopting a differential weighting system according to the exports selected.

4.2. Which Products to Import?

4.2.1. Choice of Imports

According to the type of deal or agreement, the products to be imported by developing countries may be specified in the contract or may be outlined in an indicative listing from which actual selections are made prior to trading. The latter is particularly the case with medium-term and longer-term agreements, and also some barter-style deals, which are based on the trading of a "basket" of products.

Whether or not it is in the interests of developing countries to import a basket of products is open to some question. There is an argument which states that developing countries are much better advised to accept one or a few products, or a project (turnkey factory, road, etc.), as the import component because the organisation and execution of such deals can be more easily carried out. The arguments which are sometimes advanced against basket deals are outlined in the following points.

(i) In the case of high value basket deals the administrative burden on the developing country importing the products is great. All the usual system of import licences and so on will operate and the problems of coordinating a great range of goods within the context of one deal may be more than the government departments can efficiently deal with.

(ii) In bilateral deals all the import goods will have to be sourced from the partner country, even though some of the products may be unsuitable or higher cost than the goods previously imported from elsewhere. In the case of very high value deals, great pressure may be placed on the business/industrial community to accept products from the bilateral partner which they would much prefer to source from other countries.

(iii) Dangers exist that the imports within basket deals may be split into too small "parcels", with the result that problems arise over lack of discounts, poor quality control and lack of spare parts and servicing arrangements.

The proponents of basket deals, on the other hand, point out that they offer developing countries a way of coordinating imports while at the same time developing exports. It is also important to distinguish between those which are organised by trading houses or similar organisations and governmental bilateral agreements. In the former case, the trading house is not limited to one country of origin and may source the goods from wherever the developing country wishes, thus overcoming at least one of the disadvantages outlined above.

4.2.2. Quality Control of Imports

Many of the horror stories of countertrade relate to tales of shipments of left-handed gloves, bicycles with a two week life span and so on. Clearly such dangers are apparent in all forms of trade but it is sometimes suggested that the problems are worse in countertrade.

The accusation is sometimes made against Eastern bloc countries, in particular, that their higher quality goods are sold for foreign exchange and the lower quality items are channelled through reciprocal trading agreements. Similar complaints are levelled at some suppliers in OECD countries.

One of the problems in countertrade is that intermediaries in government departments tend to play a much greater role than in conventional trade. As well as additional paperwork and administrative delays there is also the problem of interference in commercial activities. For example, a trading organisation in a developing country may be accustomed to sourcing its imports of raw materials solely on the basis of quality and price competitiveness, but then finds that it is directed towards procuring the materials from one particular country, within the context of a countertrade deal, where it has very little opportunity to check quality standards and related matters to its full satisfaction. However, if the developing country in question has run out of foreign exchange and could not source the raw materials through conventional channels, the "something is better than nothing" argument may be put forward.

Some developing countries have made a determined effort to avoid these pitfalls in their bilateral agreements by sponsoring import missions to the partner country so that representatives of their own commercial sector can visit suppliers in order to view production facilities and discuss requirements. As a second best, importers must make do with receiving specifications and samples prior to placing orders. Inspection agencies might be used to check imports prior to shipment but this involves extra costs. It is also possible, if intermediary organisations - such as trading houses - are involved, that they will assist in these matters. Lastly, product specifications should be set out in the countertrade contract documents.