

Antidumping protection hurts good firms

Hylke VANDENBUSSCHE

Antidumping measures have become an important form of commercial protection for countries, regulated by WTO. The effect of this kind of protection on firm-level productivity is highly heterogeneous. If it allows initially low-productivity domestic firms to restructure and increase their performance, it tends to hurt high-productivity domestic firms and exporters.

While for the past twenty years the world has seen a drastic fall in tariff barriers, trade protection is still around – albeit in a different form. As shown in Figure 1, the fall in tariffs has coincided with a spectacular increase in the number of antidumping measures, which have become the most frequently used instrument of trade protection¹. While there has been a downward trend in the number of Antidumping measures since 2003, since the beginning of the global financial and economic crisis, Antidumping measures and investigations have increased rapidly and this seems to continue in 2009².

Under the WTO agreements which aim at promoting free trade, by reducing barriers to trade among its members, a number of exceptions are specified, such as the possibility to impose Antidumping measures in case of unfair trade. If a company exports a product at a price lower than the price it normally charges on its own home market, it is said to be “dumping” the product. Is this unfair competition? The WTO agreement does not pass judgement. Its focus is on how governments can or cannot react to dumping – it disciplines antidumping actions, and it is often called the “Antidumping Agreement”. However, current antidumping rules are not well equipped to distinguish between “fair” and “unfair” trade.

¹ e.g. Blonigen, Bruce and Prusa, Thomas J., “Antidumping”, *Handbook of International Economics*, edited by E. Kwan Choi and James Harrigan, (Malden, MA, Blackwell Publishing), 2003, p. 251-284.

² See the contribution by Chad Bown and by Willy Alfaro on this issue.

When foreign producers produce goods more cheaply, their prices are bound to be lower, especially when they export to a large market like the US or the EU where they are likely to face more competition than in their own domestic markets. What appears to be unfair trade may well be an indication of foreign comparative advantage. This would then imply that it is the less efficient firms that have an interest in filing for and receiving protection so to get sheltered from international competitive pressure.

This note shows that European firms that file and receive Antidumping protection, which only lasts for 5 years, are indeed the less efficient ones. However, they are able to restructure and improve their efficiency levels, yet they are not able to close the gap in terms of efficiency levels with those firms that never receive Antidumping Protection. Furthermore, this note points out that within the group of firms receiving protection, laggard firms benefit the most, while frontier firms (i.e. those with initially high efficiency levels) suffer from protection. This is explained by the nature of the supply chain and the export behaviour of the frontier firms versus laggards.

Antidumping protects inefficient domestic firms

Table 1 shows the average efficiency level, measured by total factor productivity³, of European firms that apply and receive Antidumping protection and compares it with a comparable control group of European firms that never apply for Antidumping protection⁴. The numbers refer to a sample of about 4000 European firms that are followed between 1993 and 2003 and all European antidumping cases for the years 1996, 1997 and 1998 are considered. It further compares two similar time frames, one referring to the period before protection and one referring to the period during which firms that applied and received Antidumping protection is in place (usually 5 years). It is clear that firms that never apply and hence never receive Antidumping protection have on average the highest efficiency score, measured by total factor productivity. In contrast, firms receiving Antidumping protection tend to have lower efficiency before protection (1.32 versus 2.23). So, this confirms the notion that it is the least efficient firms that typically are involved in Antidumping cases and suggests that use of Antidumping measures may have little to do with “unfair” practices by foreign firms.

³ We measure efficiency by total factor productivity and report an index of total factor productivity. This is a sophisticated way to measure productivity that relates a firm's input factors to its output.

⁴ A domestic firm is a firm that does not export.

Furthermore, table 1 indicates that both protected firms and unprotected ones experience a productivity increase during the antidumping protection period, but it seems that on average the increase in efficiency is higher for protected firms (17 % versus 4 %). However, this productivity increase is never sufficient to close the productivity gap with unprotected firms (1.55 versus 2.32). While on the one hand this result points to the fact that lowly efficient firms seem to start restructuring in order to be able to cope with international competition better once protection comes off, on the other hand these restructuring efforts may not be sufficient after all given that the productivity gap cannot be closed. In the absence of protection, some firms that received antidumping protection likely would have exited. The resources freed by their exit would be reallocated towards more efficient sectors in the economy, resulting in a larger productivity increase.

Antidumping : good for bad firms, but bad for good Firms

While the average firm's efficiency seems to be different between protected and unprotected firms, it may hide important differences *between* firms. A specific feature of antidumping protection is that it applies to *all* European firms producing the product that is being investigated, even though some firms producing it have not filed for protection. Furthermore, not all firms that receive protection have the same level of initial productivity as illustrated in Figure 2. The initial productivity distribution of protected firms is skewed to the left meaning that the majority of protected firms have a relatively low productivity level prior to the protection. But at the same time the productivity distribution of protected firms has also a thin right hand tail which implies that only a small number of firms have a high initial productivity. This begs the question whether antidumping protection affects all protected firms in a similar way or whether firms respond heterogeneously to trade protection?

Accounting for these initial conditions in a regression analysis framework reveals that there is substantial firm heterogeneity in firms' responses to antidumping protection. While antidumping protection appears to raise the productivity of the lowly efficient firms it reduces the productivity of the highly efficient ones. This result suggests that antidumping protection is “good for bad firms but bad for good firms!”

Several explanations can account for this. A first explanation is that the threat of exit is higher with the least efficient firms and therefore once they receive temporary protection they have a higher incentive to restructure before being exposed to international competition.

But this does not explain why the most efficient firms lose out when they face protection. A more likely explanation is related to the global nature of the firm, i.e. the extent to which firms are active in international trade. A stylized fact is that typically the most efficient firms are the ones that are also able to be active in international markets, due to the sunk costs (transaction costs) involved with international trade. In particular, antidumping protection may adversely affect those exporters that outsource part of their production to the countries targeted by the antidumping protection. Outsourcing entails a fixed cost which only more efficient firms can cover. Since exporters tend to be more efficient than non-exporters, exporters may engage more in outsourcing than non-exporters.

Imagine a French exporting firm that outsources bicycle assembly to China for the purpose of importing these bicycles into France, while performing activities such as branding, labelling and other types of distribution activities in France. French exporters that outsource their bicycle production face more expensive imports since they have to incur the antidumping duty imposed on bicycle imports from China. Current antidumping law does not automatically exempt outsourcers from paying an import duty, not even when the majority of the value added is created domestically. This puts outsourcers at a serious disadvantage over domestic bicycle producers which do not have to pay the import duty which may negatively affect their domestic demand and exports. As a result this may undermine the competitiveness of firms exporting domestic varieties that are refrained from setting a lower price in extra-EU export markets in order not to be accused of dumping practices by others. In addition, exporters may experience reduced market access abroad if domestic trade protection results in retaliatory action whereby trade partners protect themselves in turn⁵.

Table 2, based on a recent paper by Konings and Vandenbussche (2009), shows that exports of products that receive antidumping protection tend indeed to decline during protection, compared to a control group of products that do not receive protection. Also recent case evidence⁶ in the EU suggests that the international orientation of firms or the lack thereof is what divides firms within the same domestic import-competing industry over the desirability of antidumping policy. A recent EU antidumping case on leather shoe imports

⁵ Lindsey and Ikenson (2001) argue that patterns of AD flings are consistent with retaliatory use. Prusa & Skeath (2005) and Feinberg and Reynolds (2006) also confirm that new users of AD use it for retaliation. Retaliation is also singled out as a motive for AD law *adoption* by Vandenbussche and Zanardi (2008a).

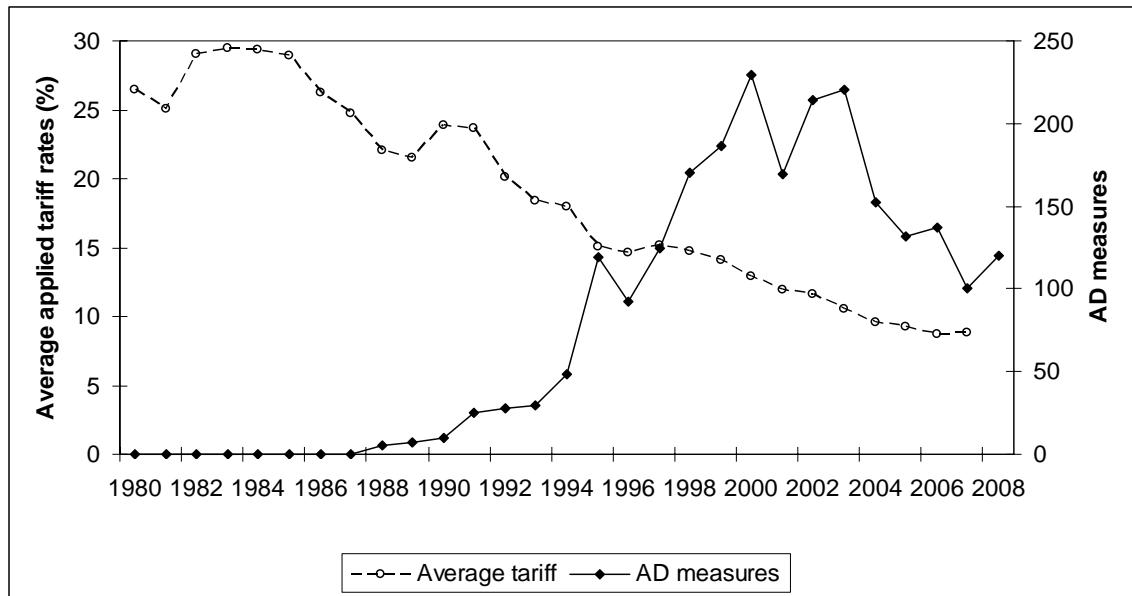
⁶ Swedish National Board of Trade (2007).

from China, divided the European shoe producers over the desirability of protection. “Globalized” EU shoe producers argued that they were harmed by the antidumping protection since they outsourced the assembly of their shoes to China which made them subject to an antidumping duty upon imports of the shoes in Europe despite the fact that well over 50% of the value added of the shoes was created inside the EU through activities such as research, design, logistics, development and marketing making the shoe a European shoe and not a Chinese one.

Conclusion

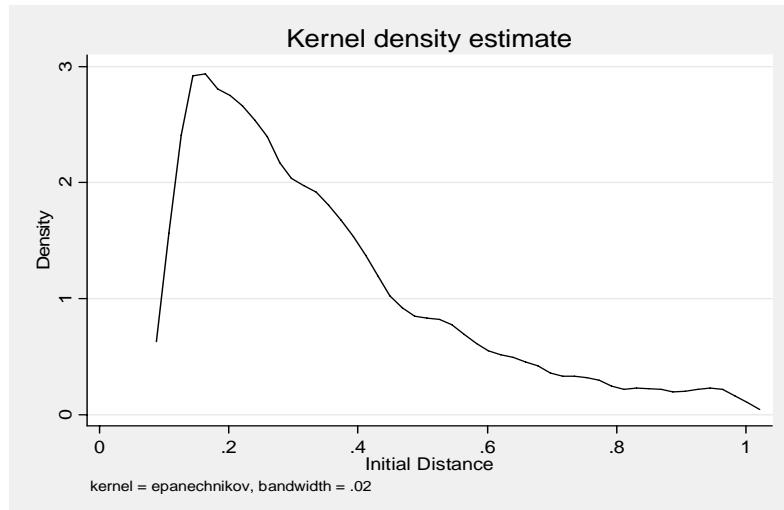
This note pointed out that typically the least efficient firms receive antidumping protection and that it helps them to restructure. However, they are not able to close the efficiency gap with firms that do not receive protection, which sheds a different light on the effectiveness of antidumping measures in protecting domestic firms. Furthermore, the effects of antidumping protection on domestic firms depend on firms’ initial conditions in terms of productivity and on their exporting status. Not taking the interests of exporters into account when deciding to protect a particular industry is bound to have detrimental long run effects which need to be considered before deciding to impose protection.

Figure 1: Evolution of Tariffs and Antidumping Measures



Source: The tariff data for 1980-2007 from UNCTAD TRAINS (WITS, 2009) which runs to 2007.
The AD data are from WTO data, and the Bown database

Figure 2: Frequency of Good firms and Bad firms



Source: Konings and Vandenbussche (2008), Journal of International Economics

Table 1: Comparing Average Total Factor Productivity Across Firms

	Productivity Before Antidumping Protection	Productivity After Antidumping protection	Percentage change in average productivity
Unprotected firms	2.23 (2.55)	2.32 (2.63)	4%
Protected firms	1.32 (1.05)	1.55 (8.65)	17%

Source: Konings and Vandenbussche (2008), Journal of International Economics; standard deviations in brackets.

Table 2: Evolution of Extra EU Exports during AD protection

	Extra-EU Exports			
	Volume		Prices	
Average AD-EFFECT	-0.369*** (0.1215)	-	0.003 (0.052)	-
AD-EFFECT after the 1 st year		-0.506*** (0.235)		0.021 (0.099)
AD-EFFECT after the 2 nd year		-0.344* (0.215)		-0.137* (0.092)
AD-EFFECT after the 3 rd year		-0.298* (0.220)		-0.034 (0.094)
AD-EFFECT after the 4 th year		-0.243 (0.211)		0.0006 (0.092)
AD-EFFECT after the 5th year		-0.177 (0.211)		-0.064 (0.081)
Year Dummies	Yes	Yes	Yes	Yes
Fixed Effects	Yes	Yes	Yes	Yes
# observations	724	724	724	724

Source: Konings and Vandenbussche (2009)

References

- Konings, J. and H. Vandenbussche (2008), "Heterogeneous Responses of Firms to Trade Protection", Journal of International Economics, 76, 371-383.
- Konings, J. and H. Vandenbussche (2009), "Antidumping hurts Exporters: firm-level evidence from France", LICOS working paper, Catholic University of Leuven.

Published in www.laviedesidees.fr, October 27, 2009.

© laviedesidees.fr