

# The Causes of Informal Trade: Importance of Trade Facilitation



---

APTFF Capacity Building Workshop:  
Designing and Implementing Trade Facilitation in Asia and the Pacific  
12 September, 2013  
Beijing, PRC

Shintaro Hamanaka  
Economist, Office of Regional Economic Integration (OREI),  
Asian Development Bank (ADB)



# Two Questions

---

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



# Mirror Comparison

---

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



# Informal Trade Revealed by Mirror Comparison

---

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



# Bilateral Mirror Comparison

---

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



# Aggregate IM-EX Ratio

---

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

# Ranking of Aggregate IM-EX (2010)



<b>Bhutan</b>	<b>3.16</b>	<b>Viet Nam</b>	<b>1.01</b>
<b>Armenia</b>	<b>1.73</b>	<b>Georgia</b>	<b>0.99</b>
<b>Nepal</b>	<b>1.55</b>	<b>Sri Lanka</b>	<b>0.99</b>
<b>Japan</b>	<b>1.40</b>	<b>Hong Kong</b>	<b>0.96</b>
<b>Singapore</b>	<b>1.35</b>	<b>Samoa</b>	<b>0.88</b>
<b>India</b>	<b>1.34</b>	<b>Philippines</b>	<b>0.84</b>
<b>Rep. of Korea</b>	<b>1.32</b>	<b>Kazakhstan</b>	<b>0.73</b>
<b>China</b>	<b>1.31</b>	<b>Kiribati</b>	<b>0.71</b>
<b>Pakistan</b>	<b>1.30</b>	<b>Azerbaijan</b>	<b>0.65</b>
<b>Thailand</b>	<b>1.30</b>	<b>Cambodia</b>	<b>0.52</b>
<b>Solomon Islands</b>	<b>1.29</b>	<b>Kyrgyz Republic</b>	<b>0.50</b>
<b>Fiji</b>	<b>1.29</b>	<b>Myanmar</b>	<b>0.46</b>
<b>Maldives</b>	<b>1.22</b>	<b>Afghanistan</b>	<b>0.45</b>
<b>Indonesia</b>	<b>1.03</b>	<b>Vanuatu</b>	<b>0.29</b>
<b>Malaysia</b>	<b>1.01</b>		



# Why Informal Import?

---

- Two plausible stories:
  - Officials are corrupted.
  - Procedures are inefficient (and traders give “speed money” to officials).
- But the two are not exclusive scenarios in reality....
- We test two hypotheses by calculating correlation using Global Enabling Trade Report





# Correlation between Informal Trade and GETR Indicators

	All Asian samples	All except Armenia
<b>Border administration</b>	<b>0.33</b>	<b>0.44</b>
<i>Efficiency of customs administration</i>	<b>0.20</b>	<b>0.27</b>
<b>Burden of customs</b>	<b>0.15</b>	<b>0.33</b>
<b>Customs services index</b>	<b>0.20</b>	<b>0.18</b>
<i>Efficiency of import-export procedures</i>	<b>0.40</b>	<b>0.50</b>
<b>Efficiency of the clearance procedures</b>	<b>0.31</b>	<b>0.47</b>
<i>Transparency of border administration</i>	<b>0.33</b>	<b>0.36</b>
<b>Irregular payments in exports and imports</b>	<b>0.24</b>	<b>0.35</b>
<b>Corruption perception index</b>	<b>0.31</b>	<b>0.41</b>



# Policy Implications

---

- In conducting reform, a large emphasis should be placed on efficiency.
- Enhancing efficiency is the best way to eliminate informal trade.
- The customs procedure is a part of trade procedure. The efficiency of non-customs procedure is critical to eliminate informal trade.