

## America's Hidden Tax on the Poor

### *The Case for Reforming U.S. Tariff Policy*

*by Edward Gresser*

Tariff policy has lain in comfortable darkness for many years. But this month, the Bush administration's 30 percent duty on imported steel returned it to the spotlight. There is good reason to hope the pool of light broadens beyond steel, because a look at today's U.S. tariff system reveals something surprising and uncomfortable: it has become steeply tilted against the poor.

Decades of trade negotiations have brought U.S. tariffs on average below 2 percent. This, however, masks the fact that on consumer goods tariffs remain high—often equaling and at times higher than the new tariffs on steel. This is above all true for two types of products—clothes and shoes—where tariffs are almost eight times the overall average. Making up only about 6.5 percent of imports, these products bring in nearly half of America's \$20 billion in annual tariff revenue.

Furthermore, tariffs within these categories are usually higher on cheap goods than luxuries. Women's underwear is an example: Tariffs on man-made fiber panties are over 16 percent, but on silk panties they are 2.4 percent and set to fall even lower. Similar disparities appear in baby clothes, sneakers, men's shirts, spoons, drinking glasses, and a vast range of other household goods. Thus, the poor—above all, single mothers who spend more of their income on clothing than other families—lose far more of their income to tariffs than wealthy or middle-class consumers.

Finally, clothes are the type of labor-intensive goods in which most industrial development begins. So Cambodia, Bangladesh, and other impoverished Asian countries, specializing almost wholly in these products, face effective tariff rates as much as 30 times above those applied to wealthy economies like Japan or the European Union. One need not adopt the theory popular in India—of a deliberate conspiracy against the poor—to consider this a remarkable inequity.

Americans seeking to reform such policies have at least three attractive options:

- ▶ a simple decision to treat tariffs as taxes;
- ▶ new market access programs for the least developed nations, ending the exclusion of shoes and clothes from existing U.S. duty-free programs; or, and ideally,
- ▶ a renewed focus on raising U.S. living standards as a principal trade policy goal, and thus use of the new WTO negotiating Round to eliminate tariffs on shoes, clothes and other household goods worldwide.

Any of these could bring higher living standards to the poor at home, and new opportunities for some of the world's poorest countries. The challenge is not one of analysis, but simply political will—because the facts are there for all to see, and they are rather devastating.

## **An Introduction to U.S. Tariff Policy**

Many people avoid tariff policy because they think it is boring and hard to understand. But this is at best half right: Tariffs are actually quite easy to understand.

The Harmonized Tariff Schedule—the basic government document setting out all U.S. tariffs—stretches out to 2116 pages.<sup>1</sup> But despite its length, it has a virtue unusual for Treasury Department documents: It is clearly written and readily comprehensible.

The schedule divides manufactured goods, foods, natural resources, and other merchandise into about 10,000 types, or “tariff lines.” Against each of these lines, the schedule places a specific tax charged against imports. For example, the first tariff line is 0101110010, for “purebred breeding horses, male.” The last tariff line (setting aside some special categories governing free trade agreements and special programs) is number 9706000060, for “antiques of an age exceeding one hundred years, other than silverware or furniture.” The lines for both breeding horses and antiques are marked “Free,” meaning the tax on each is zero. In between come everything from food and flowers to steel plate, airplanes, semiconductors, toothbrushes, and costume jewelry.

These taxes usually raise about \$20 billion in revenue a year. (Last year’s total, at \$18.6 billion, was somewhat lower than usual, reflecting the fact that overall merchandise imports fell because of the recession.) And a look at the revenues, and the products which bring in the money, reveals four basic points about the present U.S. tariff system:

- ▶ Overall, our tariffs are quite low.
- ▶ Our tariffs are higher on consumer goods than on industrial goods.

- ▶ Within the consumer goods category, our tariffs are low for luxuries and high on cheaper goods.
- ▶ The bulk of tariff revenue comes from two types of products: shoes and clothes.

### ***Overall, U.S. Tariffs Are Low...***

First, taken in aggregate, American tariffs are quite low.

When read directly from the tariff schedule and weighted by trade per category (i.e. so the 4.2 percent tariff on riding crops isn’t considered at par with the zero-tariff policy for civil aircraft), tariff rates average around 2.8 percent per dollar of imports.<sup>2</sup> The effective tariff level in the real world—the ratio of tariffs collected to the value of merchandise imports—is even lower, since Canada and Mexico provide about 40 percent of our total imports, and virtually all imports from these countries are duty-free as a result of the North American Free Trade Agreement.

To be precise, last year our \$18.6 billion in tariff revenues came from \$1.132 trillion in imports, making up an effective tariff of 1.6 percent. This is a lower figure than ever before, reflecting the fact that the United States has been negotiating tariff reductions with foreign countries since 1932. Over the past decade alone, effective tariffs have fallen by more than half, as the consequence of a remarkable set of trade achievements. To cite them in order:

- ▶ NAFTA eliminated tariffs on goods from Mexico and Canada.
- ▶ The Uruguay Round of the GATT, concluded in 1994, cut overall U.S. tariff levels by about a third.
- ▶ The Information Technology Agreement of late 1996 eliminated all U.S. tariffs on

computers, semiconductors and related goods.

- ▶ The Clinton administration gave 40 very poor countries special duty-free privileges on about 1770 types of goods in 1997.
- ▶ The Trade and Development Act of 2000 (including passage of the African Growth and Opportunity Act and expansion of the Caribbean Basin Initiative) eliminated many tariffs on goods from Africa, the Caribbean island nations and Central America.

als, and foods (like coffee or tea) not grown in the United States.

But for many consumer products, the situation is different. Here, tariffs often remain at levels most industrial products last saw in the 1970s. For knives, forks, and spoons, for example, tariffs average 7.1 percent. For foods competing with U.S. products—dairy, some juices, and so on—the rates can be very high as well. (Food tariffs are often hard to compare with tariffs on manufactured goods, as many are applied against the weight or volume rather than the price of imports.) And for clothes and shoes, tariffs are still higher—averaging over 11 percent and in some cases rising to 20 per-

**Table 1: Tariffs Then and Now**

	Total Imports	Tariffs Collected	Effective Tariff Level
1991	\$483.7 billion	\$16.2 billion	3.4%
2001	\$1,132.6 billion	\$18.6 billion	1.6%

Source: U.S. International Trade Commission (ITC) Dataweb, <http://www.usitc.gov>.

So in total, over 5,000 of the 10,000 U.S. tariff lines are now duty-free, and many others are duty-free for specific countries. The resulting drop in effective tariffs is evident in *Table 1*.

***...But On Consumer Goods Tariffs Are High***

Second, this general picture of a highly open market is a little misleading.

Tariffs are all but gone for two types of goods. The first is sophisticated, high-tech manufactured goods such as semiconductors, computers, and civil aircraft. The second includes natural resources like oil, met-

cent, 30 percent, or even above 40 percent.

This last category of goods deserves special attention, because shoes and clothes are now the main sources of U.S. tariff revenue.

Despite their visibility in department stores and daily life, shoes and clothes make up only a small fraction of U.S. imports. To be precise, they amount to 6.7 percent of the value of total merchandise imports. But they bring in nearly half of all tariff revenue. In fact, of last year's \$18.6 billion in tariff collection, a full \$8.7 billion came from shoes and clothes alone.<sup>3</sup> To look at the problem in a different way, for all merchandise but clothes and shoes, effective tariffs are 0.9 percent; at 11.4 percent, effective tariffs on

**Table 2: Clothes and Shoes vs. Everything Else**

	Total	Clothes & Shoes	Everything Else
<b>Total Goods Imports</b>	\$1,132.6 billion	\$76.3 billion	\$1056.4 billion
<b>% of Goods Imports</b>	100%	6.7%	93.3%
<b>Tariffs Collected</b>	\$18.6 billion	\$8.7 billion	\$9.9 billion
<b>% of Total Tariff Revenue</b>	100%	47%	53%
<b>Effective Tariff Level</b>	1.6%	11.4%	0.9%

Source: ITC Dataweb, <http://dataweb.usitc.gov>.

shoes and clothes are over twelve times higher.

Another approach is to compare total revenue from tariffs on shoes and clothes with revenue from tariffs on other goods. Here again, the disparity is quite striking—tariffs on shoes and clothes bring in nearly twice as much money as the next five largest sources of tariff revenue combined. (These are autos and auto parts at \$2.0 billion; electronics at \$1.0 billion; industrial machinery at \$0.8 billion; non-clothing leather goods and food, both at \$0.6 billion.)

### ***Tariffs are Low for Luxury Goods and High for Cheaper Goods***

Third, throughout the Harmonized Tariff Schedule (HTS), tariffs are lowest on industrial supplies and luxury goods marketed to wealthy and upper middle-class families, and highest on cheaper goods that poor families buy.

Women's underwear and pajamas provide a typical example. Here, heading 6208 of the Harmonized Tariff Schedule includes "women's or girls' singlets and other under-

shirts, slips, petticoats, briefs, panties, night-dresses, pajamas, negligees, bathrobes, dressing gowns and similar articles." Tariffs on these products are typically lowest on expensive designer products made from silk and highest for the cheapest goods that poor families need to stay within budgets. Panties made of silk have a 2.4 percent tariff and panties made from artificial fibers a 16.2 percent tariff [See *Table 3*].<sup>4</sup> So poorer women in department stores unknowingly pay much higher taxes than upper-class women in designer shops. This disparity will widen in the future: As the final American Uruguay tariff commitments come into effect, tariffs on silk panties will drop to a final level of 1.1 percent, and on panties from man-made fibers only to 16 percent.

Women's underwear is not an isolated or unrepresentative case. Men's shirts present an even sharper disparity. And tariffs on babies' clothes—on which the Treasury Department collected nearly \$200 million in tariffs last year—are still more troubling, as they fall directly on young mothers who have to buy new sets of jumpers, shirts, and trousers every few

**Table 3: To Avoid High Taxes on Underwear and Baby Clothes, Get Rich**

<i>Women's Underwear and Pajamas</i>			
	<b>Man-made Fiber</b>	<b>Cotton</b>	<b>Silk</b>
<b>HTS Number</b>	62089200	62089130	62089930
<b>Tariff Rate</b>	16.2%	11.3%	2.4%
<b>Revenue</b>	\$14.0 million	\$8.3 million	\$0.5 million
<i>Men's Knitted Shirts</i>			
	<b>Man-made Fiber</b>	<b>Cotton</b>	<b>Silk</b>
<b>HTS Number</b>	61052020	61051000	61059040
<b>Tariff Rate</b>	32.5%	20.0%	1.9%
<b>Revenue</b>	\$239.2 million	\$57.6 million	\$0.3 million
<i>Baby Trousers, Woven</i>			
	<b>Man-made Fiber</b>	<b>Cotton</b>	<b>Silk Blend</b>
<b>HTS Number</b>	62093020	62092030	62099090
<b>Tariff Rate</b>	29.0%	15.5%	2.8%
<b>Revenue</b>	\$2.8 million	\$15.8 million	\$0.2 million

Source: HTS numbers and tariff rates from the U.S. Harmonized Tariff Schedule. Revenue figures from ITC Dataweb. Both can be found at <http://dataweb.usitc.gov>.

months. Here, tariffs for artificial fiber goods run all the way up to 23 percent and 29 percent, with cotton somewhat lower, and silk or silk blend close to duty-free.

Tableware is another case in point, although the dollar values here are lower.

Last year, the United States imported something like two and a half billion forks, knives, and spoons. The overall 7.1 percent tariff average on these goods is nearly eight times as high as tariffs on most other goods. But even this average figure disguises something still more troubling: Tariffs are quite low for luxury tableware and escalate rapidly for the products poor people are most likely to buy.

Spoons made from precious metals have a tariff of 4.2 percent. By contrast, spoons

imported for 25 cents or less apiece face a 14 percent tariff. Silver-plated forks and knives face no tariffs at all. Table knives imported for 25 cents or less apiece have a 10.6 percent tariff, plus an additional charge of 0.9 cents apiece; and for forks imported at 25 cents or less, tariffs are 15.8 percent, again with an extra flat charge of 0.9 cents per fork.

For plates and cups, the pattern is the same. Tariffs on sets of table china valued below \$56 are 26 percent. Tariffs on very expensive porcelain sets of plates and cups—those worth more than \$200—are only 6 percent. Tariffs on drinking glasses, if they are worth more than \$5 each, are 3 percent; if they cost less than a dollar, the rate is 16 percent.<sup>5</sup> The disparity in rates

for drinking glasses, incidentally, seems to be a recent phenomenon—the original Hoover administration tariff on all such glasses was identical.

The case of shoes may be the most depressing and puzzling of all, since the United States now imports nearly 90 percent of the shoes marketed in our stores. American shoe companies make most of their goods overseas, while maintaining design, marketing, and other high-wage services employment at home. Despite this

### *Reliance on Tariffs from Clothes and Shoes is Growing*

Fourth, tariffs on clothes and shoes are growing both as a source of revenue and in comparison to tariff collection on other types of goods.

Ten years ago, while clothing and shoe tariffs were high, computers and toys also brought in a lot of revenue. Today, tariffs on these goods are mostly gone. Meanwhile, as *Table 4* shows, collection of tariffs from

**Table 4: Growing Reliance on Shoe and Clothing Tariffs**

Year	Total Tariffs Collected	Shoes and Clothes	Everything Else	Percentage of Tariffs From Shoes and Clothes
1991	\$16.2 billion	\$5.4 billion	\$9.8 billion	33%
2001	\$18.6 billion	\$8.7 billion	\$9.9 billion	47%

Source: ITC Dataweb, <http://dataweb.usitc.gov>.

fact, shoe tariffs nonetheless run up to 20 percent, 40 percent, and even higher. And as in the case of clothes, the cheapest shoes have the highest rates.

For example, cheap canvas sandals and sneakers selling at less than \$6.50 a pair are hard to find—because while such goods are easily produced in poor countries, tariffs on them are in the extraordinary range of 37.5 percent to 48 percent, and even 66 percent. Last year, the United States imported about \$50 million worth of such shoes (i.e. rubber-soled shoes with textile uppers), and imposed \$18 million in tariffs on them. Meanwhile, for sneakers imported at over \$12 dollars, the rate is 20 percent. To add insult to injury, tariffs on golf shoes range from 5 percent to 10 percent and most ski boots are duty-free.<sup>6</sup>

clothes and shoes has gone up fairly rapidly. So clothes and shoes now bring in nearly half of all tariff revenue.

### *Where Does Tariff Policy Come From?*

One may well wonder about the origin of such an approach to trade policy. Murasoli Maran, the Indian Trade Minister, has claimed that it (together with equally or more objectionable policies in the European Union, Japan, and other wealthy countries) is the result of a conspiracy. The rich countries, he says, “want the developing world to remain exporters of primary products only.”<sup>7</sup>

Actually, of course, he is wrong. There was never any deliberate plan. The present tariff system is simply the product of a long

and somewhat chaotic evolution of attitudes in Congress, the business community, and others interested in trade policy. In its essence it dates to the first decades of the 20th century, when American businesses were far more protection-minded than they are today. Makers of products like clothes and shoes, dominating the era's manufacturing economy, secured tariffs as high as 90 percent to protect themselves against rivals in Europe.

These industries are now quite small parts of the U.S. economy. Clothes and shoes in particular, the industries with the highest levels of protection apart from agriculture, now account for only about 3 percent of U.S. manufacturing production. But even as trade protection has proven unable to protect jobs—apparel employment has fallen by half since 1992<sup>8</sup>—their advocates over the decades have clung tenaciously to tariffs (and in the case of clothes, quota policies as well).

Meanwhile, newer industries—in particular high-tech manufacturers—were never as interested in trade protection. Most, and virtually all since the 1980s, saw their future in exports and thus supported international agreements to lower or abolish tariffs. And the result is the extraordinary set of disparities that make up the modern tariff system.

### *Other Countries Are No Better*

Finally, for the sake of fairness, it is important to note that other countries have equally troubling records.

European Union tariffs on clothes and shoes are at least simpler than those of the United States (most are 12.4 percent), but they are not especially lower.<sup>9</sup> More important, while the U.S. government has com-

mitted itself to deep reform of agricultural trade—an issue of equal importance to the poor, domestically and abroad—the EU is the main obstacle to it. Japan's difficulties with imports are, of course, legendary. And one suspects that some of the developing countries which complain most loudly about U.S. policy on these issues do so to disguise the fact that they are not treating their own neighbors especially well.

Most notably, despite Minister Maran's angry comments, India is not in a strong position to criticize others. It not only imposes exceptionally high tariffs but outright bans and exotic policies like "negative lists," "canalization requirements," (that is, lists of prohibited imports, and requirements for certain types of products to be sold through government agencies) and the like on many sorts of consumer goods.

As a result, India's neighbors regularly export less to India than they do to the United States. Most astonishingly, Nepal—though a land-locked nation surrounded on three sides by India and on the other by the Himalayas (and as noted below, facing exceptionally high effective U.S. tariffs)—is a case in point, exporting \$220 million worth of goods to the United States in 2000 and only \$177 million to India.<sup>10</sup> Sri Lanka and the Maldives provide additional examples.

### *Who Pays Tariffs?*

Nonetheless, the sins of others do not absolve us of our own. Our tariff system, to all appearances, could have been maliciously designed as a burden for the poor. And its consequences are at their worst for two sorts of people who least deserve them: single mothers in America, and workers in Cambodia, Bangladesh, and other very poor Asian countries.

### Who Pays Tariffs At Home? Single Mothers

The most obvious, though most often ignored, aspect of tariff policy is that tariffs are a form of taxation. But the effects of tariffs, in contrast to those of most taxes, fall most heavily on the poor. And they are perhaps heavier on young single mothers than on anybody else.

Any tax that focuses, as tariffs do, on the necessities of life will hit poor families harder than rich families. But even within poor communities, taxes that single out clothes and shoes have especially painful effects. Statistics provided by the Bureau of Labor Statistics (BLS), in the annual Consumer Expenditure Survey, show why this is so.

According to the BLS survey, average single-parent families (about five in six American single-parent families are headed by women<sup>11</sup>) earn less than half the income of married couples. To be specific, average income for a single-parent household with children is \$25,685, and average income for a married couple with kids is \$63,666.<sup>12</sup>

But despite the disparity in income, clothing expenses for the two families are not very different. While a single-parent family with children spends an average of

\$1,946 per year on clothes, the two-parent family spends \$2,520. In practical terms, this means that clothes and shoes take up about one-thirteenth of a single-mother’s income, and about 4 percent of a two-parent family’s income.

This fact is all the more troubling when one considers disposable income rather than total pre-tax income. If we subtract basic expenses—on food, shelter, health care, pensions, transport (leaving out auto purchases) and federal taxes—from total pre-tax income, the cost of tariffs to single-parent families appears remarkably high.

As *Table 6* shows, these expenses leave a two-parent family with children earning \$63,666 per year with about \$20,850 to buy quality-of-life products like books, entertainment, education, personal care, and similar categories. Then, under the conservative assumption that tariffs raise the price of clothes and shoes by 3 percent (noting that annual tariff collection from these products is about 3 percent of the total retail sales value of U.S. shoe and clothing sales<sup>13</sup>), tariffs would take \$75 a year—not a trivial sum, but a relatively small fraction of the two-parent family’s disposable income.

The single mother faces more difficult circumstances. She uses about \$18,000—over two-thirds of her income—to buy food,

**Table 5: Clothes and Shoes as a Percent of Income**

	Single-Parent With Children	Two-Parent With Children
<b>Total Pre-Tax Income</b>	\$25,685	\$63,666
<b>Spending on Clothes and Shoes</b>	\$1,946	\$2,520
<b>% Pre-Tax Income Spent On Clothes and Shoes</b>	7.6%	3.9%

Source: Bureau of Labor Statistics, <http://stats.bls.gov/cex/csxann99.pdf>.

pay rent, take the bus to work and pay for visits to the doctor. An additional \$2,000 goes to clothes and shoes, leaving only about \$4,000 for other types of purchases. The estimated \$60 she spends on shoe and clothing tariffs is slightly less than a sixtieth of this figure—the equivalent of nearly a week’s worth of her spending money for the year, and almost as much as she can afford to spend on books and other reading material.

This calculation, however, probably sharply understates the true cost of shoe and

clothing tariffs for single-mother families, for three reasons.

First, for both types of families, the calculation (assuming that 3 percent of the retail price of clothes and shoes comes from tariffs) ignores the likelihood that tariffs allow domestic manufacturers to inflate prices. This is quite implausible. On the contrary, an 11.4 percent average tariff probably enables domestic manufacturers to raise their own wholesale prices by about 11.3 percent without losing business. This would double the real cost of tariffs for all

**Table 6: Clothes and Shoes in Family Budgets**

	Single-Parent With Children	Two-Parent With Children
<i>Total Pre-Tax Income</i>	\$25,700	\$63,700
<i>Estimated Federal Taxes</i>	\$0	\$3,600
<i>Disposable Income</i>	\$25,700	\$60,100
<i>Basic Expenses</i>	\$18,000	\$32,450
Food	\$4,500	\$5,400
Housing	\$10,100	\$16,350
Transport	\$2,400	\$3,400
Health Care	\$1,000	\$2,500
<i>Insurance and Pensions</i>	\$1,800	\$4,800
<i>Clothes</i>	\$1,950	\$2,520
Tariffs	\$60	\$75
<i>Remaining Income</i>	\$3,950	\$20,850
Reading	\$70	\$200
Education	\$420	\$830
Entertainment	\$1,400	\$2,500
Personal Care Products	\$360	\$500

Source: Bureau of Labor Statistics, <http://stats.bls.gov/cex/csxann99.pdf>.

families, consuming not one but two weeks' worth of a single mother's disposable income.

Second, the calculation assumes that the two families buy an identical mix of clothes. In fact, poorer families will almost certainly buy more cheap polyester baby clothes and similar apparel, which have higher tariffs than more expensive cotton or linen products.

Third, retail stores selling cheaper clothes and shoes are less able to mark up prices than elite stores that carry more expensive goods. An informal survey of baby clothes in Washington-area Nordstrom's, Baby Gap, and Wal-Mart found the price of pajamas at the more expensive stores to be about four to five times higher than at Wal-Mart, and pants and dresses often six times higher than at Wal-Mart.<sup>14</sup> Tariffs will be a much larger part of the retail price of the Wal-Mart goods than the others.

Thus, the fraction of a poor family's clothing budget lost to tariffs, as opposed to purchasing actual clothes and shoes for children, is probably much higher in comparison to other families than overall averages suggest. And even this leaves questions for activists and budding practical trade economists to consider. Two in particular seem especially important:

### **What are the differences in retail mark-ups between cheap and expensive clothes and shoes?**

Anecdotal evidence suggests that markups are lowest—and thus tariffs as a fraction of the final retail price highest—for the very cheapest clothes and shoes. Combining this with the higher tariff rates on cheap goods, the real cost of tariffs for an average single-parent family may rise into the hundreds of dollars.

### **What fraction of the very poorest families' incomes, notably women leaving welfare**

### **for entry-level jobs, goes to clothes and shoes?**

A recent Urban Institute Study found that women just leaving welfare to join the workforce earn an average of \$7.15 per hour.<sup>15</sup> This wage, for full-time employees, would mean an average annual salary of about \$14,872. For such a family, the total budget for clothes would probably be somewhat smaller than that of an average single-mother family. But just as the average single-parent family spends nearly as much on clothes as a two-parent family, so will a successful welfare leaver have to spend almost as much on clothes and shoes as an average single-parent family. It is quite likely, though yet unproven, that tariffs pose the greatest challenge of all to the living standards of the poorest families.

### ***Who Pays Tariffs Overseas? Cambodians***

The domestic effects of tariffs make for an ugly story and the facts overseas are no prettier. Just as tariffs hit the poor in America harder than the wealthy or middle class, so they hit very poor countries much harder than rich high-tech economies and oil producers.

Cambodia is a perfect example. Most Cambodian factories selling goods to the United States opened in the last five years, as domestic politics began to stabilize in the aftermath of genocide and war, and the country re-established economic ties to the outside world. These factories now employ about 200,000 workers, nearly two-thirds of Cambodia's industrial workforce, making goods like T-shirts and baseball caps. Americans bought \$942 million worth of these goods last year; the buyers paid \$150 million in tariffs. Thus, Cambodians, with a per capita income of \$260, face one of the highest effective tariff rates in the world, at 15.8 percent.<sup>16</sup>

**Table 7: Mongolians and Cambodians Pay More**

Country	Per capita GDP	Exports to US	Tariffs Paid	As %
Mongolia	\$390	\$0.143 billion	\$23 million	16.1%
Norway	\$33,470	\$5.173 billion	\$24 million	0.5%
Bangladesh	\$370	\$2.353 billion	\$331 million	14.1%
France	\$24,170	\$30.023 billion	\$330 million	1.1%
Cambodia	\$260	\$0.964 billion	\$152 million	15.8%
Singapore	\$30,170	\$14.899 billion	\$96 million	0.6%
Pakistan	\$460	\$2.228 billion	\$240 million	10.8%
Saudi Arabia	\$6,900	\$12.359 billion	\$65 million	0.5%

Source: Per capita income statistics from World Bank World Development Indicators 2001. Trade and tariff revenue from ITC Dataweb, <http://dataweb.usitc.gov>.

Their neighbors in Singapore, a few hundred miles away, face a completely different system. Operating in a highly advanced industrial economy, Singapore businesses sold the United States about \$15 billion worth of semiconductors, surgical equipment, and similar high-end goods. For this they were charged \$96 million in tariffs—an effective rate of 0.6 percent, about one-thirtieth of the level for Cambodians.

This is one example of a pervasive disparity. Setting aside the four countries with which we have Free Trade Agreements (Canada, Mexico, Israel, and Jordan), two types of countries face very low tariffs. One is the high-tech industrial economies like Japan or the EU, where effective tariffs typically average below 2 percent. The other includes countries like Saudi Arabia, whose exports are concentrated in oil and natural resources; here, effective tariff rates are often below 1 percent. By contrast, countries just beginning to move from subsistence

agriculture and resource dependency into light manufacturing—like Cambodia—face the highest effective tariffs.

Thus, on average, the world's least-developed countries pay tariffs four or five times higher than the richest economies. And as with Cambodia, these disparities can sometimes be much larger. To cite another salient example, Mongolians and Norwegians both paid us about \$23 million in tariffs last year. But Mongolia exported \$143 million worth of goods to us, and Norway \$5.2 billion, or 40 times as much. In effect, Mongolians—and about eight American manufacturing companies willing to invest in this new democracy<sup>17</sup>—paid 16 cents to sell us a dollar's worth of sweaters and suits, while Norwegians paid half a cent for every dollar's worth of gourmet smoked salmon, jet engine parts, and North Sea crude. Bangladesh likewise pays more tariffs than France for one-fifteenth of the exports; Pakistanis pay four times more than

Table 8: Except for Africa, the Poorest Countries Pay Most

Country	Per capita GDP	Exports to US	Tariffs Paid	Tariffs as % of Exports to U.S.
<i>World Total</i>	\$5,020	\$1,132.6 billion	\$18.618 billion	1.6%
<i>Least Developed*</i>	\$420	\$8.2 billion	\$0.641 billion	7.3%
<b>Least Developed Without Energy</b>		\$5.3 billion	\$0.639 billion	12.0%
<i>China</i>	\$780	\$102.1 billion	\$3.870 billion	3.7%
<i>ASEAN</i>		\$75.9 billion	\$2.212 billion	2.9%
<i>CBI</i>		\$20.7 billion	\$0.578 billion	2.8%
<i>Japan</i>	\$32,030	\$126.9 billion	\$2.115 billion	1.7%
<i>EU</i>	\$22,250	\$218.9 billion	\$3.359 billion	1.5%
<i>OPEC</i>		\$55.7 billion	\$0.834 billion	1.5%
<i>Africa</i>	\$490	\$21.1 billion	\$0.132 billion	0.6%
<b>Africa Without Energy</b>		\$8.7 billion	\$0.127 billion	1.5%

Source: Per capita income statistics from World Bank World Development Indicators 2001. Trade and tariff revenue from ITC Dataweb, <http://dataweb.usitc.gov>.

\* "Least Developed Countries" are the 48 countries listed by the United Nations as least developed. Eight of these countries (Afghanistan, Burma, Congo, Eritrea, Laos, Liberia, Maldives and Sudan) do not receive the special GSP privilege in the United States. The list of additional products given duty-free treatment is available at <http://www.ustr.gov/gsp/treatment.pdf>—note that it does not include any tariff lines in chapters 61, 62 or 64, or chapter 42 subheading 4213, which are the lines for clothes and shoes.

Saudis for one-sixth of the value of Saudi exports.

Two further points are worth noting:

First, on the more positive side, the deplorable experience of the poorer Asian countries is not universal. This is in part due to policy reforms made very recently in the United States. Most particularly, the duty- and quota-free programs for Africa, Central America, and the Caribbean islands, created two years ago in the Trade and Development Act, seem to have been reasonably effective in keeping effective tariff rates for these parts of the world relatively low.

Most of Africa's exports are oil from Nigeria, Gabon, and Angola. But with the

support of the African Growth and Opportunity Act, the continent's sales of clothes and some other light manufacturers have grown rapidly, tripling since 1996. Nonetheless, even if energy is subtracted from Africa's export totals, effective tariffs on African goods have fallen. Since 1996, they have dropped from 2.1 percent to 1.6 percent—a level comparable to the rates imposed on Europe or Japan. Future developments could change the trends slightly, as manufactured goods are still a relatively small proportion of Africa's exports, and the Africa program does cap some apparel benefits. But for the moment, the Africa bill seems to have had good effect.

Beneficiaries of the Caribbean Basin Initiative, though with somewhat less generous apparel benefits, likewise pay tariffs only slightly above world averages. Most analyses of CBI focus on Central America and the Dominican Republic, as these countries are the largest trading nations eligible for CBI benefits. But CBI also seems to have helped keep tariffs lower for its approximately 20 small island nation beneficiaries. A case that merits attention is that of Haiti, where effective tariffs have fallen sharply

(from levels averaging 4 percent between 1996 and 2000, to 2.4 percent last year) since the Trade and Development Act.

Second, and less happily, more general efforts to reduce tariff burdens on the poorest countries appear to have failed. As noted in *Table 8*, if energy is subtracted, the rates they now face are about eight times higher than the world average. And as *Table 9* shows, effective tariff rates for these countries have nearly doubled since 1991.

Most notably, in 1997 the Clinton

**Table 9: The Top 12 Effective Tariff Rates**

	1991	2001
<b>WORLD</b>	3.4%	1.6%
<b>Least Developed Countries</b>	4.2%	7.3%
<i>12 Countries Facing Highest Effective Rates*</i>		
<b>Macao</b>	13.6%	16.6%
<b>Palau</b>	5.1%	16.4%
<b>Cape Verde</b>	0.0%	16.4%
<b>Mongolia</b>	14.4%	16.2%
<b>Cambodia</b>	—	15.8%
<b>Burma</b>	9.1%	15.7%
<b>Maldiv Islands</b>	18.5%	14.8%
<b>Bangladesh</b>	15.6%	14.1%
<b>Sri Lanka</b>	16.3%	14.1%
<b>Micronesia</b>	17.6%	12.9%
<b>Mauritius</b>	15.3%	12.8%
<b>Nepal</b>	16.2%	12.3%

Source: ITC Dataweb, <http://dataweb.usitc.gov>.

\* Includes only countries with which the United States has normal trade relations. Two countries lacking NTR but not subject to trade embargoes (Laos and Yugoslavia) have much higher effective tariff rates than any other nations, at 45.3 percent and 27.7 percent respectively. Others encountering high effective tariffs include Swaziland and Turkmenistan at over 11 percent; Pakistan, Brunei, and Macedonia at 10.8 percent, 10.5 percent and 10.1 percent respectively; Egypt at 8.9 percent, and Fiji and Hong Kong at 8.7 percent.

administration removed tariffs from about 1,770 types of goods for 40 of the world's poorest countries by enlarging the "Generalized System of Preferences." This system, commonly known as GSP, dates to 1974 and grants most developing countries duty-free privileges for about 5,000 types of goods. The least-developed country program brought this above 7,000 for the poorest countries.

Based on import growth alone, the results five years later appear remarkably good. Duty-free imports from least-developed countries under GSP have risen by \$2.85 billion—from a tiny \$49 million to a total of \$2.9 billion in 2001—since 1996. On closer examination, however, the success melts away. A full \$2.7 billion of this growth, or virtually all, comes from a single one of these 1770 tariff lines: line 27090020, a grade of petroleum otherwise subject to a 10-cent per barrel duty. Another \$70 million in growth comes from a second type of oil. Otherwise the initiative has had little effect.

The problem of course is that the extra goods added to the GSP program did not include clothes and shoes, which are the industries in which the least-developed countries with less-skilled workforces are most able to succeed. The rise in effective tariff rates for the least developed countries simply reflects the fact that during the 1990s, countries like Mongolia or Palau began to attract apparel investment and to export these types of goods. As a consequence, they and other very poor countries in Asia and the Pacific island nations now often face tariffs 10 times higher than the world average.

### ***The Remedy***

A review of the present American tariff policy yields an obvious conclusion: it is something of a disgrace. Ineffective in their

stated purpose of protecting jobs at home, tariffs nonetheless impose heavy burdens on America's poorest families and the world's poorest countries.

Such a policy cries out for reform. And understanding that few policies have stronger bureaucratic and private-sector lobbies than tariffs on clothes in particular (the case of tariffs on shoes, where domestic production is minimal, is a mystery), reformers have at least three attractive options.

#### ***Option 1: Treat Tariffs as Taxes***

The simplest option would be to stop regarding tariffs as trade policy, and instead consider them as taxes. If policymakers were willing to adopt this approach, the solution to the tariff problem would, at least in concept, be easy.

As tax policy, our current tariff schedule is sharply at odds with the tax principles of both major political parties. Democrats dislike taxes that disproportionately hurt the poor, as tariffs on clothes, shoes, tableware, and similar goods do; Republicans are often enthusiastic for tax cuts even if they benefit the poor. So the administration, if it were willing, could use the next tax or budget bill to call for eliminating tariffs on shoes and clothes. Congressional reformers could do the same.

This, of course, appears unlikely. Tariff policy has been an exclusive preserve of trade negotiators since the 1930s. It arose in none of the major tax debates of the past 20 years—neither the first Reagan budget in 1981, the Dole tax bill of 1982, tax reform in 1986, the Bush budget of 1990, nor the tax debates of 1993 and 2001. The tax-cutting enthusiasm of the present administration and House leaders has largely been reserved for different issues such as marginal rates

and Alternative Minimum Tax refunds. Neither, it must be said, have Democrats shown much more enthusiasm for tariff reform. So although this is probably the simplest option, it seems unlikely to materialize.

### ***Option 2: Special Relief for Poor Countries***

A second option would be to grant special market-access privileges to some of the small and poor countries most deeply affected by the present system—that is, Cambodia, Mongolia, Palau, Nepal, and so on.

One possibility would be a new program, comparable to the Caribbean Basin Initiative or African Growth and Opportunity Act. As noted earlier, these two laws allow Central American countries, Caribbean island nations, and African countries to sell the U.S. clothes without tariffs and quotas, up to a total of several billion dollars' worth of trade, and eliminate tariffs on shoes and other consumer goods. Another such program could help poorer countries in Asia and the Pacific attract investment, create jobs and keep both when the clothing quota program ends in 2005.

But this solution has two significant drawbacks. First, it would further complicate an already tangled U.S. trade regime. Second, it would do nothing for poor families at home.

U.S. trade policy is already getting cluttered by sometimes conflicting rules of origin. ("Rules of origin" are the method by which we decide the origin of a shirt that, given the integration of world apparel production, may be designed in Hong Kong, made from Egyptian cotton, and cut in Cambodia). The 5,000 or so kinds of products subject to tariffs now may enter the country under the normal tariff rates; or under the three special trade programs for Africa, the Caribbean Basin and the

Andes; NAFTA; the Generalized System of Preferences; and two bilateral free trade agreements with Israel and Jordan.

While such rules are supposed to be standardized under the WTO, the rapid expansion of smaller agreements with different benefits is already creating a rather complicated system for businesses to manage—especially for products subject to high tariffs or non-tariff barriers. If they continue to proliferate, their value may begin to diminish. And for national security reasons, the Middle East should be the next candidate for a special program. For the sake of efficiency and simplicity, therefore, if a solution is designed for the poorest countries, the best option might be to include shoes and clothes in the existing Generalized System of Preferences program.

The second point is still more important. A limited duty-free program might well help the poorest countries overseas. But it would provide little or no relief to single mothers and the poor at home. As long as tariffs stay in effect for large exporters of consumer goods—more developed economies like Hong Kong, Indonesia, the Philippines, Thailand, China, India, and Italy—prices for poor families will remain artificially high.

### ***Option 3: Tariff Elimination Through Doha Round***

Ultimately, if tariffs remain the exclusive preserve of trade negotiators, the solution most likely to succeed is one of negotiations. Furthermore, while bad policies in foreign countries are no excuse for our own bad policies, it is also worth remembering that others have tariff policies as egregious and ripe for reform as our own. Trade negotiations can contribute to this.

So the third, and probably best, approach is to make raising domestic living standards a trade priority comparable to the creation of new export opportunities. Elimination of

tariffs in the United States and elsewhere is a logical way to accomplish this goal. Here, the new WTO Round launched last year (and set for conclusion by 2005) is the best way to solve the tariff problem. The United States should commit itself to total tariff elimination in clothes, shoes, tableware and perhaps consumer products generally, either in exchange for reciprocal reductions in the same sectors, or market-opening in other areas where American producers have strong export opportunities, notably agriculture.

### **Conclusion**

None of this discussion should be taken as an indictment of the overall thrust of American trade policy. As a whole, trade policy has achieved a great deal. The Uruguay Round, China's WTO

accession, the Trade and Development Act, NAFTA, and other agreements have made a contribution to our domestic economic health and competitiveness, world economic growth, and also, the cause of peace.

But while cognizant of all these accomplishments, policymakers should also be aware of and willing to fix the flaws that remain in American trade policy. And few areas appear more ripe for reform than tariffs.

Is it right to impose higher taxes on single mothers than on anybody else?

Is it fair to confront some of the world's poorest nations with trade barriers 20 or 30 times higher than those the richest countries face?

The answers to these questions appear to be obvious. As obvious, in light of the facts, as the case for tariff reform.

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### **Endnotes**

<sup>1</sup>The Harmonized Tariff Schedule, <http://dataweb.usitc.gov/scripts/tariff/toc.html>.

<sup>2</sup> See World Bank, "World Development Indicators 2001," Table 6.6, pg. 338.

<sup>3</sup> Including all goods under HST Chapter 62, "Articles of Apparel and Clothing Accessories, Not Knitted or Crocheted"; Chapter 63, "Articles of Apparel and Clothing Accessories, Knitted or Crocheted"; Chapter 64, "Footwear, Gaiters and the Like"; and Chapter 42, subheading 4203, "Articles of Apparel and Clothing Accessories, of Leather or Composition Leather."

<sup>4</sup> U.S. Harmonized Tariff Schedule, Section XI, Chapter 62, subheading 6208, <http://dataweb.usitc.gov/scripts/tariff/0201c62.pdf>.

<sup>5</sup> See Harmonized Tariff Schedule, Section 13, Chapter 69, subheading 6911 for plates; and Chapter 70, subheading 7013 for drinking glasses.

<sup>6</sup> See Harmonized Tariff Schedule, Section XI, Chapter 64, subheading 6404 for sneakers and 6402 for golf

shoes and ski boots, <http://dataweb.usitc.gov/scripts/tariff/0201c62.pdf>.

<sup>7</sup> Quoted in *The Hindu*, Financial Daily, October 21st 2001.

<sup>8</sup> Bureau of Labor Statistics, Table B-1 SA, on seasonally adjusted employment by industry, <ftp://ftp.bls.gov/pub/suppl/empsit.b1sa.dat>.

<sup>9</sup> See EU tariff schedule, chapters 62 and 63, <http://dataweb.usitc.gov/scripts/worldtariffs.htm>.

<sup>10</sup> See IMF *Direction of Trade Statistics 2001*, page 340 for Nepal, page 315 for the Maldives, and page 432 for Sri Lanka.

<sup>11</sup> Bureau of the Census, "America's Families and Living Arrangements 2000," June 2001, pg. 8, <http://www.census.gov/prod/2001pubs/p20-537.pdf>.

<sup>12</sup> Bureau of Labor Statistics, *Report on Consumer Expenditures 1999*, page 9, <http://stats.bls.gov/cex/csxann99.pdf>.

<sup>13</sup> Based on figures for the year 2000 (most recent available as of this writing), when U.S. sales of shoes and clothes totalled \$319.1 billion and tariff revenue on these products was \$9.2 billion. Figures on total shoe and clothing purchases from Bureau of Economic Analysis, *Survey of Current Business*, August 2001, page 47; available at <http://www.bea.doc.gov/bea/ARTICLES/2001/08august/0801NipaTbl&Toc.pdf>.

<sup>14</sup> At Wal-Mart, for example, the price of cotton baby shirts ranged from \$3 to \$10; at Nordstrom's and Baby Gap the range was \$19-\$30. Prices for synthetic fabric were comparable. Sources for these clothes included Sri Lanka, Hong Kong, Thailand, Russia, United States, and others.

<sup>15</sup> Pamela LoPrest, "How are Families that Left Welfare Doing: A Comparison of Early and Recent Welfare Leavers," Urban Institute, April 2001, [http://newfederalism.urban.org/html/series\\_b/b36/b36.html](http://newfederalism.urban.org/html/series_b/b36/b36.html).

<sup>16</sup> In shoes, Cambodia literally does face the highest effective tariffs in the world, although totals are quite low. Cambodia sold the United States \$4,000 worth of shoes last year, and faced 30.2 percent effective tariffs on its goods. Figures from Footwear Distributor and Retailer Association. The type of shoe in question has both soles and uppers of rubber or plastic, valued at \$6.50 to \$12 per pair. These have a 20 percent tariff plus an additional tariff of 90 cents per pair.

<sup>17</sup> See report on U.S. investment in Mongolia from U.S.-Mongolia Business Council, <http://us-mongolia.com/ambiz/index.html>.