

# **PARAGUAY: Industrial Export Patterns to the United States and the European Union**

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## **Introduction**

Paraguay, as a very open economy is showing an interesting export potential to the developed world, especially in terms on non traditional and manufactured products. The purpose of this study is to reveal and estimate the degree of asymmetries in exporting manufactured and semi-manufactured products from Paraguay toward different markets, namely the United States of America (USA) and the European Union (EU). This exercise will attempt to explain, in part, the potential of manufacturing export growth in Paraguay to different markets in the world as well as to explain why the US market is more receptive of this type of products from Paraguay than the EU market.

Two different approaches will be used to assess the subject. The first one regards manufacturing export competitiveness as related to the different sizes of the importing markets (Markwald y Machado, 1998)<sup>3</sup>. The second one measures competitiveness as the capacity of an export product to get in and remain in a foreign market, competing with local manufacturing and from the rest of the world (Market Share)<sup>4</sup>. In the first case, the export pattern of Paraguay to the USA and EU markets is classified for comparison in selected products for the 1990-2006 period. In the second case products are classified in terms of competitiveness differential in both markets for 2002 and 2005.

Likewise, two different tools will be used for the purpose of discovering the causes of a competitiveness gap of selected Paraguayan products exported to the US and EU markets. First, these products will be compared in terms of tariff facilities offered by both markets. In other words what will be examined is the level of protection of preferential entries that these products have for each market. Secondly, interviews are conducted with leading export companies to both markets in order to see if factors different than tariff are also important to consider in explaining this gap.

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<sup>3</sup> These authors have found that a significant difference in Brazil export patterns toward the USA and the EU owed to the different sizes of the importing markets.

<sup>4</sup> It measures the relative participation of an export product within total imports of a destination market.

## Exports: trends and patterns

GDP growth in Paraguay has been of merely 2.2% on average in the 2000-2006 period. Agriculture participation in Paraguay's GDP is relatively high (27%) and about two thirds of its exports has consisted of basic agricultural products and manufacturing based on natural resources, during the 1990-2006 period. Paraguay's exports are highly exposed to international price volatility and climate changes given its concentration in commodities.

At the same time, Paraguay is the most open economy in the MERCOSUR region, with increasing rates during the 90s, reaching 80% by 2006 with an average import tariff of 5%. MERCOSUR is the principal market destination of Paraguay's exports (Table 1). Paraguay has increasingly concentrated its exports into the region ever since 1991, provided zero tariff and less transportation cost than in other regions of the world. However, relative participation of MERCOSUR in Paraguay's total exports has been steadily decreasing since 2000, reaching only 34% of total exports by 2006. Two factors explain this diminishing trend of exports toward the region. The first one is related to important currency devaluation in Brazil (1999) and in Argentina (2002). The second one has to do with the demand surge for commodities from the Rest of the World (especially from Asian countries). By 2005/06, exports from Paraguay to the Rest of the World represented 3.6 times more than in the early 1990s, representing the most dynamic factor of exports growth in Paraguay over the last years.

New export markets have emerged for Paraguay traditional exports over the last 6 years: Russia (frozen meat), Chile (meat and soybean), Switzerland (soy bean), Peru (soybean pellet and oil), and Bolivia (soybean). The participation of these five countries in the total exports have explained almost 80% of all exports to the Rest of the World and 93% of Paraguay's export growth in 2000-2006.

**Table 1**  
**Paraguay: Exports to Principal Market Destinations**

Years	Average ( in million of US\$)					Export Shares (%)				
	Mercosur	EU	USA	ROW	Total	Mercosur	EU	USA	ROW	Total
1990/91	317	285	38	208	848	37	34	4	25	100
1995/96	527	268	43	142	981	54	27	4	15	100
2000/01	416	179	31	304	931	45	19	3	33	100
2005/06	608	354	65	770	1.797	34	20	4	43	100

**Source:** elaborated with data of the Central Bank of Paraguay (BCP).

ROW: Rest of the World

Exports to the European Union (EU) market in 2005/6 represented only 24% more than in the 90s, in terms of absolute values. However, the share of the EU in total exports of

Paraguay has significantly diminished from 34% in 1990/1 to only 20% in 2005/6. Paraguay's exports to the United States (USA) have been consistently lower than exports to the EU. In fact, the share of exports to the USA market has never been historically higher than 4%.

Although more than two thirds of Paraguay's exports have consisted in agricultural commodities, a diminishing trend of this share is observed over the last five years (Table 2) Manufactured and semi-manufactured products represented about 18% of total exports at the beginning of the 90s, increasing this participation to 27% of the total by the end of the period. Participation of manufactured products alone has doubled during the same period, and has proved to be more dynamic than semi-manufactured products. Once a free trade zone has been installed in the region, manufacturing exports to Mercosur increased significantly, reaching 20% of all exports of the country. However, this share has been diminishing since 2000, in part due to currency devaluation of Paraguay's two major partners in the region.

**Table 2**

**Paraguay: Export Patterns**

Years	Average ( in million of US\$)				Export Share (%)			
	Basic Products	Semi-Manufactured	Manufactured	Total	Basic Products	Semi Manufactured	Manufactured	Total
1990/1	696	85	66	847	82	10	8	100
1995/6	650	142	187	979	66	15	19	100
2000/1	634	121	175	930	69	14	16	100
2005/6	1308	230	259	1797	73	13	14	100

**Source:** Elaborated with data of the Central Bank of Paraguay (BCP)

In 1990-2006, MERCOSUR has definitively become the main export market for Paraguay in terms of three group of products: basic products or commodities (38%) semi-manufactured products (54%) and manufactured products (52%) (Table 3). Non traditional exports<sup>5</sup> have been increasing their share over the last 15 years, representing more than 30% of all total exports and having MERCOSUR as their principal market. In the case of basic products or traditional exports, their relative share in MERCOSUR has decreased in 2005/6, although not in absolute values.

Historically, Paraguay's exports to the European market have been concentrated in commodities or basic products. Over the last two years (2005/6) Paraguay exported, on

<sup>5</sup> Non traditional exports in Paraguay are considered those different from basic products such as soybean, meat, cotton, timber. They are composed of other agricultural products (new in the export market) plus manufactured and semi manufactured products.

average, US\$ 305 million in basic products to Europe, while US\$ 23 million were exported as semi-manufactured products and US\$ 26 million of manufactured ones. From 2000/1 to 2005/6, commodities exports to the EU have registered a growth of 138%, although its relative share of Paraguay's total exports only went up three points (from 20 to 23%). During the same period export of semi-manufactured products have lost market share from 26 to 10% (US\$ 31 million to US\$ 23 million), while exports of manufactured products to the EU market increased both in absolute and relative values, but not representing an important share over the total exports to that market.

On the contrary, exports to the United States markets have concentrated in manufactured products representing more than two thirds of total exports to that market in the 1990-2006 period.

However, taking in account only manufactured products, the USA and the EU markets have absorbed 14% of total manufacturing exports of Paraguay, each one. In turn, participation of the USA and EU markets in total manufacturing exports is only half of all manufacturing exports to MERCOSUR. Actually MERCOSUR and the Rest of the World markets have been the principal recipients of Paraguay manufacturing exports in the whole period studied.

**Table 3**

**PARAGUAY: EXPORTS BY PRODUCTS AND REGIONS**

	Basic products					Semi manufactures					Manufactures				
	MCS	EU	USA	ROW	Total	MCS	EU	USA	ROW	Total	MCS	EU	USA	ROW	Total
<i>Average Value of Exports (in million US\$)</i>															
1990/1	254	247	7	188	696	34	22	15	15	85	29	16	16	5	66
1995/6	318	222	11	99	650	87	26	14	15	142	120	20	18	29	187
2000/1	266	128	2	238	634	62	31	9	19	119	88	21	20	46	177
2005/6	329	305	19	655	1.308	144	31	20	36	222	132	21	26	79	264
<i>Participation in Total Exports (%)</i>															
	Basic products					Semi manufactures					Manufactures				
	MCS	EU	USA	ROW	Total	MCS	EU	USA	ROW	Total	MCS	EU	USA	ROW	Total
1990/91	36	36	1%	27	100	40	25	17%	18	100	44	24	24	7	100
1995/96	49	34	2%	15	100	61	18	10%	10	100	64	11	9	15	100
2000/01	42	20	0%	38	100	52	26	7%	15	100	50	12	12	27%	100
2005/06	25	23	1%	50	100	65	10	9%	16	100	50	10	10	30	100
<i>Average 90/06</i>	<i>38</i>	<i>28</i>	<i>1%</i>	<i>32</i>	<i>100</i>	<i>54</i>	<i>20</i>	<i>11%</i>	<i>15</i>	<i>100</i>	<i>52</i>	<i>14</i>	<i>14</i>	<i>20</i>	<i>100</i>

**Source:** Elaborated with data of the BCP. Products were classified according to SECEX (Brazil)  
MCS: Mercosur; ROW: Rest of the World.

Manufacturing exports to the EU market during 2005/6 have mainly consisted of wood and leather manufacturing, textiles, cigarettes, essential oils, animal products and beverages (fruit juices). In the case of the USA market, the manufacturing export structure is similar to the EU market. Two thirds of manufacturing exports to the USA market has concentrated in 15 tariff items of the Harmonized System (HA). On the other hand semi-manufactured products exported to the EU and the USA markets, are concentrated on leather, timber, refined sugar, and vegetable oils

### Analysis of export patterns to the USA and EU markets

In order to determine the degree of symmetry in the export pattern of Paraguayan manufacturing products to the USA and EU markets, the Markwald-Machado (1998) methodology is applied, introducing certain corrections, so to adapt it to the international trade pattern for Paraguay as a small country. Particularly, adjustments were introduced to the selection criteria of competitive manufacturing products exported to USA and the EU. Products selected were those whose export figures have been greater than US\$ 100.000, on average, to the US market on the 2004-2006 period<sup>6</sup>.

Once obtained a list of manufactured products with export figures greater than US\$ 100.000 for the US market, a similar list of these products (six digits of the HS) is obtained for exports to the EU market during the same period (average). From both lists, products have been selected as follows:

$$\frac{\frac{X_i^{USA}}{X_{total}^{USA}}}{\frac{X_i^{EU}}{X_{total}^{EU}}} > 2$$

$$\forall X_i^{USA} > US\$ 100 \text{ mil}$$

Where:

$X_i$  is equivalent to exports of manufactured product  $i$  at six digits of the HS

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<sup>6</sup> The proposed methodology is based on the following: if a product is exported to the US market with all international requirements in terms of technical, quality and sanitary standards, this product is considered competitive. For the same reason, the same product could also be considered competitive for other markets like the European Union.

$X_{total}$  corresponds to total manufactured exports to the USA and EU markets

Following the adjustment of the Makrwald-Machado criteria, 21 products ( 18 manufactured and 3 semi-manufactured), have been selected, equivalent to 67% of all industrial products exported to the US market and only 12% of all industrial goods exported to the European market. As a first observation (Table 4) the competitiveness gap is larger in the case of semi-manufactured products than in the case of manufactured products when both destination markets are compared. Manufactured exports products to the US market is 19 times greater than in the case of the EU market, while semi-manufacturing exports to the US market is 456 times greater than to the EU market. This first comparison indicates certain specialization asymmetries in terms of industrial products exported by Paraguay to both markets.

**Table 4**  
**Paraguay: Selected Export Products to USA and EU**

	USA			EU		
	Manufactures	Semi-manufactures	Total.	Manufactures	Semi-manufactures	Total
Total Exports	27.923	18.514	46.437	25.468	24.032	49.500
As a proportion of Total (%)	60	40	100	51	49	100
Criterion: USA over US\$ 100.000	23.971	18.262	42.233	18.759	23.955	42.714
N° of competitive items to the USA	27	3	30		nd	
As a proportion of Total (%)	52	39	91	38	48	86
Markwald Machado (MM) Criterion	13.049	18.262	31.311	640	5.196	5.836
As a proportion of Total	28	39	67	1	10	12
N° of item with non similar export pattern	18	3	21		nd	

**Source:** Elaborated with data of BCP

In terms of the differential rates of competitiveness of products between both markets, semi-manufactured products (sugar, vegetable oils and timber) show a specialization pattern for the US market rather than in the EU market (Table 5). In the specific case of sugar (mainly organic sugar) the US market participation is 534 times greater than the participation of the EU market. Likewise, manufactured products from Paraguay are preferred by the US market much more than the European market: out 18 manufacturing products, 14 of them show a specialization pattern in the US market.

In other words, there are many products from Paraguay with export specialization to the US market that, at the same time are completely absent in the European market. These goods are: dog or cat food, wood products, leather manufacturing (bags, trunks, purses, wallets, etc...), bars and rods of iron, plastic products, insecticides, basketwork and garment products. Also there is a significant difference in terms of export values of cigarettes and wood pieces for construction between both markets.

**Table 5**  
**Paraguay: Selected Products and Market Specialization**

(in thousand of US\$ on average)

Tariff Lines		Export to USA		Export to EU		MM Criterion (**)
		Value (*)	(%)	Value (*)	(%)	
Selected Products		<u>31.311</u>	<u>67,4</u>	<u>5.836</u>	<u>11,8</u>	<u>5,7</u>
<u>Semi-manufactures</u>		<u>18.262</u>	<u>98,6</u>	<u>5.196</u>	<u>0,2</u>	<u>456,3</u>
170111	Sugar	15.963	86,2	3.883	0,2	533,6
151540	Tung oil and its fractions (1)	2.152	11,6	713	0,0	391,9
440799	Other of other wood sawn or chipped lengthwise, sliced or peeled of coniferous wood	148	0,8	600	0,0	32,0
<u>Manufactures</u>		<u>13.049</u>	<u>46,7</u>	<u>640</u>	<u>2,5</u>	<u>18,6</u>
240220	Cigarettes containing tobacco	3.626	13,0	234	0,9	14,1
441890	Wood pieces for construction	2.301	8,2	104	0,4	20,3
230910	Dog or cat food, put up for retail sale	1.246	4,5	0	0,0	Abs.
441213	Plywood, veneered panels and similar laminated wood:	1.073	3,8	0	0,0	Abs.
441830	Parquet panels	739	2,6	0	0,0	Abs.
420211	Leather: Trunks, suitcases, vanity cases, attache cases, briefcases, school satchels and similar containers:	641	2,3	0	0,0	Abs.
721420	Other bars and rods of iron or no alloy steel.	617	2,2	0	0,0	Abs.
391590	Waste, parings and scrap, of plastics of other plastics	539	1,9	166	0,7	3,0
441214	Other of plywood consisting solely of sheets of wood.	400	1,4	0	0,0	Abs.
441820	Doors and their frames and thresholds	382	1,4	136	0,5	2,6
420221	Leather: Handbags, whether or not with shoulder strap, including those without handle	305	1,1	0	0,0	Abs.
380810	Insecticidas	172	0,6	0	0,0	Abs.
460210	Basketwork, wickerwork and other articles, made directly to shape from plaiting materials	168	0,6	0	0,0	Abs.
420231	Leather: articles of a kind normally carried in the pocket or in the handbag:	161	0,6	0	0,0	Abs.
610990	T-shirts, singlets, tank tops and similar garments, knitted or crocheted of other textile materials	129	0,5	0	0,0	Abs.
620792	Men's or boys' singlets and other undershirts, underpants, briefs, nightshirts, pyjamas, bathrobes, dressing gowns and similar articles of man-made fibers	126	0,5	0	0,0	Abs.
392620	Articles of apparel and clothing accessories (including gloves)	112	0,4	0	0,0	Abs.

Total

46.437 100.0 49.500 100.0

Source: BCP

(\*) Includes 6 digits items of SA with average value export 2004-2006 over US\$ 100.000

(\*\*) It only includes items that satisfy (\*) term, with % of Export To USA/ % of Export to UE rate greater than 2.

Abs.: Absent (1) vegetable oil used for painting products and engineering machinery.

## Market share as determinant of competitiveness

Markwald and Machado (1998) argue that the great difference in import market sizes is the main factor that explains why there is divergence in terms of export patterns of MERCOSUR countries toward the USA and the EU markets. However, a relative high participation in some export markets in regards to other export markets is not necessarily determinant of the degree of competitiveness of a certain good. Product competitiveness is much more related to the capacity of a product being introduced in those markets and competing with local industries and other foreign suppliers.

The *market share* criterion adapts better to the task of assessing export product competitiveness since it measures the relative participation of a product within total imports of destination markets (or countries). As a matter of fact the *market share* criterion appears as a complementary indicator of export competitiveness of a country toward two or more markets, once the relative weight of exports products is considered in the importing countries.

In order to use the market share methodology to select export products of Paraguay to US and EU markets the threshold for market share competitiveness has been fixed for those products that are equivalent or superior than 0,1% of all imports from the United States. COMTRADE data has been used for import figures from both markets, comparing the years 2002 and 2005. Import data has been collected at 6 digits of the HS, and classified according to SECEX in: i) basic products; ii) semi-manufactured products and iii) manufactured products.

With all data collected, products imported by the United States from Paraguay were selected with market share equal or superior than 0.1%. After this first selection, another one is done with all items at 6 digits of the HS according to the following criterion:

$$\frac{M_i^{USA}}{M_{total}^{USA}} \bigg/ \frac{M_i^{EU}}{M_{total}^{EU}} > 2$$

$$\forall \frac{M_i^{USA}}{M_{total}^{USA}} > 0,1\%$$

Where:

$M_i$  = imports from the USA and the EU of a product  $i$  from Paraguay

$M_{total}$  = total imports of the USA and the EU, excluding imports of selected products from Paraguay.

Thus, selected products represented 83% of total manufactured products imported by the US market from Paraguay, and 38% from the EU. In the case of US, 80% of all products imported are manufactured and only 3% appears as semi-manufactured products. For the European markets, 37% of all products imported are manufactured and only 1% is classified as semi-manufactured ones<sup>7</sup> Competitiveness gap between the US and EU markets has been observed for 15 industrial products, from which only one product correspond to the semi-manufactured category (Table 6)

In terms of the manufacturing group, US imports from Paraguay amounted to US\$ 36 million on average for 2002 and 2005, respectively, in comparison to only US\$ 11 million imported by the EU market. Asymmetries in the pattern of export competitiveness are clearly observed in goods such as cigarettes and sugar. Moreover, out of 14 manufacturing products, 6 of them are not registered as imported by the EU market, representing the major export competitiveness asymmetries for both markets. They are timber products, leather products, insecticides and cotton threads.

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<sup>7</sup> Sugar represents 25% of all manufactured products imported by the US from Paraguay. Official customs data in Paraguay registered exports of sugar as position 17011 of the HS. This position, according to the SECEX classification criterion corresponds to a semi-manufactured product. However customs in the US and in the EU register sugar imported from Paraguay (mainly organic sugar) as position 170199 of the HS, in other words as a manufactured product according to the SECEX classification.

**Table 6**  
**Paraguay: competitiveness differentials for the USA and EU markets**  
(in thousands of US\$ on average)

Tariff Lines	USA imports from PRY		EU imports from PRY		Market Share Criterion (**)
	US\$ (*)	(%)	US\$	(%)	
<b>Selected Products</b>	<u>37.462</u>	<u>83,4</u>	<u>11.672</u>	<u>38,3</u>	<u>2</u>
<b><u>Semi-manufactures</u></b>	<u>1.305</u>	<u>2,9</u>	<u>467</u>	<u>1,5</u>	<u>2</u>
151540 Tung oil and its fractions	1.305	2,9	467	1,5	2
<b><u>Manufactures</u></b>	<u>36.157</u>	<u>80,5</u>	<u>11.205</u>	<u>36,8</u>	<u>2</u>
170199 Other of Sugarcane or beet sugar	11.593	25,8	1.518	5,0	5
440920 Nonconiferous wood (including strips and friezes for parquet flooring, not assembled)	8.316	18,5	8.853	29,1	1
440910 Coniferous wood (including strips and friezes for parquet flooring, not assembled)	6.564	14,6	0	0,0	Abs.
441890 Other of shingles and shakes	2.556	5,7	640	2,1	3
240220 Cigarettes	2.477	5,5	1	0,0	2876
441213 Plywood, veneered panels and similar laminated wood	1.759	3,9	0	0,0	Abs.
441219 Other of plywood	1.047	2,3	0	0,0	Abs.
420291 Other: with outer surface of leather	438	1,0	12	0,0	25
170310 Cane molasses	426	0,9	174	0,6	2
441299 Other of other plywood, veneered panels	328	0,7	0	0,0	Abs.
460290 Other of basketwork, wickerwork and other articles,	230	0,5	1	0,0	202
380810 Insecticides	196	0,4	0	0,0	Abs.
420211 Leather: trunks, suitcases, vanity cases, attache cases, briefcases, school satchels and similar containers	132	0,3	8	0,0	11
520513 Cotton yarn (other than sewing thread).	95	0,2	0	0,0	Abs.
<b>Total Products Imported from PRY</b>	<b>44.907</b>	<b>100,0</b>	<b>30.451</b>	<b>100,0</b>	

Sources: COMTRADE and SECEX

(\*) Only products with market share over or equal to 0.1% were selected. Average values of 2002 and 2005

(\*\*) It only includes items that satisfy (\*) t with relative market share USA/EU equal or over 2

Abs: absent

## Explaining Competitiveness Gap

Except for the case of one type of manufactured wood, all products compared in Table 6, in terms of value exports, showed a clear preference for the US market. In order to determine where the causes lie for this preference, we first examine the level of protection of US and EU markets on selected products derived from the *market share* criterion as well as the level of preferences for the entry of the same products to both markets. Then, we draw some important conclusions on other factors different than tariff through interviews conducted with entrepreneurs of leading export companies of non-traditional products in Paraguay.

### The Tariff Factor

Average tariff applied by the US on imported products are generally low. Actually average consolidated tariff for agricultural products, in 2006, was of 5.5% while the same was of 3.3% for non agricultural goods. Nevertheless, one of the most important features for the entry of goods exported from developing countries to the US market is the facility known as General System of Preference (GSP) that the US government provides unilaterally to selected countries, under conditions established by the US government itself. This preferential system consists of two programs. The first one, called Beneficiary Developing Countries (BDC), provides 3600 preference tariff lines for developing nations. The second program is named Least Developed Beneficiary Countries (LBDC) and it adds 1400 preference tariff lines to the BDC, for products imported from the poorest developing countries.

In the case of the EU, tariffs are implemented through a program known as TARIC that presents different tariffs of the European countries into an integrated system for different tariff levels. Two different set of tariffs are included in this system: the *ad valorem* tariffs that are specific and temporary ones and different levels of preferential tariffs within a facility similar to the United States, called GSPL. This facility of preferential treatment is divided in several programs corresponding to different agreements with countries and regions of the world. For manufactured and semi manufactured products tariffs are higher and progressive, especially for those imported goods used as inputs that are locally produced and for what it exists not only more protection, but also subsidies.

In Table 7 a comparison is made on the 17 tariff lines that have shown significant competitiveness gaps, following the *market share* criterion. Also included are specifications of tariff lines that benefit from preferential treatment in the US (GSP) and in the EU market (GSPL).

In terms of semi manufactured products, Tung oil and products have preferential treatment for two tariff lines in the US market and just one in the EU market. In any case there is

practically no difference in tariffs charged on import products of Tung oil in both markets, and yet more of these products are sold in the US than in the EU.

Manufactured products are present with 16 tariff lines that contains 52 products for which tariffs are established in both markets, 27 of them enjoys preferential treatment in the US and 28 of them in the EU.

Three products of *Other Cane and beet sugar* are exported by Paraguay, with two of them with preferential entry in the US market and none to the EU market. Tariffs for sugar import from both markets are the highest for all products, and there is a significant differential in tariff between both markets, being the European Union the higher. In terms of export value for this product, the US is the principal market for Paraguay by large. A similar pattern is observed on Cane molasses products.

In relation to *manufactured wood*, practically all products listed enjoy preferential treatment by the US and the EU. Preferential tariffs, in the case of the US, ranges from 0% to 8% and from 0% to 3.5% in the case of the EU. Although a number of products confront higher tariffs in the US market, most of them are imported in greater quantity and value by the US market rather than the EU market, with the exceptions of non- coniferous wood products. Other items related to manufactured wood are *shingles and shakes* whose products enjoys the same zero tariff in both markets, but, again, they are mostly exported to the US market.

*Cigarettes* products have preferential treatment in the US market and higher protection in the EU market, despite being also in the GSPL. Exports of these products are definitively directed to the US market alone.

In contrast, *manufacturing leather* products encounter higher tariff protection in the US market and preferential treatment in the European Union. Average tariff for leather products imported by United States from Paraguay is 6.5%, while the same products have zero tariff in the European Union. Despite a major opening of the European market for these products, the US continues to be the preferred export market.

Finally, products such as *insecticides* and *cotton yarn* shows more preferential treatment in terms of tariff from the EU market than in the case of the US market. However, similarly to the case of wood and leather manufactures, goods corresponding to these tariff lines end up in the US market and are completely absent in the European market.

**Table 7**  
**Paraguay: tariff differentials for the USA and EU markets**

Products with competitive advantage distinction		US Tariff 2007		EU Tariff 2007*	
		%	GSP	%	GSPL
<u>Semi-manufactures</u>		-	-		
1515.90	Tung oil and its fractions				
	1515.90.21	0,0		0,0	
	1515.90.60	0,0	A	1,6	GSPL
	1515.90.80	0,0	A	n.d.	
<u>Manufactures</u>		-	-		
1701.99	Other of Cane or beet sugar				
	1701.99.05	3,6606 ¢/kg	A*	41,90 EUR / 100 kg	
	1701.99.10	3,6606 ¢/kg	A*	41,90 EUR / 100 kg	
	1701.99.50	35,74¢/kg		41,90 EUR / 100 kg	
4409.21	Non coniferous wood (including strips and friezes for parquet flooring, not assembled) continuously shaped				
	4409.21.05	0,0	A	0,0	
	4409.21.90	0,0		0,0	
4409.10	Coniferous wood (including strips and friezes for parquet flooring, not assembled)				
	4409.10.05	0,0		0,0	
	4409.10.10	0,0		0,0	
	4409.10.20	0,0		0,0	
	4409.10.40	0,0		0,0	
	4409.10.45	0,0		0,0	
	4409.10.60	0,0		0,0	
	4409.10.65	4,9		0,0	
	4409.10.90	0,0		0,0	
4418.90	Other of shingles and shakes				
	4418.90.25	0,0		0,0	
	4418.90.46	0,0	A	0,0	
2402.20	Cigarettes containing tobacco				
	2402.20.10	0,0	A	6,5	GSPL
	2402.20.80	\$1,05/kg +2,3%		n.d.	
	2402.20.90	0,0	A	40,3	GSPL
4412.31	Plywood, veneered panels and similar laminated wood				
	4412.31.05	0,0		0,0	
	4412.31.25	8,0	A*	0,0	
	4412.31.40	0,0	A	0,0	
	4412.31.51	8,0	A*	0,0	
	4412.31.60	8,0	A*	0,0	
	4412.31.91	8,0	A*	0,0	
4412.39	Other of plywood consisting solely of sheets of wood.				
	4412.39.10	0,0		3,50	GSPL

**Table 7**  
**Paraguay: tariff differentials for the USA and EU markets**

		4412.39.30	3,4	A*	3,50	GSPL
		4412.39.40	8,0	A*	3,50	GSPL
		4412.39.50	5,1		3,50	GSPL
4201.00	Saddlery and harness for any animal					
		4201.00.30	0,0	A	0,0	GSPL
		4201.00.60	2,8	A*	0,0	GSPL
4202.91	Other: with outer surface of leather, of composition leather or of patent leather					
		4202.91.00	4,5		0,0	GSPL
1703.10	Cane molasses					
		1703.10.30	0,0	A	0,35 EUR / 100 kg	
		1703.10.50	0,0	A	0,35 EUR / 100 kg	
4412.99	Other of other plywood, veneered panels and similar laminated wood					
		4412.99.06	0,0		0,0	GSPL
		4412.99.10	0,0		0,0	GSPL
		4412.99.31	8,0	A*	0,0	GSPL
		4412.99.41	8,0	A*	0,0	GSPL
		4412.99.51	0,0		0,0	GSPL
		4412.99.57	0,0		0,0	GSPL
		4412.99.60	0,0		0,0	GSPL
		4412.99.70	0,0	A	0,0	GSPL
		4412.99.80	8,0	A*	0,0	GSPL
		4412.99.90	5,1	A*	0,0	GSPL
		4412.99.95	0,0		0,0	GSPL
4602.90	Other of basketwork, wickerwork and other articles, made directly to shape from plaiting materials or made up from articles of heading 4601; articles of loofah					
		4602.90.00	0,0	A	1,2	GSPL
4418.79	Other of Assembled flooring panels					
		4418.79.00	0,0	A	0,0	
3808.50	Insecticides, rodenticides, fungicides, herbicides					
		3808.50.10	0,0	A	0,0	GSPL
		3808.50.40	0,0	A	0,0	GSPL
		3808.50.50	5,0		0,0	GSPL
4202.11	Leather: trunks, suitcases, vanity cases, attache cases, briefcases, school satchels and similar containers					
		4202.11.00	8,0		0,0	GSPL
5205.13	Cotton yarn (other than sewing thread), containing 85 percent or more by weight of cotton, not put up for retail sale exceeding 43 nm but not exceeding 52 nm					
		5205.13.10	6,5		3,2	GSPL
		5205.13.20	7,3		3,2	GSPL

**Sources:** TARIC (Integrated Tariff of the European Union) and HTSUS (Harmonized Tariff System of the United States)

**References**

¢: US\$ cents

Kg: kilograms

A: GSP for US its refers to eligible products of designated Beneficiary Developing Countries (BDC) for purposes of the Generalized System of Preferences (*GSP*)

A\*: GSP for US indicate those articles that for some countries may not be designated as an eligible article for purposes of this preference. Paraguay is not included in this preferential group for 2007.

GSPL: Countries designated as beneficiaries for purposes of the Generalized System of Preferences of the European Union.

If the level of protection of markets, or the tariff factor, could become an explanatory variable for the different behaviour observed on selected products exported to the US and EU markets, it will only hold for manufactured sugar and cigarettes. Competitiveness gap for the rest of the products appears as definitively not related to the different tariffs imposed on them by the US and the EU markets. But how much weight differential tariffs carry on the entrepreneurial decision to choose one market over another, even for those products that clearly confront different levels of protection between markets? In the entrepreneurial perceptions there are definitively other factors regarded as more fundamental in their decision to make preferences over export markets: non-tariff barriers, different regulations on quality, technical norms, environmental norms, consumption patterns, distribution networks, transportation costs, among others.

### Entrepreneurial Perceptions

In order to understand what other factors are determinant for market preferences, interviews were conducted to eight export companies in Paraguay: three leather manufacturing companies, two in the wood manufacturing sector, and three leading companies in organic sugar, cigarettes and Tung oil.

Questions were made on four different and related topics: i) tariff and non-tariff barriers; ii) prices and consumption patterns; iii) market organization and distribution; and iv) principal competitors in destination markets.

We first offer the principal conclusions of the survey from the sugar and cigarettes manufacturing that have presented important differences in terms of tariffs for entries in both markets, to summarize afterwards the interviews with a Tung oil company and with companies that operates in the wood manufacturing and the leather manufacturing.

### **Sugar**

The differential in tariff in favour of the US market is explained because the United States government offers a system of quota for sugar imported from Paraguay. Without being part of the GSP this quota system permits that two thirds of volume imported from Paraguay be introduced to the US with zero tariff on average and only one third with the tariff established for this type of product (as observed in Table 7). This system operates through a facility called *Re-export Credit*: US companies that export sugar to the rest of the world could import the same quantity at a lower tariff to zero. Thus, this company in Paraguay, for instance, sells the product exclusively to a firm in the United States that is the major

importer of sugar, and also the major exporter of the same product. As a matter of fact, sugar exports from this company to the European market are done through the US firm.

In consequence, the tariff factor is important in comparing both markets for this product, explained by the facility offered by the US government. However and despite higher tariff in the European market, this one has no restriction in terms of quota so that eventually, export of organic sugar to this market could eventually increase more significantly than in the US market. In fact, this company, for instance, has greatly increased its exports to the EU over the last five years, from 0 to 20% of all value exported. Further, wholesale prices are more attractive in the European market, and quality requirements are not as strict as in the US market. In terms of labour and environmental norms, they have similar requirements in both markets, although *Fair Trade* is something that Europeans are more concerned than in the US.

Paraguay is the major exporter of organic sugar in the world<sup>8</sup>, and the prospect of growing export to the European market looks promising. It will depend on increasing export supply and also on lowering tariff from the EU<sup>9</sup>.

## **Cigarettes**

There is only one company that is exporting cigarettes in Paraguay. Exporting cigarettes to developed countries is a difficult task given all protective measures for consumers that have emerged over the last decades. Thus internal taxes are very high and commercials are very much restricted.

Nevertheless, the managers of this company in Paraguay state that tariff differentials between the European market and the US market are not important. The main problem is the pressure exerted by multinational companies in Europe to put hurdles to companies from developing countries, especially in terms of registration of their own brands. In this sense, they regard the US market with more clear and solid rules for competition in the internal market. In other words, legal and rules requirements from importing and selling cigarettes within the US market are more transparent than in the EU market.

Paradoxically, this company exports cigarettes to Eastern Europe, instead, because – as the managers explain - market rules are new and incipient, with little reinforcement, in that region. Also because Eastern Europe still have free zones within their territories where the bulk of exports is directed.

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<sup>8</sup> The total volume exported in the World is not high and only few countries are specialized in exporting this type of product.

<sup>9</sup> Preferential treatment for plain sugar is provided by the EU to the countries of the Lomé-Cotonou agreements. However, organic sugar is not produced by these countries, and so a higher tariff on this imported product from other countries is not justified.

## **Tung oil**

This product has been exported to the US and EU market since the 50's. Over the first decades, the European market has been the main recipient of this product. However the US market began to provide more advantages in terms of scale economies, so that on average Tung oil has ended up being sold to the US market in greater quantities.

According to the manager of an agro-industrial cooperative in the southeast of Paraguay (the main exporter of Tung oil in the country), the major volume exported have been absorbed by the US markets, and it helps the fact that the product is sold to the major distributors for the US market. On the contrary, buyers from Europe are multiple, smaller ones than in the case of US and practically all exports have to be sold to final consumers instead of distributors. Thus, exports costs are reduced in the case of the US market comparing to the EU market where the export company have to deal with several countries in separated operations.

There are no differences in terms of technical and quality norms between both markets or in the case of labour and environmental requirements and prices. The main competition is coming from China which is the major producer of Tung oil after MERCOSUR.

In summary, without tariff differentials, the US market is preferred because of the facility offered by distribution chains, and because it demand more volume than in the case of the European market.

## **Wood Manufacturing**

Interviews were conducted with two companies that produce and export wood for parquet flooring. Both firms export mostly to the US market and Canada, because of higher demand from those countries. Again, as in the case of Tung oil, the US market demands more volume from this product than the EU market.

One of the main causes for this demand differential lies in different product standards demanded by both markets. In the case of the United States, consumers prefer more natural wood in terms of floor termination, which is not the case for the European market that requires products with more quality and higher technical standard. Also, some countries in Europe, like England and Germany would only import manufacturing wood if the product has the green seal (for environment protection).

In terms of market distribution, the United States offer more advantages than the European Union. Also, US buyers and distributors travel to Paraguay to look for suppliers, to establish contracts with them and also to inform suppliers on the new requirements in terms of design, innovations and new products with different quality demanded by the importing market.

According to the exporting companies, there are no differences in terms of prices in both markets, and transportation costs seem to be less expensive for the European countries.

## **Leather Products**

Prices are more competitive in the European market, tariffs are preferential in the European market, and yet, leather products such as trunks, suitcases, vanity cases, attaché cases, briefcases, and others are ending up in the US market. Managers from the exporting companies interviewed explain the reason: the quality type of the products is preferred in the US market and specifically in the western region.

Paraguayan companies are specialized in natural and semi-finished leather products that are not demanded by the European market. Quality requirements, technical norms as well as sanitary and phytosanitary requirements are stricter in the European market. Also, there is a growing market in Europe for products with green certification (seal). Efforts are made, by Paraguayan companies, in the direction of producing with the European requirements, but still without much success.

Also, export orientation to the US market is favoured by a better networking in terms of product distribution as well as a fluid communication in terms of new designs, models and changes in fashion in the US market. Actually, US distributors travel to Paraguay to inspect plants and observed the readiness for changes required in production. According to the exporting companies, European distributors or buyers are not interested in working with suppliers the same way being is done by US buyers.

## **Concluding Remarks**

Paraguay's exports are based on agriculture commodities and on manufacturing based in natural resources. Manufacturing products are not much diversified and they have, on average, low levels of competitiveness. However, exports of manufacturing products to developed countries have provided signals of potentially increasing supply exports and of competitiveness. In the case of the US and EU markets, there is a paradox in terms on industrial exports. The US market represent only about 5% of total exports of Paraguay, yet near 90% of all goods exported to that market are manufactured or semi-manufactured, mainly based on natural resources. On the contrary, Paraguay's exports to the EU represent about 20% of the total exports, but only 38% of those exports are based on manufactured and semi-manufactured goods. However, exports of manufacturing products from Paraguay have steadily increased to both markets in the same proportion. In the case of US market, exports of semi manufactured products have also experienced growth. Finally, and as indicated by two different methods of analysis, manufacturing and semi manufacturing products have demonstrated greater competitiveness in the US market than in the EU market.

Tariff differential is not the factor that better explain why industrial products of Paraguay are more competitive in the US market, perhaps with the exception of organic sugar. Supply of manufacturing and semi manufacturing products is still scarce, despite an important increase of non-traditional products within total exports in Paraguay over the last

17 years; and most of them are directed to the regional market of MERCOSUR. Besides, and with a few exceptions the degree of quality and sophistication of manufacturing are still far from meeting consumers' desires in Europe. Also, norms and standards of manufacturing products from Paraguay are more adapted to the US market requirements than the European market.

Major demand (economies of scale) for scarce supply of manufacturing products from Paraguay, a better distribution network, less requirements in terms of technical, quality and environmental norms and a willingness to work the client-supplier relationships, are all features that distinguished the US market from the European, and these factors are the most relevant in explaining competitiveness gap in the selected manufacturing products between both markets. It has also helped the fact that Europe has historically been recipient of commodities exports from Paraguay and this trend has been slowly changing over the last decades, which is not the case of the US market.

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