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Imported inputs, Government Support and Performance of manufacturing exporters

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Access to imported intermediate inputs has been hailed as crucial in enhancing firm productivity and performance in exports. Indeed, this is perhaps the greatest gain by countries through globalization. A cut in global tariffs has promoted access to a larger variety of higher quality and cheaper inputs, enabling firms to lower their marginal costs and overcome the fixed costs of serving foreign markets. In addition, most countries go a step further and grant duty relief and tax exemptions to exporters to encourage them to use more imported intermediate inputs in their production processes.

Numerous studies using micro level datasets have found that firms having greater access to imported intermediate inputs are, in general, more productive and perform better in export markets. There are at least two channels through which access to intermediate inputs affects export outcomes of firms. Firstly, access to imported inputs raises firm total factor productivity, which in turn, boosts export performance. Secondly, access to quality and cheaper imported inputs lowers the production costs and the fixed costs of entry in export markets. These points underscore the need for trade policy in developing countries to ease access to imported intermediate goods. Duty drawback schemes and tax exemptions on imported raw materials and capital goods are a popular tool used towards this end, although implementation has remained complex and sometimes only benefit a few firms. However, studies looking at the effectiveness of these schemes are relatively scarce.

In this paper, we evaluate the effectiveness of a government duty and value added tax (VAT) exemption on the export outcomes of beneficiaries. The firm's export performance outcome of interest include the value of real exports, the number of product exported and the number of destination countries served per firm in a given year. We find that importer-exporters who benefit from duty and VAT exemptions have a significant premium over non-beneficiaries on these outcomes.

Policy that aims to boost export performance should focus on making it easier for firms to access imported intermediate inputs. More importantly we established that a policy programme such as duty and VAT exemptions, by making intermediate inputs accessible to firms, has a direct and significant impact on export performance of the beneficiaries. This makes a justifiable case to expand access to the programme to more users with potential benefits of expanding and deepening firm level export activity.