
FORMAL INVESTIGATION REPORT

Ceramic Tiles Industry:

Extension of Safeguard Action Against Imports

(SG Investigation No. 01-2004)

(Public Version)

20 October 2004

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B-1	Notice of Public Consultation, published in The Manila Times on 04 August 2004
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C	List of Participants: Preliminary Conference (13 July 2004)
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G	Summary of Landed Cost by Country of Origin – 2002
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J	Adjustment Plans

ABBREVIATIONS

AEM	ASEAN Economic Ministers
AFTA	ASEAN Free Trade Area
AHTN	ASEAN Harmonized Tariff Nomenclature
ASEAN	Association of Southeast Asian Nations
Ave.	Average
BIS	Bureau of Import Services
BOC	Bureau of Customs
BPS	Bureau of Product Standards
CEPT	Common Effective Preferential Tariff
CIF	Cost, Insurance and Freight
cm	centimeter
CMO	Customs Memorandum Order
COP	Cost of Production
CTMA	Ceramic Tile Manufacturers' Association, Inc.
DTI	Department of Trade and Industry
e.g.	exempli gratia (for example)
EU	European Union
F.O.B.	Freight on Board
GATT	General Agreement on Tariffs and Trade
IED	Import Entry Declaration
Inv.	Investigation
IRR	Implementing Rules and Regulations
ISO	International Standards Organization
kg	kilogram
KOTRA	Korea Trade Investment Promotion Agency
kwh	Kilowatt-hour
LC	Landed Cost
LPG	Liquefied Petroleum Gas
M	Million
MAV	Minimum Access Volume
MMI	Mariwasa Manufacturing, Inc.
MSCI	Mariwasa Siam Ceramics, Inc.
No.	Number
NSO	National Statistics Office
₱	Philippine Peso

PCPIA	Philippine Ceramic Products Importers Association
PNS	Philippine National Standard
POI	Period of Investigation
PROC	People's Republic of China
RA	Republic Act
RA 8800	Safeguard Measures Act of 2000
SG	Safeguard
sq. m.	square meters
SSG	Special Safeguard
TC	Tariff Commission
TECO	Taipei Economic Cultural Office
UAE	United Arab Emirates
USA	United States of America
USITC	United States International Trade Commission
VAT	Value Added Tax
VCPA	Vietnam Construction Ceramics Producer Association
Wtd.	Weighted
WTO	World Trade Organization

EXECUTIVE SUMMARY

This report is about extension of safeguard action against imports.

This report addresses the question of whether extension of the definitive general safeguard action, in accordance with Republic Act No. 8800 ("Safeguard Measures Act") and the WTO Agreement on Safeguards, would be justified against imports of ceramic floor and wall tiles.

Background

The domestic industry petitioned to extend the measure for three (3) years.

In 2002, the Secretary ordered the imposition of safeguard duty for three (3) years in the form of a specific duty on ceramic floor and wall tiles. Unless extended, the measure will terminate on 09 January 2005.

The domestic industry requested the Secretary to extend the measure for three years as it still needs more time to complete the implementation of its adjustment plan and become import competitive.

... pursuant to the provisions of the Safeguard Measures Act.

The Secretary referred the request of the domestic industry to the Tariff Commission pursuant to Section 19 (2) of RA 8800.

Statutory Framework

The Safeguard Measures Act, in consonance with the WTO Agreement on Safeguards, allows extension of definitive safeguard action against imports.

An extension of the measure may be extended if:

- the action continues to be necessary to prevent or remedy the serious injury, and
- there is evidence that the domestic industry is making positive adjustment to import competition.

A safeguard inquiry must follow the requirements spelled out in the Safeguard Measures Act and the procedures prescribed by the WTO.

In responding to the question of whether the extension of safeguard action against imports of ceramic tiles is warranted, the Commission was careful to conduct its inquiry process in accordance with the requirements of the Act and the procedures prescribed by the WTO Agreement on Safeguards.

Findings

The collective output of the two applicant companies constituted a major proportion of the total domestic production

The collective output of the two (2) applicant companies constitutes a major proportion of the total domestic production of ceramic tiles.

During the period under review...

The period under review is the period when the safeguard measure is in place, i.e., starting year 2002 up to when latest data is available.

...imports returned to pre-surge levels.

During the period under review, imports decreased to pre-surge levels.

There is evidence that the domestic industry is making positive adjustment to import competition.

The domestic industry made serious efforts to comply with its adjustment plan and there is evidence that the industry is making positive adjustment to import competition.

...applicants were able to reduce their unit cost of production ... arising from higher capacity utilization and efforts to minimize costs by the applicants

Despite the increasing cost of imported raw materials, power and fuel, the applicants were able to reduce their unit cost of production by 21% in 2004 from 2001 levels partly as a result of the economies of scale arising from higher capacity utilization and the efforts of both applicant companies to minimize costs.

...the current safeguard is effective...improvement in production, sales, market shares, employment and productivity.

The current safeguard measure is effective. The domestic industry saw improvement in its production; sales; market shares; employment; capacity utilization and productivity.

However, the measure is not sufficient to remove the threat of serious injury.

Although the safeguard measure is effective, it is not sufficient to remove the threat of increased imports that can cause serious injury. During the relief period, cheap imports continued to enter the domestic market as world export prices of ceramic tiles continue with its downward trend. Imports from countries in the *de minimis* list came in increased quantities and at low prices.

...cheap imports continued to enter...as downward trend in world prices

*... shift of imports to de minimis countries indicates that tiles are substitutable and... sensitive to price changes.
...import parity pricing...
...maintained 2001 prices...
barely enough to recover cost of production...
... industry continued to incur losses*

The ease in shifting of import source indicates that tiles are substitutable and import patterns are sensitive to price changes. These imports had driven down the prices of ceramic tiles in the Philippine market. In order to protect market share, the domestic industry continued to apply a pricing policy of import parity. The industry maintained its 2001 prices; barely enough to recover cost to produce and sell. Consequently, the industry continued to incur losses from operations despite improvements in production and sales. Thus, the full benefit of the relief for the domestic industry was not

...the full benefit of the relief ... was not maximized.

Many exporting countries in the Asian region continue to increase their production capacities.

... this indicates the likelihood of substantially increased imports ... unless safeguard action is extended, serious injury can occur

Without the safeguard measure...

... domestic selling price would fall below levels not enough to recover cost to produce and sell.

... efforts to make it competitive will put at risk...

... threaten their business recovery

Without the extension of action ... the positive gains... will be negated as it still needs to put in place its adjustment plan...

... the likelihood of increased imports the dominant cause of serious injury.

Extension of the imposition of safeguard action is justified in terms of R.A. 8800 and the WTO Agreement on Safeguards.

The extension of the safeguard measure will help the industry to complete their adjustment plan to face import competition.

maximized.

Many exporting countries in the Asian region, especially China, continue to increase their production capacities to tap the export market. These ceramic tiles are intended for export to countries mainly within the region (including the Philippines), indicating the likelihood of substantially increased exports to the Philippines and that, unless safeguard action is extended, serious injury can occur.

Without safeguard duty, the landed cost of imports will be lower than the domestic industry's selling price. The domestic industry will have to reduce its selling prices to a level which will not be enough to fully recover its cost to produce and sell (i.e., cost of production plus selling, administrative and general expenses) if it is to continue protecting its market share. If the safeguard duty is not extended, the local industry's efforts to make it competitive will be put at risk and threaten their business recovery.

Without the extension of the safeguard measure, the positive gains made by the domestic industry will be negated as it still needs time to fully put in place its adjustment plan to effectively face import competition.

Non-extension of the safeguard measure will likely lead to imports coming in at increased quantities which will be the dominant cause of serious injury to the domestic industry.

Recommendation

The Commission recommends that the definitive general safeguard action be extended for three (3) years.

The expected completion within 3 years of the natural gas distribution pipelines, together with the continuing program to reduce costs, will provide the favorable environment to make the industry competitive against imports.

The Commission further recommends that the measure shall continue to be liberalized following the linear reduction applied in the first three years of the safeguard action.

Effects of the Affirmative Recommendation

... on user industries and consumer welfare, ...

As the measure is only temporary and will be progressively liberalized, competition will return to its normal level.

... on employment, and...

Ceramic tile market is a buyers' market. Any unreasonable price increase is very unlikely, unless there are supply shocks.

... on regional development ...

With the continued existence of a viable domestic industry, consumers are assured of on-time delivery of volume orders, after-sales services in replacements of breakages and defects, and allow small lot orders.

The expected continued increase in output and sales would ensure the tenure of additional employment not only in manufacturing but also the related sales and distribution services.

The imposition of the definitive safeguard measure will ensure continuous operation of the domestic producers. This will bring continuing community development to areas where these manufacturers are located.

1 TERMS OF REFERENCE

1.1 The Initial Application of Definitive Safeguard Measure

On 11 April 2002 the Secretary of Trade and Industry (DTI), after reviewing the Tariff Commission's Formal Investigation Report (SG Inv. No. 01-02), issued the Decision imposing a definitive general safeguard duty for a period of three (3) years on ceramic floor and wall tiles.¹ Unless extended, the safeguard measure on ceramic tiles will terminate on 09 January 2005.

1.2 The Petition for Extension of the Measure

On 05 July 2004, the DTI Secretary (the "Secretary") referred the letter request of the Ceramic Tile Manufacturers' Association, Inc. (CTMA) to the Tariff Commission (TC) pursuant to the provisions of Section 19 (2) of RA 8800 (Safeguard Measures Act).

CTMA mentioned in its letter that while the safeguard action has been of immeasurable help to the domestic industry, it still needs more time to complete the implementation of its adjustment plan and become import competitive.

Section 19 (*Extension and Re-application of Safeguard Measure*) of the Safeguard Measure provides for the requirements and procedures in applying for extension of the measure.

The Commission shall evaluate if the action continues to be necessary to prevent or remedy the serious injury and there is evidence that the domestic industry is making positive adjustment to import competition during the period under review.

1.3 Period under Review

The period under review is the period when the safeguard measure is in place, i.e., starting year 2002 up to when latest data is available.

¹ The Decision provides for a safeguard duty of ₱5.40/kg on the first year, ₱4.30/kg on the second year and ₱3.50/kg for the third year. The first year of implementation of the definitive measure included the period in which the provisional safeguard measure took effect, i.e., 09 January 2002.

2 SAFEGUARD ACTION AND THE ROLE OF THE COMMISSION

2.1 The Safeguard Measures Act of 2000

On 19 July 2000, RA 8800 (*An Act Protecting Local Industries By Providing Safeguard Measures To Be Undertaken In Response To Increased Imports And Providing Penalties For Violation Thereof*) was signed into law and took effect on 09 August 2000, i.e., fifteen (15) days following its complete publication in two (2) newspapers of general circulation.

Its IRRs (Joint Administrative Order No. 03) took effect on 11 October 2000, i.e., seven (7) days after its publication.

The Act provides for:

- general safeguard measures to afford relief to domestic industries suffering from serious injury or the threat thereof as a result of increased imports, and
- special safeguard measures (i.e., additional duty not exceeding 1/3 of the existing rate of duty) on agricultural products marked “SSG” in Schedule LXXV-Philippines, when the import volume exceeds its trigger level or when the actual CIF import price falls below a trigger price level.

Extension and Re-application of Safeguard Measures

Section 19 of R.A. 8800 provides that:

“(1) Subject to the review under Rule 16, an extension of the measure may be requested by the petitioner if the action continues to be necessary to prevent or remedy the serious injury and there is evidence that the domestic industry is making positive adjustment to import competition.

(2) The petitioner may appeal to the Secretary at least ninety (90) days before the expiration of the measure for an extension of the period by stating concrete reasons for the need thereof and a description of the industry’s adjustment performance and future plan.” x x x x

The Formal Investigation

The conduct of formal investigation is governed by Rule 9 of the IRR to RA 8800.

The Commission shall, after due notification, conduct marathon public hearings to give all parties directly affected and such other interested parties as

consumers that in the judgment of the Commission are entitled to attend, an opportunity to be heard and to present evidence including the opportunity to respond to the presentations of other parties and to submit their views, inter alia, as to whether or not the application would be in the public interest.

The Commission shall conclude its formal investigation and submit a report of its findings and reasoned conclusions, whether favorable or not, to the Secretary within one hundred twenty (120) calendar days from the receipt of the referral by the Secretary, except when the Secretary certifies that the same is urgent, in which case the Commission shall complete the investigation and submit the report to the Secretary within sixty (60) days.

Upon its positive determination, the Commission shall recommend to the Secretary an appropriate definitive general safeguard measure. Thereafter, the Commission shall undertake the following post-formal investigation activities:

- monitoring of the domestic industry's progress and specific efforts to bring about a positive adjustment to import competition;
- conduct of investigation on the request for extension and re-application of safeguard measures;
- conduct of investigation on request for reduction, modification and termination of safeguard action; and
- after the termination of the safeguard measure, evaluation of the effectiveness of the actions taken by the domestic industry in facilitating positive adjustment to import competition.

Decision

Within seven (7) calendar days from receipt of the final report of the Commission, the Secretary shall make a decision, taking into consideration the general safeguard measures recommended by the Commission.

If the determination is affirmative, the Secretary shall issue, within two (2) calendar days after making his decision, a written instruction to the heads of the concerned government agencies to implement the appropriate general safeguard measure as determined by him.²

2.2 The World Trade Organization Agreement on Safeguards

Article 2 of the WTO Agreement on Safeguards provides that: *"A Member may apply a safeguard measure to a product only if that Member has determined, pursuant to the provisions set out below, that such product is being imported into its territory in such increased quantities, absolute or relative to domestic*

² In case of a negative final determination, the definitive safeguard measure on subject ceramic tiles will terminate on 09 January 2005.

production, and other such conditions as to cause or threaten to cause serious injury to the domestic industry that produces like or directly competitive products.”³

The Agreement provides further that: *A safeguard measure may be extended provided that the competent authorities of the importing Member have determined in conformity with the procedures set out in Articles 2, 3, 4 and 5 and that the safeguard measure continues to be necessary to prevent or remedy serious injury and that there is evidence that the industry is adjusting, and provided that the pertinent provisions of Articles 8 and 12 are observed.*

In order that a substantially equivalent level of World Trade Organization (WTO) concessions and other obligations to affected WTO Members is maintained, a country imposing safeguard measures may offer “adequate means of trade compensation” to affected exporting countries. If agreement is not reached on such compensation, said exporting countries are given an opportunity to suspend “substantially equivalent” concessions or obligations under GATT 1994 after the measures have been in place three (3) years, or immediately if safeguard action is taken against imports which have not increased in absolute terms and the measure does not conform to the provisions of the Agreement on Safeguards.

Disputes arising from the application of safeguard measures are subject to WTO dispute settlement procedures.

Safeguard measures, if imposed, must be liberalized progressively. A measure extended shall not be more restrictive than it was at the end of the initial period, and should continue to be liberalized.

The Uruguay Round of Multilateral Trade Negotiations resulted in a new Agreement on Safeguards which interprets and elaborates Article XIX. Article XIX of GATT 1994 stipulates that an emergency action is permissible only where the increase in imports (and the consequent serious injury or threat thereof) is due to unforeseen developments and the effect of GATT-WTO obligations, including tariff concessions. The Agreement on Safeguards, when it provides for the conditions for the application of safeguard measures (i.e., increased importation, serious injury or threat thereof, and causal link) is, however, silent on the circumstances prescribed by Article XIX.

As mentioned in the original investigation, the circumstances provided in Article XIX of GATT 1994 need not be demonstrated for the reason that the product under consideration (ceramic floor and wall tiles) is not the subject of any Philippine obligation or tariff concession under the WTO Agreement. Nonetheless, such inquiry is governed by the national legislation (RA 8800) and the terms and conditions of the Agreement on Safeguards.⁴

³ SG Inv. No. 01-02 Report (pp. 30-34) concluded that, in accordance with RA 8800, “ceramic tiles are being imported into the Philippines in increased quantities, both in absolute terms and relative to domestic production.”

⁴ SG Inv. No. 01-02 did mention two (2) developments: the Asian financial crisis and the entry of cheap imports from low-priced suppliers of ceramic tiles in the region, as totally unforeseen.

2.3 Articles 6 and 8 of the ASEAN Agreement on the Common Effective Preferential Tariff (CEPT) Scheme

Article 6 of the Agreement on the CEPT Scheme for the ASEAN Free Trade Area (AFTA) provides Emergency Measures in cases of increased importation which injures or threatens to injure an industry in the importing Member States. Said provision reads as follows:

“Article 6. Emergency Measures

1. If, as a result of the implementation of this Agreement, import of a particular product eligible under the CEPT Scheme is increasing in such a manner as to cause or threaten to cause serious injury to sectors producing like or directly competitive products in the importing Member States, the importing Member States, may, to the extent and for such time as may be necessary to prevent or to remedy such injury, suspend preferences provisionally and without discrimination, subject to Article 6(3) of this Agreement. Such suspension of preferences shall be consistent with GATT.”

Article 8, on the other hand, provides for the consultation requirement.

“Article 8. Consultations

1. Member States shall accord adequate opportunity for consultations regarding any representations made by other Member States with respect to any matter affecting the implementation of this Agreement. The Council referred to in Article 7 of this Agreement, may seek guidance from the AEM in respect of any matter for which it has not been possible to find a satisfactory solution during previous consultations.

2. Member States, which consider that any other Member State has not carried out its obligations under this Agreement, resulting in the nullification or impairment of any benefit accruing to them, may, with a view to achieving satisfactory adjustment of the manner, make representations or proposals to the other Member States concerned, which shall give due consideration to the representations or proposals made to it.”

3 THE COMMISSION'S INQUIRY

Section 19(2) of RA 8800 provides that:

“The petitioner may appeal to the Secretary at least ninety (90) days before the expiration of the measure for an extension of the period by stating concrete reasons for the need thereof and a description of the industry’s adjustment performance and future plan. The Secretary shall immediately refer the request to the Commission. Following the procedures required under Section 9, the Commission shall then submit a report to the Secretary not later than sixty (60) days from receipt of the request. Within seven (7) days from receipt of the report, the Secretary shall issue an order granting or denying the petition. In case an extension is granted, the same shall be more liberal than the initial application.”

3.1 Notifications

In compliance with the public notice requirements of the IRRs of RA 8800, the Commission made the following notifications during the course of its inquiry:

3.1.1 Commencement of Formal Investigation

The formal investigation commenced on 05 July 2004 upon receipt of the endorsement from the Secretary. (*Annex A*)

The Notice of Formal Investigation was published on 07 July 2004 in Manila Standard and The Manila Times (*Annexes A-1 and A-2*). The Notice indicated the date of the Preliminary Conference and the matters for discussion in that conference. The Commission sent individual notices to the following:

- The president of the CTMA for the petitioner domestic ceramic tile industry; other six (6) CTMA members;
- The president of the Philippine Ceramic Products Importers Association, Inc. (PCPIA), oppositor in the original investigation (SG Inv. No. 2001-02);
- Embassies in the Philippines of the following exporting countries: Australia; Bangladesh; Brazil; China; India; Indonesia; Korea; Malaysia; New Zealand; Singapore; Sri Lanka; Swiss Confederation; United States of America (USA) ; Thailand; United Arab Emirates (UAE); and Vietnam. Also invited was Taipei Economic and Cultural Office (TECO) and Korean Trade Investment Promotion Agency (KOTRA);
- 57 identified importers and 71 exporters of ceramic tiles from above-mentioned countries;
- Non-governmental organizations;
- Concerned government agencies; and
- Philippine Commercial Attaches based in above-mentioned countries.

3.1.2 Schedule of Public Consultations

The Notice of Public Consultation was published in the The Manila Times and Manila Standard both on 04 August 2004 (*Annexes B-1 and B-2*). Individual notices were sent to the concerned parties.

Parties were required to submit to the Commission within five (5) calendar days before the scheduled consultation a list of issues they want to explore other than the issues of product comparability and volume of imports. Furthermore, all principal parties, counsels, affiants, deponents and other interested parties are required to appear before the Commission on the first day of the public consultation.

3.2 Preliminary Conference

On 13 July 2004, the preliminary conference was held at the Tariff Commission. In attendance were counsels of CTMA and PCPIA.

Other parties who attended were representatives from CTMA; PCPIA; White Horse Ceramic (Phils.); Agerico Exports Corp.; Swire Realty Development Corp.; Monolith Construction; Bluish Enterprises; Global Art Concepts, Inc.; and United Architects of the Philippines – Q.C.

Representatives from the Embassy of Malaysia and Embassy of Indonesia were also present. Also present were representatives from the Bureau of Import Services (BIS) and the Bureau of Customs (BOC). (*Annex C for List of Attendees*)

The agreements reached during the preliminary conference were the following: the timetable of investigation; entry of appearance of interested parties; names of counsels; sufficient notice; accessibility of documents in the public file; treatment of documents marked confidential; submission of position papers; additional data required by the Commission; and verification thereof, including submission of adjustment plans by the domestic industry; conduct of ocular inspection; and schedule of public consultations.

These agreements were contained in a written Order dated 14 July 2004 and sent to the following parties: counsels for both the petitioner – CTMA and the oppositor - PCPIA; importers and exporters identified by the Commission based on import entries available at the Commission; non-governmental organizations; concerned government agencies; and the embassies of Australia; Bangladesh; Brazil; China; India; Indonesia; Korea; Malaysia; New Zealand; Singapore; Sri Lanka; Swiss Confederation; United States of America; Thailand; UAE; Vietnam; TECO and KOTRA.

3.3 Staff Report

The Commission issued its Staff Report on 13 August 2004. Copies of the Staff Report were issued to the concerned parties beginning 13 August 2004. Parties were given five (5) calendar days from receipt thereof an opportunity to

comment thereon. The factual findings of the Commission on aspects of product comparability and volume of imports are binding to the party who did not submit its comment.

TC received the comment of PCPIA that ceramic tiles originating from EU should be excluded from the subject matter of the investigation pursuant to Section 4 of RA 8800 and to an earlier decision of the DTI.⁵

3.4 Public Consultations

Public consultations were held on 23-24 August 2004 at the Commission (*Annex D* for List of Attendees). The consultations allowed interested parties opportunity to be heard and to present evidence, elaborate on their submissions, and respond and seek clarifications on the presentations and submissions of the other parties.

3.5 Plant Visits/Verification of Data

The technical staff of the Commission conducted an ocular inspection of the plant facilities of Mariwasa Siam Ceramics, Inc. (Mariwasa), Lepanto Ceramics Inc. (Lepanto) and Italfil Manufacturing Inc. (*Annex E* lists the visits made.)

The on-site inspection of Mariwasa Siam Ceramics, Inc. was conducted on 28 July 2004. Among the information determined/verified during the ocular inspection/verification were: the site of the leased power plant operated during the fourth quarter of 2003; actual production lines; financial records on production levels, cost, sales, selling price, employment and inventory levels. Verification of financial records was continued at the Mariwasa Manufacturing Inc. based in Rosario, Pasig City on 29 July 2004.

In the case of Lepanto, the on-site inspection and financial records verification was conducted 31 August 2004.

After the public consultation, the technical staff conducted further verification of the accounting records of Mariwasa Siam Ceramics, Inc. at Pasig City on 16 September 2004.

⁵ Ceramic tiles originating from Japan and the Member States of the EU were excluded in the 11 April 2002 decision of the Secretary.

4 PARTICIPANTS' VIEWS

4.1 Submissions to the Commission

The Notice of Formal Investigation, as published on 07 July 2004, was sent to all known interested parties. Interested parties were given until 26 July 2004 to submit their respective preliminary/supplemental position papers/documentary evidences. (*Annex F* for the List of Submissions)

The Commission received the position papers, through counsel, of the petitioner and the oppositor. The Commission received the letter dated 23 July 2004 from the Department of Trade and Industry of Indonesia. The Indonesian government is opposing the petition for extension of the measure.

Other submissions, mostly acknowledging receipt of the Notice, were also received by the Commission.⁶

As ordered during the Preliminary Conference, the Commission received from the petitioner, the non-confidential version of the application for extension of the measure, the status of compliance of Mariwasa to its adjustment plan and its future plan.

The non-confidential submissions from parties were made publicly available at the Commission for viewing or reproduction.

4.2 The Domestic Industry's Case

4.2.1 Petitioner

The petitioner, CTMA, submitted its amended position paper on 30 August 2004. CTMA alleged there is a need for extending the safeguard measure to prevent or remedy serious injury. The petitioner submits that:

- *The imposition of the Safeguard Measure contributed to the improvement of the Petitioner's financial condition:*

The stabilization of market price was due to increase in the price of imported tiles following the imposition of safeguard duty. Petitioner was able to sell their tiles above manufacturing cost although not enough to cover all financial costs. Petitioner further claims that it follows an import pricing policy to protect its market share and therefore cannot increase its prices.

⁶ Staff Report, p.6

- *Efforts made by Petitioner to implement its adjustment plan:*
 - Mariwasa's adherence to its adjustment plan resulted to better efficiency and a reduction in costs.
 - Unforeseen events and factors such as peso depreciation, re-training for starting lines, and transshipment to avoid payment of safeguard duty hindered its adjustment efforts. These were beyond its control.
 - The petitioner claims that it needs at least three (3) years extension of the safeguard measure to complete its adjustment plan and become competitive. Fuel costs account for 32% of variable cost. With the completion in 2007 of the gas distribution pipeline from Batangas to Manila, petitioner projects substantial dollar savings at current production levels.
- *Termination of the safeguard measure would be premature at this time as applicant has yet to complete its adjustment plan to be able to compete with imports on an equal footing.*

Termination would render useless the gains achieved by the petitioner during the period that the measure was in effect and risk the jobs dependent on the industry. The current export prices of ceramic tiles to the Philippines are even lower than the applicant's cost, although the gap has been reduced.

- Applicant also mentioned:
 - *the entry of low-priced but sub-standard tiles had been slowed down by the safeguard measure;*⁷
 - *its good faith and progress towards becoming more competitive; and*
 - *the additional time required for the government's program of power deregulation, operation of the natural gas pipeline, improvement of road infrastructure that would help lower the applicant's manufacturing costs.*

Adjustment Plan

Rule 4.1(a) of the IRRs of RA 8800 defines "*Adjustment Plan*" as "*an action which a domestic industry is required to submit that describes a set of quantified goals, specific plans, and timetables that a concerned industry commits to undertake in order to facilitate positive adjustment of the industry to import competition.*"

Rule 11.4 of the same IRRs provides that "*The adjustment plan shall provide a clear quantification of its proposed goals and detail the efforts that the domestic industry and other concerned parties will make to place the domestic industry in a more competitive position. The goals shall be presented using objectively verifiable indicators that will cover the period for which safeguard measures are sought.*"

⁷ The PNS 154:1992 (Ceramic Floor and Wall Tiles Specification) adopted by BPS is the standard followed by the domestic industry. It is, however, not a mandatory standard.

Measures covering more than one year shall include specific efforts to be undertaken by the domestic industry for each year of progressive liberalization of the measure. It shall likewise include a time frame to enable the Commission to monitor their attainment over the specified period.”

Submissions⁸

Mariwasa’s Adjustment Plan (2005-2007)

1. Provide even better products.
Introduce 180 new designs and features using the latest technology.
2. Improve distribution
The key to sustaining market leadership is keeping an extensive distribution network. Mariwasa will expand its distribution network by appointing new distributors throughout the country.
3. Strengthen brand equity.
Various marketing programs are in place to improve the Company’s brand equity, like increased advertising, participation in trade exhibits and upgrading product displays.
4. Reduce all manageable costs.
Three variable cost elements have the greatest impact on production costs are power costs, fuel costs and glaze raw material costs. Mariwasa will continue to maintain and operate its own power plant. Mariwasa also plans to reduce debts in 2005 by asset sales and additional capital infusion.

Quantifiable targets:

1. Reduce LPG cost by 12% over the next four years.
 2. Reduce bunker fuel cost by 12% over the next four years.
 3. Further reduce electricity consumption by 10% over the next three years.
 4. Reduce glaze costs by 8% over the next three years.
 5. Reduce maintenance cost by 8% over the next three years.
 6. Lower cost of funding.
5. Increase production yield
 1. Improve knowledge and skill of people in the production line
 2. Improve line management systems
 3. Improve equipment performance.

Lepanto Ceramic’s Adjustment Plan (2005-2008)⁹

A. Competitiveness through Cost Reduction and Efficiency

- Increasing production volume to an average of 600,000 square meters/month;

⁸ Annex J.

⁹ Summary of the adjustment plan (confidential version) submitted on 15 September 2004.

- Cost down scheme to result in 10-12% reduction of production cost.

B. Working Capital Management

- Maintain finished goods inventory at under 60 days stock;
- Trade receivables at maximum of 90 days;
- Stockpiling of body materials to hedge on cost and seasonal constraints; terms kept to 120 days maximum;
- Debt reduction by 50%

C. Product and Service Quality

- Rationalization of product mix by reviewing product mix and increase designs by 50%;
- Selective price increases where possible;
- Distribution network

4.3 The Opposing Case

4.3.1 PCPIA

PCPIA, through counsel, submitted its final Position Paper on 03 September 2004 on the following issues:

A. Requisites for an Extension

▪ *On the matter of Serious Injury*

Oppositors points that with the exception of Mariwasa, applicants registered financial losses from operations. These losses were further compounded by financial/bank charges and foreign exchange losses arising from prior borrowings. If there is serious injury caused by factors other than imports, such injury is not the one contemplated in the law. The serious financial injury reported by applicants is apparently caused by the need to service the huge prior debts incurred.

The Staff Report showed increased employment and productivity for applicant companies. Imports have significantly gone down. Thus, there is no longer significant impairment on the part of the local industry. If there is any injury, it only pertains to the financial losses which are not even causally linked to import competition.

▪ *On positive Adjustment to Import Competition*

Based on the TC monitoring report dated 04 November 2004, Lepanto's adjustment plan does not provide a clear quantification of its proposed goals. Furthermore, the goals have no objectively verifiable indicators to monitor.

In the application for extension of the measure, Lepanto appears not to have submitted any adjustment plan. To meet the “domestic industry” requirement, Lepanto should also submit its proposed adjustment plan.

B. Other Comments

Assuming for the sake of argument that an extension is granted, it should be more liberal than the initial application. With the significant reduction in the level of import volume, it would therefore be logical that the recommendation by the Commission would be more liberal than its ₱2.29/kg recommendation in the original application.

While the domestic sales of the local industry steadily increased, apparent domestic consumption decreased during the period when the safeguard measures were imposed. In-quota allocation would balance the interests of the consumers, importers and domestic producers.

4.3.2 Indonesia/ Malaysia

As mentioned in the Staff Report, the Department of Trade and Industry of Indonesia believes that imports of ceramic tiles into the Philippines, especially from Indonesia, do not cause serious injury to the domestic industry.

In its letter dated 18 August 2004, the Indonesian government opposed the extension of safeguard measures as it violated the provisions of Article 7(2) of the WTO Agreement on Safeguards. Further, the provisions in Article 12 of the same Agreement require evidence of serious injury or threat thereof caused by increased imports. Imports from Indonesia have declined rapidly from year 2001 to 2003.

According to Indonesia, the position paper of the domestic industry claimed that the selling output of the domestic industry could not cover the cost of manufacturing, selling, general and administrative cost and therefore the proceeding is irrelevant.

Indonesia and Malaysia put the investigating body on notice that they will ask for compensation if the safeguard duty is extended.

4.4 Other Submissions

Italfil Manufacturing, Inc. submitted an accomplished information sheet for the conduct of extension and re-application of safeguard measures. Attached in its submission are audited financial statements for 2001 –2003, production and quality reports.

5 THE DOMESTIC INDUSTRY AND MARKET

5.1 The Domestic Product¹⁰

The domestic industry produces unglazed and glazed ceramic floor and wall tiles. Ceramic tiles are used as outdoor and indoor floor and wall coverings in private dwellings, commercial and industrial buildings, urban facilities, etc. The more common sizes in the local market for floor tiles are 30 x 30 cm and 40 x 40 cm. In the case of wall tiles, the more common sizes are 20 x 20 cm and 20 x 25 cm. In the domestic industry, first class tiles are called commercial grade and those with slight glaze and body defects are labeled Grade B. Tiles with very visible defects are tagged rejects.

The major raw materials used to form the tile body are ball clay and feldspar which are also locally available. Silica sand may also be used. The glazing materials are all imported, mostly from Europe and China.

5.2 Market Participants

5.2.1 Domestic Producers

Table 1. Domestic Producers

COMPANY	LOCATION	Installed Capacity* ('000 sq. m.)	PRODUCT
Mariwasa Siam Ceramics, Inc. (ISO certified)	Bgy. San Antonio, Sto. Tomas, Batangas	17,191	Glazed ceramic floor and wall tiles
Lepanto Ceramics, Inc.	Km. 54, Makiling, Calamba, Laguna	11,980	Glazed ceramic floor and wall tiles **
Eurotiles Industrial Corporation (ISO certified)	Silang, Cavite	3,000	Glazed ceramic floor tiles (8"x 8" and 12" x 12")
Filcera Manufacturing, Inc. ***	San Vicente, San Pedro, Laguna	2,227	Glazed wall tiles (4'x4" and 8" x 8")
Italfil Manufacturing, Inc.	AIP-SEZ, Calibutbut, Bacolor, Pampanga	1,250	Unglazed floor tiles ****
Formosa Ceramic Tiles Mfg. Corp. (Grand Caesar)	San Simon, Pampanga	2,500	Glazed floor tiles (30 x 30 cm; 40 x 40 cm.)
Tri-Little Dragon (Pioneer)	Mandaluyong City	*****	Glazed floor tiles

* SG Inv. No. 01-2002 Report included non-operational kilns.

** Lepanto stopped production of granito tiles in 2002.

*** On-and-off operations during original POI. Shutdown since June 23, 2003. No definite period of resuming operations

**** Rated at 1,336,000 sq.m. in new information sheet.

***** Relatively small production capacity based on information from other manufacturers.

¹⁰ SG Inv. No. 01-02 Report, p.21

5.2.2 Status of Operations

From the information given, the following domestic tile manufacturers are currently in operation:

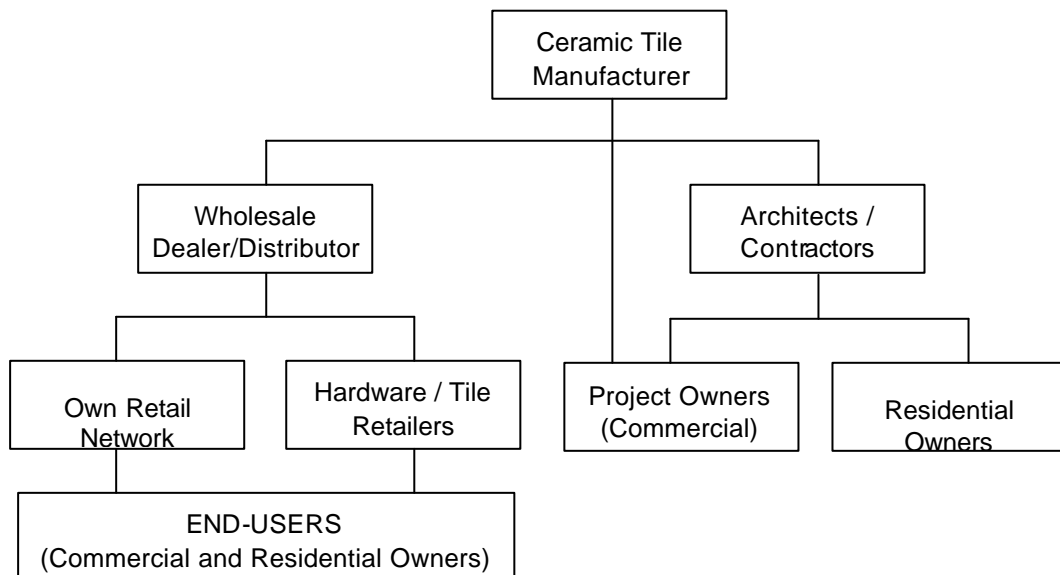
- Lepanto Ceramics, Inc.
- Mariwasa Siam Ceramics, Inc.
- Eurotiles Industrial Corporation.
- Formosa Ceramic Tiles Mfg. Corp. (Grand Caesar)
- Italfil Manufacturing, Inc.
- Tri-Little Dragon (Pioneer)

Filcera's production operations were on-and-off during the original investigation. It has been on shut-down since 23 June 2003. In its letter dated 21 July 2004, Filcera mentioned that it has no definite period for resumption of operations.

5.2.3 Distribution Channels

The finished products are distributed to wholesalers, distributors, architects and/or contractors. From the wholesalers or through the company's own retail network, these are then channeled to hardware and tile retailers where end-users can source their tiles.

Distribution Network Flow Chart *



* SG. Inv. No. 01-02 Report, p. 24.

5.2.4 Importers

Based on Import Entries on file with the Commission, 57 importers were identified for the period under review, i.e., year 2002, 2003 and 2004. The top importers identified are:

Table 2. Top Importers of Ceramic Tiles

Year	Importer	Quantity* ('000 sq. m.)	Country (Port of Origin)
2002			
1	Eurotiles Industrial Corp.	352.80	China; Vietnam
2	RAK Ceramics (Phils.) Corp	255.07	UAE
3	Generic Ent. Corp	214.93	China & Thailand
4	Femi International Trading	200.41	Vietnam
5	Cebu Oversea Hardware	148.60	Thailand
6	Felport Int'l. Marketing	106.54	Singapore; Indonesia
7	Mamj Intl. Trading	102.38	S. Korea; Vietnam
8	GA Mfg Co. Inc	96.20	India
9	Dendec Multi-industries	82.99	Thailand
10	MC Silva Enterprises	75.43	Thailand
2003			
1	Eurotiles Industrial Corp.	540.10	Vietnam, Malaysia; China
2	Deco Arts Marketing Inc.	451.62	Thailand, China, Brazil; Vietnam
3	Cebu Oversea Hardware Co Inc	189.16	Thailand; Vietnam; Malaysia; India
4	RAK Ceramics (Phils) Corp.	171.24	UAE
5	Mamj International Trading	164.03	Korea; Vietnam
6	Felport International Marketing	162.19	Indonesia; China; Singapore
7	Mountview Integrated Textile Mills	161.81	Vietnam; Korea
8	Westpoint Ind'l Sales Co., Inc	141.04	Vietnam; China; Brazil
9	Meren International Trading	137.13	Vietnam; Korea
10	Sharan Enterprises Inc.	116.70	India
2004			
1	World of Tiles	151.55	Hong Kong; China
2	FC South Trading	115.10	Hong Kong; China
3	Eurotiles	99.29	China; Malaysia
4	Sun-Lor Enterprises	88.32	Hong Kong; China
5	Wilcon Builders	86.29	China; Indonesia
6	Cebu Oversea Hardware Co., Inc	83.97	China
7	Deco Arts	61.10	Thailand; Indonesia
8	Xians Enterprises	55.13	China
9	Felport Int'l	40.11	Indonesia; China
10	Adventure	37.46	Vietnam

* SG Inv. No. 01-02 converted trade data from kg to sq. m. using factor (16 kg/sq.m).

5.2.5 Users

The major buyers of ceramic tiles are companies engaged in private and public housing, commercial projects, and infrastructure projects as well as direct purchasers at the retail level. Local contractors also utilize ceramic tiles in condominiums and shopping malls.

6 PRODUCT SUBJECT OF DEFINITIVE SAFEGUARD DUTY

The application of definitive safeguard duty covers imports of ceramic floor and wall tiles, unglazed or glazed, classified under AHTN Codes 6907.90.10, 6908.90.11 and 6908.90.21.¹¹

Imported ceramic tiles from Japan and member states of the European Union (EU) are not covered by the imposition of definitive safeguard duty per decision of the Secretary dated 11 April 2002.

Table 3. Tariff Schedule¹²

AHTN Code	Product	Duty Type	Rate of Duty (%)						
			1999	2000	2001	2002	2003	2004	2005
6907.90.10	Unglazed ceramic floor, hearth or wall tiles	MFN	20	15	10	7	7	10	10
		CEPT*	20	5	5	5	5	5	5
6908.90.11; 6908.90.21	Glazed ceramic floor, hearth or wall tiles	MFN	20	15	15	10	10	10	10
		CEPT*	20	15	10	10	5	5	5

MFN – Most-favored-nation (general rate of duty)

CEPT – Common Effective Preferential Tariff

* Requires a Certificate of Origin (CEPT Form "D") to be eligible for preferential tariff under the AFTA-CEPT Scheme. CEPT rate does not apply to Cambodia and Laos.

¹¹ Imports originating from a developing country are excluded from the imposition of safeguard measures if its share of imports of the product to the Philippines is less than 3%, provided that developing countries with less than 3% import share collectively account for not more than 9% of total imports.

¹² In 2004, the Philippines adopted the ASEAN Harmonized Tariff Nomenclature (AHTN) for tariff purposes.

7 VOLUME OF IMPORTS

The original investigation found that the surge in imports commenced in year 2000. Thus, the Commission concluded that, in accordance with RA 8800, ceramic tiles are being imported in increased quantities, both in absolute terms and relative to domestic production.

In SG Inv. No. 01-02, the period of investigation (POI) was from 1996 to the most recent period where data is available, i.e., 2001. In this investigation, the period under review is the period when the safeguard measure is in place, i.e., starting year 2002 up to the most recent period where data is available.

7.1 Volume

Table 4A. Volume of Imports of Ceramic Tiles

('000 sq. m.)

Year	1996	1997	1998	1999	2000	2001	2002	2003	2004*
Volume**	1,914	3,591	2,531	4,288	7,086	8,945	4,160	4,391	1,828
Growth Rate, (%)	-	88	(30)	69	65	26	(53)	6	

* 1st Semester of 2004

** National Statistics Office (NSO) trade data converted to sq. m. using methodology adopted in SG Inv. No. 01-02.

In the first year of imposition of the safeguard measure, total imports of ceramic tiles was reduced by more than half relative to 2001. On the second year of relief, imports increased slightly to 4.39M (million) sq. m. Imports in 2002 and 2003 approximate the total imports in 1999, the year prior to the import surge. Based on the 1st semester data for this year, imports may approximate the level of last year's total imports.

Table 4B. Import Volume and Country Shares

COUNTRY	VOLUME IN '000 SQM							
	1997	1998	1999	2000	2001	2002	2003	Jan-Jun 2004
TOTAL	3,590.60	2,530.86	4,288.47	7,085.56	8,945.26	4,159.82	4,390.85	1,827.64
PROC	326.19	251.37	593.95	650.30	2,898.46	519.08	378.38	759.69
<i>Share to Total Imports (%)</i>	9	10	14	9	32.40	12.48	8.62	41.57
SPAIN	1,326.52	728.99	766.37	1,212.72	817.92	761.65	898.70	234.72
<i>Share to Total Imports (%)</i>	37	29	18	17	9.14	18.31	20.47	12.84
BRAZIL	1.28	2.55	2.56	6.49	3.25	35.62	91.23	147.58
<i>Share to Total Imports (%)</i>	0.03	0.1	0.06	0.09	0.04	0.86	2.08	8.07
THAILAND	282.23	66.01	56.75	95.71	55.59	983.46	464.16	138.62
<i>Share to Total Imports (%)</i>	8	3	1	1	0.62	23.64	10.57	7.58
HONGKONG	33.86	19.17	19.37	346.57	655.12	96.95	33.30	108.19
<i>Share to Total Imports (%)</i>	1	1	0	5	7.32	2.33	0.76	5.92
MALAYSIA	121.27	135.54	397.69	544.15	342.23	96.77	110.13	102.64
<i>Share to Total Imports (%)</i>	3	5	9	8	3.83	2.33	2.51	5.62
VIETNAM	-	-	-	-	0.04	644.69	1,023.02	76.40
<i>Share to Total Imports (%)</i>	-	-	-	-	nil	15.50	23.30	4.18
TAIWAN	820.11	654.19	790.09	720.55	293.27	37.90	105.70	74.09
<i>Share to Total Imports (%)</i>	23	26	18	10	3.28	0.91	2.41	4.05
INDONESIA	9.25	199.62	883.56	2,769.41	3,392.31	149.37	194.53	51.09
<i>Share to Total Imports (%)</i>	0.25	8	21	39	37.92	3.59	4.43	2.80
BANGLADESH	-	-	-	-	-	15.29	77.66	37.94
<i>Share to Total Imports (%)</i>	-	-	-	-	-	0.37	1.77	2.01
ITALY	531.63	183.43	257.24	243.57	231.05	222.13	163.21	36.72
<i>Share to Total Imports (%)</i>	15	7	6	3	2.58	5.34	3.72	2.01
JAPAN	0.71	2.09	4.08	11.49	29.40	17.51	8.46	28.22
<i>Share to Total Imports (%)</i>	nil	0.08	0.09	0.16	0.33	0.42	0.19	1.54
DJIBOUTI (Affars & Issas)	-	-	-	-	-	-	-	12.48
<i>Share to Total Imports (%)</i>	-	-	-	-	-	-	-	0.68
SINGAPORE	65.55	64.75	21.99	23.94	42.81	105.25	51.34	8.66
<i>Share to Total Imports (%)</i>	2	3	1	0	0.48	2.53	1.17	0.47
UAE	28.77	172.06	401.95	367.51	113.04	192.61	150.80	6.34
<i>Share to Total Imports (%)</i>	1	7	9	5	1.26	4.63	3.43	0.35
KOREA	0.05	2.20	3.28	27.20	20.64	99.56	419.76	1.32
<i>Share to Total Imports (%)</i>	nil	nil	0.07	0.4	0.23	2.39	9.56	0.07
INDIA	-	-	1.41	19.37	2.46	156.48	186.43	1.22
<i>Share to Total Imports (%)</i>	-	-	0.03	0.27	0.03	3.76	4.25	0.07
Other Countries *	43.18	48.89	88.18	46.58	47.67	25.50	34.04	1.04
<i>Share to Total Imports (%)</i>				nil	nil	nil	nil	nil

* Lumped under "Other Countries" are Belgium; USA; South Africa; Portugal; Norway; Germany; Sri Lanka; Switzerland; Australia; New Zealand; United Kingdom; France; Austria; Brunei; Canada; Iran; Luxembourg; Saudi Arabia; Swaziland; and Virgin Island/s.

7.2 Country Suppliers

Table 5A. Major Country Suppliers

	2001	2002			2003			2004		
COUNTRY	Rank	QTY * (‘000 sq. m.)	SHARE TO TOTAL IMPORTS (%)	Rank	QTY (‘000 sq. m.)	SHARE TO TOTAL IMPORTS (%)	Rank	QTY (‘000 sq. m.)	SHARE TO TOTAL IMPORTS (%)	Rank
Indonesia	1	149	4	8	195	4	6	51	3	9
China	2	519	13	4	378	9	5	760	42	1
Spain	3	762	18	2	899	20	2	235	13	2
Hong Kong	4	97	2	11	33	1	15	108	6	5
Malaysia	5	97	2	12	110	3	10	103	6	6
Taiwan	6	38	1	13	106	2	11	74	4	8
Italy	7	222	5	5	163	4	8	36	2	11

Table 5B. De Minimis Countries in 2001*

	2001		2002			2003			2004		
COUNTRY	QTY* (‘000 sq. m.)	SHARE TO TOTAL IMPORTS (%)	QTY (‘000 sq. m.)	SHARE TO TOTAL IMPORTS (%)	Rank	QTY (‘000 sq. m.)	SHARE TO TOTAL IMPORTS (%)	Rank	QTY (‘000 sq. m.)	SHARE TO TOTAL IMPORTS (%)	Rank
Vietnam	<1	Nil	645	16	3	1,023	23	1	76	4	7
Thailand	56	0.6	983	24	1	464	11	3	6	8	4
Korea	21	0.2	100	2	10	420	10	4	1	Nil	16
India	2	Nil	156	4	7	186	4	7	1	Nil	17
UAE	113	1	193	5	6	151	3	9	6	Nil	15
Brazil	3	Nil	36	1		91	2		147	8	3
Total		<2		52			53			20	

* Table 6, SG Inv. No. 01-02 Report

The top two (2) country exporters of ceramic tiles to the Philippines prior to the imposition of the measure, i.e., Indonesia and China, accounted for only 16% of total imports. On the other hand, imports from several countries in the *de minimis* list surpassed the 3% threshold during the relief period. Imports from these sources accounted for more than half of total ceramic tile imports of the Philippines.

Thailand, whose export of ceramic tiles to the Philippines in 2001 was only 56,000 sq. m., was the major source of imported ceramic tiles in 2002.¹³ Thailand ranked second in 2003. Korea's exports, on the other hand, reached 420,000 sq. m. in 2003 from a volume of 2,000 sq. m. in 2002. India accounted for more than 4% of imports of ceramic tiles.¹⁴ The continued increase in imports from Brazil after the imposition of safeguard measures is noted to have surpassed the 3% threshold.

Vietnam, Thailand and Korea accounted for more than 40% of total imports in 2002 and 2003. In 2003, Vietnam was the top exporter accounting for 23% of total imports of ceramic tiles to the Philippines. From a negligible volume of exports to the Philippines in 2001, Vietnam's export of ceramic tiles in 2003 reached 1.02M sq. m.

The total volume of the relatively higher priced imports from Italy and Spain during the period under review approximated the level prior to the imposition of safeguard duty which is about 1M sq.m.¹⁵

The shift of import source to countries in the *de minimis* list indicates that tiles are substitutable and sensitive to price changes.

7.3 Relative to Domestic Production

Table 6. Share of Imports to Domestic Production

Year	Imports		Domestic Production		Share of Imports to Total Production
	Volume ('000 sq. m.)	Growth Rates (%)	Volume ('000 sq. m.)	Growth rate (%)	
1996	1,914		11,275		17
1997	3,591	88	11,988	6	30
1998	2,531	(30)	12,217	2	21
1999	4,288	69	12,048	(1)	36
2000	7,086	65	13,819	15	51
2001	8,945	26	13,211	(4)	68
2002	4,160	(53)	17,559*	33	19
2003	4,391	6	19,484*	11	18

* Mariwasa, Lepanto and Italfil actual production and estimates of Eurotiles and Formosa.

¹³ During interview, petitioner claims there were imports originating from Thailand, Korea and Vietnam that were noted to have Chinese markings.

¹⁴ The DTI Secretary Order of 11 April 2002 imposed the safeguard duty on ceramic tiles on Vietnam, Korea, India and Thailand. The assessment conducted by BIS from January 2002 to May 2003 showed that these countries have exceeded the 3% share of total imports of ceramic tiles.

¹⁵ According to Ceramic World Review, n.48/2002, Europe (Italy and Spain in particular) is losing its leading position as producer area in terms of output while maintaining its supremacy in terms of quality.

7.4 Findings

The original investigation found that the surge in imports commenced in year 2000 with ceramic tiles being imported into the Philippines in increased quantities, both in absolute terms and relative to domestic production.

Following the imposition of safeguard measure, volume of imports in 2002 and 2003 was reduced significantly to levels that approximate the total imports in 1999 (the year prior to the import surge). Based on the figures for the 1st semester of 2004, total imports of ceramic tiles for this year is projected to slightly decrease relative to 2003.

In the ceramic tile market, switching between import sources is rather easy. To illustrate, imports from the two (2) major country suppliers in 2001, i.e., Indonesia and China, accounted for just 16% of total imports in 2002. Thus, from a high of 32% of total imports in 2001, volume of imports from China tumbled to less than 10% in 2003.

The reduction in imports from China in 2002 and 2003, however, was apparently replaced by several countries in the initial *de minimis* list. These countries accounted for more than half of total imports in 2002 and 2003. Imports from these countries had gone down considerably after their exclusion from the *de minimis* list in October 2003. Imports from Vietnam and Thailand, however, are still above the 3% threshold.

It is interesting to note that when the safeguard duty was imposed in October 2003 on imported tiles from these other Asian sources, China rose to be the top exporter of ceramic tiles to the Philippines again with more than 40% share of total imports, surpassing its share of 32% in 2001.

The temporary protection provided by the safeguard duty was not maximized.

7.5 *De Minimis* Import Volume

The volume of imports from the following developing countries was found to be *de minimis* throughout the entire period under review:

Table 7. Developing Countries with *De Minimis* Import Volume

Developing Country	Share to Total Imports (%)		
	2002	2003	2004
Bangladesh	0.37	1.77	2.08
Djibouti	-	-	0.68
Iran	Nil	-	-
Singapore	2.53	1.17	0.47
Sri Lanka	0.03	0.09	-
Swaziland	0.01	-	-

The composition of developing countries on *de minimis* volume of imports may change depending on the most recent annual data available.

8 DETERMINATION OF SERIOUS INJURY OR THREAT THEREOF

Rule 19 of the IRRs provides for the requirements in the application for extension, to wit:

“Rule 19.1. Subject to the review under Rule 16, an extension of the measure may be requested by the petitioner if the action continues to be necessary to prevent or remedy the serious injury and there is evidence that the domestic industry is making positive adjustment to import competition.”

Likewise, Rule 9.4.c requires the determination of the *“The presence and extent of serious injury or the threat thereof to the domestic industry that produces like or directly competitive product.”*¹⁶

8.1 Domestic Industry Requirements

Sec. 4(f) of R.A. 8800 defines “domestic industry” as *“the domestic producers, as a whole, of like or directly competitive products manufactured or produced in the Philippines or those whose collective output of like or directly competitive products constitutes a major proportion of the total domestic production of these products”*.

Table 8 shows that the two (2) applicant companies accounted for 67% to 69% of the total domestic production of ceramic tiles during the relief period. The domestic industry requirement under Section 5 of RA 8800 is therefore satisfied.

Table 8. Domestic Industry Requirement

Year	Actual Production (in '000 sq. m.)			Share to Total Production (%)	
	Applicant Companies ¹	Other local Manufacturers ²	Total	Applicant Companies ¹	Other local Manufacturers ²
1996	9,134	2,141	11,275	81	19
1997	9,969	2,019	11,988	83	17
1998	9,908	2,309	12,217	81	19
1999	7,992	4,056	12,048	66	34
2000	9,423	4,396	13,819	68	32
2001	9,298	3,913	13,211	70	30
2002	11,827	5,732*	17,559	67	33
2003	13,474	6,010*	19,484	69	31

Source: ¹ Mariwasa and Lepanto

² Eurotiles, Filcera and Formosa

* Estimates using Eurotiles and Formosa production capacity and Italfil's actual output

¹⁶ In SG Inv. No. 01-02, the Commission concluded that, in accordance with RA 8800, it finds that the domestic industry has suffered and is suffering a significant impairment in its overall market position, production and sales, capacity utilization, employment and profitability.

8.2 Serious Injury Factors

8.2.1 Market Share

Prior to import surge in 2000, the Philippine ceramic tile market was predominantly supplied by the local industry. Table 9 shows that the domestic industry enjoyed an average market share of 79%. When imports surged in 2000, the share of domestic industry dropped to 63%. In 2001, its share further declined to 57%.

From 1996-2001, demand for tiles grew at an average of 12%. During that period, however, imports grew at a faster rate of 44%.¹⁷

In 2002, domestic industry captured 75% of the apparent domestic demand, the share it held prior to the import surge. In 2003, the domestic industry just maintained its share of the market.

Based on this indicator, the safeguard duty has been effective in moderating flow of imports.

Table 9. Apparent Domestic Consumption of Ceramic Tiles and Market Shares

Year	Domestic Sales ('000 sq m)			Imports ² ('000 sq. m.)	Apparent Domestic Consumption ('000 sq. m.)	% Share to Total Apparent Consumption			
	Applicants ¹	Non-Applicants	Total Mftrs			Applicants	Non-Applicants	Total Mftrs.	Imports
1996	8,786	1,496	10,282	1,914	12,195	72	12	84	16
1997	9,122	1,828	10,950	3,591	14,542	63	13	75	25
1998	9,619	2,203	11,822	2,531	14,353	67	15	82	18
1999	9,145	2,898	12,043	4,288	16,341	56	18	75	25
2000	8,996	3,074	12,070	7,086	19,156	42	16	58	42
2001	8,937	2,932	11,869	8,945	20,814	43	14	57	43
2002	11,449	892*	12,340	4,160	16,500*	69	6	75	25
2003	13,124	985*	14,109	4,391	18,500*	71	5	76	24

Source: ¹ Mariwasa and Lepanto

² NSO Foreign Trade Statistics

Non-applicants: Eurotiles, Italfil & Formosa

* Based on the applicants estimated market shares

8.2.2 Production, Sales and Ending Inventory

8.2.2.1 Production

The Commission considers production as constituting aggregate output (i.e., regardless of market segments). Thus, in the evaluation of applicant companies' production levels, the Commission did not distinguish between production for domestic and export market.

¹⁷ SG Inv. No. 01-02 Report, p. 37-38

The production data showed that despite the growth of consumption during the period of import surge, domestic production lagged behind as imports captured the increases in demand. With the imposition of safeguard duty, however, production significantly increased by 27% in 2002, and another 14% in 2003.

Table 10. Production, Sales and Ending Inventory

Year	Production		Sales				Inventory	
	Total ('000 sq m)	% Change	Domestic ('000 sq m)	Exports ('000 sq m)	Total ('000 sq m)	% Change	Total ('000 sq m)	% Change
1996	9,134	---	8,786	176	8,962	---	1,342	---
1997	9,969	9	9,122	63	9,185	2	2,126	58
1998	9,908	(1)	9,619	48	9,667	5	2,367	11
1999	7,992	(19)	9,145	126	9,271	(4)	1,088	(54)
2000	9,423	18	8,996	321	9,317	Nil	1,194	10
2001	9,298	(1)	8,937	89	9,026	(3)	1,466	23
2002	11,813	27	11,449	98	11,547	28	1,650	13
2003	13,474	14	13,124	113	13,237	15	1,879	14
2004*	6,395		6,766	364	7,130		1,126	

Source: Mariwasa and Lepanto

*As of June 2004

8.2.2.2 Sales

Sales figures in Table 10 refer to applicant companies sales out of their own production (i.e., MMI imports of ceramic tiles are excluded). In the evaluation of industry sales, the Commission considers both domestic and export sales.

Volume of sales was relatively constant from 1996 to 2001; it failed to expand despite the growth in demand during the period of import surge. With safeguard duty in place, sales increased at about the same pace as production in 2002 and 2003. Export sales constitute less than 1% of total sales for over the period.

8.2.2.3 Finished Goods Inventory

During the import surge in 2000 and 2001, ending inventories were considered normal and manageable and are generally lower than inventory levels reached during the Asian crisis in 1997. While inventory increased in 2002 and 2003 to levels equivalent to about 1½ months of sales, these levels were still manageable.

With the application of the safeguard measure, the applicant companies' were able to effectively control inventory even when they were increasing production since sales was increasing proportionately.

8.2.3 Capacity Utilization

Increase in capacity utilization in 2002 resulted not only from the mothballing of kilns, though Lepanto had operated only one kiln, but also from the increase in the production of ceramic tiles.¹⁸ Although there was a 14% increase in production in 2003, operating capacity utilization slightly decreased from 86% to 83% with the operation of another kiln.¹⁹

Table 11 . Annual Rated Capacity, Actual Production and Capacity Utilization of Applicant Companies

Year	Rated Capacity ('000 sq.m.)		Ceramic Tile Production ('000 sq.m.)	Capacity Utilization (%)	
	All Kilns *	Operating Kilns		All Kilns	Operating Kilns
1996	11,793	11,793	9,134	77	77
1997	18,414	18,414	9,969	54	54
1998	24,880	18,381	9,908	40	54
1999	26,561	19,305	7,992	30	41
2000	28,172	18,054	9,423	33	52
2001	28,496	17,702	9,298	33	53
2002	23,642	13,785	11,813	50	86
2003	25,521	16,183	13,474	53	83
2004**	12,960	7,158	6,395	49	89

Source: Mariwasa and Lepanto

* All kilns include kilns not commissioned by Lepanto

**As of June 2004

With safeguard duty in place, the applicant companies had been able to improve capacity utilization and gradually utilize idle machinery and equipment. Capacity utilization is expected to increase as demand is projected to improve in the coming years.²⁰

8.2.4 Cost of Production

It is observed that the applicants were able to improve their procurement operation of local materials. To illustrate, prices of locally procured raw materials decreased from ₱**.*/kg in 2001 to ₱**.*/kg 2004. This development could be attributed to the continuing effort of the applicants in sourcing cheap raw materials without sacrificing the quality of the tiles. On the other hand, prices of imported raw materials (glazing products) continued to increase over the years. This development may be attributed to the weakening of peso (Table 17B). Despite

¹⁸ MMI-Pasig plant had permanently ceased operation in June 2001. Pasig plant has 4 kilns (normal cap., 4.8 million sq. m.)

¹⁹ Mariwasa's SK 5/6 kiln at Pasig plant was transferred to Batangas in 2002 and became operational in the last quarter of that year.

²⁰ With the increase in production, some equipment at Pasig was transferred to the Batangas plant in 2004; one more kiln will be transferred in 2005. The remaining machinery and equipment will be transferred by the middle of 2006.

increases in the price of imported inputs, both applicant companies still managed to lower the unit cost of raw material by 25% in 2004 from 2001 (Table 12).

The increase in labor cost by 35% in 2002 can be attributed to the 80% increase in the employment (Table 13) compared with the previous year. Both companies managed to decrease labor cost per unit of production by 16% in 2003 and 12% in 2004, respectively, despite the increase in workforce as production expanded (Table 10).

Electricity cost accounts for 10-12% of the cost of producing ceramic tiles. Mariwasa and Lepanto had long been dependent on Meralco for power. Based on the applicants' cost data, electricity/power cost per kilowatt-hour (kwh) continued to increase from ₱**.**/kwh in 2001 to ₱**.**/kwh in 2003. In 2004, the cost of power, however, decreased by 18% with the installation of two (2) generating sets at Mariwasa-Batangas plant in 2003 which began operation in October of that year. On per kilogram of tiles basis, cost of power was fell by 37% in 2004 from 2001.

Fuel Cost (Bunker Oil and Liquefied Petroleum Gas) constitutes 20 -24% of the production cost of ceramic tiles. From 2001 to 2003, fuel cost per kilogram of tiles increased by 21% despite increasing volume of production for that period. However, in 2004, it decreased by 7% due to a slight price reduction per liter/kilogram of these fuels.

Average fixed overhead per kg of ceramic tiles decreased by 35% in 2004 from 2001 which could be attributed to the increasing volume of production.

Table 12 . Cost of Production (₱/kg)

	2001	2002	2003	2004	% Change 2001-2002	% Change 2002-2003	% Change 2003-2004
Raw material					(16.45)	(4.48)	(5.92)
Local/body					(41.04)	(16.68)	(8.09)
Imported/glaze					19.78	4.36	(4.66)
Labor Cost					35.01	(15.74)	(12.39)
Variable Overhead					6.52	4.07	(14.66)
Power					13.29	(9.29)	(20.58)
Fuel					8.19	11.91	(7.01)
Others					(5.52)	2.98	(28.83)
Fixed Overhead					(23.18)	(12.39)	(2.43)
Total Production Cost					(9.91)	(3.49)	(8.99)

Source: Mariwasa and Lepanto

Overall, despite the increasing cost of imported raw materials, power and fuel, the applicants were able to reduce their unit cost of production by 21% in 2004 from 2001 levels partly as a result of the economies of scale arising from higher capacity utilization combined with efforts of both companies to minimize costs through local sourcing of cheaper raw materials. Mariwasa's lower production cost compared with Lepanto's is due to the former's installation of its generating sets in

2003. With the availability of natural gas in 2007, applicants expect to save up to 40% of gas fuel or 10% reduction on the cost of producing ceramic tiles.

8.2.5 Employment

During the import surge in 2000 and 2001, employment of the applicant companies contracted by 32% and 16%, respectively. With the imposition of safeguard duty, record showed a considerable rise in employment by 80% in 2002, and further increased by 3% in 2003 which is attributable to the increase in production during those periods.

Table 13. Employment of Applicant Companies

Year	Total Employees*	% Change
1996	1,189	---
1997	1,712	44
1998	1,287	(25)
1999	1,217	(5)
2000	833	(32)
2001	697	(16)
2002	1,256	80
2003	1,288	3
2004**	1,134	

Source: Mariwasa and Lepanto

*Directly involved in the production

**As of June 2004

8.2.6 Productivity

Labor productivity is derived by dividing annual production volume of ceramic tiles by the number of employees directly involved in production. The same measure is used by the applicant companies to evaluate productivity.

Labor productivity improved during the period of import surge due to reductions in employment and not because of increases in output. Productivity in 2002 decreased with the increase in employment. With the increase in production in 2003, however, productivity improved by 11%.

Table 14. Productivity of Applicant Companies

Year	Production ('000 sq.m.)	No. of Employees	Labor Productivity	% Change
1996	9,134	1,189	7,682	---
1997	9,969	1,712	5,823	(24.20)
1998	9,908	1,287	7,699	32.22
1999	7,992	1,217	6,567	(14.70)
2000	9,423	833	11,312	72.26
2001	9,298	697	13,340	17.92
2002	11,813	1,256	9,405	(29.50)
2003	13,474	1,288	10,461	11.23

Source: Mariwasa and Lepanto

8.2.7 Profitability

Table 15 shows the combined income statements of Lepanto and Mariwasa which were culled from applicants' audited financial statements. Lepanto prepares its financial statement on a fiscal year while Mariwasa on a calendar year. For purposes of presenting the combined income statement at uniform time period, Lepanto recasted its income statement to calendar year.

Combined income statements of applicant companies showed that sales increased in 2002 by 22% and by 23% in 2003.

With the increase in sales, cost of sales also increased by 15% in 2002 and 14% in 2003. The applicants enjoyed a gross profit of ₱47 million in 2002 and ₱235 million in 2003 from higher sales.

**Table 15. Combined Income Statements of Applicant Companies
(CY 2001-2003) (₱'000)**

Particulars	2001	2002	2003
Sales	1,603,087	1,957,253	2,411,337
Less: Cost of Sales	1,655,922	1,909,574	2,176,435
Gross Profit	(52,835)	47,679	234,902
Less: Operating Expenses	512,102	464,738	449,575
Income (Loss) from Operations	(564,937)	(417,059)	(214,673)
Other Income (Expenses)	(663,282)	(829,361)	(772,319)
Income(Loss) before Income Tax	(1,228,219)	(1,246,420)	(986,992)

Source: Mariwasa and Lepanto
CY –Calendar Year

The Commission, in its evaluation of the industry's profitability puts more weight to income from operation as this financial measurement is considered to be a more stringent gauge of the industry's financial health and a better indicator of the industry's ability to propel itself into a condition of profitability. Through this indicator, the Commission could better assess the direct impact of imports on the industry's financial performance. Interest expense and foreign exchange losses that aggravate the bottom line profitability of the domestic industry are not, however, related to imports.

The surge of imports (2000-2001) put pressure on the applicant companies (who adopt import parity pricing) to sell below cost in order to defend market share. This led to a considerable increase in operating loss during the period of import surge. Despite the imposition of safeguard duty, applicant companies still incurred losses from operations in 2002 and 2003. Nevertheless, the losses were decreasing during that same period. The low export prices (Table 17B) and the shift of importation to *de minimis* sources did not increase landed cost of imports to a level where domestic industry can profit.

Imports from PROC and Indonesia continued to enter in the Philippine market at low prices despite the safeguard duty (Table 17A). Worse, imports from countries in 2001 *de minimis* list (notably, Vietnam, Korea, Thailand and India) came in at substantial quantities (Table 5B) and at low prices from 2002 until 2003.

These imports had driven down the price of ceramic tiles in the Philippine market. Considering the industry's import parity pricing policy, Mariwasa and Lepanto could not increase their domestic prices as they would lose market share and incur even more losses. Thus, cheap imports forced the domestic industry to maintain its 2001 selling price (₱11/kg) to gain market share. The consequence of import parity pricing - depressed revenues – was a direct result of competition coming from low-priced imports continuously coming in especially from the aforementioned countries.

8.2.7.1 Return on Sales

Return on sales is derived by dividing income from operation by the sales revenue. To evaluate industry sales performance, income from operations is adopted in favor of net income so as to exclude interest expenses, foreign exchange losses and other expenses (e.g., equity in net losses of an affiliate, deferred charges) which do not form part of the operating costs.

Table 16. Return on Sales of Applicant Companies

Year	Income from Operations (₱'000)	Sales Revenue (₱'000)	Return on Sales (%)
2001	(440,425)	1,586,967	(27.75)
2002	(403,483)	1,957,253	(20.61)
2003	(214,673)	2,411,337	(8.90)

Source: Mariwasa and Lepanto

Return on sales showed improvement from negative 27.75% in 2001 to negative 20.61% in 2002 when safeguard measure was imposed. In the second year of the imposition of the measure, return on sales continued to show relative improvement.

8.2.7.2 Price Trends

Table 17A shows that in 2002, the domestic industry enjoyed a price advantage over the landed cost (LC) with safeguard duty (SD) of imported product by ₱0.63/kg. In 2003, however, landed cost (w/ SD) was pegged at ₱0.56/kg lower than the selling price of local tiles. This situation arose due to increasing imports of cheap tiles from Vietnam, Thailand, Korea and India (countries in the initial *de minimis* list).

In 2004, the local industry dropped its price to ₱11.42/kg while imports landed cost increased to ₱13.42/kg. The industry pegs its prices to the landed cost of competing imports from China and Indonesia. The safeguard duty and the depreciation of peso somewhat offset the decreasing FOB (US\$) value of imports (Table 17B).

Without safeguard duty, the landed cost of imports averaged ₱9.95/kg as opposed to the domestic industry's selling price (DSP) of ₱11.42/kg. The domestic industry would have to lower its selling prices by an average of ₱ 1.47/kg which will not be enough to fully recover its cost to produce and sell (i.e., cost of production

plus selling, administrative and general expenses) if it is to continue protecting its market share.

Table 17A. Comparison between Landed Cost and Domestic Selling Price (Peso/kg)

Year (a)	Importer*							Domestic Producers (i)
	Vietnam ¹ (b)	Thai ¹ (c)	Korea ¹ (d)	China (e)	Indonesia (f)	India ¹ (g)	Wtd.Ave. (h)	
2001	17.48	38.80	-	6.77	8.46	19.82	8.27	11.38
Without Safeguard Duty								
2002	10.37	8.04	7.50	10.31	11.76	7.75	9.96	11.13
2003	9.45	10.69	6.67	12.05	9.95	6.43	9.89	11.55
2004**	9.80	13.32	13.93	9.31	9.37	-	9.95	11.42
With Safeguard Duty								
2002	10.37	8.04	7.50	15.71	17.16	7.75	11.76	11.13
2003	9.68	10.69	6.67	16.35	14.25	6.53	10.99	11.55
2004**	13.30	16.82	17.43	12.98	12.87	-	13.42	11.42

* -Wtd Ave landed cost (net of VAT)

** - As of June 2004

¹ - *De minimis*, exempted from safeguard duty until 14 October 2003, (CMO 25-003) ²¹

(h) - Wtd. Ave. landed cost from all sources except EU countries and Japan

(i) - Wtd. Ave. (ex-plant) selling price (net of VAT) based on actual sales

Source: * - IED, NSO-Foreign Trade Statistics

(a) to (h) – refer Annex G to I

(h) – Lepanto and Mariwasa

Table 17B. F.O.B Value (US\$/kg)

Year	Exchange Rate (a)	Importer* (US\$/kg)							% Change (i)
		Vietnam (b)	Thai (c)	Korea (d)	China (e)	Indonesia (f)	India (g)	Wtd.Ave. (h)	
2001	50.9927	0.1933	0.5986	-	0.0837	0.1296	0.2604	0.1194	---
2002	51.6036	0.1564	0.1177	0.0978	0.1630	0.1680	0.1107	0.1499	25.54
2003	54.2033	0.1410	0.1615	0.0884	0.1731	0.1505	0.0891	0.1464	(2.33)
2004	55.8400**	0.1426	0.1883	0.1938	0.1248	0.1339	-	0.1344	(8.20)

* - Wtd. Ave. FOB prices

** - Estimated from import entries

Sources: Import Entries

(a) - Bangko Sentral ng Pilipinas

(h) – Wtd. Ave. FOB prices from all sources, except EU and Japan

²¹ DTI Secretary issued an amended decision removing Vietnam, Korea, India and Thailand from the list of developing countries excluded from imposition of safeguard duty.

8.2.8 Conclusion

The domestic industry saw improvements in its production; sales; market shares; productivity; capacity utilization and employment following the imposition of the safeguard measure.

The industry was able to reduce its unit costs of production partly as a result of economies of scale arising from higher capacity utilization and also with efforts of both companies to minimize cost. With the projected availability of natural gas in 2007, applicants expect to save up to 40% of gas fuel or a 10% reduction in the cost of producing ceramic tiles.

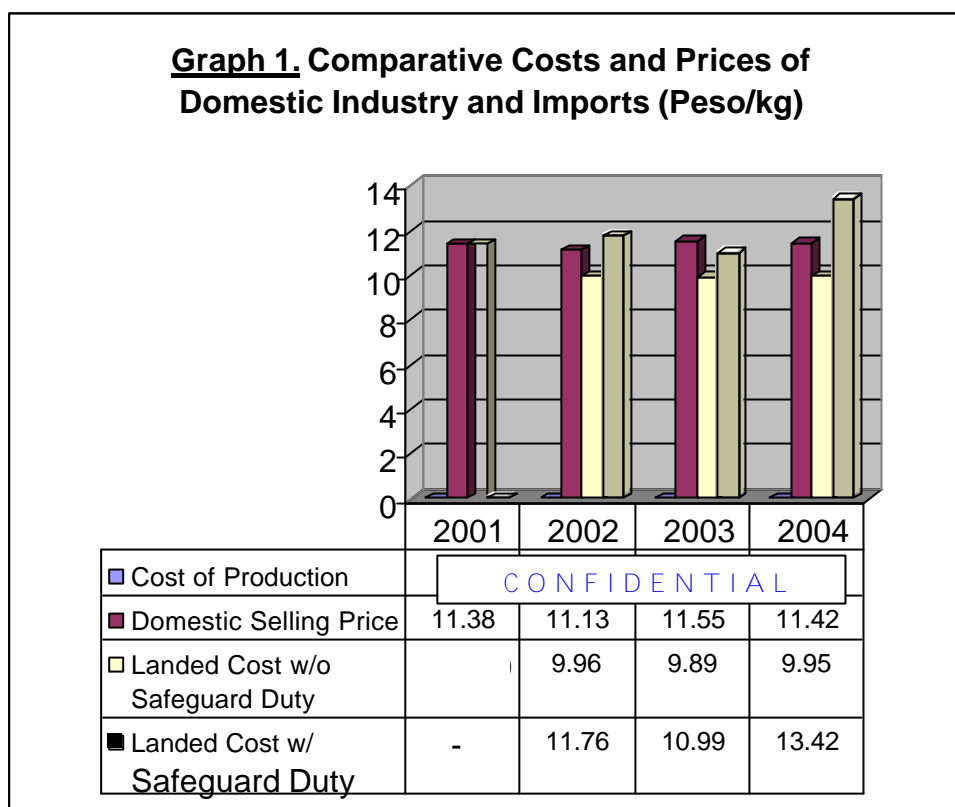
Although the safeguard measure is effective, it is not sufficient to remove the threat of increased imports that can cause serious injury. During the relief period, cheap imports continued to enter the Philippine market as world export prices of ceramic tiles continue with its downward trend. Imports from countries in the *de minimis* list came in increased quantities and at low prices.

The ease in shifting of import source indicates that tiles are substitutable and import patterns are sensitive to price changes. These imports had driven down the prices of ceramic tiles in the Philippine market. In order to protect market share, the domestic industry continued to apply a pricing policy of import parity. The industry maintained its 2001 prices barely enough to recover cost to produce and sell. Consequently, the industry continued to incur losses from operations despite improvements in production and sales. Thus, the full benefit of the relief for the domestic industry was not maximized.

Had applicant companies not maintained its price at 2001 levels, market share would have been lost. Production, sales, employment, capacity utilization, productivity and profitability would revert to levels approximating the conditions during the period of imports surge when the industry was suffering serious injury.

Without the safeguard duty, there is a price advantage of imported ceramic tiles despite the cost improvements made by the domestic industry. To illustrate, in 2003, the landed cost of imports without safeguard duty is lower than the domestic selling price (Graph 1). The same is true for the first semester of 2004. If the safeguard duty is not extended, the local industry's efforts to be competitive will be put at risk and threaten their business recovery.

Non-extension of the safeguard action will likely lead to increase in significant quantity of low-priced imports which will be the dominant cause again of significant impairment on the overall market position, production and sales, capacity utilization, employment, productivity and profitability of the domestic industry.



8.3 Foreign Industry Developments

There is need to determine whether there is sufficient freely disposable, or an imminent, substantial increase in production capacity of foreign exporters including access conditions they face in third country markets, indicating likelihood of substantially increased exports to the Philippines that justifies extending the general safeguard measure given to the domestic industry pursuant to RA 8800.

8.3.1 Asia

After the financial crisis of the late 1990s, Southeast Asian countries are increasing their capacity utilization. In the case of Indonesia, enormous investments were made in new plants in 1997-1998, but these were never commissioned due to the financial crisis. Following the economic recovery, very high levels of production have now been reached.²²

World production and consumption of ceramic tiles rose yet again in 2002. These increases were attributable to Asian countries. During 2002, ceramic tile production worldwide totaled 5.904M sq. m., 10.4% up from 2001. The increase is almost entirely attributable to Asian countries (China, India, Iran, and Vietnam) and Brazil.²³

²² Ceramic World Review, n. 48/2002.

²³ Ceramic World Review, n.53/2003

The Southeast Asian countries (principally Indonesia, Malaysia and Thailand) have finally emerged from the 1997-1998 crisis and resumed growth. They are making available ever larger quantities for exports, both in nearby markets and the United States. Vietnam continues its strong growth producing over 100M sq. m for the first time. India continues its growth with an increase in production from 109M sq. m. to 150M sq. m. to feed its constantly expanding domestic market.²⁴

8.3.2 China

In the rankings of exporting countries, China has risen from 10th place in 2000 to 4th place in 2001 (after Italy, Spain and Turkey) pushing ahead of countries such as Brazil and Mexico. China exports 53M sq. m. and imports no more than 7M sq.m.²⁵

The export volume of Chinese ceramic tiles accounted for about 15% and 7.5% of total world trade volume and export value in 2003, respectively. About 80% of China's export of ceramic tiles was destined to the Asian region. The top ten country destinations were Hong Kong, Saudi Arabia, S. Korea, Singapore, Malaysia, UAE, Nigeria, Kuwait, USA, and the Philippines.²⁶

AsianCeramics cited that China's ceramic industry is faced with anti-dumping pressure from other countries because of its sustained export growth. It is likely that anti-dumping cases may be initiated against China by its neighbors and Italy.

8.3.3 Vietnam

Vietnam is the third largest producer of ceramic tile in the Far East, after China and Indonesia. The development of Vietnam's ceramic industry has been phenomenal. For 2003, production is estimated to reach 120 M sq. m. Since its relaunch in 1994, Vietnam has concentrated mainly on glazed floor tiles. Wall tile production is still limited, split almost evenly between single fired and double fired tiles.²⁷

Vietnam's brick and tile makers are striving to boost exports of tiles in a bid to reduce a huge inventory and support its price, which has by now dropped by 20% in the domestic market. Vietnam Construction Ceramics Producer Association (VCPA) estimated that for it to be profitable, tile exports should be at least 20-30 percent of total annual output. Export earning of these producers reached only over US\$3 million in 2002 (1.3 percent of their total output value), due to the flood of cheaper Chinese tiles and oversupply.²⁸

²⁴ Ibid

²⁵ Ceramic World Review, n.48,2002

²⁶ www.AsianCeramics.com

²⁷ "Vietnam, The emerging Ceramic Industry", <http://www.ceramicandmore.com/news/> (Source: www.ceramicworldweb.it and "Ceramic World Review (26/05/2003)

²⁸ <http://www.vnagency.com.vn/Econet/English/VE2502003.htm>

Ceramic Tiles Company No.1 plans to export 24,000 sq. m. of ceramic tiles worth US\$ 72,000 to Thailand and the Philippines. Vietnamese tiles have secured a foothold in these markets due to high quality and diversified models. The company exports 24,000 – 25,000 sq. m of ceramic tiles every month.²⁹

8.3.4 Findings

Many exporting countries in the Asian region, especially China, continue to increase their production capacities to tap the export market. Many of these ceramic tiles are intended for export to countries within the region, including the Philippines. Imports of ceramic tiles are expected to continue at cheap prices.

The possibility of cheap ceramic tiles flooding the domestic market is very likely once the safeguard measure is discontinued. Import prices without safeguard duty would be lower than domestic selling prices which are not at levels to allow full recovery of the local industry (Graph 1). Termination of safeguard action would negate the positive effects gained by the domestic industry's efforts to adjust to import competition.

A repeat of the serious injury suffered by the industry prior to the imposition of safeguard duty in 2002 is imminent if it is not given enough time to complete its adjustment plan.

²⁹ <http://www.vn-style.com/news/business/>

9 EFFORTS OF THE INDUSTRY TO ADJUST TO IMPORT COMPETITION

Sec. 19 of RA 8800 provides that subject to the review under Sec. 16, extension of the measure may be requested by the petitioner if the action continues to be necessary to prevent or remedy the serious injury and *there is evidence that the domestic industry is making positive adjustment to import competition.*

In case one or more firms of the benefiting industry which applied for safeguard measure failed to comply with their commitments as reflected in the approved adjustment plan, the safeguard measure shall continue to be in effect, provided however, that the firms which complied with their commitments constitute the majority in accordance with the definition of the domestic industry under Section 4 of paragraph (f) of RA 8800.³⁰

9.1 Adjustment Plans (2002-2004)

In summary, the adjustment plans submitted in 2002 by Mariwasa and Lepanto Ceramics contained the following:³¹

Mariwasa

- Provide better products through introduction of new product series every year;
- Provide wider coverage by improving distribution network;
- Work on producing at higher efficiencies by reducing power, energy and labor costs; and
- Work for the reduction of tariffs on inputs not locally produced.

Lepanto Ceramics, Inc.

- Increase in production volume;
- To become cost competitive through improvement in yield, reduction in fuel and energy costs, organizational restructuring and efficient management of working capital;
- Improve product quality and service by means of offering a complete range; and
- Develop a well-managed local and export distribution network.

³⁰ TC Manual on Safeguards Investigation, p. 11b.

³¹ Formal Investigation Report (SG No. 2001-02), p. 13.

9.2 Specific Efforts of the Domestic Industry

Mariwasa's efforts to adjust to import competition:

- Ninety (90) new designs were developed and introduced from January 2002 to June 2004. Kilns from its old factory in Pasig City were transferred to Batangas plant beginning 2002.
- Seventeen (17) new distributors, meeting the financial and management criteria, were appointed between January 2002 and June 2004.
- The fuel consumption targeted reduction was not met due to technical experiments. It is banking on the completion of the natural gas distribution pipeline that is expected to be in operation by 2007.
- Pending completion of the natural gas pipeline from Malampaya, supply of LPG to the plant was bid out to get more competitive rates from oil industry players.
- To reduce electricity cost, a power plant was installed to reduce its dependence on power from Meralco.³² Operation commenced in the last quarter of 2003. This resulted to substantial reduction in power cost beginning the last quarter of 2003. Power cost per kwh in 2004 was reduced by 30% from 2003.
- Sourcing of cheaper raw materials to reduce its rising raw materials cost. Cost of local raw material per kg was reduced by 48% in 2004 from 2001.

In the case of Lepanto:

- Although it has not met its production target, total production in 2002 increased by 126% when compared to 2001.
- Lepanto shelved its plan to sustain an export base following a decision to stop the production of unglazed (granito) tiles. This decision was made because of the high cost of production of granito tiles.
- The focus is on middle- to high-end market. The Value tile series intended to compete with imports from Asian countries is being phased out in favor of higher grade and better margin yielding design. Production is limited to the common standard sizes.
- In terms of cost competitiveness, rejects were brought down from 10% to 6% and the water content of the slip prior to spray drying was reduced and maintained at 6%.

³² Mariwasa Siam entered into a capital lease agreement amounting to ₱130M with option to purchase the power plant at the end of the lease period at its residual value (Note 19 to financial statements (2002-2003)).

- With regard to working capital management, targets were not met except for finished goods inventory indicating that their sales picked up after increasing production.
- Local distributors were classified into three (3) groups depending on their monthly sales commitment that determine pricing and discounting packages.
- With a better product mix, the average selling price improved.
- A new management team was put in place to run the operations of the plant.

9.3 Findings

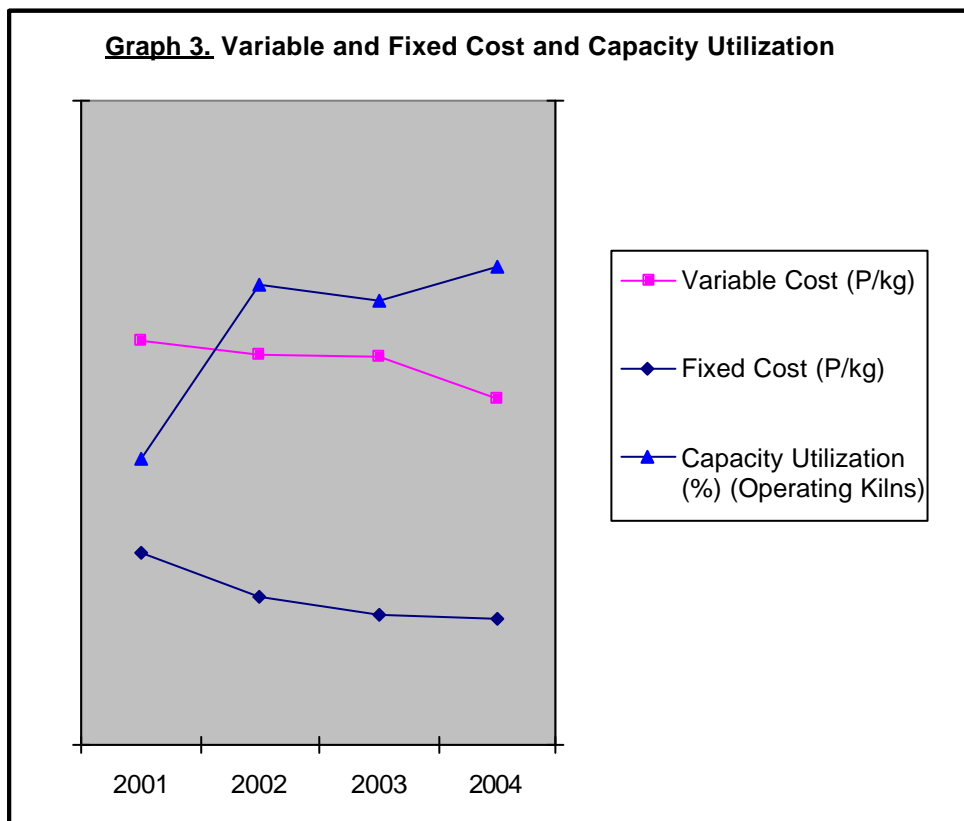
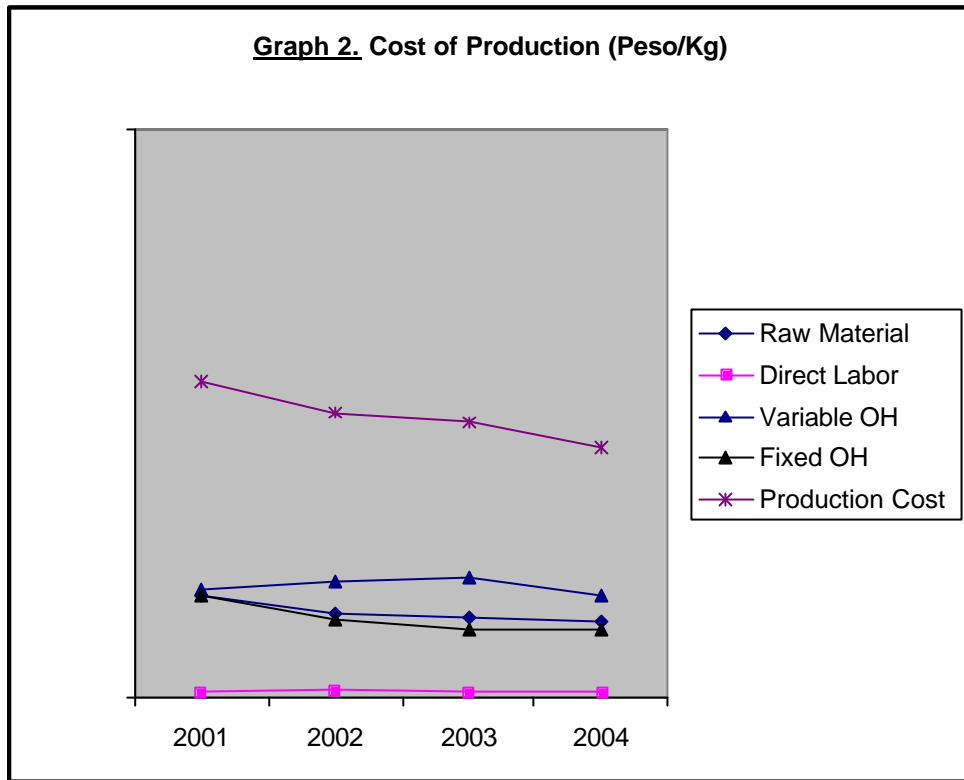
Both applicant firms made efforts to adjust to import competition. The Monitoring Report to the Secretary in November 2003 noted that Mariwasa has fared better in complying with its adjustment plan than Lepanto. Mariwasa is projected that, with the completion of the natural gas pipelines, it will be profitable in the next few years.

Mariwasa's lower production cost is mainly due to its installation of generating sets in 2003.

On the other hand, Lepanto's efforts to adjust to import competition deviated from its original plan in view of their management's decision to stop production of granito tiles. The significant increase in its production volume immediately after the imposition of safeguard measure and the significant reduction of its loss from operations is noted.

The changes made by Lepanto in its adjustment plan appear to be in line with Mariwasa's own plan that currently targeted the domestic market. Both firms moved production lines away from the cheaper low-end tiles that flooded the market during the import surge. Both firms favor production of the middle- to higher-end tiles that provide better margins.

Despite the increasing cost of imported raw materials, power and fuel, the applicants were able to reduce the unit costs of production of ceramic tiles by 21% in 2004 from 2001 level partly as a result of the economies of scale arising from higher capacity utilization combined with efforts of both companies to minimize costs (Graphs 2 and 3).



10 CONCLUSION

The Commission concludes that, in accordance with RA 8800 and the WTO Agreement on Safeguards:

1. The collective output of the two (2) applicant companies constitutes a major proportion of the total domestic production of ceramic tiles. The domestic industry made serious efforts to comply with its adjustment plan and there is evidence that the industry is making positive adjustment to import competition.
2. The current safeguard measure is effective. The volume of imports returned to pre-surge level. The domestic industry saw improvement in its production; sales; market shares; productivity; capacity utilization and employment.
3. Although the safeguard measure is effective, it is not sufficient to remove the threat of serious injury. The shift of import sourcing to countries in the *de minimis* list indicates that tiles are substitutable and sourcing patterns are sensitive to price changes. Generally, export prices from these countries (i.e., *de minimis*) were at a low level to the point that the domestic industry is forced to maintain their 2001 prices (import parity pricing) to protect market share. Consequently, the industry continued to incur losses despite improvements in sales. The full extent of the relief provided to the domestic industry was not maximized.
4. Without a safeguard duty, domestic selling prices will fall below levels not enough to recover cost to produce and sell. There is a substantial threat of serious injury if safeguard duty is not extended.
5. Many exporting countries in the Asian region, especially China, continue to increase their production capacities to tap the export market. These ceramic tiles are intended for export to countries mainly within the region, including the Philippines indicating the likelihood of substantially increased exports to the Philippines and that, unless safeguard action is extended, serious injury can occur.
6. Without the extension of the safeguard measure, the positive gains made by the domestic industry will be negated as it still needs time to fully put in place its adjustment plan to effectively face import competition.
7. Non-extension of the safeguard measure will likely lead to imports coming in at increased quantities which will be the dominant cause of serious injury to the domestic industry.

11 RECOMMENDATION

This investigation finds that the domestic industry will not be able to compete with imported tiles if the safeguard action is terminated now.

With the increasing capacity of ceramic tile producers in the Asian region, there is imminent threat that imported tiles will enter the domestic market in increased quantities if the safeguard action is not extended.

The expected completion within 3 years of the natural gas distribution pipelines from Batangas to Manila, together with the continuing program to reduce costs, will provide the favorable environment to make the industry competitive against imports.

In view of the foregoing, the Commission recommends that the action be extended for three (3) years - the timeframe needed by the industry to fully implement its adjustment plan and be competitive against imports.

Should the recommendation be adopted:

- The notification and consultation requirements of Article 12 of the WTO Safeguard Agreement and Rule 17 of the IRRs to RA 8800 shall be complied with.
 - Imports originating from ASEAN Member States shall be governed by the provisions of Articles 6 and 8 of the Agreement on the CEPT Scheme.
 - Imports originating from countries not identified in the Order of the Secretary dated 05 September 2003 as *de minimis*, shall continue to be imposed the safeguard duty.
 - Imports originating from Japan and the Member States of the European Union, however, are excluded from the imposition of safeguard duty as provided in the 11 April 2002 Decision of the Secretary.
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12 DEFINITIVE MEASURE

Section 13 of RA 8800 provides that *“upon its positive determination, the Commission shall recommend to the Secretary an appropriate definitive measure, in the form of:*

1. *An increase in, or imposition of, any duty on the imported product;*
2. *A decrease in or the imposition of a tariff-rate quota (MAV) on the product;*
3. *A modification or imposition of any quantitative restriction on the importation of the product into the Philippines;*
4. *One or more appropriate adjustment measures, including the provision of trade adjustment assistance;*
5. *Any combination of actions described in subparagraphs (a) to (e).*

The WTO Agreement on Safeguards provides that *“a measure extended under paragraph 2 shall not be more restrictive than it was at the end of the initial period and should continue to be liberalized.”*

Section 15 (3) of RA 8800 provides that *“an action described in Section 13(a), (b), or (c) that has an effective period of more than one (1) year will be phased down at regular intervals within the period in which the action is in effect”.*

12.1 Recommended Definitive Safeguard Measure

The WTO Agreement on Safeguards and the domestic law contain provisions as to the reckoning of the extended measure and the intervals of its phase down. Rule 13.1.c of the IRR to RA 8800 further provides that *“the general safeguard measure shall be limited to the extent of redressing or preventing the injury and to facilitate adjustment by the domestic industry from the adverse effects directly attributed to the increased imports.”*

However, the Agreement and the IRR to RA 8800 do not specifically provide how the measure is progressively liberalized.

It may be mentioned that in the United States' International Trade Commission (USITC) investigation on extension of safeguard action against imports of wheat gluten, its recommendation was to extend the quota for 2 years with the rate of increase the same as during the first 3 years.³³

In the original investigation, the Secretary ordered the imposition of an additional specific duty for a period of three (3) years that was progressively liberalized each year. The linear rate of reduction of the specific duty was 20%.

The Commission recommends to the Secretary that the measure shall continue to be liberalized following the linear reduction applied in the first three years of the safeguard action. Thus, the recommended definitive safeguard duty

³³ Inv. No. TA-204-4, USITC Publication No. 3407, April 2001.

shall be in the amount of ₱2.80/kg for the first year; ₱2.25/kg for the second year; and ₱1.80/kg for the third year.

The extension will allow the industry to adjust fully to import competition and thus help prepare it for the time when the action terminates.

12.2 Review of Definitive Measures

Rule 15.6 of the IRRs to RA 8800 provides that: *“The decision imposing general safeguard measure, the duration of which is more than one (1) year, shall be reviewed at regular intervals for purposes of liberalizing or reducing its intensity. The industry benefiting from the application of a general safeguard measure shall be required to show positive adjustment within the allowable period. A general safeguard measure shall be terminated where the benefiting industry fails to show any improvement, as may be determined by the Secretary.*

Rule 16.1 of the same IRR to RA 8800 provides that: *“So long as any action taken under Rule 13 remains in effect, the Commission shall monitor developments with respect to the domestic industry, including the progress and specific efforts made by workers and firms in the domestic industry to make a positive adjustment to import competition.”*

13 EFFECTS OF THE AFFIRMATIVE RECOMMENDATION

Section 14 of RA 8800 provides that: *“The report (of the Commission) shall include a description of the short and long-term effects of the affirmative or negative recommendation, as the case may be, on the applicant, the domestic industries, the consumers, the workers, and the communities where production facilities of such industry are located.”*

The likely impact of the Commission’s affirmative recommendation is discussed below:

13.1 On Competition

- Although consumer welfare is prejudiced because of higher prices, users retain the option to choose between local and imported tiles as there are no quantitative restraints on imports; and
- As the proposed measure is only temporary and will progressively be liberalized, competition will return to its normal level.

13.2 On the Domestic Industry

- Imports will be maintained at their pre-surge level;
- Additional time will be provided to the domestic industry to complete their adjustment plan to positively adjust to import competition by putting in place efficiency measures that will allow it to attain competitiveness *vis-à-vis* imports;
- Increase in output will create conditions to further reduce the cost of production;
- Reasonable margins will be generated as a consequence of reducing operating losses;
- Market share regained will be maintained enabling the industry to take part in the growth of the market;
- Increases in market share allow introduction of new models as the market grows; and
- With the availability of natural gas in 2007, the potential energy savings of using natural gas is estimated at 40% of gas fuel.

13.3 User Industries and Consumer Welfare

- Given the competition among domestic producers of ceramic tiles, the market is a buyers’ market. Any unreasonable price increases are thus unlikely, unless, there are supply shocks;
- With the continued existence of a viable domestic industry, consumers are assured of on-time delivery of volume orders, after-sales services in replacements of breakages and defects, and allow small lot orders;
- Credit line is extended by local industry to buyers; and

- Presence of local products mitigates foreign exchange risk because transaction is done in peso.

13.4 On Employment

- The expected continued increase in output and sales would ensure the tenure of additional employment not only in manufacturing but also the related sales and distribution services.

13.5 On Regional Development

- Ceramic tile production facilities are located in towns near Metro Manila. The imposition of the definitive safeguard measure will ensure continuous operation of the domestic producers. This will bring continuing community development to areas where these manufacturers are located.
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The Commission, after submitting the report to the Secretary of Trade and Industry, shall make it available to the public except for confidential information and publish a summary in two (2) newspapers of general circulation.

20 October 2004

EDGARDO B. ABON
Chairman

Commissioner

GEORGE N. MANZANO
Commissioner