

GENERAL AGREEMENT ON TARIFFS AND TRADE

RESTRICTED

BOF/R/28

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Limited Distribution

REPORT ON THE CONSULTATION UNDER ARTICLE XII:4(b) WITH FINLAND

1. In accordance with its terms of reference, the Committee has conducted the consultation with Finland under Article XII:4(b). The Committee had before it a basic document for the consultation (BOF/86), and documentation supplied by the International Monetary Fund.
2. In conducting the consultation the Committee followed the plan for such consultations recommended by the CONTRACTING PARTIES (BISD, Seventh Supplement, pages 97-98). The consultation was completed on 4 November 1968. This report summarizes the main points of the discussions.

Consultation with the International Monetary Fund

3. Pursuant to the provisions of Article XV of the General Agreement, the CONTRACTING PARTIES had invited the International Monetary Fund to consult with them in connexion with this consultation with Finland. In accordance with the customary procedure the representative of the Fund was invited to make a statement supplementing the Fund's documentation concerning the position of Finland. The statement made was as follows:

"The Fund invites the attention of the CONTRACTING PARTIES to the Executive Board decision of June 28, 1968 taken at the conclusion of its most recent Article XIV consultation with Finland, and particularly to paragraphs 2, 3, 4, and 5 which read as follows:

12. Affected by restrictive domestic financial policies and by sluggish demand conditions in Western Europe, the gross domestic product rose, in real terms, by 2.3 per cent in 1967, approximately the same as a year earlier. Unemployment rose sharply, especially toward the end of the year. There was a slight decline in real gross fixed investment. The volume of exports of goods and services rose by 4.4 per cent, with all of the increase in commodity exports going to those countries with which Finland trades on a bilateral basis. The volume of imports of goods and services declined by 1 per cent. The deficit on the current account of the balance of payments was, thus, reduced from \$207 million in 1966 to \$163 million. At the same time there was an increase in long-term capital inflow. The heavy reserve losses of the preceding years were replaced by a decline of \$5 million in 1967, but this was accompanied by substantial use of Fund resources. In the first five months of 1968 reserves rose by \$115 million.

13. On October 12, 1967 the Finnish markka was devalued by 23.8 per cent and a special temporary tax was imposed on most exports. Government expenditure is being kept under strict control and it is estimated that the cash budget (including the proceeds of the export levy) will show a surplus in the calendar year 1968 of about Fmk 400 million compared with a deficit of about Fmk 100 million in 1967. In view of the withdrawal of liquidity resulting from the government surplus, monetary policy in 1968 aims at supplying additional liquidity to the economy on a selective basis. The budgetary restraint and the easing of monetary conditions in 1968 will facilitate the needed shift in resources. The Fund believes it important however that liquidity should be supplied to the economy in such a manner that monetary policy can play an effective role in offsetting deterioration in the budget accounts when the export levy is reduced in 1969.

14. The Government has placed particular emphasis on the need to moderate the growth of costs and prices. Agreement has been reached on (a) the elimination of the clause contained in the current wage agreement providing for index compensation at the end of 1968 and the limitation of increases in hourly wages in 1969 to a flat sum estimated to raise the wage bill by 3.5 per cent; (b) a smaller increase in agricultural prices in the crop year 1968/69 than provided for under current legislation. In April 1968 Parliament passed a Law to Safeguard Economic Progress in the years 1968/69 empowering the Government to control prices, rents, and wages and abolishing price index linkages in rent and wage agreements and most financial contracts. The Fund welcomes these measures which taken as a whole should facilitate further growth and strengthen the external payments position.

15. The Fund notes with satisfaction that Finland has continued to make progress in the liberalization of trade and payments notwithstanding the payments difficulties of recent years. Effective January 1, 1968, all quotas on industrial imports from countries in the multilateral area were eliminated. The exchange regulations concerning current invisibles and capital transactions were also substantially changed and liberalized. Moreover, the one remaining payments agreement with a Fund member was eliminated.

"Official reserves at the end of September 1968 amounted to \$326.9 million, \$122.9 million more than at the end of September 1967 but still below their level at the end of 1964. At \$326.9 million official reserves were equivalent to about 2½ months payments for imports in 1967

"At the present time, the general level of restrictions of Finland which are under reference does not go beyond the extent necessary to achieve a reasonable rate of increase in its reserves."

Opening statement by the representative of Finland

4. In his opening statement, the full text of which is contained in an annex, the representative of Finland described the major developments in Finland since the last consultation, beginning with a summary of transitional measures which followed the 1967 devaluation. With respect to the special export levy, which was one of those measures, he explained the way in which the proceeds of the tax were being used to promote basic investments in infra-structure. Turning to the problem of introducing an incomes policy which might help to place the economy on a sounder basis, he explained that after lengthy negotiations a comprehensive agreement had been reached on prices and incomes. As of March 1968, the index clauses which wage contracts had contained were removed, and from the beginning of 1969 wage increases were to be kept in line with expected increases in productivity. Implementation of these agreements involved abolishing other index linkages and introducing powers to supervise and control prices and rents as well as wages. The Stabilization Act, incorporating these and various other changes, would be effective until the beginning of 1970 and there was to be no automatic reintroduction of index clauses at that time. Conceding that it might be too early to judge the overall effects of the devaluation and stabilization effort, the representative of Finland noted that price developments had become much more stable. Less encouraging had been the development of production, employment and private consumption expenditure. The Government was obliged under the stabilization agreement not to introduce tax increases and to hold borrowing to its previous level, but increased private investment was expected to have favourable effects on production; with good export prospects, the Government hoped that growth would soon be resumed. Turning to the balance-of-payments situation, the Committee was told of the encouraging development of Finland's current account, which may show a small surplus for the first time in ten years owing in part to expanded earnings from exports accompanied by a low level of imports. In the capital account, net long-term capital imports in the first half of 1968 amounted to Fmk 170 million, mainly in the form of medium-term financial loans. Short-term commercial credits had increased substantially after the rule requiring cash payment for certain imports was abolished. The position with respect to foreign-exchange reserves had greatly improved, largely reflecting the short-term capital inflow. Some continuing capital inflow was expected, but no more than enough to cover amortization of current debt and repayment of drawings which Finland had made from the IMF. Liberalization of foreign trade had proceeded; meantime, with two fifths of Finland's Kennedy Round concessions in tariffs becoming effective on 1 July 1968 and abolition of duties on EFTA goods on the "déséquilibre" list from the beginning of the year. Remaining quantitative restrictions on industrial products permitted under the EFTA Agreement had been removed and the liberalization extended to all countries under the multilateral import treatment system. Certain quantitative restrictions which had been the subject of Kennedy Round negotiations were also removed on 1 July 1968 and Finland's last bilateral trade and payments agreement with a convertible currency country had been terminated on 1 January 1968. Finland was far from complacent about the balance-of-payments outlook as reserves were still uncomfortably low, and it was felt that much of the gain achieved in reserves had been at the expense

of increased commercial debt which could not be a continuing source of gain. The fact that there had been depressed conditions within the country had undoubtedly helped to build reserves by holding imports down, but this was also a condition which could not continue. Hence, Finland would need to proceed with care, continuing to work on development of her incomes policy, but it was evident that a change in present import policies would not help but only jeopardize the attainment of the objective.

Balance-of-payments position and prospects and alternative measures to restore equilibrium

5. Members of the Committee congratulated the representative of Finland not only for his concise and informative statement on developments in his country over the past year but also for the very substantial improvement in Finland's situation due in no small measure to the courage of the Government in pursuing difficult but beneficial policies. It was especially gratifying that Finland had weathered this crisis without resorting to import policies which could in the long run only have delayed recovery. As it was, the current account surplus now in view was but one evidence of a basically healthy economy well on its way to recovery. They did, however, express some scepticism as to whether the Government of Finland might not now be under-estimating the strength of the country's situation and inquired whether the long-term foreign capital inflow might not be encouraged in some way. It was asked in particular whether thought was being given to various methods by which encouragement might be given to long-term investment from abroad, either on a loan basis or as direct investment, and whether any flotations in the United States market for capital were contemplated.

6. The representative of Finland drew attention to his statement that the expected equilibrium or surplus on current account was not something which Finland could count on as a continuing feature. Even the increase in foreign exchange reserves to which the Fund had referred in its decision would appear smaller if account were taken of the net debt of commercial banks. Net reserves, including such debt, amounted to no more than \$220 million instead of the \$327 million held by the central bank. Even this smaller figure was, to be sure, double the amount held at the beginning of the year, but the largest part of the increase, perhaps over half, would be the result of the reversal in leads and lags, a one-time gain. The figure of \$170 million for net long-term capital imports in the first half of 1968 was somewhat above the 1967 figure and it was expected that the level of total borrowing might be matched next year, but requirements for amortization of debt would not leave much net increase. Exports were also expected to increase, but if the domestic economy resumed a reasonable rate of growth, imports would be larger with the result that little, if any, further gain in reserves would come from that source. Efforts were being made to make known to potential investors opportunities available in Finland, where foreign capital enjoyed all the benefits accorded to domestic capital, though no special incentives had been offered which might be regarded as favouring foreign over domestic capital. Opportunities to interest investors

in the United States were certainly being sought in this process, along with others.

7. Members also asked how Finland expected to continue to finance the modernization of the wood industry and the development of diversified manufacturing which were an essential part in the solution of Finland's problem of developing a more profitable export trade, once the funds now being collected through the export levy had been used up. Not long ago a report on Finnish problems had suggested that perhaps incentives might be needed to bring together the necessary capital, either from domestic or from foreign sources.

8. In reply, the representative of Finland confirmed that the export levy funds will be used equally for three purposes, i.e. one third for investments in State-owned companies and for investment expenditure of the State railways and the General Direction of Posts and Telegraphs; one third for the development of power production; and one third to increase the opportunities available to the special credit institutions for providing export credit, or investment credit, for small- and medium-sized industries, to grant loans to small-scale industry, and to carry out an intensified forest improvement programme. It followed that Finland would look to private investors to provide the bulk of the capital needs for private industrial development. To that end certain fiscal and financial reforms were under way, in order to stimulate capital formation and ease industrial investment which had, to some extent, been at a disadvantage under the previous system. The new law on the taxation of business income was to become effective on 1 January 1969.

9. Turning to Finland's fiscal and monetary policies, members of the Committee expressed the view that the recovery effected by Finland during the past year offered a striking example of the effectiveness of conservative remedies. The restraint of demand through devaluation had effectively curbed imports; fiscal policies, including the temporary export tax, the restrictions on spending and selective credit policies had induced price stability, and this effect had been given some prospect of continuity by the abolition of linkages, so that gradually one could see business confidence increasing. These strong measures did, however, perhaps pose a problem for the future in the sense that they had involved fairly extensive governmental control of the economy; consequently it would be of interest to hear what thought Finland might be giving to a next stage in which controls could be eased somewhat.

10. The representative of Finland agreed that the trade balance had indeed improved, although he emphasized that this had been at the cost, mainly, of a shift in leads and lags of payments, so that the foreign debt had increased in the process. Still, long-term capital had also begun to be more readily available and this was important since the difficulties had been to a large extent associated with insufficient information provided to investors. The sacrifices which the country had made in terms of slow growth were, moreover, very real, and it was by no means certain that the balance-of-payments problems had been overcome in any permanent sense. The question as to how long it might be before the internal controls on prices and rents might be lifted went, he

said, to the heart of the matter, as the key question was how long it would take to create confidence. There was need for more confidence both internally and externally, as well between government and interested organizations as between Finland and her trade partners. Inside Finland it was understood that at the end of 1969, when the current law expired, there would be no need for a new law of its kind and the importance of avoiding the kind of threat which its continuance would present was well understood. The Government was, however, optimistic and hoped that the wage negotiations at the end of the next year would go well.

System and methods of the restrictions and effects of the restrictions

11. Members of the Committee commended the Government of Finland on recent actions in its programme of trade liberalization, especially the elimination of quota restrictions on all but a few industrial products and the elimination of the last bilateral trade and payments agreement with a non-Socialist country, both as of 1 January 1968. They expressed the hope that, in the light of Finland's improved balance-of-payments position, the remaining industrial and agricultural products still subject to global quotas or discretionary licensing would be liberalized. In this connexion, they requested clarification of action taken by Finland on 1 July 1968, liberalizing trade in the agricultural products listed in Annex III to BOP/86; they enquired whether any of the agricultural products on this list were still subject to global quotas and to discretionary licensing.

12. The representative of Finland confirmed that all the items mentioned in Annex III of BOP/86 had effectively been liberalized in the sense that they are free of licensing; they were thus not included in the global quota programme. The situation as far as the other agricultural products were concerned was clarified in the 1968 publication, "Import System of Finland".

13. Other more specific questions and comments were also made with respect to certain items which appeared still to be under restriction. The representative of Canada stated that nearly all Canadian exports to Finland are now liberalized but that there seemed still to be seasonal restrictions on canned salmon which Canada hoped might be removed. This product had recently been restricted from 1 to 31 January, throughout the month of June and from 1 October through 15 November, and reports reaching the Canadian Government indicated that it was difficult to obtain licences for import at these times, although there was no discrimination, except perhaps with respect to certain border trade. Canada would be interested to learn whether this restriction was justified on balance-of-payments grounds and how long it might be expected to continue.

14. The representative of Australia referred to the problem of non-liberalization of apples during the month of June, even though pears were liberalized at that time, and requested the removal of quota restrictions during that month. He also drew attention to the difficulty posed for distant suppliers by Finland's practice of issuing import licences for short periods of time with insufficient advance notice to permit participation in the

trade by Australian suppliers, and requested the provision of a longer period of notice for the issue of such licences. With respect to apples the question was also asked what was the specific amount of apples licensed in the month of June.

15. The representative of the United States expressed his concern that Finland continued to maintain quotas and licensing requirements on agricultural products, and raised a question concerning imports of canned fruit and juices, which had reportedly been licensed less liberally in 1968 than in past years. He said that he understood that total imports licensed in these categories were valued at Fmk 7.5 million in 1967, whereas so far in 1968 individual licences with a total value of Fmk 5 million had reportedly been issued. The reduced volume of licensing had been attributed to the tight foreign exchange situation in Finland but this situation seemed to have eased. Hence he would appreciate knowing whether the Government of Finland intended to liberalize imports of fresh, canned, and frozen fruit, fruit juices and vegetables for the rest of 1968.

16. On most of these questions the representative of Finland promised to look into the matter and see that replies were made to the countries in question. He believed that increasing consideration was being given to the distant suppliers in the issuance of licences. On the amount of licences issued for fruits and fruit juices he knew of no overall policy decision of the kind suggested but promised to communicate this concern to his Government.

17. Members of the Committee then expressed their special concern with respect to the question of the Finnish motor vehicle tax which they considered to be very heavy and is weighted so as to discourage the purchase of medium- and higher-priced automobiles. On a vehicle from overseas, whose c.i.f. cost was \$2,500, the total customs and tax burden amounted to 173 per cent, while on a vehicle whose c.i.f. value is \$1,000, the total customs and tax burden was only 133 per cent. Some members noted that this tax had had an increasingly severe effect upon sales of North American automobiles, notwithstanding the fact that the matter had been raised at every balance-of-payments consultation since 1963. They were very disappointed that their past persistent and determined efforts to seek the elimination of the discriminatory impact of this tax had brought forth no satisfactory response from the Government of Finland. They enquired whether now that Finland's balance-of-payments position has improved substantially, the Government would reduce the tax and take steps to eliminate its inordinate impact on medium- and high-priced motor vehicles by the elimination of the Fmk 2,500 reduction.

18. The representative of Finland acknowledged that this tax had caused certain countries to express dissatisfaction. He noted that in eight months of 1968, imports of automobiles from Finland's multilateral trade partners had declined by 18 per cent but that the decline in imports from bilateral partners had been even more marked, amounting to 46 per cent. It was apparent that restriction of automotive imports had very important balance-of-payments implications, given the fact that this product had accounted for 4.5 per cent of all imports in 1966

and for 3.7 per cent in 1967. Even with a stiffer tax burden the percentage would still be between 3 and 3.5 per cent in 1968. The figures spoke for themselves concerning the need for some effective restraint on imports. So far as concerned the arrangement by which the tax bore more heavily on more expensive vehicles, this was a non-discriminatory provision of a fiscal nature applicable to imports from all sources. Between 1963 and 1967 the share of the market economy countries had increased from 87 to 93 per cent and the United States share had gone up from 1.9 to 2.4 per cent. Since then the new EFTA rates had begun to have their effect. As for a possible relaxation, the matter was kept under review but could not be separated from the overall balance-of-payments situation.

19. Members of the Committee also raised the question of the differential credit restrictions applicable to vehicles purchased from bilateral sources which gave them an advantage not enjoyed by vehicles originating in market-economy countries. They enquired specifically whether it was still a matter of balance-of-payments policy that this preference should continue to be extended and asked that it be eliminated.

20. The representative of Finland replied that he could give no indication of any intent to comply with the request to eliminate this differential whose practical impact was considered to be limited and which had a definite relationship to Finland's balance-of-payments position and would continue to do so as long as uncertainty continued regarding the balance of payments.

21. The difficulty of selling alcoholic beverages to the Finnish State monopoly was also raised and it was suggested that the mark-up policy of the monopoly constituted a severe barrier to trade. The representative of Finland noted that this point had been raised in the non-tariff barrier context and suggested that it might better be pursued in that forum.

General

22. Members of the Committee thanked the representative of Finland for the presentation which he had made to them of a marked improvement in his country's position; in their view this had been the fruit of well-conceived policies well-executed. They commended Finland for progress in trade liberalization and urged that in the light of Finland's improved balance-of-payments position, the remaining industrial and agricultural products still subject to global quotas or discretionary licensing be further liberalized.

Annex

OPENING STATEMENT BY THE REPRESENTATIVE OF FINLAND

1. When we met here a year ago growth of production had almost ceased in Finland and unemployment had reached disquieting dimensions. The balance of payments was showing a persistent deficit and the foreign exchange reserves had decreased to a point which was arousing much concern. It was evident that the Finnish economy was in that state of fundamental disequilibrium, which according to the articles of agreement of the International Monetary Fund, justifies a devaluation of the currency unit. As you will recall it was decided, with the concurrence of the Fund, to reduce the gold value of the Finnmark by 23.8 per cent, with effect from 12 October.

2. The most immediate aim of the devaluation was to reduce the deficit in the balance of payments, which had forced the Government and the Central Bank to pursue restrictive fiscal and monetary policies since 1965. At the same time devaluation represented an attempt to provide scope for a new growth and development policy and for the structural changes necessitated by increasing international competition.

Developments since devaluation

3. It was understood from the very beginning, that in order to achieve the aims of the devaluation and to safeguard its success other measures were also necessary, above all to stabilize prices and wages and thus check inflation. The prevailing situation was rather unfavourable in this respect for the collective wage agreements in force, as well as various financial and other agreements and contracts, had index linkages, which seemed likely to cause a dangerous cost spiral as a result of the inevitable rise in prices following the devaluation.

4. Some of the measures which were taken at the same time as the devaluation were discussed during these consultations a year ago, soon after the event. These measures comprised the temporary Export Levy Act, a partial price regulation and the decision to discontinue the requirement of cash payment for certain imports and to abolish duties on commodities on the so-called "décalage" list of the FINEFTA Agreement. In addition, from the beginning of the year, the travellers' right to purchase foreign exchange was raised to Fmk 1,000 per person per trip regardless of the country of destination (earlier the limit was Fmk 400 for trips within Scandinavia and Fmk 800 to other countries).

5. The purpose of the temporary export levy was to sterilize part of the sudden increase in income from exports and thus to restrain increases in costs. It was decided to use funds thus accruing for basic investments indispensable for the promotion of structural changes in the economy. The export levy, originally 14 per cent, has been reduced both generally and for certain specified commodities, especially those with a high import content. Since 30 August 1968 the highest export levy percentage has been 8 per cent and the average 6 per cent.

6. By 23 October Fmk 459 million had accrued on the special export levy account at the Bank of Finland. Of this amount Fmk 121 million had been used for investment purposes as specified in the Act. According to a 1969 budget proposal of the Government, which was submitted to Parliament at the beginning of October, the total amount to be collected through the export levy is Fmk 650 million.

7. The most important of the necessary measures and the hardest to attain was, however, the institution of an incomes policy through which the impending cost inflation could be avoided. Extensive incomes policy negotiations were thus inaugurated soon after the devaluation.

8. After a series of lengthy negotiations a comprehensive agreement on prices and incomes was drawn up and approved at the end of March by the various organizations concerned. This agreement can, with good reason be regarded as a very significant milestone in a Finnish incomes policy.

9. The wage increases to be effected in 1968 were not tackled in the agreement. However, the index clauses in the contracts in force at that time, which provided for an upward adjustment of wages at the end of 1968, were removed. It was, moreover, decided that wage increases in 1969 should be kept in line with the expected increase in productivity. At the beginning of 1969 wages will consequently be raised by 16 pennia per hour throughout, which roughly equals a 3.5 per cent average increase in wages. As regards the prices of agricultural produce, it was agreed that there should be a 2 per cent increase in June 1968.

10. In order to realize this agreement it was necessary that most of the other index linkages should also be abolished and that the Government be authorized to control prices, rents and wages. The Economic Special Powers Act, providing the Government with the extensive powers necessitated by the contract and required for the execution of the stabilization programme 1968-1969, was passed by a large majority in the Diet. The Act made the prices and incomes policy agreement binding on all pressure groups.

11. The main provisions of the above Act, also known as the Stabilization Act, are as follows: index clauses in all agreements based on changes in various price indices are - with few exceptions - abolished in so far as they affect the period after the enforcement of the Act. The index clause will not automatically be reintroduced in agreements after the expiration of the Act, i.e. at the beginning of 1970.
12. With respect to lending, it is forbidden to demand interest or other compensation in excess of that applied by publicly supervised banking and insurance institutions. The presently applied interest rates are on average 7.5-8.5 per cent with a maximum of 10 per cent. The banks may, however, impose 1 per cent additional interest until the index compensation payable on deposits has been covered. As regards index-tied deposits, made before the Act came into force, the index clause may continue to apply until the end of November 1968.
13. The Stabilization Act authorizes the Government to supervise and control fees, prices, rents and wages so that wage increases are kept within the limits laid down in the prices and incomes policy agreement. A National Council for Prices and Wages, which includes representatives from the various interested organizations was established by cabinet decision for that purpose.
14. It is perhaps still too early to try to judge to what extent the targets set have been achieved by the devaluation and consequent measures. Some observations may, however, be made. One of the most promising results is that the first round of price increases following on the devaluation has levelled off; the rise in the cost of living index for instance was only 1.4 per cent from April to September this year as against a rise of 7.1 per cent from September 1967 to April 1968. Moreover, the Finnish authorities are confident that the price level will also remain fairly stable in 1969. The agreement on price recommendations for pulpwood, made by the representative organizations of the private forest owners and the wood-processing industry, will contribute to this end. The agreement covers two consecutive felling seasons, and the recommended increases in stumpage prices are quite moderate.
15. In comparison with the favourable price developments, productive activity has been slow in gaining strength. Of the main demand components, private consumption expenditure has remained, in real terms, at roughly the same level as last year, whereas the volume of private investment was on the decline during the first half of 1968. Despite an improved performance in exports the real increase in total production will remain quite small, about 2 per cent in 1968 or the same as in 1966-1967. It is for this reason that the employment situation is so alarming, taking into consideration the seasonal variation as well. Thus, in winter 1967-1968 the rate of unemployment was close to 5 per cent and it seems likely that the situation this winter will be almost as difficult as that last year.

16. The Government's proposed budget for 1969 is in line with the stabilization agreement, according to which no tax increases were to be introduced and borrowing was limited to the preceding budget's fairly low total of Fmk 550 million. As a result of these budgetary limitations it has been necessary to sharply restrict growth in expenditure. However, appropriations for such essential purposes as the development of higher education and financing of residential building have been increased. An evaluation of the general economic effects of the budget shows it to be characterized generally by neutrality. Care has been taken to make provision for the recovery of private investment, e.g. through an easing of the financial markets. In addition it should be pointed out that the greater part of the export levies budgeted for 1968 will be available for use in 1969.

17. As regards the future prospects of productive activity, the Finnish authorities are fairly confident. Private investment activity is anticipated to become quite brisk in 1969 due to the improved liquidity position of the banks, increased profit expectations of enterprises and measures taken by the Bank of Finland and the Government to advance finance for residential and industrial construction. Also, commercial fellings are expected to expand considerably, mainly as a result of the agreement on stumpage prices. If the growth rate of exports continues to be as high as is expected - about 10 per cent in real terms - real gross national profit in 1969 could reach a level 6 per cent above that for this year.

Balance of payments

18. As stated above, the most immediate objective of the devaluation was of course to strengthen the external balance of the country and to create conditions conducive to a more permanent external equilibrium. In this sector the results have without doubt been more favourable than in domestic production.

19. The Finnish authorities are satisfied to observe that developments in the current account have so far corresponded quite closely to expectations. Thus it was foreseen last autumn that the improvement in the balance of trade would occur gradually after a certain time lag. By the end of September this year accumulated Finnish exports actually exceeded the value of imports for the first time in ten years. According to our estimates, however, and as indicated by the September trade figures, there will be an expansion of imports in the last quarter so that the end result will be approximate equilibrium in the trade balance for the year as a whole.

20. Net invisible earnings have also developed rather favourably in 1968 with the surplus almost doubling during the first half of the year compared to the corresponding period 1967. Improvements have occurred mainly on tourism and transportation accounts, while the net deficit in transfer payments increased as a result of higher debt servicing expenditure.

21. According to our forecasts, the year 1968 will show a small surplus on current account compared to a deficit of Fmk 490 million in 1967.

22. Moving to capital account, it may be observed that net long-term capital imports during the first half of 1968 amounted to Fmk 170 million; the bulk of borrowing abroad consisted of medium-term financial loans. Short-term commercial credits increased substantially (by some Fmk 450 million) during the first half of the year. This resulted in the main from the abolition in January 1968 of the rule requiring cash payment for certain imports.

23. The foreign exchange reserves roughly doubled during the first nine months of the year largely reflecting the growth in the short-term capital inflow. In view of the expectation that the current account will remain in equilibrium, that projected long-term capital imports will no more than balance amortizations (including the voluntary repayment of the second credit tranche to the International Monetary Fund in July) and that the stock of short-term commercial credits had reached a "normal" level by mid-year, there seem to be hardly any changes in Finland's foreign exchange reserves during the latter part of 1968.

Trade policy

24. In her trade policy Finland has continued to promote the liberalization of foreign trade. As a result of the Kennedy Round negotiations, tariff reductions on tropical products and some other items of special interest to developing countries were put into effect at the beginning of this year.

The first two fifths of the general Kennedy Round reductions came into effect on 1 July 1968. In connexion with devaluation, it was also possible to unilaterally abolish, within the framework of the FINEFTA Agreement, duties on commodities on the so-called "décalage" list, as mentioned above.

25. As regards the elimination of quantitative import restrictions, at the beginning of the year Finland removed her remaining quantitative import restrictions on industrial products that had been permitted under the FINEFTA Agreement. This liberalization was extended to imports from all countries under the multilateral import treatment system. Furthermore, on 1 July 1968, Finland eliminated quantitative restrictions on the importation of certain products as agreed during the Kennedy Round negotiations. This measure of liberalization was also extended to cover imports from Finland's bilateral trade partners. The remaining global quota programme for 1968 consists of eleven such quotas as against twenty-one in 1967 and amounts to Fmk 104.4 million, while the corresponding figure for 1967 was Fmk 382.5 million. At the moment 95 per cent of imports from multilateral countries have been liberalized.

26. The bilateral trade and payments agreement between Finland and Colombia ceased to be effective from 1 January 1968. Presently, our foreign trade only with the Eastern European Socialist countries with the exception of Albania and Yugoslavia, and with Mainland China is maintained on a bilateral basis.

Conclusion

27. From the point of view of the balance of payments I think one could say that developments since the devaluation have been in line with our objectives. This has occurred notwithstanding the considerable liberalization of imports introduced at the beginning of the year and the further tariff reductions implemented in July in accordance with our commitments under the Kennedy Round agreement.

28. When evaluating our present position, Mr. Chairman, it is important to realize that Finland's gold and foreign exchange reserves are still below the levels achieved in the early 1960's and internationally speaking they are small in relation to our trade. Looking more closely into the reasons for the recent strengthening of our reserve position a number of elements can be distinguished. The change in domestic prices relative to those on world markets effected through the devaluation has, of course, worked in favour of our domestic suppliers. However, a major part of the increase in reserves resulted from a reversal of leads and lags of a short-term character. Due to rather favourable conditions recently on the international capital markets it has also proved possible to expand medium- and long-term capital imports to some extent and thereby add to our reserves. Unfortunately, a considerable part of the increase in our foreign exchange reserves is also due to the long recession in production and especially the decline in private investments.

29. Looking ahead into the 1970's it is obvious that our international margin for economic expansion will remain extremely narrow. Devaluation has not eliminated the structural weaknesses of the Finnish economy. Balanced growth will require a continuous improvement of the allocation mechanism and success in our endeavours to adapt Finland's industrial structure to the conditions of economic integration and international specialization. It is self-evident that, in addition, provision of an international margin sufficient from the point of view of growth policy, necessitates continuous development of our incomes policy. In this respect we are facing basically the same problems as before. In these circumstances, it is evident that any radical changes in our present import system would alter the foundation on which our policies for balanced growth have been built, and thereby jeopardize the attainment of our objectives.