

# GENERAL AGREEMENT ON TARIFFS AND TRADE

RESTRICTED

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## Committee on Balance-of-Payments Restrictions

### REPORT ON THE 1980 CONSULTATION WITH PORTUGAL

1. The Committee has consulted with Portugal in accordance with its terms of reference and the Declaration of the CONTRACTING PARTIES on Trade Measures Taken for Balance-of-Payments Purposes (L/4904). The consultation was held on 5 May 1980 under the chairmanship of Mr. C.S.F. Jagmetti (Switzerland). The International Monetary Fund was invited to participate in the consultation pursuant to Article XV of the General Agreement.

2. The Committee had the following documents before it:

- Report on the last consultation with Portugal held on 30 April 1979 (BOP/R/106)
- Basic document supplied by the Portuguese authorities (BOP/206 and Add.1)
- Background paper by the secretariat (BOP/W/39)
- Background material supplied by the IMF dated 2 April 1980

#### Opening statement by the representative of Portugal

3. In her opening statement, the full text of which is contained in the Annex, the representative of Portugal described the economic developments in the Portuguese economy in 1979, the trade liberalization measures taken since the last consultation, and the prospects and policies for 1980. She said that in 1979 the GDP had risen by about 3.4 per cent. The main stimulus to economic growth had been the remarkable 22 per cent rise in exports of goods and services. Imports of goods and services had only risen by 4.5 per cent in real terms. These developments reflected the improvement of Portugal's competitive position which was the consequence of low unit labour costs and "crawling peg" devaluations. An increase of 66.6 per cent in private transfers had further contributed to the improvement of the current account. For the first time since 1973 it had registered a surplus (over \$100 million according to the most recent estimates). There had also been a substantial increase in capital inflows and as a result the surplus in overall balance rose from \$160 million in 1978 to \$1.3 billion in 1979.

4. As a consequence of these positive developments Portugal had been able to continue to relax its restrictive import measures. The surcharge, which had been introduced in 1975 with a rate of 30 per cent had been reduced to 20 per cent in October 1978 and to 10 per cent in May 1979. Several items were lifted from the list of goods subject to the surcharge and, as a result, its coverage had dropped from 26 to 24 per cent of total imports. The quota system on consumer goods had been extended, but the removal of two items - coffee and plastic products - substantially reduced the coverage namely from 4.2 to 3.3 per cent of total imports in 1976 the year before the system had been introduced.

5. The Parliament had recently approved the Government's annual plan and budget which were based on the assumption that the GDP would grow by 3.6 per cent in 1980, private consumption by 1.5 per cent, public consumption by 0.5 per cent and productive investment by 6 per cent. The current account was expected to be in deficit (\$750 million) mainly due to a forecast 30 per cent increase in the trade deficit (\$800 million). In view of the sharp deterioration of the external financial position expected for 1980, the Government had considered it necessary to extend, until the end of the year, the 10 and the 60 per cent surcharges, to extend the quota system for consumer goods for a further twelve-month period to 31 March 1981 and to maintain the quota system for unassembled vehicles. The value of the quota system for consumer goods was about to be increased by about 15 per cent, which was estimated to compensate the increase in the average price of the goods subject to these restrictions. The escudo value of the quotas for unassembled vehicles had been increased by 36 per cent.

6. In concluding her statement the representative of Portugal declared that, given the outlook for 1980, the trade measures taken for balance-of-payments purposes had to be prorogated to safeguard Portugal's external accounts situation. She also stressed that the Portuguese authorities intended to continue to use these measures to a very small extent and to apply them only in a non-discriminatory manner.

#### Statement by the representative of the International Monetary Fund

7. Upon the invitation of the Committee, the representative of the International Monetary Fund made a statement in which he noted the further consolidation in 1979 of the success which the Portuguese authorities had achieved in reducing internal and external disequilibria in the economy, and in particular the marked improvement in the balance-of-payments position. He reviewed in some detail recent developments in the overall economic and financial conditions and policies adopted by the Portuguese authorities. The Fund representative described the outlook for 1980 as clouded by uncertainties regarding both the external environment and the stance of domestic financial policies. He referred to the concern of the Portuguese authorities about the impact of escudo depreciations on the domestic price level which had prompted a gradual shift in the focus of exchange rate policy

leading to a 6 per cent effective revaluation of the escudo in February 1980. He suggested that this was likely to impinge on Portugal's international competitiveness at a time when prospects were, in any case, for a sharply lower growth of exports in 1980 than in 1978/79. With the terms of trade likely to deteriorate as a result of oil price increases and receipts from tourism and workers' remittances unlikely to attain the same magnitude as in the past two years, the small surplus attained on current account in 1979 was expected to give way to a deficit of 3-4 per cent of GDP. However, with the support of appropriate financial policies the financing requirement for a deficit of this magnitude should be adequately met by net capital inflows and official borrowing on a moderate scale. In view of this outlook, the Fund representative expressed the view of the Fund that a further relaxation of the import restrictions maintained by Portugal, and an acceleration of their removal, can be accomplished.

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

8. Several members of the Committee prefaced their remarks by noting that the present consultation was the first held in accordance with the Declaration on Trade Measures Taken for Balance-of-Payments Purposes which had been adopted by the CONTRACTING PARTIES on 28 November 1979. They noted that in many respects this Declaration was a codification of present practices; however it also contained a number of new elements which the Committee would need to take into account in its work.

9. The Committee noted the improvement in the balance-of-payments situation of Portugal in 1979. It noted in particular that there had been a current account surplus of over \$100 million in that year compared with a deficit of \$800 million in 1978. Members of the Committee commended the Portuguese authorities for their realistic and courageous exchange, wage and monetary policies which had contributed to the strong foreign demand for Portuguese exports, stimulated remittances from abroad and capital inflows, and increased receipts from tourism. Some of them regretted however that the Portuguese authorities had not made use of the favourable situation in 1979 to further relax restrictive import measures. It was regretted in particular that the Portuguese authorities had not been able to carry out their announced plan to abolish the 10 per cent surcharge in October 1979 and that no new deadline for its termination had been set. One member said that he doubted whether there had been in 1979 any need for trade measures to safeguard the external financial position. He regretted that Portugal had not taken advantage of the improved balance-of-payments situation to remove its trade restraints when it had revalued its currency in February 1980. The question was asked whether the Portuguese authorities could now commit themselves to the gradual removal of the remaining restrictive import measures in accordance with an announced time schedule.

10. The representative of Portugal replied that it was difficult for a country on the brink of industrialization to pursue for a long time the restrictive credit and wage policies that had made the improvement in the payments situation possible. The Government had to take into account the need to secure investments, employment opportunities, and some increase in private consumption. These factors had limited the scope for trade liberalization in 1979. The legislation on the quotas for unassembled vehicles provided for a calendar for the phasing out of these restrictions. The relatively uncertain balance-of-payments situation made it however difficult to announce a time schedule for the removal of the other restrictive import measures at the present time. The Portuguese representative reaffirmed that the restrictive import measures imposed for balance-of-payments purposes were of a temporary nature and that it was the intention of the Portuguese authorities to remove them as soon as the external financial position permitted. He also declared that a time schedule for the removal of these measures would be announced whenever practicable in accordance with the Declaration of the CONTRACTING PARTIES on Trade Measures Taken for Balance-of-Payments Purposes.

11. Asked about the cause of inflation and the policies to contain it, the representative of Portugal explained that among the main factors which had contributed to the rise in prices in 1979 was a 33 per cent increase in import prices caused in large part by the effective depreciation of the escudo. Structural problems in some sectors were an additional factor. Since wage ceilings recommended by the Government had on the whole been observed, wage increases tended to be a reflection rather than a cause of inflation. The recovery of profit margins and the relatively high interest rates stimulated inflation to a certain extent. In response to a query on the influence of the rise in the price of oil, the representative of Portugal said that oil imports represented in 1979 about 20 per cent of total imports. While it was expected that there would be in 1980 a more than 15 per cent increase in the volume of oil imports and a 60-70 per cent increase in the price of oil, the volume of total imports was expected to increase by about 5 per cent and the average price of imports by 22 per cent.

12. Several members asked questions about the exchange rate and interest rate policies in Portugal. The representative of Portugal replied that the programmed depreciation of the effective exchange rate for the escudo was now set at 0.75 per cent per month, however this rate could be changed if necessary. At present the depreciation rate was sufficient to compensate the difference in the rate of inflation in Portugal and that in its trading partners, and it was therefore considered realistic. The interest rate policy of the Portuguese authorities was flexible but in general attempted to take into account interest rates abroad and the difference between the inflation rates in Portugal and in its main trading partners. The policy was, inter alia, aimed at stimulating savings, remittances from abroad and net capital inflows.

13. Some members noted that Portugal's fiscal and monetary policies, if they did not succeed in reducing inflation, could increase the pressure for the use of trade restraints. They expressed the hope that Portugal would be able to contain inflation and noted that Portugal's willingness to follow flexible exchange and interest rate policies should alleviate the pressure for import restraints.

14. Replying to a number of questions on the foreign debt and its maturity profile, the representative of Portugal said that, of the total debt of 6.5 billion dollars, 1.3 billion were government debts, 0.8 billion private debts with government guarantee, 2.8 billion private non-guaranteed debts, and 1.6 billion debts of the Bank of Portugal. He added that for the Government large repayments would begin in 1983, while the majority of the private, non-guaranteed debt fell due for repayment in 1980.

System, method and effect of the restrictive import measures

15. A number of detailed questions were asked about specific aspects of the Portuguese import régime. In reply to queries on the coverage of the 10 per cent surcharge, the representative of Portugal stated that the product categories subject to the surcharge accounted for 23-24 per cent of total imports but that a large portion of the import of products in such categories was exempt from the surcharge so that the coverage was in fact reduced by more than one half. This was because the legislation exempting certain imports from duties, such as the imports by public entities or imports for specified purposes, applied to the surcharge as well. The fiscal revenue generated by the surcharge was now only 60 per cent of what it was in 1977, which reflected mainly the reduction of the surcharge together with the decline in imports of covered goods and the reduction in the actual coverage.

16. One member of the Committee suggested that, since only five items covered by the 60 per cent surcharge were bound under GATT, the Portuguese Government might have recourse to the GATT provisions permitting the adjustment of bound duties. In reply to this suggestion and other queries related to the 60 per cent surcharge, the representative of Portugal said that his authorities had studied the possibility of replacing this surcharge by internal taxes as had been suggested at the last consultation but their preliminary conclusion was that this would not be possible since the transaction tax was already very high on these goods and a further increase would render a future harmonization of the tax with EEC requirements more difficult. The preferable solution was to gradually reduce the surcharge as balance-of-payments developments permitted.

17. One member, welcoming the removal of coffee and plastic products from the list of products subject to the quota system for consumer products asked how the escudo value of the remaining quotas was adjusted. The representative of Portugal answered that the quota value had been adjusted on a twelve-month basis to take into account the expected increase in the average price of restricted imports. In response to a further question he said that both the quota system for consumer products and that for unassembled vehicles were administered in a non-discriminatory manner.

18. Some members said that there had been delays in the issuing of import "bulletins". Delays appeared to have occurred in particular with regard to textiles imports. These members urged the Portuguese authorities to remedy the situation. The representative of Portugal said that "bulletins" were required solely for statistical but not restrictive purposes. Any delays in the issuing of the "bulletins" must have been exceptional and accidental. The Portuguese representative suggested that the members take up any specific problems through the appropriate channels.

### Conclusions

19. The Committee noted with satisfaction that Portugal's external financial position had substantially improved in 1979 and that the Portuguese authorities had lowered the main surcharge to 10 per cent, reduced its coverage and removed major items from the list of goods subject to the quota system for consumer goods. The Committee regretted however that Portugal had not been able to take advantage of the favourable payments situation in 1979 to relax the restrictive import measures further.

20. The Committee noted that Portugal's external financial position had deteriorated in early 1980, that the outlook for the remaining part of the year was uncertain and that this created problems for the immediate removal of restrictive import measures. However, it also noted that according to the International Monetary Fund appropriate financial policies should make it possible to meet the financing requirement for the deficit expected in 1980 by net capital inflows and official borrowing on a moderate scale. The Committee therefore concluded that efforts towards a further relaxation and early removal of the restrictive import measures imposed for balance-of-payments purposes should be made.

21. The Committee noted that Portugal had so far not announced a time schedule for the removal of the 10 and 60 per cent surcharges and the quota system on consumer goods. Recalling paragraph 1(c) of the Declaration on Trade Measures Taken for Balance-of-Payments Purposes the Committee recommended that the Portuguese authorities announce such a time schedule as soon as practicable. The Committee expressed the hope that the Portuguese authorities would find this possible before the next consultation.

ANNEX

Opening Statement by the Representative of Portugal

On behalf of the Portuguese delegation I would like to say that we take pleasure in having once more the opportunity to participate in the work of this Committee.

On the basis of the documents prepared by the Portuguese authorities it seems appropriate, as has been customary in the preceding consultations, to summarize the main developments in the Portuguese economy in 1979 and to give some relevant information about the prospects for the current year.

I. ECONOMIC DEVELOPMENTS IN 1979

1. In general, the economic developments in 1979 have been a continuation of the trends recorded in 1978, with most elements of domestic demand remaining weak while export growth continued at a remarkably high rate.

The most positive achievement was the strong improvement in Portugal's external accounts. The current account showed the first surplus since 1973, namely about 50 million dollars (or more than one hundred according to more recent estimates), and the overall balance registered a surplus of 1.3 billion dollars (against 160 million in 1978).

This performance of the national economy is due to the pattern of economic policy that has been followed since 1978 with special emphasis on both the exchange rate and restrictive monetary policies.

Demand and production

2. According to the most recent available information economic activity in 1979 showed the same growth rate as in 1978, that is GDP increased by about 3.4 per cent.

External demand provided the main stimulus to growth. Exports of goods and services rose by about 22 per cent showing a remarkable acceleration in comparison with the already high rate registered in 1978 (16 per cent).

The development of the other components of demand may be summarized as follows:

- Investment is estimated to have declined by 3 per cent. The share related to construction is considered to have decreased and equipment is estimated to have also decreased though not significantly.
- Public consumption increased about 6.0 per cent in real terms.

- Private consumption may have risen slightly, due to the fact that emigrants' remittances have compensated the negative trend in real wages.
- Imports of goods and services recorded an increase in real terms of about 4.5 per cent due to the fairly high increase in imports of agricultural goods.

3. In 1979, all major branches of production (except construction) experienced growth rates very similar to those registered last year. The faster growth of the agricultural sector (5 per cent in 1979 as compared to 4 per cent in 1978) reflects essentially the very good performance in wine production. As to manufacturing industries, the growth rate of 3.4 per cent corresponds to a higher dynamism in the export oriented industries. As regards the construction sector, a negative rate of 2 per cent is expected, showing a sharp deceleration as compared with the preceding year. This was mainly due to the high level of interest rates, not entirely offset by the system of credit facilities for the purchase of private dwellings.

#### Employment and productivity

4. The unemployment rate is estimated to have risen from 7.9 per cent in 1978 to around 8.5 per cent mainly due to new arrivals in the labour market not totally absorbed by the evolution of employment. In these conditions productivity is estimated to have grown by about 2.7 per cent, less than in 1978 (about 3.4 per cent).

#### Prices and wages

5. The rate of inflation as measured by the consumer price index accelerated slightly from 22.1 per cent in 1978 to 24.2 per cent in 1979. This is mainly explained by the persistence of some structural features of the economy and higher import prices in escudos (about 33 per cent) due to the depreciation of the national currency combined with international inflation. It should be stressed that in 1979 real wages declined again by about 3.5 per cent.

#### Money and credit

6. In 1979, taking into account the favourable results achieved in Portugal's external accounts, the monetary authorities eased gradually the quantitative limitations set on credit expansion. Total domestic credit, which had increased by 24.5 per cent in 1978, rose by 26.1 per cent in 1979 representing a slight increase in real terms.

On the basis of end-of-year figures, the money supply (M2) showed an increase of 36.3 per cent in 1979. This was considerably higher than the 28 per cent increase recorded in 1978. On average, the money supply grew by 27.7 per cent against 26.1 per cent in the previous year. There was practically no alteration in the income velocity of money.

#### Budget

7. The 1979 budget aimed at reducing the public sector current deficit in real terms, by maintaining the level of the deficit at the same nominal terms as last year (Esc 28 billion). However, this goal was not achieved and the current deficit is estimated at Esc 36 billion. The total deficit of the public sector is estimated to be about Esc 99 billion, representing 10 per cent of GDP.

#### Trade and payments

8. As mentioned above, Portugal's external accounts had a quite favourable evolution in 1979, as in the previous year. The current account has in fact shown a surplus of 2.7 billion in 1979 as compared with a deficit of Esc 33.6 billion in 1978.

This variation was largely due to the substantial increase in private transfers (66.6 per cent) which largely offset the deterioration of the trade balance. The services account also contributed towards that improvement since its balance also became positive as a consequence of the large increase in net receipts from tourism (77.7 per cent) which was higher than the rise in the deficit of the investment income account.

9. The trade balance is estimated to have resulted in a negative swing of Esc 17 billion - reaching the level of Esc 148.0 billion on a customs basis - entirely accounted for by price and exchange rate movements and a terms of trade deterioration of 2.4 per cent, which together more than offset the favourable developments in the real trade balance.

Portugal's exports are expected to have totalled about Esc 171.8 billion in 1979 as a result of a very sharp volume increase of about 23 per cent and a price rise of 29.5 per cent. This favourable export performance in 1979 was due to the continuing improvement of Portugal's relative competitive position arising from favourable developments in relative unit labour costs as well as the maintenance of the crawling peg devaluations. As a result of the strong competitive position of exports, Portugal improved its market shares appreciably.

Following a decline of 2 per cent in 1978, total imports were estimated to have recorded in 1979 a rise of about 4.6 per cent, which together with an increase in prices of 33 per cent led to a total value of Esc 320.5 billion.

This improvement was strongly reinforced by capital flows and the overall balance showed a surplus of Esc 64 billion (about 1.9 billion dollars) as against a surplus of Esc 9.6 billion in 1978 (160 million dollars).

10. The amount of external debt rose by Esc 1,163 million to Esc 6,583 million which corresponds to about 32.5 per cent of GDP in 1979 as against 31.8 per cent at the end of 1978.

11. Since 1978, the emphasis that has been previously given to restrictive import measures has been gradually shifted to measures aiming at the control of domestic demand.

In 1979, this policy continued to be supported by the maintenance of a "crawling peg" exchange rate policy; however, considering the favourable results achieved in the balance of payments and in order to contribute to reduce inflation, the programmed depreciation of the effective exchange rate for the escudo was reduced in April from 1.25 per cent to 1 per cent and in June to a monthly average exchange rate of 0.75 per cent. The average variation in exchange rate for 1979 when compared to 1978 was of 17.2 per cent (in the preceding year that rate was 23.8 per cent).

As regards restrictive import measures, the Portuguese authorities continued to relax the import régime in 1979. It has to be recognized that the present set of measures represent a considerable liberalization of the overall level of restrictiveness as compared to the one that prevailed in 1977.

#### Measures taken since last consultation, in relaxing or otherwise modifying import restrictions

- The 30 per cent import surcharge introduced in May 1975 and reduced to 20 per cent in October 1978, was further reduced to 10 per cent in May 1979. The removal of several items from the list of this surcharge reduced its coverage from 26.0 to 24.0 per cent of total imports (in 1978).

Mainly due to fiscal reasons and considering the adverse prospects in the international economic situation, it was not possible to terminate the surcharge last year as was planned and accordingly announced at last consultation.

- The 60 per cent surcharge, covering only about 1 per cent of total imports has remained unchanged.

- The quota system for consumer goods was extended from 1 April 1979 to 31 March 1980. The removal of two items - coffee and plastics - reduced substantially the coverage, namely from 4.2 to 3.3 per cent of total 1976 imports (the last year before the enforcement of this system). On the other hand an adjustment in value of about 18.6 per cent was applied to the remaining list so as to compensate the depreciation of the escudo. It must be mentioned that a significant number of the items under that quota system benefited also from the reduction of the surcharge.
- The quota system for unassembled vehicles was extended from 1 January 1979 to 31 December 1979. The total amount of the quota was raised by 18.7 per cent to 4.376 billions of escudos.

## II. PROSPECTS AND POLICIES FOR 1980

As far as the macro-economic "scenario" and policies for the current year are concerned I shall present a summary of the main guidelines, measures and prospects contained in the Government Annual Plan and Budget whose approval by the Parliament was recently obtained.

The main priority goals to be achieved by the macro-economic policy are the following:

- (a) Amelioration of the present standard of living of the population;
- (b) To slow down inflation;
- (c) To stimulate productive investments;
- (d) To re-assume, strongly and definitively, the "European commitment".

Recognizing that such goals must be integrated in a medium- and long-term framework the Government will develop several tasks connected with the elaboration of the general guidelines of a Medium-Term Plan and has already under preparation a programme of public investments for the coming three or five years with the view of constituting a guide to the public sector and an incentive to the productive sector.

Considering that the investment option will be dominant in 1980, a rate of increase of about 6 per cent for the G.F.C.F. is forecast which compares with a decline of about 3 per cent in 1979.

As regards inflation, the decision of controlling the rate of consumer price increases so as to attain the maximum level of 20 per cent represents a deceleration of four percentage points compared with 24.2 per cent inflation rate registered in 1979. This must be considered an ambitious goal.

taking into account that the international prospects in the major OECD countries are pointing in the opposite direction, that is towards an increase in inflation.

During the last two years, as mentioned above, the reduction of the external deficit has constituted in Portugal the main concern of the economic stabilization policy. From the preceding references to the priority goals of the 1980 Plan it is clear that, although the Government will pay significant attention to the developments of the external accounts, these will be viewed more as an important constraint to be taken into account rather than as a dominant objective.

In the present internal and international economic situation, with substantial rises on petroleum prices, a pursuit of past policies would mean to impose on the Portuguese people strong additional sacrifices and would hamper economic growth. According to the policy guidelines just mentioned the main macro-economic forecasts for 1980 are the following:

- Increase of general economic activity of 3.6 per cent, representing a slightly higher growth than the 3.4 per cent estimated for the preceding year.
- Private consumption will develop at a rate of 1.5 per cent showing a recovery as compared with the rate of 0.5 expected for 1979.
- Public consumption will remain practically stagnant: the projected increase of 0.5 per cent represents a significant deceleration as compared with the strong increases in the last two years (5.6 in 1978 and 6 per cent in 1979).
- Productive investment (G.F.C.F.) will rise to a rate of 6 per cent.
- The expected current deficit will be about 750 million dollars.

#### Current account developments in 1980

In 1980, the negative value of 750 million dollars estimated for the current account corresponds to a trade deficit of 3.3 billion dollars, a surplus of 75 million dollars on the "Service and Revenues" account and transfers of 2.5 billion dollars.

The deterioration of the trade balance - about 800 million dollars, which corresponds to a deficit 30 per cent higher than in the preceding year, is mainly due to the combined evolution of the price and the volume of imports - 22 per cent and 5 per cent respectively - which, in spite of

the fairly good expected increase of exports in volume - 9 per cent - could not be compensated by the total increase in export value. In fact, the export prices will increase by about 15 per cent, which implies an additional and stronger deterioration of the terms of trade of about 6 per cent. This is mainly due to the direct and indirect impact of the sharp increase of oil prices.

The increase of about 20 per cent forecast for net tourism receipts reflects to some extent the impact of the international crisis.

The value expected for emigrants' remittances reflects a stagnation as compared with 1979. This is explained mainly by the fact that the values registered in 1978 and 1979 must be considered "abnormal" taking into account that they reflect in part postponements of remittances not transferred in the preceding years. The 1980 figure is more in line with the normal trend of remittances.

In the conditions referred to above of a sharp deterioration in external accounts, in particular the trade account, the Portuguese Government decided to extend, until the end of this year, the enforcement of the surcharges.

The quota system for consumer goods was also extended for an additional period of twelve months. The adjustment in value of about 15 per cent is estimated to compensate the price increase for this category of goods.

The quota system for unassembled vehicles was also maintained for the whole year with an adjustment in value of about 30 per cent over the preceding year.

I would like to stress that the Portuguese authorities would like to maintain their policy of utilizing the restrictive import measures to a very small extent to phase them out as soon as possible and to apply them on a non-discriminatory basis. Unfortunately, taking into account the prospects for 1980 referred to above, the maintenance of the trade measures had to be considered essential in safeguarding the balance of payments in the context of in a set of more general economic policies.

I would like to conclude by expressing the hope that Portugal can rely once more in this Committee on the solidarity and the understanding of its trading partners.