RESTRICTED

L/746/Add.1
26 November 1957

Limited Distribution

GENERAL AGREEMENT ON TARIFFS AND TRADE

CONTRACTING PARTIES
Twelfth Session

REPORTS OF THE WORKING PARTY ON BALANCE OF PAYMENTS

On the consultations held with Four Contracting Parties

E. Ceylon
F. India
G. Turkey
H. Japan

E. CONSULTATIONS WITH CEYLON

1. In accordance with its terms of reference, the Working Party has conducted the consultations with Ceylon under paragraph 4(b) of Article XII and paragraph 1(g) of Article XIV.

2. The Working Party had before it:

(a) a basic document prepared by the secretariat in collaboration with the Ceylon authorities describing the system and methods of the balance-of-payments import restrictions in force in Ceylon. The document also contains a statement on "the effects of the restrictions on trade" embodying the views of the Ceylon authorities; and

(b) documents provided by the International Monetary Fund.

These documents should be deemed to be supplementary material annexed to this report.

3. In conducting the consultations the Working Party followed the "Plans" recommended by the CONTRACTING PARTIES for consultations. The present report summarizes the main points of the discussion during the consultations.

Consultation with the International Monetary Fund

4. 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 these consultations with Ceylon. As a part of the consultations between the CONTRACTING PARTIES and the Fund the representative of the latter referred to the results[1] and background material from its 1956 consultation with Ceylon, and to a supplementary paper on developments subsequent to that consultation. In accordance with agreed procedure the representative of the Fund was invited to make a statement supplementing the Fund's documentation concerning Ceylon's position. The statement made was as follows:

[1] See QRC/17/Add.2

"During the Eleventh Session, the International Monetary Fund transmitted to the CONTRACTING PARTIES the results and background material from its 1956 consultation with Ceylon under Article XIV of the Fund Agreement, which consultation was concluded on October 31, 1956. The Fund's 1957 consultation with Ceylon is scheduled to be held soon, with discussions between the representatives of Ceylon and the Fund staff to be held in November.

"As some time has elapsed since the conclusion of its 1956 consultation with Ceylon, the Fund has provided a supplementary paper on Ceylon, dated August 30, 1957, to supply background information on subsequent developments in the internal situation, the balance of payments, and the restrictive system. This paper, together with the background material from the 1956 consultation under Article XIV of the Fund Agreement, and the results of that consultation, have been distributed to the members of this Working Party.

"With respect to Section I of the Plan for Consultations, relating to balance-of-payments position and prospects, as the CONTRACTING PARTIES have been informed, Ceylon has taken action which resulted in a virtual elimination of discrimination against imports from the dollar area. Subject to this development, and pending the conclusion of its 1957 consultation with Ceylon, the Fund sees no reason to alter the appraisal of the situation contained in the results of its 1956 consultation which have already been made available to the CONTRACTING PARTIES.

"With respect to Section II of the Plan, relating to alternative measures to restore equilibrium, the attention of the Working Party is drawn to the results of the last Fund consultation with Ceylon. The Fund has no additional alternative measures to suggest at this time."

Statement by the representative of Ceylon

5. The representative of Ceylon opened the consultation with a general statement in which he described the economic background of the country, recent developments in its balance of payments and the present state of its import restrictions. The complete text of the statement is given in Annex I to this report. It was noted that the economy of Ceylon was highly dependent on foreign trade and that, consequently, a major aim of Ceylon's monetary and fiscal policy was to moderate the impact of external influences on the domestic economy in order to ensure stability. At the same time emphasis was laid on the longer-term objectives of economic development - of expanding and diversifying the economy so as to reduce the present structural dependence on the export of a few primary commodities.

6. As regards the balance-of-payments situation and prospects, the representative of Ceylon referred to the documents supplied by the Fund, which showed that the situation had been less favourable in 1956 than in 1955; the increase in foreign assets had been much smaller, principally due to a substantial fall in export earnings. There had also been a substantial

increase in imports which, in the view of the Ceylon representative, reflected in part the high level of liberalization that had been attained. The balance-of-payments situation in the first half of 1957 had been even less satisfactory, resulting in a considerable decline in the external assets. The Government was keeping the situation under close and continual review, particularly in view of the persistent decline in monetary reserves in recent months.

7. At present, however, restrictions were applied only on a small number of products. Among the thirty odd items for which no import licences were issued, some were being imported through State trading. The import of some other items was considered undesirable in view of the possibility of their being used for adulterating local export goods or for reasons of public health etc. under Article XX. The remaining items were restricted for balance-of-payments reasons. In applying restrictions the Government always gave due consideration to the need to reduce to a minimum any incidental protective effects that they might have on local production. On the question of discrimination, the Ceylon representative called attention to the statement of the IMF representative, noted in paragraph 4 above, that "Ceylon has taken action which resulted in a virtual elimination of discrimination against imports from the dollar area".

8. The representative of Ceylon stated in conclusion that the intention of his Government was to simplify the present system of import restrictions while continuing to pursue its policy of assuring fair opportunities for Ceylonese citizens to participate in the import and export trade. In the view of the Ceylon Government the implementation of this policy of "Ceylonization" involved no quantitative limitation of imports.

Problems relating to the balance-of-payments situation

9. As the recent deterioration in Ceylon's balance of payments was partly due to the decline in export prices for tea - a commodity which represented over 60 per cent of the country's total exports in 1956 - members of the Working Party showed considerable interest in the future prospects for the tea market and in any measures which might have been adopted in Ceylon for improving the quality, or for increasing the production, of this export commodity. Since reference had been made to the importance of price stability the Ceylon representative was requested to comment on the value and effects of long-term contracts as a measure for achieving that end. The Ceylon representative stated that through the use of improved methods in the production of tea there had been an increase in yield. The absence of an effective intergovernmental agreement on commodity trade meant that there was little likelihood of the prices of such goods as tea attaining any measure of stability. However, as this was a problem of general interest and was on the agenda of the CONTRACTING PARTIES, the Ceylon delegation would prefer to withhold comment at this consultation, and to clarify Ceylon's position during the plenary discussion on the commodity problems.

10. On the basis of the data supplied by the Fund, which showed that, as a result of a substantial influx of private capital from the United Kingdom, there was a much lower net outflow of private capital from Ceylon in 1956 as compared with the level in the previous year, a member of the Working Party invited the representative of Ceylon to comment on the effects of this trend on the country's balance of payments. The representative of Ceylon called attention to the high level of net outflow of capital in recent years (Rs. 37 million in 1953, 49 million in 1954 and 56 million in 1955). Following the improvement in 1956 the net outflow had risen again in the first half of 1957 to an annual rate of Rs. 28 million. Foreign investment, however, played only an insignificant role in Ceylon's balance of payments. In the view of a member of the Working Party the volume of capital that might flow into Ceylon would depend greatly on the policy of the Government not only in regard to the control of capital movements but also in regard to restrictions on imports. The representative of Ceylon noted that in both of these respects the policies pursued by Ceylon could not be regarded as placing any hindrance on the import of investment capital. The import of capital goods was virtually free from restriction and subject to low rates of duty. In addition, the exchange controls applying to outward remittances of capital, interest and profits were of an extremely liberal nature.

11. A member of the Working Party wondered whether, in view of lack of capital inflow and the inherent instability in commodity prices, it was really possible for Ceylon to maintain its policy of liberalization on a continuing basis. The representative of Ceylon said that the basic policy of his Government was to diversify the economy and increase production through developing the resources of the country while at the same time assuring an adequate supply of consumer goods essential to the population. In consonance with these objectives his Government would, however, always aim at acting in compliance with the General Agreement.

12. Some members of the Working Party expressed appreciation of the progress that had been made by the Government of Ceylon in relaxing import restrictions and particularly in substantially reducing discrimination. A member of the Working Party, however, pointed out that Ceylon's external reserves were at a substantial level equal to the value of five months' imports at the current rate. Referring to the short list of goods the import of which was being restricted, he wondered whether the removal of the restrictions on these items would have any significant effect on the balance of payments. The representative of Ceylon said that in view of the rapidly deteriorating position of Ceylon's balance of payments, it was necessary to proceed very cautiously in relaxing import restrictions further.

Governmental policy and internal measures affecting balance of payments

13. Members of the Working Party asked a number of questions in this field, including for example: what were the relative proportions of consumer goods and capital goods benefiting from the recent liberalization measures; whether the import and economic development policies of Ceylon were formulated on the basis that the standard of living of the country could be rapidly raised or whether the Government felt that the resources available were merely adequate

to meet the rising demand resulting from the increase in population; whether the longer-term policy of the Government was to balance external payments by increasing exports, or by limiting imports. The Ceylon representative noted that the recent increase in imports consisted principally of consumer goods although the import of capital goods had also been higher than before. Apart from the restrictions applied for certain other purposes as noted in the basic document, the restrictions which were made necessary by the country's balance-of-payments situation had been applied with due regard to securing imports which were essential to the economy; neither the need of the population for consumer goods nor the requirements for industrial and agricultural development were neglected. In considering the problem of developmental measures necessary for raising the standard of living, account must be taken of the very high rate of increase in population in Ceylon which was among the highest in the world. The current development plans included the cultivation of rice and sugar which were destined for local consumption. To the extent that the present cultivation programme succeeded, the import of rice might be reduced. The efforts made in raising the quality and increasing the yield of tea, rubber and coconuts were, on the other hand, aimed at expanding exports. On the industrial side the present plans for the setting up of new factories, for example in the textile industry, would eventually have the effect of replacing a proportion of imports. It was hoped that the expansion of exports would be at a much higher level than the expansion of import-substituting production, and the country's external payments would thus be balanced at a higher level than at present.

14. The view was expressed by a member of the Working Party that it would be in the long-term interests of the country if governmental assistance for development were given to industries that could be expected eventually to become self-sustaining and capable of meeting foreign competition; the expansion of uneconomical production would only place a burden on the country and hinder the rise in the standard of living. A member drew attention to the growing deficit in Ceylon's budget which, in his view, would enhance the tendency towards inflation. It was stated by a member of the Working Party that increases in imports beyond a country's capacity to pay should not be regarded merely as a problem for the balance of payments but rather as a symptom of internal disequilibrium. Restrictions on imports would not strike at the root of the problem but would merely serve to build up further internal demand. A government faced with balance-of-payments difficulties should concentrate on internal measures while liberalizing imports as much as possible rather than reduce the inflow of goods from abroad. The hope was expressed that the problems now faced by Ceylon were of a temporary nature and that the Government would soon be in a position to eliminate the remaining restrictions.

15. The Working Party heard certain personal views expressed by a member on the effect of State participation in industrial development on the inflow of capital, and a statement by the representative of Ceylon outlining the difficulties in making a start in industrial development in Ceylon without governmental intervention. The latter pointed out that a population accustomed to agrarian life had little inclination to enter into industrial enterprise, and that governmental intervention was indispensable at the initial stage of industrialization. Once the process had gained momentum the Government could place emphasis on assisting development in the private sector rather than on direct participation in industrial enterprise. The proposed expansion of the textile industry based on

private capital under governmental assistance was a case in point. His Government was fully aware of the country's need for foreign capital, and the general policy had been to encourage foreign investment in the country. The aim was to foster a happy partnership between foreign investors and local entrepreneurs.

16. A member of the Working Party paid tribute to the people of Ceylon for their contribution to the world economy, and pointed out that the amelioration of a country's external financial position depended not only on its ability to produce, but sometimes also on conditions beyond its control. In the case of Ceylon, stability in the world markets for its principal export products was essential, and responsibility also rested with those countries which were the important markets for those products.

System and Methods of Restrictions

17. On the basis of the secretariat document, the Working Party discussed the system and methods of the restrictions in force in Ceylon. It was noted that only about thirty items remained on the list of goods for which licences were not being issued. Some of these items were, however, being imported under State trading and some were controlled for reasons such as public health or security. Only a few items were restricted for balance-of-payments reasons. The restrictions were applied without discrimination except for four items the import of which from the dollar area either was not permitted or was limited to token quantities. Most of the goods which, according to the Ceylon delegation, were not subject to import restriction, were included in Open General Licences and could be imported freely. The Working Party noted, however, that the open general licence applying to the dollar area was substantially shorter, and that more imports from that area required individual licences. The representative of Ceylon explained that this differentiation in procedure had been maintained either for statistical reasons or for the implementation of the Government's policy of "Ceylonization" of the import and export trade.

18. The representative of Ceylon described the background of that policy and explained why the measures at present taken for that purpose, while having no restrictive effects on imports, appeared to be discriminating against imports from countries. It was noted that as a legacy of the past a substantial proportion of the country's external trade had been found at the time of Independence to be in the hands of foreign firms. Having achieved Independence it was natural for the people to wish to participate more fully in this important branch of the economy. In preference to more drastic measures, such as outright expropriation of foreign firms, the present method of Ceylonization had been adopted. This aimed at achieving the desired end of diverting trade to nationals while affecting to the least possible extent the interests of established firms. By and large the area in which importers and exporters of Ceylonese nationality were encouraged to participate at present was limited to "new trade" in the sense of trade with countries with which there had previously been no substantial transactions, or with which trade had been substantially interrupted during the war. In certain other cases, e.g. in the trade with the United States, the aim was to enable Ceylonese citizens to benefit from any

expansion of trade between two countries. The differences in the procedures for admitting imports from different countries only showed the transitional nature of the present arrangements; the methods would be more uniform once the Ceylonization policy was completed. There could be no question of discrimination because there was no effective restriction on imports, and the application of such internal regulations should not be regarded as being in conflict with the provisions of the General Agreement.

19. At the request of a member of the Working Party the representative of Ceylon supplied the following figures which, he considered, gave evidence that the measures had no restrictive effects on trade.

Ceylon Imports from two "Ceylonization" countries

(Rupees million)

Year	Germany	Japan
1954	22	76
1955	26	98
1956	38	114

20. Members of the Working Party commented on the rather cumbersome nature of the whole system of Ceylon's import restrictions. They were aware that the complicated system had resulted from modifications and changes made in the course of years to meet the requirements of new situations, but felt that in the interests of foreign exporters as well as the local trading community the system could be simplified and made more intelligible to the ordinary people. Representatives of countries in the dollar area also suggested that the Ceylon Government should explore ways of achieving the declared purpose of Ceylonization without having to retain the discriminatory features in the licensing procedure. The representative of Ceylon stated that the procedures applicable to Ceylonization policy were, in the nature of the case, unavoidable. He agreed, however, that as regards other aspects of the licensing system efforts will be made to simplify procedures, wherever possible.

21. As described in the basic document, imports into Ceylon from the dollar area were treated as follows: apart from the thirty items which could not be imported from any source, the two items which could not be imported from the dollar area, the two items which could be imported in token quantities only, and the goods on OGL No. 2, which could be imported freely from the dollar area, all other items could be imported from that area either (i) under licences which were issued freely or (ii) under licences which were issued freely to registered Ceylonese traders, and to other importers on the basis of past trade. In response to a member's request for clarification, the Ceylon representative confirmed

(a) that the licences referred to in (i) above were issued freely to any importer who applied for them, and

(b) that the import from the dollar area of goods which were listed in OGL Nos. 1 and 4 (which applied to non-dollar areas) would be treated under the procedure described in (ii) above.

The representative of a country in the dollar area stated that some exporters in his country seemed to be either uncertain or unaware of the fact that commodities on non-dollar OGL's could be imported into Ceylon from the dollar area under freely issued licences as described above. It was suggested that the Ceylon Government might give adequate publicity to its import policy and procedures so as to remove any uncertainty on the part of traders. The representative of Ceylon stated that all import regulations were published in the Government Gazette and that the new regulations resulting from the review of the present regulations would, no doubt, also be published in this manner.

22. The Working Party was gratified to hear the statement made by the Ceylon delegation that the import control procedures would be simplified and that the Government would review the list of goods subject to restriction.

Effects of the Restrictions

23. Reference was made to the list of goods given in the basic document which might be benefiting from the incidental protective effects of the restrictions, and to the statement that "for a number of commodities, mostly those which are being produced locally, it is stated in the Gazette notification that no licences will be issued". A member of the Working Party observed that in order to reduce incidental protective effects to the minimum, the import of goods which were also produced locally should be permitted rather than prohibited so as to expose local producers to foreign competition. The representative of Ceylon assured the Working Party that his Government was aware that the development of uneconomic industries would not be in the long-term interest of the country. Such protection as might be considered necessary for the promotion of new industries would be provided through means consistent with provisions of the General Agreement.

24. It was noted that, notwithstanding the fact that Ceylon was still entitled to maintain import restrictions under Article XII, a number of products had in fact been made the subject of releases under Article XVIII for developmental purposes. The Working Party felt that the successive applications and notifications lodged by Ceylon under Article XVIII were a clear indication of the Government's full awareness of its obligations under the Agreement, and its intention to abide assiduously by its provisions.

ANNEX I

Statement by the Representative of Ceylon

I propose to begin my statement by making a few general observations on the Ceylon economy. The Ceylon economy, as you are no doubt aware, is highly dependent on foreign trade. Its exports, the production of which constitutes a very considerable proportion of the Gross National Product, consist of a few primary commodities whose fortunes are determined primarily by economic conditions prevailing in the markets abroad. Its imports, which account for approximately 80 per cent of its total foreign exchange disbursements, consist predominantly of basic foodstuffs and other essential consumer goods, the demand for which is in the main inelastic.

The problem of insulating the economy from external disturbances that affect the demand for its exports is, therefore, one of the major problems of the economy. In view of the considerable inelasticities of supply of products intended for domestic consumption as well as for export, a period of prosperity is in general marked by buoyant incomes, reflecting not so much rising production as rising prices, and by a surplus in the balance of payments. A period of recession, on the other hand, tends to be characterized not only by a sharp fall in domestic incomes but also, since the demand for imports does not fall correspondingly and adjustment of imports is not as rapid as the change in incomes itself, by a deficit in the balance of payments. The need to conserve foreign exchange in the one period for use in the other is, therefore, an obvious one.

It is one of the major aims of monetary and fiscal policy to modify or neutralize the impact of these external influences on the domestic economy and thereby ensure stability in the level of incomes. It is important to emphasize, however, that underlying this problem of stability is the more basic one of long-term economic development, of expanding and diversifying the economy with a view to reducing its present structural dependence on the export of a few primary commodities.

I now turn to the balance-of-payments situation and prospects. I can do no better than point to the excellent analysis of our position given in the background papers submitted to the Working Party by the International Monetary Fund, and I would like to draw your attention in particular to the supplementary paper dated 30 August 1957. I do not, therefore, propose to go into details. You will observe that our economic situation during 1956 has not been as favourable as it was in 1955. The over-all position of the balance of payments at the end of 1956 has resulted in the very small increase in our foreign assets of Rs.14 million, as compared with an increase of Rs.254 million in 1955. This has been due primarily to the smaller trade surplus earned during the year. Total export earnings have declined by as much as Rs.205 million as compared with 1955. This decline has been due in very large part to reduced earnings

from tea, the export prices of which declined by 9 per cent during the year. The significance of this fact will be appreciated when it is realized that tea accounted for 60 per cent of our total exports in value last year. The decline in the receipts from rubber has also been an important contributory factor. On the other hand, our imports have increased by as much as Rs.169 million over 1955 despite a 10.4 per cent worsening in the terms of trade, an increase representing an expansion of 9.4 per cent in import volume. This increase in imports, notwithstanding these adverse circumstances, reflects in part the high level of liberalization achieved in the field of import restrictions.

The balance-of-payments situation in the first half of this year has been even less satisfactory. The provisional data available in respect of this period point to a surplus of Rs.32.5 million only on merchandise account, and a deficit of Rs.94 million on total current account. Our external assets have declined by Rs.195 million during the first half of this year. The decline has been of the order of Rs.19 million per month in the first quarter, and Rs.46 million per month in the second quarter. While it is hazardous to predict the course of movement of these assets with any degree of assurance, their persistent decline in the recent period has underlined the need for caution. My Government is, therefore, keeping the situation under close and continual review.

The effects on the balance of payments of the present import restrictions cannot be said to be of great proportions. Nevertheless, it is not feasible to assess with any degree of accuracy the full effects on the balance of payments of any relaxation or elimination of the present restrictions. The factors I have already mentioned argue for considerable caution in this regard and certainly do not justify the adoption of such a course.

I now come to the restrictive effect of balance-of-payments policy on external trade. There are a vast number of items coming under import control and the present regulations create the impression that the existing system is a highly complicated one. In actual fact, the system of restrictions is a very simple one. As it is fully described in the secretariat document I shall confine myself to outline its main features.

The most important items for which no import licences are issued relate to major commodities of food like rice, wheat flour and sugar. The primary consideration is that adequate supplies are secured at reasonable prices. Past experience has indicated that it is highly dangerous to the community to leave the import of these commodities in private hands. The fact that the Government is the importer has no restrictive effect on the actual importation of these commodities. The full requirements of the island are imported from the cheapest available source.

Others for which no licences are issued include such items as coconut oil and citronella oil, which are exported from Ceylon on well-established commercial standards. These items were introduced in the past in order to

prevent the import of these commodities for the purpose of adulterating Ceylon products. The remaining items have been restricted definitely for conserving exchange.

So far as discrimination against the dollar area is concerned, the position is summarized in the following statement already made by the representative of the International Monetary Fund: "Ceylon has taken action which resulted in a virtual elimination of discrimination against imports from the dollar area."

It is the intention of the Ceylon Government to simplify the present regulations, but at the same time pursuing its policy of increasing the opportunities for Ceylonese citizens to participate in the import and export trade. The implementation of this policy imposes no quantitative limitation of any kind on the flow of imports into Ceylon.

It is widely recognized that balance-of-payments restrictions are not a permanent feature of the economy and that the incidental protection they afford will disappear with their elimination. In determining the incidence of particular restrictions the need to reduce to a minimum, in conformity with our obligations under the General Agreement as well as in the interests of the consumer, the incidental protective effects of such restrictions has always been an important consideration.

F. CONSULTATIONS WITH INDIA

1. In accordance with the Decision taken at the plenary meeting of the CONTRACTING PARTIES on 17 November 1956, the Working Party has conducted the consultation with India under paragraph 4(b) of Article XII. The consultation concerning the substantial intensification of quantitative restrictions by the Government of India as from 1 July 1957 was conducted at the same time.

2. The Working Party had before it:

(a) notification of measures effective on 1 July 1957 (L/648);

(b) a basic document prepared by the secretariat in collaboration with the Indian authorities describing the system and methods of the balance-of-payments import restrictions in operation in India and the intensification of import restrictions for the period 1 July - 30 September 1957; the document also contains a statement, made by the Indian authorities, on the "Effects on Trade" (MGT/89/57);

(c) supplementary information supplied by the Government of India on the licensing policy for the period October 1957 to March 1958 (L/718);

(d) documents provided by the International Monetary Fund.

These documents should be deemed to be supplementary material annexed to this report.

3. In conducting the consultations the Working Party followed the plan recommended by the CONTRACTING PARTIES for this series of consultations and the plan previously adopted by the CONTRACTING PARTIES for consultations with countries which intensify their restrictions substantially. This report summarizes the main points of the discussion during the consultations.

Consultation with the International Monetary Fund

4. 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 these consultations with India. As a part of the consultation between the CONTRACTING PARTIES and the Fund the latter transmitted the results and background material from its consultation with India concluded on 7 September 1956, supplementary information dated 5 September 1956, and a further paper dated 6 September 1957 on developments since that consultation. In accordance with agreed procedure, the representative of the Fund was invited to make a statement supplementing the Fund's documentation concerning the position of India. The statement made was as follows:

"The International Monetary Fund has transmitted to the CONTRACTING PARTIES the results and background material from its last consultation with India under Article XIV of the Fund Agreement, which consultation was concluded on September 7, 1956.

"As some time has elapsed since the conclusion of this consultation with India, the Fund has also provided a supplementary paper on India, dated September 6, 1957, to supply background information on subsequent developments in the internal situation, the balance of payments, and the restrictive system. This paper, together with the background material from the last consultation under Article XIV of the Fund Agreement, and the results of that consultation, have been distributed to the members of this Working Party.

"With respect to Section I of the Plan for Consultations, relating to balance of payments position and prospects, the general level of restrictions of India which are under reference does not go beyond the extent necessary at the present time to stop a serious decline in its monetary reserves.

"With respect to Section II of the Plan, relating to alternative measures to restore equilibrium, the attention of the Working Party is drawn to the results of the last Fund consultation with India. Pending the conclusion of its 1957 consultation with India, the Fund has no additional alternative measures to suggest."

Opening Statement by the Representative of India

5. The full text of the opening statement of the Indian representative is attached to this report as Annex 1, and is summarized in the following paragraphs.

6. The representative of India drew attention to the facts that these consultations had been initiated under Article XII of the original GATT, and that since then the revised Article XVIII had come into operation, paragraph 8 recognizing that under-devloped countries in rapid process of development tended to experience balance-of-payments difficulties; that was precisely what had happened in India.

7. Development naturally meant considerable imports of capital goods; imports of semi-finished products (the most important being iron and steel) had also increased steadily and substantially. Unfortunately, large amounts of foreign exchange also had to be used for foodgrain imports, especially over the last eighteen months, food production being severely affected by local climatic conditions. These payments had been necessary despite the very generous assistance from the United States of America, and more recently from Canada also. Latest crop reports were discouraging.

8. India had in the past followed liberal policies regarding imports of other consumer goods and expenditure on them had been substantial.

9. The net result was a steady decline in external reserves which now were Rupees 3,290 million. It had been necessary for the Government to amend the minimum reserve requirements to Rupees 2,000 million including gold; this was equal to the value of two months' imports at current levels and four months' at 1953-54 levels.

10. The Indian representative believed that, in these circumstances, the Working Party would agree that the Government had no option but to impose the fairly drastic cuts in July-September 1957. For October 1957-March 1958, a somewhat less restrictive but nevertheless tight policy had been announced. These measures, as the IMF had pointed out, did not exceed what was required to stop the serious decline in monetary reserves; there was little likelihood also that the reserves position would improve significantly for many months to come.

11. A very relevant point was what other contracting parties could do to assist countries in such a position. India had obviously to look first of all to increased exports to finance development. The Indian representative expressed the hope that India's effort to expand exports would not be hampered by unduly high tariffs, restrictive quotas or State trading devices.

12. Recognizing the importance of foreign investment, the Indian Government had allowed not only remittances of dividends but also repatriation of capital.

13. The Government had taken several fiscal and monetary measures to reduce inflationary pressures, and appropriate action would continue to be taken in the future.

14. The very tight licensing policy regarding the import of capital goods since early 1957 ensured that uneconomic industries would not be established.

15. The new import policy provided for the granting of licences to established importers over a wide range of items, the import of which might not be justifiable on strict balance-of-payments grounds, in order to avoid undue damage to the interests of other countries.

16. Concerning future prospects, the tight position could be expected to continue for the next two or three years, but they hoped to be able to achieve a more stable position in overseas trade from 1961 onwards, and, what was more significant, to reach higher levels of overall trade because of higher living standards and higher productivity. Despite the expected increase in production under the second Five Year Plan per capita income would still be only Rupees 330 in 1960-61.

17. The Indian representative stated that the exports of India had been more than adequate to finance the import of the current requirements of industry and the consumer, making available a small surplus for investment and development. This amount together with other resources was being utilized to establish capacity for the manufacture of steel, textile, sugar mill and electrical machinery, machine tools, diesel engines, aluminium, dyestuffs and other items. As local output increased to meet a substantially larger proportion of domestic needs, funds would be released to finance imports necessary to continue the development programme. The industries were those for which India was eminently suited. Thus India had concentrated on steel production, being among the world's cheapest producers. The substantial investment in developing the transport system would help to increase exports particularly of metallic ores, the demand for which could not be met fully at present. This would increase foreign exchange earnings. Also, the increase in output of foodgrains, raw cotton and raw jute as a result of the steps being taken to increase agricultural productivity, would ease the foreign exchange position.

18. In concluding, the Indian representative affirmed that their economy was a sound one, and the object of the development programme was to make it even sounder. The main problem was that of financing the development necessary to make fuller use of their resources and to provide more employment and higher living standards. Success would result in higher levels of production and trade, so promoting the objectives of the CONTRACTING PARTIES.

Balance of Payments Position and Prospects, and Alternative Measures to Restore Equilibrium

19. In reply to questions about the prospects for an expansion of the export market for traditional products - such as jute and cotton textiles and tea - as well as for new products, the representative of India said that it was

obviously very necessary that exports should expand as that was perhaps the principal way in which the development programme could be financed. There was no doubt that exports, even of the traditional items, could be increased. There was, for example, a good market abroad for vegetable oils and, at times in the past, quite substantial quantities had been exported. Last year, however, there had been a decline due to weather conditions and the large internal demand. In the development programme, a great deal of attention was being given to agricultural production and it was hoped over the years to sell more of these products. India was an efficient producer of jute goods and had natural advantages, and some expansion in sales could be expected. There was, however, competition from substitutes. Restrictions for protective reasons constituted an additional barrier to sales. Nevertheless some growth in demand for jute was anticipated. The jute industry was being modernized in order to offer a better and cheaper product. In regard to tea and cotton, it was hoped that there would be some increases. There were also plans to develop new industries, such as pig iron, for which ores were available. It was hoped to export steel. One of the difficulties in connexion with industries of that sort was the inadequacy of transport, but as the railway programme developed that would be overcome. A start had been made in marketing light engineering products and there had been encouraging response to efforts to export cottage industry products. A member asked whether special efforts had been made to increase exports of new products to neighbouring countries. These markets were likely to expand in the future. He mentioned in particular the possibility of exporting the output of the electronics factory at Bangalore. The Indian representative replied that these possibilities were being actively pursued as part of the export promotion drive.

20. A member noted with satisfaction the recognition of the role which foreign capital could play in India's development, and asked what sectors of industry were considered most attractive to foreign capital and what impediments there might be to the admission of such capital.

21. In reply, the representative of India said that there were no special fields in which foreign capital was restricted. Foreign capital was welcome throughout the whole field of industrial development. The Government undertook a general screening of all industrial projects, primarily for the purpose of ensuring that facilities, such as land, power, raw materials and water supply were available. This applied to all investments. It seemed natural that a foreign investor would wish to consult the government on matters of that sort before investing his money. In regard to particular fields for development, foreign capital was welcome in any of them; but the initiative had primarily to come from the foreign investor and the Indian business man with whom he was collaborating. One of the advantages of that sort of collaboration was that it helped to raise the general level of technical and managerial skill. Foreign capital could be invested in manufacture from local raw materials for export; ferro-manganese and ferro-chrome would be examples. Engineering and chemical industries such as machine tools, aluminium and dye-stuffs were all promising fields. Manufacture of film also offered attractive prospects; India was the second largest consumer of film, next to Hollywood. These examples were illustrative.

22. One member asked what the prospects were for foreign investment in India and whether any positive measures were being taken to attract foreign capital. The Indian representative stated in reply that there were good prospects for foreign investment. The basic conditions required were present in good measure, e.g. political and economic stability, provision of basic facilities such as power and transport, availability of raw materials and a steadily expanding market.

23. Replying to a member who asked what the policy was in regard to compensation in the event of nationalization, the representative of India said that it was the Government's firm policy to pay full and adequate compensation. The foreign investor had been fully satisfied with the compensation given in the very few recent cases of nationalization involving foreign capital. Further, the Government of India had declared that as a great deal of industrialization had yet to be undertaken, it would not wish to expend its resources in nationalizing private undertakings.

24. A member of the Working Party said that the success of India's development effort was important not only to that country but to other countries also. He referred in this context to the steady rise in India's population and the strain this imposed on the Indian economy. In reply, the Indian representative stated that this was one of the reasons why a rapid rate of development was essential. In spite of the big effort contemplated under the second Five-Year Plan, it would be able to absorb only the increase in the labour force, and the existing level of unemployment and under-employment might continue. The problem could only be solved through greater investment and productivity over a number of years.

25. Questioned about the effect of the intensification of restrictions which had been undertaken last July, the representative of India said that the position had to be viewed as a whole in the light of the measures introduced not only in July but in January and October as well. Together, they represented an adjustment of the import licensing programme to the changed conditions which had resulted from the increase in the level of development expenditure. In 1956 there had been an extremely liberal import policy which obviously could not be sustained along with an intensive development programme. In assessing their effect, no one of the measures introduced could be considered in isolation, as their results would overlap. Broadly speaking, the effect of all the policies (- as of any specific policy -) would be to enable the financing of the imports of raw materials needed to keep the country's industries going, and to maintain licences for consumer goods at as high a level as practicable.

26. A member noted that since the time of the 1956 IMF consultation it was clearly apparent that there had been a very heavy decline in India's reserves. The pressure seemed to have been due to a considerable increase in imports. Did that, he wondered, indicate that there had been a "bunching" of imports required for the development programme; and would such an exceptional concentration of demand mean that, perhaps for the next couple of years there would not need to be such a high level of imports? Was it the case that a substantial part of India's needs for development purposes had been met by those imports and that, consequently, within the next two or three years,

the balance of payments would not have to bear as heavy a burden of capital goods imports? Or was the picture worse and was there likely to be very heavy pressure on the reserves within the next few years, even with a fair amount of foreign investment and public loans?

27. The representative of India replied that a combination of factors had been responsible for the change in the balance-of-payments position from 1955/56 to 1956/57. A poor monsoon had led to an increase in imports and to a lesser extent a reduction in exports of agricultural products. Secondly, there had been a higher rate of imports because of much higher development outlays. Thirdly, there had been the consistent policy of liberalization which India had followed, not merely in relation to development goods but also for other kinds as well. As regards the future, it appeared that the position would continue to be difficult for the next two or three years. The level of imports was likely to remain high, although that did not imply a continuing drain on reserves. In the past, most of the imports had been paid for out of reserves. In the near future it was expected that the pattern of India's imports would be such that much of them would be covered by loans, e.g., equipment for the steel plants, railways and ports. In framing its current import policy, the Government had taken its commitments fully into account and would proceed in the light of its available resources.

28. A member asked whether imports of steel would continue at the current high level. In reply, the Indian representative stated that there would be some reduction in the coming months, and more after the expansion schemes of the existing steel plants had been completed.

29. A member asked whether the extent to which the current development programme was implemented would depend on the level of additional resources that might become available. The Indian representative replied that it should in any event be possible to meet essential current requirements, to honour existing commitments and to implement the "hard core" of the Plan consisting of rail transport, power, coal and steel production. The extent of further investment and the fields in which it would take place would depend on the level of additional resources that might become available.

30. A member observed that there was a possibility of an inflationary situation developing in India. But it was also clear that the Government was fully aware of the situation and was taking measures to deal with it. There had been, for example, two issues of Government bonds and he wondered what effect they had had on the situation. Had the issues absorbed funds which might otherwise have been idle? In reply, the Indian representative indicated that it was difficult to say whether money subscribed to loans would otherwise have been used or not. He added that money was generally tight and credit difficult to obtain.

31. Members of the Working Party from the dollar area noted with appreciation the policy of the Indian Government in enabling established importers to utilize 50 per cent of the face value of their soft currency licences (or where the value did not exceed Rs. 5,000, the full value) for imports from the dollar area, and welcomed the latest policy which enabled these importers to utilize half the value of soft currency licences or Rs. 5,000, whichever was the greater,

for dollar imports. This represented a reduction in discrimination, and they hoped the Indian Government would be able to maintain the momentum towards complete elimination of discrimination, when the balance of payments permitted. They asked whether this right to employ 50 per cent of the value of soft currency licences for imports from the dollar area was applied to all importers - established importers, actual users and others, and to all types of imports and enquired to what extent the soft currency licences in question had in fact been utilized by Indian importers to procure goods from the dollar area. A question was also posed concerning the criteria applied in import licensing policy and procedures and especially on the parts played by relative price factors and by availability of the goods in question from domestic production.

32. The Indian representative stated that the problem of India's balance of payments was an overall one. The import licensing system discriminated only between the dollar area and the rest of the world, though India had substantial deficits with some soft-currency countries. Import discrimination against dollar areas had been progressively reduced. There was no discrimination at all in regard to licensing of goods required by actual users and of capital goods. The discrimination in licensing to established importers had been further reduced under the current policy. Detailed information was, however, not readily available regarding the extent to which the soft currency licences had been utilized for dollar imports. There had also been reduction in discrimination with regard to licensing under the Export Promotion Scheme; whereas previously dollar licences had been granted only if the finished products were exported to the dollar area they were now being granted (subject, of course, to considerations of price and quality) even if the finished products went to non-dollar areas.

33. In regard to criteria applied, he emphasized that price considerations were certainly taken into account, and were most carefully studied in various quarters; for example, on the Import Advisory Councils consumer representatives had ample opportunity to help keep a check on this point. They did take into account domestic availabilities - because if satisfactory local products were available at reasonable prices, it would clearly be disadvantageous to the balance of payments to import them.

34. One member expressed appreciation of the adequacy of the Indian Government's publications and notices on import and licensing policy and procedures, a matter which his country regarded as one of considerable importance. The Indian representative welcomed the expression of opinion concerning the publications on import and licensing policy and procedures.

35. One member, commenting on the Indian distinction between the "dollar area" and the "soft currency area", suggested this could be misleading, and could imply that all currencies other than the dollar area were "soft". He wondered whether India could not employ other more suitable terms to describe the position.

36. The Indian representative replied that this had a historical basis. The Government of India had progressively moved towards non-discrimination in import licensing. They had not therefore expanded the hard currency list or created further currency-area categories for import licensing purposes, even when India had substantial balance-of-payments deficits with particular areas, and even though some of these currencies might be said to be hard in the same sense that the dollar was hard. This policy could obviously be sustained only if trading partners were prepared to reciprocate. It was to be hoped that all concerned would adopt policies which would ensure an increased level of world trade on a non-discriminatory basis.

37. Another member said he wished to mention a specific point of importance to his country. When restrictions had been intensified on 1 July 1957, the import of some commodities was totally or almost completely prohibited. Unfortunately this affected his country's important exports very much; as far as he could understand there was no discrimination by India between "soft currency" countries (in which his own was included) so far as quantitative restrictions were concerned. But the import ban on some of his country's products might necessarily be felt as a kind of discrimination. This was due to the fact that his country's exports to India were limited to a few commodity groups. The hardship to his country was therefore more serious than for most others. He mentioned as examples, staple fibre and fish-oils, imports of which into India were, for the time being, prohibited. Furthermore, it seemed to him that this policy was not in accordance with the obligations under Article XII:3(c) of the revised GATT.

38. On this point, the Indian representative observed that his Government's policy was not based on any discrimination, except, as pointed out earlier, between the dollar and soft-currency areas. It was necessary to differentiate between commodities as foreign exchange reserves had to be used to the fullest possible advantage. The basic document of the secretariat had referred to the liberal policies previously in operation, but now it had become necessary to impose import cuts over a fairly wide range of goods. The provisions of Article XII of the GATT required countries not to apply restrictions so as to prevent unreasonably the importation of any goods. In view of India's foreign exchange difficulties, the restrictions imposed could not be considered unreasonable. The point raised by the member of the Working Party would, however, be kept in mind.

39. One member asked whether the quantitative restrictions imposed by India had rendered less effective the concessions on bound items made during tariff negotiations since 1947.

40. The Indian representative pointed out that import controls dated back to 1940 when they were being applied under the Defence of India Rules. War-time regulations could not be continued indefinitely, so legislation was passed in 1947. Concerning the question on bound items, he observed that quantitative restrictions were certainly being applied at the time the tariff negotiations took place; but over the years India's import control policy had been determined by the balance of payments and reserve position; there had been periods when the level of restrictions was appreciably lower than at the time when tariff concessions were negotiated. At the end of 1956 quotas were liberal, and the liberal licensing scheme was in operation. They had tried to ensure that imports were permitted of items for which tariff concessions had been granted. Generally speaking, it would be quite incorrect to suggest that where tariff concessions had been granted they had been vitiated by the use of quantitative restrictions. The Indian representative cited figures to illustrate his point. Imports of many items on which direct or indirect concessions had been granted had increased substantially.

41. One member, referring to the new credit and deferred payment conditions associated with the granting of licences for imports of capital goods, suggested that these terms went beyond those normally regarded as commercial, and created problems for countries unable to extend such facilities. This tended to accentuate the restrictive effects of the import policy. He also enquired about other conditions attaching to the issue of certain licences (mentioned in paragraph 2, page 3 of the secretariat basic document) especially that concerning price for re-sale after importation; if international prices were not taken into consideration, this too could have restrictive effects on imports.

42. The Indian representative, replying to the question about capital goods imports, stated that in view of the difficult foreign exchange position, licensing of capital goods had necessarily to be restricted to schemes covered by foreign investment, or, for relatively small projects which would show quick results, by medium-term credits. In regard to the point about price considerations, he remarked that the object of the regulations was to ensure that users in India obtained supplies from established importers at import prices plus a reasonable mark-up. There was no intention on the part of the Government to use the price condition to restrict imports - it was imposed only to secure distribution of the imported product at equitable prices.

43. A member enquired about the prospects of overcoming the deferred-payment problem, and asked where the firms were to be found which were prepared to accept this type of contract.

44. The Indian representative referred to page 17 of the "Red Book" for October 1957-March 1958 and quoted paragraphs 50-52, where it is stated that import licences (for capital goods) against long-term overseas investment would be issued when the value of the goods to be imported was covered by fresh long-term equity or loan investment or other forms of finance not requiring any remittance before 1960; and that applications for import licences against medium-term credits would be considered for industries, projects or undertakings which were of importance as earners or savers of foreign exchange. Licences would as a rule be granted against medium-term credits only when the outlay on imported plant and equipment was relatively small and would be covered by savings or earnings as a result of the implementation of the scheme within a period of three years from the date of initial payment.

45. He agreed that a credit not involving any payment before 1960 could not be regarded as "normal commercial", and would require special financing.

46. In response to a question about the rate of interest on credits, the Indian representative stated that they would vary from country to country and would have to be considered in conjunction with the duration of credits, and prices and quality of the equipment. He did not think an answer in general terms would be entirely satisfactory. Generally, the importer in India would negotiate with the supplier after obtaining the Government's preliminary approval and then submit detailed proposals.

47. Several members expressed their appreciation of the measures taken by India in the fields of liberalization and of reducing discrimination. They recognized fully the fact that India had considerable balance-of-payments difficulties, and welcomed the fact that, despite this, import policy had moved in the direction of non-discrimination. It was hoped that India would continue to reduce discrimination and also avoid the placing of complete prohibitions on some imports, with a view to preventing unnecessary damage to the economic or commercial interests of other countries.

48. The Indian representative replied that they had fully in mind the possible effects of their restrictions on other countries' trade. Even the current licensing policy provided for the importation of a number of consumer goods which on strict balance-of-payments grounds could justifiably have been kept out. They would continue to bear fully in mind the interests of other countries.

49. One member pointed out that if too much consideration were given to the possible effects of import policy on <u>individual</u> countries this could quickly result in bilateral negotiations and agreements which might well amount to discrimination.

50. The Indian representative said he recognized this as a valid argument, and recalled his earlier statement that they did not discriminate between countries, but differentiated between commodities. Therefore, the question of bilateral negotiations for exchange of concessions in this field did not arise.

51. Members referred to the advantages associated with purchasing and importing at the best possible price. It was encouraging to note the efforts which India had made in the direction of trade liberalization and of reducing discrimination, but they would like to point out that if import commodities were shut out for too long, local production would develop, and make the necessary internal re-adjustments of resources, and subsequent imports of these commodities, very difficult.

52. Appreciation was expressed by the Working Party of the very full and informative statements made by the Indian representative, who, in turn, expressed his thanks for the sympathetic hearing given him during the consultations.

ANNEX I

OPENING STATEMENT OF THE INDIAN DELEGATION

I should at the outset express the appreciation of the Indian delegation of the work done by the GATT secretariat and the International Monetary Fund in preparing a careful and objective analysis of the situation. These documents are before the Working Party, as also a short statement from the Indian delegation describing their latest import policy. I need, therefore, in these opening remarks refer merely to some broad aspects of the problem which the Working Party might take into account.

These consultations have been initiated under Article XII of the original GATT. Since then the revised Article XVIII has come into force. Paragraph 8 of that Article recognizes that under-developed countries when they are in rapid process of development tend to experience balance-of-payments difficulties. This is precisely what has happened in India.

Development has naturally meant considerable imports of capital goods. The value of our machinery imports has gone up from Rupees 549 million in April/September 1955 to Rupees 824 million in the half year October 1956 to March 1957.

Our imports of semi-finished products have also gone up. The most important of these products is iron and steel, imports having risen steadily from Rupees 205 million in April/September 1955 to Rupees 594 million in October 1956/March 1957. Most of the steel has been required for our transport programme and for basic facilities and for irrigation and similar projects.

Unfortunately we have also had to provide exchange in large amounts for foodgrain imports. Our food production is still largely at the mercy of the monsoons and while favourable and timely rains enabled us to manage with relatively small imports in 1955-56, our requirements have gone up since. We have had over the last eighteen months to import more than two-thirds of the quantity of grain that we had assumed to be necessary over five years. In spite of the very generous assistance received from the United States of America under the PL480 programme and recently also from Canada, which has made it possible for us to build up the stocks required to deal with shortages and prevent undue price rises, we have had to increase substantially the allocations of exchange for the purchase of grain. The latest crop reports are discouraging and an increased level of imports may well become necessary.

Other imported consumer goods are not of much significance to the mass of the Indian people. Even so, we have in the past followed liberal policies in regard to imports and the total expenditure on items like drugs and medicines, paper, electrical goods, etc. has been fairly substantial.

The nett result of all this has been a steady decline in our external reserves. The decline has often averaged £ 1 million sterling per day for weeks together and the reserves are now Rupees 3290 million. It has become necessary for the Government of India to issue an ordinance amending the minimum reserve requirements to Rupees 2,000 million inclusive of gold, which is equal to the value of two months' imports at current levels and four months imports at 1953-54 levels.

Against this background and in the circumstances which I have explained, I trust the Working Party will agree that the Government had no option but to impose the fairly drastic cuts which they made in the import policy for the quarter July-September 1957. For the period October 1957 to March 1958, a somewhat less restrictive but nevertheless tight policy for imports has been announced and is in operation. These measures, as the IMF has pointed out, do not exceed what is required to stop the serious decline in our monetary reserves. Indeed, it is our estimate that with the fulfilment of orders already placed and the fresh licensing that will take place, there is little likelihood of the position of our reserves improving significantly for many months to come.

In these consultations, we aim not merely at exploring what can be done by the country which has had to impose restrictions but also what other contracting parties can do to assist the country concerned. India must obviously look first of all to increased exports to finance development. Our three main export commodities are jute manufactures, cotton textiles and tea. I shall refer briefly to each of these. We are modernizing our jute textile industry and we would hope that we will be enabled to sell our product without being faced with unduly high tariffs, or State trading arrangements or quota restrictions for protective considerations.

Our cotton textile exports have declined somewhat last year. Here again we would hope that our trading partners would give us adequate facilities for marketing on a competitive basis. We would hope that the efforts of India and other producers to market their teas will not be hampered by the levy of high duties.

Foreign investment can play a very useful part in developing the economy. Recognizing its importance, we freely allow not only remittances of dividends but also repatriation of capital.

The Government have taken several fiscal and monetary steps to reduce inflationary pressures in the economy and these have been set out in the statement circulated to contracting parties. Appropriate action will continue to be taken from time to time in these fields.

The very tight licensing policy followed for capital goods since the beginning of this year ensures that uneconomic industries will not be set up as a result of the intensification of import restrictions. Licences for the import of capital goods are now granted to an extremely limited extent and only for really sound schemes. The industrial projects now being implemented are

almost entirely against 1956 capital goods licences. At that time, a very liberal import policy was in effect for nearly all items and the private investor could not anticipate the tight policy we are now following.

The new policy provides for the grant of licences to established importers over a wide range of items, the import of which might not be justifiable on strict balance-of-payments grounds, in order to avoid damage to the intesests of other countries. The import of samples and advertising materials continues on Open General Licences.

Having explained the nature of our present difficulties and indicated that the restrictions on imports which we have imposed are by no means too severe or unmindful of the interests of other contracting parties, I feel I ought briefly to indicate the picture as we see it, of the future. For the next two or three years the tight position will, I am afraid, continue. But we expect to be able to achieve a more stable position in our overseas trade from 1961 onwards, and, what is more significant, we hope then to have higher levels of overall trade than at any time in the past on account of better standards of living in the country and higher levels of productivity.

For the past few years our industrial production has been increasing at the rate of 8 to 9 per cent per annum. We have also during the first Five Year Plan achieved an increase of 11 per cent per capita in the national income - a rate of a little above 2 per cent per annum. It is our hope to achieve a further increase in the second Five Year Plan. Nevertheless, our per capita income would still be only Rs. 330/- in 1960-61.

There is an urgency about all this in a country which is so poor and whose population is steadily rising.

Even today India can finance its imports of the current requirements of industry and the consumer and have some surplus of foreign exchange for development. In 1955-56, there was a small surplus on current account. This was in spite of substantial imports of commodities for developmental purposes. A rough calculation indicates that about one-fifth of India's imports in that year consisted of capital goods and if these are left out of account, there would have been a large current account surplus. Imports of machinery, steel and transport equipment were substantial. What we are now doing is to try to develop at a faster pace. But we are determined to see that development is on sound lines.

We have concentrated on steel. We are probably among the cheapest producers of steel - and have to subsidize the two million tons we import annually at present. When our steel expansion is complete we would save on steel imports. Similarly, with increased production in India of items like textile machinery, sugar mill machinery, machine tools, electrical machinery, diesel engines, aluminium, dyestuffs and other chemicals, we hope to meet a substantially larger proportion of domestic needs with indigenous production and thus release funds for sustaining the imports necessary to continue our development programmes.

The substantial investment in developing our transport system will help us in increasing our exports, particularly of metallic ores for which we find it difficult to cope with all the demand we receive.

Our cotton and raw jute imports between them cost us Rs.760 million in 1955-56. We shall continue to import these commodities but we trust that domestic supplies will increase significantly.

The Indian economy is a sound one, Mr. Chairman, and the object of our development programme is to make it sounder still. What we face at the present moment is the problem of financing the development necessary to make fuller use of resources and to provide more employment and higher standards of living. The success of this programme will result in higher level of production and exchange of goods, and thus promote the objectives which we as contracting parties have set ourselves.

G. CONSULTATION WITH TURKEY

1. In accordance with the Decision taken at the plenary meeting of the CONTRACTING PARTIES on 17 November 1956, the Working Party on Balance of Payments conducted a consultation with Turkey under paragraph 4(b) of Article XII.

The Working Party had before it:

(a) a basic document prepared by the secretariat in collaboration with the Turkish authorities, describing the system and methods of the balance-of-payments import restrictions in operation in Turkey. The document also contains a statement under Part II - "Effects on Trade", submitted by the Turkish authorities;

(b) documents provided by the International Monetary Fund.

All these documents should be deemed to be supplementary material annexed to this report.

2. In conducting the consultation, the Working Party followed the plan recommended by the CONTRACTING PARTIES for the consultations. The present report summarizes the main points of the discussion during the consultation.

Consultation with the International Monetary Fund

3. Pursuant to the provisions of paragraph 2 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 Turkey.

4. As a part of the consultation between the CONTRACTING PARTIES and the Fund, the latter transmitted the results and background material from its recent consultation with Turkey concluded on 22 July 1957. The results of the Fund's consultation with Turkey are reproduced in document QRC/17 of 16 October 1957.

5. In accordance with the procedure agreed upon by the Working Party, the representative of the Fund was invited to make a statement supplementing the Fund's documentation with respect to the position of Turkey. The statement made was as follows:

"The International Monetary Fund has transmitted to the CONTRACTING PARTIES the results and background material from its last consultation with Turkey under Article XIV of the Fund Agreement, which consultation was concluded on July 22, 1957.

"With reference to Section I of the Plan for Consultations, relating to balance-of-payments position and prospects, the general level of restrictions of Turkey which are under reference does not go beyond the extent necessary at the present time to stop a serious decline in its monetary reserves.

"With reference to Section II of the Plan, relating to alternative measures to restore equilibrium, the attention of the Working Party is drawn to the results of the last Fund consultation with Turkey. The Fund has no additional alternative measures to suggest at this time."

Opening Statement by the Representative of Turkey.

6. The representative of Turkey opened the discussion with a statement the full text of which is appended to this report in Annex I. This statement, which outlines the policy followed by his Government, is summarized in the following paragraphs.

7. In his general remarks, the representative of Turkey laid special emphasis on the vital questions of economic recovery and development with which the Turkish Government is concerned. He recalled that Turkey sincerely believed in free trade, in the necessity and value of multilateral co-operation and in the liberalization of trade and payments, and was resolved to adhere to the principles of the General Agreement. But other preoccupations deriving from its firm determination to overcome balance-of-payments difficulties, to achieve a substantial expansion in national production and productivity, to secure for the Turkish people adequate standards of living and adequate purchasing power, to provide employment for the ever-increasing labour force and to achieve full internal economic and financial stability, inevitably checked, for the time being, the speed at which it would like to proceed.

8. He recalled the reasons for which Turkey might well become, in the near future, one of the most interesting markets for its trading partners. At the same time, however, its vital recovery programme could be carried out only at the cost of certain sacrifices which the Turkish people were prepared to accept during a well-defined period of transition. Consequently, a country like Turkey, which had no other foreign exchange receipts than its export proceeds, needed a period of controls and restriction. Turkey had resorted to restrictions whenever forced to do so, but it had not failed on each occasion to demonstrate its intention of moving towards a much more liberal system.

9. The present system could be described as follows: this was a transitional period; the non-discriminatory restrictions applied at present could be considered to be temporary because their purpose was only to pave the way for the creation of a sound, viable, powerful and profitable national economy, which would enable Turkey to play in world markets its rightful constructive part within a free multilateral trading system.

10. The representative of Turkey also stated that, in his opinion, existing difficulties could be overcome only through mutual understanding of the problems and close economic and trade co-operation. As the final objective was the introduction of a far-reaching and continuing multilateral system, the problems affecting a given country were, in a sense and at the same time, problems of concern to other countries and the strength of the economic potential of that country was merely an integral part of the common potential.

Balance-of-Payments Position and Prospects

11. With respect to this part of the plan for consultations, the delegation of Turkey submitted an additional statement on the balance of payments and financial problems of Turkey. The full text of this supplementary statement, which is appended to this report in Annex II, is summarized in the following paragraphs.

12. In his statement the representative of Turkey pointed out that his country was essentially an agricultural country and that the economic development which had been in progress since 1950 was one of the most characteristic features of the Turkish economy. Until 1952, the policy of economic expansion had yielded excellent results in the field of trade. Between 1949 and 1952, exports had risen as much as 80 per cent and at the same time imports had increased to an exceptional degree. Unfortunately, exports did not rise at the same rate as imports and the drought years which Turkey had suffered since 1954 had further aggravated the situation. The disparity between domestic and international prices and in particular the slackening of trade in agricultural products had influenced exports unfavourably. The result was disequilibrium in the trade balance and balance of payments which in 1952 had led the Turkish Government to suspend the liberalization measures which it had been applying successfully since 1950.

13. From 1952 to the present time, Turkey's balance of payments had shown an annual deficit of about £T.500 million. The principal factors which led to the deterioration in the balance of payments had been: (a) a fall in exports since 1953; (b) a relative rise in imports since 1950, which was mainly due to the expansion of investment in the public and private sectors, to the population increases and also to the rising standard of living.

14. In view of the foregoing, the Turkish Government had taken certain measures in recent years with a view to stabilizing the internal situation and the country's balance of payments. Such measures could be summarized as

follows: (a) suspension of trade liberalization in 1952 and reinstatement of imports controls; (b) maintenance of budgetary equilibrium and reductions in public expenditure; (c) control of bank credit; (d) certain tax reforms; (e) investments, and (f) increased productivity.

15. The fiscal measures taken had consisted essentially in introducing a new tax on production to replace the transaction and consumption taxes, in raising the income tax, the taxes on inheritance and real estate, and in introducing the so-called "treasury tax". It was expected that these internal measures would yield a revenue of £T.500 million which would ensure budgetary equilibrium. The representative of Turkey also made reference to the law on the petroleum industry under which exemption from all taxes and internal charges is granted for equipment, tools, machinery and raw materials used for the construction and the operation of refineries. He also recalled that all such materials and equipment were free from all import duties and related taxes.

16. Among the monetary measures which might have a favourable influence on the balance-of-payments situation, the Turkish representative first mentioned the steps which had been taken in order to check the expansion of bank credit by establishing selective credit controls. A committee known as the "Committee for the Administration of Bank Credit" had been established as of 7 February 1956 and its main task was to promote a policy of selective credit in order to prevent the use of bank credit for speculative purposes, particularly in non-productive branches of activity. The Committee had taken a number of decisions, in particular:

(a) a credit ceiling had been fixed for banks;

(b) the utilization of liquid funds which were immobilized had been made compulsory;

(c) The use of credit for importation of consumer goods had been prohibited; and

(d) steps had been taken to prevent the banks from engaging in real estate transactions in order to avoid a reduction in their liquidities.

As a result of these measures, the volume of credit granted to the industrial sectors had increased considerably, while a decline had been recorded in the trade sector.

17. As regards long-term measures, the Turkish representative mentioned investments and the financing of economic development through credit made available in the budget. Such investments in favour of several sectors of the Turkish economy, and the resulting increase in industrial production had prevented a further deterioration of the trade deficit, notwithstanding a very sharp drop in agricultural production in the course of the last few years.

18. The representative of Turkey also stressed other measures which had been taken by his Government, including severe controls over the financial transactions of State enterprises, the tightening of price control measures, and the freezing of rents at the 1953 level.

19. As regards import restrictions which had had to be taken in the form of the re-imposition of the licensing system, the Turkish representative said that at the present time no change could be foreseen in his Government's policy. He made it clear, however, that in administering the existing system, due account was taken, in allocating foreign exchange within the limits of existing availabilities, of the following criteria:

(a) the essentiality of goods from the point of view of public health;

(b) whether the requests related to domestic production requirements;

(c) any special factors such as the wish to meet the needs of the people.

Although balance-of-payments difficulties had compelled the Turkish Government to suspend liberalization and to introduce quantitative restrictions, the Turkish Government nevertheless remained firmly attached to the principle of multilateral trading. Since deterioration had occurred in the balance of payments, it had endeavoured by all possible means not to reduce the volume of imports and very liberal consideration had always been given to applications for licences.

20. The Turkish representative then gave some indications as regards the balance-of-payments prospects for 1957. According to current estimates, the 1957 figures would exceed the 1956 levels. Such estimates were based in particular on the assumption that receipts from infra-structure equipment and off-shore purchases, as well as Commodity Credit Corporation procurements, would show a considerable increase. Export estimates in 1957 were very close to the 1956 export figure. Imports, on the other hand, tended to decline. As far as the area composition was concerned, figures for the first half of 1957 showed that both imports to and exports from the dollar area tended to increase. The Government was trying to maintain trade with EPU countries at the level reached in 1956. The Turkish representative then quoted a few figures relating to previous years and recalled that the balance-of-payments deficit as a whole was covered by the considerable assitance extended by the United States Government, by credit granted by the International Bank and the International Monetary Fund, by American surpluses and by import credit, as well as various other forms of assistance and credit.

21. In conluding, the representative of Turkey recalled that his country was addressing itself to the arduous and heavy task of creating a new infra-structure and economic framework. The major part of investments had not yet been fully carried out, but there was no doubt that when they had been concluded, they would have beneficial results on the Turkish balance of payments. At present, however, Turkey remained in balance-of-payments difficulties because of the heavy expenditure which had to be incurred in order to meet the needs of economic development and quantitative restrictions were therefore indispensable.

22. A member of the Working Party thanked the Turkish delegation for the very complete and detailed information it had been good enough to supply and said that he recognized the serious nature of the Turkish balance-of-payments difficulties. He did not wish therefore to urge that Turkey should alleviate the existing system of restrictions. He was pleased to see that the Turkish Government had taken internal measures of a fiscal and monetary nature, and expressed the hope that these measures would remedy the present situation. He also recognized the difficulties which Turkey was encountering as a result of the disparity existing between internal prices and prices on world markets. As to the tax alleviation measures in favour of certain industries, such as the petroleum industry, he expressed the hope that they would lead to a reduction in costs for the industry concerned. In this connexion he asked whether the tax alleviation measures concerned could also be applied to other industries. In reply the representative of Turkey stated that for the time being tax alleviation measures were applicable only to the petroleum industry. Similar measures had been taken previously in respect of agricultural machinery, but had been rescinded when they were no longer justified. The Turkish representative added, however, that if the need arose, further such exemptions could possibly be granted.

23. Another member of the Working Party said that he also appreciated the detailed and extensive statement by the representative of Turkey. He stressed that the serious difficulties with which the Turkish Government was confronted warranted a frank and constructive exchange of views. He then made a few observations on the following two fundamental problems;

(a) There was in Turkey an excessive internal demand as a result of the economic development plan. This acted as an export disincentive to the extent that domestic outlets could easily be found. The Turkish Government had therefore adopted certain measures to counteract these difficulties.

(b) Another difficulty resulted from the disparity between domestic and international prices. As a consequence, even when there was a desire to export, the question of prices raised additional difficulties. It also tended to stimulate imports.

These combined factors worked to intensify the balance-of-payments problems and made it the more difficult to restore trade on a multilateral basis. This member also noted with pleasure the assurances given by the Turkish delegate concerning his Government's desire to progress towards greater trade multilateralism and welcomed the measures thus far taken by Turkey to reduce monetary circulation, thereby working towards deflating internal demand.

24. A member of the Working Party noted with pleasure that Turkey had engaged in a very extensive plan for economic development. Naturally, this had repercussions on the balance-of-payments situation but not on the total value of the external trade of Turkey, in view of the fact that as a consequence part of the exchange availabilities were directed to meet the needs of economic development rather than the ordinary requirements of the domestic economy. In other words, the existing situation brought about an increase in imports of capital goods to the detriment of consumer goods. This led the member in question to ask whether the investment policy of Turkey was liberal enough to attract foreign capital and whether it favoured economic development, considering that internal demand was steadily growing and that the Turkish population was increasing. The representative of Turkey stressed in reply that this was a very important question for his country and that inflow of foreign capital was considerably facilitated. He mentioned that the relevant legislation was very liberal.

25. In connexion with the same question one member of the Working Party asked the Turkish delegation whether it could give an indication as to those sectors of Turkish economy where foreign investment would be welcome. In response to this question the representative of Turkey read out the text of Article I of the Law of 18 January 1954, which encourages inflow of foreign capital. This Article reads as follows: "This law applies to foreign capital to be imported to Turkey and to loans to be floated abroad under the relevant Decision taken by the Committee for the promotion of foreign investments, in accordance with Decisions by the Council of Ministers; provided that the undertaking for which investment is intended: (a) should work towards the economic development of the country; (b) should operate in a field of production to which Turkish undertakings have access; and (c) should not involve any monopoly or special privileges". He added that such provisions, the purpose of which was to encourage inflow of foreign capital, had been supplemented by two agreements signed with the Government of the United States concerning (1) transfer guarantees, and (2) guarantees against expropriation and confiscation. Another agreement on war risks was under discussion.

Alternative measures to restore equilibrium

26. Commenting on certain information included in the IMF paper, a member of the Working Party pointed out that 1956 had shown improvements in certain sectors in Turkey but that there had also been an intensification of inflationary trends. He recalled that the budgetary deficit was still very large and that the increase in prices, although less marked than in 1955, was continuing. This situation had resulted in an increase in monetary circulation and the Turkish Government therefore had to face a serious situation, since on the one hand it had fewer resources available to finance imports, and on the other hand the amount of money in circulation had increased. In those circumstances, this member of the Working Party said that he would like to be informed of the prospects for 1957 regarding the deficit of State enterprises. The Turkish representative declared that the Committee to encourage foreign capital inflow, to which he had already referred, exercised strict control in the field of

public investment, and that no programme of this type was accepted unless the budget of the department included sufficient provision to cover the expenditure involved, without any decisions of an inflationary nature having to be taken.

27. With regard to point 7 of the plan for the consultations, a member of the Working Party asked to what extent the Turkish authorities had considered the possibility of reducing the degree of discrimination which existed in import controls in order to improve the competitive power of certain sectors, in the light of the fact that the European currencies were becoming increasingly hard. In his opinion there was a considerable degree of discrimination in Turkish trade, which favoured particularly imports from the EPU countries and imports under bilateral agreements. He therefore asked whether it could not be in the interest of the Turkish Government to reduce the degree of the discrimination in view of the fact that importers of raw materials and machinery would reap the benefit of more favourable price conditions offered by other supplying countries. The Turkish delegate stated in reply that he did not believe that his country's foreign trade system discriminated between, on the one hand, imports from the dollar area, and on the other hand, imports from EPU countries or under clearing agreements. He reminded the Working Party that in order to import, Turkey had to export, as she relied mostly on her export earnings for the settlement of imports. Referring to capital goods, he pointed out that those were imported from EPU countries under economic co-operation agreements which provided for multilateral credit arrangements. He added that capital equipment was also imported from the United States, though perhaps to a lesser extent, and that such imports were financed by means of United States assistance. In each case, however, Turkey had always been guided by the amount of her foreign exchange availabilities, and therefore if there was any discrimination, this was due solely to the existence or the lack of the necessary means of payment; if the latter was lacking the Turkish authorities could not issue licences. The same was true of imports of consumer goods for which the Turkish authorities had to take into account exchange availabilities in respect of the EPU area as a whole, in view of the fact that at the end of each month any deficit had to be settled in gold or dollars. Imports from countries with which Turkey had bilateral agreements were effected under such agreements in accordance with the provisions thereof within the framework of existing arrangements. The Turkish delegate concluded that if there was any discrimination, such discrimination was not intended. Furthermore, he mentioned that, after the Turkish Government had learned that Canada was supplying capital equipment to certain Asian countries under long-term credit arrangements, the Turkish Embassy in Ottawa had contacted the Canadian Government in order to ascertain whether closer economic co-operation could be established between the two countries.

28. The member of the Working Party who had raised this point stated that his question had not been directed previously to the problem of discrimination in Turkey, but that his intention was rather to ascertain whether that country had taken into consideration the price advantages, particularly with regard to raw materials and capital equipment, which the national economy would reap from an increased

liberalization of imports. The Turkish representative replied that his Government attached great importance to the question of prices, and that a special committee supervised such matters. That committee frequently had to consider complaints from Turkey's trading partners who wanted to sell their products at prices higher than those prevailing on world markets.

29. A member of the Working Party drew attention to the fact that Turkey's economic development resulted not only in greater utilization of manpower, but also in increased imports of raw materials. The need for increased imports, in turn, resulted in additional demands on the balance of payments. If, however, Turkey were to import finished products manufactured from the same raw materials, the cost of imports would be even higher than at present. There was therefore some saving, in spite of the increased expenditure resulting from the industrial development programme. In connexion with this problem, this member of the Working Party asked whether the Turkish delegation could give an indication of the amount of the saving. In his reply, the Turkish representative recalled that his country's economy was essentially agricultural. Industrialization had been introduced, but on a relatively modest scale. For the time being, therefore, the administration did not intend to make Turkey an important competitor on world markets of industrial products, and only the first step towards industrialization was being made. Progress in that direction was dependent on the credit and assistance which his country would receive, and in those circumstances Turkey had to conform to certain criteria set by the United States, the IMF, other international institutions and the countries granting credit. The guiding principle at present was to establish in Turkey industries which could utilize Turkish raw materials and could therefore be placed on a paying basis within a very short time. That would make it possible to reduce imports and save foreign exchange, which could then be used elsewhere. Wider plans for industrialization could only be envisaged at a later stage.

30. In connexion with problems resulting from Turkey's rapid rate of population increase, a member of the Working Party enquired whether the present level of investment was sufficient to absorb the extra manpower, or whether increased investment would be required for that purpose. He asked whether that manpower surplus had employment possibilities in agriculture, or whether, on the contrary, as a result of increased productivity and the market situation, agriculture had attained such a degree of stability, from the point of view of employment, that this surplus manpower would have to be employed in industry. The Turkish representative reminded the Working Party that the Turkish population was currently increasing at the rate of 3 per cent per annum. Since there was at present under-employment in agriculture, that sector of the Turkish economy could absorb part of the surplus manpower, but not all, and therefore industry would have to absorb part. Having regard to this situation, the present level of investment was adequate. However, it was possible that in the future it might be necessary to set up new industries if the rate of population increase was maintained. The Turkish representative added, however, that his country could not move too fast in that field, nor could it continue to invest indefinitely.

31. With regard to the question raised in the preceding paragraph, the same member of the Working Party asked the IMF representative a question of a general nature. In particular, he asked whether, in examining the adequacy of the level of a country's monetary reserves, the Fund took account first of the volume of trade, or if it also took into consideration the rate of population increase. In his reply, the IMF representative stated that in considering the situation of a given country, the Fund took into account all factors which might affect the balance of payments and the country's requirements for monetary reserves. Those factors included the rate of population increase and also investment programmes. He also recalled that, in the case of Turkey, the Fund had taken this aspect of the problem into account. As an illustration he quoted the passage in the background paper supplied by the Fund which states: "As a result of these developments, and of the significant rise in population, the per capita income has not increased since 1953. The Turkish population (24.1 million in 1955) increases annually at a net rate of 2 per cent, representing an estimated increase of some 480,000 persons in 1956." At the request of a member of the Working Party and in order to avoid any confusion in the figures, the Turkish representative indicated that the present rate of population increase was 3 per cent, representing about 750,000 inhabitants per annum.

System and methods of restriction

32. A member of the Working Party stated that, while recognizing the difficulties which Turkey had to face, he wished to make a few comments concerning the thorough network of bilateral agreements in that country's foreign trade system. He expressed the hope that in the near future progress would be made towards the establishment of a multilateral system. He emphasized that bilateralism was particularly a cause for concern when associated with the settlement of a high level of short-term debts and arrears, as this prevented the free utilization of export receipts. This system also had the disadvantage of resulting in higher production costs and prices, which, in turn, had a harmful effect on exports and by this very fact led to the diversion of trade. In connexion with this statement another member of the Working Party stated that trade between Turkey and countries which did not have bilateral agreements with Turkey was being affected adversely. As was mentioned in the basic document prepared by the secretariat, he recalled that Turkey had concluded many bilateral agreements with certain countries in order, in particular, to settle outstanding commercial debts.

However, some countries which wished to see outstanding commercial debts settled were not anxious to enter into bilateral agreements. On the one hand the existence of a complicated network of bilateral agreements concluded by Turkey, and on the other hand the fact that there was no agreement of this type between Turkey and other countries had the following consequences: (a) in order to avoid certain risks, exporters in these countries had been cautious in their trade with Turkey; (b) the absence of bilateral agreements had affected imports from Turkey because many of Turkey's more competitive exports were occuring for the most part under bilateral agreements;

(c) such countries export trade with countries other than Turkey had also been affected because of the existence of those bilateral agreements which had the affect of pre-empting overseas markets in some degree for certain products. Replying to this statement, the Turkish representative pointed out that those agreements which Turkey had concluded with certain countries of the EPU were, in fact, payment protocols which were intended to make possible increased exports of certain Turkish agricultural products to those countries. He added, however, that those exports were not of very great significance for those countries, but they were very important for the Turkish economy. In support of his statement he quoted the following statistics: Turkish exports to the United Kingdom represented 30 per cent of Turkey's total exports to the EPU area, while in the United Kingdom's trade balance the corresponding imports only accounted for 0.22 per cent of total imports. Similarly, imported Turkish products only accounted for 3 per cent of the total imports of the EPU countries. Considering these figures, the Turkish representative found it difficult to admit that the situation could have harmed the interests of other countries.

33. A lengthy discussion took place in the Working Party regarding the problem of bilateralism which had thus been raised. One member expressed his satisfaction at seeing that the Turkish Government wished to follow a multilateral policy, but at the same time he pointed out the difficulties which the implementation of such a policy was meeting with countries which, like Turkey, were in the process of economic development always had special difficulties in maintaining the balance of payments. Those difficulties included the following: (a) the reserves available were not adequate to maintain a certain standard of living which was usually already very low; (b) the requirements of economic development caused pressure on foreign exchange reserves, which were already inadequate; (c) exports of those countries were usually subject to seasonal fluctuations and were in many cases affected by drought, floods and other calamities. He had been happy to note that the Working Party had taken those factors into consideration in examining the case of Turkey. Nevertheless, some members of the Working Party had pointed out that in that country there still existed a number of measures, and, in particular, the network of bilateral agreements, which did not conform to the philosophy of the General Agreement. This member of the Working Party recognized that bilateralism was not a desirable system, but on condition that competition be open to all countries and that there was monetary convertibility. That unfortunately was not the case. Imports and exports were not entirely free, certain countries accumulated reserves in non-convertible currencies, and other countries only had access to markets by means of bilateralism. That being so, bilateral agreements presented certain advantages to those countries and it was sometimes useful, and even essential, to conclude them. Another member of the Working Party, stated that, in his view, even countries faced with serious balance-of-payments difficulties would want to weigh carefully the long-term disadvantages against the apparent short-term advantages of those agreements. He considered that this system could not result in the establishment of a sound economy or in a higher

standard of living. With regard to the two contrary theories which had thus been expounded, a third member of the Working Party stated that, in his view, there was an intermediate solution: the conclusion of arrangements regarding primary products. In the case of Turkey, for instance, it seemed to him that price and market stability for cotton was an essential factor for the restoration of that country's balance of payments. In that connexion he noted that the United States were making praiseworthy efforts, which had met with great success, to maintain cotton prices at a remunerative level; that policy of the United States had a greater effect on Turkey's economic position than all the latter country was doing or could do alone. That was a good example of a case in which action by one country contributed greatly to another country's situation, and it illustrated the advantage of collective action in such matters. This member of the Working Party then asked if it would not be useful to recall during the consultations that the prospects for improving the balance of payments, and consequently the return to trade liberalization, depended to a great extent on the level and stability of the prices of raw materials exported by those countries.

34. Referring to the network of bilateral agreements which his country had concluded, the Turkish representative again recalled that those measures were only of a temporary nature, and his Government was resolved to follow a multilateral policy as soon as possible. That intention had already been put into effect in the framework of OEEC where his Government had recently announced that it would participate in the setting up of the European free-trade area, as well as in the Economic Committee of the countries belonging to the Baghdad Pact, which was also studying the possibility of establishing a free-trade area between those countries. Those were the first two steps which the Government had made towards a more multilateral system. He recognized that the question of the level and stability of prices of agricultural products was of interest to his country; for the time being his Government was endeavouring to keep Turkish prices in line with world prices. That policy entailed certain sacrifices, but those sacrifices had been accepted during the current transitional period. For the time being the most pressing problem was, nevertheless, that of production, which had to be increased to the greatest extent possible.

35. A member of the Working Party pointed out that imports under long-term credit arrangements were only allowed if certain conditions were met; one such condition was that the credit must be for at least one year. In his view, such a policy favours tied loans which hampered free competition and gave an advantage to the exporting countries which granted the longest credit. As his own country was not in a position to compete on such terms, he feared that the system might have harmful effects on its export trade towards Turkey. He also asked if, once the requirements were fulfilled, authorization to transfer foreign exchange was automatically given. In reply, the Turkish representative pointed out that the system applied principally to imports of equipment goods. The minimum one-year period seemed to him a normal requirement, paricularly in view of the fact that the Turkish Government did not have sufficient funds

at its disposal to permit the issue of licences for imports under very short-term credit arrangements. Those imports of equipment goods were necessary and could only be increased if Turkey enjoyed long- and medium-term credit facilities. In any case, the system was not discriminatory in any way, it was a case of provisional arrangements which had had to be made in view of current difficulties. In reply to the second question, the Turkish representative stated that once the licence had been granted, transfer authorizations were granted automatically when instalment payment became due. By way of further information, he indicated that the country of the delegate who had raised the question had recently made available to Turkey a credit of $1 million to finance imports of certain equipment goods, and the establishment of a chemical industry in Turkey was being discussed.

36. A member of the Working Party asked whether imports financed out of the economic assistance funds granted by the United States Government could come from any contracting party, or if certain conditions and limitations were imposed by the country providing those funds. The Turkish representative replied that the terms of the United States aid had provided that such imports may be allowed from any country.

Effects on Trade

37. A member of the Working Party asked if the Turkish authorities took advantage of every opportunity to remind those concerned that the quantitative restrictions at present in force were of a temporary nature. The Turkish representative replied in the affirmative, and cited several examples. In the first place, Turkey maintained the OEEC liberalization list in its foreign trade system. For the time being, that list was not applied, but the fact of its existence drew the attention of all concerned to the fact that it might be applied at any moment. The Turkish representative also reminded the Working Party that the question of the application of the list was examined each year by OEEC, and the Chambers of Commerce and Industry were kept informed of the decisions taken by that organization. With reference to the work which was under way in OEEC and in the Economic Committee of the Baghdad Pact countries regarding the establishment of free-trade areas, the Turkish representative mentioned that one or two representatives of the Chamber of Commerce and Industry were always invited to attend the preparatory discussions as observers: in that way, the private sector was kept informed of the difficulties which it would have to face. From the practical point of view, the Turkish representative pointed out that new industries had been established in the country, and from time to time the authorities granted import licences for goods produced by those industries, not to meet domestic needs, but rather in order to maintain those industries in a state of alertness and to impress it upon them that they might feel the wind of open competition at any time.

General

38. Concluding the consultation with Turkey, several members of the Working Party expressed their satisfaction with the very detailed statement made by the Turkish delegation at the beginning of the discussion. They also thanked the

Turkish representative for his very clear and detailed replies to the many questions which had been asked. Several members also recorded their appreciation of the fact that Turkey had decided to take part in the consultations. The Working Party wished the Turkish Government much success in its endeavours to restore the country's economy, and expressed the hope that the results of those endeavours would soon become apparent and that, as the delegation had not failed to point out, Turkey would then be able to move towards a multilateral system and a greater degree of trade liberalization. The consultations had achieved its objective since it had led to a better understanding of the problems with which Turkey was faced and of that country's policy. The Chairman of the Working Party also thanked the Turkish delegation for the co-operation and readiness which it had shown during the consultation.

39. The Turkish representative congratulated the Chairman on the way in which he had conducted the discussions, and said that he was overwhelmed by the friendly way in which the Working Party had consulted with his delegation; he was happy to have been able, by replying to questions that had been asked, to throw additional light on his country's very complex foreign trade system. He added that he hoped at a future consultation to be able to announce to the Working Party that more liberal trade measures had been introduced.

ANNEX I

There are two basic documents for your consideration to-day of problems concerning Turkey's exchange control and foreign trade control systems, and other related questions; one of these documents has been prepared by the International Monetary Fund, and the other by the GATT secretariat.

The report by the Fund is the result of the consultations which took place in Ankara a few months ago between the Turkish Government and the Fund representatives, and it deals in all necessary detail with the problems which may also be of interest to GATT. From the point of view of presentation, this report is perhaps not completely in accordance with the GATT plan for the consultations, in particular with regard to the table of contents.

Considering this, and in order to give more detailed information on the problems as a whole, the Turkish delegation will make a further statement to supplement the information contained in the report regarding the points which are of particular interest to GATT.

The second document, prepared by the secretariat, sets forth the system and methods of the restrictions which are applied in Turkey, and their effect on trade; a list of valid decrees and lists is also included.

We can congratulate Mr. Doig and Mr. Arents for their work on behalf of the secretariat. This comprehensive document, which is available in English and in French, will not only be very useful for the GATT but will also be considered as a valuable acquisition by the Turkish departments which deal with such questions.

At first sight these two documents have perhaps given you the impression that the system in force in Turkey is rather complicated and complex and could not easily be implemented for that reason. Perhaps I should admit now that the Turkish Government also has that impression. But in order better to understand the reasons which lead the Turkish authorities to adopt such a system, would it not be better to take into account first of all the vital problems of economic recovery and economic development which are of such concern to the Turkish Government.

Turkey believes sincerely in the notion of free trade and in the necessity and value of multilateral co-operation, as well as in the liberalization of trade and payments, and is resolved to adhere to the principles of the GATT. But there are other preoccupations which for the time being prevent Turkey from making all the progress which it would desire. These preoccupations stem from the Turkish Government's firm determination to overcome Turkey's present balance-of-payments difficulties, to achieve a substantial expansion in national production and productivity, to secure for the Turkish people a satisfactory standard of living and adequate purchasing power, to provide employment for the ever-increasing labour force, and to achieve full internal economic and financial stability.

Turkey has tremendous untapped reserves, mineral wealth, and an active demographic potential which increases by almost 1,000,000 inhabitants each year, and there is, therefore, every reason why it may well become in the near future one of the most interesting markets for its trading partners. Pending the realization of these objectives, the Turkish Government has found it necessary to maintain the present system for some time yet to come. The vital recovery programme can only be carried out at the cost of certain sacrifices which the Turkish people is prepared to accept during a well defined period of transition. Such a period of controls and restriction is therefore necessary for a country which, like Turkey, has no other foreign exchange receipt than export proceeds. The system currently enforced is a sort of combination, on the one hand, of essential restrictions and controls, and, on the other hand, of measures which reflect the Turkish Government's support of more liberal principles. As you will see, despite existing difficulties, Turkey has resorted to restrictive measures whenever there was no alternative, and, at the same time and on each occasion, has not failed to demonstrate through its restrictive systems its intention of moving towards a much more liberal system. The essential features of the system may be summarized as follows:

This is a transitional period; the non-discriminatory restrictions which are applied to-day can be considered to be temporary, since they will only serve to pave the way for the creation of a sound, viable, powerful and profitable national economy, which will enable Turkey to play in world markets its rightful constructive part within a free, multilateral trading system.

The Turkish delegation has come to Geneva for these consultations with the firm conviction that our GATT partners will show understanding, and with the comforting hope of receiving as much support and assistance from them in order to fulfil the legitimate and constructive objectives which the Turkish Government has set itself.

We believe sincerely that if there are difficulties, they can only be resolved through mutual understanding of our problems and through close economic and trade co-operation.

Our objective is to bring about some day a far-reaching and continuing multilateral system and, therefore, the problems which concern one or other of us are in a sense, and at the same time, problems of concern to other countries; the strength of the economic potential of that country is an integral part of the common potential.

After this general statement, the Turkish delegation is prepared to make a statement on individual questions, and in particular on questions relating to Turkey's balance-of-payments and financial problems.

My delegation is also ready to meet to the fullest extent possible any requests for additional information which representatives may wish to make.

ANNEX II

Turkey's balance-of-payments position must be examined in the light of the structural development of the Turkish economy since 1950, and in particular in the light of the consequences of the economic development policy which Turkey has pursued for the last few years.

1. Turkey is essentially an agricultural country. Agricultural products account for 87 per cent of exports, and 8[illegible] per cent of the population derive their livelihood from agriculture.

2. Furthermore, one of the most characteristic features of the Turkish economy is the economic development which has been in progress since 1950. In order to diversify Turkey's economy through the co-ordinated development of natural resources, it was considered necessary to follow a policy of economic expansion which will at the same time raise the standard of living of the Turkish population, which increases by about 750,000 inhabitants each year.

3. Up until 1952 this policy of economic expansion yielded excellent results, particularly in the field of trade. Between 1949 and 1952 exports rose by as much as 80 per cent. At the same time Turkey's imports increased to an exceptional degree. Turkey entered the world market with new export products such as wheat and cotton, which had hitherto only been traded on the domestic market. However, contrary to expectations, exports did not rise at the same rate as imports. The drought years which Turkey has suffered since 1954 aggravated this situation further and hampered the export drive, thus making it impossible to reach the export target. Without going into details, it may be said that the disparity between domestic and international prices, and above all the slackening in trade in agricultural products, had unfavourable influence on exports, as is the case in all countries in the process of economic development. The result was disequilibrium in the trade balance and balance of payments, which in 1952 led the Turkish Government to suspend the liberalization measures which it had been applying successfully since 1950.

4. Government and private investments led to increased imports. Among the factors which brought about an increase in the volume of imports, one may mention first of all the exceptionally high rate of increase in income and investments, as well as the growth of population already referred to. This rise in income, which represented increased purchasing power, was used in particular for the purchase of various capital and consumer goods abroad. The rapid expansion of the trade volume coincided with the application of liberalization measures. At the time when the Turkish Government decided to suspend liberalization, the balance-of-payments deficit was tending to become structural.

5. From 1952 to the present time, Turkey's balance of payments has shown an annual deficit of about 500 million Turkish pounds. More detailed information concerning the 1956 financial year and the outlook for 1957 will be given later.

6. The factors which led to the deterioration in the balance of payments, and to which reference has already been made, are briefly as follows:

(a) a fall in exports since 1953;

(b) a relative rise in imports as compared with exports; since 1950 we have noted a very marked annual increase in imports although the import level remains far below the country's needs and has suffered a net decline in the last few years. This relative rise is mainly due to the expansion of investment in the public and private sectors, to the population increase, and also to the rising standard of living.

7. In view of the foregoing, and also because no economic expansion can be achieved unless a solution is found to the balance-of-payments deficit either by means of investments of foreign capital or by long-term credit, the Turksih Government has taken certain measures in recent years with a view to stabilizing the internal financial situation and the balance of payments.

8. These measures which affect in particular budget, trade, monetary and fiscal questions, may be summarized as follows:

(a) suspension of trade liberalization in 1952, reinstatement of import controls,
additional measures to control exchange and import prices;

(b) maintenance of budgetary equilibrium,
reductions in public expenditure;

(c) control of bank credit to prevent any increase in the volume of credit;

(d) certain tax reforms;

(e) investments; and

(f) increased productivity.

Among the measures intended to improve the balance-of-payments situation, I wish to make particular reference to action taken in the fiscal and monetary fields.

Fiscal measures

The fiscal measures taken have consisted essentially in introducing a new tax on production to replace the transaction and consumption taxes, in raising the income tax, the taxes on inheritance and real estate and in introducing the so-called Treasury tax. It is expected that these internal measures will yield a revenue of 500 million Turkish pounds, which will ensure budgetary equilibrium. The new production tax will encourage productivity and will indirectly have beneficial effects on the balance of payments. Other legislative provisions applicable to certain branches of industry, such as the petroleum industry, for instance, provide for tax exemption on machinery, plant equipment and complete installations. The law on the petroleum industry grants exemption from all

taxes and internal charges for equipment, tools, machinery and raw materials used for the construction and operation of refineries. All such materials and equipment are also free from all import duties and related taxes.

Monetary measures

Among the monetary measures which may have a favourable influence on the balance of payments, reference may first be made to the steps which have been taken in order to check the expansion of bank credit by establishing selective credit controls. By a decree dated 7 February 1956, a committee known as the "Committee for the Administration of Bank Credit" was established. Its main task is to promote a policy of selective credit in order to prevent the use of bank credit for speculative purposes, particularly in non-productive branches of activity. This Committee also makes credit available depending upon production requirements and productivity in the various economic sectors. The following are some of the decisions which this Committee has taken:

(a) a credit ceiling has been fixed for banks;

(b) the utilization of liquid funds which are immobilized has been made compulsory;

(c) the use of credit for importations of consumer goods has been prohibited; and

(d) steps have been taken to prevent the banks from engaging in real estate transactions in order to avoid a reduction in their liquidities.

These new regulations, which provide for both quantitative and selective restrictions on credit, have so far yielded appreciable results. As a result of these measures the volume of credit granted to the industrial and agricultural sectors has increased considerably, while a decline has been recorded in the trade sector. The annual increase in the amount of credit granted by the Central Bank of the Turkish Republic was about 761 million Turkish pounds in 1955, but the 1956 figure did not exceed 620 million. Furthermore, the rediscount rate was raised from 4.5 per cent to 6 per cent in 1956 in order to check the rate of monetary and credit expansion. A number of other legislative measures are also under consideration, and the relevant bill which provides for a certain flexibility in the rate of interest and is intended to encourage private savings has been submitted to the Turkish National Assembly.

Long-term measures

As regards long-term measures mention should first be made of investments and the financing of economic development. With regard to investments, credit made available in the budget for 1955, 1956 and 1957 amounts to 3,156 million Turkish pounds, representing more than $ 1,000 million. This credit has been used for the following sectors in particular: industry, mining, energy, agriculture, transport and public works. Such investments, and the resulting

increases in industrial production prevented a further deterioration of the trade deficit, notwithstanding a very sharp drop in agricultural production in the course of the last few years. The following measures have also been taken:

(a) severe controls over the financial transactions of State enterprises (tightening of price control measures and particularly in the whole trade sector);

(b) rents have been frozen at the 1953 level. These measures have had favourable effects on prices in general;

(c) an increase in the retail price and cost of services by enterprises in the public sector.

The situation which I have just outlined led my Government to restrict imports by placing them under licence. At the present time no change can be foreseen in the policy governing the application of these restrictions. The intention is not at present to make any change in the administrative structure of the regulations. In administering the existing system, the following criteria are taken particularly into account in allocating foreign exchange for imports, within the limits of existing availabilities:

(a) the essentiality of goods from the point of view of fuller health;

(b) whether the requests relate to domestic production requirements;

(c) any special factors such as the wish to meet the needs of the people.

Although balance-of-payments difficulties have compelled my Government to suspend liberalization and to introduce quantitative restrictions, it remained nevertheless firmly attached to the principle of multilateral trading. In fact, since deterioration occurred in the balance of payments, the Government has endeavoured by all possible means not to reduce the volume of imports and very liberal consideration has always been given to applications for licences. As in the past, the Turkish Government endeavours to direct its foreign trade towards the European Payments Union countries and the dollar area.

Balance of Payments Prospects for 1957

Statistics regarding the Turkish balance of payments in the first half of 1957 are not yet final. According to estimates, however, they should reach a higher level than in 1956. Such estimates are based in particular on the assumption that receipts from infra-structure equipment and off-shore purchases, as well as Commodity Credit Corporation procurements, would show a considerable increase. Export estimates in 1957 are very close to the 1956 export figures. Imports, on the other hand, tend to decline. It is hoped, however, that in the second half of the year, imports will show an increase to balance the drop in the first half of the year. According to figures available for the first half of the current year, both imports to and exports from the dollar area tend to increase. The Government is trying to maintain trade with EPU countries at

the level reached last year. In 1956 the value of foreign trade reached 1,939 million Turkish pounds, while a deficit of some 230 million Turkish pounds was recorded in the trade balance. In 1955, these amounts were respectively 2,210 million Turkish pounds and 456 million Turkish pounds. As can be seen from these figures, the trade deficit fell by 50 per cent as compared with the preceding year. This reduction of the balance-of-payments deficit is accounted for by the actual fall in the volume of imports. In 1956 the value of exports dropped by about 23 million Turkish pounds, principally on account of a fall in exports of cotton and hazelnuts. The tightening of import restrictions has affected mainly the following sectors of the domestic economy: textiles, iron and steel, machinery and cement, liquid fuels, chemicals, coffee, etc. and other consumer goods.

The balance-of-payments deficit as a whole is covered by the considerable assistance extended by the United States Government, by credit granted by the International Bank and the International Monetary Fund, by American surpluses, by import credit as well as by various other forms of assistance and credit.

Turkey which is a country in the process of economic development, has, particularly since 1950, addressed itself to the arduous and heavy task of creating a new infra-structure and economic framework. The major part of investments have not yet been fully carried out, but there is no doubt that when they have been completed they will have beneficial results on our balance of payments. At the present time, however, because of the heavy expenditure which is necessary in order to meet the needs of economic development, Turkey is in balance-of-payments difficulties. For the time being, quantitative restrictions are indispensable to meet such difficulties. Consequently, the progressive elimination of such restrictions can only begin as and when the balance of payments is being restored to normal.

H. CONSULTATION WITH JAPAN

1. In accordance with the Decision taken at the plenary meeting of the CONTRACTING PARTIES on 17 November 1956, the Working Party has conducted the consultation with Japan under paragraph 4(b) of Article XII.

2. The Working Party had before it:

(a) a basic document prepared by the secretariat in collaboration with the Japanese authorities describing the system and methods of the balance-of-payments import restrictions in operation in Japan. The document also contains a statement under Part II, "Effects on Trade", submitted by the Japanese authorities.

(b) documents provided by the International Monetary Fund.

3. In conducting the consultation the Working Party followed the Plan recommended by the CONTRACTING PARTIES for the consultations. The present report summarizes the main points of the discussion during the consultation.

Consultation with the International Monetary Fund

4. 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 Japan. As a part of the consultation between the CONTRACTING PARTIES and the Fund, the latter had transmitted the results and the background material from its consultation with Japan concluded on 16 October 1957.

5. In accordance with the procedure agreed upon by the Working Party the representative of the Fund was invited to make a statement supplementing the Fund's documentation concerning the position of Japan. The statement made was as follows:

"The International Monetary Fund has transmitted to the CONTRACTING PARTIES the results and background material from the last consultation with Japan under Article XIV of the Fund Agreement, which consultation was concluded on October 16, 1957.

"With respect to Section I of the Plan for Consultations, relating to balance-of-payments position and prospects, the Fund draws the attention of the CONTRACTING PARTIES to the results of its recent consultation with Japan under Article XIV of the Fund Agreement, and particularly to paragraph 2, and to paragraph 4 which reads as follows:

> '4. The Fund welcomes the fact that Japan, before the balance of payments difficulties set in, made considerable progress in relaxing restrictions and reducing their discriminatory and bilateral aspects. Recently there has been a reduction of exchange allocations for imports. The Fund hopes that progress in reducing discrimination and bilateralism will continue, and that progress in reducing restrictions will be resumed as soon as practicable.'

"With respect to Section II of the Plan, relating to alternative measures to restore equilibrium, the attention of the Working Party is drawn to the results of the last Fund consultation with Japan. The Fund has no additional alternative measures to suggest at this time."

Opening Statement by the Representative of Japan

6. The full text of the opening statement of the Japanese representative is attached to this report as Annex I, and is summarized in the following paragraphs.

7. The Japanese representative said he would like to make a statement on the basic features of the Japanese economy and on the principles of their import control, to supplement the documentation already circulated. Considering her enormous population, Japan was poorly endowed with natural resources and had to import 100 per cent of her requirements of raw cotton, raw wool, crude rubber, phosphate rock, bauxite and potassic salt, 80 per cent to 95 per cent of sugar, crude oil and iron ore, 60 to 80 per cent of soya beans, wheat, hides and salt. The imports of foodstuffs and raw materials represented more than 70 per cent of total imports. It was accordingly most essential for Japan to promote her exports to pay for imports. Though Japan's production had increased considerably since the war, her exports were still far below their pre-war level. The imbalance between imports and exports had hitherto been covered by receipts from procurements by foreign troops in Japan.

8. The basic trade control policy of Japan was, so far as the economic situation permitted, to pursue the aims of the Foreign Exchange and Foreign Trade Control Law, namely "the proper development of foreign trade and the safeguarding of the balance of payments and the stability of the currency, as well as the most economic and beneficial use of foreign currency funds, with a view to rehabilitating and expanding the Economy". He emphasized the fact that the Law

expressly stated that "the provisions of this law and of orders issued thereunder shall be reviewed with the objective of gradually relaxing and eliminating the restrictions as the need for them declines".

9. During the past few years the Japanese Government has taken measures for trade liberalization including expansion of the Automatic Approval System, enlargement of global quotas, abolition of open account arrangements, reduction in the so-called "retention quota" under the Special Foreign Exchange Allocation System, and simplification of foreign exchange control procedures for visible and invisible trade. These measures had had significant effects in regard to liberalization, and he gave figures to demonstrate these points. The policy of abolishing open account arrangements would be pursued in future, as far as circumstances permitted. Japan tried to accord non-discriminatory treatment to her trade partners; it was hoped that this treatment would be reciprocated. The Link System had now been limited to certain raw materials only.

10. The economic situation had changed in 1957, when Japan found herself confronted with a crisis in the balance of payments, with a deficit of $ 542 million during January-June 1957. To cope with this situation the Japanese Government, instead of resorting to an intensification of import restrictions, had adopted internal monetary and fiscal measures from March 1957 such as: raising the Bank of Japan's official interest rate, raising commercial banks' lending rates and interest rates on time deposits; restrictions of loans by the Bank of Japan; postponement of 15 per cent of public investment and Government loans; curtailment of loans by commercial banks for private investment; increase of the advance deposit required for obtaining import licences.

11. As these measures would require some time before their effects were fully felt, the Japanese Government had applied to the International Monetary Fund and the Export-Import Bank for short-term credits, and in June a purchase of $ 125 million had been authorized by the IMF and in August a credit of $ 175 million had been granted by the Export-Import Bank (of which $ 60 million was a renewal of the credit for the previous year on revised conditions).

12. Despite the difficulties in the payments position, import restrictions had not been intensified; for the first half of the fiscal year 1957 the amount used under the Automatic Approval System was $ 447 million (covering 595 items) or 25.9 per cent of the total exchange budget, an increase over 1956 in both the number of items and the percentage of the total amount. For the budget under the Foreign Exchange Allocation System, the amount for global quotas accounted for 67.9 per cent of the total budget for imports, and the amount for single quotas represented 6.2 per cent. Compared with 1956 figures the percentage under global quotas increased, while that for single quotas decreased.

13. The foreign exchange budget for the second half of the 1957 fiscal year showed a slight decrease compared with that of the preceding period. Because of the internal measures taken, domestic production had been gradually declining, and growing stockpiles of imported raw materials, due to a sharp increase in imports in 1956 and the early part of 1957, had resulted in a considerable decrease in domestic demand for imports. The foreign exchange budget for the latter half of 1957 was expected to meet the requirements of domestic industries.

14. Concerning the prospects for the balance of payments in the immediate future, the Japanese representative stated Japan expected to reach equilibrium in the latter half of the 1957 fiscal year. Exports were expected to expand gradually, as domestic demand fell, and as goods were diverted towards overseas markets. It was hoped that for the next fiscal year, with the continuance of the present tight money policy, equilibrium, or even a surplus, in the balance of payments would be attained, though such forecasts were difficult to make.

15. The Government was making the utmost efforts to curb an excessive expansion of the economy by tightening credits and curtailing public investment, and it was hoped that further progress would be made towards trade liberalization.

16. The Japanese representative pointed out that the liberalization of imports would be greatly facilitated if Japan's exports could be expanded. Accordingly, they deeply regretted the fact that more than ten contracting parties were still refusing to apply the GATT provisions in regard to their trade with Japan, thus discriminating against the latter's exports.

17. In conclusion, he stated he anticipated with confidence that Japan's present difficulties would soon be overcome by their own efforts and by the sincere co-operation of the countries concerned. He emphasized that they intended to continue their efforts, to an even greater degree, towards the relaxation of import restrictions, when the balance-of-payments situation improved.

Balance-of-Payments Situation and Prospects, and Alternative Measures to Restore Equilibrium

18. Members of the Working Party stated they fully appreciated the fact that Japan had been experiencing balance-of-payments difficulties over the past few months, and they welcomed the reassuring statements made by the Japanese representative concerning the alternative fiscal and monetary measures which had been taken to cope with the situation. It appeared that an investment boom had developed in Japan, and as this gathered momentum, had been accompanied by inflationary pressures. To contain the boom and to try to reach equilibrium the Government had introduced internal measures and it was gratifying to see that this policy had been adopted, rather than one of imposing new import restrictions. The Working Party noted with satisfaction that the Japanese Government had made real progress in relaxing import restrictions and in reducing discrimination, and that their current policy was much more liberal than it had been previously. It would not be appropriate to press too hard for further relaxation of restrictions, but it was hoped that as soon as a position of equilibrium was reached, the Japanese Government would re-examine the position, with a view to introducing further liberalization and non-discriminatory measures and to resuming substantial progress away from bilateralism. There were still distinctions made between imports from the dollar area and elsewhere, and some members wondered whether this distinction, especially in regard to certain raw materials,

was valid or necessary; they hoped that consideration would be given to this particular aspect of import policy. A member asked if the Japanese delegate could give figures showing current gold and foreign exchange reserves as compared with 1954, when Japan was emerging from similar balance-of-payments difficulties.

19. In answer to the last point, the Japanese representative referred to page 48, Table 11, of the International Monetary Fund's background paper for their 1957 consultations, and gave the following information for the months of July and August 1957:

(i)	Gold	- no change, this figure remaining at $23 million
(ii)	US $	- July $730 million August $702 million
(iii)	Sterling	- July $126 million August $135 million
(iv)	Open account balances	- July $274 million August $286 million
(v)	Total	- July $1,153 million August $1,146 million

In 1954 Japan's total international reserves had been $1,130 million, comprising gold - $21 million, US dollars $685 million, sterling $232 million, and Open Account Balances $192 million. Over the past few years Japan's reserves had been highest in December 1956 with a total of $1,646 million; dollar reserves were also at their highest level - $1,211 million.

20. Commenting on these figures, a member noted that although the level of reserves was approximately the same in August 1957 as at the end of 1954, it was clear from the figures in Tables 9 and 10 of the IMF document that, whereas the level of imports in 1954 had been about $2,040 million, in 1957 they were running at the rate of $3,600 million. Special Government Receipts had fallen progressively over the years - from $602 million in 1954 to $498 million in 1956. These were two developments which seemed to have an important bearing on the balance-of-payments situation.

21. The Japanese representative expressed appreciation of the remarks made in the preceding discussion about his Government's problems and about the internal measures taken. It was recognized that there was some discrimination regarding imports from the dollar area, but Japan had an unfavourable trade balance with that area and had to take that into consideration. In 1955 the unfavourable balance was $113.5 million and in 1956 $80.5 million. For the period January-June 1957 the unfavourable trade balance amounted to $476.8 million.

In every year Japan had a large unfavourable balance with the dollar area, but fortunately they had considerable invisible receipts, mostly arising from special procurements by the United States Army in Japan. The situation was one which made the complete abolition of discrimination very difficult; but when their balance of payments was improving they had tried to relax this discrimination, and would continue to do so as the balance of payments permitted.

22. Members from the dollar area emphasized the fact that they hoped the Japanese Government would, as the balance-of-payments position improved, consider the overall payments and reserve position and not determine their policy by reference to a strictly bilateral balance situation.

23. One member pointed out that Japan was very dependent on imports for her exports, and must increase her exports to obtain equilibrium in the balance of payments. The Japanese Government had adopted an austere internal policy, and it should be remembered that there were still fifteen countries applying Article XXXV of the GATT against Japan. In his view some solution of this problem would have to be found, otherwise Japan could not re-establish a competitive export position.

24. The Japanese representative said he welcomed these remarks; the withdrawal of the application of Article XXXV to Japan by countries concerned was of very considerable importance and significance to his country's trade policy and balance-of-payments position.

25. A member from the dollar area stated that before Japan's balance-of-payments difficulties set in, the trend had been towards elimination of restrictive and discriminatory trade practices, and some relaxation of trade and payments. He wished, however, to express concern that liberalization had not been proportionately extended to certain dollar area goods, and hoped that, as the balance-of-payments position improved, the Japanese Government would reduce discrimination against dollar area goods, particularly those which competed with domestic manufacturers. He also asked if the Japanese authorities expected that the measures taken to reduce overall demand, principally through internal monetary and fiscal controls, would have the effect of reducing the external payments deficit sufficiently so that there would be an approximate balance at the end of the year.

26. The Japanese representative said that they had liberalized imports from the dollar area as well as from other areas; there was still some discrimination: he gave as an example the policy concerning the import of scrap iron; from the sterling and open account areas this commodity was under the Automatic Approval System, whereas for imports from the dollar area it was under the Foreign Exchange Allocation System. In point of fact, however, import figures showed there were considerable quantities coming in from the dollar area. If dollar imports of this commodity were put under the Automatic Approval System, they would be too large as the Japanese users showed considerable preference for imports from the dollar area. Theoretically there was a difference in treatment but actual figures showed dollar imports to be very substantial, and in fact it would seem in this, as well as in some other cases, that there was little or no discrimination.

27. He added that receipts from special procurements by foreign troops might well decrease considerably and accordingly the Japanese Government could not depend on these receipts. The United States Government was making efforts to purchase more under the ICA programme and the Japanese authorities hoped these purchases would increase in the near future. Overall, however, special procurement receipts were likely to decrease, and Japan was therefore trying as much as possible to increase her exports. He assured the Working Party that his Government's policy was, as circumstances permitted, to make every effort to increase liberalization and to reduce discrimination against dollar imports.

28. A member observed that three points seemed worthy of note in relation to the discussion thus far. First, that though Japan was experiencing moderate balance-of-payments difficulties its overall dollar position was strong. Second, that Japan anticipated a decline in foreign government dollar expenditure in Japan. However, the member observed, it was important to focus on the basic problem in Japan - i.e. the balancing of overall demand and supply of resources. If foreign governments reduced their purchases, he said, the resources became available to meet demand elsewhere, and could be exported. This member in making his third point concluded that the most logical way of assuring that these released resources were exported was to maintain their competitiveness through a liberal and non-discriminatory import policy.

29. A member enquired about the outlook for private foreign investment in Japan as one means to augment the foreign exchange position, improve productivity, export-earning capacity and the future balance-of-payments position. Were the Japanese authorities considering any measures to attract foreign private equity capital, and were there any specific sectors of the economy which the Japanese considered to be especially attractive, and if so what special efforts were being taken to obtain such capital?

30. The Japanese representative replied that a law concerning foreign investment had been passed, and special assurances and protection had been provided, so long as the investment would contribute to easing the balance of payments and to the development of the economy.

System and Methods of the Restrictions, and Effects on Trade

31. One member referred to the discrimination applied to the import of certain dollar goods. He recalled the statement by the representative of Japan to the effect that, since substantial imports of scrap iron and certain other goods were permitted under quota from the dollar area, there was little or no discrimination in spite of the difference in treatment under the import control system. While he appreciated the view that the import demand for such goods from the dollar area might justify quantitative controls on balance-of-payments grounds, such controls did constitute real and effective discrimination. In regard to the commodities which had been excluded from the Automatic Approval System when originating in the dollar area - for example, cheese, oats and soya beans - he asked for information concerning the basis on which such items had been so excluded. Had such goods been included under global quotas within the Exchange Allocation System?

32. The Japanese representative referred to his previous remarks concerning the need to distinguish in import policy between certain goods from the dollar, and non-dollar, areas respectively. He used again the example of scrap iron and scrap steel; these, when originating in the sterling area, were under the Automatic Approval System, but from the dollar area were under the Exchange Allocation System; there would appear to be some discrimination, but import figures showed that large quantities in fact came from the dollar area. The reason why the Japanese authorities could not place the dollar goods in question under the Automatic Approval System was that if they did so dollar imports would be greater than their balance of payments could stand; there was a strong preference by manufacturers for dollar goods; heavy increases in dollar imports would disturb Japan's normal trade relations with other areas. The basic reason was the balance-of-payments situation.

33. A member observed that up to June 1957, when applying for import licences, Japanese importers were required to deposit with a bank a bank-guarantee or government bonds amounting to 1 to 5 per cent of the invoice value of the goods concerned. Such a measure was no doubt taken only to keep the number of non-utilized licences to a minimum. Since the date mentioned, important modifications had been introduced, the deposit being increased to an amount which could go as high as 35 per cent, and it had to be made in cash. He called attention to the fact that the discount rate in Japan had gone above 9 per cent. He also observed that, in these conditions, it appeared that a technical measure introduced to make effective the functioning of a quota system was moving towards a mechanism capable of putting a real brake on imports. The freezing, for a relatively long period, of an amount which represented a substantial percentage of the value of the imports increased their cost. It would be interesting to know whether it involved an attempt to introduce a new method of import control or a new type of restriction to be added to those already in force. It would also be interesting to have information about the products to which the highest deposits applied and about the additional burden thus put on imports. It was perhaps useful to draw attention to the fact that this new procedure could have a certain discriminatory effect; it tended to strengthen the natural discrimination resulting from the different distances from Japan of some exporting countries. In the case, for example, of European countries, the Japanese importer would be influenced not only by the higher transport costs but also by the freezing, for a longer period, of his liquid assets.

34. In reply, the Japanese representative stated that the purposes of the advance deposit system were (i) to prevent frivolous applications and the possible loss of confidence in certain Japanese importers by overseas suppliers and (ii) to prevent applications for speculative imports. The system also served as a supplementary measure in the restrictive monetary policy. In May-June 1957 the rate of deposit had been increased, but the objectives were to reinforce the tight money policy adopted since March-April. It was recognized that the deposit requirement had some effect in restricting certain imports; before the rates were raised certain commodities were considered. The highest rate was now 35 per cent, the lowest 1; but in most cases it was only 5 per cent.

In raising the rates there was no intention of discriminating in regard to the origin of imports. The main criterion was that of essentiality; 1 to 5 per cent was applied to imports of raw materials; 25 to 35 per cent to imports of less essential or luxury goods.

35. After further discussion of this subject it was agreed by the Japanese representative that he would provide a full list of all goods affected, showing the rate applicable to each.

36. One member enquired about the criteria applied in import licensing policy, in particular about the role of price and quality of imported products in relation to those domestically produced; in other words if the same product was available from either dollar or non-dollar sources did relative prices (import as compared with domestic) play a significant role in import licensing policy?

37. The Japanese representative replied that they had to consider price and quality in formulating their import budget. Concerning the import of raw materials, in drawing up the foreign exchange budget, consultations were held with representatives of the Industry Bureau and with industries. The essential requirements, from the dollar area and elsewhere, were calculated, and then consideration was given to the foreign exchange available. Certain raw materials could be obtained by users from any source, and no doubt they gave full consideration to the questions of price and quality; the Government, in that case, did not consider the price factor, leaving purely commercial considerations to apply. In the case of commodities such as wheat, barley and rice, import was through a Government Agency which worked on the system of tenders, in which price and quality were important factors.

38. In some cases prices of Japanese products were higher than those of import goods, but in licensing policy the Japanese authorities did not give attention to the protective aspect. Balance-of-payments difficulties required that there be import control and some discrimination. Where there was an adequate supply of certain goods from domestic industries, there was little or no need to import them; otherwise the balance of payments would be detrimentally affected. Where imports were regarded as necessary, the Japanese authorities did not consider the domestic industries concerned.

39. Members noted with appreciation that Japan was now tending to rely much less than hitherto on bilateral trade agreements, and hoped that this trend would continue. They noted also that the percentage of retention of certain foreign exchange earnings under the Special Foreign Exchange Allocation System (page 7 of secretariat Basic Document) had been reduced from 10 to 3 per cent and that the period of utilization had also been reduced; this was an encouraging and welcome sign, and they hoped that in due course the system could be abolished. Members also noted again with appreciation,

the internal fiscal and monetary measures which had been taken by the Japanese Government and again expressed the hope that Japan would continue her efforts towards reducing restrictions and discrimination. It was hoped that such action would include provision for the importation at least of minimum commercial quantities of consumer goods; this would be beneficial not only in exposing domestic industries to competition but also in avoiding unnecessary damage to foreign commercial interests; progressive trade liberalization would ensure not only the avoidance of the uneconomic use of Japan's resources, but also the most effective use of such resources.

40. The Japanese representative stated they were ready to consider carefully all applications for imports of minimum commercial quantities, in order to avoid unnecessary damage to foreign commercial interests, as far as circumstances permitted.

41. The Working Party expressed appreciation of the information given by the Japanese representative, who in turn expressed his thanks for the patience and co-operation of the Chairman and members.

ANNEX I

OPENING STATEMENT BY THE JAPANESE REPRESENTATIVE

1. The Japanese Government appreciates the importance of this series of consultations in facilitating better understanding on import restrictions which have still been maintained by so many contracting parties.

We are desirous of cooperating with this Committee to make clear the present system of exchange and trade control in Japan as well as the prospects for reducing the restrictions. As a supplement to the basic document and background paper which covers the balance-of-payments situation and system and methods of the import restrictions, I would like to make a brief statement on the basic feature of the Japanese economy and the principles of her import control.

2. Considering her enormous population, Japan is poorly endowed with natural resources. She must import 100 per cent of her requirements of raw cotton, raw wool, crude rubber, phosphate rock, bauxite, and potassic salt, 80 to 95 per cent of sugar, crude oil and iron ore, 60 to 80 per cent of soya beans, wheat, hides and salt. The imports of foodstuffs and raw materials represent more than 70 per cent of the total imports. Under these circumstances, it would be no exaggeration to say that her imports affect vitally Japan's economy and her people's living. In other words, it is most essential for Japan to promote her exports to pay for the imports. In fact, however, her exports fall far short of her imports. Japan's production has shown a considerable recovery since the end of the War, while her exports are still far below the prewar level. To take the situation in 1956, industrial production was 220.5 per cent of the average figure of 1934-36 and the volume of imports was 114.4 per cent. Whereas the volume of exports was only 86 per cent, which means that this is the only sector in our economy which has failed to regain the prewar status. It is noted that the imbalance between imports and exports has hitherto been covered by receipts from procurement of foreign troops in Japan.

3. Control of foreign trade and exchange in Japan is essentially based on the economic situation in which this country is placed. The Foreign Exchange and Foreign Trade Control Law, which is the basic law in this field, has clearly stated in its outset that the controls are intended "for the proper development of foreign trade and for the safeguarding of the balance of payments and the stability of the currency as well as the most economic and beneficial use of foreign currency funds, with a view to rehabilitating and expanding the economy." Further, it is expressly stated in the same law that "the provisions of this law and of orders issued thereunder shall be reviewed with the objective of gradually relaxing and eliminating the restrictions as the need for them declines."

It is needless to say that the basic trade policy of the Japanese Government is to pursue such aims faihfully and to enforce this reviewing clause of the same Law. The Japanese Government, as already clarified at

its annual consultations with the International Monetary Fund, has in the past several years taken measures for liberalization of foreign trade and exchange as far as the payments situation permitted and consistent with the most effective use of foreign currency funds.

The measures taken along this fundamental policy included: expansion of the Automatic Approval System; enlargement of global quotas: abolition of open account arrangements; reduction in the so-called "retention quota" under the Special Foreign Exchange Allocation System; and simplification of foreign exchange control procedures for visible and invisible trade. These measures have produced significant effects toward the liberalization. In the case of the budget allocated for the Automatic Approval System, while it was $141.3 million in the first half of the fiscal year 1954, covering 335 items and representing 12.8 per cent of the total exchange budget, it expanded to $513.5 million in the second half of the fiscal year 1956, covering 560 items and representing 20.7 per cent of the total budget.

The budget for the Foreign Exchange Allocation System stood at $931.3 in the first half of the fiscal year 1954, of which the single quota budget amounted to $913.2 million and represented 83.2 per cent of the total exchange budget. It increased in the second half of the fiscal year to $1,969.7 million, of which the single quota budget amounted to $387.5 and represented 13.6 per cent of the total foreign exchange budget. These figures indicate the remarkable expansion in the sphere of the Automatic Approval System and great reduction in the single quota budget.

Japan had open Account arrangements with sixteen countries in April 1955, but these arrangements have subsequently been abolished in respect of ten countries including Federal Republic of Germany, the Netherlands, Indonesia and the Philippines, and mutual transactions are conducted in transferable currencies. The policy of abolishing open account arrangements will be pursued in the future as far as circumstances permit. By adopting the system of multilateral payments, Japan upheld the principle of "the same currency, the same treatment" and tried to accord non-discriminatory treatment to her trade partners. We have pursued this course in the expectation that we shall be reciprocated by other countries with equal fair treatment.

The Link System has now been limited to certain kinds of raw materials, and measures for reduction of the rate of the "retention quota" was taken in regard to the Special Foreign Exchange Allocation.

4. The economic situation in my country changed in 1957. We found ourselves confronted with a crisis in her balance of payments, with a deficit of $542 million during the period of January-June 1957. To cope with this urgent situation, the Japanese Government, instead of resorting to measures intensifying import restrictions, has adopted a tight money and fiscal policy since March, 1957.

The principal measures for carrying out this policy were:

(1) Raising by the Bank of Japan of its official interest rate, in March and May.

(2) Raising by the commercial banks of their lending rates and interest rates on time deposits.

(3) Restriction of loans by the Bank of Japan.

(4) Postponement of 15 per cent of public investment and Government loans.

(5) Curtailment of loans by the commercial banks for private investment.

(6) Increase of the advance deposit required for obtaining import licences.

As these domestic measures will require some time before their effects are fully felt, the Japanese Government temporarily applied to the International Monetary Fund and the Export-Import Bank of Washington for short-term credits and, in June, a purchase of $125 million was authorized by the IMF and in August a credit of $175 million was granted by the EXIM, of which $60 million was a renewal of the credit for the previous year on the revised conditions.

5. I would now like to deal with the situation in regard to our exchange budget this year. As to the exchange budget for import for the first half of the fiscal year 1957 which actually amounted to $1,725 million, the amount used under the Automatic Approval system was $447 million covering 595 items, and accounting for 25.9 per cent of the total exchange budget. This is an increase both in the number of items and in the percentage of the amount as compared with the figures for 1956. And of the total budget for the Foreign Exchange Allocation which was $1,278 million, the budget for global quota was $1,171 million, accounting for 67.9 per cent of the total budget for imports, and the budget for single quota, was $107 million, representing 6.2 per cent of the total budget. As compared with the figures for 1956 the percentage of imports under global quota increased, while single quota imports decreased.

Therefore, I can say that we have not intensified our import restrictions, in spite of the difficulties in payments position.

The foreign exchange budget for import recently prepared for the second half of the fiscal year 1957 amounts to $1,652 million, which is a slight decrease as compared with that of the preceding period. Due to the monetary and fiscal measures as mentioned before, domestic production has gradually been declining. The mining and industrial production for the latter half of 1957 is expected to be about 105 per cent of the figures for the corresponding period of the previous year, whereas the same index for April-July, 1957 stood at 112 per cent. Furthermore, the growing stockpiles of imported raw materials due to a sharp increase in imports in 1956 and in the early part of 1957 has brought about a considerable decrease in domestic demand for import. I would like to point out that the foreign exchange budget for import during the latter half of this year will not sacrifice the domestic demand but, on the contrary, it will fully meet the requirements of domestic industries.

6. Now I wish to refer to the prospects of our balance of payments in the immediate future. It is expected that we shall attain equilibrium in the balance of payments in the latter half of this fiscal year. We have formulated the exchange budget for this period on this assumption. Import demand has been declining, as I have mentioned already. Exports are expected to expand gradually as the domestic demand falls and goods are more and more diverted to overseas markets.

Therefore, we are calculating that the deficit of $515 million for the first half of this fiscal year will be carried over to the end of this fiscal year, and will represent the final balance of the whole year.

With regard to the prospects for the next fiscal year, we are intending to continue our present ~~tight money policy to attain~~ equilibrium or even surplus ~~in our balance~~ of payments although it is rather difficult to forecast the future.

7. Now, I wish to speak a little about the course which the Japanese Government is to take, hereafter, with regard to import restrictions and to certain problems of exports.

Recognizing that current difficulties in the balance-of-payments situation are mainly due to the rapid expansion of our economy, particularly over investment for the past one year or two, our Government is making utmost efforts to curb an excessive expansion of the economy by tightening credits and curtailing public investment, with a view to tiding over the difficulties within as short a period as possible. I hope that we shall soon succeed in overcoming the present difficulties and shall be able to make a further progress in the liberalization of trade.

In this connexion, I should like to draw your attention, Mr. Chairman, to the fact that the liberalization of imports would be greatly facilitated if exports could be expanded. This is especially true for a country like Japan, who has a high degree of dependence on exports for sustaining the

national economy. However hard we endeavour to improve the payments position by resorting to tight money policy or other domestic measures, if the optimum rate of expansion in our exports could not be maintained, we are afraid that we could not liberalize our imports further.

Therefore, we deeply regret to see that more than ten contracting parties are still refusing to apply GATT provisions with respect to their trade with Japan, thus discriminating against our exports.

To repeat my main theme again, I anticipate with confidence that the difficulties now confronting Japan will soon be overcome by our own efforts and by the sincere co-operation of the countries concerned, and I also wish to emphasize once again that we intend to continue our efforts, in an even larger scope, towards the relaxation of import restrictions, when Japan's payments situation is improved.