

GENERAL AGREEMENT ON TARIFFS AND TRADE

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REPORT OF THE COMMITTEE ON BALANCE-OF-PAYMENTS RESTRICTIONS ON THE CONSULTATION UNDER ARTICLE XII:4(b) WITH

D E N M A R K

1. The Committee has conducted the 1962 consultation with Denmark under the provisions of paragraph 4(b) of Article XII. In conducting the consultation, the Committee had before it a basic document prepared by the secretariat (BOP/13) and documents provided by the International Monetary Fund, as mentioned in paragraph 2 below. The Committee conducted the consultation according to the Plan recommended for such consultations by the CONTRACTING PARTIES (BISD, 7S, pages 97/98). The consultation was completed on 26 September 1962. The present report summarizes the main points of discussion during the consultation.

Consultation with the International Monetary Fund

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

"The International Monetary Fund has transmitted to the CONTRACTING PARTIES the Executive Board decision relating to the last consultation with Denmark under Article XIV of the Fund Agreement and the background material prepared in connection with that consultation.

"With respect to Part I of the Plan for Consultation, relating to balance of payments position and prospects, and with respect to Part III, relating to system and methods of the restrictions, the Fund calls the attention of the CONTRACTING PARTIES to the Executive Board decision of September 10, 1962, taken at the conclusion of its recent consultation with Denmark, and particularly to paragraph 5, which reads as follows:

'Denmark has made some further progress in relaxing its import restrictions and in reducing import discrimination. The Fund believes that the recent measures designed to restrain internal demand and to strengthen the external payments position should allow Denmark at an early date to reduce substantially its reliance on such restrictions, especially those maintained for balance of payments reasons. Reduced reliance on restrictions would also be helpful in restoring price

stability and in obtaining the most economic utilization of resources. The Fund notes that the export incentive scheme and the payments agreement with Turkey have been abolished, and urges the early termination of the two remaining payments agreements with Fund members.'

"With respect to Part II of the Plan for Consultations, relating to alternative measures to restore equilibrium, the Fund draws attention to the decision taken at the conclusion of its last consultation with Denmark, including the paragraph quoted above. The Fund has no additional alternative measures to suggest at this time."

Opening statement by the representative of Denmark

3. In opening the discussion, the representative of Denmark explained that during the past year the Danish economy had continued to expand, though at a slower rate than in 1960. As a result of the high level of economic activity and because of increasing import liberalization, Denmark's imports had increased in 1961 by 6 per cent over the high level of imports reached in 1960 thus bringing the total increase of imports over the four-year period 1958 to 1961 to 35 per cent. The increase in imports over this period had been considerably larger than the increase in exports, which had amounted to approximately 20 per cent. While exports of industrial products had increased by about the same percentage as imports, exports of agricultural products, which continued to account for more than one half of Danish exports, had risen by only 7 per cent due to difficulties of access to foreign markets. The drain on the balance of payments which had resulted from the more rapid increase in imports as compared with exports had become more pronounced during the last twelve months. This was primarily because of a more rapid rise in imports of investment goods and manufactured consumer goods, but due also to inflationary tendencies in the economy as increasingly full utilization of plant and equipment and a scarcity of labour led to a slowing down of industrial expansion and the rate of growth of industrial exports.

4. During the first half of 1962 the balance on current account showed an overall deficit of about DKr 800 million. The corresponding figure for the first half of 1961 was approximately DKr 400 million. The deterioration was due mainly to a very fast increase in the import of investment goods but there had also been a general increase in imports of raw materials and consumer goods.

5. In order to ease the pressure of demand and to improve the foreign reserve position the Danish Government, under a compromise agreement with the two largest opposition parties, had imposed a general wholesale purchase tax of 9 per cent on most consumer goods, except foodstuffs, from 1 August 1962. The Government had also placed a ceiling on Government expenditure for the fiscal

year 1 April 1962 to 31 March 1963. As a result of these measures and higher tax collections in the current fiscal year (reflecting the higher incomes in 1961 on which these taxes were levied), the budget for 1962-63 provided for an overall surplus of Dkr 500 million. This compared with a deficit of Dkr 450 million in 1961-62. In addition, special measures had been taken to limit public and residential construction. In the monetary sector the tight credit policy was being continued.

6. While it was too soon to estimate the impact of these measures, a damping down of demand, particularly for consumer goods, could be expected, which in turn should have favourable effects on the balance of payments and, by restraining the increase in internal costs and prices, on Denmark's competitive position in export markets. Nevertheless, the situation remained precarious because of the very low level of the country's foreign reserves. Due to the link between the cost-of-living index and wages, and because of the expiration of collective wage agreements affecting large numbers of industrial workers in the spring of 1963, wage payments were bound to increase. The representative of Denmark explained that the "wage adjustment" cost-of-living index was expected to increase by a total of approximately 5 per cent as a result of the imposition of the turnover tax and the expected increases in prices of eggs, poultry, bacon, beef, and veal by approximately 15 per cent following the recent agreement between the Government and the agricultural organizations for an upward adjustment of internal prices in respect of these products during the year ending 30 June 1963. Moreover, it might be difficult to keep the budget surplus during the next fiscal year at the high level envisaged for the fiscal year 1962-63. The compromise agreement between the Government and the two largest opposition parties provided for the proceeds of the turnover tax to be used for reducing other taxes, primarily income tax, in the 1963/64 fiscal year. This provision was, however, subject to reconsideration in the spring of 1963 in the light of the situation prevailing at that time. Thus, the reduction in direct taxation might not become effective if the balance-of-payments situation at that time turned out to be less favourable than was envisaged. On the external side, there was considerable uncertainty regarding the prospects for Denmark's agricultural exports, particularly to the EEC countries. It was impossible, therefore, at the present time to predict with any degree of precision the development of Denmark's balance of payments in 1963.

7. Referring to his Government's import control policy, the representative of Denmark stated that despite the heavy deficit on current account in recent years, import liberalization had been constantly carried forward. Also, the free-list area had been extended, the latest country to be added being Israel, and the Danish Government constantly endeavoured to widen the geographical scope of liberalization. It was recognized that this policy of liberalization had further stimulated efficiency of Danish industries and had added therefore, to their competitiveness. The large increase in imports had also been an important factor in reducing inflationary pressures. Notwithstanding the Government's desire to

free imports from restrictions, further import liberalization would have to be effected gradually in view of the country's very low level of reserves. Experience had shown that imports of newly liberalized items would increase considerably faster than imports in general, especially during the first year following the liberalization.

8. Another factor to be taken into consideration by the Government in implementing its import policy was that, over the many years during which Denmark had been forced to restrict imports for balance-of-payments reasons, industries had grown up which were not fully competitive. These industries would need some period of adaptation and adjustment until they could face the full force of international competition. Accordingly, import liberalization affecting certain industries had to take place gradually and had to be carefully planned if disruption of national production and the resulting unacceptable waste of resources and of foreign exchange reserves were to be avoided.

9. The method adopted by his Government in respect of these imports was to increase quotas every year by at least 20 per cent so as to expose the industries concerned to a continual increase in foreign competition. It was his Government's hope that, in pursuing this policy, it would be possible over a relatively short span of years to eliminate all import restrictions on industrial goods and to achieve this goal without exposing the balance of payments to undue strains.

10. As regards the import policy for agricultural products, it had to be remembered that Danish agriculture was fully competitive. Denmark could, however, not be expected to open its home market to imports of subsidized foreign food products. Among other reasons the precarious balance-of-payments situation would not permit the use of foreign currency for such imports. His Government regretted that it had not so far been possible to find a solution within the framework of GATT to the problems created for agricultural exporting countries as a result of agricultural protectionism.

11. With reference to the Fund decision of 10 September 1962, which states: "The Fund believes that the recent measures designed to restrain internal demand and to strengthen the external payments position should allow Denmark at an early date to reduce substantially its reliance on such restrictions, especially those maintained for balance of payments reasons", the representative of Denmark said that he fully agreed with the content of this statement but had certain difficulties in accepting the implication that Denmark also maintained restrictions which were not motivated by balance-of-payments reasons. From what he had said, this was obviously not the case.

Balance-of-payments position and prospects

12. The Committee thanked the representative of Denmark for his frank and informative statement. They welcomed the further progress made by Denmark since the last consultation in relaxing import restrictions and the determined efforts of the Danish authorities to improve the country's foreign reserve position through internal measures. They expressed the hope that these measures would soon be reflected in an improvement in the foreign reserve position and would thus provide further scope for import liberalization.

13. In reply to questions regarding the pattern of and prospects for exports, the representative of Denmark explained it was the Government's hope that it would be possible to resume, and possibly exceed, the annual growth rate of industrial exports of 10 to 15 per cent which had been experienced over most of the 1950's. In view of the continuing heavy investment in industry at an average annual rate of approximately DKr 1.5 billion over the last three or four years, compared with approximately DKr 500 million in the early fifties, and in view of the measures adopted by the Government to prevent an overstimulation of the already booming economy, this goal appeared attainable if business conditions abroad continued to be favourable. The high rate of investment in industry, and the consequential large outlays in foreign exchange for imports of capital equipment, had been undertaken to reduce the country's dependence on agricultural exports. It had to be remembered that agricultural production in Denmark continued to be held back as a result of foreign restrictions on agricultural imports.

14. Members of the Committee noted the decrease in net receipts from services in 1961 as compared with 1960, and enquired about the expected development of receipts from services. The representative of Denmark explained that, although there had been some decrease in net receipts from services in the past year, the overall balance on services account was expected to remain essentially unchanged in 1962 as compared with earlier years.

15. In reply to a question regarding prospects for increased capital inflows the representative of Denmark said that his Government was encouraging foreign investment. Capital imports had been an important factor in recent years in permitting the high rate of investment in industry. No official forecasts of capital inflow had been made but it was the Government's hope that capital imports would continue at a high level.

16. Referring to the level of import liberalization already achieved and the fact that approximately half of the restrictions appeared to affect agricultural items, products in which Denmark had a strong competitive position, members of the Committee enquired about the effects on the balance of payments of a relaxation or removal of these restrictions. The representative of Denmark explained that for some considerable time his country had been forced to operate on very low foreign exchange reserves, at present equivalent to

approximately only one month's imports, but had nevertheless made considerable progress in import liberalization. Against the background of its limited freedom of action, his Government had laid the greatest emphasis on the liberalization of goods in the industrial sector where the Danish competitive position, as explained in his introductory statement, was relatively weakest. He agreed that Danish agriculture was highly competitive; therefore the motives behind his Government's move for the gradual abolition of restrictions within the industrial sector were not present in the case of agricultural products. The actual level of reserves did not allow any waste of foreign currency for the importation of subsidized agricultural products. The representative of Denmark further stated that, in accordance with its international obligations, his Government would nevertheless continue its endeavours to proceed further with import liberalization as soon as possible and to the extent permitted by the balance-of-payments position. With respect to the level of reserves, the representative of Denmark said that Denmark traditionally operated with relatively low reserves. Although it could be wished that the reserves were higher, Denmark did not consider it economically or politically desirable to strive for increased reserves at the expense of slowing down the rapid pace of industrial development.

Alternative measures to restore equilibrium

17. In discussing the effect of the fiscal measures adopted by the Danish Government on the internal price level and on demand, members of the Committee noted that, in order to compensate for the income effects of the turnover tax introduced on 1 August 1962, certain tax concessions had been made and provision had also been made for increased public expenditure on social benefits. There had also apparently been a considerable amount of anticipatory buying prior to the imposition of the tax. They enquired whether these factors would not reduce prospects for achieving the budgeted surplus. The representative of Denmark stated that, although it was too soon to assess the impact of the new turnover tax on the level of demand, the Government was determined to convert last year's budget deficit of DKr 450 million into a surplus of DKr 500 million this year. The increases in child allowances, old age and invalid pensions and tax reduction for low income groups, to compensate in part for the income effect of turnover tax, were an integral part of the compromise agreement reached between the two coalition parties in the Government and the two largest opposition parties. Increased expenditure and reduced revenues under these headings were relatively small and had been taken into account in budgeting for a surplus of DKr 500 million. Similarly the increase in consumer expenditure in anticipation of the coming into effect of the turnover tax had been taken into account in estimating the revenue from this tax. Thus the turnover tax could definitely be expected to have a significant impact on consumer demand.

18. As regards the provisions of the compromise agreement that purchase tax yields should be used for reducing income and real estate taxes and for increasing social payments in the next fiscal year, it had to be remembered that the final use of the funds was subject to review prior to the preparation of the budget proposals for 1963/64, and any decision reached at that time would take account of the foreign exchange position and the level of income, employment and prices and future prospects.

19. In reply to questions regarding the effect of the turnover tax and the price increases for certain agricultural products, referred to in the opening statement, on the special cost-of-living index for wage adjustments, the representative of Denmark said that the price increases for certain agricultural products were expected to lead to an increase by approximately 1 per cent, and the turnover tax by approximately 2 to 3 per cent, in the "wage adjusting" cost-of-living index by 1 January 1963, as compared with July 1962, and would thus, together with other foreseeable price increases, lead to a 4 to 5 per cent wage increase with effect from 1 April 1963. He further explained that an additional increase in wage payments might be expected in the spring of 1963, at which time collective wage agreements for large groups of industrial workers would come up for renewal. It was the Government's hope that, in the interest of internal price stability and Denmark's competitiveness in export markets, wage increases resulting from the re-negotiation of collective wage agreements would remain within the limits set by the increase in productivity. He explained that as a result of the heavy investment in industry, annual productivity gains of the order of 5 to 6 per cent had been registered in recent years.

Systems and methods of the restrictions

20. Members of the Committee welcomed the liberalization measures put into effect by Denmark on 1 January and 1 July 1962. They noted, however, that, as a result of the de-liberalization of coarse grains in September of 1961, countries which depended for a large part of their export income on such products had experienced a sharp decline in overall export possibilities to the Danish market. The policy of the Danish Government to admit such imports only if prices for domestic feedgrains exceeded a specified limit, increased recently by 15 per cent, appeared to have encouraged domestic production and had led to a further curtailment of import possibilities for traditional suppliers. Moreover, it was felt that this system of import control discriminated against overseas suppliers of non-subsidized grain, since it would be difficult for such exporters to take advantage of import opportunities which existed only if prices exceeded a certain level. They expressed the hope that the Danish authorities would review the need for these restrictions and, in the meantime, take appropriate measures for avoiding discrimination resulting from the operation of these restrictions.

21. The representative of Denmark explained that it was with regret that his Government had de-liberalized imports of feedgrains. The de-liberalization had been related to developments in the bacon market in the United Kingdom, as explained in the report on last year's consultation (L/1617). The recent increases in minimum import prices for feedgrains had been necessary because of a continuing weakness in the United Kingdom bacon market. The increase was not designed to protect domestic producers of feedgrains. Any protection resulting therefrom was incidental. Licences would be issued automatically when world market prices were above the fixed minimum, and, as far as he was aware, the validity of licences was fixed in such a way as to avoid any discrimination against distant suppliers. Nevertheless he would bring the point raised in this regard to the urgent attention of the authorities concerned.

22. In reply to questions concerning the import treatment of tropical products, the representative of Denmark explained that almost all tropical products were admitted free of restrictions. As regards chocolate and chocolate products which, in contrast to cocoa, were still subject to restrictions, the representative of Denmark explained that, in view of the present low level of reserves, it had not been possible to liberalize these items. Quotas had, however, been significantly increased each year with a view to preparing the industry for increasing import competition. His Government hoped to remove the remaining restrictions on these items within a few years.

23. In the discussion of the operation of licensing controls, the representative of Denmark confirmed that the so-called regional quotas were applied to imports from all countries in the free-list area. In reply to a question regarding the import régime for apples and pears, the representative of Denmark explained that it had not so far been possible to liberalize imports of these items. As in 1962, imports of these commodities would be permitted freely in 1963 in the Danish off-season i.e. 15 April-15 July in the case of apples and 15 April-31 July in the case of pears. In 1962, the first year when this system had been applied, imports had amounted to at least DKr 10 million.

24. Members of the Committee enquired about any concrete plans which Denmark might have for the elimination of the remaining restrictions and whether the Government was planning to impose other measures having a restrictive effect on demand for products scheduled for liberalization. The representative of Denmark stated that, the balance of payments permitting, it was his Government's firm intention, in accordance with a three-year liberalization programme adopted earlier, to liberalize additional industrial items with effect from 1 July 1963. He pointed out that Denmark was in negotiation with the EEC and, if eventually it joined the Community and thereby secured increased access to export markets for its agricultural products, his Government planned to dismantle all remaining import restrictions in the industrial sector two years after accession to the EEC. In any event, Denmark would continue to increase global quotas in accordance

with the EFTA Agreement. So far, Denmark had relaxed restrictions far beyond its obligations under that Agreement. The representative of Denmark said that his Government had no present intention of pursuing a general policy of raising tariffs or adopting other measures to offset liberalization, although he could not, of course, undertake to guarantee that there would be no changes in tariff rates on particular items.

25. In the discussion of the effects on trade of Denmark's bilateral trade and payments agreements, members of the Committee expressed the hope that Denmark would soon find it possible to reduce its reliance on bilateralism. The representative of Denmark explained that his Government was at present negotiating for the termination of certain of these agreements with non-State-trading countries. He stated further that such agreements had lost much of their practical significance following the recent elimination of most bilateral quotas through the establishment of new global quotas and liberalization.

Effects of the restrictions

26. Referring to the opening statement of the Danish representative, members of the Committee welcomed the importance attached by the Danish authorities to import liberalization as a means for influencing the internal price level and for increasing the competitiveness of national industries. They expressed the hope that the Danish authorities would continue to bear these considerations in mind in the administration of their import controls.

General

27. The Committee thanked the representatives of Denmark for the frank and co-operative manner in which they had responded to the many questions put to them during the consultation. The Committee welcomed the further progress made by Denmark in relaxing import restrictions and the action recently taken by Denmark for curbing inflationary pressures. They expressed the hope that these latter measures would prove effective and would provide further scope for import liberalization.

28. The representative of Denmark thanked the members of the Committee for the spirit of understanding with which the consultation was conducted. He assured the Committee that the points raised would be given careful consideration by his Government.

ANNEX

ANNEX

International Monetary Fund Executive Board Decision Taken at the
Conclusion of the Fund's Consultation with Denmark on 10 September 1962

1. The Government of Denmark has consulted the Fund under Article XIV, Section 4, of the Fund Agreement concerning the further retention of its transitional arrangements.
2. Since mid-1958 Denmark has experienced a markedly more rapid expansion in economic activity than in the earlier 1950's. The large volume of industrial investment in recent years and the structural changes in the economy which this involved have provided the basis for a substantial growth. Practically full employment was reached during 1960 and, subsequently, scarcity of labor resulted in a distinct slowing down in the expansion of industrial output. In 1961 the real gross national product rose by 4.5 per cent following a 7 per cent increase in the preceding year. The pressure on resources, particularly in the building sector, gave rise to inflationary income developments in 1961. Average hourly earnings in industry increased by 13 per cent between 1960 and 1961. The consumer price index rose by 7 per cent in the course of 1961 and by a further 2 per cent in the first quarter of 1962. Mainly as a result of the introduction of the agricultural support program and of the increase in salaries of civil servants, government expenditure rose substantially more than the revenue and the over-all budget surplus of DKr 400 million recorded in the fiscal year 1960/61 was turned into a deficit of DKr 450 million in 1961/62. This deficit was almost entirely financed by drawings on balances with the National Bank.
3. Sharply increased internal demand was also responsible for the deterioration in the balance of payments. The value of merchandise imports was 3.6 per cent higher in 1961 than in 1960. Import of machinery and manufactured consumer goods continued to rise steeply but there was a reduction in imports of feeding stuffs and of industrial raw materials. The value of exports increased by 2.9 per cent as a decline in agricultural exports and in the export of ships partly offset the continued expansion of export of industrial products. Net income from services declined and the deficit on the current account of the balance of payments increased from DKr 425 million in 1960 to DKr 663 million in 1961. Net inflow of capital amounted to DKr 264 million in 1960 and DKr 443 million in 1961. The net foreign assets of the banking system which had declined by DKr 161 million in 1960 fell by DKr 220 million in 1961. Long-term borrowing from abroad in the first half of 1962 was larger than in the corresponding period of the previous year. However, the trade deficit continued to increase and the reserves declined by a further DKr 166 million in the first half of 1962. At the end of June 1962 they amounted to DKr 1.048 million, representing less than one month's imports.

4. To contend with the internal pressures and to improve the foreign position, the National Bank in 1961 and early 1962 took steps designed to tighten monetary conditions and urged the banks to restrain their lending. Bank credit, which continued to be facilitated by borrowing from abroad for trade purposes, rose less strongly in 1961 and early 1962 than in 1960. Borrowing in the bond market, where the National Bank and the commercial banks acted as net buyers in 1961, increased substantially; in the first half of 1962, however, the National Bank sold a considerable amount of bonds. In June 1962 a set of measures designed to strengthen the fiscal situation and to limit public and residential construction was adopted and the budget for 1962/63 is estimated to show an over-all surplus of DKr 500 million, to be sterilized in the National Bank. The Fund welcomes these measures, which should help to restore a better balance between aggregate domestic demand and available resources and, thus, also lead to a strengthening of the external position.

5. Denmark has made some further progress in relaxing its import restrictions and in reducing import discrimination. The Fund believes that the recent measures designed to restrain internal demand and to strengthen the external payments position should allow Denmark at an early date to reduce substantially its reliance on such restrictions, especially those maintained for balance of payments reasons. Reduced reliance on restrictions would also be helpful in restoring price stability and in obtaining the most economic utilization of resources. The Fund notes that the export incentive scheme and the payments agreement with Turkey have been abolished, and urges the early termination of the two remaining payments agreements with Fund members.

6. In concluding the 1962 consultations, the Fund has no other comments to make on the transitional arrangements maintained by Denmark.