

GENERAL AGREEMENT ON TARIFFS AND TRADE

RESTRICTED
BOP/R/134
19 October 1983

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Committee on Balance-of-Payments Restrictions

REPORT ON THE 1983 CONSULTATION WITH PORTUGAL

1. The Committee consulted with Portugal in accordance with its terms of reference and the Declaration of the CONTRACTING PARTIES on Trade Measures Taken for Balance-of-Payments Purposes (BISD 26S/205). The consultation was held on 11 October 1983 under the Chairmanship of Mr. J.N. Feij (Netherlands). The International Monetary Fund was invited to participate in the consultation pursuant to Article XV of the General Agreement.

2. The Committee had the following documents before it:

Basic Document	(BOP/236 and Add.1)
Secretariat Background Paper	(BOP/W/68)
IMF report "Portugal - Recent Economic Developments", dated 19 May 1983	
Notifications by Portugal:	
- Import Surcharge Scheme	(L/5145/Add.2)
- Import Quotas for Consumer Goods	(L/5534 and L/5543)
- Quota System for Completely Knocked Down (CKD) Vehicles	(L/5558)

Opening Statement by the representative of Portugal

3. In his introductory statement, the representative of Portugal said that the external debt of his country had reached US\$ 13.5 billion or 60 per cent of GDP at the end of 1982, and that the deficit in the trade balance had risen to US\$ 4.8 billion in that year. In spite of these serious problems and of certain constraints on the expansion of exports - in particular in the field of textiles - his authorities would take the decision to reduce the import surcharge from 30 to 10 per cent by a single step before the end of the year. The government which took office in June of this year had adopted an 18-month emergency programme backed by an IMF stand-by arrangement. The emergency programme aimed at reducing both the fiscal and the current account deficits. In pursuance of this programme it had been decided to devalue, on 22 June 1983, the escudo by 12 per cent in effective terms, to cut back the public investment programme, to increase administered prices and to raise interest rates. Budgetary policy had been tightened both through a reduction of expenditures and additional measures of direct and indirect taxation. The emergency programme, while leading to a decline in GDP growth and an increase in inflation in the short run, was expected to improve the trade balance both through better export performance and a slower import growth resulting from the decline in economic activity.

4. The short-term emergency programme was backed up by the progressive implementation of two other programmes: a two to three-year programme designed to improve the functioning of the economic and financial system and a four-year programme aimed at modernizing the Portuguese economy.

Statement by the representative of the International Monetary Fund

5. At the invitation of the Committee, the representative of the International Monetary Fund made a statement, the full text of which is reproduced in the Annex.

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

6. Several members expressed concern about the large budget deficits in Portugal and the related high rates of inflation. One member stressed that, to avoid recurring payments problems, it was necessary to implement the government's stabilization programme fully and not to relax the financial discipline as soon as the external balance had improved. One member, noting that at present about half of Portugal's fiscal deficit was financed by the Bank of Portugal and that this had inflationary effects which led to a decline in export competitiveness, said that he welcomed the decision of the Portuguese government to diversify budget deficit financing by creating a private market for government bonds. The representative of Portugal said in response that the overall public-sector deficit was expected to decline to about 9.5 per cent of GDP in 1983. Important fiscal measures, such as further direct and indirect taxes and the reduction of both state subsidies and public investments, were aimed at achieving this result.

7. Several members, noting that the Committee had encouraged Portugal at the 1982 consultation to pursue monetary and fiscal policies which would foster an improvement in the current account, asked what steps Portugal had taken to improve the balance-of-payments situation. The representative of Portugal said that among the main steps taken was an increase in interest rates by a total of 6.5 to 7.5 percentage points in March and August 1983, a substantial decline in the rate of growth of the supply of credits and an effective devaluation of the escudo by 12 per cent in June 1983, combined with an increase in the monthly depreciation rate from 0.75 to 1 per cent as of March 1983.

8. The representative of Portugal added that these macroeconomic adjustment efforts would be supplemented by programmes designed to bring about structural improvements in the Portuguese economy. A two to three-year "Financial and Economic Recovery Programme" was to be presented to Parliament in the first half of 1984. It would bring about changes in the institutional framework governing economic and financial activity, in the regional development policies and in the management of public funds. In addition, the Portuguese government intended to present to Parliament in the second half of 1984 a four-year programme for the modernization of the Portuguese economy. This programme was aimed at the structural reorganization of the economy so as to prepare it for Portugal's accession to the European Communities.

9. One member, noting that some elements of the emergency programme could have an inflationary impact in the short run (in particular the depreciation of the escudo, the rise in administered prices and the reduction of certain subsidies) asked what the expected inflation rates during the programme period were. The representative of Portugal replied that the annual rate of price increases was expected to reach about 29 per cent at the end of 1983 (24 per cent for the calendar year) and then decline to about 20 per cent at the end of 1984 (24 per cent for the calendar year). In response to a question about the performance of the Portuguese economy during the first half of 1983, the representative of Portugal made the latest balance-of-payments statistics available to the members of the Committee. These showed that the current account deficit had declined from US\$ 2,203 million in the first half of 1982 to US\$ 1,428 million in the first half of 1983. During these periods, imports had declined from US\$ 4,832 million to US\$ 4,190 million, while exports had increased from US\$ 2,049 million to US\$ 2,326 million.

10. One member, noting that Portugal had at present the lowest agricultural production per unit of labour or land among the Western European countries, asked whether the Portuguese government had instituted policies to improve the performance of the agricultural sector. The representative of Portugal replied that the government attempted to modernize this sector through programmes in the fields of standardization, accounting, training and soil improvement.

11. In response to a question from a member, the representative of the IMF noted that, of the total use of Fund resources of SDR 703 million approved by the Fund on 7 October 1983, the amount of SDR 258 million, equivalent to 100 per cent of quota, was made available under the Compensatory Financing Facility. He noted that drawings under this facility in excess of 50 per cent of a member's quota were authorized only if the Fund was satisfied that the member concerned was cooperating with the Fund in finding appropriate solutions to its balance-of-payments problems. The Fund had also simultaneously approved a stand-by arrangement in the upper credit tranches; the requirement of cooperation under the Compensatory Financing Facility had been met in the case of Portugal.

System, method and effect of the restrictive import measures

12. In reply to a query about the overall effect of the import surcharge, the representative of Portugal said that imports of goods subject to the surcharge had increased faster than other imports; as a result, their share in total imports had risen from 20.3 per cent in 1980 to 21.1 per cent in 1982. One member asked how the products included in the list of goods subject to the surcharge had been selected. In response the representative of Portugal said that the list included non-essential consumer goods as well as intermediate and capital goods used for the production of non-essential goods.

13. Several members asked whether the Portuguese government had plans to remove the quotas and surcharges and whether a time schedule for the removal of these measures could be announced in accordance with paragraph 1(c) of the Declaration on Trade Measures Taken for

Balance-of-Payments Purposes and the recommendations of the Committee in previous consultations. The representative of Portugal replied that the quota system for consumer goods was a temporary measure, which had been instituted only on a yearly basis. The quotas on unassembled vehicles were going to be phased out at the end of 1984, when the legislation for the restructuring of the automotive industry expired. The 60 per cent surcharge on luxury goods would be transformed into an internal tax as soon as the value-added-tax system had been introduced, which the Portuguese authorities planned to do at the time of accession to the European Communities. The Portuguese government would take the decision to reduce the 30 per cent surcharge to 10 per cent by a single step before the end of this year, and the stabilization policies to be undertaken under the programme agreed with the Fund should create conditions favourable to a total removal of this surcharge.

14. Asked to indicate the rationale for the increase of the surcharge to 30 per cent in March 1983 and the planned roll-back to 10 per cent in January 1984, the representative of Portugal explained that the increase, decided in politically difficult circumstances, had been introduced as an interim measure pending the implementation of more basic adjustment policies.

15. One member, referring to Portugal's latest notification of the quota system for consumer goods (L/5543, Annex I), asked why the licences were still distributed among importers on the basis of their imports in 1975 and 1976; why Portugal applied a special régime for the allocation of the quotas for fruits classified under the heading 08.01; and whether the grant of additional quotas to exporters had the effect of stimulating countertrade. The representative of Portugal replied that 1975 and 1976 had been chosen as a basis for quota allocations because these were the two years that had preceded the introduction of the quota system. However, 15 per cent of the total quotas were set aside for new importers. New importers were given licences only if their share of the quota exceeded a certain minimum amount so as to facilitate a control of the proper use of the licences. Fruit imports could be subjected to a different quota allocation system because of the special nature of these imports. Additional import quotas corresponding to a part of the national value added to exported goods could be allocated under certain circumstances.

16. Several members noted that the import licensing system continued to be restrictive. One member referred to reports that an informal quota had been applied which limited established importers to an import value no greater than the level of the previous year. Moreover, import bulletins for the importation of new products were reportedly virtually impossible to obtain. In addition it had been reported that bulletins for imports after regular quotas were frequently denied or delayed. The Portuguese representative was asked to explain the system and to indicate the legal basis for these measures under Portuguese law. The representative of Portugal replied that the import licensing system was not intended to be restrictive, and not aimed at maintaining the import value at the level of the previous year. His government planned to make the system more

transparent and to avoid delays, inter alia, by introducing a computerized system. The new system was likely to be fully operative at the end of 1983. The representative of Portugal added that import licenses under the quota system were granted as required.

17. One member asked why petroleum imports had increased sharply in 1982. The representative of Portugal replied that this had been due to the installation of a steam-cracker in Portugal. This rise in imports of oil products had been followed by an increase in exports of chemical products. In reply to a further query, the representative of Portugal confirmed that the imports of certain agricultural products by public agencies (BOP/236, page 4) were not subject to quota restrictions or surcharges. These import monopolies were presently examined with a view to bringing their activity into conformity with the requirements of membership in the European Communities. In response to a question about the volume effect of the value increase of the quota for unassembled vehicles the representative of Portugal said that the increase by 30.27 per cent in the escudo value of the quota had been designed to maintain the volume of imports during 1983 at the level of 38,000 units.

Conclusions

18. The Committee noted that Portugal, faced with a sharp deterioration in its balance-of-payments in 1982, had increased in February 1983 the 10 per cent surcharge to 30 per cent and had retained the 60 per cent surcharge and the import quotas for certain consumer goods and unassembled vehicles.

19. The Committee regretted that, although the surcharges had been applied since 1976 and the import quotas for consumer goods since 1977, no time schedule for the removal of these measures had as yet been announced in conformity with paragraph 1(c) of the Declaration on Trade Measures for Balance-of-Payments Purposes and the Committee's recommendations in previous consultations. The Committee therefore again requested the Portuguese authorities to announce a time-table for the removal of the restrictive import measures as soon as possible.

20. The Committee was concerned about indications that the procedures for the issuing of import licences had been used for restrictive purposes. It therefore welcomed the statement of the Portuguese representative that the licensing systems were not intended to be restrictive as well as the intention of the Portuguese authorities to make the import licensing procedures more transparent and to avoid delays in the issuing of licences.

21. The Committee noted with satisfaction that the Portuguese authorities had recently embarked on a comprehensive programme to bring about lasting improvement in the external position and that they intended to roll-back the 30 per cent surcharge to 10 per cent by 1 January 1984. The Committee asked Portugal to reduce its reliance on restrictive import measures for balance-of-payments purposes as soon as the stabilization efforts begin to produce results.

ANNEX

Statement by the Representative of
the International Monetary Fund

Following some years of reasonably good performance, there has been a significant deterioration in Portugal's economic performance over the past three years. The restoration of external balance in 1979 encouraged the Portuguese authorities to relax the stance of financial policies in the following year, with the principal objectives of stimulating investment and of securing a recovery in real disposable income. The easier stance of financial policies that ensued, accommodated a rate of growth of real domestic demand in Portugal some 15 percentage points in excess of the OECD average over the period 1980-82. Moreover, the relative inflexibility of interest rate and exchange rate policies during that period reduced incentives for Portuguese residents to hold domestic financial assets, contributing to disguised capital outflows. The adverse impact of these policies on Portugal's external accounts was compounded by external factors. These included a 10 1/2 percent deterioration in the terms of trade between 1979 and 1982, the international recession, high interest rates abroad, and adverse weather conditions, which necessitated a sharp increase in energy and agricultural imports. As a result, the current account of the balance of payments shifted from near equilibrium in 1979 to deficits of US\$1,250 million or 5 percent of GDP in 1980, US\$2,850 million or 11.5 percent of GDP in 1981, and US\$3,240 million or 13.2 percent of GDP in 1982. The growth of real GDP, which had averaged some 5 percent annually during 1976-80, fell to below 2 percent in 1981, but recovered to over 3 percent in 1982. The rate of annual price increase remained considerably above the OECD average, rising to 22 percent in 1982.

The current account deficits over the past three years were financed through substantial external borrowing, mainly by the public sector enterprises. By end-1982, Portugal's external debt had risen to US\$13 1/2 billion, of which some US\$4 billion was of short-term maturity. The debt service ratio (excluding the rollover of short-term debt) reached 27 1/2 percent in 1982. The deterioration in economic performance in 1982, together with political uncertainties, caused considerable uneasiness in international capital markets in the first half of 1983. Foreign exchange reserves of the Bank of Portugal (excluding gold) declined to less than two weeks' imports, forcing the Bank to request sizable BIS loans secured by gold collateral. During the first half of 1983, Portugal's net foreign assets declined by US\$980 million to around US\$8 1/2 billion at the end of June 1983, with gold valued at market prices.

Preliminary indications point to a significant improvement in the current account balance during the first half of 1983, with the deficit tentatively estimated at US\$1,400 million as compared with US\$2,200 million in the first half of 1982. The main factor underlying this improvement was a sharp drop in imports, particularly of oil and agricultural products, associated in part with the difficulties of the public sector enterprises in obtaining external financing. For the whole of 1983, the Fund staff is projecting that the current account deficit will be held at US\$2,000 million or 9 percent of GDP, while for 1984 the deficit is projected to decline further to US\$1,250 million or around 6 percent of GDP. These projections are based on both an expected recovery in foreign exchange earnings and the containment of import demand, as a consequence of the stabilization program on which the Portuguese authorities have embarked, and in support of which they have requested a stand-by arrangement from the Fund in the upper credit tranches.

The improvement in the external position at which the Portuguese authorities are aiming is to be achieved through a comprehensive policy effort designed to reduce domestic demand and to promote foreign exchange earnings. Steps already taken in this direction include a 12 percent effective devaluation of the escudo on June 22, 1983, a substantial cut-back in the public investment program, a wide range of sharp increases in administered prices, including those of essential foodstuffs and of oil products, and the raising of interest rates in August by 2-2 1/2 percentage points following increases of 4-5 percentage points last March. The main contribution to the stabilization effort is to come from fiscal restraint with the combined position of the General Government and of the Supply Fund, which subsidizes essential commodities, targeted to move from a deficit equivalent to 12 1/2 percent of GDP in 1982 to a deficit of 9 1/4 percent in 1983, and to 6 percent in 1984. The improvement in the finances of the General Government is to be complemented by a comprehensive effort to contain the borrowing requirement of the public enterprises. At the same time, monetary policy is to be geared toward securing a scaling down in the rate of growth of the monetary and credit aggregates consistent with the targeted improvement in the balance of payments, and a deceleration of inflation. The rate of inflation is targeted to decline from a peak of 29 percent expected by end-1983 as a consequence of the recent sizable administered price adjustments and of the devaluation, to 20 percent by end-1984.

Faced with a sharp deterioration in the balance of payments in the previous two years, Portugal at the beginning of 1983 raised the 10 percent import surcharge initially introduced in 1975 to 30 percent, pending the introduction of more fundamental adjustment policies. There are also indications of some tightening of the administration of import licences over the past year. The import quota system introduced in 1976 for balance of payments reasons, and the 60 percent import surcharge on less essential products, were retained. The Portuguese authorities have recently embarked on a comprehensive program to bring about a lasting

improvement in the external position. The Fund welcomes the commitment of the Portuguese authorities to an open trade and payments system, and in particular their undertaking to roll back the import surcharge to 10 percent, effective January 1, 1984. The Fund hopes that Portugal will reduce further its reliance on trade restrictions for balance of payments purposes as the current stabilization efforts begin to produce results.