

GENERAL AGREEMENT ON TARIFFS AND TRADE

RESTRICTED

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

1. In accordance with its terms of reference, the Committee has conducted the consultation with Iceland under Article XII:4(b). The Committee had before it a basic document for the consultation (BOP/47) and documentation supplied by the International Monetary Fund, as mentioned in paragraph 3 below.
2. In conducting the consultation the Committee followed the Plan for such consultations recommended by the CONTRACTING PARTIES (BISD, Seventh Supplement, pages 97-98). The consultation was held on 6 May 1965. The present report summarizes the main points of the discussion.

Consultation with the International Monetary Fund

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

"The International Monetary Fund has transmitted to the CONTRACTING PARTIES the Executive Board decision and background material from the last consultation with Iceland under Article XIV of the Fund Agreement.

"With respect to Part I of the Plan for Consultations, relating to balance of payments position and prospects, and with respect to Part III, relating to system and methods of the restrictions, the Fund invites the attention of the CONTRACTING PARTIES to the Executive Board decision of April 28, 1965 taken at the conclusion of its recent consultation with Iceland. After a reference in paragraph 4 to "a substantial reduction in import restrictions....carried out early in 1965", paragraph 5 of this decision reads as follows:

'In addition to reducing import restrictions, Iceland has virtually eliminated restrictions on payments for current invisibles. The Fund welcomes these measures and believes that the balance of payments permits Iceland to make further progress in reducing restrictions. The Fund reiterates its view that the early termination of the remaining bilateral payments agreement with a Fund member country is feasible and desirable.'

"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 recent Article XIV consultation with Iceland and has no additional measures to suggest at this time."

Opening statement by the Icelandic representative

4. In his opening statement, the text of which is annexed to this report, the representative of Iceland described the evolution of the Icelandic restrictive system and of Iceland's efforts to move toward a liberalization of imports as part of a comprehensive stabilization programme. Two liberalization measures have been placed in effect since Iceland's provisional accession to the General Agreement last year and a further liberalization has been announced, to be effective 1 July 1965. As from that time, liberalization will apply to 79.2 per cent of actual imports in 1964. An additional 10.2 per cent of 1964 imports are under global quota, comprising chiefly lumber, certain wood products, iron and steel and sugar. The principal commodities which are imported under other licensing arrangements are petroleum products, wooden barrels and coffee. Arrangements for licensing of this last-mentioned group of products are generally designed to facilitate trade relations with seven bilateral trade partners which are important customers for Icelandic fish.

5. Thanks to the stabilization programme of 1960, Iceland's balance of payments was favourable in 1961 and 1962. In 1963 and 1964 unusually large imports (especially of ships and planes in 1964) resulted in deficits on current account, even though the gold and foreign-exchange reserves did not decline because some important imports are being financed by foreign credits. Even so, reserves of gold and foreign exchange are equal to four months imports, hardly adequate in view of the uncertain outlook for the economy, especially as concerns 1965 exports of fish and the possibility that wage negotiations in June may result in increased inflationary pressures. Iceland nevertheless intends to continue to liberalize as much of her trade as may be possible without risk of a subsequent need to retreat, with a view to the gradual abolition of most of her import restrictions.

Balance-of-payments position and prospects

6. Members of the Committee thanked the representative of Iceland for his clear and informative statement and were pleased to note the improvement in Iceland's balance-of-payments position since 1961. If Iceland had recently run a deficit in her current account, it was at least welcome that her foreign exchange reserves had not been depleted and it was encouraging that further steps to liberalize imports had been taken this year. The question was raised however to what extent Iceland considers that quantitative restrictions contribute to an improvement in the balance of payments and what were the prospects for a further easing of restrictions. The representative of Iceland noted that the rôle of quantitative restrictions was of course a matter of judgment and indicated that he would not want to try to answer in detail. The importance of Eastern European markets for salted and frozen herring and frozen fish was very great and Iceland could not afford to place herself in a position of being unable to market all of

a highly variable annual catch. If the herring were not marketed in Eastern Europe it would be necessary to process them into meal or oil, in which form the return would be only about one third their value as fish. Up to now other markets for the particular fish products currently sold in Eastern Europe were not sufficient to absorb the entire catch in a good fishing year. As for prospects for further liberalization, that would depend in part on other countries who might (for example in the Kennedy Round) open their markets to Iceland's fish to a greater degree than they had so far done, but if that did not happen Iceland would need to continue to seek satisfactory trading arrangements with those countries which are now willing to buy.

7. Members of the Committee appreciated Iceland's heavy dependence on fish exports and her need to sell where there are buyers. They also expressed appreciation of the various steps taken in the last few years to narrow the scope of imports not yet liberalized.

8. It was pointed out that the Eastern European countries have, over the past few years, been running a trade surplus with Iceland which would seem to suggest that there has been scope for a rather wider degree of liberalization, as is recognized in the penultimate paragraph of page 4 of the basic document. It was not clear why Iceland reserved for import under bilaterals more than the equivalent of fish sold under the bilaterals. The representative of Iceland explained that the catch of herring suitable for human consumption, normally marketed to a large extent in Eastern Europe, has been exceptionally short in recent years and that it would therefore not be prudent to reduce the scope of possible marketings in those countries as reduced markets there could present great difficulties in a year when there was a large production of herring.

Alternative measures to restore equilibrium

9. In looking at Iceland's economy as a whole, members of the Committee expressed some concern that notwithstanding the internal stabilization measures taken by the Government of Iceland, there was danger that inflationary pressures might have an adverse effect upon exports and lead to balance-of-payments difficulties if purchasing power in the hands of consumers were to expand further. Conceivably subsidies might be used to offset high costs of producing export commodities, but this would place a great strain on the budget. The better course might therefore be to hold wage increases to a minimum, and it was gratifying to note that this was a policy which seemed to be in the minds of the Icelandic authorities with respect to coming wage negotiations. In particular it would be desirable if the automatic link between prices and wages could be abolished. The representative of Iceland agreed that a difficult situation would threaten if further cost increases were to occur under the wage agreements to be negotiated. He noted, however, that fears of the Icelandic authorities on this count had already proved groundless once earlier, though this was of course no reason for complacency. As to consumer subsidies, he agreed that they could not well be increased further. In fact, because of an anticipated budgetary deficit in 1965, investment expenditures of the Government had already been cut by 20 per cent in March, and it was not yet known whether this cut would be

sufficient to balance the budget. He agreed that it would be desirable to be free from the wage-price link, which in fact the Icelandic authorities had successfully resisted for a number of years, but noted that it had not been possible to avoid acceptance of it last year.

System and methods of restriction and effects of the restrictions

10. It was noted that Iceland uses State-trading companies to handle importation of certain products, and the representative of Iceland was asked what policies and criteria were followed with respect to purchase and resale of these commodities. He replied that so far as purchasing was concerned, the few commodities handled by State trading are bought on purely commercial considerations, both as to the choice of kinds and qualities of merchandise to be stocked and as to the sources of supply. In fixing resale prices, however, the primary consideration was revenue, and prices were set accordingly. The representative of Iceland stated that he believed the mark-up on wines might be lower than that on distilled spirits.

11. A member of the Committee enquired about restrictions which he believed had recently been imposed on the terms of credit on which imports might be purchased. The representative of Iceland explained that until late in 1963 importers had generally been allowed to purchase on credit of up to three months. At that time however, in order to reduce imports to avoid balance-of-payments difficulties and to take some excess purchasing power out of circulation, more stringent regulations concerning payment had been introduced on select items; a principal item affected was automobiles. The proof that this measure had not hurt foreign suppliers unduly was that imports had continued high, though somewhat less so than before. While credit restrictions do now extend to certain other goods, machinery and capital goods may still be paid for over a period of up to one year. For more extended payment terms, Government approval is needed and is usually given only for large purchases having an export-producing potential, notably fishing vessels.

12. Another member noted at this point that his country has been involved in a problem concerning the exemption of certain automobile imports from a temporary licensing fee which was increased from 100 per cent to 125 per cent at the beginning of this year. The fee in itself appears rather burdensome, coming on top of a 90 per cent duty, but a special difficulty has been the exemption of some but not all similar vehicles from this fee. The member noted that both exempt and non-exempt kinds were available for export from his country. The representative of Iceland confirmed that the fee had been increased as stated, for revenue purposes, though he emphasized that it had been even higher only two years' ago and that imports were continuing at a high rate notwithstanding. As for the apparent discrimination among similar motor vehicles, he explained that the object was to favour farmers by allowing a utility vehicle to be imported subject to lower charges than those paid on regular passenger vehicles and that it was very difficult to find a dividing line which would not appear arbitrary to some. The existing regulation was based on length of wheelbase and he feared that any extension of the allowable wheelbase would immediately raise a complaint about exclusion of the next larger model from this special benefit.

13. The question of goods not liberalized was again raised, and one member of the Committee asked what might be the prospect for liberalization of some goods licensed mainly for import from bilateral agreement countries. He wondered whether the maintenance of such discriminatory measures which seems to be involved in the administration of such licences could be fully justified on balance-of-payments grounds; and he suggested that the authorities of Iceland might wish to review this question with a view to, if appropriate, reducing this element of discrimination in the importing system. The representative of Iceland again stressed the importance of Eastern trade mentioned in paragraph 6 and emphasized that certain of the "other licensing" commodities could be imported from convertible currency countries. He mentioned wooden barrels as a product imported entirely from convertible currency countries even though it was not liberalized as an illustration of use of control as a means of ensuring orderly marketing.

14. Another member of the Committee expressed interest in knowing what were the items on "the list" of products that had been mentioned as being licenced only for import from bilateral trading partners. The representative of Iceland said that the main products involved were petroleum products; of lesser importance are coal and potato starch. Even within this range of products, aviation gasoline was imported from convertible currency countries.

15. Another member of the Committee suggested that Iceland might perhaps be a victim of a tendency sometimes noted for each of two bilateral trading partners to feel that the other wants to continue existing arrangements when in fact both might be happier with a more flexible arrangement moving away from the "classical" balanced trade and payments agreement. He urged Iceland to explore the possibility that some move toward flexibility might be acceptable without damage to essential export considerations. The representative of Iceland agreed to this general analysis of the situation as it sometimes occurs, but felt that fish might be harder to sell, as more readily available from alternative sources, than certain more elaborate items such as, for example, a chemical plant.

16. A member of the Committee referred to a statement in the background material that products which Iceland is purchasing under PL 480 arrangements may only be imported from the United States and asked whether this applied to purely commercial purchases. The representative of Iceland confirmed that banks are authorized to restrict purchases of such products to United States sources; but the restriction is not in practice effective, he said, as private traders mainly prefer to buy those particular commodities from the United States so that there is no need to apply the restriction.

General

17. The Committee expressed appreciation for the frank and clear presentation made by the representative of Iceland in this first consultation with Iceland. Satisfaction was expressed at Iceland's progress in liberalization, which it appeared might be maintained and extended in the year ahead within Iceland's possibilities,

especially if domestic inflationary tendencies could be contained. Iceland's dependence on fish exports was recognized but the hope was nevertheless expressed that the marketing of these exports might be effected with progressively less dependence on methods involving discrimination against contracting parties.

The representative of Iceland promised to convey to his Government the views expressed by the Committee.

ANNEX

OPENING STATEMENT BY
THE REPRESENTATIVE OF ICELAND

These are the first consultations under Article XII 4(b) with Iceland since Iceland acceded provisionally to the GATT on 5 March 1964. I therefore think it is appropriate to begin my statement with a brief historical description of the Icelandic restrictive system.

Quantitative restrictions were introduced in Iceland, as into many other countries, during the world depression, in the early thirties. Restrictions have since been applied with differing degrees of strictness in view of the fluctuations in the balance of payments. Until 1950 all commodities were subject to import licence control, although in many cases licenses were granted automatically.

In connexion with the economic stabilization measures of 1950, and influenced by the liberalization efforts of the OEEC, quantitative restrictions were then abolished on a fairly large share of the total imports. The liberalization had to be curtailed within a few years due to the difficult balance-of-payment position and the growing trade with the State-trading countries. The second half of the fifties saw further tightening of restrictions while the economic balance steadily deteriorated.

The year 1960 marks a turning point in the development of the restrictive system. In February of the year a substantial devaluation took place and various other stabilization measures were adopted. The liberalization of imports was an integral part of this comprehensive stabilization programme. In June 1960 about 60 per cent of the imports were liberalized. Every year since the liberalized list has been expanded. Since Iceland's provisional accession to the GATT a little over a year ago new liberalization measures have twice been put in effect. First on 1 August 1964 twenty commodities or groups of commodities were liberalized. Then on 29 January 1965 sixty additional commodities were liberalized and at the same time it was announced that a further fifteen commodities would be freed effective 1 July 1965. The recent liberalization measures have primarily affected a large number of consumer goods. The number of commodities which remain on the restricted list have now been reduced to about 100.

The liberalization has now reached 79.2 per cent of the actual imports in 1964. Document BOP/47, page 3, contains a table of 1963 imports, broken down according to import procedure. The table shows the liberalization percentage as 75.7 as compared with 79.2 according to 1964 imports. The reasons for this difference are that imports of ships and planes, which are liberalized, were abnormally large in 1964 and imports of certain items liberalized in August 1964 increased substantially. In order to complete the comparison between 1963 and 1964, I want to tell you that commodities under global quota represented 10.2 per cent of 1964 imports, (in 1963 11.7 per cent) and other licensed commodities in 1964 10.6 per cent (in 1963 12.6 per cent).

The main commodities under global quota are lumber 1.9 per cent of 1964 imports, plywood and building board 0.7 per cent, iron and steel 2.5 per cent, sugar 1.6 per cent, fishing lines and ropes 0.7 per cent, stockings 0.6 per cent, glass and glassware 0.4 and electrical cables 0.4, totalling 8.8 per cent, which leaves only 1.4 per cent for miscellaneous articles. Other licensed commodities consist mostly of petroleum products 7.2 per cent of 1964 imports, wooden barrels 1.5 per cent and coffee 1.3 per cent leaving only 0.6 per cent for miscellaneous. Generally speaking these commodities are important for the maintenance of trade with the seven countries with which Iceland still has bilateral trade and payments agreements.

These trade arrangements facilitate the sale of Icelandic fish products to Eastern Europe and Brazil. The maintenance of these traditional markets is important for the balance-of-payments position. These exports to the bilateral trading countries have, however, declined in recent years. They represented 14.8 per cent of total exports in 1964 compared with 34.7 per cent in 1959. Consequently, it has been possible to reduce substantially the restrictions that had previously been maintained for the sake of the trade agreements. The growing competitiveness of our trading partners has also furthered this liberal development, which we hope will continue.

Liberalization of imports has been made possible by the favourable development of the balance of payments in recent years. Until 1961 the current account of the balance of payments had for many years shown a substantial deficit, but this changed with the stabilization programme of 1960. Both 1961 and 1962 showed a surplus, 7.1 million and 11.4 million dollars respectively. In 1963 there was a deficit of 4.3 million dollars owing to an unusually large increase in imports. Last year is estimated to show a deficit of 7.7 million dollars, because of the exceptionally high imports of ships and planes. These imports amounted to 22 million dollars, whereas the average annual imports of ships and planes over the last ten years has been 8 million dollars. As these imports are largely financed by foreign credit the foreign exchange reserves continued to grow both in 1963 and 1964. At the end of 1964 the gold and foreign exchange position of the banks amounted to 37 million dollars, which corresponds to four months imports.

In view of the uncertain outlook for the economy the present level of reserves is hardly adequate. The fish catch during the winter season has been considerably less than during the record season last year. Although export prices remain favourable it is to be expected that exports will be somewhat lower in 1965 than last year. During the first quarter exports have been 2.6 per cent lower than in the same quarter of 1964, while imports were 5.8 per cent higher.

Despite the favourable development of the external balance, the internal balance continues to be subject to serious inflationary pressures. Negotiations for general wage agreements, which expire in June, are starting. For the time being it is impossible to predict their outcome. One thing is clear, however, that external balance and the reserve position may be threatened if the negotiations cannot be concluded without large wage increases.

The progress that Iceland has made since 1960 in dismantling restrictions, after thirty years of import controls, is gratifying. The question can, however, always be raised - and we ask it ourselves during our regular reviews of the remaining restrictions - cannot something more be done in this field? This is always subject to discussion. The Government has tried to follow the goal of liberalizing as much as it has seemed possible each time, without risking a relapse. A steady progress forward is better than a jump forward followed by a retreat. I want to assure the Committee that the Government will continue to review the remaining restrictions with the view of gradually abolishing most of them.