

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 FINLAND

1. In accordance with its terms of reference, the Committee has conducted the consultation with Finland under Article XII:4(b). The Committee had before it a basic document for the consultation (BOP/51), L/2367 transmitting the Finnish publication entitled "Import System of Finland as applied from 1 January 1965", 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 completed on 1 November 1965. This report summarizes the main points made in 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 Finland. 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 Finland. The statement made was as follows:

"The International Monetary Fund has transmitted to the CONTRACTING PARTIES the Executive Board decision and background material from its last consultation with Finland under Article XIV of the Fund Agreement. The Fund has also provided a supplementary paper dated October 7, 1965 to supply background information on recent developments.

"With respect to Part I of the Plan for Consultations, relating to balance of payments position and prospects, the Fund invites the attention of the CONTRACTING PARTIES to the Executive Board decision of April 21, 1965¹ taken at the conclusion of the last consultation with Finland under Article XIV of the Fund Agreement. As indicated in the Fund's supplementary background paper a deterioration in the balance of payments position of Finland has subsequently emerged. The general level of restrictions of Finland which are under reference does not go beyond the extent necessary at the present time to stop a serious decline in its monetary reserves.

¹Reproduced in Annex I to this report.

"With respect to Part II of the Plan for Consultations, relating to alternative measures to restore equilibrium, and with respect to Part III, relating to system and methods of the restrictions, the Fund again invites attention to the decision taken at the conclusion of its last Article XIV consultation with Finland. The Fund has no further comments on these matters at this time."

Opening statement by the Finnish representative

4. In his opening statement, the full text of which is reproduced in Annex II to this report, the representative of Finland said that at the present time his country was facing a serious balance-of-payments crisis. It was estimated that the current account deficit for the whole of 1965 would be as high as Fmk650 million, compared with Fmk565 million for 1964. In 1964 this deficit had largely been covered by long-term borrowing abroad but a sharp tightening of the capital markets in Western Europe and the United States had meant that in January-September 1965, Finland's net foreign long-term borrowing had been at a level of only Fmk45 million, compared with Fmk390 million during the corresponding months of 1964. From the beginning of this year until the middle of October the Bank of Finland has lost nearly one third of its net foreign exchange reserves, the decline being in convertible currencies. At the present time reserves equalled about two months' imports.

5. Certain corrective measures consistent with Finland's international commitments had been taken in spring 1965. These measures provided for a tighter credit policy, increased excise duties on passenger cars and further restrictions on hire purchase transactions. Various measures to facilitate the financing of export credits were also included. To their regret the Finnish authorities had noted that additional measures might still be needed and a measure curtailing the liberal treatment accorded the Finnish tourist had entered into force on the day of the consultation. The new balance-of-payments measures are also planned to include further selective relaxations of credit restrictions regarding exports. Additional measures to encourage the development of new exports were being studied. The Finnish authorities firmly intended to design their internal fiscal and monetary policies with due regard to the deteriorating external payments situation.

6. The representative of Finland pointed out that, despite the growing trade deficit, his authorities had in 1965 continued to eliminate quantitative restrictions on imports. On 1 August 1965 four global quotas had been abolished, with the result that the products had been liberalized, and twelve quotas partly liberalized. As of 1 January 1965 global quotas had been expanded by an average

of 27 per cent compared with 21 per cent in 1964. In spite of the difficulties which his Government faced it was planning further liberalization of its imports at the beginning of 1966 in conformity with its obligations towards EFTA.

7. In conclusion the representative of Finland said that during the current year the multilateral import system had been extended to cover four new countries and certain measures had been undertaken with a view to liberalizing trade with countries to which Finland applied bilateral import treatment.

Balance-of-payments position and prospects

8. The Committee thanked the representatives of Finland and the International Monetary Fund for the comprehensive documentation which they had provided and for the informative opening statement which had been made. It was recalled that at the last consultation with Finland the Finnish representative had warned the Committee against too optimistic a view of the external financial position and prospects of his country. The Committee noted the serious balance-of-payments difficulties which had developed since that time and the uncertain outlook for the future. The Committee therefore particularly welcomed the fact that further measures had nevertheless been taken to reduce restrictions on trade and the intimation that the Finnish authorities planned to continue the process of liberalization in 1966.

Alternative measures to restore equilibrium

9. In reply to questions on the scope of the credit restrictions imposed by the Finnish authorities in order to eliminate the pressure of overall demand, the representative of Finland recalled that as had been explained at earlier consultations in the Committee the monetary arsenal at the disposal of his authorities was not as highly developed as in other Western European countries. The main measures which had been used to exercise control over the commercial banks were a tightening of rediscount conditions and the utilization of extra interest charges penalizing banks not keeping within the target figure laid down by the central bank, which provided for a moderate annual increase of 6 per cent in the volume of credit. The central bank could also use moral persuasion and could in the last resort refuse to rediscount bills from a particular bank. There was in Finland no compulsory variable cash reserve requirement system but draft legislation was under examination in the parliament and it was hoped that the legislation would be enacted during the current session. The Finnish authorities had, indeed, preferred to use those measures at present at their disposal rather than quantitative restrictions on imports.

10. One member of the Committee inquired concerning the effects of Finland's new measures on cars, and certain other members indicated that their exports of cars to Finland had been substantially affected by the imposition of increased

excise duties and further restrictions on hire purchase transactions to which reference had been made in the Finnish opening statement. Replying to the questions he explained that shortly before the introduction of these measures in the spring of 1965 imports had suddenly increased very considerably in anticipation of the tax, but that since that time the level of imports had of course been below normal. This made it difficult to estimate the longer-term effects of the measures. The representative of Finland said that he would convey the concern expressed to his Government.

11. In reply to questions on steps recently taken to encourage the development of new export products (in contrast to the traditional forest-based export products) the representative of Finland explained that a large number of relatively minor measures had been taken, and it was hoped that these would gradually produce results. Among the measures taken were market research, participation in industrial fairs, training of foreign marketing personnel and an expansion of the number of commercial secretaries in the foreign service.

12. In answer to questions the Finnish representative said that an attempt had been made to remove hindrances to foreign investment in Finland, but that no special incentives which would not apply equally to Finnish capital were to be introduced as his Government had adopted a non-discriminatory policy in this regard.

System and methods of the restrictions

13. The Committee welcomed the further measures taken by Finland since the last consultation to reduce discrimination arising from bilateralism. Certain members noted that Finland still had bilateral trade and payments agreements with ten countries. In reply to questions on the remaining bilateral agreements, the representative of Finland pointed out that these fall into two distinct categories, those with countries with centrally-planned economies and those with members of the International Monetary Fund. The Committee would be aware of the difficulty of dispensing with bilateral agreements in the first category. As to agreements with members of the Fund, the representative of Finland recalled that since the last consultation agreement had been reached on the termination of the bilateral payments agreement with Turkey; his Government had also expressed its willingness to terminate the two remaining bilateral agreements with Fund members (Greece and Colombia) and had made specific proposals to this end. He pointed out however that the termination of these agreements did not depend on his Government alone. Members of the Committee welcomed the declaration of the representative of Finland on the termination of bilateral agreements with members of the Fund.

14. One observer referred to the statement made in the basic document supplied by the Government of Finland (BOP/51, page 3) that Finland's bilateral trade and payments agreements were, with one exception, of a rigid bilateral type. He said

that his Government's position on the question of bilateralism versus multilateralism was well known and pointed out that the recently concluded agreement between his country and Finland could not be considered as being of a rigid bilateral type as during the negotiation of the agreement his authorities had requested modifications in the direction of the multilateralization of payments and the liberalization of imports into Finland from his country. The Finnish Government had, however, felt unable to accept these proposals at that time. The representative of Finland noted this statement. He also recalled the last paragraph of his opening statement, in which reference was made to measures recently taken by his Government with a view to liberalizing import controls in trade with countries to which Finland applies bilateral import treatment.

15. In response to a question, the representative of Finland informed the Committee of the breakdown of imports of coarse grains and alcoholic beverages as between multilateral and bilateral countries. In 1964 the f.o.b. values of imports from multilateral and bilateral countries respectively were, in thousands of Finnish marks, as follows: grain, 12,896 and 28,331; alcoholic beverages, 18,568 and 1,025. In reply to questions he said that both were imported by State monopolies which in their operation were guided by commercial considerations and, in the case of the State monopoly for alcoholic beverages, by social considerations.

16. Reference was made to the statement made in the Finnish opening remarks that in conformity with obligations towards EFTA the Finnish authorities were planning further liberalization of imports at the beginning of 1966. The representative of Finland confirmed that, as in past years, such liberalization would be applied to all countries and territories to which Finland applied multilateral import treatment.

Effects of the restrictions

17. One member of the Committee recalled that at the last consultation his delegation had mentioned that details of Finnish quotas for apples and pears were usually not made available in sufficient time for distant exporters to make accurate reservations of shipping facilities and had received certain assurances from the Finnish authorities on this matter (see L/2299, paragraph 22), the understanding being that publication of the details of import quotas not later than the first week in January each year would be acceptable. His country had in December 1964 instructed its Trade Commissioner in the area to advise on details of the quotas as soon as they became available. After several enquiries advice of the quotas in respect of the licensing period 1 April to 30 June 1965 was finally received on 30 April 1965, i.e., one month after the licensing period had commenced. A firm undertaking was again requested in the Committee that notification of the details of the quotas for apples and pears would be given

sufficiently early for distant exporters to reserve shipping space. The Finnish representative agreed to report this statement as well as the intervention of another member on the subject of apples and pears to his authorities, who would definitely make their very best endeavours to deal with the matter in a way satisfactory to the exporting countries concerned.

General

18. The Committee once again thanked the Finnish representative for the detailed information supplied during the course of the consultation. The Committee noted the undeniable deterioration in the Finnish balance-of-payments position since the time of the last consultation and, in the light of this, welcomed the steps taken to reverse this trend; it was particularly gratifying that Finland had been able to avoid new balance-of-payments restrictions and that it had even been possible to eliminate certain quantitative restrictions on imports, to increase the size of global quotas and to reduce discrimination arising from bilateralism. They expressed the hope that further progress would be possible in the forthcoming period.

19. The representative of Finland thanked the Committee for its sympathetic consideration of the situation of his country and assured its members that their views would be transmitted to his Government.

ANNEX IInternational Monetary Fund Executive Board Decision
Taken at the Conclusion of the Fund's Consultation
with Finland on 21 April 1965

1. The Government of Finland has consulted the Fund under Article XIV, Section 4, of the Fund Agreement concerning the further retention of its transitional arrangements.
2. Since mid-1963 the gross national product has been growing at an annual rate of some 5 to 6 per cent. Despite the absence of excessive demand pressures, large increases in wages and costs occurred in 1964 and the cost of living index rose by 10 per cent. There is an urgent need for better incomes policy arrangements so as to avoid further substantial increases in costs.
3. Exports increased by 12 per cent in 1964 and imports by 21 per cent. The balance of payments deficit on current account rose from \$20 million in 1963 to \$131 million in 1964. There was a substantial net inflow of foreign capital in 1964, largely in the form of foreign bond issues by both the Government and the private sector. Gross official reserves rose by \$62 million and at the end of the year they amounted to \$409 million, including the gold tranche.
4. In 1964 the Government increased taxes and the deficit on current and investment account of the government budget was reduced; a further reduction in this deficit is envisaged for 1965. Owing to its large-scale, long-term borrowing abroad (\$178 million), the Government's call on the domestic credit market was markedly lower in 1964 than in the previous year. While the Bank of Finland continued to pursue a policy of monetary restraint in 1964, the reduction in government borrowing and the net influx of foreign exchange enabled the banks to increase credit to the economy by 13 per cent during the year.
5. Finland has taken further measures to reduce restrictions on trade and payments and discrimination arising from bilateralism. The Fund welcomes these measures and considers that further progress in this direction could contribute toward the maintenance of price stability. The Fund urges Finland to terminate the remaining two bilateral payments agreements with Fund member countries.
6. In concluding the 1964 consultations, the Fund has no other comments to make on the transitional arrangements maintained by Finland.

ANNEX II

Opening Statement by the Finnish Representative

You may recall that during our last consultations almost exactly a year ago my predecessor painted a rather sombre picture of the rapid deterioration of the Finnish balance-of-payments situation. I am sorry to say that in retrospect even that picture appears to have been somewhat too optimistic. Apart from the permanent structural difficulties of our balance of payments which have been discussed in this Committee during a number of years, Finland is today facing what really could be termed a serious balance-of-payments crisis.

In 1964, our balance-of-payments deficit on current account was alarming enough, amounting to FMks.565 million, equivalent to \$175 million. In that year, however, an atmosphere conducive to real crisis measures did not yet exist, since we were able to borrow heavily abroad on long term. In fact, the surplus on the capital account - largely due to a record amount of FMks.344 million raised through ten public bond issues in Western Europe and the United States - was so large that it not only covered the current account deficit but also sufficed to create a modest increase in our foreign exchange reserves.

However, towards the end of last year it was felt that such a borrower's paradise as existed in 1964 on the international capital markets could not continue. At the same time, the available forecasts indicated that our current account deficit would continue to increase. The fears regarding the ability of the foreign capital markets to absorb further Finnish bond issues were, alas, transformed into grim realities in a matter of a few months. The members of the Committee are surely aware of the rather sudden and sharp tightening of the capital markets in Western Europe and in the United States, our main sources of external long-term finance. I need not go into the relatively technical and complex reasons for this tightening, but I should like to quote some statistics which indicate its impact on my country. In January-September 1964 we were able to borrow abroad on long term a net amount of FMks.390 million. In the corresponding months of the current year Finland's net foreign long-term borrowing remained at the alarmingly low level of FMks.45 million, or less than \$15 million. For a rapidly developing economy such a violent drop in available external resources carries strong repercussions throughout production, commerce, monetary policy and also the Government's fiscal policy.

As I indicated a moment ago the current account deficit has continued to grow. This year imports have again been rising faster than exports. On the one hand, imports of raw materials, investment goods and quite particularly of passenger cars have continued to expand rapidly. On the other hand, the rate of growth of exports is slackening. The Finnish authorities estimate that the current account deficit for the whole of 1965 will be as high as FMks 650 million, which compares with the 1964 figure of 565 million.

In the absence of new foreign long-term loans such a deficit is bound to be reflected in the foreign exchange reserves of the nation. From the beginning of this year until the middle of October the Bank of Finland has thus lost nearly one third of its net foreign exchange reserves, and, as indicated in the documentation submitted to you by the International Monetary Fund, the decline has taken place in convertible currencies. At their peak early this year, the Bank of Finland reserves corresponded roughly to three months' imports. At present these same reserves equal about two months' imports. The indications are that without effective corrective measures the balance-of-payments deficit in 1966 would still be some two thirds of this year's figure. Since the foreseeable future carries no promise of a revival of our possibilities to borrow on the tight international capital markets, we might end up in a little over a year's time with a foreign exchange reserve equivalent to only ten or twenty days' imports.

These are the rather dismal facts based on the best forecasts available today. It is obvious that in such a situation something has to be done.

In early April this year the Government and the Bank of Finland got together to discuss various measures designed to ward off the impending threat to the country's external liquidity. At the outset, it was agreed that the steps to be taken would not include such measures as quantitative import controls, increased customs duties or import surcharges. Nor could we, politically or economically, afford the "horse cure" of natural self-corrective methods, which through a drastic reduction of the central bank money, as the foreign exchange reserve declines, would gradually eliminate the excessive import demand but would also lead to a tighter liquidity position in the economy as a whole, increased unemployment, slow-down of production and so on.

Thus the Government's programme at that time mainly consisted of internal and external measures which would not affect our existing international commitments towards the CONTRACTING PARTIES, our EFTA partners and the International Monetary Fund. The main elements of measures undertaken last spring were a tighter credit policy, increased excise duties on passenger cars (which, as members of the Committee will remember, are de facto free of quantitative restrictions), and further restrictions on hire purchase transactions.

Various measures to facilitate financing of export credits were also included as well as a very modest publicity campaign designed to further the consumption of competitive domestic products. We in Finland have unfortunately had to put up with a sort of national inferiority complex since the war, and the snob value generally attached to foreign products tends to be more pronounced in our country. We feel that this underestimation of national production is something that we can cure.

The measures which I have described have now been in operation for about five months. To our regret we note that additional corrective measures might still be needed. I want to underline again that our approach to the problem is not one of intensifying existing import restrictions. On the contrary, in spite of the serious balance-of-payments situation, an additional liberalization of our import trade was carried out on 1 August 1965, and in conformity with our obligations towards EFTA we are planning further liberalization of our imports at the beginning of 1966.

One of the new balance-of-payments measures which by the way has entered into force this very morning is a curtailing of the liberal treatment which the Finnish tourist has enjoyed in comparison with some of his continental European counterparts. The value of goods which a returning Finnish resident may import free of duty and purchase tax has been reduced from FMks.150 to FMks.70, and the amount of Finnish currency which he may take with him when departing has been cut down by half from FMks.200 to FMks.100. The normal foreign exchange tourist allowance is not affected, however, and therefore we believe that these reductions do not circumscribe the traditional freedom of travel. We fully understand that such measures affect some of our neighbouring countries, particularly Sweden where in 1964 about 45 per cent of the total Finnish tourist expenditure of FMks.222 million was used.

New balance-of-payments measures also include further selective relaxations of credit restrictions regarding exports, which will enable us to compete on fair and equal terms with other suppliers on international markets. Additional measures to encourage the development of what we call "new exports" - in contrast to the traditional ones, pulp, paper and other forest products - are being studied with due consideration given to our international obligations.

The Finnish authorities hope that a programme such as I have just outlined will prove sufficient to arrest the present alarming decline in our foreign exchange reserves before they fall to a level which would endanger the country's international liquidity and the good reputation which Finland, fortunately, enjoys on the international capital markets. The Finnish authorities firmly intend to design their internal fiscal and monetary policies with due regard to the deteriorating

external payments situation, although in the case of fiscal policy such a task is a rather difficult one in an election year. One of the major unknown factors is the forthcoming wage settlement, since existing wage agreements expire at the end of this year. New guidelines for wage policies are being negotiated right now by the labour organizations. The authorities hope that the new collective agreements will not increase wages and fringe benefits beyond the expected normal growth in productivity.

I should now like to turn to the subject of quantitative restrictions.

In spite of the fact that our trade deficit has still been growing from last year's figure we have continued to eliminate quantitative restrictions on imports. However, due to the critical balance-of-payments situation it has not been possible to proceed with the liberalization as rapidly as in previous years.

We have abolished as of 1 August 1965 four global quotas, thus reducing the total number of quotas in the global quota list to fifty. Further, twelve quotas were partly liberalized. These new measures covered all together seventy-one tariff items or sub-items, to the value of 47 million marks based on 1964 figures.

In addition I should like to mention that global quotas were expanded as of 1 January 1965 on the average by 27 per cent which compares with 21 per cent in 1964. As in previous years, the actual licensing has in many instances considerably exceeded the originally fixed quota limits, particularly in the case of passenger cars.

In spite of the difficulties to which I have referred numerous times the Government plans to continue the liberalization in 1966 partly by increasing the global quotas and partly by further reducing the number of these quotas.

During the current year the multilateral import system has been extended to cover four new countries and it is at present applicable to more than 100 countries and almost as many territories.

Before concluding my statement I should like to inform this Committee of certain measures taken by my Government with a view to facilitating trade with countries to which Finland applies bilateral import treatment. According to a Cabinet Decree of 24 September 1965, the Licensing Office may decide that the import from the above-mentioned countries of certain commodities, liberalized in our trade with the multilateral countries, is permitted without an import licence provided that the country of purchase and that of origin is the same. The Licensing Office may, however, reintroduce the import licence requirement in respect of these commodities if such a step is considered necessary for instance for balance-of-payments reasons or in cases where the liberalization measure causes or threatens to cause injury to Finnish producers of a similar or competitive product.