

**GENERAL AGREEMENT ON  
TARIFFS AND TRADE**

Committee on Balance-of-Payments Restrictions

REPORT ON THE 1984 CONSULTATION WITH HUNGARY

1. The Committee consulted with Hungary on 22 May 1984, in accordance with its terms of reference, pursuant to Article XII of the General Agreement and the 1979 Declaration of the CONTRACTING PARTIES on Trade Measures Taken for Balance-of-Payments Purposes (BISD 26S/205). The consultation was held under the Chairmanship of Mr. J.N. Feij (Netherlands). The International Monetary Fund was invited to participate in the consultation, in accordance with Article XV of the General Agreement.

2. The Committee had the following documents before it:

Basic Document	(BOP/243)
Secretariat Background Paper	(BOP/W/79)
Trade Measures taken for Balance-of-Payments Purposes	(L/5363 and Addenda 1-3)
IMF Recent Economic Developments, dated 23 December 1983	

Opening Statement by the Representative of Hungary

3. In his opening statement, (the full text of which is attached as Annex I), the representative of Hungary referred to the economic conditions in 1982 which had first led his authorities to introduce restrictive measures for balance-of-payments purposes. He recalled the conclusions of the Committee at the last consultation in 1982 (BOP/R/131, paragraph 19). The principal objective of Hungary's economic policy in 1983 and 1984 had been to achieve and sustain an improved current account position in convertible currencies. Hungary had relied primarily on restrictive internal measures to limit domestic demand, as the external economic and trading environment remained unfavourable. The measures aimed at keeping down real consumption through curbs on wage increases, higher social security contributions, higher rates of price increases accompanied by significant reductions in consumer price subsidies. Measures were also taken to curtail the volume of fixed investment. In addition, the forint had been devalued by 7 per cent in 1983 and a further 3 per cent in early 1984 to promote a more rational use of imports and improve the competitive

position of Hungarian exporters on international markets. As a result of these measures, GNP increased only slightly in 1983, and domestic demand decreased by 2 to 3 per cent; industrial output increased by only 1 per cent. Agricultural production was set back by a severe drought. Exports settled in convertible currencies increased slightly in volume but remained unchanged in United States dollar terms, while imports settled in convertible currencies increased somewhat in volume but decreased in dollar value. The positive convertible currency trade balance of US\$877 million on a balance-of-payments basis, while approximately US\$100 million higher than the previous year, fell short of expectations due primarily to a US\$200 million export loss caused by the effects of drought, unfavourable world price developments, and persistent protectionist measures abroad. The current account balance in convertible currencies showed a surplus of US\$297 million, an improvement of US\$360 million over the previous year.

4. Despite unfavourable developments in the external environment, the Hungarian authorities had made progress towards easing the import restrictions introduced in 1982. In January 1984, the number of import quotas had been reduced from 12 to 6 and the 20 per cent import surcharge on components had been eliminated as of 1 April 1984. The key objective in 1984 continued to be the further improvement of Hungary's external balance, through the regulation and further reduction of domestic demand. The authorities were making every effort to reach a stage when restrictive import measures would no longer be necessary. In order to accomplish this, the confidence of international financial circles must be maintained. On the other hand, internal policies of the Hungarian authorities should be matched by corresponding trade policy efforts by Hungary's major partners with a view to liberalising and facilitating market access for Hungarian products.

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 text of which is attached as Annex II.

Balance-of-Payments Position and Prospects; Alternative Measures to Restore Equilibrium

6. Members welcomed the improvement which had taken place in the trade and current account balances of Hungary with convertible currency areas, and the easing in restrictions which had taken place in 1984. One member stated that in his view, the consultation could be used as an opportunity to identify areas where Hungary's trading partners might take action to improve its market access. In this connection, the Chairman recalled that all internal and external factors were to be taken into account in Article XII consultations, as set out in paragraph 2 of the 1970 procedures (BISD 18S/49).

7. One member noted that reductions in private and public consumption of  $\frac{1}{2}$  per cent and  $1\frac{1}{2}$  per cent, as well as a cut of over 8 per cent in gross fixed investment, were envisaged in the 1984 Hungarian plan. This was the fifth consecutive year in which the main burden of adjustment fell on investment. He asked what measures were envisaged to ensure that such cuts would not have an adverse effect on future GDP and export growth. He also noted that the main external objective for 1984 was to improve the convertible currency current account balance principally through an increase in the trade surplus, and asked what products and markets were envisaged as contributing to this increase. He also asked for greater detail to be provided on the amount of government subsidies and on plans to reduce them.

8. In reply, the representative of Hungary stated that the possible long-term adverse effects of cutbacks in investment were alleviated by ensuring that scarce capital resources were channelled to more efficient firms or projects with a higher than average rate of return. Disbursements of credits were concentrated in the export and energy-saving sectors. Products to be exported should be determined by the enterprises on the basis of their assessment of market possibilities. As to the subsidies contained in the budget, he stated that roughly half of them were devoted to consumption subsidies and half to the restructuring of industry. The objective was to reduce the share of subsidies within budgetary expenditures, but caution must be exercised in reducing consumption subsidies because of social considerations.

9. Some members expressed the view that a complex array of factors had led to the present balance-of-payments situation, and commented on Hungary's comparative trade performance vis-à-vis convertible currency areas and other areas. In their opinion, subsidies extended for exports to Eastern trading area countries might indicate that such exports were not particularly profitable. They called attention to the increasing trade deficits with other Eastern trading area countries, as against the recovery of the trade balance with convertible currency areas. Hungary's exports to these members had grown by 8 per cent during 1983, and the trade deficit with them had been halved. Hence they expressed surprise that so much of Hungary's basic document for the consultation should be devoted to measures affecting its exports to them. While welcoming the improvement in the Hungarian economic situation and the reduction in Hungary's import restrictions, they noted that the remaining restrictions still covered a significant proportion of trade.

10. The Hungarian representative stated in reply that the subsidies referred to were made necessary by the different price-setting methods of Hungary's trading partners in non-convertible currency areas. Regarding the measures taken by Hungary's trading partners affecting Hungarian exports, mentioned in document BOP/243, he stressed that the importance given to particular measures described in that document was due to the importance of that market for Hungary's exports.

11. One member, referring to the difference between trade patterns with convertible currency areas and clearing arrangement countries noted that the trade deficit with clearing arrangement countries was financed at minimal interest rates and over long maturity periods, and indeed trade had increased most with these countries.

12. One member asked how Hungary would be able both to maintain its debt servicing requirement, estimated at US\$2 billion in 1984 as well as an adequate level of foreign exchange reserves, equal to five months' imports, given a projected current account surplus of US\$400 million. He also enquired about the likely effect of the removal of the 20 per cent surcharge on Hungarian imports. The Hungarian representative replied that these objectives could be achieved partly through borrowings from the International Monetary Fund and the World Bank and from the international money market, and partly through import credits. Net Hungarian indebtedness was expected to be reduced by some US\$400 million in 1984, equivalent to the projected current account surplus. As to the effect of the removal of the surcharge, the representative of Hungary drew attention to the fact that this, or the phasing out of other import restrictive measures, would not necessarily result in a rise in imports, since measures taken to contain domestic demand would be expected to have an effect on the volume of imports, due to the high import content of investment and current consumption.

#### System, Method and Effects of Restrictive Import Measures

13. In the context of recent improvements in Hungary's balance-of-payments situation, and bearing in mind the provisions of Paragraph 1(c) of the 1979 Declaration, a number of members asked Hungary to announce a time schedule for the removal of remaining restrictions, including quotas on consumer goods imports, and a return to automatic import licensing.

14. One member asked what value of trade was involved in the annual import quota for consumer goods from convertible currency sources, as well as a detailed product breakdown of the quotas. He also asked when Hungary could consider reverting to a system of automatic licensing. In addition, he wished to know Hungary's intentions with regard to allowing more firms to import directly rather than through specialized foreign trading companies.

15. The representative of Hungary replied that it was his authorities' intention to phase out all restrictions and to revert to a system of automatic licensing as soon as possible, although he could make no firm commitment as to a timetable. The consumer goods quotas had been notified to the Group on Quantitative Restrictions and Other Non-Tariff Measures and was included in the documentation issued by this Group (NTM/W/6/Rev.1). Data on the value of quotas for 1981, 1982 and 1983 had been provided in the Part IV Consultation background note for Hungary (COM.TD/W/385). In relation to the decentralization of foreign trade, the Hungarian representative noted that there were currently some 220 companies authorized to carry out foreign trading activities on a permanent basis, and several hundred ad hoc authorizations were granted last year. It was the intention of the Hungarian authorities to continue to widen the number and scope of such activities.

16. A question was posed regarding figures provided by the secretariat, in paragraph 29 of BOP/W/79, on the estimated trade effects resulting from the reduction of import quotas and the elimination of the import surcharge. In clarification, it was stated that trade covered by import quotas had been reduced by some US\$120 million at 1983 values; approximately US\$351 million, or some 7 per cent of 1983 imports, thus remained subject to quotas in 1984, after allowing for recent quota increases. Imports affected by the import surcharge by Hungary stood at US\$512 million in 1983.

17. The Hungarian representative reiterated that his authorities were making every effort to reach a stage when restrictive import measures would no longer be necessary; in this connection, however, he stressed that the external environment was beyond the control of the Hungarian authorities and that an improvement of the external economic and trading environment would certainly facilitate Hungary's adjustment efforts.

### Conclusions

18. The Committee noted that since the last consultation Hungary's balance-of-payments situation had improved as a result of the demand management measures taken, despite some continuing negative external factors. The Committee welcomed the efforts made by Hungary to ease the restrictions introduced in 1982, in particular the lifting of the 20 per cent import surcharge on 1 April 1984 and the partial elimination of quantitative restrictions, and noted the transparency of the measures taken. Taking into account the various internal and external factors affecting Hungary's balance-of-payments position, the Committee reiterated the hope that in the light of progress achieved in internal adjustment, Hungary would soon be in a position to announce a timetable for the phasing out of the remaining restrictions and the return to automatic licensing, in accordance with Paragraph 1(c) of the 1979 Declaration on Trade Measures Taken for Balance-of-Payments Purposes.

ANNEX I

Statement by the Representative of Hungary

1. This is the second time, that Hungary takes part on a consultation with the Contracting Parties on the trade measures taken for balance-of-payment purposes. As well known for the members of this Committee Hungary introduced these measures under Article XII:2/a/ of the General Agreement as from September 1, 1982 in order to safeguard the country's balance of payment position.

2. Hungary's liquidity position sharply and suddenly deteriorated in 1982. The country's reserve position also worsened largely due to external economic conditions; the national economy had to face with the cumulative effects of spreading protectionism and discriminatory trade measures, the sharply deteriorating international financial environment, as the prevailing high interest rates, limited credit access possibilities and the rapid withdrawal of short-term deposits held by the National Bank of Hungary. In that situation the instruments and measures of the domestic demand management policy could not be sufficient by themselves, to maintain the country's paying capacity and the Hungarian authorities were compelled to introduce certain import restrictive measures, on a temporary basis to prevent a further sharp decline in the country's monetary reserves and to assure a reasonable rate of increase of those reserves.

As during the last consultation the Committee on Balance-of-Payment Restrictions recognized: "Hungary had serious balance-of-payments problems, which lead to the invocation of Article XII. The committee noted that Hungary's balance-of-payment situation had deteriorated sharply in the early part of 1982 against the

background of worsening external economic conditions, adverse trade policy measures, increased difficulties in foreign borrowing, the withdrawal of short term funds by some lenders and domestic demand policies that were less effective than expected".

3. Speaking about the period that have passed since the last consultation, in 1983 the principal objective of the economic policy was to achieve a significant and sustainable improvement in the current account in convertible currencies. In achieving this aim, the Hungarian authorities relied mostly on restrictive internal economic policy measures, as the unfavourable external economic environment still prevailed and market access possibilities and terms of trade even worsened. Further measures were taken to limit domestic demand. Real consumption was kept down through curbs on wage increases, higher social security contributions and higher rate of price increases accompanied by significant reductions on consumer price subsidies. Several measures intended to curtail the volume of fixed investments. The 7 per cent devaluation of the forint in 1983 /followed by a further 3 per cent devaluation in early 1984/ aimed to promote a more rational use of imports and to improve the Hungarian exporters' competitive position in the international markets.

In 1983, as a result of these measures the GNP only slightly increased, while domestic demand decreased by 2-3 per cent. Industrial output increased only by 1 per cent. Agricultural production was set back by a very severe drought.

Exports settled in convertible currencies increased slightly in volume but remained unchanged in US \$, because of the unfavourable price movements in the world market. Imports settled in convertible currencies somewhat increased in volume, but decreased in \$ value terms.

The trade balance in convertible currencies resulted a surplus of US \$ 877 million /on balance-of-payment/ this was about 100-million US \$ higher than in the previous year, but less than expected, due mainly to the effects of the drought on exports amounting to a loss of above 200 million US \$, the unfavourable development of prices and to the effects of persistent protectionist measures in the world.

The current account balance showed a surplus of 297 million US \$, representing of an improvement of 360 US \$ compared to the previous year.

4. The external economic conditions which have very significant influence on the Hungarian economy have not improved, market access possibilities have been limited, and in the agricultural sector the market conditions definitely worsened. The export possibilities are also influenced by such factors as: strong export subsidization by some countries on third markets, in certain cases solvency problems of our trading partners etc. Despite these unfavourable developments in the external environment, due to domestic demand management resulting some improvement in the reserve position Hungarian authorities made some progress towards the easing of the import restrictions introduced in 1982.

The number of import quotas was diminished from 12 to 6 as from January 1984, the 20 per cent import surcharge on the imports of components was eliminated as from April 1, 1984.

5. In 1984 the key objective of the Hungarian economic policy remains the further improvement of external equilibrium. In achieving this goal most important policy measures remain the regulation and further reduction of domestic demand.

The Hungarian authorities make every possible effort to achieve a sustainable balance of payment position, to improve the per-

formance of its economy in order to arrive to a stage when the import restrictive measures are not needed anymore. The economic policy objectives can be realized and the efforts aiming at the gradual elimination of the import restrictions can lead to positive results if the confidence of the international financial circles vis-à-vis Hungary is maintained and the internal efforts of Hungarian authorities are supported and accompanied by corresponding trade policy measures of Hungary's major partners with a view to liberalizing, facilitating and improving the conditions for the market access of Hungarian products.

ANNEX IIStatement by the Representative of  
the International Monetary Fund

The key objective of Hungarian economic policy over the past several years has been to achieve a sustained improvement in the balance of payments position. The external current account deficit in convertible currencies was reduced, from US\$727 million in 1981 to US\$63 million in 1982 (or by the equivalent of nearly 3 percentage points of GNP). Although this strengthening permitted a moderate recovery in official reserves during the last three quarters of 1982, the external liquidity position remained very tight. The authorities' adjustment efforts were thus strengthened in late 1982. A stand-by arrangement for SDR 475 million was approved by the Fund on December 8, 1982.

However, the buoyancy of demand, already apparent in mid-1982, carried over into early 1983, and necessitated additional action in the course of 1983. In the early months of the year, measures were adopted which sought to reduce the rate of investment through a tightening of credit and an acceleration of credit repayment schedules. Measures to restrain consumption were introduced around midyear and included a reduction of consumer subsidies, increases in administered prices, a virtual freezing of wages in the government sector, and a depreciation of the forint. Steps were also taken to reduce the liquid funds of enterprises further and to increase the cost of investment.

The efforts of the authorities in pursuit of their adjustment program in 1983 met with only partial success. The current account surplus in convertible currencies for the year as a whole reached some US\$300 million, about half the original target. The shortfall from the objective of the program stemmed mainly from a greater-than-expected fall in the terms of trade and a sharp drought-related reduction in the supply of farm exports. Nonetheless, the volume of exports settled in currencies other than the ruble is estimated to have grown--after adjustment for the effect of increased re-exports--by some 4.9 percent. The forint was depreciated against the basket of currencies to which it is pegged by about 18 percent in nominal terms--7 1/2 percent in real terms--between the middle of 1982 and the end of 1983.

Despite the various measures to contain domestic demand introduced in 1983, final domestic absorption is estimated to have been reduced substantially less than originally programmed. Household incomes grew more rapidly than envisaged, and the increase in consumer prices, at 7.3 percent, fell short of expectations. However, the resulting over-run on real personal consumption was more or less matched by additional

output. The latter was associated in large part with a greater-than-anticipated expansion of private economic units, whose activities the authorities had liberalized in 1982. Fixed investment outlays also declined less in real terms than foreseen under the program. The stronger-than-programmed demand, however, appears to have spilled over into trade in convertible currencies only to a limited extent. The import restrictions vis-a-vis the convertible currency area introduced in September 1982, were maintained. The excess in fixed investment expenditures was accommodated by a rundown of machinery stocks, larger-than-anticipated imports from the nonconvertible currency area, and additional output in the construction sector. On the whole, real domestic demand is estimated to have fallen by 1.5-2 percent in 1983.

The stronger current account has brought a significant improvement in the attitude of financial markets toward Hungary. During the first six months of 1983, there was still a net outflow--albeit on a smaller scale than in 1982--of maturing short-term deposits. Since then, the availability of both short- and long-term capital has improved. In particular, short-term capital inflows amounted to SDR 390 million in 1983, compared to an outflow of SDR 900 million in the preceding year. At the same time, the maturity structure of the stock of external liabilities began to improve. Gross official reserves in convertible currencies rose to the equivalent of 5.6 months of imports in convertible currencies at the end of 1983, compared with 3.6 months of imports a year earlier.

A new one-year stand-by arrangement for Hungary in an amount equivalent to SDR 425 million (80 percent of quota) was approved by the Executive Board on January 13, 1984, in support of a program designed to strengthen the external position further. Key demand management policy elements include wage and price measures aimed at achieving a small reduction in real household income, improved incentives to save, a tighter credit policy, and a further improvement of the position of the state budget. Reflecting these measures, domestic demand is programmed to be reduced by 2 percent in real terms in 1984. In addition, structural reform measures are being implemented to increase the efficiency of production and the intersectoral allocation of resources. These include steps to liberalize the process of price and wage formation, increase the autonomy of enterprises, and improve financial intermediation.

The authorities are committed to continue making active use of exchange rate policy vis-a-vis the convertible currency area, in order to ensure the profitability of exports and promote a more rational use of imports. The forint was devalued further, by 3 percent, against its basket of currencies on February 7, 1984; at the same time, tax rebates to exporters and fees on imports were reduced.

The program for 1984 envisages a current account surplus in convertible currencies of US\$400 million, with most of the US\$100 million improvement over 1983 deriving from an increase in the trade surplus.

The larger trade surplus is expected to be achieved despite a projected further worsening of the terms of trade and the introduction of further liberalization measures. Accordingly, a strong performance of exports, with a further small gain in market shares, will again be required.

Effective September 1, 1982, several measures were introduced to restrict imports. Imports of specified primary products were made subject to quantitative restrictions, while imports of component parts became subject to a 20 percent surcharge. In addition, all import licenses were made subject to discretionary individual approval. The import license is subject to Fund jurisdiction as a joint exchange and trade license. Also, the quotas on imports of certain raw materials are part of this licensing system. The tightening of the import licensing system and the imposition of certain import quotas since September 1982 amounted to an introduction of an exchange restriction, which the Fund approved on a temporary basis under Article VIII, Section 2. Hungary avails itself of the transitional arrangements of Article XIV with respect to certain other exchange measures.

While the authorities had intended, in 1983, to eliminate the restrictions introduced in late 1982, unfavorable developments on the capital account in early 1983, and uncertain prospects for the remainder of the year concerning both capital inflows and foreign prices, resulted in a postponement of their removal. Nevertheless, the quota and import licensing restrictions were eased partially as of January 1, 1983. Additional steps were taken in early 1984. From January 1, 6 of the 12 existing quotas applying to imports of raw materials were removed. This represents more than one quarter of the value of imports of raw materials subject to quotas. In the first half of 1984, reference limits for large and frequent importers have been raised by 14.35 percent compared to the limits applied in the first half of 1983. The reference limits are set for the first six months of 1984, rather than quarterly, as in 1983. In addition, the 20 percent surcharge on imports of component parts was removed with effect from April 1, 1984. On the export side, the policy of authorizing domestic producers to export directly rather than through foreign trade organizations is to be continued. Foreign trading rights for export and import will be granted liberally upon proof of the ability of the enterprise to deal in foreign markets, and competition among foreign trading organizations will be permitted by the elimination of administrative restrictions on their activities.

The Fund welcomes the recent liberalization of the restrictions introduced in 1982, and believes that continuing adjustment efforts should permit Hungary to further liberalize its restrictive system.