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SM/88/166
Correction 1

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INFORMATION

August 24, 1988

To: Members of the Executive Board
From: The Secretary
Subject: Trade Policy Issues and Developments

The following corrections have been made in SM/88/166 (8/3/88):

Page 17, 2nd full para., line 10: for "Of the 24 structured adjustment facility"
read "Of the 24 structural adjustment facility"

Page 18, 1st full para., line 5: for "enhanced Fund facility"
read "extended Fund facility"

Page 20, 1st full para., lines 2 and 3: for "issues and its links with macroeconomics"
read "issues, including the links between trade policy, macroeconomic"

Page 24, 5th item, line 3: for "Article VI permits CVDs"
read "Article VI and the Tokyo Round... permits CVDs"

Corrected pages are attached.

Att: (4)

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absent; and (iv) staff appraisals placed emphasis on the need for import liberalization, reflecting the staff's concern about high levels of existing protection.

Overall, there is room to improve and expand the analysis in many consultation reports, particularly with respect to the interlinkages between trade policy and structural adjustment issues. Potential also exists for experimentation on quantification of protection. In view of the importance of the ongoing Uruguay Round for the multilateral trading system, greater attention is warranted to the consulting country's interests and views on the new Round.

2. Trade policies in Fund-supported programs

In recent years, an increasing proportion of Fund-supported programs has gone beyond the standard "standstill" clause (i.e., no imposition of new, or intensification of existing, import restrictions for balance of payments purposes), and trade liberalization has been included as an integral part of the external and structural policies under the programs. A staff survey indicates that more than half the stand-by and extended arrangements approved in 1985 included some form of specific trade liberalization measures during the program period; this proportion rose to over two thirds in 1986, and to over 90 percent in 1987. Of the 24 structural adjustment facility (SAF) arrangements approved during the period July 1986-March 1988, 23 included some form of trade liberalization.

The increased emphasis on trade liberalization in Fund-supported programs reflects the greater weight being given to structural adjustments in designing stabilization programs. Developing countries increasingly recognize the need for structural adjustments, of which trade liberalization is an important element, as being essential for improved efficiency in resource allocation, enhanced competitiveness, and a shift toward outward-oriented development strategies.

Programs which did not contain specific trade liberalization measures included cases where (i) the trade regime was already liberal; (ii) trade liberalization had been undertaken prior to the approval of the program or in the context of previous programs (e.g., Thailand, Uruguay, and Zaire in 1985); and (iii) trade liberalization was held over until better control of a fragile external position was established (e.g., Chad (1987), Congo (1986), the Gambia (1986), Guinea (1986), Niger (1986), and Tanzania (1986)).

The design of trade liberalization programs takes into account the circumstances of individual countries, and in most cases a gradual approach has been adopted. ^{1/} This is an important area of consultation and collaboration with the Bank. The focus and depth of trade liberali-

^{1/} Also see "Conditionality--A Survey of Current Issues," EBS/88/50.

zation have varied widely, ranging from the elimination of QRs to a simple streamlining of regulations. These variations reflect factors such as the nature and level of the initial restrictions, complementary exchange rate action, balance of payments prospects, and the authorities' commitment to the liberalization process. Given that exchange and trade restrictions can be effective substitutes, the nature and extent of measures in the area of exchange restrictions and exchange rate policies are of particular importance in influencing meaningful trade liberalization.

Relaxation of QRs, which are less transparent and more distortive than tariffs, was the most common type of trade liberalization in Fund-supported programs. The staff survey revealed the following features. (i) Reduction in the scope of QRs was featured in about a quarter of the countries which were granted stand-by or extended Fund facility (EFF) arrangements in 1985, and in about one half in 1986-87; (ii) within this category, elimination or substantial relaxation of QRs, or restrictive import licensing, were featured in a number of programs (e.g., Argentina, Equatorial Guinea, and Somalia in 1985; Bolivia, Guinea, Mexico, the Philippines, Sierra Leone, and Zambia in 1986; Argentina, Central African Republic, and Senegal in 1987; Ecuador and Kenya in 1988); (iii) a number of other programs also included reductions in QRs (in some cases from a relatively low base) (e.g., Jamaica, Korea, Madagascar, and Morocco in 1985; Burundi, Ghana, Morocco, and Tunisia in 1986; Ghana, Mauritania, and Zaire in 1987; and Malawi in 1988); (iv) in the case of the SAF, 16 out of 24 arrangements approved by March 1988 featured liberalization of QRs, in most cases significantly; and (v) in a number of cases, the removal or substantive reduction of QRs was part of a more comprehensive liberalization package including major exchange rate and domestic price reforms.

Tariff reform was increasingly featured in Fund-supported programs. The staff survey revealed the following features: (i) some form of tariff reform was included in the programs for 7 out of 25 stand-by and EFF arrangements approved in 1985, 8 out of 22 arrangements approved in 1986, and 11 out of 17 arrangements approved in 1987-March 1988; and 23 out of 24 SAF arrangements approved up to March 1988; (ii) comprehensive tariff reforms were often part of wider trade liberalization programs designed in collaboration with the Bank, and supported also by Bank resources (e.g., the Bank's trade policy loan to Jamaica in 1987); (iii) comprehensive tariff reforms were typically implemented according to a phased schedule in conjunction with a phased reduction in QRs, often as part of medium-term programs (e.g., Korea, Morocco, and Panama in 1985; Burundi, Mexico, Morocco, the Philippines, Senegal, and Tunisia in 1986; and Ghana, Kenya, Madagascar, Nepal, Sri Lanka, and Tanzania in 1987-March 1988); (iv) the aim of tariff reforms in most cases was to lower the average nominal rate of protection, in order to reduce the effective rate of protection as well as the dispersion of tariffs; (v) however, in some cases tariff reform was not acceptable to the authorities because of its fiscal revenue repercussions. In cases where QRs were replaced by tariffs, revenues from

tariff collections were envisaged to increase after the tariff reform (e.g., the SAF program for Bangladesh). In other cases, revenues were augmented by improvements in tariff collections or increases in tariff rates (e.g., Thailand and Zaire in 1985; Guinea-Bissau (SAF)).

Other types of trade liberalization in Fund-supported programs included: (i) liberalization or abolition of requirements for importer's licenses, sometimes in conjunction with other trade measures (e.g., Egypt, Madagascar, and Togo in 1986); (ii) rationalization of the exchange rate used for customs valuation (e.g., Egypt in 1986-88); and abolition of import or export monopolies (e.g., Somalia in 1985; Congo, the Philippines, Senegal, and Togo in 1986; Mozambique (SAF) in 1987).

Export promotion has also been featured (e.g., in the programs for 10 out of 12 stand-by arrangements, and 8 out of 13 SAF arrangements approved in 1987) in the form of tariff rebates or exemptions on imported inputs used for export production, administrative streamlining, preferential tax treatment for exports, elimination of export duties, and foreign exchange retention privileges for exports, etc. (It may be noted that export promotion via elimination of the anti-export bias implicit in restrictive import regimes is usually more efficient compared with the more direct measures of export subsidization.)

In most of the cases reviewed, trade liberalization measures were not used as performance criteria, but were monitored in the context of overall reviews of performance. This partly reflects difficulties in quantifying trade liberalization, as well as attempts to minimize the number of performance criteria. In a few cases, trade liberalization measures were implemented prior to the approval of the program. Monitoring of trade liberalization under the SAF took place through the use of benchmarks and annual reviews.

V. Issues for Discussion

1. Multilateral surveillance

Within its overall surveillance responsibilities, the Fund has been encouraging its members to implement appropriate measures to eliminate macroeconomic imbalances and reduce structural distortions. The continued pressures for protection, combined with an increase in trade restricting measures, suggest the need for the Fund to continue to emphasize the importance of policies that can contribute to an improvement in the world trading environment. Likewise, encouragement by the Fund for countries to liberalize their trade regimes continues to be necessary.

While recognizing that macroeconomic imbalances cannot be corrected through protection, a reduction in these imbalances can play a positive role in reducing protectionist pressures. The Fund through its surveillance activities can contribute to an improvement in the

international trade environment by assisting its members to adopt appropriate macroeconomic policies. This is particularly the case for major trading nations in view of the weight of these countries in world trade and the corresponding larger impact on the trading system of their policies. Equally important is the adoption of structural measures by these countries on a timely basis.

Executive Directors may want to indicate whether the continued pressure for protection calls for an increased coverage of trade issues, including the links between trade policy, macroeconomic imbalances and structural adjustment, in the WEO exercises.

2. Relations with member countries

Given the difficult international environment, it is important that countries not delay trade reforms, or increase restrictions, to improve their bargaining positions in the Uruguay Round. The recent increase in "gray-area" measures to protect industrial country markets is therefore a source of concern, as are views which suggest that liberalization is possible only if all major trading countries liberalize. All countries therefore need to be encouraged to abide by the spirit of the "stand-still" and "rollback" commitments of Punta del Este. In this context it is also important to note that joint or unilateral liberalization by major industrial countries could make an important contribution to the resolution of the debt problem.

a. With regard to Article IV consultation discussions, the coverage of trade issues could be further improved. The suggestions below are consistent with the thrust of views expressed by Directors in previous discussions of trade papers and Article IV consultations. It needs to be recognized, of course, that substantive improvements may be constrained by available staff resources; the size of Fund missions; the availability of resources in national capitals and the willingness of national authorities to devote more time and effort to trade matters in Article IV discussions; and the degree to which Executive Directors may be able to devote time to trade issues given that there are many other priority issues to be dealt with in Article IV consultations.

(i) Scope exists for a more in-depth analysis of the links between trade, structural adjustment, and external imbalances.

(ii) A greater focus on the regional effects of trade policies, particularly for countries that are members of regional trading arrangements, is desirable; such coverage would include trade policies implemented at both the national and regional level, and the impact of individual member countries on regional policies.

(iii) A more explicit focus on country views on issues under discussion in the Uruguay Round would also be useful.

SB	Surveillance Body (Uruguay Round)
TEA	Targeted Export Assistance Program (United States)
TNC	Trade Negotiations Committee (Uruguay Round)
TRIMs	Trade related investment measures (Uruguay Round)
TRIPs	Trade related intellectual property rights (Uruguay Round)
TSB	Textile Surveillance Body
UNCTAD	United Nations Conference on Trade and Development
VERs	Voluntary export restraints
WEO	World Economic Outlook
WDR	World Development Report

Glossary of Terms

Administered protection: Use of administrative procedures (e.g., in antidumping and countervailing duty investigations) in a manner which impedes trade flows.

Antidumping duty (AD): Duty levied on imports to offset the competitive advantage provided by dumping of imported goods. GATT Article VI and the Tokyo Round Antidumping Code permit ADs on dumped imports of like products provided they cause or threaten to cause material injury to the domestic industry.

Contingent protection: See Administered protection.

Countertrade: Trade transaction committing the exporter to receive payment for the value of his exports, in whole or in part, by imports from his trading partner.

Countervailing duty (CVD): Duty levied on imports to offset the competitive advantage provided by subsidies on imported goods. GATT Article VI and the Tokyo Round subsidies code permit CVDs on subsidized imports provided they cause or threaten to cause injury to the domestic industry.

Customs Union: As defined in GATT Article XXIV, a group of countries forming a single customs territory in which (a) tariffs and other barriers are eliminated on substantially all trade among member countries, and (b) substantially the same measures are applied by each of the member countries to their trade with third countries, including a common external tariff.

Dumping: Price discrimination between exports and domestic sales of a given product. The dumping margin, which forms the basis of antidumping duties, may be determined according to GATT Article VI as the price difference between the price of the product exported from one country to another and (a) the comparable price, in the ordinary course of trade, for the like product when destined for consumption in the exporting country or, in the absence of such domestic price, (b) the highest comparable price for the like product for export to any third country, or (c) the cost of production in the exporting country plus a reasonable addition for selling cost and profit.

Effective rate of assistance: The ERA is defined as the difference between the value added per unit of output in the domestic price and the value added in the world price, expressed as a percentage of the world price. This measure thus includes the effects of subsidies and other nonborder measures in addition to the effects of border measures.

Effective rate of protection: A measure of protection provided by an import restriction, calculated as a percent of the value added of the product concerned. Effective protection is higher than nominal