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Balance of Payments and Related Issues in the  
Uruguay Round of Trade Negotiations

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Abstract

The paper discusses the balance of payments provisions of the GATT, particularly as they apply to developing countries. It argues that these provisions should be reconsidered, and strengthened, in the Uruguay Round of multilateral trade negotiations.

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### Summary

Despite the growing international interest in the role of the developing countries in the multilateral trading system, so far little attention has been paid so far to the balance of payments and related provisions and practices of the General Agreement on Tariffs and Trade (GATT) that directly influence these countries' trade policies. This paper suggests that there is a need to reconsider these provisions in the context of the ongoing Uruguay Round of multilateral trade negotiations.

The paper traces the historical evolution of GATT practices on trade restrictions by industrial countries for balance of payments purposes, on balance of payments restrictions by developing countries, and on infant-industry protection. By the mid-1960s, most industrial countries had eliminated their quantitative import restrictions for balance of payments purposes and have subsequently resorted to such restrictions only sporadically and generally for strictly temporary periods. In contrast, developing countries frequently use trade restrictions for balance of payments purposes; over time, GATT surveillance over such restrictions has been somewhat loosened. Most countries currently invoking the GATT's balance of payments provisions are developing countries. In addition, in some cases balance of payments restrictions may go undetected by the Committee of Balance of Payments Restrictions--the GATT body charged with overseeing the application of the relevant GATT provisions with the cooperation of the Fund.

The paper suggests that, with the introduction of generally more flexible exchange rate arrangements in both developing and industrial countries, the original rationale for temporary import barriers to safeguard a country's external financial position appears to have lost its force. Also, recent theoretical and empirical work has demonstrated that neutral or export-promoting trade strategies are more effective for development than the import substitution frequently advocated by economists in the 1950s and 1960s. The current focus on balance of payments viability in the context of developing countries' debt problems has probably reinforced the need to maintain a relatively open trade and payments regime by using flexible and appropriate exchange rate and macroeconomic policies.

Finally, the paper suggests that stronger international discipline over trade restrictions for balance of payments purposes is unlikely to be achieved without other improvements in the multilateral trading system that are already on the agenda of the Uruguay Round. At the same time, agreement on the other elements of GATT reform is likely to be facilitated by an effort to address the balance of payments and related issues in the Uruguay Round.



## I. Introduction

Recent years have seen an extensive, renewed discussion of the role of developing countries in the multilateral trading system. New concepts such as "graduation" have been advanced, while arguments for and against "special and differential treatment" of developing countries have been renewed. An important focus of the Uruguay Round of trade negotiations will be to elaborate further on these concepts, while shaping the future trade relations between developed and developing countries. 1/

Yet, surprisingly, the balance of payments provisions and practices incorporated in the General Agreement on Tariffs and Trade (GATT), which significantly bear on the trade policies and positions of many developing countries, and hence on the role of the developing countries in the GATT system, have not been discussed in the context of the preparations for the new round. The purpose of this paper is to fill this lacuna.

## II. The Issue

A fundamental premise of the GATT is that domestic industries must be protected only by "bound" tariffs applied on a nondiscriminatory basis. Thus tariff rates so negotiated in the GATT may not be raised without compensation to, or negotiation with, affected trading partners. Since quantitative restrictions can nullify the effects of such disciplines on tariffs, the GATT includes a general presumption against the use of quantitative restrictions. But, from the outset, the balance of payments situation was viewed as justifying an exception to this general presumption.

The developed countries have lowered tariff and nontariff barriers since the GATT was founded and, in recent years, have avoided all but a strictly temporary use of balance of payments restrictions. By contrast, the developing countries have traditionally maintained high tariff and nontariff barriers, and most continue to do so today. In GATT terminology, developing countries' tariff schedules are often largely "unbound"--i.e., most of the tariff rates may be unilaterally raised at any time. 2/ Quantitative import restrictions are prevalent,

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1/ Along with nondiscrimination, the treatment of domestic measures such as subsidies, and the future role of a strengthened GATT, the subject of trade relations between developed and developing countries will be one of the key elements of the Uruguay Round. See Anjaria (1986).

2/ Typically, at least 70-85 percent of imports may be subject to an "unbound" tariff in a developing country. Two notable exceptions among the developing countries in this respect are Chile and Mexico, both of which maintain "bound" tariff schedules at maximum tariff rates of 35 percent and 50 percent, respectively.

although it is often difficult to determine the extent to which these are considered by the countries resorting to them as necessary for "balance of payments" or for "infant industry" reasons.

If participation by the developing countries in the GATT negotiations is to be meaningful in terms of more open markets, it will involve a greater degree of tariff bindings and/or a lowering of their tariff and nontariff barriers. This in turn will require attention by trade officials to the links between trade policy, external adjustment, and development strategy. If these officials believe that development prospects or balance of payments adjustment are retarded, rather than advanced, by more open trade regimes, fuller participation in the world trading system by developing countries through their increased acceptance of reciprocal market-access obligations would be difficult to achieve.

As it happens, the developmental or "infant industry" provisions of the GATT allow a developing country to provide "governmental assistance" to establish a particular industry. 1/ Nevertheless, the record shows that in the formal arena very few developing countries have sought to justify their "infant industry" protection. As of September 1986, only five countries (Côte d'Ivoire, Indonesia, Malaysia, Thailand, and Zimbabwe) had formally invoked the relevant GATT Article XVIII:C. 2/ By contrast, about twice as many invoked Article XVIII:B which deals with the balance of payments provisions for developing countries. 3/ Evidently therefore the balance of payments provisions need to be carefully reexamined.

Given the prevalence of developing countries' trade restrictions for balance of payments reasons, the treatment at the Uruguay Round of this issue will be critical in shaping the future role of developing countries in the GATT system.

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1/ Attachment I describes the infant industry provisions of the GATT in greater detail.

2/ In the 1950s, releases under Article XVIII:C had been obtained by Cuba, Haiti, India, and Sri Lanka, but subsequently few countries resorted to this provision until rather recently. See Jackson (1969, p. 655).

3/ A possible explanation for this paradox is that the GATT has applied relatively restrictive notification and compensation requirements for invoking Article XVIII:C, which may have induced some developing countries to leave certain restrictions "unapproved." But a more important reason may be that some developing countries find it relatively easy to obtain "GATT cover" for infant industry protection under the guise of "balance of payments" reasons which are invoked more frequently. Thus, to deal effectively with infant industry protection in the new round presupposes that clearer distinctions will be drawn between balance of payments and infant industry protection.

The plan of this paper is as follows. Sections III and IV describe the historical background to, and the main features of, the GATT provisions and practice pertaining to balance of payments-induced trade restrictions. Section V outlines the main rationale for reconsidering the GATT's approach to balance of payments restrictions. Section VI suggests some issues that are likely to arise in considering a possible reform of the balance of payments provisions. And the final section provides concluding observations.

### III. Background to the Balance of Payments Provisions of the GATT

Under the current provisions, subject to established consultation and review procedures by the CONTRACTING PARTIES, the General Agreement permits member countries to protect their external financial situation by imposing temporary trade restrictions in the face of a balance of payments deterioration. To understand this approach, it is useful to refer to several aspects of the historical development of GATT rules and practice and the attitude of the framers of the General Agreement toward trade restrictions. 1/

From the outset of the discussions leading to the Havana charter for the International Trade Organization (ITO), which subsequently formed the basis for the General Agreement on Tariffs and Trade, it was generally accepted that quantitative trade restrictions to safeguard the international reserves and balance of payments position of a country would need to be built into the framework of the new international trade rules. A basic principle of the ITO charter, carried over into Article XII of the GATT, allows countries to use, but not to abuse, import restrictions during a balance of payments crisis. Further, given the dollar shortage faced by European countries in the immediate postwar period, the GATT Articles included a provision (Article XIV) allowing discrimination in the application of trade restrictions for balance of payments purposes. In 1955, the provisions of GATT Article XII were reviewed, but in this review a proposal to introduce fixed time limits after which trade restrictions for balance of payments purposes would be expected to lapse was not accepted.

Although several developing countries participated actively in the negotiations on the Havana charter in the late 1940s, no differentiation in the balance of payments provisions governing developing and developed countries was introduced until 1955. GATT Articles XII and XIV were then amended, and GATT Article XVIII dealing with governmental assistance to economic development was overhauled. As part of the changes, an explicit balance of payments provision relating to developing countries was introduced in Article XVIII. With the 1955

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1/ The following paragraphs, as well as Attachments I and II, draw heavily upon Jackson (1969), especially pp. 673-716.

amendments to the GATT Articles, international surveillance over trade restrictions imposed by developing countries for balance of payments reasons was loosened, and developing countries were thereafter required to consult in the GATT once every two years rather than once a year as was expected of developed countries that invoked the provisions of GATT Article XII. 1/

By the mid-1960s, industrial countries negotiating under the auspices of the Organization for Economic Co-operation and Development (OECD) and the GATT had virtually eliminated reliance on trade restrictions for balance of payments purposes. 2/ The remaining restrictions by industrial countries were no longer justified as balance of payments-induced, but either fell within one of the other GATT exceptions to the general ban on quantitative restrictions--such as for agricultural restrictions--or were submerged into a broader catchall category of "residual restrictions," which proved quite difficult to address despite repeated efforts. Although, in the subsequent period until the mid-1970s, industrial countries introduced trade measures such as import surcharges and advance import deposit requirements for balance of payments purposes, these were applied for temporary periods. Moreover, international surveillance over such measures was exercised relatively expeditiously under GATT Article XII or under other provisions and practices in the OECD designed to discourage trade and payments restrictions. 3/

By contrast, the position of the developing countries in the GATT evolved in quite the opposite direction. In addition to the concept of infant industry protection incorporated in Article XVIII:C, the notion of special exemptions from rules became enshrined from the mid-1960s in

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1/ In some respects the IMF discipline was also slow to develop in the payments field. Thus, a conclusion on the scope of Article VIII, Section 2(a) of the Articles of Agreement, the main instrument for achieving among IMF members the multilateral system of payments and transfers for current international transactions, was not reached until June 1960, more than 15 years after the Articles had become effective. See Gold (1986), pp. 166-167.

2/ Between 1958 and 1964, the number of industrial countries invoking GATT Article XII fell from 14 to 3. See Eglin (1987).

3/ In the GATT, several consultations with industrial countries applying import surcharges or advance import deposit requirements took place in special working parties set up for this purpose. In part, the working parties were considered necessary since technically Article XII permitted only quantitative restrictions for balance of payments reasons, and not other measures. With the adoption of the 1979 Declaration on Trade Measures, all GATT balance of payments consultations were formally integrated under the responsibility of the Committee on Balance of Payments Restrictions.

Part IV of the GATT, which entered into force in June 1966. <sup>1/</sup> The United Nations Conference on Trade and Development (UNCTAD), with its broad mandate to discuss and advance proposals for improving the developing countries' trade and development prospects, was established in March 1964, and pressed strongly for generalized tariff preferences. Thus, from the mid-1960s until about the mid-1970s, trade restrictions by developing countries became part and parcel of the broader questions regarding the responsibilities of the developed countries for the trade, finance, and development requirements of developing countries as a group. <sup>2/</sup>

In the environment then prevailing, questions about the usefulness of quantitative restrictions to deal with balance of payments problems were infrequently addressed at the international level. Indeed, when they were, the focus was, not always on applying common understandings on which to base trade liberalization by all countries but rather, on reinforcing in international rules the special treatment of developing countries. <sup>3/</sup>

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<sup>1/</sup> It should be noted that Part IV of the GATT, entitled "Trade and Development," obliges developed contracting parties to extend special and differential treatment to developing countries on a "best endeavors" basis, while imposing no equivalent obligation on developing member countries.

<sup>2/</sup> In the IMF this development was reflected in the compensatory financing facility, first introduced in 1963, and then extended and liberalized in 1966. In December 1975, following extensive debate, the facility was again substantially liberalized. More broadly, the commodity price shocks of the early 1970s, and the disappointing performance of aid donors, led to demands by developing countries for a new international economic order which included, inter alia, suggestions for a link between allocations of Special Drawing Rights and development finance.

<sup>3/</sup> It is interesting to note, in this connection, that the Outline of Reform prepared by the IMF's Committee of Twenty in June 1974 included explicit acknowledgment of the special position of developing countries and of the need to promote their interests. Specifically, in the area of trade, the outline noted that:

There will be a strong presumption against the use of controls on current account transactions or payments for balance of payments purposes...

It also provided that:

Wherever possible developing countries will be exempted from controls imposed by other countries, particularly from import controls and controls over outward long-term investment. The special circumstances of developing countries will be taken into account by the Fund in assessing controls which these countries feel it necessary to apply...

See IMF, Committee on Reform of the International Monetary System and Related Issues, International Monetary Reform: Documents of the Committee of Twenty, (Washington: International Monetary Fund, 1974), pp. 12-13.

An important contribution of the 1973-79 Tokyo Round negotiations to the subject was the adoption by the CONTRACTING PARTIES in 1979 of the Declaration on Trade Measures Taken for Balance of Payments Purposes. As described below, the Declaration broadened the scope of Articles XII and XVIII to cover trade measures other than quantitative restrictions, such as import surcharges and advance import deposits, and established a somewhat weak presumption--expressed only in its preamble--that "developed contracting parties should avoid the imposition of restrictive trade measures for balance of payments purposes to the maximum extent possible." In addition, the conditions for the application and surveillances of such trade measures were spelled out more clearly. However, the Declaration left unchanged the basic difference in the degree of international surveillance over such trade measures by both developed and developing countries. Indeed, the economic uncertainties of the 1970s appear to have reinforced the notion in the GATT that the balance of payments difficulties of developing countries were of a recurrent nature and that resort to trade restrictions were an acceptable means of dealing with their external payments problems.

#### IV. Present Balance of Payments Provisions and Procedures

Developed countries invoking Article XII consult in the GATT Committee on Balance of Payments Restrictions every year; developing countries invoking Articles XVIII:B consult in the same committee once every two years. The first consultation on invocation is normally a "full consultation." This involves an examination of the balance of payments justification for the trade restrictions in question and the nature and modalities of the trade restrictions themselves. A statement, representing an IMF view on the balance of payments situation and prospects and on the policies being adopted by a consulting contracting party to deal with external and internal imbalances, forms a main input for the full consultation, together with background documentation provided by the consulting country, the GATT secretariat, and the IMF. Subsequent consultations with developing countries are normally held under "simplified procedures." These consultations involve no discussion of the trade measures or the balance of payments justification for their maintenance. Rather, their objective is to provide members of the Committee on Balance of Payments Restrictions with information on the balance of payments situation and measures taken by the consulting country, in order to assess whether a further full consultation is necessary. <sup>1/</sup> The IMF does not present a statement during these "simplified" consultations.

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<sup>1/</sup> Such a decision rests, inter alia, on the time elapsed since the previous full consultation, the steps the consulting country has taken in response to previous conclusions by the Committee, changes in the overall level or nature of trade measures taken for balance of payments purposes and in the balance of payments situation and prospects.

In most respects, consultations under the two main balance of payments provisions--Articles XII and XVIII:B--are quite similar, as outlined in Attachment II. The main differences between the two sets of the provisions relate, first to the frequency of the consultations--with annual GATT consultations under Article XII and, biennial consultations under Article XVIII:B, and, second, the nature of the consultation discussions and the conclusions reached by the Committee on Balance of Payments consultations--with the Article XII consultation giving greater emphasis to early phasing out of the balance of payments restrictions. 1/

Table 1 lists the 24 contracting parties that have consulted with the GATT under Articles XII or XVIII:B on one or more occasions since 1974. The vast majority of consultations in the Committee on Balance of Payments Restrictions in this period have been with developing countries under Article XVIII:B. Although many developing countries have expressed concerns about the burden imposed on them by the consultation requirements, Table 1 suggests that in fact, full consultations under Article XVIII:B have been relatively infrequent for most of the countries which have claimed balance of payments justification during the whole period. For example, over the 13-year period covered, full consultations were held most frequently with Brazil, but only on a total of four occasions. With Korea and Yugoslavia, full consultations were held three times each, and with a number of other countries they were held only once. Colombia and the Philippines, which have acceded to GATT since the Tokyo Round, have held one and two full consultations, respectively, in the period since their accession. 2/ With a few countries (including Bangladesh and Sri Lanka) no full consultation has been held during the entire 13-year period.

No comprehensive and definitive information is available for determining whether or not all GATT member countries that resort to trade measures for essentially "balance of payments" purposes in fact invoke Article XVIII:B to justify their restrictions in the GATT. Although some informal steps taken in the Committee on Balance of Payments Restrictions are designed to encourage non-invoking countries to justify apparent balance of payments restrictions under GATT, by and large the initiative to invoke Article XVIII:B is the responsibility of each GATT member. 3/

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1/ As already noted, the 1979 Declaration on Trade Measures established the basic premise that developed countries under Article XII should avoid the imposition of trade restrictions for balance of payments purposes.

2/ Argentina, which had phased out previous balance of payments restrictions in 1978, reinvoked Article XVIII:B in 1984 and held a full consultation in 1986; Nigeria invoked Article XVIII:B in 1983 and held a full consultation in 1984. At present, full consultations are scheduled for 1987 with Egypt, India, Israel, Korea, and Peru.

3/ However, the Declaration on Trade Measures Taken for Balance of Payments Purposes also provides for the reverse notifications.

The possibility that several countries applying restrictions for balance of payments reasons may remain outside GATT surveillance is suggested by Table 2, which is based on information compiled by the IMF from official sources. 1/ At the end of 1985, some 16 developing countries did not invoke GATT balance of payments provisions for the import surcharges or advance import deposit requirements applied by them. 2/ Similar information on quantitative restrictions maintained or intensified at the end of 1985 for balance of payments reasons is not readily available. Even so, there is an evident strong case to be made for more careful scrutiny by the GATT of trade restrictions for balance of payments purposes that at present may remain outside the surveillance of the GATT Committee on Balance of Payments Restrictions. 3/ As the maintenance of trade restrictions for balance of payments purposes may be associated with overvalued exchange rates, the IMF has a particular interest in encouraging the identification of such restrictions and their liberalization. 4/ Closer IMF-GATT cooperation might therefore be especially fruitful in this area.

Another aspect of the balance of payments provisions concerns the commodity coverage of the trade restrictions. Available information regarding the countries that invoke Article XVIII:B is summarized in Table 3. Although, by definition, trade restrictions for balance of payments reasons must be across-the-board, in most developing countries

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1/ Some of these measures may be exchange measures subject to prior approval of the IMF under its Articles. The IMF's interest in promoting an open trade and payments system, and its activities in relation to international trade, have been described most recently by Gold (1986). For an earlier account of the role of the IMF in trade policy issues, see Anjaria et al. (1985), pp. 83-86.

2/ The 16 countries that are not included as consulting countries in Table 1 are: Belize, Burkina Faso, Burundi, Cyprus, Dominican Republic, Gambia, Haiti, Jamaica, Kenya, Mauritius, Nicaragua, Rwanda, Sierra Leone, Suriname, and Uruguay.

3/ In accordance with the 1982 Ministerial Declaration, a GATT Group on Quantitative Restrictions and other Nontariff Measures initiated an examination of the legal basis of quantitative restrictions. With the launching of the Uruguay Round, this group's work will be taken up by the negotiating committees.

4/ The objectives of effective IMF surveillance over the exchange rate policies of member countries are laid down in Article IV of the Second Amendment of the IMF's Articles which abrogated the previous par value system. Here it is noteworthy that one of the principles for IMF surveillance over the exchange rate policies of its members is that:

... the introduction, substantial intensification, or prolonged maintenance, for balance of payments purposes, of restrictions on, or incentives for, current transactions or payments...

may give rise to the need for discussion with a member. See International Monetary Fund, Selected Decisions, Twelfth Issue, Washington, April 1986, p. 12.

the proportion of the tariff nomenclature notified to the GATT has been relatively small, ranging from only a handful of product categories in some cases to more than 50 percent of the number of CCCN categories in only half a dozen cases. 1/ This raises a question whether specific criteria should be developed to distinguish genuine "balance of payments" restrictions notified to the GATT from other types of trade restrictions, such as those for protective or security reasons, which are more likely to be sector-specific. Although historically the GATT has been concerned about the incidental protective effects of balance of payments restrictions no attempt has been made to establish a sharp distinction between across-the-board balance of payments restrictions and sector-specific restrictions motivated by other considerations. 2/ Indeed, under Article XVIII:B:10, GATT members have the explicit right to vary the restrictiveness of their balance of payments measures depending upon the essentiality of the products in question for economic development. This provision, while not a basis for explicit sectoral differentiation in recent years, tends to cloud the distinction between infant industry and balance of payments protection in developing countries. 3/

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1/ Interestingly, countertrade transactions, which are of growing importance in world trade and partly motivated by balance of payments considerations in some developing countries, are often concentrated in certain product categories. However, these have not been notified to the GATT as restrictions for balance of payments reasons. See United States International Trade Commission (1985) for a description of countertrade practices. Huh (1983) and Gold (1986) outline IMF concerns about countertrade, which is similar in some respects to bilateral payments agreements.

2/ In 1955, the GATT approved the so-called hard-core waiver, allowing countries a transitional period of exemption from Article XI, which establishes the basic presumption against quantitative restrictions, following the end of Article XII applications, in "exceptional" circumstances. See Jackson (1969), p. 709.

3/ In this connection the IMF practice is of some interest. In applying policies on the use of its resources, the IMF is required to make a judgment on what constitutes a trade restriction for balance of payments purposes. The IMF's approval vis-a-vis a member's representation has been described as follows:

A member may declare that its intention in imposing a measure is, or is not, to manage its balance of payments. The member's representation is given the benefit of any reasonable doubt, but the Fund reserves the right to pass upon the representation on the basis of the facts. These facts include the rationale offered by the member for its measures, the effect of the measures on the balance of payments and on exchange rates of the currency of the member in relation to the currencies of other members, the member's domestic and external conditions or policies that may explain its choice of the measures, expectations regarding the duration of the measures, and the prevailing practice among members in general with respect to the use of the measures for the purpose of managing the balance of payments.

See Gold (1986), p. 217.

At the conclusion of each full consultation, the Committee on Balance of Payments Restrictions adopts a report which is subsequently endorsed, usually without further discussion by the GATT Council. Among the points generally included in the Committee's conclusions are: references to the nature of the balance of payments problem and, in particular, the extent to which the external disequilibrium is seen to be related to trade imbalances; a brief expression of the Committee's general views on the other external and domestic financial policies being pursued to correct the balance of payments problem; the application, where relevant, of multiple trade restrictions where a more simplified trade regime might be appropriate; and the incorporation of any announced plans by the consulting contracting party to phase out the restrictions or, in their absence, the Committee's views on the desirability of establishing such a timetable. Following the introduction of more flexible exchange rates worldwide, the IMF finding and the GATT conclusions have generally sought to welcome or encourage a policy stance that is conducive to achieving medium-term viability in the external payments position. Thus, in recent years, unduly specific conclusions about the "need" for trade restrictions for avoiding a decline in the country's holdings of monetary reserves have been avoided. Attachment III includes extracts from the conclusions of the Committee on Balance of Payments Restrictions in four recent consultations.

#### V. Need for a New Approach

Major changes in the world economy suggest a need for re-examining the rules governing trade restrictions for balance of payments purposes. First, there is a greater willingness among countries to use macroeconomic policy instruments to deal with external sector difficulties. Second, greater mobility of capital in the past decade has changed the nature of balance of payments problems facing many developing countries. Finally, overlaying the discussion of the trade policies of developing countries is a considerable improvement in the understanding of the links between growth, development, and trade strategy which gives urgency to a reexamination of all arguments in favor of trade barriers. In certain important respects, the IMF's surveillance over exchange rate policies has been adapted to reflect these changes in the 1970s, while the adaptation of GATT rules and practice has lagged behind. Modernization of the GATT balance of payments provisions would thus be a logical part of the overall strengthening of the GATT system that is now being negotiated. At the same time, it would contribute positively to the achievement of the IMF's objectives.

It is evident that the balance of payments provisions of the GATT permitting the use of quantitative import restrictions were formulated on the assumption of fixed exchange rates--or at least they presumed that exchange rate adjustments, in the absence of "fundamental disequilibrium," were undesirable. Following the abandonment of the par value system from the early 1970s, there is a greater awareness of the role of exchange rate policy in balance of payments adjustment. Even if they do not float freely in many developing countries, exchange rates are often actively used for balance of payments adjustment. Hence, a

fundamental assumption on which the GATT provisions and practice are based is no longer applicable. Moreover, at the time the General Agreement was formulated, quantitative import restrictions were seen as an appropriate or necessary short-term device to switch the pattern of demand toward home-produced goods while policies to reduce real expenditures to bring about an improvement in the external current account balance took effect. <sup>1/</sup> Today, however, the efficacy of exchange rate adjustments to bring about the necessary reduction in real expenditures is recognized, and even among alternative demand-switching policies, quantitative restrictions are regarded as an inferior policy instrument compared to price-related measures such as import surcharges or advance import deposit requirements. There has thus developed a certain difference between most governments and the IMF, on the one hand, and the GATT, on the other hand, in their respective attitudes on the appropriate choice of policy instruments for balance of payments adjustment. Exchange rate adjustment supported by appropriate macroeconomic policies are generally considered as the "first-best" policy package to deal with a lasting balance of payments deterioration; yet the GATT's mandate is limited mainly to considering the legitimacy of quantitative import restrictions. Thus, one outcome of the disparate evolution of GATT and IMF disciplines and practices--paradoxical, given the commonality of purposes of the two bodies--is that while, as IMF members, countries are called upon to explain why in particular crisis situations they prefer quantitative restrictions or import surcharges to exchange rate adjustment, as GATT members the same countries have come to expect GATT to sustain the use of such restrictions for balance of payments purposes.

Perhaps the most notable change in balances of payments since the early 1970s is the profoundly greater importance of capital movements in determining the overall external sector position of any country. In the major industrial countries, the rapid growth of capital markets and the responsiveness of capital flows across international borders has introduced a new element in the balance of payments adjustment process. It is now generally recognized that, in a world of floating exchange rates and capital mobility, attempts to improve the balance of payments position through the introduction of trade restrictions are, at best, unworkable, if not actually counterproductive, as they may induce

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<sup>1/</sup> Even more than a decade ago, however, the "equivalence" of quantitative restrictions and exchange restrictions for balance of payments reasons was recognized. Thus, a rather radical view advanced prior to the Tokyo Round negotiations by Sir Eric Wyndham-White, former Director General of the GATT, questioned the rationale for dealing with balance of payments restrictions in the GATT:

[T]he time has now come to recognize that the provisions relating to the use of QR for balance of payments reasons are inappropriate in what purports to be essentially a trade agreement. Commercial measures adopted exclusively for balance of payments reasons are essentially exchange restrictions applied by a particular technique and should be dealt with as such.

See Eric Wyndham-White, "Negotiations in Prospect," in Bergsten, C. Fred (ed.), Toward a New World Trade Policy: The Maidenhead Papers (Lexington Books, Lexington, 1975, pp. 321-340).

a compensating appreciation of the currency of the restricting country. 1/ In some cases, indeed, the current account of the balance of payments may be said to be "driven" by the capital account, rather than vice versa. Restrictions imposed by a major trading nation would almost certainly prove counterproductive by provoking retaliatory restrictions by trading partners. The numerous governmental statements and declarations issued in the past decade testify to the awareness of policymakers in industrial countries to the dangers of resorting to trade restrictions for correcting payments imbalances. 2/

For developing countries, greater worldwide capital mobility has shifted the focus from balance of payments deficits per se to concerns about medium-term external viability. Many developing countries which engaged in heavy external borrowing in the 1970s found, in the worsened external economic environment they faced subsequently, that their debt burden became unsustainable. Major debt restructuring and exceptional financing were coupled with strong adjustment policies to bring the external position closer to medium-term viability. But in no instance was it thought possible or desirable that the objective of medium-term viability could be achieved by increased reliance on trade and payments restrictions. Moreover, even where, in the early 1980s, adjustment packages entailed a sharp degree of initial import compression, reliance was placed mainly on demand management policies, rather than on intensified and prolonged trade and payments restrictions. Indeed, over the medium term it was considered necessary to establish the basis for permitting the growth of imports at a sustainable rate by combining exchange rate and demand management policies with appropriate, but often slower acting, supply-side policies. Thus, the "freedom" available to developing countries under GATT to impose trade restrictions for balance of payments purposes proved to be somewhat irrelevant, as the countries concerned often found it feasible to go beyond reliance on trade restrictions to an active search for policy packages that reduced this reliance.

Another major consideration relates to the links between trade strategy and development. A growing body of evidence demonstrates the positive experience of an outward-oriented trade strategy for developing countries' growth and development prospects. Although work on outward-oriented or export-promoting strategy for promoting economic development started as far back as the 1960s, it was not until the late 1970s that sufficiently extensive analysis was undertaken establishing the superiority of more open (or, strictly, more neutral) trade policy over the import-substitution policy often recommended by economists in the

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1/ Even under a system of fixed exchange rates, a trade restriction may result in a real effective appreciation of the exchange rate through its inflationary impact.

2/ For example, in May 1974 the member countries of the OECD adopted a declaration expressing their determination to avoid resort to import restrictions and similar measures, a declaration that has been successively renewed since then.

1950s and 1960s. <sup>1/</sup> A number of detailed studies have found that the export-promoting strategy enabled developing countries with an already-established industrial base to take advantage of the post-war economic boom of the 1950s and 1960s, an opportunity that was missed by countries that pursued an import-substitution strategy. Furthermore, the former strategy was found to be superior in promoting overall economic growth as well as more rapid industrialization and promotion of employment. <sup>2/</sup> Given these findings, it has been increasingly evident that the cost of using balance of payments difficulties as a justification for maintaining trade barriers is not negligible for developing countries. The view that trade barriers are an inappropriate way to address payments difficulties has thus been further reinforced.

#### VI. Some Issues for the Future

Notwithstanding the clear theoretical as well as practical grounds for re-examining the balance of payments provisions of the GATT, it is premature to predict whether this re-examination will be conducted or how it will be concluded. If there were to develop a broad consensus for reviewing the GATT provisions and practice, the main issues that may prove difficult in the context of the Uruguay Round are: the degree of discipline that should be applied on balance of payments-induced restrictions; and the nature of the relationship of possible reforms in this area to other aspects of the GATT system and negotiations.

As to the degree of discipline, the discussions will sooner or later involve the specific features or characteristics which would regulate countries' use of trade restrictions for balance of payments purposes. Among the elements that may be included are: whether temporary restrictions would be authorized for predetermined time limits; whether stricter discipline would be imposed on new restrictions than on pre-existing ones; how the generalized or across-the-board nature of the restrictions would be defined (e.g., a balance of payments restriction must cover at least x percent of a country's imports); and whether the possible inclusion of services and trade-related investment measures in the negotiations would require corresponding adjustment of the balance of payments provisions.

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<sup>1/</sup> The "export-promoting" strategy is something of a misnomer, since the literature defines such a policy as one that, on balance, maintains an effective exchange rate for exports at a level not significantly different from that of imports. Thus, the export-promoting strategy merely calls for eliminating the bias against exports, while the import-substitution strategy is one based on a higher effective exchange rate for imports than for exports. Of course, the maintenance of an overvalued exchange rate is not consistent with pursuit of the export-promoting strategy. See Bhagwati (1987), p. 92.

<sup>2/</sup> Two major studies in this area are Bhagwati (1978) and Krueger (1978). See also Bhagwati (1987), p. 96.

How would strengthened international surveillance over trade restrictions for balance of payments purposes be exercised? From the standpoint of a country's trading partners in the GATT, it may be desirable to decide whether the country's program for phasing out trade restrictions and implementing adjustment policies is "on track" or "off track." However, in practice such judgments may be difficult to reach in the GATT context as they bear on macroeconomic developments and policies that are normally covered in the IMF's consultations with member countries. In the GATT context, among the questions that would require resolution would be: How frequently would the GATT Committee on Balance of Payments Restrictions make its determinations, and on the basis of what information, given that balance of payments prospects are often volatile? If a country's adjustment effort were to be considered "inadequate" in the GATT context, what would be the practical consequences? Could such a declaration trigger retaliatory actions by trading partners? If so, would retaliation not impede, rather than assist, in the attainment of the country's adjustment objectives? If the rules were too strictly formulated, would there be a greater risk of nonreporting of balance of payments restrictions? How would the IMF be expected to cooperate in a strengthened surveillance process, given its traditionally key role in the GATT balance of payments consultations?

Apart from these somewhat formalistic or institutional questions, two substantive issues appear critical. The first is the optimal speed of trade liberalization. Actual experience in the developing countries suggests that no hard and fast rules can be applied a priori as to whether trade liberalization should be massive and quickly completed, or gradual. On the one hand, an argument can be made that liberalization of restrictions applied for balance of payments reasons requires alternative macroeconomic policy adjustment to take hold. On the other hand, there is some recent evidence that in the majority of liberalization episodes in developing countries in the post-war period, a more rapid liberalization effort than was actually implemented might have proved both feasible and more effective. <sup>1/</sup> In any event, if countries can be expected to have their own, different timepaths for trade liberalization, how should these be fitted to the overall timetable of the ongoing trade negotiations?

The second set of issues has come to be known under the rubric of "links between trade and finance," and concerns whether some special or additional financial or trade measures are needed to encourage further trade liberalization (including protection for balance of payments or infant industry reasons) by developing countries. In informal discussions of the trade-finance link in the GATT and elsewhere, no firm conclusions have been reached, in part perhaps because of the somewhat different vantage points from which trade and finance officials in

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<sup>1/</sup> Papageorgiou, Demetris, M. Michaely, and A. Choksi, "The Phasing of a Trade Liberalization Policy: Preliminary Evidence," paper presented at the 1986 Conference of the American Economic Association (Washington, IBRD, unpublished).

national governments often address these matters. However, "trade-finance links" may resurface in the context of a re-examination of GATT balance of payments provisions. Specifically, the financial aspect of these links concerns the availability of external financing; the trade aspect concerns the openness of markets.

As to the financial aspects, concerns have been voiced, particularly against the background of the recent economic difficulties facing developing countries, that ways be found to ensure the availability of additional external financing to secure the "permanence" of trade liberalization measures by developing countries. As mentioned earlier, because the "binding" of tariffs assumes a special importance in the context of GATT negotiations, the argument that additional external resources should be available to finance any unexpected increase in imports resulting from a developing country's binding commitments under the GATT appears, *prima facie*, quite reasonable. For example, if concessional long-term capital flows are directed toward countries which pursue appropriate macroeconomic policies combined with an outward-oriented trade policy, such additional financing may play a very helpful role. Indeed, recently the IBRD has increased its emphasis on policy-based, quick-disbursing loans for structural and sectoral adjustment, in which trade liberalization often plays a very important part. However, insofar as such suggestions seek to address a possible additional need for balance of payments financing, a strong note of caution is in order. In the broadest sense, the availability of balance of payments financing by the IMF is already tailored to the objective of promoting a liberal trade and payments system. As already mentioned, the IMF through the use of its resources supports open, rather than more restrictive, policies in member countries. The policies governing the use of IMF resources, including the limits on access for each member as a proportion of its quota, are established after a careful review of a range of factors, including the global need for balance of payments financing and the quality of programs that the IMF should seek to support. Therefore, it is questionable whether it would be desirable to establish a specific balance of payments financing feature linked directly to increased imports occasioned by the liberalization effort: such an open-ended scheme would risk ignoring the essential role of macroeconomic and exchange rate policies in achieving a sustainable medium-term balance of payments outcome. Hence, such a proposal has not appeared to be desirable or feasible.

As to the trade aspects, it has been argued that if economic growth is to be restored in the context of the balance of payments and debt problems of developing countries, indebted countries, particularly those undertaking trade liberalization under IMF or IBRD programs, must be allowed better opportunities to export to major markets abroad. Thus it has been suggested that specific and concrete measures be considered by the industrial countries to improve access for developing countries undertaking trade liberalization with IMF or IBRD financial support. The suggestion appears eminently reasonable at first glance. Nevertheless, several difficulties have been raised about the desirability of a special trade liberalization effort of this nature.

Some policymakers have questioned the justification for limiting any liberalization effort to a relatively narrowly-defined group of countries such as "indebted countries" or "countries with IMF or IBRD programs." Their argument has been that, if trade liberalization is desirable and feasible, particularly in the so-called sensitive sectors in the industrial countries, the effort should be broad-based and not limited to a few countries. Also, and more fundamentally, questions have been raised about how, under such special liberalization, the main GATT principle of nondiscriminatory treatment would be respected. The questions raised by "trade-finance links" will thus not be easily resolved.

Finally, and perhaps most importantly, the question will have to be addressed as to how the strengthened GATT provisions and practice in this area would fit with the overall program of trade liberalization that is a key objective of the Uruguay Round of negotiations. In the negotiating context, a determination will be made by each participating country on the bargains to be struck with other trading partners. While it is clearly difficult to suggest how such deals might be struck, it is evident that the treatment of restrictions applied by developed countries in sectors of special interest to developing countries will be important in influencing developing countries' willingness to offer liberalization of balance of payments restrictions. More broadly, since the success of balance of payments adjustment depends crucially on the assurance of open markets abroad, prospects for success in strengthening other key trading rules, such as on safeguards, subsidies, and quantitative restrictions, will be helpful in strengthening discipline on balance of payments restrictions.

## VII. Concluding Observations

The issues discussed above relating to the role and interest of developing countries in the Uruguay Round form part of a complex array of questions that will be examined in the coming years. A few general ideas deserve to be highlighted in conclusion.

First, it is evident that the GATT treatment of balance of payments restrictions merits a re-examination more substantive than has been undertaken since the inception of the GATT, because the economic premises on which the original approach was founded have largely lost whatever merit they might have had originally. It is now well understood that recourse to trade restrictions to correct the underlying imbalance between output and expenditure may have the effect of inducing compensating exchange rate changes, distorting trade and payments positions among countries, shifting the burden of adjustment to trading partners, and inviting retaliation. Equally, in the developing countries there is no basis for believing that trade restrictions can correct balance of payments problems, and insofar as the balance of payments provisions of the GATT are concerned, there is no valid economic reason to prefer resolution of balance of payments problems through trade restrictions. In addition, consistency of policy would

argue for tighter GATT disciplines on trade restrictions for balance of payments purposes, whose effects may be quite similar to exchange restrictions which are disallowed by the IMF.

Second, reexamination of the balance of payments provisions of the GATT will, in practice, need to proceed side by side with consideration of the related issue of infant industry protection. The rationale for long standing restrictions in the complex and restrictive trade regimes of many developing countries is often unclear. In many cases, infant industry protection and balance of payments protection apparently exist simultaneously. Thus it is difficult to see how the balance of payments provisions of the GATT could be improved and made effective without reconsidering the justification for most other trade restrictions in developing countries as well.

Third, insofar as the GATT's balance of payments provisions are concerned, the division of the world into "developed" and "developing" camps--whatever its validity in the late 1940s and the 1950s--appears to be increasingly irrelevant. Prospects for liberalization of trade restrictions in favor of developing countries in markets abroad would be enhanced if discipline on trade restrictions for balance of payments purposes were strengthened in markets of increasing importance to the industrial countries. A shift in developing countries' approach toward more flexible exchange rate arrangements and market-oriented incentives, which would make possible a reduced reliance on trade restrictions, is more likely to be acknowledged and built into the GATT framework if developing countries expect that there would be a substantial liberalization of trade in their important foreign markets. Whether the industrial countries are prepared to concede the usefulness to them of such a quid pro quo remains, of course, to be seen, but, in the author's view, such a re-orientation deserves careful consideration.

Infant Industry Protection and the GATT Enabling Clause

The basic "infant industry" provisions of the GATT are contained in GATT Article XVIII:C, whose main features may be described as follows. A "developing" member country for the purposes of this Article is defined in the General Agreement as an economy "which can only support low standards of living." Such a country is "free to deviate temporarily" from the provisions of the other Articles of the General Agreement, subject to the conditions described in the remainder of Article XVIII. In particular, Article XVIII:C entitles a developing country to provide governmental assistance to establish a particular industry "with a view to raising the general standard of living of its people," provided the member finds that no measure consistent with the other GATT provisions is practicable to achieve that objective. Article XVIII:C is narrower than Article XVIII:B in that, as modified by the 1979 Declaration on Safeguards for Development purposes, it permits measures to promote the establishment of a particular industry, and development of a new or extension of an existing structure--as compared with measures to safeguard the balance of payments which should, by definition, be applied across-the-board. However, in one respect, Article XVIII:C may be considered as being broader than Article XVIII:B: it permits the application of almost any measure necessary to achieve the stated objectives. The provision requires notification to the GATT, a wait of 30 days or 90 days depending upon whether consultation with affected contracting parties is requested, and the application of the measure on a nondiscriminatory basis. It allows trading partners adversely affected by the measure to suspend "substantially equivalent concessions" upon prior notice to the GATT. Thus, in comparison with Article XVIII:B, which excludes the possibility of retaliation by countries adversely affected by the balance of payments measure, Article XVIII:C has, in principle, a built-in safeguard against excessive recourse.

The original GATT provisions requiring prior notification and concurrence appeared quite onerous; thus developing countries were given additional flexibility by a CONTRACTING PARTIES' decision of November 1979 entitled "Safeguard Action for Development Purposes." In "unusual circumstances," developing countries were authorized to introduce the measures contemplated on a provisional basis immediately after notification, without awaiting concurrence by the CONTRACTING PARTIES. Even so, recourse to these "development provisions" is relatively infrequent compared to Article XVIII:B.

Also in November 1979, as part of the Tokyo Round package of decisions, the CONTRACTING PARTIES adopted a decision entitled "Differential and More Favorable Treatment, Reciprocity and Fuller Participation of Developing Countries"--the so-called enabling clause, which is usually interpreted as encouraging developing countries to lower protection. In addition to "legalizing," once and for all, tariff preferences in favor of developing countries, the decision includes a declaration that "developed countries do not expect reciprocity for commitments made by them in trade negotiations to reduce or remove

tariffs and other barriers to the trade of developing countries." 1/ In addition, the decision states that:

Less-developed contracting parties expect that their capacity to make contributions or negotiated concessions or take other mutually agreed action under the provisions and procedures of the General Agreement would improve with the progressive development of their economies and improvement in their trade situation and they would accordingly expect to participate more fully in the framework of rights and obligations under the General Agreement.

These provisions of the "enabling clause" reflect in part a view advanced in the Tokyo Round by a number of industrial countries that it would be desirable to "graduate" at least the more advanced developing countries from their "developing country status" under GATT. However, the specific modalities of applying this provision, particularly the way in which a developing country's trade policy should be adapted as its economy grows and matures, have not been discussed extensively in the GATT. In mid-1985, a statement made by India on behalf of a group of 23 developing countries proposed that GATT members should establish techniques and modalities to quantify concretely the application of GATT provisions on special and more favorable treatment for developing countries, but this suggestion has not been pursued. In the Uruguay Declaration, the relevant paragraphs on special and differential treatment are based on the language of the enabling clause, without further elaboration. Thus, an important question in the new round will be how to give substance to the enabling clause.

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1/ It should be noted that similar language had been incorporated in the GATT since 1966 in its Part IV.

GATT Balance of Payments Provisions: Main Features

The GATT balance of payments provisions at present consist of five main rules: (i) GATT Article XII, the basic balance of payments provision which applies in principle, to all GATT members, but in practice has been interpreted to apply mainly to developed members; (ii) GATT Article XVIII, which was amended in 1955 to include an explicit provision for balance of payments-induced trade restrictions by developing member countries; (iii) Article XV on the framework of GATT cooperation with the IMF, which the General Agreement recognizes as the organization with technical competence on balance of payments questions; (iv) Article XIV of the GATT which permits members under certain circumstances to impose discriminatory trade restrictions to deal with balance of payments problems; and (v) the 1979 Declaration on Trade Measures. The following paragraphs summarize the main features of these provisions and their practical application in recent years.

By and large, each GATT member is free to decide for itself whether to invoke the balance of payments provisions to justify some or all of its import restrictions. Thus, in practice there has been considerable variation in both the frequency of invocation and the particular GATT Article invoked. For example, certain countries (such as Bangladesh, Brazil, Egypt, Ghana, India, Korea, and Pakistan) have regularly invoked Article XVIII:12B and have periodically consulted with the GATT on their trade restrictions for balance of payments purposes. Other countries have invoked balance of payments provisions only infrequently, and some developing countries have hardly ever invoked these provisions. In some cases (e.g., Hungary), nonindustrial countries have invoked Article XII. In a few cases, countries (e.g., Israel and Portugal) have invoked neither Article XII nor Article XVIII--and yet, consultations with them on the balance of payments restrictions have been conducted as if they had invoked these provisions.

In most respects, the provisions of GATT Articles XII and XVIII are quite similar. The basic premise on which these provisions are based is that balance of payments problems are manifested primarily in movements in a country's international reserves. Thus, under Article XII:2(a), import restrictions to safeguard the balance of payments

shall not exceed those necessary: (i) to forestall the imminent threat of, or to stop, a serious decline in its monetary reserves, or (ii) in the case of a contracting party with very low monetary reserves, to achieve a reasonable rate of increase in its reserves.

Under Article XVIII:B(9), the word "imminent" is omitted. A developing contracting party is authorized to institute or maintain or intensify trade restrictions so long as they do not go beyond the extent needed

- (a) to forestall the threat of, or to stop, a serious decline in its monetary reserves, or
- (b) in the case of a contracting party with inadequate monetary reserves, to achieve a reasonable rate of increase in its reserves.

The premise underlying the balance of payments provisions of Article XVIII as stated in its preamble is that developing contracting parties, "when they are in the process of development, ...experience balance of payments difficulties arising mainly from efforts to expand their internal markets as well as from instability in their terms of trade."

The IMF was deeply involved in the formulation of the balance of payments provisions of the GATT from the very outset. Jackson has written that:

At the preparatory sessions in 1946-47, it was very clear that coordination with the International Monetary Fund was necessary. Indeed the close connection between trade matters and payments matters ...dictated that the trade organization, viewed prospectively at the 1944 Bretton Woods Conference as the necessary complement to the Fund, have a close relationship to the Fund at least in some matters ...[T]he Fund was represented at the ITO-GATT Preparatory Session and this liaison assisted in the development of those clauses relating to the IMF that now appear in the GATT. 1/

The relationship of the GATT and the IMF is established in Article XV of the GATT, which is entirely devoted to the subject of exchange arrangements. Article XV:2 of the General Agreement stipulates that:

In all cases in which the CONTRACTING PARTIES are called upon to consider or deal with problems concerning monetary reserves, balances of payments or foreign exchange arrangements, they shall consult fully with the International Monetary Fund.

Furthermore, CONTRACTING PARTIES called upon to accept IMF determinations and findings pertaining to, for example, what constitutes "a serious decline" in monetary reserves, or a "very low level" of

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1/ Jackson (1969), p. 693.

monetary reserves, but also with respect to "financial aspects of other matters ...in such cases." 1/

Article XIV is an interesting illustration both of GATT pragmatism and of the extent of Fund-GATT collaboration envisioned by the framers of the GATT. Thus, while discriminatory restrictions are, in principle, ruled out under GATT Article XIII, the subsequent GATT Article provides that a country invoking the balance of payments provisions of Article XII or Article XVIII:B:

May ...deviate from the [nondiscrimination] provisions of Article XIII in a manner having equivalent effect to restrictions on payments and transfers for current international transactions which that contracting party may at that time apply under Article VIII or XIV of the Articles of Agreement of the International Monetary Fund.

This provision finds its origin in the discriminatory quantitative restrictions applied by most European countries against the dollar area in the immediate postwar period, with little parallel in today's situation. This exception from the nondiscrimination principle of the GATT has therefore been little used in recent years. This is no doubt largely due to the reluctance of contracting parties to resort to discriminatory balance of payments restrictions. Moreover, IMF policy and practice have themselves moved strongly toward removing discrimination, particularly since the early 1960s; thus, it is difficult to imagine today that the IMF would be willing in most cases to grant authorization for discriminatory exchange restrictions, and hence the GATT for "equivalent" discriminatory trade restrictions.

The Declaration on Trade Measures adopted by the CONTRACTING PARTIES in November 1979 clarifies certain aspects of the rules governing balance of payments restrictions without modifying the substantive provisions of the General Agreement. Its three new stipulations are: (1) that, in applying restrictive import measures, GATT members should give preference to the measure which has the least disruptive effect on trade--an implicit recognition that price-related restrictions, such as import surcharges, are often preferable to quantitative restrictions; (2) that the simultaneous application of more than one type of trade measure for balance of payments reasons should be avoided; and (3) that whenever practicable, contracting parties should announce publicly a time schedule for the removal of the measures. The Declaration also removes an anomaly that arose because the GATT's balance of payments provisions (Articles XII and XVIII) refer explicitly only to quantitative restrictions. As a result, the main GATT body charged with examining the balance of payments restrictions of members--the Committee on Balance of Payments Restrictions--found that it had a clear mandate only to examine quantitative restrictions, while other

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1/ Article XV:2.

measures by a number of industrial countries were frequently examined by other special bodies established for this purpose, such as the GATT Working Party on the U.S. import surcharge of 1971. 1/ Under the 1979 Declaration, the GATT Committee on Balance of Payments Restrictions was explicitly given the mandate to examine all restrictive import measures for balance of payments purposes, including import surcharges and advance import deposits.

Two other elements of the Declaration on Trade Measures are noteworthy. First, its preamble acknowledges that "developed contracting parties should avoid the imposition of restrictive trade measures for balance of payments purposes to the maximum extent possible." This recognition reflects the pledges made by industrial countries in the OECD and elsewhere that balance of payments problems should not be dealt with by relying on trade restrictions. Second, the Declaration elaborates somewhat on an earlier provision by stipulating that the Committee on Balance of Payments Restrictions should, if so requested by a developing consulting country, give particular attention to the possibilities for "alleviating and correcting the balance of payments problem through measures that contracting parties might take to facilitate an expansion of the export earnings of the consulting contracting party." Under this provision of the 1979 Declaration, the issue of access to markets abroad was explicitly taken up, for the first time, in the 1983 balance of payments consultation with Brazil, which put forth concrete proposals on measures its trading partners could take to reduce protectionist trade barriers affecting its exports. 2/

The GATT Committee on Balance of Payments Restrictions is formally charged with carrying out the consultations on behalf of the CONTRACTING PARTIES and preparing a report on the individual consultations for adoption by the GATT Council, which generally follows without further discussion. Although membership of the Committee is open to all contracting parties, in practice the Committee is composed of about a dozen members. 3/ As per the practice in other GATT bodies, the European Community member states are represented by the Commission of the European Communities. The Community and the United States are generally the most active participants in the Committee's consultations. With the exception of the delegation of a consulting

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1/ Between 1970 and 1973 consultations on temporary trade restrictions for balance of payments purposes were held with Denmark, Finland, Iceland, New Zealand, South Africa, Spain, the United Kingdom, and the United States.

2/ The conclusion of the Committee on Balance of Payments Restrictions with respect to Brazil reproduced in Attachment II includes reference to the Brazilian request.

3/ The current members of the Committee are: Argentina, Australia, Brazil, Canada, Chile, the European Communities and member States, Finland, Ghana, Hungary, India, Japan, Malaysia, Philippines, Romania, Sweden, United States, and Zaire. The Committee is chaired by Ambassador P.L. Girard of Switzerland.

country, which is usually drawn from the capital for a full consultation, delegations are represented on the Committee by ambassadors or other senior officials of the country delegations accredited to Geneva. The GATT Director General is represented by one of his Deputies or by a senior member of the GATT secretariat. The IMF is represented by a senior staff member.

The documentation and information available to the Committee for each consultation include the following: a basic paper submitted by the consulting country, outlining the balance of payments problems facing it and the specific trade restrictions it justifies under the GATT's balance of payments provisions; a factual background paper prepared by the GATT secretariat, describing the trade aspects of the measures taken; and background documentation supplied by the IMF--usually the latest Recent Economic Developments report on the consulting country prepared by the IMF staff for their Executive Board and made available for the GATT consultation to the CONTRACTING PARTIES. At the consultation meeting, the IMF representative presents a statement of the IMF's "findings" concerning the consulting country. This statement is approved beforehand by the IMF's Executive Board and reflects the official views of the IMF. It covers broadly a description and an assessment of economic and financial trends and prospects in the consulting country, including in particular the balance of payments situation and policy measures taken by the authorities to deal with the external imbalance. Recent changes in the trade and payments system are briefly described. The statement usually concludes with the IMF's opinion on the strength or adequacy of the consulting country's policy stance for achieving a fundamental correction in the balance of payments and reducing reliance on restrictions.

The basic "plan of discussion" for GATT balance of payments consultations was adopted in 1958, and is still applied today. Comments by members of the Committee on Balance of Payments Restrictions are, in principle, invited under four broad headings: (1) balance of payments position and prospects; (2) alternative measures to restore equilibrium; (3) system and methods of the restrictions; and (4) effects of the restrictions. In practice the plan is applied flexibly, and the discussions rely quite heavily on the IMF documentation and the statement for arriving at an assessment under the first two headings, and on the documentation of the GATT secretariat and of the consulting country with respect to the last two headings.

In December 1972, the GATT Council approved new procedures for regular consultations on balance of payments restrictions with developing countries. Although the intent of procedural changes was to maintain the effectiveness of the consultations with developing countries while lessening the burden on the GATT and the developing countries concerned, their effect has probably been to dilute considerably GATT surveillance over developing countries' trade restrictions for balance of payments purposes. Under these procedures, once every two years developing countries acting under Article XVIII:B submit a written document on the nature of the balance of payments

difficulties, the system and methods of restrictions, the effects of the restrictions, and prospects of liberalization. In the Committee on Balance of Payments Restrictions this document serves as the basis of a consideration of whether a full consultation is desirable. In practice, unless one or more Committee members requests a full consultation, the requirement of consultation under Article XVIII:B is "deemed to have been fulfilled" for that year. If requested, the full consultation is scheduled for a subsequent session of the Committee, the documentation is assembled, and an IMF statement is delivered. In adopting the revised procedures, the GATT Council noted that a number of developing countries maintained import restrictions apparently for balance of payments purposes, without justifying these under GATT provisions. The adoption of the streamlined provisions would, it was hoped, contribute substantially to "easing the way for all developing countries to define their position regarding their restrictions in relation to the GATT provisions." <sup>1/</sup> In practice, this simplification does not appear to have increased substantially the frequency with which contracting parties resort to GATT balance of payments provisions.

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<sup>1/</sup> GATT, BISD, Vol. 20, p. 49.

Conclusions of the GATT Committee on  
Balance of Payments Restrictions in Selected Recent Cases

1. Argentina (April 1986) 1/

The Committee recognized that Argentina had faced serious economic disequilibria in the period since 1980. These concerned questions of fiscal balance, wage and price inflation and balance of payments. Serious outflows of capital had occurred. At the same time, world market prices and access conditions for Argentina's major exports in certain markets had markedly deteriorated. Despite efforts of the Argentine authorities in that period to reverse the situation, there had been no durable improvement in either internal or external imbalances. The Committee noted that import restrictions had markedly increased and that the import system had become considerably more complex and restrictive between 1982 and 1984, with certain discriminatory elements.

The Committee welcomed the adjustment measures taken by Argentina under the Plan Austral. These included the strengthening of fiscal and monetary policy, the freezing and subsequent de-indexation of prices and wages, exchange rate adjustments and measures to liberalize trade policy. The Committee expressed its understanding for the situation confronting Argentina and its support for these policies. It noted that significant positive results had already been achieved in the fields of the budgetary deficit, the level of inflation, the growth of the money supply and the balance of payments. The Committee welcomed the moves made by Argentina from mid-1985 to liberalize its trade and payments systems, in particular the liberalization of import licensing, and the prospects of further liberalization, as well as reductions of export taxes and the planned elimination of the emergency increases in import duties during 1986. The Committee encouraged Argentina to continue and strengthen its adjustment and liberalization policies and looked forward to further positive results being achieved.

2. Brazil (December 1983) 2/

The Committee noted that Brazil's balance of payments and reserves situation had deteriorated sharply since the last consultation, due to a number of factors. These included the impact of the world economic recession on external demand, difficulties of external financing and debt servicing, and problems of budgetary adjustment, amongst others, in the Brazilian economy. In addition, Brazil's export efforts were hampered by protectionist pressures abroad.

While recognizing the seriousness of Brazil's balance of payments problems and the need to maintain import restrictions in the current situation, the Committee noted that the Brazilian import system remained complex and lacking in transparency. The Committee welcomed the

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1/ BOP/R/159 (5/12/86), p. 6.

2/ BOP/R/135 (12/15/83), pp. 7-8.

statement by Brazil that a number of the measures included in its imports system were currently under review with a view to their modification, simplification, or phasing out, as the case might be. The Committee expressed the hope that, in this review process, views expressed in the Committee relating to the multiplicity and complexity of Brazil's measures and the desirability of establishing a time frame for the liberalization of such measures would be taken into account, in accordance with the provisions of Paragraph 1 of the 1979 Declaration.

The Committee, noting the statements by Brazil on the extent to which import measures adopted by its trading partners impinged upon its balance of payments, recognized the importance of giving particular attention to the possibilities for alleviating and correcting balance of payments problems through measures that contracting parties might take to facilitate an expansion of the export earnings of consulting contracting parties. Accordingly, the Committee agreed that members should jointly consider this issue in the broader GATT context, in the light of further consultations. The Committee noted the specific proposals made by the Brazilian delegation concerning ways to improve Brazil's export prospects. It was agreed that members would reflect further on these proposals.

3. Colombia (December 1985) 1/

The Committee noted that Colombia's domestic economic situation, as well as its trade and current account balances, had deteriorated sharply in the period 1981-83. This deterioration was due to a number of internal and external factors, including, as regards the former, the budgetary deficit and the level of exchange rate, and as regards the latter, unfavorable world markets for Colombia's principal exports, stagnation of import demand in its regional trading partners and restrictive import measures affecting products of export interest to Colombia in a number of markets.

The Committee, while noting the concurrent application of a number of import restrictions, which might be a source of uncertainty for traders, welcomed the clarifications given by Colombia in this regard, which alleviated some of its concerns regarding the complexity of the system.

The Committee appreciated the efforts being made by Colombia to restore internal and external equilibrium through fiscal, monetary and exchange rate policies as well as its efforts to stimulate the growth and diversification of exports. It recognized that the success of these policies would depend partly on the evolution of world commodity markets and of the economic and commercial situation in Colombia's trading partners. The Committee welcomed the announcement by Colombia that the process of import liberalization initiated in 1985 would be continued and strengthened.

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1/ BOP/R/156 (12/20/85), pp. 5-6.

4. Hungary (May 1984) 1/

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 percent import surcharge on April 1, 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.

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1/ BOP/R/141 (5/30/84), p. 5.

Table 1. Consultations Under Articles XII and XVIII:B of the GATT  
Committee on Balance of Payments Restrictions

Country	Year													Article	
	1974	1975	1976	1977	1978	1979	1980	1981	1982	1983	1984	1985	1986		
Argentina		X			X								<u>X</u>	XVIII:B	
Bangladesh	X		X		X		X		X		X		<u>X</u>	XVIII:B	
Brazil			<u>X</u>		<u>XX</u>		X	<u>X</u>		<u>X</u>		X		XVII:B	
Chile	X	X			<u>X</u>									XVIII:B	
Colombia													<u>X</u>	XVIII:B	
Egypt		X		X		X		X		X			<u>X</u>	XVIII:B	
Finland		<u>X</u>	<u>X</u>	<u>X</u>	<u>X</u>									XII	
Ghana	X		<u>X</u>		<u>X</u>		X		X	<u>X</u>		X		XVIII:B	
Greece	<u>X</u>		X		X		<u>X</u>	<u>X</u>						<u>X</u>	XVIII:B/XII
Hungary										<u>X</u>				XII	
India		X			<u>XX</u>		X		X		<u>X</u>			X	XVIII:B
Indonesia		X		X		X									XVIII:B
Israel	<u>XX</u>		<u>X</u>		<u>X</u>		<u>X</u>		<u>X</u>		<u>X</u>	<u>X</u>			Not stated
Italy								<u>X</u>							XII
Korea		X	<u>X</u>		X	<u>X</u>		<u>X</u>		X	<u>X</u>			X	XVIII:B
Nigeria											<u>X</u>			X	XVIII:B
Pakistan		X		X	<u>X</u>		X		X				X		XVIII:B
Peru	X	<u>X</u>		X		X		X		X				X	XVIII:B
Philippines							<u>X</u>		X		X				XVIII:B
Portugal		<u>X</u>	<u>X</u>		<u>X</u>	<u>X</u>	<u>X</u>	<u>X</u>	<u>X</u>	<u>X</u>	<u>X</u>	<u>X</u>			Not stated
Sri Lanka		<u>X</u>		X		<u>X</u>		<u>X</u>	<u>X</u>	<u>X</u>		<u>X</u>			XVIII:B
Tunisia	X		X		X	<u>X</u>		X		X		X			XVIII:B
Turkey		<u>X</u>		X		<u>X</u>		X		X		X			XVIII:B
Yugoslavia	<u>X</u>		<u>X</u>		X			<u>XX</u>			X			X	XVIII:B

Source: GATT secretariat.

X = Simplified consultation.

X = Full consultation.

Table 2. Use of Import Surcharges or of Advance Import Deposits  
by Common GATT-IMF Members--Developing Countries 1/

Country	Year											
	1974	1975	1976	1977	1978	1979	1980	1981	1982	1983	1984	1985
Argentina	X	X	X	X	X	X	X	X	X	X	X	X
Belize 2/	////	////	////	////	////	////	////	////	////	////	////	////
Brazil	X	X	X	X	X	X	0	0	0	0	0	0
Burkina Faso	0	0	X	X	X	X	X	X	X	X	X	X
Burundi	X	X	X	X	X	X	X	X	X	X	X	X
Chile	X	X	X	X	X	X	X	0	0	0	0	0
Colombia	X	X	X	X	X	X	X	X	X	X	X	X
Cyprus	0	0	0	0	X	X	X	X	X	X	X	X
Dominican Republic	X	X	X	X	X	X	X	X	X	X	X	X
Egypt	X	X	X	X	X	X	X	X	X	X	X	X
Gambia	0	0	0	X	X	X	X	X	X	X	X	X
Ghana	0	X	X	X	X	X	X	X	X	X	X	X
Greece	X	X	X	X	X	X	X	X	X	X	X	X
Haiti	X	X	X	X	X	X	X	X	X	X	X	X
Hungary 2/	////	////	////	////	////	////	////	////	0	X	X	0
India	X	X	X	X	X	X	X	X	X	X	X	X
Indonesia	X	X	X	X	X	X	X	X	0	0	0	0
Israel	X	X	X	X	0	0	X	0	0	X	X	X
Jamaica	0	0	0	0	X	X	X	X	X	X	X	X
Kenya	0	0	0	0	0	X	X	X	X	X	X	X
Korea, Rep. of	X	X	X	X	X	X	X	X	X	X	X	0
Malaysia	X	X	X	X	X	X	X	X	X	0	0	0
Malawi	X	X	X	X	X	X	X	X	X	X	X	X
Mauritius	0	X	X	X	X	X	X	X	X	X	X	X
Nicaragua	X	X	X	X	X	X	X	X	X	X	X	X
Nigeria	X	0	0	0	0	X	X	0	0	X	X	0
Pakistan	X	X	X	X	X	X	X	X	X	X	X	X
Peru	X	X	X	X	X	X	X	X	X	X	X	X
Philippines	X	X	X	X	X	X	X	X	X	X	X	X
Portugal	0	0	X	X	X	X	X	X	X	X	X	X
Rwanda	X	X	0	0	0	0	0	0	0	0	X	X
Sierra Leone	0	0	0	X	X	X	X	X	X	X	X	X
South Africa	0	0	0	X	X	X	X	0	0	X	0	0
Suriname 3/	////	////	////	////	////	////	X	X	X	X	X	X
Thailand	0	0	0	X	X	X	X	X	X	X	X	X
Tunisia 4/	0	0	0	0	0	X	X	X	X	0	0	0
Turkey	X	X	X	X	X	X	X	X	X	X	X	X
Uruguay	X	X	X	X	X	X	X	X	X	X	X	X
Yugoslavia	X	X	X	X	X	X	X	X	X	X	X	X
Zaire	X	X	X	X	X	X	X	0	0	0	0	0
Zimbabwe 5/	////	////	////	////	////	////	////	////	X	X	X	X

Sources: Based on IMF, Annual Report on Exchange Arrangements and Exchange Restrictions, various issues.

1/ The common GATT-IMF members considered are the common members on June 1, 1986; the definition of "developing countries" is in accordance with the convention used in IMF, International Financial Statistics. An "X" indicates that a country applied an import surcharge and/or an advance import deposit requirement either through the exchange or trade system usually at the end of the calendar year for which the IMF's Annual Report on Exchange Arrangements and Exchange Restrictions (AREAER) was prepared. An "0" indicates that no such restriction was applied. In a few cases, import surcharges are defined here to include additional import taxes not treated as "surcharges" in the AREAER.

2/ Belize and Hungary became members of the IMF in 1982.

3/ Suriname became an IMF member at the end of 1978.

4/ Tunisia acceded provisionally to GATT membership in 1985.

5/ Zimbabwe became an IMF member at the end of 1980.

Table 3. Selected Countries:  
Trade Coverage of Quantitative Restrictions for  
Balance of Payments Reasons under Article XVIII:B

Country	Year	Number of goods affected <u>1/</u>
Argentina	1986	728
Bangladesh	1986	606
Brazil	1985	320
Colombia	1986	864
Egypt	1985	49
Ghana	1985	602
India	1985	488
Korea	1986	200
Nigeria	1983	184
Pakistan	1985	435
Peru	1986	502
Philippines	1985	46
Sri Lanka	1986	137
Thailand	1983	2
Tunisia	1985	738
Turkey	1986	222
Yugoslavia	1984	192
Zimbabwe	1984	1

Source: GATT document NTM/W/17 (9/1/86).

1/ Each quantitative restriction refers to an affected commodity, where a commodity is defined by one of 1,010 four-digit Customs Cooperation Council Nomenclature (CCCN) categories. The quantitative restriction may affect all or only part of the four-digit group in question. The information is assembled from self-notifications to GATT. It excludes quantitative restrictions notified as being applied under GATT Article XVIII without further specification of whether Article XVIII:B or Article XVIII:C is invoked. It also excludes quantitative restrictions notified specifically under Article XVIII:C.

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