Dear Colleague,

I am transmitting with this letter a paper dealing with the third of the negotiating objectives before the Group on the Functioning of the GATT system. The paper is intended to focus the issues surrounding this objective and to summarize some of the substantive and procedural proposals which have been offered in the FOGs Group. The summary of proposals does not purport to be comprehensive.

It is my hope that the paper will assist delegations and their governments in their consideration of the third objective in advance of the next meeting of the group on September 26. I propose that this subject be the first item on our agenda at that time.

Sincerely yours,

Julius L. Katz
Chairman
Negotiating Group on the Functioning of the GATT System
Negotiating Group "Functioning of the GATT System"

Increasing the Contribution of the GATT to Achieving Greater Coherence in Global Economic Policy-Making

Chairman's Paper

1. Objectives (iii) and (iv) of the Ministerial Declaration on the Uruguay Round express the following aims:

"to increase the responsiveness of the GATT system to the evolving international economic environment, through facilitating necessary structural adjustment, enhancing the relationship of the GATT with the relevant international organizations and taking account of changes in trade patterns and prospects, including the growing importance of trade in high technology products, serious difficulties in commodity markets and the importance of an improved trading environment providing, inter alia, for the ability of indebted countries to meet their financial obligations;

and

"to foster concurrent cooperative action at the national and international levels to strengthen the interrelationship between trade policies and other economic policies affecting growth and development, and to contribute towards continued, effective and determined efforts to improve the functioning of the international monetary system and the flow of financial and real investment resources to developing countries."

2. The third part of the Negotiating Objectives on the Functioning of the GATT System states that:

"negotiations shall aim to develop understandings and arrangements to increase the contribution of GATT to achieving greater coherence in global economic policy-making through strengthening its relationship with other international organizations responsible for monetary and financial matters."

3. These objectives stem from a recognition by the CONTRACTING PARTIES that the state of the international economy, and prospects for such key issues as the growth of output and trade, job creation and the flow of resources to developing countries, depend on a whole array of policy elements, of which trade policy is only one. However, trade policies and other policies bearing on adjustment at the micro-level are closely interrelated to and interact with financial, monetary and exchange rate policies at both national and international levels. Greater coherence of these policies at both levels would ease many of the imbalances and pressures facing the world economy and stimulate world economic growth and trade.
4. The primary responsibility of the participants in GATT's work lies in the area of trade policies and does not extend to the overall coordination of macro-economic policies. However, governments of all contracting parties have a responsibility to ensure that, both at the national level and between countries, the effects of the financial, monetary and trade policies followed by them are consistent with each other. Financial, monetary or exchange rate policies should not frustrate the objective of trade liberalization. Similarly, protectionist measures should not be allowed to impede the effective functioning of macro-economic or financial policies. The efforts of the international institutions concerned should be directed in a mutually consistent manner towards these ends.

5. Within the overall framework of macro-economic policies, trade policy can effectively contribute to increasing structural flexibility by reducing impediments to the efficient allocation of resources. The reduction of structural impediments is likely not only to create better domestic conditions for growth, but also to reduce external imbalances, inter alia by increasing the scope for international trade and investment. It would also assist monetary and fiscal policies bearing on demand management and growth in output, and create better conditions for developing countries, through trade, to earn foreign exchange and alleviate their debt burdens.

6. The link between international trade policy and financial and monetary policies is particularly evident for developing countries. The maintenance of trade barriers against their exports adds to their difficulties in achieving the export growth needed to service external debt and increases the social costs of their adjustment programmes. At the same time, even the generation of substantial export surpluses would not provide a sufficient condition for the resumption of economic growth in some developing countries unless progress is also made in debt rescheduling and the restructuring of official financial flows.

7. Within the GATT context, governments can contribute directly to greater coherence in international trade policy-making by making firm commitments to adhere to the rules of the GATT, by the widest possible trade liberalization and expansion by all contracting parties and by the creation of more effective and enforceable multilateral disciplines where needed. Regular review and surveillance of trade policies by the CONTRACTING PARTIES and closer political-level involvement through participation of Ministers would assist this process. These elements would reinforce the commitment of governments to the central contractual provisions of the General Agreement, and would strengthen the credibility and functioning of the GATT as an institution. This would enable GATT to play a more effective policy role, helping to ensure greater coherence between trade policies and financial and monetary policies.

8. It is against this background that proposals by participants for consideration of substantive issues and for the establishment of institutional linkages between GATT and relevant international financial
and monetary institutions should be considered. It is recognized that institutional relationships are not an end in themselves but a means through which a policy framework can be established to better ensure that decisions taken within each institution do not conflict or cancel each other out.

9. Among "substantive" questions which have been proposed for examination are:

- the granting of credit to developing countries for trade liberalization commitments undertaken autonomously, or in the context of structural adjustment programmes, by them;

- the extent of coherence between commitments undertaken by developing countries towards the IMF and the World Bank respectively, and the consistency of such commitments with GATT undertakings;

- the involvement of GATT in the formulation of trade policy objectives included in IMF or World Bank programmes;

- the consideration by GATT, Fund and Bank of financial "contingency clauses" which might be included in stabilization or structural adjustment programmes;

- changes in the provisions of the General Agreement which would help to place it on a firmer legal footing.

10. The same broad considerations underlying the objectives and scope for greater coherence among trade, monetary and financial policies should determine the approach to be made in the group to the following proposals by participants for strengthening GATT's relationship with other relevant international institutions:

- consideration of the legal and practical provisions for consultations between the IMF and GATT: possibilities for consultations on relevant issues with other appropriate international institutions;

- regular joint meetings of Trade and Finance Ministers, or concurrent meetings of a joint Standing Group of Ministers in GATT and the Interim and Development Committees to consider questions of the interaction of trade, financial, monetary and development policies; preparatory arrangements for such meetings including interorganizational meetings of senior officials and task forces within each organization on areas of their respective competence;

- establishment of "special joint group on trade and finance" among Secretariats at DG level, reporting to all three institutions;
- mutual exchange of information and sharing of services among relevant international institutions, including common use of data bases;

- strengthened co-operation between the GATT Secretariat and the staffs of other institutions, including:
  - informal or formal inter-agency contacts at Director-General or Deputy level;
  - representation in meetings of each organization;
  - staff exchanges or secondments;
  - GATT liaison office in Washington.

- strengthening the capacity of the GATT Secretariat in economic analysis and establishing geographical desks (also relevant to the enhanced surveillance of trade policies envisaged under Objective (i)).