The Factual Position under the Treaty

1. The detailed information furnished by the Six is reproduced in the table appended to this Annex. The following are the salient features as noted by the Working Party, any discussion of these matters being reported in Part Three of this Annex or in the Working Party's main report.

Present Import Duties of the Six

2. The Benelux countries and the Federal Republic of Germany fully apply their specific import duties on leaf tobacco. These duties had an equivalent average incidence of 8 per cent and 32 per cent in 1956 respectively. France and Italy have no import duty on manufactured tobacco at present but control their imports through State Monopolies.

The Establishment of the Common Tariff

3. The common external tariff rate for leaf tobacco does not represent an arithmetical average of the existing tariffs of the Member States but has been fixed in List F at 30 per cent ad valorem. The German specific rate - the incidence of which is shown in the table as 32 per cent - will eventually be converted to an ad valorem duty and will be brought into conformity with the common rate as from the first stage. In Belgium the duty rate will be increased at the end of the first two stages and the 30 per cent ad valorem rate will be
applied at the end of the transitional period. In France and Italy where State Monopolies exist and where no import duties as such are levied, ad valorem duties will be applied at the rate of 9 per cent and 18 per cent at the end of the first and second stages and will be increased to 30 per cent at the end of the transitional period.

4. Since the full tariff item No. 24.01 (unmanufactured tobacco; tobacco refuse) is included in List F, the rate of 30 per cent will be applicable to stemmed as well as unstemmed tobacco; the table relates only to unstemmed tobacco simply because for the time-being trade in stemmed tobacco is small.

5. Reference was made also to the fact that in its GATT Schedule France had granted duty-free treatment to raw tobacco (item Ex 233A) and that this concession was supplemented by a Note to the Schedule providing for the annual importation by the State Monopoly of 15,000 tons of leaf tobacco originating in countries outside the French Union, and further that provision was made for this amount to be increased in certain circumstances. Asked whether this concession would be maintained, the representatives of the Six stated that if any change were contemplated, it would be effected through the tariff negotiation procedures of Article XXIV:6.

Duties on Imports from the A.O.T's

6. The Benelux and German duties will be reduced for imports from the A.O.T's by stages. The following are the differences between the duties that will apply to imports from third countries and the duties, if any, applying to imports from the A.O.T's:

<table>
<thead>
<tr>
<th>Duty Differentials in favour of the A.O.T's</th>
</tr>
</thead>
<tbody>
<tr>
<td>After</td>
</tr>
<tr>
<td></td>
</tr>
<tr>
<td>Benelux</td>
</tr>
<tr>
<td>France</td>
</tr>
<tr>
<td>Germany</td>
</tr>
<tr>
<td>Italy</td>
</tr>
</tbody>
</table>
Fiscal Duties

7. Although duties on tobacco were mainly of a fiscal nature the representatives of the Six indicated that the question of their replacement by internal charges was unlikely to arise since in Germany the new duty would be roughly equivalent to the present specific duty, in the Benelux countries the duty would be increased, and in France and Italy no duties are imposed at present.

Quantitative Restrictions

8. No restrictions on imports of leaf tobacco are maintained by Germany. The Benelux countries have a licensing system but import licences are issued freely. Imports into France and Italy are in the hands of State Monopolies.

The Agricultural Provisions of the Treaty

9. Tobacco (item 24.01) is included in Annex II of the Treaty. The provisions of Articles 39 to 46 of the Treaty could therefore be applied.
PART TWO

BACKGROUND INFORMATION ON TRADE AND TRADE PATTERNS OF TOBACCO

General

10. The export value of international trade in tobacco in 1955 amounted to about $700 million.

11. Tobacco exports are of particular importance in the export trade of several GATT countries as indicated in the following table:

Raw Tobacco Exports from Selected Countries

<table>
<thead>
<tr>
<th>Country</th>
<th>1955 Quantity (000 tons)</th>
<th>1955 Value (£)</th>
<th>1956 Quantity (000 tons)</th>
<th>1956 Value (£)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Madagascar</td>
<td>4</td>
<td>5</td>
<td>4</td>
<td>5</td>
</tr>
<tr>
<td>Belgian Congo</td>
<td>-</td>
<td>-</td>
<td>0.1</td>
<td>*</td>
</tr>
<tr>
<td>Greece</td>
<td>55</td>
<td>76</td>
<td>48</td>
<td>65</td>
</tr>
<tr>
<td>Turkey</td>
<td>60</td>
<td>89</td>
<td>61</td>
<td>93</td>
</tr>
<tr>
<td>Rhodesia &amp; Nyasaland</td>
<td>56</td>
<td>72</td>
<td>75</td>
<td>79</td>
</tr>
<tr>
<td>Cuba</td>
<td>22</td>
<td>42</td>
<td>21</td>
<td>48</td>
</tr>
<tr>
<td>Dominican Republic</td>
<td>13</td>
<td>43</td>
<td>19</td>
<td>44</td>
</tr>
<tr>
<td>Indonesia</td>
<td>12</td>
<td>27</td>
<td>11</td>
<td>27</td>
</tr>
<tr>
<td>United States</td>
<td>245</td>
<td>355</td>
<td>231</td>
<td>333</td>
</tr>
<tr>
<td>India</td>
<td>40</td>
<td>23</td>
<td>42</td>
<td>32</td>
</tr>
<tr>
<td>Brazil</td>
<td>28</td>
<td>18</td>
<td>31</td>
<td>20</td>
</tr>
<tr>
<td>Canada</td>
<td>22</td>
<td>26</td>
<td>14</td>
<td>17</td>
</tr>
<tr>
<td>Philippines</td>
<td>6</td>
<td>2</td>
<td>8</td>
<td>3</td>
</tr>
</tbody>
</table>

* Less than 1 per cent

12. It is apparent that tobacco is a particularly important item in the economy of a number of GATT countries, for example, Greece, Turkey, Rhodesia and Nyasaland, Cuba and the Dominican Republic.

13. The Six are of major importance in world tobacco trade. In 1955 and 1956 they accounted for about 27 per cent of total imports, as compared with about 23½ per cent for the United Kingdom - at present the most important single market for this commodity. Any economic or political change which may affect the pattern of the tobacco trade of the Six is, therefore, bound to be felt by tobacco exporting countries and especially by those referred to in paragraph 3 above.

14. The market of the Six is of special direct importance to certain GATT countries, notably the Federation of Rhodesia and Nyasaland, which in 1957 sent over 16 per cent of its total quantity exported to the Six compared with about 14 per cent in 1956 and 10 per cent in 1954. The Dominican Republic sent per cent of its total exports to the Six in 1956, Indonesia per cent, Brazil per cent, India per cent and Cuba per cent. Imports of cigar leaf tobacco alone were currently about 33,000 metric tons per annum into the Six and four contracting parties to GATT (Brazil, Cuba, the Dominican Republic and Indonesia) accounted in 1956 for 84 per cent of that amount.

15. The general pattern of the trade of the Six in 1956 was that of their total imports of unmanufactured cigar and cigarette leaf tobacco as given in their import statistics of about 167,000 tons in 1956, 5,000 tons (3 per cent) came from the French Associated Territories, 52,000 tons (31 per cent) from the United States, 38,000 tons (23 per cent) from Greece and Turkey, and 10,000 tons (6 per cent) from Brazil. The other

* Figures will be inserted by the secretariat.
principal suppliers were Rhodesia and Nyasaland (3 per cent), Indonesia (5 per cent), Dominican Republic (3 per cent). Smaller quantities were supplied by India, Canada and Cuba. It is difficult to split these figures into types but it can be assumed that the French Associated Territories provided mainly light and dark air-cured, Greece and Turkey - oriental leaf, Dominican Republic and Cuba - cigar leaf, Brazil and Indonesia - chiefly cigar leaf but some flue-cured, United States of America, Rhodesia and Nyasaland, India and Canada - predominantly flue-cured.

16. Within this overall picture, France took the whole of the production (excluding the small internal consumption) of 5,000 tons from her A.O.T's. Belgium-Luxemburg took an insignificant quantity from the Belgian Congo, but there were no imports from the A.O.T's into the other countries of the Six.

17. Tables B and C appended show the more detailed pattern of trade in tobacco in 1956. Table B is based on export statistics of the main exporting countries and Table C on import statistics of the Six and certain other large importing countries. There are certain discrepancies between the export and import statistics referring to the same trade flow, due mainly to differences in the system of recording trade (General and Special trade) but also to a number of other factors.

Varieties

18. World tobaccos are usually grouped into eight major categories as shown below. The groupings are made primarily on the basis of characteristics due to genetics, and to environment - soil, fertilizer, and climate - together with the method of curing.

1 These tables based on FAO figures will be attached by the secretariat.
Tobacco can be grown in a great variety of soils and climates and sources of importance in world trade only are shown. Similar types grown in different areas have different characteristics, and there is a wide range of qualities within the varieties shown. The following table shows the approximate production harvested in the calendar year 1956, by types. (Source: World Tobacco Analysis - United States Department of Agriculture).

<table>
<thead>
<tr>
<th>Variety</th>
<th>1,000 pounds</th>
<th>Percentage of total</th>
</tr>
</thead>
<tbody>
<tr>
<td>Flue-cured</td>
<td>2,937,782</td>
<td></td>
</tr>
<tr>
<td>Burley</td>
<td>606,733</td>
<td>35</td>
</tr>
<tr>
<td>Other light air-cured</td>
<td>283,808</td>
<td>7</td>
</tr>
<tr>
<td>Oriental and semi-Oriental</td>
<td>929,944</td>
<td>3</td>
</tr>
<tr>
<td>Light sun-cured</td>
<td>844,123</td>
<td>11</td>
</tr>
<tr>
<td>Dark air-cured</td>
<td>1,835,577</td>
<td></td>
</tr>
<tr>
<td>Dark sun-cured</td>
<td>852,324</td>
<td>10</td>
</tr>
<tr>
<td>Fire-cured</td>
<td>137,617</td>
<td>2</td>
</tr>
<tr>
<td>Total:</td>
<td>8,427,908</td>
<td>100</td>
</tr>
</tbody>
</table>

19. In the following the main sources and the normal use of the various types of tobaccos are indicated:

**Flue-cured**

Light Virginian type tobaccos used mainly in cigarettes, but to some extent in pipe and cigarette mixtures. Main sources are the United States, China, the Federation of Rhodesia and Nyasaland, India and Canada.

**Burley**

Heavy type tobacco, used primarily in the United States in cigarettes and elsewhere as a pipe or chewing tobacco. Sources are wide e.g. North American continent, Italy, Spain, Japan, Argentina, Germany and the Federation of Rhodesia and Nyasaland.
Other light air-cured

Primarily for use in cigarettes. Production is small but expanding. Main sources of supply are the United States, Madagascar and Italy.

Oriental and semi-Oriental

Popularly known as "Turkish", these tobaccos have a distinctive aroma and flavour, and are used chiefly in cigarettes. Principal sources of supply of Oriental are Turkey, Greece, USSR, Bulgaria, Yugoslavia, Italy and Middle Eastern countries. Semi-Orientals are grown in Italy, Yugoslavia, USSR and Eastern European countries.

Light sun-cured

The bulk is used in cigarettes and in pipe tobaccos, although some types are used in cigars and cigarillos. Production is centred in Asia, especially China, Japan, India, Korea, Pakistan. A little is grown in Algeria, Mexico and Paraguay. With the exception of a few minor types, this kind of leaf is not important in world trade.

Dark air-cured

These are used for cigarette, cigar and pipe tobaccos. Production is widespread in North and South America, Europe, Asia, Africa, the individual countries with the greatest production being the United States, Brazil, China, Indonesia and the USSR.

Dark sun-cured

Produced mainly in Asia and the Caribbean areas. In the former area this tobacco is used in hookah pipes, conventional pipes, snuff and low-priced cigarettes. The Caribbean leaf is used mostly in cigars and cigarillos.
Fire-cured

This tobacco is "strong" and is used in the making of heavy pipe and cigarette tobaccos. Nearly all production is centred in the United States, Italy and the Federation of Rhodesia and Nyasaland, although small amounts are grown in Uganda, Tanganyika and a few other countries.

Manufactured Products

20. As stated before the United Kingdom is at present the most important single importer of raw tobacco in the world. Her export trade in manufactured cigarettes is also not inconsiderable. United Kingdom cigarette exports average 18,000 metric tons per annum over the three years 1955 to 1957, of which over 4,000 metric tons on an average were exported to the Six, or almost 23 per cent of the total.

Transit and re-export trade

21. A large well-balanced transit and re-export trade is carried on in the Netherlands and, to a lesser extent in Belgium, chiefly in cigar and flue-cured leaf. The Dutch trade concerns especially Indonesian tobacco which in 1956 amounted to 50 per cent of the total. The remainder of the trade consists of leaf produced in other exporting countries such as the United States, the Dominican Republic, the Federation of Rhodesia and Nyasaland and India. According to data supplied by the Netherlands delegation, the situation was as follows in 1956:

<table>
<thead>
<tr>
<th>Total entered into bonded warehouse</th>
<th>Total re-exports</th>
</tr>
</thead>
<tbody>
<tr>
<td>88,900 metric tons, of which, 44,000 tons from Indonesia</td>
<td>76,700 metric tons, of which, 58,800 tons to the Community</td>
</tr>
</tbody>
</table>
22. It must be emphasized that the figures given in paragraph 6 above have been taken from the official statistics of the Six and that these figures, in several cases, do not correspond with the export statistics of the supplying countries. For instance imports of leaf tobacco into the Six in 1956 from the Federation of Rhodesia and Nyasaland have been given in this report at 5,200 metric tons, whereas the export statistics of this country disclose an amount of 10,700 tons. Similarly the statistics of exports of the Dominican Republic reveal a figure of 7,062 metric tons as against 4,955 metric tons shown by the import statistics of the Six. The discrepancy between the two sets of figures could probably be partly attributable to the complexities of the entrepôt transit and re-export trade of the Benelux countries and Germany.

Prospects of world supply and demand

23. Tobacco is an annually planted crop and, unlike commodities such as cocoa, coffee and tea production can be adjusted rapidly so as to meet any changes in demand.

24. It is extremely difficult to assess the future demand for leaf tobacco throughout the world. It is virtually impossible to get such information from some non-GATT countries which consume substantial quantities of tobacco. Furthermore, demand is governed to a large extent by the level of taxation on tobacco products in consuming countries. It is also influenced by the changes in smokers' tastes and by the reaction of consumers to the propaganda on the dangers to health brought about by cigarette smoking. There has, for example, been a significant change in cigarette smoking over the last few years in many parts of the world, and increased quantities of filter tipped cigarettes - which contain less tobacco than non-filter cigarettes - have been consumed in many countries.

\[1\] See IC/WPI/13.
25. Although the consumption of cigarette tobacco in the United Kingdom - the largest importers - is relatively steady (in 1947 the United Kingdom consumption was 116,000 metric tons and 108,500 metric tons in 1955), the world cigarette consumption is increasing at a moderate rate, while cigar consumption is slowly declining on a per capita basis. Pipe tobacco is now steady, while snuff and chewing tobacco are still showing a decline in consumption.

26. At present the world supply position adequately meets demand and indeed in the case of the largest producing country in the world, the United States, heavy stocks of leaf tobacco are being held by the Commodity Credit Corporation; the acreage planted to tobacco is controlled by government action. In the other exporting countries too there has been concern about the future of the tobacco trade and some of these countries have taken steps to limit production. In the long-term, therefore, it can be said that world production of tobacco is likely to be adequate to meet any increased demand, but there are definite indications of the supply potential being substantially in excess of consumption.
PART THREE

THE SHORT AND LONG-TERM PROBLEMS WHICH THE ASSOCIATION OF THE A.O.T's RAISED FOR THE TRADE OF OTHER CONTRACTING PARTIES TO THE GENERAL AGREEMENT

I. The New Tariff Régime

A. Effects within the Community and the A.O.T's

27. Representatives of the tobacco producing countries other than the Six considered that the common tariff of 30 per cent and the duty-free entry of tobacco from the A.O.T's of the Community into the whole market of the Six under Article 133(1) of the Treaty would constitute a discriminatory tariff in favour of the O.T's. This compared with the previous position in 1957 in which there were no applied preferential tariffs on behalf of the A.O.T's in any market of the Six.

28. The representatives of the Six were of the opinion that the abolition of tariffs on trade inside a free-trade area could not be considered as constituting a discriminatory measure.

(1) Effects on price levels in the Community and the A.O.T's

29. Representatives of the tobacco producing countries other than the Six thought that the preferential element of the tariff would be reflected in a corresponding difference between the price offered by importers in the Six to exporters in the A.O.T's on the one hand, and to exporters in third countries on the other. There will be a corresponding increase in price levels within the Community. This margin of preference would be from 6 per cent to 9 per cent at the end of the first period and increasing by stages at the end of the transitional period to 30 per cent.

Tobacco producers participating in the Working Party were: Brazil, Dominican Republic, Federation of Rhodesia and Nyasaland, Ghana, Greece, India, Indonesia, United Kingdom and United States of America. Canada, Turkey and Union of South Africa participated as observers.
30. Reply of the Six, see paragraph 2 of Part III, document MGT/32/58.

(ii) Effects on consumption in the Community

31. Representatives of the tobacco producing countries other than the Six pointed out that the margin of preference which would in future be offered in the whole market of the Six would enable A.O.T. exporters to obtain as much of the market of the Six as they desired for the types, quantities and qualities they could offer. The French and Italian requirements were already filled to a very large extent by their domestic and A.O.T. production so that in the long-run, as production in the A.O.T's is stimulated by the 30 per cent preference, there would be a switch in demand in Germany and the Benelux countries away from tobacco produced by third countries to the duty-free tobacco offered by the A.O.T's and this demand would increase progressively.

32. Referring to the different types under Part II, paragraph 9, pointed out that the effect of the preferential duty would have somewhat different effects on many of the various types of leaf tobacco. First of all tropical cigar tobacco is divided into three types: wrapper, binder and filler. Wrapper leaf is a high quality, high-priced speciality, imported at present from Indonesia and Cuba. Binder leaf is similar but not quite such a specialized, expensive product and is exported from Brazil and the Dominican Republic as well as from Cuba and Indonesia. The effect of a 30 per cent duty would be to raise considerably the landed price for the wrapper and binder types of tobacco and by doing so would reduce the demand for cigars generally. But a more serious effect would be suffered by the producers of cigar filler tobacco, which is a more ordinary and inexpensive quality tobacco. With a high incidence of the duty on wrapper and binder leaf, which up to now has been largely imported into the Six, the manufacturers would have to look elsewhere for lower priced filler and even possibly binder to keep the cost of the finished product at a level that would affect their trade as little as possible. These representatives are therefore most anxious about the exports of their filler tobacco trade as it is practically
certain that manufacturers, placed in such a position, would endeavour to replace their normal filler supplies with cheaply available leaf that can be produced in the A.O.T's under a preferential margin of 30 per cent. This would have a most damaging effect on the present imports of filler leaf from non-Community countries which are contracting parties to GATT such as the United States, Dominican Republic, Brazil and Cuba.

33. Of the leaf tobacco imports into the Six the major part consists of types used in cigarette manufacture - mainly flue-cured and oriental. These are relatively high priced tobaccos; a 30 per cent duty will cause a sharp rise in the price of cigarette brands which include these two types of tobacco and a consumer resistance may occur.

34. Since it is not known whether oriental types could be easily produced in any significant quantity in the A.O.T's, the effect of the 30 per cent duty would be to raise the price of oriental types to consumers and thereby tend to lower the demand, or to depress prices to producers as a consequence of the necessity to offset a part of the increased preferential duty. Greece and Turkey, both contracting parties to GATT, are the countries that would be especially affected.

35. Virginia flue-cured and air-cured tobaccos account for the greater proportion of cigarette tobacco consumption in the Six. Production of flue-cured tobacco requires capital and skill, and it is most successfully grown within a fairly narrow range of soil and climatic conditions. The cost of production of this type of tobacco is high in relation to that of some other types - notably fire, air and sun-cured, which can be grown comparatively easily under tropical and sub-tropical conditions, and requires less skill. In fact, fire, sun and air-cured tobaccos are very suitable cash crops for peasant production, and given price and market incentives it can be foreseen with certainty that their production in the A.O.T's will be increased.
36. These representatives held the view that while flue-cured tobacco has very different characteristics from sun, and air-cured tobaccos, experience in France and Italy, however, has shown conclusively that consumers will, in the long run, accept the substitution of a large proportion of flue-cured by these other types in their blends. In France, flue-cured only is about 5 per cent of consumption, as compared with over 40 per cent in Germany. Under a 30 per cent preference the existing price differential between flue-cured and air-cured tobacco imported from non-Six countries and the A.O.T's respectively will be greatly widened, and this artificial distortion of existing price relationship, which reflects the existing demand pattern, must lead to the gradual replacement of a substantial part of the flue-cured tobacco imported from non-Six countries by air-cured and other types produced in the A.O.T's, Italy and Algeria.

37. They draw attention to the threat to the trade of the non-Six producers from the large potential production of flue and as well as other types of tobacco in Algeria and also other North African countries which may be associated with the European Economic Community and which would therefore come under the umbrella of the preferential market. These members wish their fears to be recorded, although the above-mentioned countries cannot come under discussion in view of the terms of reference of this Working Party.

38. In this context these representatives considered that the history of the tobacco trade showed clearly that consumption habits regarding the various types of tobacco can be permanently influenced by price or supply conditions. Reference was made to the shift in consumer preference in the United Kingdom toward Rhodesian tobacco and away from American tobacco, as a result of import restrictions introduced on imported tobacco as a consequence of balance-of-payments difficulties. A similar development has occurred in France, and reference was made to the United States Department of Foreign Agriculture Circular of 15 July 1955, which states on page 6:
"The decline in United States exports of fire-cured tobacco to France during the post-war period can be attributed to increased demand for milder dark cigarettes and smoking mixtures. During the war, when supplies of United States fire-cured were cut off, consumers became accustomed to milder tobacco products than those smoked in pre-war. As a consequence, the quantity of United States fire-cured types used in cigarettes and smoking mixtures is considerably below pre-war proportions. Pro-war, about 20 per cent Kentucky was used in the ordinary cigarettes, such as Gauloises and Celtiques; this proportion declined to about 15 per cent during the early post-war period, and has further declined to less than 5 per cent during the past few years.

"The acute dollar shortage resulted in increased imports of oriental types of tobacco, which further modified consumer taste for fire-cured leaf. Also, the relative price differential between United States fire-cured tobaccos and other foreign dark and sun-cured tobaccos has resulted in reduced purchases of our dark leaf. The price factor in sales of United States tobacco to France has always been important and became especially significant during the period of dollar exchange difficulties."

The account given in this bulletin of changes in French consumption habits showed conclusively how first the supply position and later the price factor have both had permanent influences on the types of tobaccos smoked.

39. These representatives considered furthermore, that the new duty rate on tobacco especially the higher priced cigar leaf, oriental and flue-cured types would cause a decrease in demand for tobacco imported from third countries. Demand for these tobaccos might eventually recover again with increasing wealth in the Community, and it was by no means certain since increases in wealth would necessarily result in increased tobacco consumption. In any event, such increase as might take place would be taken up first on a preferential basis by producers of the A.O.T's, thus the percentage share of the market supply by the non-Six countries would decline. This would be particularly significant for cigar filler tobacco.

40. The representatives of the Six replied that by stimulating the economic development of the A.O.T's, the implementation of the Treaty would result in increased consumption from which third
countries would inevitably benefit. Furthermore - as already mentioned in the case of other commodities - the creation of the Common Market of the Six would lead to a more stable market situation, which was very important to producers throughout the world.

41. They recalled in reply to the statements reproduced in paragraphs 6 to 10, in the first place, that it was impossible to assess the extent to which a rate of duty was reflected in prices; in general, price formation was governed by complex factors among which a customs preference was often only a minor element. In their opinion it was difficult to infer from such a precarious basis that at the end of the transitional period the A.O.T's would be in a position to produce tobaccos which could be substituted for all those types at present imported from third countries. In any case experience had shown that even with monopoly protection A.O.T's in the French franc area had not developed production of those types of tobacco, and that the total quantities produced were still very small.

42. These representatives agreed that consumer taste might change. They pointed out, however, that such a change usually came about very slowly and in rather exceptional circumstances, for instance in times of shortage as had been the case during the last war. With regard to the example cited in paragraph 10 above, the representatives of the Six thought that the shift in favour of Rhodesian tobaccos which had occurred in the United Kingdom was attributable not so much to price considerations but rather to dollar import restrictions. They also argued that in order to determine to what extent the common tariff duty was likely to influence consumer taste, one should first consider to what extent the duty would be reflected in consumer prices; as had already been indicated, a preferential margin was very seldom reflected automatically and fully in price levels. It was obvious that consumption was affected by price levels and the supplies available, but it was also influenced by other factors among which price levels were relatively of secondary importance in the case of a product like tobacco which was not an essential commodity.
43. They also recognized that the price impact of the duty, to the extent that it was reflected in prices would vary depending on the types of tobacco concerned. In general the duty would affect cheaper quantities to a lesser extent; as regards higher grades, they again emphasized that such tobacco was a luxury product and that consumers of such varieties were relatively well off so that in general any increase in prices would only have a very limited effect on consumption. Experience had shown that in general, above a certain income level the influence of prices decreased proportionately, and the representatives of the Six again reminded the representatives of the non-Six producers that in their opinion the discussion should, as in other cases, be based on the hypothesis of an expanding economy, and therefore of an increase in consumption.

44. These representatives also said that in considering the future pattern of trade, it must be taken into account that consumption would probably increase substantially. The present needs of the Six and the A.O.T's amounted to 300,000 metric tons per annum, of which they produced only about 4 per cent, and it was estimated that by 1965 requirements would have risen to 375,000 metric tons.

(iii) Effects on Production in A.O.T's

45. Attention was drawn by representatives of the tobacco producing countries other than the Six to the fact that in 1953, the last year for which complete figures are available, production of tobacco in the A.O.T's was nearly 12,000 metric tons, and appeared to be increasing. Although this was a considerable increase on production ten years ago, it could nevertheless still be considered a small quantity. So far as the French overseas territories are concerned their production had no doubt already reached the limit of the market available to them in France, the greater part of their tobacco requirements, other than that imported for blending purposes, being already grown by home producers in France and Algeria. It would have been difficult to find economic outlets for any greater production. The proposal to give the A.O.T's duty-free entry into the whole market of the Six, however, would completely alter the
picture. It might be foreseen, as already mentioned, that under these conditions their type of tobacco would gradually replace that presently imported from non-Six countries.

46. They considered furthermore that there were strong possibilities of a marked increase in production of cigar leaf tobacco in Madagascar and some of the other A.O.T's. With the 30 per cent price advantage, it could be assumed that the production of cigar tobacco from those territories would replace by the end of the transitional period, a large part of the 33,000 tons of cigar leaf tobacco at present imported from third countries. The land and labour required to produce this relatively small quantity would not be great, but the consequences would be.

47. They also were of the opinion that production of air-cured and sun-cured tobacco could also be very readily increased in large areas of the A.O.T's. As already stated, it is a cash crop highly suited for peasant cultivation, requiring no capital and well suited to a wide variety of tropical and sub-tropical regions. Apart from the extensive production of tobacco by Africans in the Federation of Rhodesia and Nyasaland, tobacco growing is expanding rapidly in all parts of Nigeria and is being developed in Ghana. There seemed no reason why similar developments should not take place in most of the A.O.T's. The price advantage which tobacco from these areas would have over tobacco from third countries was such that there would be a new and considerable demand for it from the Benelux countries and Germany. Present A.O.T. production of 12,000 tons of this type of tobacco might well be expanded to 60,000 tons by the end of the transitional period and could continue to increase—possibly at a more rapid rate thereafter.

48. Referring to the views expressed by the representatives of the producing countries, the representatives of the Six pointed out that neither the qualities nor the quantities currently produced in the A.O.T's could probably replace those at present consumed in the Community countries, and that there were no grounds for assuming that the A.O.T's would be in a position to do so in future, and that
account should be taken of the fact that consumption was increasing in those territories which were importing greater quantities of tobacco each year. An article in "Tobacco Intelligence", published by the Commonwealth Economic Council (Vol. 9 No. 2 - May 1957) confirmed the view that it was unlikely that production in the A.O.T's could be expanded sufficiently to meet the Community's requirements. These representatives stressed the point that, in 1953 the A.O.T's had produced about 12,000 tons of tobacco, as compared with a production of about 10,000 tons twenty years ago; in that time, production had therefore only increased by 20 per cent, which was virtually negligible, both in terms of absolute and relative value. A rapid development also in the future was moreover unlikely, because of limiting factors such as the amount of capital available for investment, and also labour, particularly in the Belgian Congo, where the density of population was very low.

49. With regard to the different types of tobacco, these representatives observed that at least two of the varieties consumed in the Community countries were not produced in the A.O.T's. The first type - Oriental tobaccos - required such ecological and other (especially soil) conditions that it was impossible to expect that production would expand to any appreciable degree. Moreover, because of their special taste features, these tobaccos cannot be replaced by other varieties, and no increase in imports of this type can therefore be expected. In Germany, which is the principal importer of Oriental tobaccos (25,000 tons out of a total of 44,000 tons), the average price paid is DM 6 per kg. The common tariff duty which has been established by the Treaty at 30 per cent, will therefore amount to DM 1.80, which exactly corresponds to the present specific duty of DM 1.80 levied on tobacco imported into Germany. The second type - cigar-leaf tobacco - is not produced in any notable quantities in the overseas territories, with the exception of a very small production in the Cameroons, and the Community's present requirements are about 30,000 tons per annum. It is difficult to see how in future years the A.O.T's could develop production, since it is specialized and requires skilled labour and
certain established techniques, not to mention the capital required for planting on a large scale. Production in the Belgian Congo is very limited and there are no indications that it is developing to any extent.

50. It was not impossible that production of certain types of tobacco might develop in some of the associated territories, but experience has shown that there would be many difficulties and that even if any such development was undertaken, it would only yield results very slowly. The representatives of the Six recognized that in the case of Rhodesia successful results had been achieved, but pointed out that many other countries which had similar conditions of soil and climate were nevertheless not tobacco producers. They pointed out that for a long time past, the indigenous inhabitants in Africa had been producing small quantities of tobacco of rather mediocre quality in their fields and around their villages; efforts had been made to improve the quality of this tobacco and to encourage the producers to extend their plantings, but such efforts had met with many difficulties as could be seen from the production statistics. The representatives again emphasized that tobacco for export required special attention as well as certain installations, such as dryers, which, however modest in some cases; nevertheless represented a not inconsiderable investment on the part of these populations whose standard of living was still very low.
B. Effects on Trade of Third Countries

(i) Effects of New Tariff Regime on Trade Patterns

51. Representatives of the tobacco producing countries other than the Six considered that the change in market preferences arising from the discriminatory tariff would begin by the end of the first stage of the transitional period to divert purchases within the Six from third country suppliers to the tobacco of the A.O.T's. The preferential margin in the tariff in favour of A.O.T's would then vary between 6 per cent and 9 per cent. This diversion of trade would increase rapidly as the discriminatory element in the tariff increased and production in the A.O.T's rose. The effect would be most immediate on the dark-fired tobacco exported by third countries, e.g. the United States and Rhodesia and Nyasaland, since a similar type of tobacco to that which has already displaced United States dark-fire cured in France is already produced in the A.O.T's. The exports of third countries to the Six of that type of tobacco could disappear completely within a few years. Thereafter, the flue-cured tobacco imports from non-Community countries would be increasingly displaced by air-cured and other types of tobacco from the A.O.T's.

52. Markets for cigarette tobacco from third countries would be progressively reduced. The production in the A.O.T's, artificially stimulated by the preferential duty, could well reach 40,000 tons of cigarette tobacco and 20,000 tons of cigar tobacco by the end of the transition period. Demand for tobacco from third countries would thus be reduced by some 60,000 tons below what it would otherwise have been. This process could continue in the more distant future so that although third country suppliers of cigarette tobacco are not likely to be totally excluded from the markets of the Six, their share of that market will be steadily reduced in favour of the preferred A.O.T producers. This would affect all types of tobacco, but the high priced flue-cured and oriental tobaccos would be particularly affected among cigarette tobaccos. Similarly the cigar-leaf tobacco market would be sharply influenced. This would
be the position even if demand in the Community were to increase, though such increases were by no means certain. Third country suppliers would not in these circumstances enjoy any appreciable share of such increases as might occur. This would be particularly serious for countries such as the Federation of Rhodesia and Nyasaland and the Dominican Republic which have been relying on an increasing market within the Six to provide an outlet for their increased production.

53. Outside producers would thus tend to be reduced to the position of residual suppliers to the Six, only supplying such part of the demand as could not be met by the A.O.T's and from within the Common Market area. This would be particularly important in any period of general recession. At such a time the agricultural provisions of the Treaty could be used (paragraph 32 below) to support the prices paid to A.O.T. producers and cause an absolute priority for their production in the markets of the Six.

54. As previously mentioned in paragraph 26, the relatively small cigar leaf tobacco market would suffer even more heavily than in the case of cigarette leaf and imports into the Six from non-Community countries might virtually disappear by the end of the transition period.

55. The representatives of the Six stated that, in order to make an accurate assessment of the effects of a 30 per cent duty on the trade of third countries, it was necessary to know what effect such a duty would have on prices; moreover, a 30 per cent duty could not be considered as being higher than the average of the duties at present applied in the various countries of the Community. They added that there was nothing to indicate that the present pattern of trade would be modified to any appreciable degree in the near future, and stressed once more that consumption in the European countries would increase in coming years, thus creating new outlets. They also pointed out that the A.O.T's which were not tobacco producers represented an expanding market.

56. These representatives also drew attention to the fact that, on the assumption that the quantities at present produced in the
A.O.T's would increase sufficiently to affect trade, it was in any case in the interest of those territories, as well as of other producers, to avoid any action which might have a depressing effect on prices. They added that before there could be any diversion of the present pattern of trade to the benefit of the A.O.T's, those territories would have to be in a position to offer purchasers in importing countries those qualities and quantities of tobacco which they required. There was nothing to indicate that the A.O.T's would be able to meet even part of the requirements of the Community for a very long time to come.

(ii) Effects on World Prices

57. Representatives of non-Six producers agreed that the reduced demand for tobacco in the Community as a result of the 30 per cent duty and the artificially stimulated production in the A.O.T's would tend to depress world prices - the effect varying with the different types of tobacco. For cigar leaf producers, since the Six are an important part of the whole world market in their tobaccos, the effect could be particularly serious - perhaps leading to a major decline in world prices for these tobaccos. For oriental and other cigarette tobaccos there could also be substantial adverse effects on the world prices from the additional quantities of tobacco produced in the A.O.T's. It is realized, however, that as far as cigarette tobacco production in the A.O.T's is concerned the effect is likely to be gradual.

58. $\frac{Reply of the Six to be inserted}{/}$

II. Quantitative Restrictions and Agricultural Provisions of the Treaty

59. Representatives of the tobacco producing countries other than the Six considered that the application of quantitative restrictions or of the agricultural provisions of the Rome Treaty could be particularly serious in the case of tobacco. As noted in the General Report, these provisions of the Treaty could be used in various ways to give substantial non-tariff preferences to the
tobacco production of the A.O.T's. If the demand for the types of tobacco produced in the A.O.T's failed to rise in the Community as rapidly as production there, these provisions could be used to ensure a diversion of consumer demand to those varieties of tobacco. Similarly, if demand for tobacco were to fall substantially the provisions could be used to ensure a market at sustained prices in the Six for the whole tobacco production of the A.O.T's. The adverse effects of the depressed prices would then be wholly borne by third country tobacco producers.

60. They also stated that a monopoly system was at present applied by France and Italy to tobacco from all sources. Under the Treaty of Rome the monopoly system might be extended to the other members of the Community. In view of the financial importance of these monopolies in France and Italy in raising revenue, there appeared to be little likelihood that they would be dissolved, and if this was the case, then the only practical alternative when the Treaty was in full effect would seem to be for all Six countries to have a unified monopoly system. This could be used to give the tobacco production of the A.O.T's and from within the Six themselves a non-tariff preference in their markets, and this could not fail to worsen the position of third parties in respect of their exports of tobacco.

61. The representatives of the Six replied that the State monopoly was operated in such a way as to yield the maximum fiscal effect. If therefore the State, which operated the monopoly, had itself to pay duty, the total fiscal burden of the consumer could no be altered. Furthermore, they drew attention to the fact that Article 37 requires the Member States to adjust their monopoly system in such a manner as to remove all discrimination between their nationals. If this stipulation was read together with the other provision contained in the same Article, namely that the obligations incumbent on Member States shall be binding only to such extent as they are compatible with existing international agreements, it seemed to them that the future development could not lead to an intensification of the existing system but would tend rather towards a relaxation.
62. These representatives also stated that any extension of the French and Italian monopoly systems to the whole Community was unlikely, though it was a possibility permitted under the Treaty; but in any case, if such a system acted as a stimulus to production, as assumed by some governments, the question arose as to why the development of tobacco production had been so slow in territories such as Madagascar since the end of the 1914-18 war, in spite of the existence of the French tobacco monopoly.

III. Summary of Views of Tobacco Producers other than the Six

63. The representatives of tobacco producing countries other than Six, after examining the arguments of the Six, maintained their view that the creation of a new preferential system at a tariff margin of 30 per cent on behalf of the production of the A.O.T's throughout the large tobacco market of the Six must have serious consequences for the trade of other tobacco producers. For the reasons already stated they considered that the preference must cause substantial diversions of trade in the markets of the Six in favour of the A.O.T's supplies and that the assurance of preferential treatment throughout the markets of the Six must artificially stimulate production of many types of tobacco within the A.O.T's (where production is at present relatively small) to a very substantial degree.

64. In the short term they considered that by the end of the first period of five years, the effects of increased production in the A.O.T's would begin to be increasingly felt on the markets of the Six, and the impact on third countries would be more pronounced by the development of production within the Common Market itself following the establishment of the common tariff and by the preferential arrangement for the A.O.T's.

65. These representatives said that in the A.O.T's every encouragement would be given to the development of tobacco production by peasant farmers, while in contrast it would be necessary in third countries to take immediate steps to adjust development plans now in hand. Those third countries included many which were under-developed contracting parties to GATT and to which
the prospects of increased tobacco sales were vitally important. Even by the end of this comparatively short period, prices of tobacco on the world markets would show a decline.

66. The representatives of the Six replied that those views did not take into account the growing needs of the Community which, according to reasonable estimates, would rise from 300,000 tons in 1956 to about 375,000 in 1965 - an increase of 75,000 tons - nor did they take account of the actual production possibilities in the associated territories. They reminded the representatives of the non-Six producers that, although tobacco trade had been protected by the French State Monopoly, and in spite of the great efforts which had been made to increase production of this very profitable crop, tobacco production had nevertheless remained at the same level for the last twenty years; even assuming that this production might increase two - or even three-fold - though such an assumption was contradicted by past experience - the growing needs of the Community would still be far above what the territories could produce. It would therefore be necessary to import from third countries even more than today. The representatives of the Six also pointed out that from 1948 to 1956, i.e. for a period of almost ten years, tobacco production in a country such as Rhodesia seemed to have reached a maximum level; it was difficult to compare the position of Rhodesia with that of the associated territories since in that country most, if not all, of the tobacco produced was grown on plantations owned by Europeans, but nevertheless this example seemed to indicate that production possibilities were not inexhaustible. These representatives also said that they could not see how, with these reasonable estimates for a larger market, tobacco prices could fall; they emphasized, as on other occasions, that if any such price falls were to occur, they would have the same effects on producers in the associated territories as on those in producing countries which were not members of the Community.

67. In the long term, representatives of the non-Six tobacco producers feared that the dislocation of patterns of trade would be serious. It could be expected that cigar-leaf tobacco exports
from non-Six countries which were contracting parties to GATT would be irrevocably damaged, as the present quantity imported from them—about 28,000 tons—was not large in relation to the production potential of the A.O.T's, having regard to the relatively small acreage needed. With regard to other types of tobacco, while it was not foreseen that the present imports from non-Community countries could be entirely replaced in the near future by increased production in the A.O.T's, nonetheless the increase that would take place would have serious repercussions. Current total imports of cigarette and other types of tobacco into the Six were roughly of the order of 140,000 metric tons per annum, and even if the A.O.T's increased their production to replace only one-quarter of this market, this could completely alter the economy of the tobacco export trade because of its depressing influence on world prices. There appeared to be no reason why, in the very long run, after the end of the transitional period, the proportion supplied by the A.O.T's could not rise still further.

68. Tobacco producers in third countries would be in a particularly vulnerable position as they already relied to a large extent on tobacco as an important cash crop. In their case a depressed world market would tend not simply to prevent expansion, but force them to reduce production, with a corresponding adverse effect on their standard of living, while at the same time A.O.T. producers, having the benefit of the 30 per cent preference, would be induced to expand their production. If the latter producers were also to be protected by monopoly control, as seemed highly probable in view of the existing State monopolies in France and Italy, the effects would be still more serious. Even a much higher level of efficiency by non-Community producers would not enable them to compete in the Common Market. Contracting parties to GATT who were particularly liable to be affected included the Dominican Republic, Cuba, the Federation of Rhodesia and Nyasaland, Indonesia, India, the United States, Turkey and Greece. Some other countries, such as Canada, who have a small but rapidly growing export trade in tobacco with the Six are also likely to be affected.
69. With reference to the probable long-term effects of the Treaty, i.e. after 1965, the representatives of the Six considered that it would be risky to make forecasts for any period later than 1965, but said that in any case there was no cause for predicting that there would be a drop in consumption or a disruption of trade. That seemed to them to be a pessimistic view which was contradicted by the prospects of expansion that were held out by the Treaty. The representatives of the Six reminded the representatives of the non-Six producers that at present the French dependent overseas territories exported only about 700 tons per annum of cigar leaf tobacco, and that there were no exports from the Belgian Congo; before it could meet the Community's requirements, present production would have to increase thirty-fold. It could be seen from instances where there had been a spectacular increase in production, such as Rhodesia, for example, that it was difficult to do more than treble production over a period of twenty years. This example, which was valid in the case of cigar-leaf tobacco, was also applicable to the other types of tobacco imported by the Community countries and which amounted to more than 140,000 tons. In these circumstances, it was hard to see why third countries should be obliged to reduce their production, or how the world market could suffer a depression as a result of the small quantities of tobacco which the Associated Territories might eventually produce at some future time. The representatives of the Six also pointed out once more that any drop in prices on world markets would also be felt by producers in the Associated Territories, and that therefore it was in the interest of the latter as well as of producers in third countries to avoid such fluctuations.