Introduction

1. The consultation with the United Kingdom had been initiated by the United Kingdom Government in March 1956 in accordance with the provisions of paragraph 1(g) of Article XIV, and was concerned with its continued resort to the provisions of Annex J for the application of discriminatory import restrictions. In conducting this consultation the Working Party broadly followed the plan recommended by the CONTRACTING PARTIES for such consultations. The following notes set out the main points of the discussion.

Basis and background for the application of discrimination

2. In opening the consultation, the United Kingdom representative recalled the previous consultation in 1955 when attention had been called to the deterioration in 1954/55 in the United Kingdom current balance of payments. This had forced the United Kingdom to slow down the rapid rate at which restrictions were being relaxed and discrimination removed in the course of 1954. It had been noted that this process had not come to a complete stop, and that some progress was still being made towards freer trade. The Working Party conducting that consultation had expressed gratification that in spite of balance-of-payments difficulties then faced by the United Kingdom, import restrictions had not been invoked as a means of overcoming them. In 1955/56 events had taken a somewhat similar course.

3. The second half of 1955 had seen a further deterioration in the United Kingdom current account balance. Even allowing for the fact that the second half of the year was always seasonably unfavourable to the United Kingdom, the decline was evident from the following figures:

<table>
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<th>Current Account Balance including Aid Items (in £ millions)</th>
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<td>1954 Jan.- June</td>
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<td>1954 Jul.- Dec.</td>
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<td>1955 Jan.- June</td>
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<td>1955 July- Dec.</td>
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During the last eighteen months the gold and dollar reserves of the United Kingdom had fallen substantially. After a rise from $2,518 million at the beginning of 1954 to $3,017 million by the middle of that year, they had declined to $2,120 million by the end of 1955.

Spec/196/56
4. In 1955, the United Kingdom Government had taken a number of measures to relieve the pressure of internal demand and to strengthen the balance-of-payments; these included rises in the Bank Rate, checks to hire purchase, reduction in bank advances and finally a supplementary Budget involving increases in the purchase tax and the tax on distributed profits. Steps had also been taken to curb the capital expenditure of local authorities, nationalized industries and the central Government. A full account of the measures taken was given in the background paper of 16 February 1956, supplied by the Fund. Further measures taken in 1956, as outlined in the Fund paper of 12 October, included the raising of the Bank Rate to 5 1/2 per cent, suspension of investment allowances, the restriction of hire purchase, the curtailment of capital expenditure and the reduction of subsidies on bread and milk. The Budget introduced in April had been particularly designed to encourage savings.

5. Although this was not entirely surprising, since old weapons were being tried out in new conditions, the restrictive measures taken by the United Kingdom Government over the past eighteen months had been disappointingly slow in having sufficient effect. There was now welcome evidence that they were exerting noticeable restraint on the economy and affecting the balance of payments. From the appended table which shows the regional balance of payments of the United Kingdom from 1953 to June 1956, it might be seen that there had been a substantial improvement in the first half of 1956. It must be remembered, however, that the first half of the year was seasonably favourable to the United Kingdom, and that of the total surplus of £144 million, only £95 million were added to the United Kingdom gold and dollar reserves. The surplus for the whole year would almost certainly be below that rate, which was itself inadequate, having regard to the need to replace the reserves which were still exceedingly low. The policy of the Government was to consolidate each move forward before beginning the next. Had the Government seized upon the favourable developments of the first half of 1956 to make a big move forward in the removal of restrictions and discrimination, it might have been forced by the subsequent events to have taken retrogressive steps. In the last few months sterling had been again under some pressure, and in the third quarter the United Kingdom gold and dollar reserves had declined by £20 million. The current account balance had fluctuated considerably in the last eighteen months, and the Government had to be on guard against taking action on too short a view; close watch must be kept, for instance, on the impact of the unfolding of events in the Middle East.

6. Consequently despite the improvement in its current account balances in the first half of the year, the United Kingdom had considered itself unable to risk any significant additional calls upon its reserves. It would, in the United Kingdom's view, have been a mistake further to liberalize imports while restraining demand by the various internal measures described above. Reducing discrimination by intensifying restrictions on imports from the non-dollar countries, even if this could be done consistently with the United Kingdom's obligations, would hardly be an acceptable way of proceeding. The alternative way, namely to liberalize dollar imports, could not be followed for the reasons given above.

7. The United Kingdom representative then referred to the decision which, in spite of the situation, his Government had taken in July 1956, to free imports of pulp, paper and board. This had been done in such a way as not to increase discrimination against dollar imports. In addition, with the ending of state
trading on 1 October 1956, the Government had placed bacon and pork on open individual licence from most of the non-dollar countries. With effect from 1 January 1956 sulphur had been placed on open general licence. Other relaxations had taken place towards the end of 1955.

8. In summing up the basis and background for the continued application of discrimination, the United Kingdom representative said that the underlying economic position was sound, and stressed his Government’s resolution to maintain it so. The internal fiscal and monetary measures taken in the last eighteen months were now creating noticeable restraints on the domestic economy and on the balance of payments. On the other hand, the United Kingdom had not achieved a current account surplus which could be considered adequate or raised its reserves to a level which could be considered sufficient. It had to guard against the danger of moving forward at the first signs of improvement and so risking having to move back later. For these reasons the United Kingdom had not felt justified in making further significant moves in liberalizing imports, and so in reducing discrimination. It would move forward, however, as soon as the balance of payments permitted.

Consultation with the International Monetary Fund

9. Pursuant to the provisions of Article XV:2, the CONTRACTING PARTIES had invited the International Monetary Fund to consult with them concerning this consultation. As a part of the consultation between the CONTRACTING PARTIES and the Fund, the latter had supplied a substantial amount of documentation including (a) a background paper prepared in the Fund in connexion with the Fund’s 1955 consultation with the United Kingdom, and (b) a supplementary paper dealing with developments in the United Kingdom since October 1955, which had been specially prepared by the Fund for the assistance of the CONTRACTING PARTIES. In addition, the Fund had supplied the following text of the Decision taken by its Executive Board at the conclusion of its 1955 consultations with the United Kingdom on 21 March 1956.

"1. The Government of the United Kingdom has consulted the Fund under Article XIV, Section 4, of the Fund agreement concerning the further retention of its transitional arrangements.

"2. United Kingdom production continued to rise in 1955 in all sectors except coal and textiles. A rise in fixed investment, public and private, together with a continued moderate increase in consumption and a rise in stocks accompanying the expansion of production, led to pressure on resources. There was some further advance in wages and prices. Exports rose but there was a larger increase in imports, e.g., of coal and other raw materials, and a decline in net invisible receipts. The payments deficit with non-sterling areas increased, and there was a substantial fall in the gold and dollar reserves.

"3. During 1955 and 1956 credit policy has been tightened and budgetary and other measures have been taken to restrain consumption and moderate the rise in public and private investment. The Fund welcomes these steps and the intention of the United Kingdom
authorities to take, if necessary, further measures to reduce the strain on resources and, thereby, strengthen the payments position.

"4. The Fund also welcomes the United Kingdom's policy of meeting its difficulties through other measures than by reimposing restrictions on trade and payments. Some progress was made in removing restrictions and reducing discrimination, although the pace of relaxation was slower in 1955 than in 1954. The Fund believes that the United Kingdom should continue to follow policies designed to make possible further advances toward freer trade and payments, particularly in view of the key role of sterling in the general approach to convertibility.

"5. The United Kingdom has made considerable progress in widening the transferability of sterling and in reducing reliance on bilateral arrangements. The financial reasons for the use of bilateral arrangements by other countries have thus been reduced. The Fund attaches especial importance to the efforts made by the United Kingdom to reduce bilateral practices.

"6. In concluding the 1955 consultations, the Fund has no other comments to make on the transitional arrangements maintained by the United Kingdom."

10. The representative of the Fund stated that although the Decision has been taken some several months ago, the Fund had not considered it necessary to make any modifications to it at this time. The Fund's present position in regard to the United Kingdom remained as outlined in that document.

Questions relating to the policy of discrimination

11. A member of the Working Party enquired whether the increase in United Kingdom's exports to the dollar area during the first half of 1956 was in any way related to the recent reduction in discrimination against dollar goods in many countries. The United Kingdom representative considered that while possibly keener competition in EPU markets might have compelled United Kingdom exporters to pay more attention to the North American market, the principal reason for the increase in exports to the dollar area was the success of Northern American countries in maintaining a high level of economic activity.

12. The Working Party discussed the possible effects of the restrictions which were discriminatory in favour of EPU countries and against the dollar area, on the gold and the dollar reserves of the United Kingdom. A member of the Working Party suggested that as the United Kingdom was making substantial gold and dollar payments to the EPU in settlement of its deficits with EPU countries a reduction in discrimination, by reducing the United Kingdom's deficit with EPU countries, might help to reduce the drain on its gold and dollar reserves. The United Kingdom representative replied that while any reduction in imports from the EPU countries would undoubtedly reduce the country's EPU deficits, the corresponding increase in the imports from the dollar area would bring a greater drain on its reserves; whereas EPU deficits were settled only to the extent of 75 per cent in gold and dollars, deficits with the dollar area were charged 100 per cent to the gold and dollar reserves. Another member of the Working Party
considered, however, that the relative effects of the discriminatory restrictions on dollar and EPU imports could not be so simply regarded, as a number of other factors had also to be taken into account. For example, imports diverted from EPU to dollar sources would presumably be at lower prices and to that extent a lesser charge would be made to the dollar reserves; secondly, the accumulated deficit to EPU resulting from the 25 per cent credit payment carried an interest which was by no means insignificant; and thirdly, the payment of 25 per cent in credit simply meant a deferral of real payment as the accumulated balance had to be settled eventually. The United Kingdom representative agreed to the validity of these considerations, which had, of course, not been ignored by his Government.

13. A member of the Working Party observed that in spite of the reduction in restrictions on dollar goods, there had been no substantial diversion of imports to that source, and that the increased competition arising from the liberalization of dollar imports should have a salutary effect on the efficiency and competitive strength of the United Kingdom producers. The United Kingdom representative commented that it might not always be legitimate to relate directly any changes in imports to changes in the restrictions, as there were many more determining factors. For example, the sustained high level of activity in North America must have contributed to lessening pressures on European markets, including that of the United Kingdom. His Government recognized the advantages that domestic industries might derive from external competition, and would be ready to submit the economy to that test as the balance-of-payments position permitted.

14. The United Kingdom representative was invited to comment on the view that, having regard to the importance of sterling as an international currency, its increased transferability had been beneficial not only to sterling area countries, but to all countries outside the dollar area; the present high degree of transferability of sterling had laid the ground on which further progress towards convertibility of the major currencies of the world could be achieved.

The United Kingdom representative stated that the United Kingdom Government was always conscious of its responsibility in regard to sterling. Over 50 per cent of world trade was carried on in sterling, and his Government’s policy was directed towards furthering the use of sterling in international payments and encouraging multilateral trade by all possible means. In this connexion he would refer to a recent statement of the Chancellor of the Exchequer to the effect that in achieving a healthy economy, all countries must have regard to the impact of their policies on other countries, since prosperity is indivisible.

15. A member of the Working Party noted that certain people were of the opinion that with the reduction in dollar restrictions in many countries, the free flow of dollar goods, and at any rate of goods with dollar components, between them appeared to have substantially reduced the value of stringent restrictions on dollar imports maintained in any particular country. On this point the United Kingdom representative said that the desirability of keeping progress in the liberalization of dollar imports in phase has been considered by some countries, but the conclusion had been that no special action was necessary. In practice, the possibility of dollar goods imported by one country being diverted to another country was not a great one, since the price differences would seldom be sufficiently large to cover the extra costs in transport and handling. If there should be any evidence in future that dollar import controls were being undermined, the United Kingdom Government would have to review the situation.
In reply to a further question about relative cost of supporting the transferable rate, as compared with the cost of reducing discrimination, the United Kingdom representative said that it could be accepted that claims of all kinds on the gold and dollar reserves, including the cost of supporting the rate, would not, in the United Kingdom's view, be reduced by a reduction of discrimination; otherwise the United Kingdom would already have taken this step.

Reduction of discrimination in the restrictions

16. For a detailed description of the system of discriminatory restrictions and of the changes which took place in the past year, the United Kingdom representative referred to the reply of his Government to the questionnaire issued by the CONTRACTING PARTIES in connexion with the preparation of the Seventh Annual Report on the Discriminatory Application of Import Restrictions. Among the main changes which were relevant for the present consultation should be mentioned the addition of pulp paper and board to the World Open General Licence in July 1956. At present only one-sixth of the United Kingdom's imports remained subject to control, and more than half of its imports from the United States and Canada had been freed from restriction. There had been no reduction in quotas or any unfavourable changes in the criteria used in licensing imports remaining subject to administrative control. Full account was taken of the price factor in deciding on the sources of supply. The possibility that competition from the dollar area might have a restraining influence on prices was one of the factors which led the United Kingdom when liberalizing pulp, paper and board to put these items on World Open General Licence. Some members of the Working Party expressed gratification at the progress achieved in the circumstances. It was noted that though the measures taken in July had not resulted in a substantial increase in imports from the dollar area, they had exerted a psychological effect on North American exporters by reassuring them that the United Kingdom was resolved to progress in the direction of freer imports.

It was suggested that similar action could be taken in regard to other items which were, for example, sufficiently covered by customs tariffs, and the liberalization of which would therefore not be likely to involve increased charges on the balance of payments. The United Kingdom representative observed that other items undoubtedly existed which could be liberalized at little or no cost to the balance of payments. At this juncture, however, it was politically and psychologically unwise further to expose the economy to potential burdens when the Government were putting into force numerous measures which were unfavourable to various sections of the population, but whose success depended on their full support. In addition, it could never be absolutely certain that the balance of payments would not be affected by the liberalization of even such items. Certain members of the Working Party said that while they fully realized the weight of these considerations, they hoped that the United Kingdom Government would give the fullest consideration to any possibility of further liberalization and reduction of discrimination. The momentum which had been built up in recent years in reducing restriction and discrimination had been of great value to the world, and should be maintained if at all possible. In taking a conservative outlook, the Government might well be under-estimating the breadth of understanding of the public in problems of international economic relationship. There were many ways of experimenting with liberalization with varying degrees of risks in regard to the balance of payments, and it was hoped that further action would be taken consistent with safety, so that the reaction of the public
could be gauged. In reply the United Kingdom representative said that in taking the various steps in the past year, to which reference had been made, his Government had had in mind considerations of this kind. For the future he could say no more than that they would continue to bear them in mind.

Multilateral and bilateral payments and trade agreements

17. The United Kingdom representative referred to the multipartner payments arrangements which had been developed in the past year between Brazil and Argentina on one hand, and certain European countries, including the United Kingdom, on the other, and assured the Working Party that neither of these arrangements involved any discrimination in favour of the two Latin-American countries. As for the bilateral trade agreements described in the background paper supplied by the Fund, the United Kingdom representative stated that none of them involved any obligation for the United Kingdom other than to issue licences; whether imports into the United Kingdom from the partner countries would expand as a result of such agreements entirely depended on the ability of their exporters to compete with other suppliers on the United Kingdom market. Further, as liberalization of imports was further pursued, the area of trade which could be covered by bilateral arrangements became progressively limited. At present only 2.5 per cent of the United Kingdom's imports from OEEC countries was covered by bilateral quota arrangements.

18. In reply to a question on the basic policy of the United Kingdom Government in regard to the use of bilateral trade agreements, the United Kingdom representative stated that it was the long-term policy of his Government to eliminate import restrictions and discrimination. With the progressive achievement of that aim, the scope for bilateral arrangements would, of course, become increasingly less and ultimately disappear, and consequently there was no need for a deliberate policy of eliminating bilateral arrangements which had a historical origin and served a useful, although limited, purpose. In the context of the present discussion the question was whether, in effect, these agreements resulted in discrimination; insofar as such agreements were used for purposes other than to assure a more favourable treatment to the exports of any particular country, they could not give rise to discrimination.

Effects of the discriminatory restrictions

19. The United Kingdom representative assured the Working Party that his Government was doing its best to minimize any undesirable effects of the restrictions still being maintained. It was ready to discuss with any contracting party problems arising from the restrictions. Certain members of the Working Party observed that the most important means of preventing damage to the interest of other contracting parties was to refrain from taking retrogressive steps in regard to newly liberalized imports. They therefore welcomed the consistent policy of the United Kingdom in this regard. The United Kingdom representative expressed appreciation of this support for his Government's cautious policy of consolidating each move forward before attempting the next.
20. Members of the Working Party noted that the most remarkable development in recent years had been the tendency for countries faced with balance-of-payments difficulties to put more emphasis on the use of internal fiscal and monetary means than on import restrictions for the correction of internal and external disequilibrium, and that the policy pursued by the United Kingdom was a case in point. It was hoped that the United Kingdom would be able to contribute further to maintaining the momentum of the progress towards freer trade. In particular it was hoped that action would be more and more related to imports from all countries.

21. In conclusion the United Kingdom representative assured the Working Party that his Government would persevere in its endeavours to promote freer and more multilateral trade. He would recall, however, the statement made by the Chancellor of the Exchequer at the recent meeting of the International Monetary Fund that governments today were rightly pledged to policies of full employment and a high level of economic activity, and that they could not therefore carry their monetary and fiscal policies to the point of outright deflation. It would not be right to think that internal policies were the only answer. In the United Kingdom's view prosperity was a common responsibility, and countries in strong creditor positions - of which there were now a number - should frame their external policies having regard to the effect of their strength on other, weaker, countries.