1. In accordance with its terms of reference, the Committee has conducted the consultation with Finland under Article XII:4(b). The Committee had before it a basic document for the consultation (BOP/86), and documentation supplied by the International Monetary Fund.

2. In conducting the consultation the Committee followed the plan for such consultations recommended by the CONTRACTING PARTIES (BISD, Seventh Supplement, pages 97-98). The consultation was completed on 4 November 1968. This report summarizes the main points of the discussions.

Consultation with the International Monetary Fund

3. Pursuant to the provisions of Article XV of the General Agreement, the CONTRACTING PARTIES had invited the International Monetary Fund to consult with them in connexion with this consultation with Finland. In accordance with the customary procedure the representative of the Fund was invited to make a statement supplementing the Fund's documentation concerning the position of Finland. The statement made was as follows:

"The Fund invites the attention of the CONTRACTING PARTIES to the Executive Board decision of June 28, 1968 taken at the conclusion of its most recent Article XIV consultation with Finland, and particularly to paragraphs 2, 3, 4, and 5 which read as follows:

'2. Affected by restrictive domestic financial policies and by sluggish demand conditions in Western Europe, the gross domestic product rose, in real terms, by 2.3 per cent in 1967, approximately the same as a year earlier. Unemployment rose sharply, especially toward the end of the year. There was a slight decline in real gross fixed investment. The volume of
exports of goods and services rose by 4.4 per cent, with all of the increase in commodity export going to those countries with which Finland trades on a bilateral basis. The volume of imports of goods and services declined by 1 per cent. The deficit on the current account of the balance of payments was, thus reduced from $207 million in 1966 to $163 million. At the same time there was an increase in long-term capital inflow. The heavy reserve losses of the preceding years were replaced by a decline of $5 million in 1967, but this was accompanied by substantial use of Fund resources. In the first five months of 1968 reserves rose by $115 million.

'3. On October 12, 1967 the Finnish markka was devalued by 23.8 per cent and a special temporary tax was imposed on most exports. Government expenditure is being kept under strict control and it is estimated that the cash budget (including the proceeds of the export levy) will show a surplus in the calendar year 1968 of about Fmk 400 million compared with a deficit of about Fmk 100 million in 1967. In view of the withdrawal of liquidity resulting from the government surplus, monetary policy in 1968 aims at supplying additional liquidity to the economy on a selective basis. The budgetary restraint and the easing of monetary conditions in 1968 will facilitate the needed shift in resources. The Fund believes it important however that liquidity should be supplied to the economy in such a manner that monetary policy can play an effective role in offsetting deterioration in the budget accounts when the export levy is reduced in 1969.

'4. The Government has placed particular emphasis on the need to moderate the growth of costs and prices. Agreement has been reached on (a) the elimination of the clause contained in the current wage agreement providing for index compensation at the end of 1968 and the limitation of increases in hourly wages in 1969 to a flat sum estimated to raise the wage bill by 3.5 per cent; (b) a smaller increase in agricultural prices in the crop year 1968/69 than provided for under current legislation. In April 1968 Parliament passed a Law to Safeguard Economic Progress in the years 1968/69 empowering the
Government to control prices, rents, and wages and abolishing price index linkages in rent and wage agreements and most financial contracts. The Fund welcomes these measures which taken as a whole should facilitate further growth and strengthen the external payments position.

5. The Fund notes with satisfaction that Finland has continued to make progress in the liberalization of trade and payments notwithstanding the payments difficulties of recent years. Effective January 1, 1968, all quotas on industrial imports from countries in the multilateral area were eliminated. The exchange regulations concerning current invisibles and capital transactions were also substantially changed and liberalized. Moreover, the one remaining payments agreement with a Fund member was eliminated.

"Official reserves at the end of September 1968 amounted to $326.9 million, $122.9 million more than at the end of September 1967 but still below their level at the end of 1964. At $326.9 million official reserves were equivalent to about 2½ months payments for imports in 1967."

"At the present time, the general level of restrictions of Finland which are under reference does not go beyond the extent necessary to achieve a reasonable rate of increase in its reserves."

Opening statement by the representative of Finland

4. In his opening statement, the full text of which is contained in an Annex, the representative of Finland described the major developments in Finland since the last consultation, beginning with a summary of transitional measures which followed the 1967 devaluation. With respect to the special export levy, which was one of those measures, he explained the way in which the proceeds of the tax were being used to promote basic investments in infrastructure. Turning to the problem of introducing an incomes policy which might help to place the economy on a sounder basis, he explained that after lengthy negotiations a comprehensive agreement had been reached on prices and incomes. As of March 1968, the index clauses which wage contracts had contained were removed, and from the beginning
of 1969 wage increases were to be kept in line with expected increases in productivity. Implementation of these agreements involved abolishing other index linkages and introducing powers to supervise and control prices and rents as well as wages. The Stabilization Act, incorporating these and various other changes, would be effective until the beginning of 1970 and there was to be no automatic reintroduction of index clauses at that time. Conceding that it might be too early to judge the overall effects of the devaluation and stabilization effort, the representative of Finland noted that price developments had become much more stable. Less encouraging had been the development of production, employment and private consumption expenditure. The Government was obliged under the stabilization agreement not to introduce tax increases and to hold borrowing to its previous level, but increased private investment was expected to have favourable effects on production; with good export prospects, the Government hoped that growth would soon be resumed. Turning to the balance-of-payments situation, the Committee was told of the encouraging development of Finland's current account, which may show a small surplus for the first time in ten years owing in part to expanded earnings from exports accompanied by a low level of imports. In the capital account, net long-term capital imports in the first half of 1968 amounted to Fmk 170 million, mainly in the form of medium-term financial loans. Short-term commercial credits had increased substantially after the rule requiring cash payment for certain imports was abolished. The position with respect to foreign-exchange reserves had greatly improved, largely reflecting the short-term capital inflow. Some continuing capital inflow was expected, but no more than enough to cover amortization of current debt and repayment of drawings which Finland had made from the IMF. Liberalization of foreign trade had proceeded, meantime, with two fifths of Finland's Kennedy Round concessions in tariffs becoming effective on 1 July 1968 and abolition of duties on EFTA goods on the "décalage" list from the beginning of the year. Remaining quantitative restrictions on industrial products permitted under the FINEFTA Agreement had been removed and the liberalization extended to all countries under the multilateral import treatment system. Certain quantitative restrictions which had been the
subject of Kennedy Round negotiations were also removed on 1 July 1968 and Finland's last bilateral trade and payments agreement with a convertible currency country had been terminated on 1 January 1968. Finland was far from complacent about the balance-of-payments outlook as reserves were still uncomfortably low, and it was felt that much of the gain achieved in reserves had been at the expense of increased commercial debt which could not be a continuing source of gain. The fact that there had been depressed conditions within the country had undoubtedly helped to build reserves by holding imports down, but this was also a condition which could not continue. Hence, Finland would need to proceed with care, continuing to work on development of her incomes policy, but it was evident that a change in present import policies would not help but only jeopardize the attainment of the objective.

Balance-of-payments position and prospects and alternative measures to restore equilibrium

5. Members of the Committee congratulated the representative of Finland not only for his concise and informative statement on developments in his country over the past year but also for the very substantial improvement in Finland's situation due in no small measure to the courage of the Government in pursuing difficult but beneficial policies. It was especially gratifying that Finland had weathered this crisis without resorting to import policies which could in the long run only have delayed recovery. As it was, the current account surplus now in view was but one evidence of a basically healthy economy well on its way to recovery. They did, however, express some scepticism as to whether the Government of Finland might not now be under-estimating the strength of the country's situation and inquired whether the long-term foreign capital inflow might not be encouraged in some way. It was asked in particular whether thought was being given to various methods by which encouragement might be given to long-term investment from abroad, either on a loan basis or as direct investment, and whether the United States market for capital was being explored.
6. The representative of Finland drew attention to his statement that the expected equilibrium or surplus on current account was not something which Finland could count on as a continuing feature. Even the increase in foreign exchange reserves to which the Fund had referred in its decision would appear smaller if account were taken of the net debt of commercial banks. Net reserves, including such debt, probably would amount to no more than $220 million instead of the $327 million held by the central bank. Even this smaller figure was, to be sure, double the amount held at the beginning of the year, but the largest part of the increase, perhaps over half, would be the result of the reversal in leads and lags, a one-time gain. The figure of $171 million for net long-term capital imports in the first half of 1968 was somewhat above the 1967 figure and it was expected that the level of total borrowings might be matched next year, but requirements for amortization of debt would not leave much net increase. Exports were also expected to increase, but if the domestic economy resumed a reasonable rate of growth, imports would be larger with the result that little, if any, further gain in reserves would come from that source. Efforts were being made to make known to potential investors opportunities available in Finland, where foreign capital enjoyed all the benefits accorded to domestic capital, though no special incentives had been offered which might be regarded as favouring foreign over domestic capital. Opportunities to interest investors in the United States were certainly being sought in this process, along with others.

7. Members also asked how Finland expected to continue to finance the modernization of the wood industry and the development of diversified manufacturing which were an essential part in the solution of Finland's problem of developing a more profitable export trade, once the funds now being collected through the export levy had been used up. Not long ago a report on Finnish problems had suggested that perhaps incentives might be needed to bring together the necessary capital, either from domestic or from foreign sources.
8. In reply, the representative of Finland confirmed that the export levy funds will be used equally for three purposes, i.e. one third for investments in State-owned companies and for investment expenditure of the State railways and the General Direction of Posts and Telegraphs; one third for the development of power production; and one third to increase the opportunities available to the special credit institutions for providing export credit, or investment credit, for small- and medium-sized industries, to grant loans to small-scale industry, and to carry out an intensified forest improvement programme. It followed that Finland would look to private investors to provide the bulk of the capital needs for private industrial development. To that end certain fiscal and financial reforms were under way, in order to stimulate capital formation and ease industrial investment which had, to some extent, been at a disadvantage under the previous system. The new law on the taxation of business income was to become effective on 1 January 1969.

9. Turning to Finland's fiscal and monetary policies, members of the Committee expressed the view that the recovery effected by Finland during the past year offered a striking example of the effectiveness of conservative remedies. The restraint of demand through devaluation had effectively curbed imports; fiscal policies, including the temporary export tax, the restrictions on spending and selective credit policies had induced price stability, and this effect had been given some prospect of continuity by the abolition of linkages, so that gradually one could see business confidence increasing. These strong measures did, however, perhaps pose a problem for the future in the sense that they had involved fairly extensive governmental control of the economy; consequently it would be of interest to hear what thought Finland might be giving to a next stage in which controls could be eased somewhat.

10. The representative of Finland agreed that the export balance had indeed improved, although he emphasized that this had been at the cost, mainly, of a shift in leads and lags of payments, so that the foreign debt had increased in the process. Still, long-term capital had also begun to be more readily available and this was important since the difficulties had been to a large extent associated with insufficient information provided to investors. The sacrifices which the
country had made in terms of slow growth were, moreover, very real, and it was by no means certain that the balance-of-payments problems had been overcome in any permanent sense. The question as to how long it might be before the internal controls on prices and rents might be lifted went, he said, to the heart of the matter, as the key question was how long it would take to create confidence. There was need for more confidence both internally and externally, as well as between government and interested organizations as between Finland and her trade partners. Inside Finland it was understood that at the end of 1969, when the current law expired, there would be need for a new law of its kind and the importance of avoiding the kind of threat which its continuance would present was well understood. The Government was, however, optimistic and hoped that the wage negotiations at the end of the next year would go well.

System and methods of the restrictions and effects of the restrictions

11. Members of the Committee commended the Government of Finland on recent actions in its programme of trade liberalization, especially the elimination of quota restrictions on all but a few industrial products and the elimination of the last bilateral trade and payments agreement with a non-Socialist country, both as of 1 January 1968. They expressed the hope that, in the light of Finland's improved balance-of-payments position, the remaining industrial and agricultural products still subject to global quotas or discretionary licensing will be liberalized. In this connexion, they requested clarification of action taken by Finland on 1 July 1968, liberalizing trade in the agricultural products listed in Annex III to BOP/86, through the issuance perhaps as an Addendum of BOP/86; they enquired whether any of the agricultural products on this list were still subject to global quotas and to discretionary licensing.

12. The representative of Finland confirmed that all the items mentioned in Annex III of BOP/86 had effectively been liberalized in the sense that they are free of licensing; they are thus not included in the global quota programme. The situation as far as the other agricultural products are concerned is clarified in the 1968 publication, "Import System of Finland".
13. Other more specific questions and comments were also made with respect to certain items which appeared still to be under restriction. The representative of Canada stated that nearly all Canadian exports to Finland are now liberalized but that there seemed still to be seasonal restrictions on canned salmon which Canada hoped might be removed. This product had recently been restricted from 1 to 31 January, throughout the month of June and from 1 October through 15 November, and reports reaching the Canadian Government indicated that it was difficult to obtain licences for import at those times, although there was no discrimination, except perhaps with respect to certain border trade. Canada would be interested to learn whether this restriction was justified on balance-of-payments grounds and how long it might be expected to continue.

14. The representative of Australia referred to the problem of non-liberalization of apples during the month of June, even though pears were liberalized at that time, and requested the removal of quota restrictions during that month. He also drew attention to the difficulty posed for distant suppliers by Finland's practice of issuing import licences for meat for short periods of time with insufficient advance notice to permit participation in the trade by Australian suppliers, and requested the provision of a longer period of notice for the issue of such licenses. With respect to apples the question was also asked what was the specific amount of apples licensed in the month of June.

15. The representative of the United States expressed his concern that Finland continued to maintain quotas and in licensing requirements on agricultural products, and raised a question concerning imports of canned fruit and juices, which had reportedly been licensed less liberally in 1968 than in past years. He said that he understood that total imports licensed in these categories were valued at Fmk 7.5 million in 1967, whereas so far in 1968 individual licences with a total value of Fmk 5 million have reportedly been issued. The reduced volume of licensing had been attributed to the "tight foreign exchange situation" in Finland but this situation seemed to have eased. Hence he would appreciate knowing whether the Government of Finland intended to liberalize imports of fresh, canned, and frozen fruit, fruit juices and vegetables for the rest of 1968.
16. On most of these questions the representative of Finland promised to look into the matter and see that replies were made to the countries in question. He believed that increasing consideration was being given to the distant suppliers in the issuance of licences. On the amount of licences issued for fruits and fruit juices he knew of no overall policy decision of the kind suggested but promised to communicate this concern to his Government.

17. Members of the Committee then expressed their special concern with respect to the question of the Finnish motor vehicle tax which they considered to be very heavy and is weighted so as to discourage the purchase of medium- and higher-priced automobiles. On a vehicle from overseas, whose c.i.f. cost is $2,500, the total customs and tax burden amounted to 173 per cent, while on a vehicle whose c.i.f. value is $1,000, the total customs and tax burden was only 133 per cent. Some members noted that this tax had had an increasingly severe effect upon sales of North American automobiles, notwithstanding the fact that the matter had been raised at every balance-of-payments consultation since 1963. They were very disappointed that their past persistent and determined efforts to seek the elimination of the discriminatory impact of this tax had brought forth no satisfactory response from the Government of Finland. They enquired whether now that Finland's balance-of-payments position has improved substantially, the Government would reduce the tax and take steps to eliminate its inordinate impact on medium- and high-price motor vehicles by the elimination of the Fmk 2,500 reduction.

18. The representative of Finland acknowledged that this tax had caused certain countries to express dissatisfaction. He noted that in eight months of 1968, imports of automobiles from Finland's multilateral trade partners had declined by 18 per cent but that the decline in imports from bilateral partners had been even more marked, amounting to 46 per cent. It was apparent that restriction of automotive imports had very important balance-of-payments implications, given the fact that this product had accounted for 4.5 per cent of all imports in 1966 and for 3.7 per cent in 1967. Even with a stiffer tax burden the percentage would still be between 3 and 3.5 per cent in 1968. The figures spoke for themselves concerning the need for some effective restraint on imports. So far
as concerned the arrangement by which the tax bore more heavily on more expensive vehicles, this was a non-discriminatory provision of a fiscal nature applicable to imports from all sources. Between 1963 and 1967 the share of the market economy countries had increased from 87 to 93 per cent and the United States share had gone up from 1.9 to 2.4 per cent. Since then the new EFTA rates have begun to have their effect. As for a possible relaxation, the matter was kept under review but could not be separated from the overall balance-of-payments situation.

19. Members of the Committee also raised the question of the differential credit restrictions applicable to vehicles purchased from bilateral sources which gave them an advantage not enjoyed by vehicles originating in market-economy countries. They enquired specifically whether it was still a matter of balance-of-payments policy that this preference should continue to be extended and asked that it be eliminated.

20. The representative of Finland replied that he could give no indication of any intent to comply with the request to eliminate this differential whose practical impact was considered to be limited and which had a definite relationship to Finland’s balance-of-payments position and would continue to do so as long as uncertainty continued regarding the balance of payments.

21. The difficulty of selling imported beer to the Finnish State monopoly was also raised and it was suggested that the mark-up policy of the monopoly constituted a severe barrier to trade. The representative of Finland noted that this point had been raised in the non-tariff barrier context and suggested that it might better be pursued in that forum.

General

22. Members of the Committee thanked the representative of Finland for the presentation which he had made to them of a marked improvement in his country’s position; in their view this had been the fruit of well-conceived policies well-executed. They commended Finland for progress in trade liberalization and urged that this policy be continued as rapidly as continuing progress might permit, and urged that in the light of Finland’s improved balance-of-payments position, the remaining industrial and agricultural products still subject to global quotas or discretionary licensing will be further liberalized.