1. In accordance with its terms of reference, the Committee has conducted a consultation with Finland under paragraph 4(b) of Article XII and has examined the Finnish Import Deposit Scheme as instructed by Council at its meeting of 24 March 1975. The Committee noted that the previous consultation with Finland under the same provisions had been held on 18 June 1973 (see BOP/R/66). In conducting the consultation the Committee had before it a basic document supplied by the Finnish authorities (BOP/150) and notifications of the Surcharge and Import Deposit Measures (L/4165 and Add.1), a Background Paper provided by the International Monetary Fund dated 30 December 1974, and the text of a decision of the Executive Board of the International Monetary Fund taken on 22 January 1975.

2. The Committee generally followed the plan for such consultation recommended by the CONTRACTING PARTIES (see BISD, 18th Supplement, pages 52-53). The consultation was held on 21 April 1975. This report summarizes the main points of the discussion.

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 the consultation with Finland. Upon the invitation of the Committee, the representative of the Fund made a statement as follows:
"Following a slight downturn in 1971, the Finnish economy experienced a strong rate of economic growth in 1972 and 1973. In 1974 supply bottlenecks and an exceedingly tight labor market became factors constraining real GDP growth, which declined slightly to 5 per cent. Curbing inflation was the principal focus of official policy. Substantial tax concessions and increases in social benefits were granted as part of an incomes agreement, which had the effect of reducing the Government's budget surplus from a level which had in 1973 become very large. The wage agreement provided for increases in wages of 12 per cent in 1974 and, subject to a review in early 1975, of a further 11 per cent in 1975. In 1974, however, wage drift was very strong and earnings increased by nearly 17 per cent, with consumer prices rising by a similar amount. The negotiations concerning the renewal of the agreement in early 1975 will lead to additional increases in wages in 1975 and to increased social benefits being provided through the budget.

"The balance of payments continued to deteriorate with a trebling of the current account deficit to over SDR 1 billion in 1974, equivalent to more than 5 per cent of GDP. Despite the higher oil costs, there was only a slight deterioration in the terms of trade as export prices rose sharply. Though export supply capacity remained insufficient in many sectors, there was a noticeable decrease in demand for exports of plywood and other materials in the second half of the year. The volume of exports to the U.S.S.R., from which Finland imports two thirds of her oil, rose by 66 per cent in 1974, but the volume of exports to other countries declined. The volume of imports, under the influence of rising domestic demand, continued to rise strongly. Gross official convertible reserves showed little change in 1974, and the deficit was financed to a large extent by short-term capital inflow and by an increase in Finland's debtor position under the bilateral clearing arrangements.

"The balance of payments situation worsened sharply in the first two months of 1975, partly as a consequence of an upsurge of imports apparently in anticipation of the imposition of trade controls. During the first two months of the year the trade deficit amounted to SDR 400 million, and gross official convertible reserves fell by SDR 133 million to SDR 446 million, the equivalent of about one month's imports. The debit balance under the clearing arrangement with the U.S.S.R. continued to rise.

"Finland maintains global quotas and individual licensing in respect of certain agricultural commodities, mineral fuels, and unwrought gold and silver from countries with which she does not maintain bilateral payments arrangements. These restrictions are maintained essentially for agricultural policy and in order to facilitate the implementation of bilateral trade and payments agreements. While their removal might lead to a sudden increase in imports in the short run, it is unlikely that it would have a sustained or substantial effect on the value of total imports."
"In the face of the worsening balance of payments situation, the Government announced in March 1975 fiscal and monetary measures designed to restrain the growth of domestic demand. The authorities considered, however, that these policies would be insufficient to yield quick improvement in the balance of payments, and they were supplemented by a temporary import deposit obligation on imports. The decision to impose the obligation may not extend beyond 12 months at a time but the authorization is valid until the end of 1976. The deposits are for six months. Full details of the implementation of the scheme are not yet available, but it is believed that in practice the scheme will cover about half of imports. The deposits vary between 5 and 30 per cent of the import price of the goods and they do not bear interest; they are to be held in a special account with the Bank of Finland.

"The Fund believes that in view of the very low level of Finland's reserves, the temporary imposition of the import deposit requirement does not go beyond what is necessary to prevent a further fall in the level of reserves. The authorities have adopted a number of other measures, including fiscal and monetary measures, to deal with the economic situation. These policies should be supplemented with additional measures, if necessary, so as to allow the termination of the import deposit scheme within 12 months of its introduction."

Opening statement of the representative of Finland

4. In his opening statement, the text of which is contained in the Annex, the representative of Finland outlined the developments in the Finnish economy and the balance of payments during 1974, and described the rapid deterioration of the current account in the first months of 1975. The first quarter of 1975 showed a deficit in the trade balance of almost 2.3 billion Markkas. Most of the 1974 deficit in the balance of payments had to be financed by short-term credit or by foreign exchange reserves. As a result net foreign indebtedness had increased by over 50 per cent and the level of convertible foreign exchange reserves of Finland had declined to about 1.7 billion Markkas at the end of 1974. The decline in reserves accelerated in the first months of 1975 and convertible currencies in the
reserves fell by roughly 50 per cent. At the end of March total convertible reserves stood at 1.2 billion Markkas, the equivalent of less than three weeks imports. Since mid-1974 the external demand for Finland's main export products slowed down; the forecast for the export performance in 1975 being very pessimistic there was a danger that the total 1975 deficit would easily rise to much higher figures than that of the previous year. The Finnish Government's ability to maintain growth oriented policies is dependent on the possibilities for reasonable financing of the foreign trade deficit arising from such policies. As these possibilities are reduced, in the light of the international business outlook, Finland was forced to adopt a more restrictive economic policy.

5. On 24 March 1975 a temporary import deposit system was introduced. The deposits are for six months and amount to a maximum of 30 per cent of the import price of the goods. The deposit rates vary between 5 and 30 per cent, are non-interest bearing and are held in a special account with the Bank of Finland. Products covered by the Scheme amount to 63 per cent of the total value of imports. In practice the Scheme covers about half of imports because materials used as inputs by the export industry are exempted from the Scheme. The Import Deposit Act is valid until the end of 1976. However a decision to impose the obligation may not extend beyond twelve months at a time.

6. The Finnish authorities have taken other measures to restore a more balanced economic development; among these are fiscal measures to limit the growth of domestic demand in the next few years, the volume of central government and local government consumption expenditures will be considerably restricted and the
volume of central government investment will be kept approximately on the low level of 1974. Credit policy guidelines by the Government to State-controlled financial institutions have been given to improve the effectiveness of investment policy. Priority is to be given to productive investment in manufacturing industries which can help redress the balance of the current account. Energy saving measures are in preparation. Tight monetary policy will also be continued in support of the Government's economic objectives.

7. The representative of Finland explained the basic reasons why quantitative restrictions, under Article XII to safeguard the Finnish balance of payments, were still needed. The structural changes of the economy continued to exert pressure on the external position of the country; Finland's bilateral trade was of great importance for the economy and especially for the supply of fuels and certain raw materials. This trade had enabled Finland to diversify the economy and to liberalize multilateral trade. Finally the outlook for Finland's trade and current balance was not very good in the near future. Thus, in the opinion of the Finnish Government circumstances did not permit any major changes in the present import system. However, as soon as balance-of-payments developments would allow, the Government would take measures to abolish the temporary import deposit system.

Balance-of-payments position and prospects

8. Members of the Committee expressed their regret that Finland had to resort to import restrictions, especially at a time when there was danger of proliferation of such restrictions. While regretting the need for restrictions they expressed understanding for the particular situation of Finland, the difficulties
faced in its balance-of-payments position and the level of its reserves, which at three weeks imports could hardly be called large. They hoped that the situation would be redressed in the near future, so that restrictions would be eliminated at an early date. They noted that the deterioration in the current account of 1973 continued in 1974 and that the first two months of 1975 saw a substantial worsening in trade deficit. They noted that the level of international demand for Finland's traditional products had fallen and asked whether exports of other than forestry products had also diminished. The representative of Finland said that the slackening had been felt mainly in the timber and paper industries; some decline had been felt in light metal industry exports, although the metal industry was not yet in difficulty.

9. In reply to questions concerning the sharp rise of imports in 1974 the representative of Finland explained that both the volume and the value of imports had contributed to this rise. The price of petroleum and petroleum products had risen sharply, as had the price of raw materials and that of some investment goods. In addition, the volume of imports had risen by some 7 per cent in 1974 and this increase had continued in the first months of 1975.

10. It was remarked that from the information supplied by the Finnish delegation the share of imports in 1974 under multilateral import treatment had fallen by 6 percentage points whereas the share of imports from bilateral trade agreement countries had risen by the same percentage points. The representative of Finland explained that Finland imported two thirds of its crude oil from the Soviet Union and all its coal from Poland; the price of these commodities had trebled, therefore increasing the value of total imports from socialist countries.
Exports to these countries had also increased mainly because the trade with the USSR was on a bilateral basis and, therefore, paid by Finnish exports. In 1974 the value of exports to socialist countries had increased by 17 per cent.

11. Asked to comment on the transport, other services, and invisibles account of the balance of payments the representative of Finland stated that this net balance still showed a slight surplus in 1974.

12. Members of the Committee noted that a substantial deficit on current account was expected in 1975 and enquired what plans were being made to meet this deficit with very low reserves and poor prospects for capital inflows. It was asked whether Finland expected to draw on the International Monetary Fund’s Oil Facility in 1975 or on their IMF quota. The representative of Finland said that earlier estimates for the 1975 balance of payments indicated a deficit of the same order as for 1974; however, later development showed that the deficit could reach twice that figure. The possibilities of covering the deficit through long-term capital movements seemed slim. In 1974 only one fifth of the deficit had been covered by this means. Drawing on the International Monetary Fund’s Oil Facility and/or quota can of course among other possibilities be taken into consideration. After the implementation of new measures and the slackening of export demand, no revised estimate of the balance-of-payments deficit in 1975 has yet been made. Developments in the balance-of-payments situation will be constantly kept under review.

13. In reply to a question as to whether the Finnish authorities would be in a position to consider giving more scope for market forces to determine the exchange rate of the markka the representative of Finland pointed out that the
markka being a small currency its floating would always have to be guided. The policy was to keep the average value of the markka as constant as possible in terms of a trade weighted basket of currencies. In mid-1974 some consideration had been given to revaluation of the markka, however, now with a deterioration of the balance-of-payments position no change could be expected in the exchange rate. The deficit on current account was not due to uncompetitive prices of the Finnish exports but to conditions prevailing in Finland's main exports markets.

Alternative measures to restore equilibrium

14. Members of the Committee noted that the Temporary Import Deposit Scheme had been supplemented by a number of other measures including fiscal and monetary measures to deal with the economic situation. In this context they noted the finding by the IMF to the effect that "these policies should be supplemented with additional measures, if necessary, so as to allow the termination of the Import Deposit Scheme within twelve months of its introduction". Members of the Committee enquired as to the nature and scope of these other measures and the dates, past or future, of their application.

15. With regard to measures adopted to encourage exports it was remarked that one of the obstacles encountered in this field was the limits of the production capacity and the lack of diversification of industry. The representative of Finland explained that measures to encourage exports consisted mainly of directives to State-owned financial institutions concerning the grant of credit to export-oriented industries which could contribute to redressing the current account deficit. Simultaneously, the Government was considering to intensify its export promotion efforts by reinforcing the network of commercial secretaries abroad.
16. It was asked whether energy saving measures, taken or envisaged, worked through the price mechanism. The representative of Finland said that it was premature to reply to this question as new measures had not yet been taken. A committee had been set up to make recommendations on this matter - some time was needed for the elaboration of such measures.

17. Several questions were posed as to the different fiscal measures envisaged and on the level of receipts from direct and indirect taxes, particularly on firms. The representative of Finland explained that policy guidelines had been set for the public sector including ceilings on growth of central government expenditures and there are negotiations under way to limit the growth of local government expenditures as well. The growth in the volume of central government consumption expenditures will be kept at $\frac{3}{4}$ per cent this year and 2 per cent in 1976. The average annual growth rate has been slightly over 4 per cent in recent years. Almost zero growth target was set for central government administrative investments. Among these measures the expenditure for the school reform will be somewhat less than that planned in the original programmes. Also, the cost of implementing the National Health Act will be reduced both by cutting part of the planned increase in staff and postponing certain investments.

18. Questions were asked concerning the price control and surveillance mechanism. The representative of Finland explained that price controls had been in force for some time. Price control was extended to all goods on 11 March 1975. The scope of the control was on 11 April 1975 adjusted back to the level, which was agreed on in the incomes policy agreement in 1974. The only exception was
the measure prohibiting the inclusion of the costs of the temporary import deposit in prices. For that reason the price control was extended to import goods which are subject to a deposit charge.

19. The Committee noted that the Finnish Import Deposit Scheme was introduced on 24 March 1975 and applied retroactively to all imports as from 12 March 1975; that the rates of the deposit ranged from zero to 30 per cent on the value of the imported goods; that the deposits were placed on a special account of the Bank of Finland for six months, without interest; and that the duration of the measure was one year. The Committee noted and welcomed official statements by Finnish authorities that the Import Deposit Scheme was applied on a non-discriminatory basis and that no special credits would be provided to offset the Import Deposit requirements for imports from CMEA countries.

20. It was asked what procedures were used to determine which imported goods would be exempted from the prior import deposit when used to produce for exports. Did this exclude for instance, machinery and other capital goods purchased by exporting firms. It was also asked whether duty-free imports under Articles 89-93 of the Finnish Customs Law were exempt. Noting that imports of small quantities were exempt from the deposit requirements it was asked what criteria were applied to this category. The representative of Finland stated that imports of goods under Articles 89-93 of Finnish customs law were exempted from import deposit scheme. Also non-commercial consignments of a value of less than 1,000:- markkcas imported by private persons were free from import deposits.
21. Members of the Committee asked what provisions and criteria governed additions to or deletions from the import deposit requirements list. The representative of Finland said that requests for exemption from the deposit had to be made by direct application to the Government; the request would first be examined by a committee on a case by case basis. No fixed guidelines had been set for exemptions. Exceptions to the present list were not expected to be numerous and would be limited to cases of hardship or unjust treatment.

22. In reply to a question as to whether the price surveillance mechanism would prevent importers from passing on the import deposit burden to consumers in the form of higher prices, the representative of Finland explained that when a producer wanted to increase the price of his goods the present legislation required him to file a request giving the basis of his prevailing price and accounting for the factors which would justify an increase. The cost of the imported deposits was not an acceptable justification. As most goods included in the consumer price index were covered by the price surveillance system the Government has an effective tool to prevent importers from passing the cost of the deposit to consumers in the form of higher prices.

23. Members of the Committee asked whether any provisions were being considered by the Finnish Government to lessen the impact of the deposit requirements on importers of goods from bilateral trade countries or from countries with which Finland had a trade surplus. The representative of Finland stated that the import deposit system was non-discriminatory and that no special treatment of imports from CMEA area countries would be provided. Nor would such treatment
be provided for imports from countries with which Finland had a surplus, as this would amount to discrimination. He pointed out that in any case Finland had a trade deficit with most CMEA countries. Asked whether the import deposit could be financed by the exporting country or firm, the representative of Finland stated that according to regulations exporters could not finance the import deposit. He explained that foreign financial credits always went through the Bank of Finland. Import credits up to six months can normally be employed, however, some imports amounting to less than 1/5 of total imports are subject to cash payment requirement prior to customs clearance; this effectively rules out foreign suppliers' credit for this latter category of goods. The Bank of Finland will not allow special arrangements to finance the deposit; importers could, however, find some easing in the financing for imports of goods not subject to the cash payment requirements, if they could prolong their import credits to the allowed maximum of six months. Asked whether foreign long-term import credits could be drawn on to finance the deposit the representative of Finland said that long-term import credit for investment goods were subject to Central Bank discretion.

24. The representative of Finland confirmed that goods shipped between 12 and 24 March were not exempted from the import deposit: the decisive date for application of the Import Deposit Scheme was entry of the goods into the country as from 12 March 1975. He added that in fact very few goods, except for a few perishable imports, had been customs cleared between 12 and 24 March.

25. Questions were asked concerning the criteria used to determine the rates of the deposits which, apart from the exemptions were of five, ten, twenty and thirty per cent of the value of the goods. The representative of Finland said
that the rates of the import deposits were set according to the essentiality of the goods; essential goods were exempted, necessary goods enjoyed a low rate, 5 or 10 per cent, and less necessary goods would have higher rates.

26. It was asked whether in view of the current problem of payments imbalance, Finland would continue to make foreign exchange available for imports of items subject to global import quotas, in excess of the indicative level of the quotas, as it had done in the past. The representative of Finland replied that the system would continue. He pointed out that the level of the global quotas for 1975 had been set at a little over 67 million markkas compared to the 1974 level of 57 million markka. Up to 15 April 1975 total licensing has already amounted to 41 million markka.

27. In reply to a question the representative of Finland confirmed that the existing global quotas were maintained for balance-of-payments reasons and that when the balance-of-payments situation improved the Government would review the need to maintain the global quotas. He also confirmed that under the import licensing system treatment of imports from the Soviet Union and other countries with which Finland had bilateral trade agreements was not more favourable than that accorded to imports from the multilateral trade area.

Effects of the restrictions

28. Members of the Committee noted that after exemptions had been taken into account the Import Deposit Scheme covered some 50 per cent of total imports and asked whether any data was available on the volume of imports covered by the Scheme under its different rates. The representative of Finland said that on
the basis of 1974 import figures the Deposit Scheme covered the following percentage of imports: 32.1 per cent at 30 per cent deposit rate, 5.7 per cent at 20 per cent deposit rate, 18 per cent at 10 per cent deposit rate, and 7.3 per cent at 5 per cent deposit rate and 36.9 per cent at zero rate.

29. Asked whether Finland had any estimates of the impact of the deposit scheme on its main suppliers, the representative of Finland said that at this stage it was too early to tell; as they had no experience in the matter it was difficult for them to forecast. It has been estimated that the Deposit Scheme would tighten the financial market by some 1.5 billion markka and that this would be felt most strongly by importers. This represents a selective monetary measure. Short-term foreign capital inflow might increase by some 500 million markka due to increased use of short-term import credits. He stressed that the strongest effect would be felt during the first six months of the Scheme, when the deposits were being built up. This would probably lead to a reduction of stocks held by importers. The effect on overall demand would depend on the duration of the Deposit Scheme and that of other measures. It was not expected that there would be any significant impact on the growth of the economy; the possibilities of import substitution being slight. The expected effects would be to reduce the growth rate of imports by some 4 percentage points. However, despite this measure Finland expected to continue having a current account deficit out of proportion with the global deficit of industrial countries.

30. With regard to the duration of the Import Deposit Scheme and its termination members of the Committee noted that although the authority to apply the Scheme went up to the end of 1976 its expiry had been set by the Finnish Government
at 23 March 1976. It was expected that Finland would want to terminate the Scheme at a time when it had sufficient margin of manoeuvre to counterbalance the effect of releasing the funds frozen on the special account for the import deposit. The representative of Finland said that while the Government had authority until the end of 1976 to apply the Scheme its intention was not to apply it longer than absolutely necessary. The developments in the external accounts would be followed very closely. Time was needed for other measures to take effect. He stressed that one of the principal elements of the situation was the development of economic conditions in Finland's main export market.

31. One member of the Committee raised the question of a particular product which, whether imported or produced in Finland, was subject to an excise duty. However the excise duty on the domestically produced product was offset by a restitution payment of the same amount. This resulted in discriminatory treatment and was not conform to the provisions of Article III of the GATT. The representative of Finland said that the matter would be looked into and the reply given on a bilateral basis.

32. In reply to question concerning the prospects for reviewing and/or eliminating the various import restrictions such as the cash payment system, import licensing etc., the representative of Finland said that the present situation was of such a serious nature that it was not possible for the time being to revoke any of these measures.

Conclusion

33. The Committee regretted that Finland had to impose an Import Deposit Scheme, but expressed understanding for the particular situation of Finland's balance of payments and the low level of its reserves.
34. The Committee noted with satisfaction that the Import Deposit Scheme was applied on a non-discriminatory basis. Import restrictions including the Deposit Scheme, were not more restrictive than measures authorized under Article XII of the General Agreement. The Committee welcomed the statement by Finland that the Import Deposit Scheme would not be applied longer than absolutely necessary, and hoped that the Finnish balance-of-payments situation would be redressed in the near future so as to allow an early termination of import restrictions, including the import deposits. In the meantime, they urged Finland to make as liberal a use as possible of the exemption possibilities of the Deposit Scheme, in particular for investment goods for export-oriented industries, and to review the measure periodically with a view to reduce deposit rates at an early date.