GENERAL AGREEMENT ON TARIFFS AND TRADE

RESTRICTED

Spec(75)44
20 November 1975

Committee on Balance-of-Payments Restrictions

DRAFT REPORT ON THE CONSULTATION UNDER ARTICLE XVIII:12(b) WITH PERU

1. In accordance with its terms of reference, the Committee met on 17 November 1975 to conduct a consultation with Peru under the provisions of Article XVIII:12(b). The Committee noted that a consultation under the simplified procedures (L/3772/Rev.1) had taken place with Peru on 25 March 1974 when it had been decided that a full consultation would be held under the applicable procedure. The previous full consultation with Peru under the provisions of Article XVIII:12(a) and (b) had been held on 19 June 1970 (BOP/R/46). In conducting the consultation the Committee had before it a statement submitted by Peru (BOP/161 and Addendum 1), and supplementary background material provided by the International Monetary Fund dated 3 October 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 17 November 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 IMF to consult with them in connexion with the consultation with Peru. Upon the invitation of the Committee, the representative of the Fund made a statement as follows:

"The economy of Peru grew by 6 per cent in real terms in 1974, reflecting increased activity in the construction sector and a partial recovery of fishmeal production.

"Public investment expanded rapidly despite a marked deterioration in the savings performance of the public enterprises brought about by the program of consumption subsidies. However, large-scale reliance on foreign borrowing allowed the public sector virtually to refrain from resorting to domestic bank credit. As regards the private sector, the change in the import financing mechanism introduced during the second quarter of the year, i.e., the introduction of a 180-day foreign financing requirement for private sector imports other than capital goods, resulted in a reduced need for domestic credit. As a result of these developments, net domestic credit expansion remained moderate and was financed by the growth in the monetary liabilities of the banking system. Resort to foreign borrowing prevented a decline in international reserves. Demand pressures resulting from the stepped-up economic activity and the reduced rate of domestic savings were reflected in the domestic price level; consumer prices, on average, rose by 17 per cent in 1974 against 9.5 per cent in 1973.

"Favorable price movements for Peru's exports resulted in a 34 per cent increase in merchandise export receipts despite a sluggish rise in the export volume. At the same time, however, rising import prices for petroleum, food, and capital goods, together with a 20 per cent increase in import volume associated with expansionary demand policies, brought about a

60 per cent rise in the value of merchandise imports. Thus the trade account moved from near-equilibrium in 1973 to a deficit of SDR 235 million in 1974. The deficit on services and transfers increased from SDR 232 million to SDR 268 million mainly on account of sharply rising transport costs and interest payments on the external debt. As a result the current account deficit more than doubled to over SDR 500 million in 1974. Net official capital inflows, however, together with increased foreign priviate investments and large short-term private capital inflows associated with the change in the private sector import financing mechanism mentioned above, more than compensated for the widening current account deficit. The overall balance of payments registered a surplus of SDR 225 million and the net international reserves of the banking system increased from SDR 340 million to SDR 566 million, or equivalent to about four and a half months' imports at their 1974 level.

"Partial data for 1975 point to a substantial further growth of imports in the first half of the year, while export receipts reportedly remained unchanged following a decline both in the volume and prices of mineral exports. Given the continued rapid increase in interest payments on the external debt, the current account deficit is estimated to have deteriorated further. With official capital inflows falling short of last year's levels, the public sector deficit was financed to an important extent by recourse to domestic bank credit. Bank lending to the private sector also accelerated moderately. The resulting domestic credit expansion brought pressures to bear on the balance of payments. The net international reserves of the banking system declined by an estimated SDR 420 million during the first six months of 1975.

"In these circumstances, the Peruvian Government in June 1975 decided to scale down the subsidies and to reactivate domestic output by sharply raising prices on a number of price-controlled goods and services. In addition, domestic agriculture was to be aided by a reduction in the price of fertilizers. A general readjustment of wages and salaries was also decreed to compensate for part of these price increases. These measures were supplemented on September 25, 1975, by a depreciation of the Peruvian sol by about 14 per cent in the certificate market in terms of the U.S. dollar and a unification of the exchange rates previously prevailing on the certificate and draft markets at S/. 45 per U.S. dollar.

"While an assessment of the quantitative impact of the measures taken since mid-1975 would be premature, they should help in restoring internal and external equilibrium. For the time being, in view of Peru's current balance of payments difficulties, the restrictions in effect do not exceed those necessary to prevent a further decline in Peru's monetary reserves."

Opening statement by the representative of Peru

4. In his opening statement, the full text of which is annexed to this report, the representative of Peru said that his Government sought to relate more closely than in the past, Peru's overall development objectives, with the expansion of the external sector. This was the aim of the foreign trade policy currently pursued.

5. After briefly reviewing and assessing the financial and trade measures adopted by the Peruvian Government to overcome balance-of-payments difficulties in 1967, the representative of Peru described the adverse effects of recent trade developments on Peru's external financial position and he discussed some

of the measures taken to counter those developments. Owing to substantial increases in export prices, Peru's export earnings increased considerably in recent years, despite serious shortfalls in the domestic production of some important export goods, such as fish oil and meal. Since mid-1974, however, the upward trend of export prices was reversed and, due to prevailing economic conditions in world markets, foreign demand for Peruvian goods had contracted. This, together with the sharp rise in import prices and Peru's increasingly large import requirements, especially for intermediate and capital goods for development projects, had led to a trade deficit of $389 million in 1974, which was expected to reach some $1,000 million in 1975. At the same time Peru's structural deficit on services account had also grown in recent years and reached $711 million in 1974, i.e. twenty-two times larger than in 1972. This was due mainly to increases in freight costs and heavy foreign debt servicing. While in 1973 and 1974 the deficit on current account had been entirely financed by inflows of long and short-term capital, this was not expected to happen in 1975; although it was difficult at this stage, to estimate, the overall balance-of-payments deficit for 1975.

6. The Government had taken several measures to restore equilibrium. Peru had devalued the sol against the United States dollar this year. There were good prospects of substantially increasing Peru's foreign exchange receipts in the near future, owing to the considerable investment effort in the petroleum, phosphates and copper industries. The major reason of existing import restrictions was to allocate scarce foreign exchange availabilities to priority projects, necessary to the country's development.

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

7. The members of the Committee thanked the Peruvian delegation for the ample information they had supplied to the Committee. They took note of the movements in the level of reserves over the past decade and of the recent decline in Peru's foreign reserves. They expressed sympathy and understanding for the different problems facing Peru, in particular those concerning its balance-of-payments position. Some members of the Committee pointed out that Peru was facing the same set of problems in its balance of payments as other non-petroleum producing developing countries; that was, on the one hand, the increase in the price of petroleum and petroleum products and on the other hand, the increase of prices of imports from developed countries, imports which were essential for development purposes. In this context it was asked what the prospects were for the balance of payments in 1976. The representative of Peru said that his authorities were very concerned about developments for 1976; it was difficult at this stage to determine what the level of export income would be, as this would depend on the general situation of world prices for Peru's exports. If Peru's imports were to increase in 1976 the prospects for Peru's balance of trade would be very poor and would probably result in a higher deficit than that expected for 1975.

8. Noting that the rate of inflation in Peru had increased dramatically in the twelve months ended in August 1975, some members of the Committee enquired what measures were being taken in the monetary and fiscal fields to combat this trend. It was also asked whether a modification of the structure of interest rates and encouragement to savings would not be measures which would contribute to reduce price pressures. In reply the representative of Peru said that

so far the Peruvian authorities had endeavoured to contain the effects of inflation, which came from abroad, so that they would not be felt within the country. The policy adopted had been to subsidize a number of essential consumer goods such as petroleum, wheat and some lesser products. While it was not the intention of the Peruvian authorities to apply subsidies on a permanent basis, the representative of Peru pointed out that if subsidies were to be reduced at this time there would be severe internal inflation and the effects would be felt on the national budget. He added that the subsidies given were not equivalent to price fixing.

9. Members of the Committee noted the substantial foreign capital inflows which had occurred in 1974. Large investments in the private sector had thus been made through foreign financing. It was asked what measures were envisaged to attract further foreign capital investments and what guarantees could be extended to foreign investors. The representative of Peru replied that existing legislation within the Cartagena Agreement regulated the inflow of foreign private investment in Peru. The provisions of this law encouraged increased foreign investment in order to provide the necessary financing for the development of the country.

10. Commenting on the level of the external debt in 1974, members of the Committee asked whether the Peruvian authorities expected to have problems with regard to the servicing of this debt and whether measures were being envisaged to avoid further growth of the foreign debt. The representative of Peru assured the members of the Committee that the servicing and amortization of the foreign debt was of prime concern to his authorities, who would be

prepared even to limit imports, which were essential to the country's development, in order to meet its debt commitments. He stressed that if the external debt had been allowed to grow it was in order to invest in development programmes in Peru, which were expected eventually to pay for themselves and to earn foreign exchange. Examples of such programmes were the petroleum development programme for 1976-77 when the first refinery would be opened, as well as the programme for building a refinery for copper ore. One delegation pointed out that the future servicing of Peru's external debt could pose some problems as the current interest rates were higher now than they were in 1974.

11. In the context of expansion and diversification of Peruvian exports, it was noted that the composition of exports would be altered by 1977 when Peru would be exporting petroleum and phosphates. It was asked whether Peru expected to be self-sufficient in petroleum by then and also whether further diversification of exports was planned. The representative of Peru said that the export of petroleum was expected to have a significant influence on the balance of trade and on the current account. It would enable Peru to reduce its imports of petroleum and petroleum products and would increase its export earnings. He added that Peru had adopted a policy of promotion of exports with a view to improving the balance-of-payments position. This consisted of the diversification of export products and markets and encouragement to production through the financing of projects and through various promotional measures such as the exoneration of taxes on the production of goods for exports. It was the intention of Peru to increase its exports of non-traditional goods. This had partly been achieved; in 1969 non-traditional exports amounted to $16 million whereas by the end of 1974 they had reached over $150 million. Several important internal measures would have to be completed

before Peru would be in a position to achieve a measure of balance; an agrarian reform was an important factor in this context, it was expected to play a large part in the redistribution of income, and to stimulate an increase in domestic agriculture production. Another field which needed to be further developed was the internal capital market, which was at present too narrow. While there were some promotional interest rates which were low and which were designed to promote export projects the internal capital market remained insufficiently developed.

12. Noting that Peru had an extensive programme of subsidies for public sector consumer goods, details were asked as to the present volume of these subsidies and whether their recent reduction had had any effects on the level of consumption and imports. It was also asked whether the Peruvian authorities had any intention to further reduce these subsidies and eventually to remove control on prices. The representative of Peru said that the elimination of price controls would depend on the amount of fiscal pressure at a given moment. He added that subsidies were given on a selective basis, mainly on products which affect family budgets or development programmes for certain industries. His authorities realized that subsidies would have to be continually adapted to the prevailing situation. One member of the Committee remarked that subsidies could be counter-productive to Peru's objective, in so far as they might divert funds from development projects.

13. Referring to paragraph 21 of BOP/161, one delegation enquired how import demand, in particular of consumer goods, had been affected in 1970-74 in relation to total imports. The representative of Peru replied that at present import of consumer goods (durable and non-durable) represented some 15 per cent of total imports; imports of raw materials and its immediate goods such as products for

agriculture and semi-manufactures for industry made up some 40-45 per cent of imports, while imports of capital equipment, in particular for construction, transport and industry, made up some 40 per cent of imports.

14. Some members of the Committee noted that there were a number of internal measures in Peru which had the effect of subsidizing exports and consumption, while on the other hand non-tariff measures were resorted to restrict imports. This caused some anxiety to Peru's trading partners. It was hoped that Peruvian authorities would find it possible to move away from a system of non-tariff measures in order to control the level of its imports towards a system based on tariffs. It was also hoped that Peru's oil exports to come would, by reducing Peru's need for imports of petroleum and by increasing its export earnings, enable the authorities to introduce some relaxation of its import control measures.

Parts III and IV Systems and methods of restrictions, and effects of restrictions

15. Members of the Committee noted that on 1 January 1975 Peru had introduced a new tariff which incorporated all the various taxes and charges, including a 10 per cent surcharge and 2 per cent statistical tax, which had until then been levied separately. They welcomed this incorporation into a single tariff as a step towards simplification of import procedures. In this context it was asked whether the new tariff regrouped all additional taxes or charges and whether any supplementary charges were still levied separately. It was also asked why the new tariff did not list the bindings of Schedule XXXV Peru. The representative of Peru stated that the new tariff incorporated all the previous additional

charges. He pointed out that the different treatments accorded to various areas such as LAFTA, the Cartagena Agreement and GATT were not specifically mentioned. With regard to possible modifications of bindings in Schedule XXXV the matter would have to be ascertained in consultation with the GATT secretariat. In reply to another question the representative of Peru said that tariff rates were under continuous examination and changes did occur when these were necessary. A member of the Committee asked what conditions would be required by Peru to move towards more reliance on its tariff as an instrument to control imports rather than the non-tariff measures used at present and which were expensive to administer and generally caused trade distortion. The representative of Peru said that such a change would necessarily have to be undertaken gradually in the light of the prevailing national and international economic situation; it could not be expected that Peru could restructure its whole system without allowing time for the necessary adaptations. The adoption of a new tariff in January 1975 was one step towards rationalization and greater reliance on a system based on tariffs. However, it was not possible at this stage to give any indication of when Peru would move towards more reliance on tariffs alone. He added that many of the non-tariff measures adopted were transitional and temporary in nature.

16. Members of the Committee noted and welcomed the fact that Peru had eliminated the requirement for consular invoices. They noted that this was in conformity with the Recommendation of 30 November 1957 of the CONTRACTING PARTIES. However, it was pointed out that there was a customs tax of 10 per cent which had to be paid at the time of clearance of the goods. The representative of Peru explained that this 10 per cent tax was paid by the

importer. It was levied to cover the costs of customs procedures; it applied only to the domestic importer and was not meant to be a tax on imports. A member of the Committee suggested that the rate of the tax could be reduced to an amount that approximated the cost of services rendered in accordance with the provisions of Article VIII of the GATT.

17. It was pointed out that an export tax of 10 per cent had been introduced by the Peruvian authorities in 1974 and had been prolonged in 1975. It was enquired whether no negative effects on the balance of payments had resulted from this tax, as it would have the effect of making Peruvian exports more expensive. The representative of Peru said that it was his authorities' policy to seek balance-of-payments equilibrium through measures to diversify and increase Peruvian exports. He explained that the 10 per cent tax applied only to traditional exports. It had not acted as a disincentive. It was to be remembered that some 85 per cent of Peruvian exports were undertaken by State entities and that the tax therefore was a fiscal measure applicable to government public enterprise. The export tax did not apply to all traditional exports; furthermore, non-traditional exports included reimbursement of taxes levied at the production stage on goods imported for processing or on dutiable inputs. There were also measures to finance investment for export production, to supply firms with working capital; to this could also be added assistance measures in marketing at the domestic and foreign level. A central point of information had been created to supply information on foreign markets. Abroad, Peruvian authorities endeavoured to search for new markets which could be supplied by Peruvian firms. These export promotion measures, which were selective and necessarily had to remain within the financial and staff possibilities of the Government, were destined to encourage exports both of traditional and non-traditional goods.

18. Some delegations referring to paragraph 34 of document BOP/161 which describes the system of prohibitions applied in Peru asked clarification concerning the purposes of prohibitions and under what conditions goods could be put on the list or deleted from the list of prohibitions. It was also noted that the prohibitions amounted to some 13 per cent of tariff positions, but that this did not give a clear picture of the real importance of these prohibitions. It was recalled that the measure had been first introduced in 1968 for a duration of ninety days then prolonged and the list expanded. The representative of Peru said that the products included in the list of prohibitions were usually either consumption products and some products that were produced in Peru. Total prohibitions in terms of 1967-68 imports amounted to some 10 to 13 per cent of total imports in volume. The object of this measure was to divert internal demand from imports to domestic products and to encourage development of national industry. It did not amount to a reduction of trade but to a diversion of trade. He added that the prohibitions were flexible to a certain extent: for instance exceptions were made in cases when a need arose to import goods included in the list of prohibitions; this had occurred typically in the construction industry.

19. Questions were asked concerning the national register of manufactures; in particular on the criteria used to determine which products should be included in the register and whether there were frequent changes in the list and if time was allowed for adaptation before a new modification was introduced in the register. The representative of Peru explained that the national register of manufactures was designed to protect domestic infant industry. It was a flexible mechanism and did not entail a complete prohibition of importation of the products listed. Importation was still allowed for instance when the product in question was in

short or insufficient supply from domestic production. Some products found their way on the national register of manufactures even if they were not entirely similar or competitive with the corresponding foreign products; this was done in order to stimulate the development of national industry. He added that the protection of infant industry was flexible; to the extent that a national product was not up to quality requirements, imports of the corresponding product were still authorized. Also to the extent that domestic production of a particular product could not meet all the demand limited importation was authorized. This need for adaptation to the prevailing conditions resulted in products being placed on-and-off the list according to Peru's requirements.

20. Questions were asked concerning the system of customs valuation which used a list of minimum and maximum prices, in particular concerning how these prices were set, on what criteria, and whether they could be altered. The representative of Peru said that the system of minimum and maximum prices for customs valuation was applied mainly to avoid under- and over-valuation of imports and exports. He added that the Peruvian authorities did not have at its disposal full information on the prices of all the products concerned in foreign markets, so that it had selected those products to collect information on where there seemed to be some doubt or conflict as to the value. This information was gathered on external markets and served as a basis to set the minimum and maximum prices. Imports were allowed to the extent that they were within the range of prices set. He added that Peru did not yet have sufficiently large an infrastructure to gather as complete information as was desirable.

21. Members of the Committee asked for explanations concerning the objectives of State trading and how it affected the allocation of resources. The representative of Peru replied that essentially the system of marketing through State enterprises was used to dispose of surpluses of certain products and to regulate trade in certain products, which were either significant to Peru's trade or to its domestic consumption or which were basic inputs for the development of Peru's domestic industry. He confirmed that State trading covered some 33 per cent of Peru's imports while on the export side, State trading covered mainly traditional exports, to the extent of some 80-85 per cent of Peru's total exports. State trading was mainly a tool for the national development strategy. The State had set up an infrastructure for external and internal marketing, although in some cases it resorted to private firms as well. In a few cases the measures extended into production as well as marketing.

22. In reply to questions concerning regional integration the representative of Peru recalled that the LAFTA Agreement and the Cartagena Agreement had been discussed in GATT. The aim of regional integration was to increase trade between the member countries, to optimize the advantages that could be derived from complementary industries and generally to encourage industrial development. There had been no significant reduction in volume of trade between the A group and LAFTA countries and the developed countries as a result of these agreements. Some members of the Committee welcomed these efforts toward regional integration. In this context one delegation asked whether it was Peru's intention, to eventually remove those non-tariff measures that favoured LAFTA and A group countries.

23. Members of the Committee noted that Peru has two bilateral trade and payments agreements; one with Hungary and one with Poland. They enquired whether there were plans to terminate these agreements. In reply, the representative of Peru said that the aim of these agreements was to ensure a certain continuity of trade in goods between the countries concerned. He specified that the agreements provided for payment in freely convertible currencies, that they were flexible in that they could be extended, revised or terminated when they came to expiration. At that time such criteria as world prices and quality of the goods traded were taken into consideration by the parties concerned. He added that under these agreements, which were of interest to Peru for the time being, the products involved for Peru were its traditional exports. Also involved were manufactured products such as mechanical and electronic products. In fact these were nearly compensatory agreements.

24. In reply to a question concerning exchange control (BOP/161, page 11, paragraph 2) the representative of Peru said that the requirement for external financing of private exports other than capital goods had not been eliminated, but that the requirement for an irrevocable L/C had been removed.

Conclusions

25. The Committee noted with understanding the balance-of-payments and development problems facing Peru. They also noted that the level of import restrictions, especially non-tariff restrictions, was high. The Committee, bearing in mind the International Monetary Fund's finding to the effect that the restrictions did not exceed those necessary to prevent a further decline in Peru's monetary reserves, also noted that development programmes, particularly in the petroleum,

phosphates and copper industries, could be expected to contribute in the near future to redressing the balance-of-payments position. The Committee expressed the confident hope that these new factors would soon place Peru in a position to start relaxing progressively its system of restrictions, and in particular would allow Peru to move away from reliance on non-tariff measures toward control of imports through tariffs only. In the meantime, the Committee recalled the provisions of Article XVIII:B, paragraph 10.