DRAFT REPORT ON THE CONSULTATION UNDER ARTICLE XVIII:12(a)
WITH ARGENTINA

1. In accordance with its terms of reference and as requested by the Council the Committee has carried out a consultation under the provisions of paragraph 12(a) of Article XVIII with Argentina concerning the quantitative import restrictions which it introduced on 30 June 1971, for the purpose of safeguarding the balance of payments.

2. For this consultation, the Committee had before it the following documentation:

(a) A document supplied by the Government of Argentina to serve as a basis for discussion BOP/122 and Add.1
(b) A notification of subsequent modifications BOP/127 and Add.1
(c) A paper supplied by the IMF on Recent Economic Developments in Argentina, dated 13 March 1972

The Committee also referred to earlier documents, notably:

(i) Original notification by Argentina of the introduction of the measure L/3587
(ii) Memorandum by the Argentine Government on the balance-of-payments position L/3615
(iii) Text of the relevant decrees and regulations L/3615/Add.1
(iv) Minutes of GATT Council (C/M/73 and 74)

3. The Committee generally followed the established plan for such consultations (L/3388, Annex I). The consultation was held on 23 June 1972. This report summarizes the main points of the discussion.

Consultation with the International Monetary Fund

4. 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 Argentina. Upon the invitation of
the Committee the representative of the International Monetary Fund made a statement, as follows:

"The Fund invites the attention of the CONTRACTING PARTIES to the paper on Argentina—Recent Economic Developments, dated March 15, 1972, which has been transmitted to the CONTRACTING PARTIES.

"In 1971 there was a sharp deterioration in both the current and the capital accounts of the balance of payments, and the overall deficit (including the allocation of SDRs) totaled about SDR 570 million, compared with a surplus of about SDR 300 million in 1970. There was a further SDR 180 million deficit in the first four months of 1972. Gross official reserves, which stood at SDR 673 million at the end of 1970, fell to SDR 267 million at the end of 1971 and to SDR 209 million at the end of April 1972.

"Exports declined by almost 4 per cent in 1971 as a result of a bad wheat crop and a decline in shipments of beef and other livestock-related products as farmers retained stock in response to rising prices. Imports rose by 12 per cent in 1971 with particularly substantial gains in imports of capital goods and petroleum. The increase in imports was a response to rising inflationary expectations and to the reactivation of the economy after a brief slowdown late in 1970. During the second half of the year, the authorities took several measures to discourage imports, including a temporary tightening of payments regulations, the imposition of a 15 per cent surcharge between November 1971 and February 1972, and the complete prohibition of imports of certain nonessential goods.

"During the period April-September 1971, the authorities followed a policy of small frequent adjustments of the exchange rate. On September 20, 1971, a dual exchange market was created in which the official rate remained pegged at $a 5.00 per U.S. dollar, while the financial rate moved in response to supply and demand. At the end of 1971, the financial rate was $a 8.25 per U.S. dollar, and in May 1972 it was $a 9.90 per U.S. dollar. Mixing arrangements, whereby specified proportions of exchange relating to trade transactions were to be negotiated in the financial market, were introduced along with the splitting of the market. In October 1971, 20 per cent of exchange for most exports and imports was to be negotiated in the financial market, and this proportion was raised to 30 per cent in December, 43 per cent in February 1972, and 64 per cent in March."
"In the middle of May 1972, the suspension of imports of certain nonessential goods was extended until June 30, 1973, and other less essential imports were shifted entirely into the financial market. At the same time, the Central Bank prohibited the sale of exchange for imports with less than 180-day financing except with the approval of the Central Bank. Argentina also levies a tax on sales of exchange for tourism, and prohibits remittances of profits, dividends, and royalties. However, those who are entitled to make such remittances are permitted to subscribe with pesos to interest-bearing, dollar-denominated bonds which are freely negotiable at home and abroad.

"The Fund believes that at the present time the general level of import restrictions of Argentina which are under reference does not go beyond the extent necessary to stop a serious decline in its monetary reserves."

Opening statement by the representative of Argentina

5. In his opening statement, the head of the Argentine delegation described in considerable detail the balance-of-payments position of Argentina in 1971, the underlying economic factors affecting trends in exports and imports and the capital account, the nature and scope of the import restrictive measures which the Government had adopted in mid-1971 in order to stop the threatened serious decline in foreign exchange reserves, the changes which had since been made in these restrictions in the light of a continuing external deficit, and the prospects for the balance of payments and international reserves during 1972. The complete text of this statement by Mr. Diz is reproduced in the Annex to this report.

Balance-of-payments position and prospects

6. The Committee thanked the representative of Argentina for the very full documentation which had been made available by the Argentine authorities, and for his opening statement which formed a useful basis for the consultation. Members of the Committee expressed sympathy with the Argentine Government for the economic and balance-of-payments difficulties that it faced, and understanding regarding the need for the measures that it had taken.

7. In the course of discussion, members of the Committee sought clarification on certain specific aspects of the Argentine balance of payments. Questions were asked, for instance, on the current livestock and wheat supply situation, and the reasons why supply had been so hampered in 1971. The representative of Argentina explained the complex nature of beef production and marketing. An increase in the expected relative price of beef (an expectation that the behaviour of prices in 1971 and 1972 tended to confirm) induces an increase in producers' desired flow of supplies to the market. But in order to increase these flows it was necessary to build up cattle stocks first. Since some of the final products in livestock marketing (cows, heifers and young animals in general) could also at
times be considered as raw materials for more finished products, current supplies were curtailed in order to expand stocks. Since the implicit biological process took time the gap between desired and actual stocks was only gradually closed. These inherent characteristics of the livestock cycle implied that adjustments took time (in fact, years) and that in periods of cattle stock-building (as was the case during 1971 and early part of 1972) current supplies were negatively affected and exports declined. Reduced cattle slaughtering during 1971 also affected exports of other livestock products as hides. In order to minimize the reduction in exports, the Government had taken steps to regulate domestic consumption; every other week was made a meatless week. These measures had been intensified in June 1972, when the meatless period was lengthened to two in every three weeks. At present the authorities were considering the opportunity of conducting a cattle census to ascertain the true size of the cattle stock, but less systematic available information indicated that market supplies would rise during the second half of this year.

8. Members of the Committee enquired whether the Argentine monetary authorities envisaged any plans to phase out or reduce the use of swaps which had incurred substantial losses in pesos for the Central Bank, why the crawling peg system, which seemed to have functioned so satisfactorily had been abandoned in favour of the more cumbersome two-layer exchange market, whether and when these multiple rates might be unified, and whether, in the view of the Argentine authorities, the use of the "financial rate" for commercial transactions had placed an additional protective incidence on the imports in question.

9. The Argentine representative replied that swaps had been arranged by the Central Bank at increasing levels of implicit interest rates which currently were at 22 per cent per year. This was part of a more comprehensive policy of adapting the domestic structure of interest rates to the prevailing inflationary conditions so that domestic yields could be sufficiently attractive to retain funds in the country. Central Bank losses on swap operations during 1972 stemmed from the rapid adjustment of the exchange rate. As the devaluation of the peso during 1972 was expected to be lower than that registered in 1971, it was to be expected that such losses would decline. The level of outstanding swaps which had reached $400 million at the end of 1971 was expected to be gradually reduced.

10. The actual operation of the crawling peg system in the early part of 1971 proved to be difficult as it was uncertain to what level of the exchange rate in real terms the system should be geared. The ongoing changes in leads in payments and lags in receipts made things still more difficult. The gradual increase in the proportion of trade payments, channelled through the financial market (at higher rates than those of the commercial market) had placed import costs and
export prices on a more realistic basis in view of the growing external deficit, and would eventually also serve the purpose of unifying the rates when all commercial transactions had been transferred to that market. This process had been resorted to for administrative convenience since there are differences between the legal requirements for the modification of exchange rates and for changing the proportion of different exchange rates used. At present foreign exchange related to most commercial transactions was negotiated up to 64 per cent in the financial market and the upward trend in this proportion would eventually bring about the unification of the two foreign exchange markets. As regard the "protective effect" of the system, the representative of Argentina pointed out that all effective devaluation, no matter what the administrative system chosen to achieve it, naturally increased the cost of imports in terms of local currency. After all, this was the very purpose of the measure.

11. A member referred to the current negotiations by Argentina with foreign banks and expressed the view that if these were successful and the performance of the balance of payments in 1972 was adequate, there should be a moderate increase in the level of reserves. Invited to comment on the scope and prospects of these negotiations, the Argentine representative stated that an agreement had been reached with the International Monetary Fund on the use of the first credit tranche equivalent to SDR 110 million or US$119.4 million. With respect to current negotiations with different groups of banks in twelve different countries, including the United States, Canada, Japan, EEC countries excluding Luxembourg, Spain, Sweden, Switzerland and the United Kingdom, it was expected that these agreements would amount to the equivalent of US$350-400 million approximately.

12. Members of the Committee, supported the findings of the International Monetary Fund (see paragraph 4 above) and considered that the balance-of-payments position faced by Argentina justified its action in mid-1971, to introduce the import restrictions and that the present position justified their maintenance. They expressed the hope that the various policies being followed would help to improve the position so as to enable the adoption of a liberalization programme in the near future.

Internal measures to restore equilibrium

13. Members of the Committee noted that the root cause of the external payments difficulties was clearly the rampant inflation which had progressively accelerated since mid-1969 and which seemed to have been given impetus by the credit expansion and other measures taken in 1970 and 1971 to counter the threat of recession. They expressed the hope that the 1972 financial programme to redress the internal and external equilibrium would be successful. In response to questions on various aspects of the internal stabilization policy put by members, the representative of Argentina stated that:
(a) as part of a firm monetary policy, new reserve requirements and more strict control of lending operations had been established. Previous policies on the expansion of short-term credit not been sufficiently restrictive and had the effect of increasing the demand for foreign exchange. Consequently, they had been modified;

(b) important decisions had been taken in the area of interest rates in order to adapt them to the inflationary conditions, to increase the cost of credit, and to afford domestic financial assets a better yield so as to increase their attractiveness relative to foreign assets;

(c) public debt bonds carrying an 8 per cent interest and a scaling clause according to the exchange rate of the dollar in the financial market, had been issued. Long-term public debt and private indebtedness were also being placed under control;

(d) delays in revenue collection, which had caused substantial losses to the State owing to inflation were being remedied. Ways of more prompt collection, such as the "pay-as-you-go" were being considered;

(e) a new law and new regulations governing foreign private investment, though only of a consolidative nature, should have the effect of encouraging capital inflow by way of clarifying the rules of the game;

(f) as regards the nature and scope of the economic programme agreed upon with the International Monetary Fund in connexion with the first credit trench drawing, the main objectives were to reduce the rate of inflation (currently at 55-58 per cent on an annual basis) and the balance-of-payments deficit while maintaining an acceptable level of economic activity and real wages. The main elements concern fiscal policy, with a substantial reduction in the government deficit in real terms, and monetary policy with a deceleration of net domestic credit;

(g) an incomes policy had also been established and price agreements had been reached with practically all of the main industrial firms, destined to increase their absorption of the recent wage increases.

Administration and effects of the restrictions

The Committee took note of the information given in the documents before it concerning the import restriction system in Argentina. In response to an enquiry, the Argentine representative stated that the May 1972 additions of the suspensions goods comprised nineteen items, and undertook to supply a detailed list of these additions to the Committee (see BOP/127/Add.1 of 30 June 1972). All items whose imports were suspended were therefore included in the lists in documents L/3615/Add.1 (original items) and BOP/127/Add.1 (new additions). Imports of these products represented the following proportions of total imports in the years 1969 to 1971:
The Argentine representative notes that since these imports were suspended in the second semester of 1971, the $28.3 million of imports for the first six months showed a considerable acceleration with respect to the amounts imported in previous years.

15. In reply to an enquiry on the relative importance of imports by the public sector, the representative of Argentina gave the following figures:

<table>
<thead>
<tr>
<th>Year</th>
<th>$ million</th>
<th>% of total imports</th>
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<tbody>
<tr>
<td>1969</td>
<td>30.0</td>
<td>1.9</td>
</tr>
<tr>
<td>1970</td>
<td>35.6</td>
<td>2.11</td>
</tr>
<tr>
<td>1971</td>
<td>28.3</td>
<td>1.52</td>
</tr>
</tbody>
</table>

During the first five months of application of the law suspending imports by the public sector the value of imports on account of exceptions permitted by the law amounted to $320 million. The value of 1971 total imports being $1,890 million, public sector imports (comprising those by the central authorities, the provinces and municipalities), represented slightly less than one quarter of the total.

16. Members of the Committee pointed out that this technique of import restrictions by totally excluding all imports of the products in question from the domestic market, inevitably afforded incidental protection to domestic industry and that it would be contrary to the long-term interest of the country if uneconomic production were thus stimulated and expanded. They enquired whether the Argentine authorities had taken into account the provisions of Article XVIII:10 of the General Agreement and taken the necessary precautions. The representative of Argentina said that in the grave emergency situation in which it had found itself last year, severe measures of a temporary character were needed to meet the balance-of-payments crises, precisely so as not to endanger the long-term interests of the country. In relation to Article XVIII:10 he considered that even if the incidental "protective effect" might not be insignificant, the restrictions were necessary in view of the acceleration of imports covered by the measure during the first half of 1971. In addition, the importance of the measure should be judged in relation with the other decisions also taken, particularly in the exchange rate field.
17. In reply to questions concerning the Argentine import deposit system, the Argentine representative stated that these deposits were applied at present to about 20 per cent of total imports and that the scope of their application had been reduced in May 1972 when 364 items were taken off the list. He agreed with members of the Committee that these deposits, by placing an additional burden on importers, certainly had an inhibitive effect on imports. The measure, however, had also liquidity absorbing effects which were important in a period of accelerating inflation.

18. The Committee discussed with the Argentine delegation the need and justification for exempting goods of LAFTA origin from the import deposits and the import prohibition. The representative of Argentina considered that this exemption was necessary in order to avoid disruption of the progress towards regional integration and that it was in accordance with the LAFTA agreement, which had been transmitted to the CONTRACTING PARTIES for examination. He also confirmed that the exemption did not apply to all imports from the other LAFTA countries, but only to products on which Argentina had assumed an obligation in the LAFTA negotiations; these comprised some 1,600 tariff items and sub-items, in which imports in 1971 amounted approximately to $300 million or about 15 per cent of Argentina's total imports. In the view of the Argentine authorities, the exemption had practically no trade diverting effect. Some members of the Committee stated that, while recognizing the necessity and desirability of economic integration in Latin America, they could not see why imports from particular countries should be exempted from restrictions which were applied on balance-of-payments grounds. In their view the exemption of intra-LAFTA trade from the advance deposit and the import prohibition was not consistent with the provisions of Articles XI and XIII of the General Agreement. The representative of Argentina stressed that discrimination against non-members was inherent in the nature of free-trade associations provided for in Article XXIV of the General Agreement. This was a matter of principle which he did not feel should be discussed in the context of this consultation.

19. A member of the Committee expressed the view that the method of customs valuation used by Argentina did not seem to follow the GATT rules and requested additional information. The representative of Argentina stated that the general system of valuation used in his country followed the Brussels Customs Valuation Convention. Exceptionally, and for a limited range of commodities, the Argentine authorities applied a method of official valuation involving reference to prices of three exporting countries, which did not imply, however, that they were determined on an arbitrary basis. Nor was the method applied in a discriminatory way. The system had been fully examined by the CONTRACTING PARTIES at the time of the Argentine accession to the General Agreement and, since it was found to cause no concern, had not called for any special recommendation. Furthermore, Argentina participated in GATT's Working Group on Customs Valuation and would give due consideration to its conclusions.
20. A member of the Committee expressed the view that the full application of the financial rate to imports of books was unjustified and was damaging to his country's exporting interests. The representative of Argentina said that the financial rate was being fully applied to an increasing number of items and that the proportion of financial market exchange had been gradually increased for all imports. Thus, these two processes were considerably reducing through time the relative exchange disadvantage for books.

Conclusions

21. The Committee expressed appreciation for the complete and clear documentation that the Argentine authorities had supplied for this consultation and the highly competent and thorough manner in which the Argentine delegation had responded to the various, sometimes difficult questions. The Committee expressed sympathy for the serious economy and external financial difficulties faced by the Argentine Government and expressed the hope that the current economic policy would be successfully implemented so that improvement in this regard, and the additional credit resources being obtained, would combine to ease the pressures on the balance of payments. The Committee hoped that the Argentine Government would soon find itself in a position to begin removing the restrictions.

22. The Committee, noting the findings of the International Monetary Fund quoted in paragraph 4 above, concurred in the view that the restrictions applied at present by Argentina were consistent with the provisions of Article XVIII:B.