

The Fund and Exchange Restrictions

Consultations in 1954

Beginning in 1952, member countries maintaining restrictions under Article XIV, Section 2, of the Fund Agreement have consulted the Fund each year on the continuance of these restrictions. During the third series of consultations beginning in April 1954, 40 member countries consulted the Fund on the further retention of their restrictive practices, either in Washington or in member countries, or, in the case of four countries, by a simplified procedure of exchange of correspondence.

The international economic climate has continued to be propitious during the last year for the reduction of restrictions on trade and payments. The increases in output and real income in many countries, the stronger competitive position of European industrial exporting countries, the more balanced distribution of monetary reserves, and the course of economic activity in the United States have already been examined earlier in this Report. Another favorable factor has been the continued maintenance of internal stability in a number of countries. Several countries, moreover, have dismantled a large part of their internal control machinery. When confronted with balance of payments difficulties, these countries are likely to find it more rational and convenient to restore equilibrium by means which do not involve the reimposition of restrictions.

One manifestation of progress toward convertibility has been the reduction of over-all restrictions, particularly in Western Europe and the sterling area. In some countries, indeed, there have been

movements in the opposite direction, and renewed payments difficulties have caused the reintroduction of restrictions which had earlier been relaxed or removed. The definite elimination of controls has sometimes been delayed by unwillingness to dismantle a control apparatus which it is feared may have to be re-established in the event of a deterioration of the payments situation. On the whole, however, world trade is less subject to restrictions than it was a year ago, and a large measure of freedom for trade and payments has been re-established. Some controls have been applied less rigorously without any formal change in the regulations themselves; regulations have sometimes been made less rigid and formalistic; and, finally, some controls have been definitely eliminated.

Fairly satisfactory progress has also been made in the reduction of discriminatory practices. Both in Europe and elsewhere there is less discrimination against the dollar area. Some ten member countries outside the dollar area (Belgium, Ethiopia, Greece, Indonesia, Luxembourg, the Netherlands, Pakistan, Peru, Thailand, and the Union of South Africa) make little significant distinction between their treatment of the dollar area and of other countries.

The importance of discrimination has also been diminished by the free transferability of deutsche marks within the non-dollar area, and by the widening of commodity markets in Western Europe. Goods purchased in these commodity markets against convertible currencies cannot as a rule be resold against inconvertible currencies; the regulations of the markets, however, permit authorized brokers to purchase and sell freely throughout the world, subject to certain general principles of exchange control.

The stringency of exchange restrictions on invisible transactions and capital transfers has been relaxed, particularly in Western Europe, and the restrictions that have been retained are less discriminatory against the dollar area. In several member countries, restrictions on investments abroad have been relaxed. In Belgium-Luxembourg and the Netherlands, the relaxation on capital transfers has been facilitated by the establishment of a free exchange market (see Chapter VIII). Although the arrangements made for this purpose can give rise to exchange rates deviating from parity by more than

one per cent, the Fund has regarded them as steps toward convertibility and has not objected to their introduction on a temporary basis.

Much less progress has been made in the elimination of multiple currency practices and similar arrangements, still used by a large number of countries. In some countries, however, these are used as an alternative to quantitative exchange restrictions. In any event, a mere enumeration of multiple currency practices does not indicate their importance for the world as a whole, for some of those that are still retained have little practical significance. In some cases, changes in multiple currency practices during the past year have reflected progress toward a unified rate structure. Nevertheless, because of balance of payments or other difficulties, a number of countries have found it necessary to intensify their multiple rate systems or to establish special exchange arrangements for exports for which there have been marketing difficulties.

A number of member countries are still confronted with payments difficulties, and in several of them the rate of progress toward convertibility recorded in recent years has not been maintained. Many underdeveloped countries use restrictions to cope with balance of payments difficulties generally associated with their investment programs, to assure supplies of certain categories of imports considered essential, or to protect infant industries. In countries whose economies are largely dependent upon the production and exportation of primary commodities, particularly coffee or rice, world price fluctuations have led to alternating relaxation and intensification of restrictions.

Some of the most important European exporting countries have made efforts to diminish the number and scope of their bilateral payments agreements. In many countries, however, bilateral arrangements are still regarded as a useful instrument of international trade and financial policy. Some countries practice bilateralism because they see in it a means for maintaining exports that are important in their trade while sometimes preventing a decline in the prices of these exports. They fear that it would otherwise be difficult for them to maintain or to expand the flow of their exports in the

face of state trading practices elsewhere and the balance of payments difficulties of some underdeveloped countries. Bilateralism is also sometimes used as an instrument to deal with the difficulties that arise when current commercial obligations fall into arrears. Debtor countries may use bilateral arrangements to give priority to sources of import supply where payment or credit facilities are available to them. Other countries wish in principle to get rid of bilateralism, but hesitate to deprive themselves of its protection as long as their competitors refuse to renounce bilateral arrangements or other countries retain such devices as agricultural import restrictions.

The picture as a whole during the 1954 consultation period is thus one of cautious but sustained effort, consolidation of gains linked with a desire to make further progress, and general improvement despite certain setbacks. General economic trends, both at home and abroad, are everywhere being closely observed as indicators of opportunities for further measures of liberalization.

Consultation Program for 1955

On April 1, 1955 the Fund began the fourth series of consultations provided for in Article XIV, Section 4, of the Fund Agreement. The consultation procedures approved by the Executive Board last year have been found to provide a flexible and convenient working technique which enables the Fund to discharge its responsibilities in this matter. In these consultations the Fund's main interest will be to ensure the maintenance of the current momentum in the relaxation of restrictions.

Member countries that need additional exchange resources if their currencies are to be declared or kept convertible can count on the Fund's assistance. Fund policy regarding the use of its resources also enables it to help those countries that, though not able to establish convertibility, seek to avoid the intensification of restrictions or to accelerate their relaxation or removal. The Fund's aim is to help to ensure that restrictive measures which are likely to compromise the success of movements toward convertibility are not taken.

In formulating Fund policy, account must, of course, always be taken of changes in the world economic situation. Economic con-

ditions in the United States and other industrial countries and the judgment of these conditions formed by other countries are always matters of great importance. As has been noted elsewhere in this Report, these conditions are currently favorable. Further constructive steps taken by countries with strong balances of payments to liberalize their trade and tariff policy would encourage other member countries to relax or abandon their restrictions. Such steps have an importance that extends beyond the volume of trade immediately affected, for they would have a strong influence on the attitudes of countries still maintaining restrictions toward the possibility of getting rid of them.

Within the framework of its general policy the Fund will, as in the past, endeavor to take proper account of any special difficulties with which individual members have to deal, while having regard both to the way in which restrictions may injure the interests of other countries and their effect upon the general movement toward convertibility.

If exchange measures are found necessary, they should be no more restrictive than is justified by the severity of the balance of payments difficulties that they are intended to relieve, taking into account the other measures which may be open to the members for this purpose. Without excluding other relevant factors, similar considerations apply in determining whether there is any justification for discriminatory measures against either individual countries or currency areas. This applies both to discrimination directed specifically against particular currencies and to discrimination that may result from bilateral arrangements. If they are to be effective, bilateral payments arrangements necessarily involve certain elements of discrimination that are contrary to the principles of the Fund. Moreover, for a country that practices discrimination, bilateralism, like other forms of un-economic restrictionism, stands in the way of the best use of resources. In addition, when, as at present, conditions for a return to general convertibility are becoming more favorable and certain countries contemplate this action as a possibility in the fairly near future, bilateral arrangements require particularly close scrutiny since they may impede further progress toward convertibility.

The procedure to be followed in the 1955 consultations with member countries under Article XIV was considered by the Executive Board on April 13. The Board decided that it would be appropriate to undertake a complete examination of the bilateral arrangements of the members consulted and examine with members, among other matters, the economic justifications for such arrangements.

Subsequently, the Executive Board, by a decision of June 22 (see Appendix I) adopted a general policy on bilateral arrangements that involve the use of exchange restrictions. The Fund stated that the objective of its policies and activities is the elimination of foreign exchange restrictions and the earliest possible establishment of a multilateral system of payments in respect of current transactions between members. The Fund welcomed the reduced reliance on bilateral arrangements, but considered that the improvement in the international payments situation makes it less necessary for members to use such arrangements. The Fund urged the full collaboration of all its members to reduce and to eliminate as rapidly as practicable reliance on bilateralism. In this respect the Fund recommended close cooperation of those members who plan to make their currencies convertible in the near future. Collaboration was also requested from countries whose domestic and foreign economic policies may adversely affect the balance of payments of other members.

The purpose of this decision is to avoid the persistence of widespread discriminatory restrictions that would impede the attainment and maintenance of convertibility. The Fund will have discussions with its members on their need to retain existing bilateral arrangements and their ability to facilitate the reduction of bilateral arrangements in other countries. The Fund will explore the possibility of an early removal of such arrangements and the ways and means, including the use of its resources, by which it can assist in this process. In its examination of the justification for reliance on bilateral arrangements, the Fund will, without excluding other considerations, have particular regard to the payments position and prospects of the member concerned.

The Fund has received assurances from many member countries that maintain multiple currency practices that efforts would be

made to move toward a unitary rate system as conditions permit. The Fund will continue to study with these members the prospects of unifying their exchange systems, taking into account the repercussions of multiple currency practices on the economies of the countries applying them and on the trade of other countries.

Finally, the Fund is concerned about the effects upon world trade of certain export promotion practices. The urgency of the problem of retention quotas and similar practices is no longer as great as it was, but other forms of export incentive have recently appeared which may cause distortion in trade currents. Whenever the Fund has had knowledge of practices of this type, it has discussed them with the countries concerned, particularly from the point of view of the obligations of the Articles of Agreement and of the repercussions that such practices might have on the trade of other member countries.

Article VIII, Article XIV, and the Transitional Period

The general obligations of member countries concerning restrictions on current payments are set forth in Article VIII, Sections 2, 3, and 4, of the Articles of Agreement. A member may not, without the approval of the Fund, impose restrictions on the making of current payments or engage in discriminatory currency arrangements or multiple currency practices vis-à-vis other members. Two exceptions to the rule of prior approval are specified in the Articles of Agreement. The first exception, set forth in Article VII, Section 3(b), covers restrictions imposed when the Fund has declared a currency scarce. The second is the subject matter of Article XIV, which, as a temporary measure during the postwar transitional period, permits members to maintain and adapt to changing circumstances restrictions on international payments in order to cope with their balance of payments difficulties. Temporary restrictions of this kind are commonly referred to as “transitional arrangements.” To qualify as transitional arrangements, the restrictions must have been in effect when the member joined the Fund, unless the member’s territories were occupied by the enemy, in which case it may also introduce new restrictions where necessary. The restrictions must be withdrawn

as soon as the member is satisfied that it will be able, in their absence, to settle its balance of payments in a manner which will not unduly encumber its access to the resources of the Fund.

For restrictions on payments imposed in accordance with Article XIV, prior Fund approval is not prescribed, and the extent to which the Fund is authorized to control their use is limited. The Fund has an obligation to report annually on all restrictions still in force under Article XIV, and Fund members have an obligation to consult the Fund annually as to their further retention. The Fund may, if it deems such action necessary in exceptional circumstances, make representations to a member that conditions are favorable for the withdrawal of any or all of the member's transitional arrangements. In making decisions on requests occasioned by changes and adjustments of the transitional period, the Fund is required to give any member the benefit of any reasonable doubt.

On the other hand, to all restrictions on payments, discriminatory currency arrangements, and multiple currency practices, which fall under the provisions of Article VIII, the rule of prior Fund approval applies.

At the present time 45 of the 56 members of the Fund still avail themselves of the transitional arrangements under Article XIV.

At the time of the Bretton Woods Agreement, it was recognized that special provisions permitting exceptions to the general obligations of members were required to deal with the problems of the transitional period. There is no indication in the Articles of Agreement of the duration of this transitional period, but it is logical to assume that the transitional arrangements were to be connected with the special difficulties that had arisen from the war. Generally speaking, most of the members of the Fund that still have balance of payments difficulties requiring the use of exchange restrictions no longer have to face problems related to war-caused conditions, and with the progress already achieved in the removal of exchange restrictions and the possibility of further advances toward convertibility, the question has arisen whether the maintenance of transitional arrangements is still justified. Moreover, the entry into force of the reviewed GATT rules concerning quantitative restrictions and

discrimination is linked specifically to the application of Article VIII of the Fund Agreement to a wider range of countries. At the time of writing this Report, the issues raised by these considerations were still being studied by the Fund.

Cooperation with CONTRACTING PARTIES to the General Agreement on Tariffs and Trade

A Fund mission attended, as observers, the Ninth Session of the CONTRACTING PARTIES to the General Agreement on Tariffs and Trade (GATT) which was held in Geneva, Switzerland, from October 28, 1954 to March 7, 1955. The major item on the Agenda of the Ninth Session was a comprehensive review of the General Agreement in the light of seven years' experience. The review resulted in proposals for a substantial revision of the Agreement, and for the establishment of an Organization for Trade Cooperation. These proposals have been submitted to governments for acceptance.

The proposals arising from the review of the General Agreement include a reaffirmation of its basic objectives and obligations, including the principle of nondiscrimination in trade and the general prohibition (with specified exceptions) of quantitative restrictions on imports, subject as hitherto to any requirements of existing domestic legislation; a renewed undertaking to prolong the period during which the tariffs of contracting parties are bound under the Agreement; the provision, in a special article, of procedures for dealing with the problems of countries in the early stages of economic development; and new provisions relating to export subsidies.

The Fund welcomes the proposal for the establishment of the Organization for Trade Cooperation and the decision of the CONTRACTING PARTIES to adopt measures designed to promote closer cooperation between the CONTRACTING PARTIES and the Fund. The Fund has in the past actively cooperated and consulted with the CONTRACTING PARTIES when they were called upon to deal with problems involving monetary reserves, balances of payments, and foreign exchange arrangements. It looks forward to further close cooperation in the pursuit of the common objectives of the Fund and of the CONTRACTING PARTIES.

As in the past, the CONTRACTING PARTIES consulted with the Fund in connection with other items on the Agenda of the Ninth Session. Members of the mission participated in the consultations conducted by the CONTRACTING PARTIES on the discriminatory aspects of the import restrictions applied by two governments for the purpose of safeguarding their balance of payments and monetary reserves. In this connection, the Fund transmitted to the CONTRACTING PARTIES the results of its consultations under Article XIV with governments which had initiated consultations under the GATT, and background material on the countries concerned. This material was taken into account and used in the GATT consultations. During the Ninth Session, the CONTRACTING PARTIES adopted the same procedures as in previous years for the conduct of consultations initiated in 1955 on the continuance of discrimination.