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## Tariff preferences for industrial products

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area preferences though it favours the formation of a single common market with an effective integration of industries there.

### **East-West Trade**

While the expansion of trade between Europe and Soviet-type economies is looked upon with sympathy (except for limitations due to Vietnam), no particular steps are being taken to expand US trade with these areas. Basically, there are very few types of commodities the US wishes to purchase from these countries, nor do they offer attractive pricing propositions. It is true that the US, on conceptual grounds, is seeking to improve commercial relations with the Soviet Union and Eastern Europe. However,

for the duration of the Asian conflict, trade limitations related to various aspects of military and economic security make trade expansion unlikely. The Trade Convention, in its summary position, opposes long-term credits to all Communist countries and also wishes to exclude from trade all products involving technical information, advanced technology or know-how. However, the American business community regrets recent Congressional proposals aimed at contraction of trade in non-strategic commodities with Soviet-type countries and supports the motion that the President be given discretionary powers to grant them most-favoured-nation tariff treatment. Furthermore, all local ordinances designed to discourage retail sales of imported products from Eastern Europe, should be outlawed.

## DEVELOPMENT POLICY

# Tariff Preferences for Industrial Products

by Dr Hans O. Schulte, Washington

The Kennedy Round has made it clear again that there are class distinctions in international trade. On the one side there are the 10 to 15 important industrial countries that hold the lion's share of world trade and between whom the negotiations proper of the Kennedy Round were carried out. On the other side there is the great number of developing countries in Asia, Africa as well as in Central and South America, that entered the Kennedy Round with the most sanguine expectations, but at Geneva played a minor role only. Their hopes and wishes by and large were disappointed if one leaves out of account the food aid programme within the scope of the international grains agreement as decided upon on principle. Neither have above-average tariff reductions been made for products which are of particular interest for the export of the developing countries, nor have any preferential foreign trade arrangements in favour of the less developed nations been agreed on. It is not even certain whether the developing countries will be granted the tariff cuts, as decided on at Geneva, immediately and to what extent instead of in five annual rates. Small wonder if representatives of the developing countries made the bitter remark that the Kennedy Round had been exclusively "a rich men's deal" and did not consider their wishes sufficiently.

### **Increased Exports of Manufactures?**

The major part of the developing countries' foreign exchange proceeds is still originating from the exports of raw materials. The share of raw material exports in these countries' total exports amounts to between 80 and 90 per cent. Therefore the less developed countries attach great importance to obtaining stable and optimum proceeds for their raw materials. According

to their opinion this target can be achieved best by the conclusion of international commodity agreements regulating the markets of individual products, i.e. that are to "guarantee" by a multitude of interventions production, prices and sales of the manufactures concerned.

However, hitherto progresses of international commodity policy remained most moderate. No more than five international commodity agreements—i.e. on wheat, sugar, tin, coffee, and olive-oil—have been accomplished so far, but only the international coffee agreement of 1963 should be of any practical importance to the developing countries' export trade.

Thus for several years already the idea to assist the developing countries in their trade with manufactures (semi-finished and finished products) is increasingly coming into prominence. Apart from the reduction of quantitative restrictions and other trade obstructions the granting of tariff preferences is regarded as one of the most important measures to be taken.

The developing countries are vigorously demanding tariff preferences for their semi-finished and finished goods in the industrial countries' markets, particularly since the first United Nations Conference on Trade and Development at Geneva in 1964. For one thing they substantiate their demand by pointing at the comparatively decreasing importance of their raw material exports—the share of these exports in the developing countries' total exports decreased from 87.2 per cent in 1955 to 82.6 per cent in 1965<sup>1</sup>—and at the little progress made as regards the organisation of international raw material markets. On the other hand

<sup>1</sup> Source: (also for the following data): UNCTAD-Dokument TD/C. 2./30/Add. 1, of June 22, 1967.

they emphasise that in the near future due to their low economic and technical level of development they will not be able—or with great difficulties only—to compete with products of the industrial countries and that therefore a preferential treatment in the field of tariffs would be justified. Only tariff preferences would enable them to gain a foothold in the industrial countries' markets and to realise export proceeds which they require, apart from their receipts from raw material exports, in order to finance imports of capital goods needed for their further economic expansion as well as for the servicing of their continuously growing foreign debts.

The degree of a possible detriment to the industrial countries' trade interests caused by the granting of tariff preferences to developing countries depends on the extent to which these countries' exports can be promoted by preferences. If the effects of such preferential arrangements are insignificant, then the risk to the industrial nations' markets is also minimal. Would, however, tariff preferences be an instrument of optimum efficacy for the promotion of the developing countries' trade, then of course the competing production sectors in industrial countries would have to put up with losses in certain markets.

#### Small Share in Trade of Manufactures

The economic significance of tariff preferences to the developing countries' exports of manufactures is difficult to judge. In 1965 the less developed countries' exports of semi-finished and finished products totalled \$ 6,400 million. Although this figure implies a doubling of export values in absolute terms vis-à-vis 1955, the share of the developing countries' exports of semi-finished and finished products in international exports of these goods is still very small. In 1955 it amounted to 6.6 per cent, decreased to 5 per cent until 1960 and since that year it rose but very slightly to 5.8 per cent in 1965.

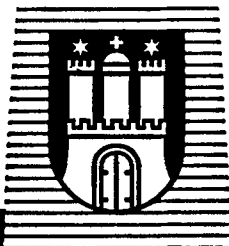
In 1965 the developing countries participated at only 9.5 per cent in the industrial nations' imports of semi-finished and finished goods. As compared to 1960 this is a reduction by 1.3 per cent and vis-à-vis 1965 one of 3.2 per cent.

The developing countries' exports of semi-finished and finished products are in the main supplied by a comparatively small number of about 15 to 20 countries. According to the above quoted UNCTAD-Document 65 per cent of the manufactures exported by them originated from but 15 main supplying countries in 1965. A similar situation exists with regard to the composition of goods. In 1965, 18 products or product groups, respectively—including mainly textiles, wood and leather products, and foodstuffs—represented approx. 75 per cent of the developing countries' exports to the Western industrial nations.

#### An Instrument with Limited Effectiveness

These figures alone suggest that the introduction of tariff preferences for manufactures from less developed countries would have but rather limited effects regarding the group of favoured countries as well as the number of products to be promoted through the granting of preferences. Nevertheless it cannot be disputed that tariff preferences would give the developing countries real competitive advantages concerning these products and would thus enable higher export proceeds. However, concerning the judgement of possible effects of tariff preferences not only those products matter that are exported already now, i.e. with the application of the most-favoured-nation tariffs. In particular those goods are also important which will possibly become competitive in the industrial countries' markets and thus exportable just by the granting of tariff preferences. In this connection, on the one hand, the volume of the developing countries' potential supply of those products is decisive, and, on the other, the degree of tariff protection still shielding the industrial nations' markets from these imports. This would suggest the "market-development-effect" that could be obtained at all by a certain reduction of tariff barriers. The developing countries' potential supply of exportable goods is difficult to estimate. A first clue is given by a commodity list worked out by GATT and UNCTAD<sup>2</sup>, including all those goods in the export of which the less developed countries are interested. Well-

<sup>2</sup> cf: GATT-Document COM TD/23, of June 29, 1966, and UNCTAD-Document TD/B/C.2/L.10, of February 9, 1966.



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established statements about the effects of tariff preferences on the developing nations' export proceeds could, however, only be made, if for every individual product, for which tariff preferences might be granted, detailed market analyses were worked out in order to ascertain possible increases of proceeds. Such investigations, that would be extremely difficult if not impossible at all due to the lack of statistical data, are not available so far. A first step in this direction is the study of tariff preferences in favour of developing countries, which the Bremen Committee for Economic Research has published on May 1, 1967.<sup>3</sup> In this study the Bremen Committee investigated by means of a very extensive analysis concerning the most important commodities as mentioned in the GATT and UNCTAD lists, what importance a possible granting of preferences by EEC would have for the developing nations' export proceeds.

The Bremen Committee's study leads to the result that exaggerated hopes of the effectiveness of tariff preferences for less developed countries are not justified. As regards products, that the developing countries export already now, the Committee does not believe impressive increases in proceeds to be possible by the application of tariff preferences. In many cases preferences for these products would only serve for supporting the superiority of some developing countries in certain markets, without, however, helping to diversify the range of export products.

#### Necessary Prerequisites for Exports

The Committee does not think much of the developing countries' chances of gaining a footing in the industrial nations' markets by selling new products. This attitude is due to the antiquated structure of production in most developing countries and their frequently exaggerated transport costs. In addition many of these countries are incapable of adapting the quality and design of their products to the industrial nations' requirements.

Therefore the Bremen Committee comes to the conclusion that tariff preferences are "an instrument of limited effectiveness" for the improvement of the developing countries' exports. To begin with everything depends on the creation of the prerequisites to the manufacture of exportable industrial goods in less developed countries. Their efforts as well as the

<sup>3</sup> The Bremen Committee for Economic Research, *Tariff Preferences in Favour of Developing Countries*, Bremen, May 1967. (Bremer Ausschuss für Wirtschaftsforschung, Zollpräferenzen zu Gunsten von Entwicklungsländern, Bremen, Mai, 1967)

industrial nations' aid measures will have to concentrate mainly on this task in the next few years.

#### How to Grant Preferences

All the same, the international discussion of granting tariff preferences for many manufactures from developing countries should not be underrated. The industrial nations' obligingness in this field would be regarded as a true proof of their helpfulness and might be considered a compensation for the insufficient results of development aid. The granting of tariff preferences would assuage the developing countries' growing dissatisfaction, which time and again they bring home to the international public particularly in UNCTAD, and would considerably improve the political atmosphere between the rich and the poor nations.

During the last years also within the group of Western countries the deliberations on the question of tariff preferences for developing countries have been intensified increasingly. Most important in this connection should be the activities within OECD, that at the end of 1965, following a decision of the Council of Ministers, appointed a special group—the so-called Group of Four—whose task it is to examine the chances for a promotion of trade between industrial nations and developing countries. High officials of the four most important Western trading countries—the United States, West Germany, Britain and France—belong to this group.

Today the opinion is prevailing within the group of industrial nations that preferences should be multilateral and not discriminating, i.e. they should be granted all developing countries by all industrial states in the same manner. However, as regards commodities to be excepted from preferential treatment and the protection of domestic production, different possible solutions are under discussion. In the Group of Four set up by OECD the representatives of the Federal Republic of Germany, Britain and France developed the idea of a tariff quota system. According to this system the duty-free imports—or those at a reduced tariff rate—of commodities from less developed countries would be limited to a quota amounting to a certain share (e.g. 3 or 5 per cent) of domestic production or domestic consumption, respectively, of the products in question. Another method would be the introduction of a general safeguarding clause, that in the case of troubles in the home market or of balance of payments difficulties would admit exceptions from the general granting of preferences. In a message to the Council of



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Ministers, dated November, 1966, the EEC Commission proposed to combine both instruments and to decide according to the situation in the individual commodity markets whether the tariff quota system or the safeguarding clause system should be preferred with the introduction of tariff preferences.

Regarding the duration of granting preferential arrangements there is general agreement that after a certain period the principle of the general most-favoured-nation treatment and non-discrimination in world trade should be restored and that thus the granting of preferences to developing countries should be temporary only. The abolition of a discrimination through tariff preferences is made possible by raising again preferential tariffs to the level of the general most-favoured-nation treatment or by a progressive reduction of the existing tariffs, based on the most-favoured-nation treatment, to the level of preferential tariffs. The last mentioned possibility has been emphasised in particular by the United States. Most of the other Western nations, however, advocate a restoration of non-discrimination by a time limitation of the preferential system or a gradual degression of preferential margins. Such a short time after the strains of the Kennedy Round they are little inclined to incur liabilities for further reductions of most-favoured-nations tariffs. It is not yet cleared up whether from the beginning a final date will be fixed as regards the limitation of preferential treatment, whether an accurate time table for the degression of preferential margins will be decided on, or whether it will only be agreed to examine and adapt the system of preferences after a certain period.

#### **The Problem of the Existing Preferential Systems**

The already existing preferential systems are a special problem for the introduction of general tariff preferences for developing countries. It is understandable that for instance the developing nations within the Commonwealth, allied with Britain, or those associated with the EEC do not wish to share their privileged position in the British or the Common Market, respectively, with the other less developed countries. They demand that, together with the introduction of a general preferential system, they should be granted other "advantages of at least the same value" by way of compensation for no longer existing benefits. What these compensations will be like in practice has not yet been defined so far. Many developing countries

demand financial compensations, others would agree to special trade concessions.

For good reasons the industrial nations reject financial compensations categorically. They take the quite plausible view that, if a general preferential system is introduced, the "compensation" to developing countries—which so far enjoyed preferences in industrial countries—will now consist in their preferential treatment by all industrial nations.

Which countries should be granted preferences is a question of fundamental importance. There is no such thing as a generally acknowledged definition of a "developing country". The United Nations use other criteria than for instance OECD. Particularly with some of the European countries—e.g. Greece, Spain, Portugal—and with countries as Israel, Mexico, Hongkong, etc., it will be difficult to decide whether they should be granted preferences or not.

#### **Difficulties not Unsurmountable**

Apart from the other fundamental questions—e.g. the inclusion of basic materials and farming products in the preferential arrangements—other also quite important technical and administrative problems would have to be clarified—administration of tariff quotas and questions concerning certificates of origin. Finally yet another "legal" problem remains to be solved: the granting of general tariff preferences to developing countries is an infraction of Article 1 of the General Agreement on Tariffs and Trade (GATT) of 1947. It may, however, be assumed that a solution will be possible either by a modification of Article 1 in view of the developing countries' special position or by granting a special regulation.

Summing up, it may be stated that the introduction of a system of general tariff preferences for developing countries is connected with numerous major difficulties, which, however, should not be unsurmountable if the most important countries participating in world trade are prepared to meet the less developed countries half way. Negotiations on the problem of preferences seem to become more topical in any case. A fundamental decision on the problem of tariff preferences for developing countries may be expected from the World Trade Conference at New Delhi in 1968. Therefore, it is about time that the Western nations, in particular also the EEC countries, come round to a common "negotiable" conception in order to enable a real success in this field at New Delhi.



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