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STATEMENT OF

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BEFORE THE

SUBCOMMITTEE ON INTERNATIONAL ECONOMIC POLICY

SENATE COMMITTEE ON FOREIGN RELATIONS

ON

INTERNATIONAL RULES GOVERNING TRADE

Mr. Chairman and Members of the Subcommittee:

We are pleased to be here today to discuss the preliminary information we have compiled in our work related to the international rules governing trade, a study we have begun at your request. As you know the basic objectives of this study are to analyze international trade practices and the discipline provided by multilateral and bilateral arrangements to cope with barriers to competitive trade. This work also builds on our past and ongoing work on the trading system which includes reviews of the Tokyo Round non-tariff barrier codes and sectoral studies.

In the aftermath of the tariff and trade wars of the 1930s and the economic devastation of World War II, international leaders recognized the need to develop an international framework through which gradual liberalization of trade could be realized and trade frictions discussed and resolved. The outcome of these discussions was the General Agreement on Tariffs and Trade (GATT). There are currently 88 contracting parties to the GATT. The trade discipline of the GATT is based on several key concepts, including that of the most favored nation principle or non-discrimination, national treatment, minimum protection, transparency, and dispute settlement through consultations.

The most favored nation concept essentially states that contracting parties will conduct their commercial relations with each other on the general basis of non-discrimination. National treatment implies that foreign firms should be treated on the

same basis as domestic firms involved in the same activities. The GATT recognizes the use of tariffs as the preferable mechanism of protection and encourages contracting parties to ensure that such measures are kept at a minimum level to avoid serious distortions to trade. The concept of transparency implies that a contracting party's regulations and procedures are open and unambiguous. Finally, bilateral and multilateral consultations are encouraged as the means to settle disputes. The GATT is also the only multilateral trade organization with a formal dispute settlement process.

From its inception in 1947 through the early 1970s, the GATT framework has achieved remarkable success in reducing tariff barriers to trade. It has also attempted to reduce non-tariff barriers. Since the late 1970s, however, the increasing use of protectionism in a number of different forms, has raised questions about the continued viability of the GATT principles and structure.

Our current study is intended to clarify the trade practices employed by individual countries and the applicability of multilateral and bilateral agreements to these practices. In the services sector, we are looking at the telecommunications industry, in the agricultural sector, wheat, and for safeguard issues, steel. To illustrate the scope of recent bilateral agreements, we have chosen Brazil as a case study.

Trade in services is becoming increasingly important in the world economy. The service sector, as defined by the United

States, consists of economic outputs which are not tangible goods or structures, including, but not limited to transportation, retail and wholesale trade, advertising, construction, design and engineering, utilities, finance, insurance, real estate, professional services, entertainment and tourism, telecommunications, and overseas investment associated with the export and sales of such services.

Telecommunications is one of the largest and fastest growing areas of world trade in services. The world-wide market for telecommunications equipment and services is estimated at $45 billion to $50 billion annually, with forecasts that the market could grow to $90 billion in 5 years. Accurate estimates of the totals and comparison of country data are difficult because of definitional problems and the manner in which services are included in balance of payments statistics.

Agriculture has long been an area of extensive government involvement through subsidies and quantitative restrictions on trade. At the GATT's inception, the United States supported special and differential treatment for agricultural products. The variety of exclusions, waivers and other special treatment provided by the GATT reflect U.S. concerns at that time. More recently, however, the United States has been in the forefront of those pushing for reforms. The dispute settlement process has been used extensively and has provided a forum for discussion of many of the problems in agricultural trade.

Each agricultural commodity presents its own unique trade problems. We have chosen wheat as a commodity for study because (1) its production and export are important to the United States, (2) a relatively large amount of world production is traded, and (3) a relatively large number of countries participate in the wheat market.

An increasing number of trade restricting agreements have been negotiated outside the GATT rules, particularly Article XIX, the safeguard provision of the GATT. Sector arrangements limiting competition are in place for a number of mature industries including textiles and apparel (the Multi-Fiber Arrangement), autos (US/Japan voluntary restraint agreement--VRA, European Community/Japan arrangements), steel (US/European Community voluntary restraint agreement on carbon steel and the European Community's 14 bilateral arrangements limiting imports of steel from various countries), and footwear. These actions are intended to protect industries subject to severe competitive pressures, and for some industries, it is hoped that necessary investment and structural changes will take place to make these industries more competitive. One criticism of these actions is that they tend to protect declining or inefficient industries. Furthermore, such actions also lead to trade diversion--i.e.--goods are diverted from the restricted market and flood open markets. These trade distorting effects are of concern to developed and developing countries alike.

Steel making is viewed as important by both developed and developing countries. Developing countries have invested heavily in steel making facilities. The steel sector in much of the developed world is an example of a mature industry affected by slowed demand and competition from newly industrializing countries. Additionally, the steel industry, as is true for other mature industries, is politically significant in developed countries because of its employment levels. Thus, support for protecting domestic steel-making capacity has been strong. A significant number of import restraint actions have been taken to protect domestic steel interests in developed countries.

While recent government actions in each of the above areas have been motivated by important domestic objectives, they are viewed with increasing concern because of their effect on trade. At the heart of these trade concerns is the extent to which such actions are undermining the trading system that has served us well in the postwar period. Because the principles and structure of the trading system are at variance with many of the actions undertaken in response to important domestic objectives, negotiations in these areas are likely to be very difficult. The fact that the United States and some of its trading partners are at odds over the appropriate role of the government in the economy, makes the definition of problems and their resolution all the more difficult.

In the following discussion, we describe some of the current trade problems and explain the difficulties that are likely

to confront negotiators attempting to deal with them in any new round of multilateral trade negotiations.

SERVICES: A GROWTH INDUSTRY NOT COVERED BY THE GATT

Generally speaking, provisions of the GATT are understood to cover trade in goods. At the 1982 GATT Ministerial meeting, however, the United States proposed that the contracting parties consider discussions within the GATT on service sector trade. Both developed and developing countries expressed significant reservations about this proposal. One problem is that each service industry has its own set of characteristics and concerns. It is unclear how general trade principles can be applied to all service industries. Countries expressed concerns that basic GATT principles such as national treatment and non-discrimination might not be desirable as disciplines for service trade, at least not without some revisions. The view was also expressed that it was not readily evident what benefits would accrue from such discussions or a potential agreement on service sector trade. Despite these reactions, the United States obtained agreement that contracting parties with an interest in services would undertake national studies of the issues in that sector. Some countries have submitted studies to the GATT and discussion on them has begun.

To date, the most comprehensive coverage of the service sector trade issue has been in the Organization for Economic Cooperation and Development (OECD). Specifically, member states of the OECD have agreed to three non-binding codes which have applicability to services.

1. The Code on Liberalization of Current Invisibles Operations calls for a halt in new restrictions on trade in services.

2. The Code on Liberalization of Capital Movements contains similar provisions for liberalizing foreign investment in service and other industries.

3. The Declaration on International Investment and Multinational Enterprise provides for national treatment in these areas.

In addition, OECD conventions of 1980 and 1981 pledge signatories to reduce and abolish obstacles to the exchange of goods and services.

Barriers to Trade in Services

Barriers to trade in services may take many forms. They may include investment performance requirements, exclusionary import policies, discriminatory treatment of foreign versus domestic firms, discriminatory government procurement, and government monopolies. The barriers may reflect economic or non-economic concerns, such as national security or individual privacy. Regulation of domestic service industries for domestic policy reasons has inhibited trade. The degree of restrictiveness of these barriers varies from one service industry to another; for example, insurance companies often face heavy restrictions in developing countries, while management consultants experience few restrictions on their activities.

Provision of telecommunications equipment and services is restricted to varying degrees by different countries. Developing countries tend to have fairly restrictive policies in an effort to reserve their domestic markets for indigenous producers. Market reserve policies of this nature tend to affect increasingly greater segments of the industry as indigenous capacity and technological know-how develop.

Brazil provides an excellent example of such a market reserve policy. The Brazilian government combines the use of import and export restrictions, investment requirements and various industrial policies to encourage the growth of its domestic computer and telecommunications capabilities. When a product or service can be provided by Brazilian companies, those respective market segments are protected to give the infant domestic industries time to develop. At the same time, foreign affiliates in Brazil are encouraged to shift toward the provision of more sophisticated products and services.

With few exceptions, most developed country markets are protected by monopoly post, telephone and telegraph (PTT) companies which most often are government-owned and operated. Until recently, the United States telecommunications market was dominated by a private monopoly. Within these monopolistic markets, there are varying investment requirements, tariff restrictions, interconnect restrictions, licensing requirements, local content requirements, and so on. Most of these restrictions are justified on the basis of protecting the integrity of the national telecommunications network and national security.

In the last few years, in addition to the break up of American Telephone and Telegraph in the United States, Japan and the United Kingdom have taken preliminary steps that may result in deregulating their telecommunications markets.

In Japan, the Diet is considering two bills. One proposes significant changes in foreign investment restrictions for providers of basic and enhanced services. The second bill proposes gradually privatizing Nippon Telephone and Telegraph, the domestic government-owned monopoly provider.

In the United Kingdom, the government has begun to liberalize and privatize British Telecommunications, the domestic and international carrier for basic and enhanced services. British Telecommunications' monopoly hold over the domestic market was broken with the government's decision to permit a second corporation to provide domestic long-distance services. The British legislature has also enacted a bill calling for the privatization of 51 percent of British Telecommunications to be completed later this year. At the present time, British Telecommunications still retains 95 percent of the market.

The flow and processing of information across national borders has caused increasing concern in many countries for economic, political and national sovereignty reasons. These concerns have heightened with the increasing convergence of computer systems and telecommunications networks.

Developing a well-defined international discipline in services

At the United States' initiative, discussions of a service sector agreement have begun both within the GATT and the OECD. The GATT Secretariat is beginning to receive studies by member countries examining the issues concerning service sector trade. The 1982 GATT Ministerial declaration also invited interested countries to review the results of these studies as well as information provided from other sources at the annual meeting of contracting parties scheduled for 1984. At that time, it was planned that the contracting parties would consider whether any multilateral action concerning services issues would be appropriate and desirable. As yet there seems to be no consensus on whether the trade in goods principles of the GATT can apply to services trade. Neither is there a consensus among the contracting parties that development of a services agreement is desirable.

The United States believes that GATT is the appropriate forum for discussions on this issue because (1) its membership is larger than that of the OECD and includes both developed and developing countries and (2) GATT provisions are binding, while those of the OECD are not. These same two factors, however, are also those which will make agreement exceedingly difficult to achieve.

Similar discussions in the OECD have progressed somewhat further. OECD protocols and agreements, although non-binding and limited to developed country participation, have historically been construed to apply to trade in goods and services, and thus

initiating discussion in this forum has not been as difficult. Discussion of these issues in the OECD is also easier because of the more common interests of its developed country membership, although agreement is still not easy to achieve.

The OECD Trade Committee, Working Party on Services has embarked on an ambitious effort to identify the nature and extent of barriers to service sector trade in its 24 member countries. In addition, this Committee has held extensive discussions concerning the potential application of basic trade principles to trade in services.

The trade principles of primary concern in services trade are non-discrimination (or most favored nation treatment), national treatment, right of establishment, minimum protection, and reciprocity. At present, there appears to be some agreement that the principle of non-discrimination could be applied to services on a conditional basis. However, some countries are concerned that applying non-discrimination on a conditional basis would imply reciprocal treatment and could lead to a more restrictive environment than currently exists in services trade.

The applicability of the national treatment principle to services is not so straightforward and has resulted in considerable debate among OECD members. These discussions have focused primarily on the extent of national treatment coverage. In other words, should national treatment apply to (1) imported services, (2) the ability of service companies to establish operations in

foreign countries, and/or (3) the "rights" of a foreign subsidiary once it has been established in a host country? Generally speaking, there is consensus that national treatment could not apply literally in services, and that exceptions to this principle would have to be clearly and carefully defined. Adopting a principle of national treatment in and of itself, however, would not ensure open trade. For example, the existence of national monopolies in the telecommunications industry could preclude operations by both domestic and foreign firms without violating the national treatment principle.

An additional principle being debated in the OECD deals with minimizing the level of regulation applicable to service industries. The debate focuses on host country regulations affecting service industries and the extent to which these are considered reasonable. This principle parallels the GATT principle of minimizing protection granted traded goods.

In both the OECD and GATT forums, a significant amount of work must be done before meaningful negotiations on a discipline governing service sector trade can begin. The applicability of the issues discussed above to each specific service industry must be fully assessed. Agreement must be reached on the "applicability" of GATT to service sector trade and the usefulness of trade in goods principles to service sector trade. Moreover, the concerns of the developing countries with regard to any discipline that is finally concluded must be resolved.

At present, it would appear that negotiations on trade in services are likely to be approached through consideration of

principles that could relate to all service industries and concerns unique to each service industry or like grouping of service industries. It is conceivable that agreement may be achieved on the general applicability of the principles discussed above. However, our discussions with numerous government officials indicate that this general agreement would have to be carefully analyzed in terms of its impact on specific industries within the service sector. Given this and the significant reservations expressed about a discipline on services by both developed and developing countries alike, negotiations on both a multilateral and bilateral basis are likely to be protracted and difficult.

EXCEPTIONS REMOVE TRADE IN AGRICULTURAL PRODUCTS FROM GATT DISCIPLINE

Many of the problems in agricultural trade result from policy decisions by countries in support of important domestic objectives. These include the price of food, self-sufficiency and security of supply, and raising the income level of farmers. As a result, domestic policy objectives tend to override trade considerations making negotiations difficult.

The problems in developing and enforcing rules for agricultural trade are very basic. To begin with, there is no internationally accepted definition of the term "agriculture" as used in trade and it is not defined in the General Agreement. GATT articles exempt trade in primary products from some of the disciplines applied to trade in manufactured goods. For example, Article XVI specifies that the contracting parties should seek to avoid the use of subsidies on the export of primary products but

then goes on to describe the conditions such subsidies should meet if they are granted. These conditions include, among others, the requirement that countries should not gain more than an equitable share of world export markets. Substantial disagreement exists over defining both what is a primary product and what is a country's equitable market share. Article XI, which generally prohibits the use of quantitative restrictions, allows such restrictions on agricultural products when they are necessary to enforce domestic marketing or production programs or to remove temporary surpluses.

Because of the problems arising in agricultural trade, the work program of the 1982 GATT Ministerial established a Committee on Trade in Agriculture to examine all measures affecting trade, market access, and competition and supply in agricultural products, including subsidies and other forms of assistance. This examination is to be made with a view toward achieving greater liberalization in trade and greater transparency. The Committee is to make appropriate recommendations to the GATT Council.

GATT's Committee on Trade in Agriculture reported last fall that submissions from 23 countries and the European Community showed an extensive panoply of restrictive practices affecting both imports and exports, which were often justified through GATT Articles. These practices include customs duties, sanitary and phytosanitary regulations, various prohibitions, state trading enterprises, quotas, subsidies, various forms of price supports, and voluntary restriction agreements.

Dispute settlement mechanisms in both the General Agreement and the Subsidies Code have been used to discuss and mediate problems in the international agricultural arena. Disputes between the United States and the European Community over exports of wheat flour and pasta both resulted in GATT panel examinations and reports. Each party refuses to accept the panel report which found against its practices, however, and bilateral negotiations are ongoing.

There have been some pressures for change in domestic agricultural programs which may have an impact on trade. These have been prompted, however, not by trade considerations but by domestic financial constraints. Generally speaking, the cost of maintaining farm programs is very high in most countries. For example, close to 70 percent of the European Community's budget goes to maintain price support programs under its Common Agricultural Policy. Increasing program costs and the expected enlargement of the Community have led to a new set of programs in the EC which may lead to fewer surpluses and therefore less need to export with the help of subsidies. Reductions in agricultural subsidies, as part of an overall program to reduce public sector expenditures, have taken place in Brazil in response to that country's international debt problems. Even in the United States, pressures resulting from increasing agricultural costs and budgetary deficits have led to changes in domestic programs.

Attempts to deal with trade issues are continuing. As noted above, the GATT is currently engaged in an exercise to have countries identify all practices in their agricultural sectors. A similar effort is underway in the OECD. There are also some discussions underway in these multilateral and other bilateral forums to establish new rules of appropriate behavior in agricultural trade in an attempt to bypass, and therefore solve, current differences in interpretations of existing rules.

Despite these efforts it is unlikely that an agreement to substantially liberalize agricultural trade will be concluded in the near future. The reality of large and politically influential farm sectors in many countries limits room for negotiation.

PROTECTIVE ACTIONS TO SAFEGUARD DOMESTIC INDUSTRIES

While the GATT is primarily focused on liberalizing trade in goods, one important exception is Article XIX, the safeguard clause. This clause provides the general framework under which signatory nations may take emergency measures to restrict imports when they threaten a domestic industry with serious injury. The key provisions of this Article are that

--serious injury must be present or threatened;

--this injury must be caused by the imports in question;

--consultations concerning any action to be taken should take place between the country taking the action and those it is most likely to affect; and

--if no agreement is reached during such consultations, the affected parties have the right to withdraw substantially equivalent trade concessions.

Article XIX provisions and other GATT articles have been interpreted to include the concepts that actions should be temporary and applied in a non-discriminatory, or most favored nation fashion. In addition, countries taking safeguard actions must notify the GATT of these actions, thereby ensuring transparency in the process.

The stringency of these features, particularly the serious injury standard, the requirement that safeguard actions be applied on a most favored nation basis, and the potential for demands for compensation, has made recourse to Article XIX a last resort measure. The drafters of Article XIX clearly intended to make its use exceptional rather than normal and routine. Indeed, the growing number of protective measures taken outside the framework of Article XIX and the GATT indicates that coutries do find the requirements burdensome.

The devices used most often in lieu of formal safeguard measures are informal arrangements, voluntary restraint agreements and orderly marketing agreements. There is flexibility in the design of these arrangements and they may or may not involve government participation. They are limited in scope and generally applied on a selective and discriminatory basis. Detailed information concerning these agreements is often restricted to the small group of countries directly involved. In addition, such actions have been taken when the GATT standard of injury has not been demonstrated. These actions are often referred to as grey area measures, so-called because their status under the GATT has not been determined, since they have not been brought into the GATT framework.

Attempts to develop a safeguard code

During the Tokyo Round of the Multilateral Trade Negotiations, there was an unsucessful attempt to negotiate an elaboration of Article XIX in the form of a safeguards code. Several critical features of the proposed code were not resolved, including (1) whether an action should be applied to the exports of a limited number of countries or to all exporters, (2) how to determine what constitutes injury, (3) the proper role of domestic adjustment mechanisms used in tandem with import restraints, and (4) whether there is a need for preferential treatment for the developing countries.

The 1982 GATT Ministerial work program called for the development of a comprehensive understanding on a more efficient safeguard system, to include the elements of

--transparency;

--coverage;

--objective criteria for action including the concept of serious injury or threat thereof;

--temporary nature;

--a progressive liberalization and structural adjustment;

--compensation and retaliation; and

--notification, consultation, multilateral surveillance and dispute settlement, with particular reference to the role and functions of the Safeguards Committee.

Although some countries' positions have moved closer to agreement in the intervening time period, progress toward reaching formal agreement has been extremely slow.

In part because of the slow pace of discussions, the United States and Canada have recently concluded an understanding on safeguards. The understanding sets out the procedures which the two countries will follow in applying any safeguard action which affects the trade of the other.

Actions in steel trade

The current lack of urgency in establishing a new code may, in part, reflect the ability and willingness of countries to take grey area measures. The steel industry provides some illustrations.

On a global basis, steel is a mature industry, one for which there is excess worldwide capacity and poor prospects for growth in demand. There are marked differences in the industry on the national level, however, with a number of countries establishing and expanding modern facilities, and differences on the sub-national level. For example, in the United States a profitable competitive minimill industry segment has developed in certain product lines.

As domestic demand in most steel producing countries has decreased, exports have become increasingly important. This in turn has led to greater pressure in importing countries with their own steelmaking capacity to limit increasing imports. Countries have used various means to restrict trade.

A number of actions have been taken outside the provisions of Article XIX. These include the following.

--The United States has entered into an agreement with the European Community to restrict the imports of steel into the United States in 10 product categories through 1985. This agreement resulted from a request by the European Community to enter into such an agreement after affirmative determinations were found by the United States regarding EC dumping and subsidy practices.

--Although there is no formal agreement, Japanese exports of steel to the United States have remained at a fairly constant percentage share of apparent consumption.

--The European Community has negotiated bilateral arrangements to limit steel imports to the EC with 14 countries.

Reactions to the U.S. safeguard actions taken under provisions of Section 201 of the Trade Act of 1974 on behalf of the specialty steel industry provide examples of the frictions which result even when all the rules are followed. In several discussions with European officials and producers, the U.S.-EC dispute over this case was cited as one of the most contentious and troublesome industrial problems between the United States and the Community. Even though the United States met all the criteria for taking a safeguard action, agreement between the United States and the Europeans on retaliatory measures was almost not reached.

A different type of problem regarding this case involved Brazil. Brazil has stated that, although mechanisms appear to be in place which provide recourse to countries against whom restrictive actions are taken, Brazil, in fact, has no options. Because of the international debt crisis, Brazil is importing only essential items from the United States. Therefore, if no mutually acceptable arrangement to limit the imports of Brazilian

steel under a safeguard action can be negotiated, Brazil has few opportunities to withdraw substantially equivalent concessions without incurring additional costs.

The GATT safeguard provisions for the most part are designed to deal with emergency situations in which import surges injure or threaten to injure a domestic industry. The problems of the steel industry however, appear to go beyond trade issues. The European Community has underway an ambitious domestic program to cut substantial capacity and modernize the steel industry in member countries. According to EC officials, import restrictions do not play a major role in that process. In the United States, import restrictions have played a much larger role in policies toward the steel industry. Japan is just beginning to face similar problems as its steel imports are increasing.

Future discussions in the international arena on appropriate safeguard actions and procedures may likely focus on (1) limits on the types and conditions of unilateral actions which countries take to ensure that protection of uncompetitive industries is temporary or (2) requirements that such trade actions will be accompanied by domestic programs that have genuine industry adjustment as their goal. There is as yet no apparent consensus on those issues. In general, these problems reflect the wide divergence of views on the appropriate role of government in industry decisionmaking.

THE RISE OF BILATERALISM

We are also looking at the rise of bilateral trade arrangements and resulting trade issues from the perspective of identifying in one country new forms of export competition practiced by U.S. trade competitors in three sectors of great commercial interest to U.S. business--energy, aircraft, and informatics.

We chose Brazil as our case study, first, because last year the United States signed several bilateral trade accords with Brazil in the energy area which were meant to match the trade practices of certain European countries and, second, because Brazil's trading environment is characterized by industrial policy and debt-related import restrictions now common in many countries. Our focus is on our trading competitors' responses in exporting to such a trading environment and the trade issues affecting U.S. interests that have emerged as a result of these different responses.

The bilateral trade practices we have identified so far as important or emerging competitive factors in exporting to these sectors include (1) exclusionary government-to-government agreements, (2) financing practices, such as countertrade, bilateral clearing accounts, and export credits at below-market interest rates, and (3) compliance with trade-related investment performance requirements, such as technology transfers and export obligations.

For the most part these practices are not governed by existing multilateral trading rules, and we are seeking to learn

Whether U.S. firms are able and willing to compete in this environment and whether the U.S. government should assist these firms.

Bilateral trade agreements

Over at least the last decade, the Brazilian government has used detailed, government-to-government agreements as the basis for awarding long-term major projects contracts for some sectors.

Early in 1983 the U.S. government recognized such bilateral accords as the only method of gaining access to significant sectors of Brazil's large energy market. In April 1983 it signed several similar accords, or Memorandums of Understanding (MOUs), with the Brazilian government for developing Brazil's hydroelectric and thermoelectric resources. These accords, publicized in the United States as a flexible response to competitors' trade practices, are potentially significant as an instance where the U.S. government response to an exclusionary practice has been to imitate it. Brazil, like most developing countries, has not signed the GATT Government Procurement Code, and so the United States has had no basis to complain about its trading competitors' acquiescence to Brazilian government purchasing practices.

At the time these accords were signed, the Deputy Secretary of Commerce said that, if they were successful in Brazil, they could lead to similar agreements with other countries not subject to the GATT Procurement Code. In our present review we are seeking to learn (1) how these accords are working to help American exporters gain access to the Brazilian energy market, (2) how the

benefits offered by the U.S. accords compare with those offered by trading competitors' accords, and (3) to what extent such bilateral trade practices occur elsewhere in the world.

Preliminarily, we have found the accords to be moving on schedule in terms of American businesses working together with Brazilian partners. A major uncertainty for both U.S. and Brazilian firms, however, is the availability and terms of Eximbank financing for these energy projects, which are expected to total $1 billion in U.S. exports to Brazil over the next several years. Eximbank, unlike some European export credit agencies, does not establish lines of credit for countries and objected to any mention of Eximbank support in the U.S.-Brazilian agreements. In the fall of 1983, it did, however, announce a $1.5 billion facility to guarantee the financing of exports to Brazil. This facility is not specifically tied to the agreements.

In contrast to the detailed agreements signed between Brazil and other countries, the U.S.-Brazil agreements do not specify financing sources or individual firms; rather, they simply express the intent of the Commerce Department and the Brazilian Ministry of Mines and Energy to work together to facilitate the participation of their private sectors in reaching commercial agreements.

Elsewhere in the world, we have not so far found many instances of government-to-government trade agreements of the type U.S. competitors have signed in Brazil. Nevertheless, some trade

competitors, because of close government, banking, and business ties, are able to put together and negotiate complete project packages, and these in effect resemble their accords with Brazil.

Within the government there appears to be some uncertainty whether to more actively pursue such bilateral trade agreements. Commerce officials have cautioned that widespread use of such bilateral arrangements could encourage U.S. competitors to sign more explicit and exclusive agreements with less developed countries, resulting in the exclusion of U.S. suppliers and in increased subsidized export financing by other countries.

Nevertheless, the U.S. experience in Brazil with its bilateral arrangements has so far been positive, and further agreements are contemplated for access to other market sectors in Brazil.

Countertrade

Another trade practice emerging as a potentially important competitive factor and trade issue is countertrade. For financially troubled nations such as Brazil, which have been forced to cut imports in order to conserve foreign exchange to service their debts, countertrade can be a device to support imports. In our review, we are seeking to learn whether Brazil, in choosing among exporters vying for its markets, considers willingness to countertrade a significant factor, whether U.S. competitors are responding to this interest, and whether U.S. exporters are able to match the competition's abilities to countertrade.

Countertrade, often thought of as merely barter, actually encompasses an array of trade practices which do involve some exchange of money. Broadly stated, a countertrade transaction obliges the seller to purchase certain goods from the buyer as a condition of the transaction in order to offset the original purchase and reduce the outflow of scarce hard currency.

In our Brazil study, we have encountered various forms of countertrade and some instances where it appears to have been an important competitive factor. The Brazilian government does not formally promote countertrade, although it did create a state agency in 1976 to countertrade for its oil imports and it has set up bilateral clearing accounts with several East European and Latin American nations. However, as a condition for imports, Brazilian industry often seems to require some form of offset arrangement, guarantee of exports, financing package, and/or licensing agreement. We hope to learn more about countertrade activities in Brazil through a questionnaire of U.S. businesses involved in Brazil.

Although countertrade threatens an open, non-discriminatory multilateral trading system by foreclosing market sectors from competition based on price and quality, its use is not governed by the GATT. Current U.S. government policy generally opposes government-mandated countertrade, but on a recent occasion the government did engage in a barter arrangement for Jamaican bauxite. Otherwise, it seeks to remain neutral regarding privately-arranged trade deals.

Within the U.S. business community, on the other hand, there is a developing trend toward gearing up for increased use of countertrade; businesses and banks have established their own countertrade groups and export trading companies also serve a countertrade function.

An important trade question, we believe, is whether countertrade is a temporary phenomenon accompanying the current world recession or whether it may become an institutionalized practice as businesses become adept at finding profits in it. For the time being, in any case, most studies report countertrade to be growing in developing countries, and its importance as a competitive factor for U.S. exporters needs to be more clearly assessed.

Export financing tactics

Concessionary financing practices have been part of the competitive environment for many years, but have become increasingly important as a result of the debt problems of many U.S. trading partners.

During the late 1970s and early 1980s, foreign competitors seeking to export to Brazil were willing to provide a type of untied loan, known as parallel financing, in addition to the official export credit loan, to meet general balance-of-payment or local cost needs. Such loans are not covered by the OECD Arrangement on Export Credits, which governs such aspects of official export credits as loan terms and interest rates. These types of parallel credits have virtually dried up in Brazil over the last few years since most lenders have already reached their

debt exposure limits; but they could reappear as the debt situation improves.

Another financing tactic of increased interest now in Brazil is leasing, because International Monetary Fund financing conditions focus on improving Brazil's export balance and leased equipment is not recorded as an import in Brazil's balance of trade. Little is known currently about the increased use and trade implications of leasing, which as a financial service is not covered by the GATT. The U.S. government is making studies on this subject, and we also plan to collect information on competitive factors in this area.

The use of mixed credits (e.g., aid blended with official export credits) has not been a major competitive factor in Brazil, since France, West Germany, and Japan have not recently had large aid programs there. Mixed credits, however, continue to be an important competitive factor elsewhere in the world. U.S. competitors' aid programs are not as closely defined as those of the United States, and they have had more flexibility to offer the very low-interest mixed credits that our Congress has now directed Eximbank to match on appropriate occasions. The United States within OECD has supported increasing the grant element of these mixed credits to clearly distinguish them from commercial transactions, but has not so far been successful.

In terms of relieving Brazil's recent debt problems, however, the United States has led its competitors in providing financing as part of the debt renegotiations and did take the unusual step last fall in announcing the $1.5 billion Eximbank loan guarantee facility.

Compliance with trade-related investment performance requirements

In sectors where Brazil has active industrial policies, such as informatics and aircraft, an emerging key factor vis-a-vis U.S. trade competitors is likely to be willingness to comply with Brazil's trade-related investment performance requirements. These requirements, increasingly frequent around the world, usually include local content, technology transfer, and export obligations. They also involve transferring majority equity to Brazilian partners. Through our questionnaire of U.S. businesses, we hope to get some information about how foreign competitors are responding to these Brazilian requirements. As you know, the U.S. government sought at the November 1982 GATT Ministerial to get investment performance requirements included under GATT discussions, but was not successful. Instead of continuing to press investment concerns multilaterally, the government has recently shifted its immediate strategy to negotiating bilateral investment treaties.

ADDITIONAL OBSERVATIONS

As we have mentioned throughout our discussion, the issues facing trade negotiators today are highly contentious, primarily because they involve discussion of issues which heretofore have been almost completely within the realm of national policymaking. The increased interdependence of countries in the last decade has made it more and more difficult to ignore the international consequences of domestic policy decisions. That most of these decisions are taken in response to important domestic concerns in no way limits their impact in the international arena.

U.S. trade negotiators are currently discussing the need for and agenda of a new round of multilateral trade negotiations. The impetus behind these discussions is a concern that the liberalization process achieved in previous GATT rounds is threatened by the recent increase in trade restrictions.

The general premise that discussions in the GATT and OECD on current trade problems should continue is widely held. However, the necessary preparation for a new round of formal negotiations, which would include the problems surrounding safeguards, services and agricultural trade, is substantial. A consensus on key underlying principles needs to be reached before formal negotiations begin. Without such a consensus it would be difficult to conduct constructive negotiations and the likelihood of concluding a meaningful agreement would be reduced. Inadequate preparation for a new round of multilateral trade negotiations could result in failed negotiations and have serious implications for the trading system.

This concludes my statement, Mr. Chairman. I would be happy to answer any questions you may have.