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EC – Association Policy

An Interview on Development and Association Policy with Herbert Westerich, President of the Hamburg Chamber of Commerce.

This October the EC and 43 associated and associable countries of the Third World are entering into negotiations which will occupy them for about a year. The 43 developing countries have already presented one of their most important demands: That the Community is to dispense with reciprocal preferences. Should this claim be accepted by the EC?

There are, as I see it, two aspects to the demand to do without reciprocal preferences. One involves the question whether the exporting industries can "afford" and ought to do without these preferences. That is I think a question which can be answered in the affirmative, certainly for the German economy as a whole.

The other aspect has to do with the most-favoured-nation principle of Gatt: if the reciprocal preferences are given up, the relationship known as association can no longer be justified as a sum total of free trade agreements, which could have the consequence that the preferences still granted to the as-

sociated states should at least be conceded likewise to all the other developing countries. Whether the reciprocal preferences of the associated states could be offset in other ways, e.g. by assurances concerning legislation on investments, without contravening GATT is still an open question.

The Hamburg Chamber of Commerce has long been in favour of gradually transferring the part of the association agreement which pertains to trade policy to the system of generalised preferences. Its sudden cessation however would raise the question of repercussion on the policy of integration and in particular the French reaction. A provisional solution is perhaps provided by the idea of the Commission that the Community though not dispensing with reciprocal preferences should leave it to the associated and associable states to decide whether or not they want to grant reciprocal preferences.

Other demands by the 43 developing countries included

greater liberalisation of EC imports, especially agricultural products, price guarantees for raw materials to cover their costs, and increased financial engagement by the EC in these countries. How are these demands viewed in business circles?

Price Guarantees for Raw Materials

From the Hamburg point of view I can subscribe in principle to the demand for greater liberalisation of Community imports, especially for agricultural products. The views of the negotiating parties will however still have to be set out in greater detail before a final judgement is possible.

As regards price guarantees for raw materials I may point out that the Hamburg Chamber of Commerce drew up detailed comments on the proposals of the Commission at the end of July. Detailed discussions with the circles interested in such imports, the traders as well as manufacturing industry, have convinced the Chamber that for

reasons of principle as well as in the light of practical considerations the proposed stabilisation mechanism cannot be considered an acceptable model for development policy.

Points of Criticism

What are your objections to the proposals of the Commission?

In the first place, the stabilisation measures in question are not of a kind to promote and encourage the indispensable efforts which the favoured countries themselves must make to adapt their production of basic materials to the requirements of the world market. On the contrary, it must be feared that the envisaged adjustment for the difference between actual export value and reference value will tempt them to produce "for the reference price" and thereby miss the market.

Secondly, the incentive for the favoured countries to turn to subsequent processing stages will be the smaller the more safeguards and encouragement are provided for raw material exports by means of export guarantees. This being the case, the stabilisation proposals would probably strengthen the tendency in the favoured countries to retain the role of raw material supplier and neglect the vertical diversification which is desirable for development.

Furthermore, it must be feared that the proposals of the Commission for the favoured countries will make for inflexibility in the regional distribution of their exports. In order to avoid manipulation by diversion of exports the Commission wants to take precautions based on the premise that the raw material exports from the favoured countries to the Community and to third countries will continue at a more or less constant ratio. Such a fixation of the regional

distribution of the exports however can operate to the detriment of the favoured countries by limiting their choice of the most advantageous outlets.

A Heterogeneous Group of Countries

When the future relations with the associated and associable countries are decided, more consideration should also be given to the fact that they are a very heterogeneous group of countries which differ greatly as regards their state of development. We believe that the Commission's system for the stabilisation of earnings is likely to benefit mainly the most advanced developing countries, and not the poorest because their inconsiderable external trade is chiefly confined to exchanges with their direct neighbours.

Moreover, the Commission's estimates of the likely cost of the stabilisation mechanism are understandably only approximate and subject to several qualifications, apart from the fact that they do not include the cost of the possible support scheme for sugar. In the light of the present boom in most commodity markets which would of course be of relevance for the calculation of the reference prices it must be feared however that its costs would in fact put a much heavier burden on the Community than has been assumed by the Commission.

Transfer to the System of Generalised Preferences

Unlike the Commission, the Hamburg Chamber of Commerce has always spoken up in favour of gradually transferring the special preferences to the system of generalised preferences. The proposals of the Commission however amount to a perpetuation of the trade preference margin insofar as any multilaterally agreed tariff reductions are to be offset by lift-

ing the reference prices in proportion.

The Commission has drawn up its proposals on the basic assumption that the dominant feature of the commodity situation is a surplus of raw materials. Recent experience shows that conditions can change quickly. In the view of the Hamburg Chamber this is another aspect which suggests that it is not very advisable to operate a product-related stabilisation mechanism which third countries in bottleneck situations can use as a welcome excuse for giving the Community the "brush-off". Global aid could not be misused so easily.

To sum up, it may thus be said that for a variety of reasons the Chamber does not regard the stabilisation system in the form presented by the Commission as an acceptable development model. It believes that an aid system which is neutral as between different commodities and takes any other foreign currency earnings into account, combined with tying aid to individual projects, would be a more suitable alternative.

Extension of the Preferences only in the Longer Term

Clearly the EC will soon have to develop a new concept for its association policy. Would it not be more logical to grant the preferences and technical and capital aid to all the developing countries, including the non-associated ones?

I answered part of this question already in connection with the first question. I agree with you that association policy has undergone a great change of scenery since the opening meeting at the end of July, but I have doubts about the permanence of the consensus of opinion in the speeches of the three speakers from favoured countries. Will it last through the

whole of the negotiations? You know that associate status for the then French territories in Africa was one of the preconditions for the conclusion of the Treaties of Rome. Extension of the preferences to all developing countries — or substitution for the special preferences of universal UNCTAD preferences — would be in line with the long-term view of the Chamber which has been consistent in its warnings against the dangers to world trade of regional blocs. Bearing in mind that the policy of European integration is in any case progressing rather slowly, the apparent change of attitude on the part of the associated countries should be no cause for injudicious action jeopardizing eventual success merely in order to hasten a development which is going to take place anyhow since the margin of preference in favour of the associated countries is narrowing as a result of the multilateral negotiations.

On the other hand, there would be strong objections to proposals which have the aim of compensating for possible cuts in preferential tariffs under multilateral agreements by such devices as the fixing of higher reference prices as part of commodity stabilisation systems so as to solidify the associates' advantage over third countries in the sphere of trade policy.

Another development issue still in dispute, especially in the

Federal Republic, is the extension or amendment of the Development Aid Taxation Act which serves the purpose of encouraging German direct investment in developing countries by offering tax concessions for them. In fact the share of German direct investment going into these countries has declined from 38 p.c. of total direct investment abroad in 1962 to 28 p.c. in 1971. This caused Minister for Economic Cooperation, Dr Eppler, to describe the Development Aid Taxation Act as inadequate. How do you assess the past effects of this law?

Scope for Improving the Development Aid Taxation Law

As the Federal Minister concerned has gone on record with the view that the Development Aid Taxation Act is inadequate, I should first of all like to point out what I think to be the right conclusion: We should make sure that the Act remains in force — in an improved version — and is not allowed to expire at the end of the year or abrogated without anything else being put in its place.

The figures which you mentioned can of course be looked at from another angle. One can ask what share of the German investments abroad would have gone to developing countries if there had been no development aid tax law. There is certainly scope for improving the Act but one must beware of regarding

even an improved version as a universal remedy for development problems. However, I believe that by and large the Act as it stands deserves to be judged positively. Abuses which could unfortunately occur in the past, and are deplored also by me, have been cut out in the meantime anyhow.

A Warning against Generalisation

Critics have found fault with the Act on the ground that it discriminates against labour-intensive productions which are desirable from the point of view of development policy and favours capital-intensive productions. What is your experience in this respect?

My conversations with firms in Hamburg which have invested in developing countries do not bear out this charge at all. Our firms, in particular the local branches of trading enterprises, have mostly committed themselves on a small or medium scale with, as a general rule, entirely positive effects on training and employment. Many individual instances could be mentioned.

Besides, I should utter here a warning against thoughtless generalisation. One of the major problems facing the governments in many developing countries is certainly that of unemployment, which owing to rapid population growth is in many cases still increasing. If employ-

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ment aspects are for this reason given more attention when the Act comes up for amendment, the problem should be tackled in a way which does not impair the practical applicability of the Act.

It must be clearly understood however that if heavy stress is laid on the labour intensity of an investment, this may conflict with other, perfectly reasonable economic objectives. I may point out that in the light of experience many developing countries have come to realise that it is better to orientate an investment towards exports than towards import substitution. The demand for the highest possible labour intensity can obviously clash with the orientation towards exports.

Besides, there may be developing countries which have already reached a level of development which allows preference to be given to capital-intensive investments as offering superior opportunities for the future. It is often the case that investments involving a large capital input give rise to a large number of new jobs in the preceding and succeeding sectors of the economy. I do not however deny that the creation of the largest possible number of jobs in the shortest possible time is certainly the prime consideration for investments in many developing countries. That this may retard the solution of their problems in the long term should not be overlooked.

A Very Important Piece of Legislation

What do you think of the charge that the Act is merely subsidising German enterprises whose field of activity is international and has no effective influence on their decisions about investments in developing countries?

You are referring here to criticism that the opportunities

opened by the Development Aid Taxation Act are a bonus for the big firms which comes in handy for them but has no influence whatever on their entrepreneurial decisions. I believe one should look at the matter the other way round. One must realise that the Development Aid Taxation Act cannot be the sole basis for an investment decision. It would not be reasonable for anybody to invest in a developing country merely in order to avail himself of the opportunities offered by the Act. The investment decision rests on a "package" of diverse individual appraisals. To judge from my talks with firms in Hamburg, the Development Aid Taxation Act is certainly not the sole factor in this respect but nevertheless plays an important role. For this reason I believe that the overall approach in the business world to investments in developing countries might well change if the Act were dropped and nothing else took its place.

Selective Public Aid Must Come First

Criticism has been levelled in particular at the insignificant effect of the Act on the course of investments in the thirty poorest countries of the world. How can this be remedied?

There should be clarity that while the direct investments in a developing country are as a rule beneficial from the point of view of development policy, their main motivation is to be found in business considerations. This commercial motivation of private engagement in other countries is inherent in our economic system. Commercially it often does not make sense for the businessman to engage in the least developed countries to a similar extent as elsewhere. In general the private entrepreneur cannot launch his venture before the macro-economic basis of a country, e.g.

its infrastructure, fulfils certain minimum prerequisites. No responsible businessmen can operate where these are as yet lacking. Selective public development aid in its various forms must come first.

What do you think are the most essential considerations to be taken into account for an amendment of the Development Aid Taxation Act?

You know that there are advocates of an abrogation of the Development Aid Taxation Act without any kind of alternative arrangement to take its place. My first demand is therefore that the continuing validity of the Act must be ensured. The various contributions to the debate which have become known in the course of the prolonged discussion have this in common that they all aim at a more differentiated use of the instruments provided by the Act. Take, for instance, the demand that more consideration should be given to employment-intensive investments, to the grading of the favoured countries according to their state of development, etc. Though appreciating some of these demands, one should — I think — bear in mind that the practical applicability of the Act must not be unduly impaired. A quite essential advantage of the present law is that it lends itself to relatively simple administrative procedures, to the benefit of both the administrators and the firms. There must not be too much differentiation. If a piece of legislation can only be applied after prolonged investigations the outcome of which cannot be assessed in advance, it is bound to fail in its purpose despite the best intentions. Besides, it must be noted that a greater measure of differentiation between developing countries involves the use of criteria bound to intrude upon foreign policy.