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A.I.D. Policy Paper

Trade Development

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TRADE DEVELOPMENT POLICY PAPER

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Executive Summary

World trade is one of the primary keys to international economic growth and development; LDC exports are of increasing importance in achieving a level of sustained economic growth that will improve the living conditions of the poor. Because foreign assistance is a relatively less significant source of foreign exchange for LDCs, countries that seek self-sustained economic growth will have to rely principally on an expansion and diversification of trade to meet their energy needs, and finance imports of capital goods, intermediate inputs, and, in a number of cases, food. The purpose of this policy paper is to provide direction to A.I.D. in the encouragement of appropriate LDC trade policies and a framework for the design of trade-related programs and projects.

For developing countries, sound trade policies are an integral component of an effective development strategy that will stimulate growth and the productive use of natural and human resources. The opening of markets to foreign trade is an important step in accelerating economic growth. Exports play a vital role in long-term job creation and overall employment in an LDC's economy.

Despite the advantages of an outwardlooking trade policy as a mechanism for achieving economic growth, there are many barriers that must be overcome before such a policy can be pursued successfully by an LDC. These barriers include import substitution strategies; LDC parastatal policies and their impact on private investment; the LDC's lack of international marketing information, experience, and networks; industrialized countries' trade barriers and market access policies; low and unstable prices of primary products; financing constraints and LDC indebtedness; and increased use of countertrade.

The U.S. view of appropriate trade policies for both developed and developing countries derives from the same basic principles to which the United States itself subscribes. A.I.D.'s policy on trade and its role in development are fully consistent with and derive from the following three fundamental principles of U.S. trade policy: (1) free and open trade benefits all nations; (2) fair trade is essential to support free trade; and (3) an effective international trading system is essential to preserve open markets and

growing and fair trade. These basic principles have been the cornerstone of U.S. trade policy for over 37 years, and complement the United States' belief that only through a strengthened international trading system can effective rules governing fair trade be established, trade liberalization be negotiated, and disputes be settled.

A.M.'s trade development policy is designed to encourage LDCs to utilize international trade as a key instrument in the process of achieving broad based, sustained economic growth, and place a greater reliance on complementary domestic competitive markets that support more open trade policies.

A major focus of the trade development policy is on building developed country and LDC private enterprise ties on a continuing, long-term basis, consistent with the broad American objectives of trade liberalization. The formation of such ties should lead to:

- e development of stronger LDC economies based on the efficiency of market-based resource allocation;
- * development and strengthening of mutual economic interests between developed countries and LDCs.;
- * encouragement of entrepreneurship, economic institution building, and reliance on sources of private finance; and
- * adoption of appropriate economic policies.

A.I.D. will focus its trade development efforts within the framework of the four pillars. Specifically, the policy directs that A.I.D. policy dialogue, programs, and projects (1) establish a policy environment that is conducive to private enterprise and expanded participation in international trade; (2) encourage the transfer of technology, skills, and information required to expand and diversify LDC agricultural and industrial bases for export production in areas with comparative advantages; (3) support trade and investment promotion efforts; (4) introduce or expand private sector competition in the export or import of essential or economically important commodities; (5) broaden the scope of export development projects to provide for greater U.S.-LDC two-way trade opportunities; and (6) encourage prudent investments in infrastructure to improve an LDC's trade

position. The guidance reflects A.I.D.'s experience with trade policy and projects, and should be applied when a Mission has **made the decision to pursue trade** or export development as part of its economic development strategy-

Trade Development Policy Paper

I. Introduction

World trade is one of the primary keys to international economic growth and development; LDC exports are of increasing importance in achieving a level of sustained economic growth that will improve the living conditions of the poor. Because foreign assistance is a relatively less significant source of foreign exchange for LDCs, countries that seek self-sustained economic growth will have to rely principally on an expansion and diversification of trade to meet their energy needs, and finance imports of capital goods, intermediate inputs, and, in a number of cases, food. A.I.D. will assist LDCs in improving their ability to trade because, through expanded trade, industrialized and developing countries benefit from increased economic efficiency, higher levels of income and employment, and greater access to technology. This approach is consistent with U.S. Government trade policy, which has historically promoted policies oriented towards liberalizing world markets and limiting government management of trade and investment.

The purpose of this policy paper is to provide direction to A.I.D. in the encouragement of appropriate LDC trade policies and a framework for the design of trade-related programs and projects. It is intended to be useful to Missions in thinking about and conducting their dialogue with LDCs on trade policy and in crafting A.I.D. interventions where appropriate. This policy paper builds upon A.I.D.'s experience with trade and export development and its private enterprise initiative. It supersedes "AID Policy on Trade, Investment and Development" (dated May 15, 1978).

II. Trade and Investment in LDC Economic Growth

The opening of markets to foreign trade is an important step in accelerating economic growth. Exports play a vital role in longterm job creation and overall employment

in an LDC's economy. If the processes used for export production are labor-intensive, the country will realize significant employment gains in the short- and long-term.

Although foreign assistance may be needed in the early stages of development of the poorest LDCs to help provide capital and to develop export-oriented institutions, this aid becomes less important as an LDC's capacities to export are strengthened. Once their industrialization process begins, aid should be used to encourage those countries receiving assistance to graduate in a timely fashion from that assistance. For example, the economic well being and growth prospects of many emerging middle-income developing countries now depend on their ability to access international product and financial markets rather than on foreign assistance. Export earnings in many LDCs contribute a far more significant proportion of foreign exchange resources than Official Development Assistance; the LDC's export earnings of \$324 billion in 1983 amounted to 10 times their inflow of resources from foreign aid. With the flow of foreign assistance unlikely to expand in the foreseeable future, reliance on trade as a means to earn foreign exchange will be of even more critical importance for most LDCs.

Recent studies have confirmed the strong relationships between export- or outward-oriented strategies, a reliance on open market trading policies, and economic growth in LDCs.* The success stories of many of the Newly Industrialized Countries (NICs) illustrate this point. Although the characteristics of individual NICs differ, four factors were very important for their success and ability to compete in world markets: (1) a reliance on export promotion and the international economy as major sources of expansion for their manufacturing and industrial sectors; (2) a commitment to achieving market-based economic growth that enabled them to alter domestic policies accordingly; (3) a sustained investment in human resources development; and (4) close cooperation between government and the private sector. Another

*See Jagdish Bhagwati, *Anatomy and Consequences of Exchange Control Regimes* and Anne O. Krueger, *Liberalization Attempts and Consequences*, National Bureau of Economic Research, New York, 1978; and Alvin Rabushka, *Free Markets and Economic Development in Postwar Developing Countries*, U.S. Agency for International Development, December 1983.

important factor contributing to this growth was the presence of a proper mix of export-oriented development policies and import substitution policies. In some cases, this meant that economic growth was spurred by, or relied in part on, a sound agricultural sector.

The NICs, who accounted for much of the impressive LDC economic growth during the 1974-1980 period, are now expanding their activities into more complex, skill-intensive, and higher wage manufacturing. As these more advanced NICs (like South Korea, Taiwan, Hong Kong, and Singapore) progress to higher technology products (such as consumer appliances, electronics and computers), there is potential for other nations to take advantage of opportunities to supply more labor-intensive manufactured goods on world markets. In fact, a second group of countries that includes Colombia, Malaysia, Thailand, and Tunisia has recently accelerated economic growth via the export of labor-intensive manufactured goods.

An LDC can maximize its benefits from freer trade to attain sustained economic growth and a reasonable approximation of full employment only if the opening of its economy to international markets is accompanied by domestic policies which foster market-based resource allocation and permit development of those activities in which it has a comparative advantage. A country that restricts trade and controls (or distorts) its internal resource allocation through administrative measures is most likely forcing some of its resources to flow into less efficient uses. Government policies and administrative efforts that ignore this fact cause some production to become more costly than the domestic market will bear. This restrictive approach could cause, in effect, a "tax" on the production in which the country may have a comparative advantage in order to "subsidize" the production in which it has no comparative advantage. These efforts to protect LDC economies from competitive world trade also result in a diversion of resources that could be applied to other development problems.

As an LDC removes import and export restrictions and controls, the market will allocate resources away from, less efficient uses and toward productive activity in which they are more suited. This shift of resources to their more efficient use

accounts for an initial period of increased specialization in production (as well as a genuine savings to an economy). The relaxation of import restrictions will also provide indigenous businesses with access to the financial, technological, and managerial inputs necessary to fuel economic growth. In the longer run, as a country's human resource base develops, a country may expand the number of activities in which it has a comparative advantage. Such diversification of production is important for stability and sustained growth in order to hedge cyclical or secular declines in export prices,

Increasingly, trade and investment flows are interrelated. The opening of markets to foreign direct investment also provides a way for LDCs to diversify their economies at the same time they gain access to new technology and managerial skills. Open and fair investment policies are essential to an expansion of investment and technology transfer. An open and stable investment environment will position developing countries to acquire the capital necessary for private sector development. Less government intervention in the economies of developed and developing countries with correspondingly fewer restrictions on domestic and foreign investment will greatly assist rapid development and growth in world trade.

1.11. Obstacles to Improving LDC Trade Capabilities

In the near term, there is some doubt about the capability of many LDCs to compete successfully in world markets or to serve as major sources of world demand. Despite the advantages of an outward-looking trade policy based upon open markets, there are many barriers that must be overcome before such a policy can be implemented by an LDC. These barriers reflect problems that are both internal and external to LDCs. Although the nature of these barriers varies from country to country and generalizations may not be applicable in all LDCs, some of the more severe obstacles are common to many LDCs.

A. Import Substitution Strategies

Many LDCs have promoted import substitution strategies for economic growth and employment generation. These strategies are generally initiated by enacting temporary protection, such as high tariffs, for infant industries against foreign competi-

tion. Although these tariffs have gradually been decreased, they remain well above developed country tariffs and are used increasingly in tandem with nontariff barriers to protect these industries.

This new form of protectionism is difficult to dismantle once it has been established. In these instances, import substitution leads to increased inefficiency in the domestic market (encouraged by government policies that subsidize industries in which a country may have no comparative advantage) and keeps foreign products out of LDCs on a selective basis. It is better for an LDC to develop its economy through development of the market with increased exports leading to an appropriate percentage increase in imports than to try to do so behind barriers of import substitution.

Inward-looking development strategies utilize a variety of measures to allocate imported goods toward priority areas (as perceived by the EDC). These measures include an overhauled exchange rate, restrictive exchange controls, tariffs, and quantitative import and export restrictions. Such interventions in the market favor certain imports, but cause high prices to be charged on imported items not under official exchange rates. Moreover, productive activities in which the country has a comparative advantage may also be severely affected by the restrictions on imports of intermediate goods, the higher export price of their products, the higher transaction costs due to controls on trade, and the tax effects of cross-subsidies required to sustain the inefficient producers in other industries or sectors.

B. LDC Parastatal Policies and their Impact on Private Investment

Since inefficient sectors or industries cannot survive unless policies are in place that distort price signals, an economy that restricts trade almost always requires the use of parastatals or government-sanctioned private monopolies to provide the necessary goods and services. The existence of the parastatals or monopolies creates additional obstacles to liberalization in the future, through the creation of "vested interests" as well as the inability of such enterprises to compete against more efficient private concerns. Developing countries find themselves in the dilemma of wishing to attract private investment in a sector where a public

while at the same time having to shield the less efficient public company from full competition.

In this conundrum, the private investor -often loses. Existing foreign or indigenous investors often become frustrated by the favorable treatment and the unfair competitive advantage given public companies and may often see their firms forced out of business, while the LDC spends precious resources keeping the SOEs afloat. Similarly, foreign or indigenous private investors may sometimes be discouraged from entering the market altogether because of the more favorable treatment extended to the public enterprise.

C. Lack of International Marketing Information, Experience, and Networks

Many firms in LDCs find it difficult to obtain the technical skills or knowledge needed to identify products appropriate for export. The lack of information is a particular problem when new export activities require a clear technical and managerial understanding of production possibilities, a firm grasp of present and future market conditions, and international marketing skills. Among the factors contributing to this lack of market information are the (1) high cost of obtaining information; (2) lack of knowledge about new business practices; (3) insularity of many LDC businesses from market channels; and (4) costs of developing contracts and sales networks.

D. Trade Barriers and Market

In the wake of a global recession in the early 1980s, followed by an imbalanced recovery concentrated almost entirely in North America, many industrialized countries are intensifying and expanding protectionism for their domestic industries and agriculture against imports from LDCs. A major concern about the renewed protectionism is that it poses new obstacles against products that might form the basis of a feasible export expansion program by these LDCs. Although some analyses indicate that the new protectionism has had a modest impact on the volume of trade, the following considerations have been raised:

• the adverse effects on trade may show up later, since investment in export-oriented activities will be inhibited and since some of the measures are only recent;

the pattern of trade may have been distorted even though total trade has not fallen; and

in the absence of these protectionist measures, trade would have expanded much faster than gross national product, so that a shift to more export-oriented growth is being inhibited.

Widespread protectionism would lower long-term growth by reducing international trade, economic flexibility, and the productivity of capital and labor, as well as serve as a disincentive to greater foreign trade and investment in LDCs,

The United States market has been more open to LDC exports than have those of our major trading partners in recent years. In both 1982 and 1983, for example, a majority (55-60 percent) of LDC exports of manufactured goods to the industrialized countries went to the United States alone. Our more robust economic recovery, and the high value of the dollar, have drawn imports to our economy. The fact that such a large percentage of manufactures from LDCs is entering our market, despite strong protectionist pressures, is testimony that U.S. barriers to imports are relatively low.

E. Low and Unstable Prices of Primary Products

Many LDCs, especially the lowest income nations, specialize in the export production of one or a limited number of primary products. Due to technological advances in the production of substitute goods and a softening of world demand, a number of these products have experienced downward price trends.

F. Financing Constraints and Indebtedness

Much of the funds borrowed by the non-oil producing LDCs in the 1970s was invested in projects that did not produce foreign exchange earnings sufficient to cover the ensuing debt service. The debt service burden has, in turn, reduced the amount of foreign exchange available for new investments, and caused private banks to exercise more cautious lending policies than in the past. New foreign investments in LDCs have slowed as well, cutting off a valuable source of funds for economic growth and limiting indigenous investment possibilities.

G. Increased Use of Countertrade

Many LDCs resort to countertrade* arrangements because of the weakness of commodity markets and their deteriorating foreign exchange positions. Countertrade is always less efficient than normal commercial transactions-bilateral arrangements are cumbersome, costly to LDC governments, deprive LDC companies of direct marketing and financing experience, and, in some cases, intensify downward price pressures on LDC commercial exports. When LDCs deal with foreign exchange shortfalls by using countertrade as an export financing mechanism, they should take care that the comparative advantage is clear and there is minimum distortion to market allocation. Although, as a matter of policy, the U.S. Government does *not* oppose the participation of private enterprises in countertrade arrangements (as this may be one of the few ways that they can meet some of their import needs), it does not support government-mandated countertrade.

IV. U.S. Trade Policy and Its Relevance to LDCs

The U.S. view of appropriate trade policies for both developed and developing countries derives from the same basic principles to which the United States itself subscribes. For developing countries, sound trade policies are an integral component of an effective development strategy that will stimulate growth and the productive use of natural and human resources. A.I.D.'s policy on trade and its role in development are fully consistent with and derive from the following three fundamental principles of U.S. trade policy:

- Free and open trade benefits all nations. The United States believes that free trade and open markets permit the principles of comparative advantage to work, produces more jobs, more productive use of natural resources, more rapid innovation, increased consumer choices, a higher standard of living, and higher incomes. (Comparative advantage does not mean LDCs must continue to depend on natural resources as the

*Countertrade may be defined as transactions in which the seller provides the buyer with deliveries (such as technology or finished products) and contractually agrees to purchase goods from the buyer equal to an agreed-upon percentage of the original sales contract value. Countertrade is a term that encompasses barter, buy back, counterpurchase, offset, and compensation trade.

principle export; it means a greater opportunity for them to develop non-traditional exports.)

- Fair trade is essential to support free trade.

The United States believes that fair trade must be based on mutually acceptable rules that give no country an unfair advantage. Trade opportunities derive from the principles of comparative advantage, not artificial advantages that create barriers or close markets. (Fair trade principles are as relevant to industrial as to developing countries since the benefits to growing world trade should not be limited to one group at the expense of another.)

- An effective international trading system is essential to preserve open markets and growing and fair trade.

The United States believes that only through a strengthened international trading system can effective rules governing fair trade be established, trade liberalization be negotiated, and disputes be settled. The interests of developing and industrial countries can best be realized through participation of all countries in the GATT. (In particular, developing countries' active participation in trade negotiations under GATT auspices is the only effective means to assure that their trade interests are considered and respected.)

These basic principles are inherent in the General Agreements on Tariffs and Trade and, therefore, have been the cornerstone of U.S. trade policy for over 37 years. Although the basic principles of U.S. trade policy have not changed during these years, the importance of trade to the world economy and to economic development has grown.

More open trade and investment policies are particularly important for debt-burdened developing countries. The major element of Treasury Secretary Baker's Program for Sustained Growth is the adoption of policy reforms that maximize the contribution that trade and investment can make to the growth and adjustment process of developing countries. For example, those developing country economies that have continued to advance during the debt crisis of the 1980s are those that have adopted outward oriented growth strategies characterized by open trade and investment policies.

V. A.I.D. Policy for Trade Development

A.I.D.'s trade development policy is designed to encourage LDCs to utilize international trade as a key instrument in the process of achieving broad based, sustained economic growth, and place a greater reliance on complementary domestic competitive markets that support more open trade policies.

A major focus of the trade development policy is on building developed country and LDC private enterprise ties on a continuing, long-term basis, consistent with the broad American objectives of trade liberalization. The formation of such ties should lead to:

- development of stronger LDC economies based on the efficiency of market-based resource allocation;

- development and strengthening of mutual economic interests between developed countries and LDCs;

- * encouragement of entrepreneurship, economic institution building, and reliance on sources of private finance; and

- * adoption of appropriate economic policies.

This policy is consistent with two of the principal goals set forth in the Foreign Assistance Act of 1961, as amended: (1) the promotion of conditions enabling developing countries to achieve self-sustained growth with equitable distribution of benefits; and (2) the integration of the developing countries into an open and equitable international economic system.

VI. Specific Components of A.I.D.'s Policy

A.I.D. will focus its trade development efforts within the framework of the four pillars. Specifically, the policy directs that A.I.D. policy dialogue, programs, and projects (1) establish a policy environment that is conducive to private enterprise and expanded participation in international trade; (2) encourage the transfer of technology, skills, and information required to expand and diversify LDC agricultural and industrial bases for export production in areas with comparative advantages; (3) support trade and investment promotion efforts; (4) introduce or expand private

sector competition in the export or import of essential or economically important commodities; (5) broaden the scope of export development projects to provide for greater U.S.-LDC two-way trade opportunities; and (6) encourage prudent investments in infrastructure to improve an LDC's trade position.

ThAs guidance reflects A.I.D.'s experience with trade policy and projects, and should be applied when a Mission has made the decision to pursue trade or export development *as part of its* economic development strategy. Whether explicit trade development activities should be initiated by Missions depends upon several factors, including Mission priorities, staff capacity, and country strategy. It is not expected that all Missions have the staff capabilities to undertake these activities. However, even if program or project interventions may not be called for, policy dialogue activities should be considered and carried out if at all possible. Missions should look to private sector contractors and consultants; business, trade, and professional associations, and U.S. and LDC private enterprises involved in trade for assistance in designing a trade strategy- AID/W will help Missions where it can.

A. The Policy Environment for Trade and Investment

1. The Trade Environment

LDCs can most effectively enter the international trading system by pursuing trade-oriented strategies that reduce import protection in favor of economic diversification, competitive markets, and technology acquisition. A.I.D.'s efforts to help strengthen the trade capabilities of LDC private enterprises can be truly effective only if they are carried out in a policy climate that encourages market-based activity and maximizes the capabilities of the private sector. **Therefore, A.I.D.'s first effort related to trade should be directed towards establishing and improving a policy environment that is conducive to private enterprise and expanded participation in international trade.** Over the long term, it will be these policies, coalescing around trade-oriented strategies, that will be the dominant influence affecting an LDCs economic growth.

Trade-oriented strategies seek to eliminate, or at least minimize, economic distortions so that the prices of exports reflect as near

as possible the real opportunity costs of the items to the country. Successful export strategies, usually include the following:

- the reduction or elimination of duties and quotas on imports essential to the production of exports;
- the reduction or elimination of taxes and quotas on exports;
- * the simplification of licensing and other bureaucratic procedures needed to export;
- the reduction, to real levels, of transaction costs associated with the handling of exports and related imports (e.g. licensing requirements, embarkation and disembarkation processes, etc.)
- * elimination of subsidies on exports; and
- * exchange regimes that reflect market rates.

Missions should pursue a policy dialogue with host governments to remove existing trade restrictions and controls. Political and social resistance to reevaluating import substitution policies and adopting an export orientation may be particularly strong in countries that have an elaborate structure of import substitution supports and considerable sunk investment in noncompetitive import substitution industries. It may require the reversal of many long held, politically-based policies and the decline of inefficient industries. Any change in business activities to support exports may involve resistance by those who face possible losses. Opposition may arise from Owners and managers of inefficient firms that would have their markets opened to competition, from workers threatened by *displacement*, and from others who benefit by the status quo, Missions should explore, with LDC governments and private enterprises, alternative uses for the human and financial resources that had been devoted to these industries.

Although this is a difficult process for some LDCs, this difficulty is not infrequently exaggerated by LDC politicians. Countries that have limited their import substitution efforts, and instituted policies to keep their import substitution industries competitive with imports, are likely to be less resistant to policies that would increase trade. If restrictions can be removed and the immediate adverse impacts of removing protection are hedged or lessened, the potential

for sustained economic growth will be dramatically increased. Although this may be easier said than done, it is important to pursue our targets here.

In a number of LDCs, the enactment of those policies that support the expansion of exports and the removal of those policies that restrict trade, must be accompanied by fundamental policy changes that may have more profound consequences for the economy at large. These may include:

* open market sales of foreign exchange;

- liberalization of financial systems so that the market will determine domestic rates of interest;

41 elimination of laws or conditions that reduce or eliminate competition in production and trade; and

e policies that ensure that establishment of wage and benefit packages more nearly reflect the value of labor input.

There is no single rank ordering of the issues related to improving trade that can be applied in each Mission's policy dialogue with the host country. In some LDCs, opportunities may emerge to program A.I.D.'s assistance in direct support of a comprehensive policy reform program that will have a significant impact on improving trade and moving away from import substitution policies. In other LDCs with a relatively long tradition of import substitution and central management of their economies, A.I.D. assistance may have to be programmed to help the host country overcome fundamental fears of exposing its economy to world (and domestic) market forces. In such countries, A.I.D. may need to support a learn-by-doing approach focused on the development of a country's comparative advantage in nontraditional exports. Missions should obviously be careful not to augment distortions or introduce new disincentives into an LDC economy; their actions should be consistent with or designed to reinforce market-oriented activities and to encourage predictability in LDC policies.

Critical to the success of an open trading strategy is stability in government policies affecting trade and investment in particular and economic growth in general so that exporters, importers, and investors can develop long-term linkages. Stability contributes to confidence that public policies

favorable to economic growth and the development of a competitive private sector will continue (assuming that they exist in the first place), which is necessary to encourage the long-term commitment required for trade and investment.

An important policy issue that should be discussed with host governments is the use of standards. Generally accepted standards, both for product quality and for measures and weights, are crucial to the efficient functioning of markets and their growth. Standards permit the rapid and wide spread of information that, in turn, is needed for truly competitive markets. The lack of common minimum standards often frustrates achievement of the consistent quality needed for trade in large quantities or over great distances. This is especially essential to the development of agricultural trade in LDCs; it is also one of the major inhibitions to small scale manufacturers. In addition, many LDCs utilize unfair and arbitrary standards to discriminate against foreign products.

There are many vehicles available in LDCs for standards development. Government attitudes toward standards need to be improved through the policy dialogue. Trade associations can help to promote voluntary industry-wide standards. **A.I.D. should encourage LDC private and public institutions to develop and strengthen quality and other standards. A.I.D. should also work with host governments to eliminate the use of product standards, testing, and certification procedures that unfairly restrict imports.**

Missions should also consider providing aid to LDC business associations in order to involve more deeply the indigenous private sector in the policy dialogue. These groups, representing the local business community, should be a primary mechanism for keeping the host government institutions aware of private sector concerns with respect to trade and other government policies or programs that affect business.

2. The Investment Environment

Foreign direct investment offers LDCs a way to acquire new production facilities at a lower risk than financing and building their own operations. The investments bring new technology, provide employment, and transfer new managerial skills.

In order for LDCs to attract foreign investment, businesses must be confident that such countries pursue realistic economic policies and maintain a stable and open investment environment.

Missions should encourage LDCs to adopt a market-oriented investment climate so these countries will be able to attract the investment capital essential for private sector development.

The basic elements of an open investment environment include policies that-

- * treat investors equally on most-favored nations principles and provide comparable treatment to foreign and domestic investment (in such areas as taxes);

- o conform to internationally recognized standards for compensation in the event of expropriation;

- * permit the transfer of Profits and other funds associated with investments;

- o do not encourage performance requirements that mandate conditions on investments regarding local content, exports, or equity;

- o provide adequate and effective protection of intellectual property rights such as copyrights, patents, and trademarks; and

- * provide effective means for settling disputes.

The attractiveness of a particular LDC market to potential investors depends upon the restrictions that the country imposes on such relationships. If approval and import licensing procedures are excessively lengthy, foreign equity limitations stringent, and requirements to export a portion of the production or to source local goods unreasonable (without regard to availability, price, and quality), then a foreign investor may be discouraged from pursuing LDC investments or joint ventures altogether. Even if the investor is not put off at the outset, the government approval process may require the investor to spend a great deal of money before any returns can be realized, Investors sometimes have cancelled projects if delays are too prolonged.

In addition, foreign companies should (1) not be limited to producing for small segments of the market, or to concentrate on exports, as protection for competing local concerns; (2) have access to foreign exchange to acquire needed imported in-

puts; and (3) be allowed to hire management talent of their choice, regardless of nationality. These obstacles to investment suggest additional agenda items for Missions' policy dialogue with host governments.

The issue of intellectual property rights, raised above, deserves special attention. Inadequate intellectual property rights protection continues to hinder foreign investment and innovation in many LDCs. If the country fails to guarantee patents and copyrights, and to license and protect trademarks, investors will be reluctant to come to that country in the first place and, in any event, will be hesitant to make the most up-to-date methods of production or formulas available to local partners. Many countries that wish to comply with internationally recognized copyright, trademark, and patent conventions, however, often lack the resources and capabilities to enforce these conventions. **A.I.D. should undertake efforts to assure LDC governments that proper enforcement of copyright, trademark, and patent conventions is essential to strategies intended to increase the transfer of technologies and expand LDC access to information.**

B. Trade Diversification and Technology Transfer

A country's comparative advantage in production (or international trade) is not static; new competitors emerge and old ones disappear, technology changes, essential resources become scarce, substitute products become available, and consumer preferences change. Successful participation in international trade requires the dynamic involvement of producers and governments in a process of regular adjustment of practices and policies, respectively, that responds to current market conditions and anticipates future trends. LDCs are particularly vulnerable to a loss of their comparative advantage in production because of their limited human resource base, limited access to new technology, and limited access to market information, as well as rigidities imposed by poor policy.

Where appropriate, Missions should direct program and project resources to encourage the transfer of technology, skills, and information required to overcome the limitations that threaten the comparative advantage of LDC exports or inhibit the

emergence of new areas of comparative advantage in production. In this regard, A.I.D. programs should seek ways in which the capacity of indigenous firms can be increased in order to engage in, expand, or diversify exports.

One important method of achieving this objective is through the encouragement and facilitation of cooperative business relationships or joint ventures between developed and developing country private enterprises (such as joint ownership ventures, licensing, contract manufacturing and assembly, management contracting, and supplier agreements). These types of business relationships serve as a means for promoting trade linkages between private enterprises, and are based on the mutual desire of the involved firms to improve their competitive position in the world market.

These business relationships usually result in a new source of inputs and substantial transfers of technology, managerial techniques, marketing expertise, and market information to the LDC entrepreneur; represent a way to minimize costs and share risks; and open up access to markets and channels of distribution. They also provide a conduit for information on world market conditions which is almost impossible to obtain from publications usually available within the LDC or from contacts with other indigenous firms. The LDC firm's adoption of the management and quality control standards required for success in the world market results in immediate financial gain. **Missions should encourage joint ventures (as well as other forms of cooperative business relationships) as additional sources of technical assistance for LDC private enterprises.**

Special attention should be given to the development of producers in new lines of exports. Such action is particularly suitable for nations whose export earnings are tied to a few primary products that experience wide fluctuations in world prices. In addition to diversifying an LDC's export base and market risk, nontraditional exports are less likely to compete with most U.S. producers. However, A. L. D. -supported country export development projects should not favor some individual exporters at the expense of others, as this might lead to the exclusion of potentially viable exporters and the subsidization of current exporters.

The services sector (finance, training, software, maintenance, and others) is a major and growing component of trade and an important complement to the efficient use of capital in LDCs. Developing countries frequently restrict business opportunities in these areas, assuming that these can be reserved for local entrepreneurs; however, these restrictions are often at substantial costs in terms of access to technologies and management practices. **A.I.D. should encourage LDCs to open up their economies to imports of services, and develop the local private sector institutions and technological capability to complement foreign-supplied services.**

A growing number of sophisticated manufactured imports require continued service input to keep them in operation; this input, in many cases, may not be available in the importing markets (such as user training or maintenance). A.I.D. should encourage countries to overcome the tendency to buy only the capital components of a particular technology, and to devote greater attention to the technical information and process technologies that may be embodied in more complete packages.

Finally, increasing developing country to developing country trade is another method for stimulating economic development. Food emergencies often exist in one country while its neighbors may have adequate or even abundant food supplies. A combination of poor information, inefficient (or non-existent) market channels, and the absence of transport are often as important as lack of foreign exchange or creditworthiness in keeping normal trade and market activity from quickly dissolving these emergencies. As more LDCs adopt the proper trade environment and overcome their financing constraints, indebtedness, and barriers to "national selfinterest," there will be greater opportunities for inter-LDC trade.

C. Trade and Investment Promotion

Trade and investment promotion are important for promoting and diversifying exports, attracting new capital and technology, and generally improving the participation of a country in the world market. Missions are encouraged to review the variety of approaches available for export and investment promotion. In

developing export promotion projects. Missions should perform appropriate analyses to identify exportable products, determine potential markets, and make realistic determinations of the changing environment in which the Potential Export Products must compete, as well as identify cost-effective ways to have local firms evaluate their prospects and undertake marketing initiatives.

1. Private Sector Activities

A.I.D. Missions are encouraged to support the development of private sector institutions that can help indigenous entrepreneurs improve their export capacity and capabilities, as well as attract foreign investors. Where there are existing private sector organizations providing trade and investment promotion and services, Mission projects should rely on the private sector to continue providing these services and channel assistance for this activity directly to private sector entities.*

The development of private sector institutions may consist of establishing export promotion centers and marketing offices; (channels of distribution); business associations that promote the sharing of technologies and technological innovation; private financial institutions (export financing and credit facilities, industrial and agricultural banks, and other financial intermediaries); export trading companies, and other institutions. For example, in the area of export promotion, USAIDs should examine the possibility of contracting (through competitive bidding) for a promotion facility to be established within one of the local business associations or other firms, rather than establishing one within a government ministry,

Mission programs should also seek opportunities to assist current and potential LDC export industries to gain needed information and technology to enhance their competitive position. A.I.D.'s assistance could support management and technical training for LDC producers, exporters, private bankers, and lawyers; promote access to advisory and consultant services for LDC firms and industries; support the develop-

*This approach is consistent with A.I.D. views on Institutional Development and Private Sector Development, which emphasize reliance on the private sector rather than the public sector. However, where necessary and when host country officials make this possible,

ment of product and market information services; and assist firms conducting market analyses to identify new areas of comparative advantage. In providing such assistance, Missions should seek ways to provide, through the efforts of private sector organizations, labor organizations, and

2. Public Sector Activities

A number of LDC governments are involved in trade through incentive programs designed to promote specific export programs designed to attract imported capital for new commercial ventures. In some countries, particularly NJCs, such programs have been quite successful. Experience in many LDCs, however, suggests that government-managed export or investment promotion schemes have not been successful and may have retarded growth and development by introducing market distortions into the economy. This has often resulted because (1) LDC investment promoters are often government officials with little business experience (42) g

government promotion agencies often operate in the context of governmental bureaucratic and legal structures that often complicate otherwise simple LDC activities; and (3) management decisions on the targets and types of incentives were responsive to perceptions of government rather than, based on market conditions, which inhibited the effectiveness of efforts at the attraction of

In general, A.I.D. Missions are advised to exercise considerable caution before agreeing to support LDC government-managed export or investment promotion schemes.

Assistance to LDC governments for export and investment promotion schemes should have as its objective the fostering of market-based trade between their private enterprises and foreign markets similar to the services provided by the U.S. Foreign Commercial Service and the U.S. Foreign Agricultural Service). Support should be given when the following conditions are met:

* The proposed incentive scheme does not violate any international or U.S. laws, conventions, or agreements related to export

*SRI, international, investment insurance, and other activities. This report was prepared for the Bureau of Economic Affairs, U.S. Agency for International Development, Washington, D.C., January 1980.

subsidies, anti-dumping, or other unfair trade practices.

The proposed incentive scheme does not target commodities that would conflict with statutory provisions (e.g. FAA Section 620(d)) and existing Agency policies proscribing activities that would result in direct competition with U.S. enterprises.

* The incentives are appropriate to specific, identified constraints on exports or investment and their duration must be terminated within a reasonable period of time (as agreed upon by the Mission and the host government).

* Decisions on general areas in which incentives will be targeted and the types of incentives provided must be made in close consultation with a broadly representative group from the LDC's private sector, and must be consistent with efficient use of the country's resources.

4. It should not add unnecessarily to the host country's restrictive practices or to already excessive red tape, which would inhibit trade.

Missions should investigate providing technical assistance to host governments to help them effectively implement their trade programs and streamline their procedures. This could include, for example, consolidating the decision-making authority over export and investment licenses and other necessary permits in one centralized institution, or supporting training for LDC public sector personnel who are central to the export process (such as personnel in ministries of trade and commerce) to strengthen their effectiveness in representing their country's commercial interests overseas.

Evaluation of costs and benefits is a crucial activity if a Mission chooses to pursue a public sector approach to export promotion. These promotion programs can be subjected to cost/benefit analysis, since quantifiable costs are incurred and quantifiable benefits are achieved. Costs may include the operating budget of the promotion agency, marginal expenses of applied promotion techniques, cost of the project, and the costs associated with incentives provided. Among the benefits are the eventual econon-dc gains derived from new investments (in the form of employment, income, foreign exchange earnings, and tax revenues).

Missions may also wish to encourage LDC governments to adopt laws that allow the establishment of free trade zones as a means of encouraging private enterprise development. In addition to the manufacturing and assembly activities derived from the import of duty- or tariff-free items into these zones, there may develop indigenous suppliers that provide backward or forward linkages to firms in these zones.

3. Small Enterprises and Entrepreneurs

Special attention should be given to exports by small and medium enterprises. The production techniques employed by these entrepreneurial firms are generally less capital- and import-intensive than those of large firms, which makes them an important economic force in areas in which the LDC develops its comparative advantage. These enterprises may be important sources of employment and can compete favorably on world markets due to the low wages that prevail in LDCs. If market forces justify small scale enterprise exports, Missions should carefully look at ways to encourage them. This may take the form of supporting directed programs in financial institutions, organizing cooperatives, or providing information and training, as well as insuring that the policy environment does not discriminate against small and medium enterprises and allows them to contribute to export expansion. Missions should look to existing LDC private and public sector institutions that deal with small enterprises rather than undertake direct support to individual firms.

4. Government-restricted Markets

Government-restricted markets will become more commonplace as LDCs increase their exports and pose market challenges to competitors in industrialized countries. Missions are aware of the growing tendency by industrialized countries to levy import quotas or other trade barriers in response to LDC exports (such as higher tariffs, tariff-rate quotas, orderly marketing arrangements, or some combination of these). Although protectionist sentiment in the United States has received considerable publicity, the United States' openness to LDC imports and President Reagan's strong stand in support of free trade should be borne in mind in discussions with host country officials.

**conflicts and opportunities when reviewing
CDSSs, Action Plans, and Mission**

project proposals in their respective regions. Where practicable, Regional Bureaus should first look at the countries within their jurisdiction as well as

of and demand. It might also be useful for Regional Bureaus to share information on their trade-related programs

D- Trade J. Monopolies and Parasitals

LI -C governments have become heavily involved in their country's international trade by granting

special rights to import or export certain commodities

such as fuel, agricultural commodities, and inputs, and a few firms, in

addition, the granting of special trade privilege results in a separation of the resource allocation decisions from world market signals, so that these SOEs concentrate their efforts on production in a secure and protected market, and on the manufacture of products that are below world quality standards and above price levels.

Over time, the SOE's production or consumption generally requires substantial subsidization and may discourage private enterprise involvement in the import or export of particular commodities. In addition, the country itself becomes locked in a particular pattern of trade and technological dependency that hastens its loss of comparative advantage in key exports. State trading companies also are more likely to seek countertrading arrangements. To the extent that countertrade transactions are less efficient and introduce distortions in trading

, patterns, the state trading companies themselves can intensify their country's economic problems, especially if the controlled commodities constitute a large portion of a country's export.

These particular trade restrictions and their resulting price distortions on fundamental economic activity have profound consequences for the entire LDC economy in terms of fostering inequity and suppressing economic growth. A.L.D. strongly encourages and supports efforts to introduce or expand private sector competition in the export or import of essential or economically important commodities. It is recognized, of course, that many LDCs may

In an effort to avoid the imposition of quotas or other restrictions on LDC exports to the United States, U.S. supply and demand projections for the particular product to be produced should be undertaken when planning export projects that would include the United States as a potential market. Similarly, export data from A.I.D.-supported export promotion projects and private sector trade efforts in neighboring LDCs should be included in these analyses. Among the other factors that Missions should consider are the potential injury to U.S. producers (based upon the export potential of the project), and the condition of the U.S. industry that would be affected by the LDC export.

At present, an A.I. D.-supported export development project in one LDC may be prepared in isolation from an export development project in another LDC. The potentially negative impact that one country's export development will have on the export efforts or import needs of other LDCs in the region is often not taken into account. A.I.D. should not encourage potential LDC exporters to compete with each other for restricted markets; Regional Bureaus are in a position to help guard against this problem. **Regional Bureaus should advise Missions on potential export**

raise political and social objections to this approach; the dialogue in this area is of great importance.

A.I.D. resources may be programmed to assist LDCs to terminate trade monopolies and oligopolies, dismantle marketing boards, and divest parastatals.* When A.I.D. resources are used to start a policy dialogue to initiate the dismantling of a marketing board or the divestiture of an SOE when there is no initial commitment from the LDC, Missions must show that any improvement in the performance of the marketing board or SOE resulting from our assistance will contribute to increased dependence on market forces and the eventual dismantling of the marketing board or divestiture of the SOE. Clear benchmarks of substantial progress toward market-based operations and divestiture must be established and adhered to in the assistance program. **In general, if the SOE is providing unfair trade competition to private enterprises, restricting private enterprise development, or is enjoying special trade privileges or preferential treatment, these activities should be phased out before funds are provided to the parastatal in accordance with A.I.D. policy.**

E. U.S.-LDC Trade Promotion

What is good for development should not be inconsistent with what is good for the expansion of mutual economic activity between U.S. and LDC private enterprises. **A.I.D. should broaden the scope of its export development projects to provide for greater U.S.-LDC two-way trade opportunities. A.I.D., in concert with other U.S. government agencies, should also increase its efforts to make U.S. companies aware of A.I.D.'s varied activities.** Many mechanisms are available for accomplishing these linkages. These include:

* **Interagency cooperation.** Missions and AID/W should seek greater cooperation with other government agencies that are seeking greater U.S.-LDC trade and investment ties, such as the Overseas Private Investment Corporation, the Trade and Development Program, the U.S. Export-

*A.I.D.'s involvement in the dismantling of marketing boards and parastatal divestiture should adhere to policy as stated in A.I.D.'s Policy Paper on Private Enterprise Development (March 1985) and Policy Determination #14 on Implementing A.I.D. Privatization Objectives (June 1986).

Import Bank, the U.S. Department of Commerce (the U.S. and Foreign Commercial Service, and other offices within the International Trade Administration), the U.S. Department of State (embassy economics officers, in particular), and the Office of the U.S. Trade Representative (which administers the Generalized System of Preferences).

¶ **Brokering.** In recent years, a small number of U.S.-based organizations have begun to offer commercially viable packages of consulting, brokering, and facilitation services designed to help LDC firms (particularly small- and medium-sized enterprises) by furthering their relationship with U.S. private enterprises. These brokering services include identifying potential U.S. and LDC firms interested in entering into joint ventures or other collaborative business relationships; providing information to the potential collaborating firms about business conditions, risks, policy, and other concerns; and assisting client firms to identify technology or other inputs needed to exploit a particular business opportunity. Similarly, the International Executive Service Corps (IESC), through its Project ABLE, looks to match emerging or existing LDC firms with U.S. suppliers and customers.

* **joint ventures.** The benefits derived from joint ventures and other cooperative business relationships between firms in developed countries and LDCs were identified in Section VI.B. It should be noted, however, that these business relationships result in more than a one-way transfer of knowledge and experience from the developed country firm to the LDC partner. In reality, valuable skills in marketing products in LDCs and redesign suggestions to adapt products for LDC markets can be transferred from the LDC firm to the U.S. partner.

¶ **U.S.-LDC trade associations.** As many business associations are cooperative efforts between foreign and host country private enterprises, Missions should consider providing assistance to these associations so they can help foster trade and increase access to technology and information between indigenous and foreign private enterprises.

¶ **Mixed credits.** The use of mixed credits and other concessional financing programs by foreign governments presents a growing problem for effective development

assistance and trade development. Mixed credits do not directly promote two-way trade; however, A.I.D. recognizes that other donors are actively using mixed credits to subsidize their own exports and that this can put U.S. exporters at a serious competitive disadvantage. Therefore, until such time as an effective agreement is reached with other bilateral donors on restricting the use of mixed credits for export financing, A.I.D. will use the U.S. tied aid credit program (under ESF funding) for defensive purposes in selected countries to match the concessional credit terms offered or arranged for in support of a tender of a non-U.S. supplier in an international tender competition in which a U.S. supplier is the lowest responsive bidder. This approach is consistent with the new mixed credit program announced by President Reagan in his September 23, 1985, statement on trade policy.

It is important that A.I.D. be responsive to U.S. private sector activities in LDCs, as early participation in export sales is critical in building long-term trade and investment relationships. Many of our foreign assistance activities currently generate additional future demand for U.S. products directly through the need for replacement or spare parts, the purchase of complementary equipment, and familiarization with U.S. products. These activities are also encouraged.

F. Economic Infrastructure

LDCs have attempted to promote greater international trade through investments in economic infrastructure. Infrastructure has been built to (a) relieve transportation and communications bottlenecks; (b) ease congestion at seaports, airports, and other transfer points; and (c) attract new investment by site improvement or new site development. Infrastructure has also been built to open new areas for resource development and exportation. **Investments in infrastructure to improve an LDC's trade position can be very beneficial but should be undertaken only when (1) there are firm assurances that the expected complementary private investment in export production will occur; (2) the LDC has firm commitments from the principal investors who will use the facilities; and (3) adequate provision is made to maintain these facilities.**

Support for infrastructure should not be used as an incentive to investment in the

absence of such conditions. **In addition, A.I.D. resources should support trade-related infrastructure only when the host country's policy environment is supportive of competitive trade or when A.I.D.'s investment in infrastructure is in exchange for appropriate export-oriented policies.**

For the most part, LDCs should undertake trade-related infrastructure investments (such as widening roads or improving ports) only when there is clear evidence that the capacity of current facilities will restrict trade unless the improvements are carried out in a timely manner. Furthermore, before initiating such infrastructure, LDCs should ensure that current policy and practices (particularly regarding maintenance) result in the efficient use of existing facilities.

To a considerable degree, trade-related infrastructure benefits a distinct group of entrepreneurs in an LDC. Consequently, A.I.D. should seek ways in which the capital costs of trade-related infrastructure are shared by the private firms that receive the majority of the benefits. In this regard, there is considerable room for the use of capital levies or debentures subscribed to by firms engaged in export production or other aspects of trade, or introduction of a system of user fees that provides for full cost recovery of the trade-related infrastructure. Additional guidance on the use of A.I.D. resources for infrastructure is presented in Section V.I. of the revised Private Enterprise Development Policy Paper.

G. U.S. Trade Policy Coordination

A.I.D. is also involved in the U.S. trade policy coordination process. The major U.S. government fora for consideration of most trade issues and resolution of agency disagreements on U.S. and international trade issues are the White House Economic Policy Council, chaired by Treasury Secretary, and the Trade Policy Committee (TPC), chaired by the United States Trade Representative. The TPC coordinates (1) interagency views on U.S. positions for multilateral trade negotiations, (2) recommendations for the President on certain import remedies, and (3) U.S. Government policy on international investment issues, international commodity negotiations, and other trade policy matters. A.I.D. participates in the TPC (and its staff committee and review group structures) under the auspices of the office of the Director of the



International Development Cooperation Agency.

PPC represents IDCA at the TPC and in its working groups. Some LDCs are, in particular sectors, exporting products that fall under U.S. export controls or quotas. **PPC will serve as a channel between U.S.**

Government trade experts and A.I.D. Missions with information on how to help LDC exporters deal with the myriad of U.S. and international trade agreements, when this information is not available through direct communications. (Brief

descriptions of the General Agreement on Tariffs and Trade (GATT) and the U.S. Generalized System of Preferences (GSP) program, two of these agreements and trade preference programs, are provided in Appendices B and C.) PPC will also provide U.S. -, trade policy decision-making entities with information on the impact of U.S. trade policies on LDCs, and will continue its efforts to press for open U.S. and LDC economies through the trade policy coordination process.

ANNEX A

THE WHITE HOUSE

Office of the Press Secretary

FOR RELEASE AT 11:30 A.M. EDT
MONDAY, SEPTEMBER 23, 1985

**The President's Trade Policy
Action Plan**

FACT SHEET

The President's trade policy is based on five principles:

1. Free trade and fair trade are in the best interest of the citizens of the United States. Free trade produces more jobs, a more productive use of our nation's resources, more rapid innovation, and a higher standard of living. Free trade also advances our national security interests by strengthening the economic and political systems of our allies. Fair trade based upon mutually acceptable rules is necessary for support of free trade.

2. The United States plays the critical role in ensuring and promoting an open trading system. If the United States falters in its defense and promotion of the free worldwide trading system, the system will collapse, adversely affecting our national well-being.

3. The United States' role does not absolve our trading partners of a major obligation to support a more open trading system. This obligation includes: dismantling trade barriers, eliminating subsidies and other forms of unfair trade practices, and entering into trade liberalization negotiations in the GATT.

4. The international trading system is based upon cooperation. Since World War 11, we have made significant progress in moving toward an open worldwide trading system. Protectionism threatens to undermine the system. Our trading partners must join us in working to improve the system of trade that has contributed to economic growth and security of ourselves and our allies.

5. America has never been afraid to compete. When trade follows the rules, and there is an equal opportunity to compete, American business is as competitive as any. This is fair trade and we will not impair it.

When these conditions do not exist, it is unfair trade, and we will fight it,

The President has taken a number of actions to translate these principles into policy.

Making Free Trade Fair Trade

The President will vigorously pursue U.S. rights and interests in international commerce under U.S. law and the GATT, and will see that other countries live up to their obligations and trade agreements with the U.S. More specifically:

1. The President will attack foreign unfair trade practices. The President has directed the United States Trade Representative to initiate or accelerate unfair trade practice proceedings, the first time done so by a President of the United States. Other actions, when appropriate, will be taken. Proceedings accelerated or initiated so far are:

9 Japanese leather and leather footwear import restrictions;

1 European Community canned fruit subsidies;

* Korean insurance policy barriers;

* Brazil's import restrictions on micro-electronics products; and

Japanese tobacco restrictions.

2. To discourage our trading partners from seeking unfair advantage by using predatory credits to subsidize their exports, the President will propose that Congress approve a fund of \$300 million in grants which would support up to \$1 billion in tied-aid credits to maintain U.S. markets in the face of this practice,

3. The President has directed the United States Trade Representative to initiate and accelerate both bilateral and multilateral negotiations with countries where the counterfeiting or piracy of U.S. goods has occurred. The Administration will increase efforts to protect intellectual property rights (patents, copyrights, trademarks), with a view toward possible legislative or administrative initiatives,

4. The President has directed that a strike force be established among the relevant agencies of the Federal Government, with the task of identifying unfair foreign trade

practices and executing the actions necessary to counter and eliminate the unfair practices.

5. The President has directed the Secretary of State to seek time limits on the current discussions with Japan designed to open access to specific Japanese markets, at the end of which specific commitments will be evaluated and follow-up procedures begun. New sectors will be added that offer the promise of expanded U.S. exports.

Promoting Free Trade and Exports

The United States is a great trading nation. The health of our economy depends on both exports and imports. The President's goal is to preserve as free and open a trading system as possible. A free and open system will be a fair system.

1. The President seeks to engage our trading partners in multilateral negotiations in the GATT to achieve freer trade, increase access for U.S. exports, provide more effective dispute resolution, and strengthen the fabric of the international trading system. The President wants to use the multilateral negotiating process to eliminate unfair trade practices and improve access for U.S. exports, particularly agriculture and high technology, and address newer forms of international trade problems, including intellectual property protection, services trade, and investment issues.

2. The President will also explore possible bilateral and regional trade agreements that would promote more open trade and serve U.S. economic interests.

3. The President has directed the Secretary of Commerce and the Economic Policy Council, in conjunction with the President's Export Council, to review current export promotion activities with a view toward strengthening them and increasing private sector involvement. The Commerce Department will also work with state governments interested in expanding their export promoting activities.

4. To better assist workers in adjusting to the dynamics of the world trading system, the President has directed the Secretary of Labor and the Economic Policy Council to review existing worker assistance programs to assure that they promote an effective policy that contributes to maximum capacity for change, mobility, and increased productivity.

Improving the World and Domestic Economic Environments

The trade deficit has grown because economic difficulties abroad have persisted while the U.S. has been more successful in utilizing our economic opportunities. Better balance in world economic performance must be achieved.

1. To do our share in achieving the needed balance in the world economy and lowering the value of the dollar, the United States must reduce excessive government spending. The President will hold Congress to no more than the spending levels established in the Senate budget resolution.

2. The President will press for his tax reform proposal, which is essential to strengthening the economy and making U.S. businesses more competitive in international markets.

3. The President has directed the Economic and Domestic Policy Councils to review, and if warranted, seek to amend antitrust laws that impede our international competitiveness. The President will also use the trade leverage created by domestic deregulation to seek to open foreign markets.

4. The President authorized the Secretary of the Treasury to join his counterparts from other major industrial countries yesterday to announce measures to promote stronger and more balanced growth in our economies and the strengthening of foreign currencies. This will provide better markets for U.S. producers and improve America's competitive position.

5. The United States is prepared to consider the value of hosting a high-level meeting of the major industrial countries to review, implement and build upon the Group of Ten monetary studies by considering in a cooperative fashion, the policies and performance of the major industrial countries, and how these can be improved to promote convergence toward non-inflationary growth.

6. The President has also directed the Secretary of the Treasury to use the international financial institutions to encourage debt-burdened LDCs to reduce government impediments to the functioning of markets, encourage private sector production, and substitute equity capital for debt by encouraging both domestic and foreign investment.

Legislation which would reflect the President's principles and policies would include:

1. Trade *Negotiating Authority*.

Authority to support trade negotiating initiatives including:

- a new round of negotiations;
- elimination of non-tariff barriers (current authority expires January 3, 1988);
- tariff reductions; and
- compensation to other countries when the U.S. increases tariffs (through Congressional action or Customs reclassification) to avoid unilateral foreign retaliation against U.S. exports,

2. Intellectual Property *Rights*.

Further protection of *intellectual property* rights (patents, copyrights or trademarks), including:

- protecting against trade in articles that infringe U.S. process patents;
- extending the Patent term for agricultural chemicals to match that for pharmaceutical inventions;
- eliminating the requirement in Section 337 of injury to an efficiently and economically operated U.S. industry as a precondition for a relief where the International Trade Commission found a patent, trademark or copyright infringement;
- more liberal licensing of technology under the antitrust laws;
- better protecting "firmware" through amendments to U.S. copyright law; and
- eliminating Freedom of Information Act abuses by giving affected companies notice and an opportunity to oppose release of their business confidential information.

3. Export Promotion.

Promote U.S. exports through.

- submitting legislation authorizing and appropriating approximately \$300 million in grant funds to enable the Administration to offer \$1 billion in mixed credit loans to targeted buyers. This program is designed to enable U.S. exports to compete effectively in third country markets until we can eliminate predatory mixed credit competi-

tion through negotiations;

- clarifying the accounting provisions and liabilities of foreign agents under the Foreign Corrupt Practices Act of 1977 to

- and

- allowing U.S. companies to export new drugs and biologicals not yet approved by the Food and Drug Administration to countries where they can be sold lawfully.

4. Existing Trade Laws

Strengthen the antidumping and countervailing duty laws with a predictable pricing test for non-market economies, place deadlines on Section 301 dispute settlement, and establish Section 201 fast track procedure for perishable items,

ANNEX B

Background information on the General Agreement on Tariffs and Trade (GATT)

The General Agreement on Tariffs and Trade (GATT) is a multilateral agreement subscribed to by 90 governments that together account for more than four-fifths of world trade. Its basic aim is to liberalize world trade and place it on a secure basis, thereby contributing to international economic growth and development. GATT is the only multilateral instrument that sets rules for international trade; these rules govern the trade of its *member* countries and the conduct of their trade *relations* with one another.

"The substantial reduction of tariffs and other barriers to trade is a principal aim, of the GATT. During the negotiations held in GATT's first 25 years, the tariff rates for thousands of items entering into world commerce were reduced or bound against increase. The concessions agreed upon in these negotiations have affected a high proportion of the total trade of contracting parties and have indirectly affected the trade of many nonmembers as well, as many tariff concessions have been extended to all trading partners under the most-favored-nation (MFN) principle. Under this principle, countries agree to extend automatically to other trading partners the same treatment as that given to the "most favored" trading partner,

GATT's original Articles of Agreement incorporate several basic principles which all signatories agree to follow. Two of these are discussed below. The first and most basic is to conduct trade on a nondiscriminatory basis. Under the "most-favored-nation" clause, a GATT nation must treat all other signatories as favorably as any other nation when administering and applying its tariff charges. GATT gives no nation special advantages, except in certain important cases. For example, LDCs may receive preferred tariff treatment as in the Generalized System of Preferences (GSP).

A second basic principle is the concept of national treatment. Not only must a nation treat all foreign countries equally, but it also must not discriminate between foreign and domestic goods once foreign goods enter its local market. Its goal is to prevent internal domestic taxes or other regulations from replacing any tariffs removed as trade barriers.

Much of the attention of the latest round of multilateral trade negotiations (The Tokyo Round), which took place between 1973 and 1979, was designed to shape the multilateral trade system and international trade relations into the 1980s and beyond. The Tokyo Round resulted in the further lowering of many tariffs. A major new focus of that round was liberalization of nontariff measures that restricted or distorted trade, in contrast to earlier rounds of trade negotiations where tariff reduction was the primary objective. However, the negotiations revealed that many apparently unfair NTBs were actually domestic policies with various goals, some legitimate and some unfairly restricting trade.

It also defined special rules for developing countries' participation in the world trading system. Under the concept of "special and differential treatment," developing countries asked to be treated more leniently as to the degree of concessions they were expected to give in trade negotiations. They also asked the developed countries to extend the legal basis under which developing countries receive preferential treatment under the GSP. Developed countries accepted the principle of "special and differential treatment" of developing countries in areas of the negotiations where it was feasible and appropriate, including preferential tariff treatment, provided that the

developing countries would forego such special and differential treatment as their development, financial, and trade needs permitted (the concept of "graduation").

Five codes of behavior, incorporating the "special and differential" principle, were negotiated by the Tokyo Round's conclusion. They cover subsidies and countervailing duties, government procurement, technical barriers to trade (standards), import licensing procedures and customs valuation.

ANNEX C

Background Information on The U.S. Generalized System of Preferences Program (GSP)

The Generalized System of Preferences (GSP) is a program of tariff preferences granted by industrialized countries to developing countries to assist them in their economic development by encouraging greater diversification and expansion of their exports. In 1968, the United States joined with other industrialized countries in supporting the concept of granting tariff preferences as a means of facilitating development through the auspices of expanded trade rather than increased aid. With the expectation that developing countries and territories could be encouraged to become more active participants in the international trading system, 19 developed countries instituted GSP programs in the early 1970s. The United States implemented its program in 1976 pursuant to the statutory authority contained in the Trade Act of 1974.

Trade with developing countries and territories has increased dramatically since the inception of the GSP program. The U.S. GSP program currently provides duty-free treatment for approximately 3,000 products from 140 developing countries and territories; however, these GSP imports represent only about 3 percent of total U.S. imports.

The GSP program is vitally important because of: (1) its recognition that trade is an effective and cost-efficient way of promoting broad-based sustained economic development; (2) the program's ability to provide greater access for U.S. exports in the markets of developing countries; and the desire to (3) promote the integration of

developing countries into the international trading system; (4) assist developing countries in generating sufficient foreign exchange to meet their international debt obligations as well as further stimulate U.S. exports to these countries; and (5) maintain the program's role as an important element

of U.S. foreign policy with respect to developing countries. Many GSP beneficiary countries consider the program an important indication of the seriousness with which the United States views its policy of encouraging self-sufficient economic development.