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TRADE: RELATIONS WITH THE INDUSTRIALISED COUNTRIES

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Brief by Department of Trade

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OBJECTIVE

1. Generally to endorse Commission analysis while sounding a note of caution on relations with Japan.

POINTS TO MAKE

2. Generally agree with Commission analysis.

3. Confirm UK's commitment to the open trading system and its determination not to resort to large scale protectionism.

4. But other countries must also play their part. Problems over US exports of chemicals and textiles, where US domestic energy policy can be cited as unfair, are a major irritant to EC/US relations.

5. Need cautious approach to negotiation with Japan to ensure that the Community does not make concessions to the Japanese except in return for concessions of at least equal value.

BACKGROUND

Reference A: Commission paper COM(80)303 final: Relations with the Industrialised Countries.

6. Trade issues are not expected to figure very largely at the Venice Economic Summit and the Commission paper is largely, but not wholly, a description we can endorse of current issues and

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problems in developed world trade, particularly trade relations between the EC and the US and Japan. It has a rather narrow perspective because it does not cover developed countries' markets in, and dependence on, the third world.

7. Our policy is to avoid protectionist measures except where the injury to UK industry makes action necessary and fully compatible with our international commitments. This is also the line taken by the Commission and the Community generally, though some Member States (notably the Germans), defending free-trade principles, take a more hard-line attitude against any restrictions at all. In some cases anti-dumping action may be an alternative and this is more readily accepted internationally.

#### UNITED STATES

8. The potential advantages for US producers arising out of US domestic energy policy have been and will continue to be a major bilateral issue between the Community and the US. The Commission has already taken anti-dumping action on acrylic fibres and introduced quotas on imports of two types of synthetic yarn into the UK. Other anti-dumping cases against textile products and some chemicals are in the pipeline. The Germans have made clear, through their resistance to the anti-dumping case and one of the UK quotas, that they are prepared to see action only in the most exceptional cases, and that they will take a very rigorous interpretation of the Community's international trading obligations.

9. Despite the limited coverage of the synthetic yarn quotas and their relatively generous levels, the US has maintained a firm line in seeking some recompense. (The GATT provisions give them an automatic right to retaliate in order to restore a balance of concessions, regardless of whether or not the action is justified under the provisions). So far they have refrained from

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retaliation and sought compensation from the EC; this would mean that the EC would reduce some tariffs, instead of the US raising some. Their original demands were excessive and it is not yet clear whether an accommodation will be found. If there is no agreement by 20 June, there is a strong expectation that the US will retaliate against products of special interest to the UK - notably in the wool textiles area. This would almost certainly lead in turn to an argument in GATT about whether the retaliation was excessive.

10. After a long and eventually unsuccessful negotiation with the US Administration for tax and environmental concessions United States Steel (much the weakest of the big US steel firms) launched seven anti-dumping cases against Community steel exporters, including BSC, in March. As a result the Administration immediately suspended the 'Trigger Price Mechanism' whereby American steel producers were guaranteed rapid anti-dumping action if minimum reference prices were not honoured. The United States domestic procedures for deciding whether anti-dumping duties should be imposed are now in train. The independent International Trade Commission found a prima facie case that US industry was being materially injured in early May and a full investigation is now under way. Community exporters are becoming increasingly concerned at the probability of anti-dumping duties being imposed. BSC stand to lose less than other Community producers from the effective closure of the US market which would follow, but the repercussive effects on other markets - notably the UK itself - would be extremely serious for them.

11. There is therefore a strong case for asking the Commission to try to negotiate a settlement, which could involve re-instatement of the Trigger Price Mechanism at higher price levels and some

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measure of control on quantities. The sooner negotiations begin the better. Any orders that BSC take after July will be at risk from duties likely to be imposed in October; there are formidable difficulties involved in getting the Community producers to agree what would be appropriate quotas for each of them; and the longer the parties delay the more likely it is that the US Presidential election will influence the Administration in its response to pressures for tough protective action. Commissioner Davignon has had some contacts with the Administration but it may need a direct approach from Mr Jenkins to the President to get serious discussions under way. This would best be urged on Mr Jenkins privately, unless other Community leaders have been briefed to raise the matter.

#### JAPAN

12. The last section of paragraph 9, about the Community's residual quantitative restrictions on imports from Japan is likely to be contentious. France and Italy have the biggest ranges of these; we have none but we use voluntary restraint arrangements (see para 14 below), which the Japanese are happier about. Some QRs are restraints of real economic importance (e.g. on cars) while others are of very much less economic importance.

13. (Not for use). The main attack on the Commission's willingness to negotiate the removal of residual QRs can be expected to come from France and Italy. It is doubtful whether it will be possible in the short term to obtain sufficient concessions of real value from the Japanese to justify the removal of many restrictions, and whether the Germans would anyway agree to quotas on their imports from Japan so as to complete a pan-Community import policy. But it would be useful to get French and Italian QRs dismantled in the interests of a more even distribution of Japanese imports

/within

within the Community, and because we can hope to benefit from the substantial concessions the Japanese would have to make in return. So we support the Commission view that consideration should be given within the Community to whether some QRs could be eliminated, bearing in mind that we will need major concessions from the Japanese in exchange.

14. From our point of view it is voluntary restraint arrangements with Japan that are important. These arrangements are mostly informal ones between industries though some have intergovernmental backing. Our objective in any Community policy towards Japan is to avoid any threat to these arrangements unless this was part of a Community-wide policy within which our particular arrangements could be subsumed without conceding anything. If the Commission do wish to bring forward detailed proposals they will have to be scrutinised carefully in the Foreign Affairs Council.

Department of Trade

4 June 1980

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REF A

COMMISSION OF THE EUROPEAN COMMUNITIES

COM(80) 303 final

Brussels, 29th May 1980

RELATIONS WITH THE INDUSTRIALISED COUNTRIES

(Communication from the Commission to the European Council)

COM(80) 303 final

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RELATIONS WITH INDUSTRIALISED COUNTRIES

Introduction

1. This note discusses the problems to be faced after last year's successful conclusions of the GATT Tokyo Round negotiations, the prospects for trade relations between the major industrialised countries, and ten principal current issues in the Community's relations with the United States and Japan.

Progress since the Tokyo Summit

2. The Tokyo Summit was able to note the effective conclusion of these negotiations in April of last year. Thus the reference to trade policy in the Communiqué was that "the agreements reached in the Tokyo Round are an important achievement. We are committed to their early and faithful implementation. We renew our determination to fight protectionism. We want to strengthen the GATT, both to monitor the agreements reached in the MTNs and as an instrument for future policy in maintaining the open world trading system. We will welcome the full participation of as many countries as possible in these agreements and in the system as a whole."

3. The Tokyo Round agreements were formally signed in Geneva in December. The tariff concessions began to be implemented in stages on 1 January 1980 among the major participants. A wide range of MTN non-tariff barrier codes (those on subsidies and countervailing, technical barriers to trade, civil aircraft, antidumping, licensing, and meat and dairy arrangements came into effect at the beginning of this year). It is planned that the code on customs valuation will enter into force on 1 July this year and that on government procurement at the beginning of 1981.

4. These agreements have played a major part in preventing, so far, any significant outburst of protectionism. They have consolidated the multilateral trading system embodied in GATT as the basic relationship, notably between the entrepreneurial economies of Western Europe, North America and Japan. But the economic outlook and the prospects for the maintenance of a world open trading system are not encouraging.

Outlook for trade relations between industrialised countries

5. The outlook for 1980 in particular is not encouraging. The volume of world trade grew by nearly 7% in 1979, following a 6% increase in 1978, more or less in parallel with the growth of production in OECD countries from over 4% in 1978 to about 5% in 1979. GDP growth in the Community is now expected to be approximately 1 1/2% in 1980. The two immediate problems relate to inflation and the general level of economic activity over the remainder of this year. For the industrial countries as a whole the rate of increase in consumer prices has been accelerating for the past eighteen months with very little prospect of any relief. The return of two-digit inflation rates in several large industrial countries and the reversal of the downward trend of price increases in others represented, as the GATT Secretariat pointed out in February of this year, a major policy setback.

6. The economic outlook for Japan is much better than for either Europe or the US, where inflation and rising unemployment are much greater problems. Japan has gone from a very big surplus in 1978 to deficit (current account) in 1979. The American deficit has been reduced. The Community is also in current account deficit; but it additionally had in 1979 large bilateral trade deficits with both the US (\$ b.) and Japan (\$7b.). Japan per contra has large bilateral surpluses with both the U.S. and the EC.

EC and US bilateral trade with Japan

7. While no-one would argue that bilateral trading balances should be the central preoccupation of either US-Japan or EC-Japan relations, they loom very large in post-MTN thinking, being politically "visible". That is why both the Commission and the US Administration, separately, press Japan strongly to secure a real opening of the Japanese market to trade and investment. In 1979 the US bilateral trade deficit was halved while that of the Community grew. In the first 4 months of 1980 the trade gap of the EC with Japan was larger than that of the US - and this was on a much smaller volume of two-way trade. The outlook for us is gloomy since the EC has lost a lot of its competitive edge (mainly because of currency movements) and the prospect is now zero growth for total Japanese imports of manufactures, and the U.S. market shrouded in uncertainty.

Current problems

8. Against this background, protectionist pressures have strengthened generally over the last year. Low growth, higher inflation, large budgetary deficits, interest rates often at a crippling level, and general uncertainty, have made far-ranging structural adjustment in particular extremely difficult. This is not to say that a breakdown of the open world trading system is imminent or inevitable. Indeed, it is remarkable testimony to the strength in particular of the GATT mechanisms and the impact of close consultation over the last decade among the major industrialized countries that the line against "beggar-my-neighbour" policies has by and large been held. But the situation remains a dangerous one.

9. The current range of trade issues that the Community faces with the U.S. and with Japan can be exemplified as follows.  
With the U.S. :

Steel

EC steel exports to the U.S. could, in theory, be virtually brought to a halt by the present antidumping action against Community producers. The Commission has warned the U.S. Administration about the consequences of such an unacceptable development. The Administration itself is under various legal and other constraints in seeking an acceptable way out, and it is still too early to say how best to solve this problem which affects \$ 1 1/2 billion of Community exports.

"Material Injury"

One of the Community's achievements in the Tokyo Round was the insertion of a "material injury" criterion into U.S. countervailing-duty law. The first determinations of "material injury" under the new law will be made in June and will cover a number of sensitive Community items such as canned hams (E.C. exports : \$ 200 million). The Commission has made it clear to the Administration that a failure to give real meaning to the "material injury" test would undermine the credibility of U.S. implementation of the new GATT rules.

Energy and feedstock "dual pricing"; and U.S. exports of chemical fibres  
Although a start has been made in phasing out dual pricing in the U.S., the Community has had to take safeguards and antidumping action against certain American exports because of the distortions of competition already experienced, and the damage caused to Community producers.

With Japan:

Japanese imports of manufactures

To achieve a healthier relationship with the E.C., Japan must step up its imports of manufactures and processed agricultural products. There remain a number of technical and administrative difficulties in exporting to Japan, as well as protectionist quotas or tariffs for certain agricultural items and for footwear.

Residual quantitative restrictions in the Community

Japan wishes these to be terminated. Certainly it is timely to consider what start could be made, for political, trade policy and indeed industrial strategy reasons, to bring the formal basis of the bilateral relationship more up to date.

Cars

10. A current trade issue which links Europe, North America and Japan is the pressure in the U.S. to introduce import restrictions on cars, primarily against Japan but possibly also against the Community. The U.S. Administration has taken a firm stand against protectionist measures. To encourage this, Japan recently made a number of moves to facilitate imports to Japan of certain automotive parts and components. This move could benefit some Community exporters to Japan.

Conclusion

11. The maintenance of the open world trading system of the post-war years depends of course on the political will of the Governments of the major trading nations. The political will to fight protectionism and pursue liberal trade policies was successfully manifested in the conclusions of the Tokyo Round - the biggest and the most complex international trade negotiation ever held - and held at a time of severe economic recession. Moreover, it is axiomatic that the economic system of the free world is supported by the US/EC/Japan tripod. Each maintains close and varied contacts bilaterally with the other two (though the EC/Japan side of the triangle is the weakest one). There is on all sides a willingness to try to make the Tokyo Round accomplishments work and to preserve the present trading system against the forces of protectionism. But "crisis-management" - including dealing effectively with the kind of problems that are no more than exemplified in paragraph 9 above - will require a lot of determination, and hard work, in an American election year which is also a year of recession for the U.S. and Europe.