A. Introduction

1. This paper evaluates the IMF’s trade conditionality in five emerging market programs during the capital account crises of the late 1990s: Indonesia (1997), Korea (1997), Ukraine (1998), Brazil (1998), and Turkey (1999). These programs, supported by IMF Stand-By Arrangements (SBAs) or the Extended Fund Facility (EFF), were particularly high profile as they exemplified the Fund’s response to a new type of balance of payments crisis that involved massive reversals of short-term capital flows and contagion. The arrangements were also high-access, involving hitherto unprecedented loan amounts for the Fund. Brazil, Korea, and Turkey drew on the IMF’s new Supplemental Reserve Facility (SRF), which had been created expressly to provide very short-term financing on a very large scale. Table 1 summarizes the history of IMF arrangements in the five countries.

2. This paper focuses only on the trade policy aspects of these programs. The programs have been evaluated elsewhere—notably in IEO (2003), Stone (2002), IMF (2005a), IMF (2006a), and IMF (2008b)—but not from the trade policy angle. Hence, this paper will cover some familiar ground, but it will also bring a fresh perspective because the five case study countries had very similar trade regimes and trade policy issues before the onset of their crises yet widely differing experiences with trade conditionality under their IMF-supported programs. The evaluation questions addressed are:

• Did the trade conditionality conform to and carry out well a reasonable interpretation of the Fund’s mandate? Internal memos and guidance notes set out parameters for the inclusion and design of trade conditionality; key guidelines relevant for this evaluation are listed in Table 2.

• Was the trade conditionality appropriate in scope? In other words, were trade issues identified and analyzed in sufficient detail and included in program conditionality when they were critical to macroeconomic outcomes and vulnerabilities, and omitted when they were not? Such an assessment needs to be balanced against the internal guidelines prevailing at the time (Table 2).

• Was the trade conditionality sufficiently well thought out? Did it adequately reflect country-specific analysis of institutional frameworks, supply capacity, and spillovers within the economy, and was it embedded in a framework for macroeconomic policy and strategies?

• Was the Fund evenhanded and balanced in its application of trade conditionality? Were there systematic factors underlying the decision to include or exclude trade conditionality?

• Was the trade conditionality effective? Were the Fund’s views clear, persuasive, and apparently consistent with overall macroeconomic advice and the country’s other commitments, such as ongoing/future negotiations with the World Trade Organization (WTO) and regional trade agreements? Did the conditionality help spur debate and develop political consensus for change? Was it implemented, and were the reforms sustained?

B. Indonesia

Trade policy regime and IMF advice before the 1997 program

3. In the late 1990s, Indonesia’s trade regime was rated by the IMF as “moderately restrictive.” A series of reform packages beginning a decade earlier had sought to shift the economy away from an inward-looking import substitution strategy by reducing tariffs and other trade restrictions and liberalizing investment regulations in some sectors (Box 1). But the liberalization was not complete. In 1997, Indonesia scored 5 on the IMF’s 10-point aggregate Trade Restrictiveness Index (TRI), based on a “relatively open” tariff rating of 2 (out of 5) and a “moderate” nontariff barrier rating of 2 (out of 3). The unweighted average tariff rate was 13 percent. About one-fourth of imports were subject to nontariff barriers including quantitative restrictions and
<table>
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<th>Type of Arrangement</th>
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Source: IMF Finance Department.
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<tr>
<th>Date</th>
<th>Guidance</th>
<th>Key Point(s)</th>
</tr>
</thead>
<tbody>
<tr>
<td>November 17, 1994</td>
<td>Concluding Remarks by the Acting Chairman: Conditionality Review—Distilling the Main Messages and Direction for Further Work (IMF, 1994b)</td>
<td>“[F]rom the start, Fund supported programs should give high priority to a coherent set of structural measures, institution building, and removal of distortions that will stimulate supply responses and investment.”</td>
</tr>
<tr>
<td>November 1, 1995</td>
<td>Reference Note on WTO Consistency (IMF, 1995b)</td>
<td>Fund staff should identify policy measures that are potentially inconsistent with WTO rules at an early stage; encourage the authorities to clarify the issue directly with the WTO; and explore alternative measures with the authorities.</td>
</tr>
<tr>
<td>October 30, 1997</td>
<td>Summing Up by the Acting Chairman: Trade Liberalization in Fund-Supported Programs (IMF, 1997h)</td>
<td>Trade liberalization should be pursued as part of a broad-based adjustment program, i.e., staff should ensure an appropriate overall policy mix and a critical mass of complementary structural measures, including financial sector reform, privatization, and other external reforms.</td>
</tr>
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<td>Greater emphasis on clearly defined, quantifiable, and monitorable medium-term policy objectives is crucial for enhancing prospects for success of trade reform. Programs should also emphasize intermediate targets to measure progress and supporting policies, and should be accompanied by an early public announcement of the medium-term targets.</td>
</tr>
<tr>
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<td>Trade liberalization efforts must continue to be undertaken in close cooperation with the World Bank and the WTO.</td>
</tr>
<tr>
<td>April 2, 1998</td>
<td>Index of Aggregate Trade Restrictiveness—Operational Implications (IMF, 1998f)</td>
<td>Staff should begin to assess the trade reforms of program countries by including in staff reports on new medium-term (two or more years) adjustment programs the estimated Trade Restrictiveness Index (TRI) at the outset of programs, and after the implementation of program measures.</td>
</tr>
<tr>
<td>January 8, 1999</td>
<td>Note on Import Surcharges (IMF, 1999a)</td>
<td>In line with the Fund’s mandate, and consistent with WTO principles, the Fund opposes surcharges in the great majority of cases. In the event they are introduced, the surcharge should be uniform across all imports, on a temporary basis, and subject to a pre-announced timetable for elimination.</td>
</tr>
<tr>
<td>July 20, 1999</td>
<td>Guidelines on Designing and Implementing Trade Policy Reforms (IMF, 1999f)</td>
<td>Trade reform should first target the least transparent and most restrictive elements of the trade regime, particularly nontariff barriers, export restrictions, and exemptions. Thereafter, emphasis should be placed on attaining low and relatively uniform tariff protection, but commencement of tariff reduction need not wait until the elimination of nontariff barriers is complete.</td>
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<td></td>
<td>Fund advice should be guided by considerations of efficiency in resource allocation. Thus, trade reform programs will typically need to be more ambitious than is required under the WTO. However, such reforms should not contravene countries’ obligations under the WTO.</td>
</tr>
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<td></td>
<td>Fund staff should stress that trade reforms need to be accompanied by complementary policies, because of the strong mutual and supporting links between trade policy and macroeconomic and structural policies.</td>
</tr>
<tr>
<td>September 18, 2000</td>
<td>Streamlining Structural Conditionality—Interim Guidance Note (IMF, 2000c)</td>
<td>Fund structural conditionality should cover only reforms that are relevant for a program’s macroeconomic objectives. The assessment of macro-relevance should be established on a case-by-case basis and made explicit in program documents.</td>
</tr>
<tr>
<td></td>
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<td>Structural reforms that are macro-relevant and critical for the achievement of the program’s macroeconomic objectives must be covered by Fund conditionality.</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Structural reforms that are macro-relevant but not macro-critical and within the Fund’s core areas of responsibility may be covered by Fund conditionality. However, the presumption would be that structural performance criteria would not be used in these cases, and that prior actions or structural benchmarks would be used sparingly and would require justification.</td>
</tr>
<tr>
<td>September 20, 2001</td>
<td>Concluding Remarks by the Acting Chair: Trade Issues—Role of the Fund (IMF, 2001b)</td>
<td>Any conditionality pertaining to trade measures should be consistent with the guidelines and evolving practice for streamlining conditionality.</td>
</tr>
</tbody>
</table>
Box 1. Indonesia: Trade Liberalization During 1985–96

A series of reform packages beginning in 1985 aimed to shift the Indonesian economy away from a heavy dependence on oil exports and import substitution (Fane, 1996; Feridhanusetyawan and Pangestu, 2003). During 1985–90, tariffs were rationalized and reduced across the board to an unweighted average rate of around 20 percent and some nontariff barriers (such as import licensing and import monopolies) were removed. Other important reforms included transferring customs inspection duties to a private Swiss surveying company, improving the duty drawback scheme for exporters, and relaxing restrictions on foreign direct investment. Reform fatigue set in 1991—a few more nontariff barriers were abolished (e.g., import bans on certain steel products and export bans on copra and palm oil were abolished) but average tariff reduction was minimal. Trade liberalization was reinvigorated in 1994, the year Indonesia hosted the Asia-Pacific Economic Cooperation (APEC) summit and signed the Bogor Declaration to achieve free trade and investment within APEC by 2020. In May 1995, the unweighted average tariff was lowered to 15 percent and a comprehensive program of tariff reductions was announced to lower most tariffs to 0–5 percent by 2003, in line with Indonesia’s WTO commitments and the accelerated ASEAN Free Trade Area (AFTA)’s common effective preferential tariff scheme. This was followed by a trade liberalization package in January 1996, with further (relatively small) tariff reductions, reductions in import licensing, and measures to enhance export competitiveness (e.g., extending the duty drawback facility, easing import and export restrictions on foreign-owned exporting firms, and removing a number of export taxes) and another package in June 1996, which lowered the unweighted average tariff rate to 13 percent and included measures to simplify export procedures (e.g., eliminating export inspections and reducing documentation requirements).

Several preferential policies also emerged during the 1990s. Among the most controversial were the establishment in 1990 of a Clove Marketing Board run by one of the President’s sons; a 20 percent tariff surcharge on propylene and ethylene imports in 1993 to protect a petrochemical complex owned by another of the President’s sons; and preferential tax and duty arrangements for the national car, the Timor, in 1996. But Fane (1996) notes that these interventions were “of less quantitative importance than the very large reductions in trade and investment barriers which [had] occurred since the mid-1980s.”

4. Indonesia’s national car project came under dispute in the WTO in 1996. The project, launched by President Soeharto in February of that year, gave a three-year exemption from import duties and luxury taxes (averaging 20 percent) to Indonesian companies that manufactured cars locally using an Indonesian brand name and predominantly local parts. Only one company qualified for this privileged tax treatment—the automobile manufacturing company in the Timor Putra National (TPN) group, a holding company created and owned by the President’s youngest son. However, the national car, the Timor, was actually produced abroad by a Korean company, Kia Motors, in a joint venture with TPN, and imported duty-free into Indonesia. The special advantages given to TPN and the national car project were widely criticized, especially by competing automobile manufacturing companies. In October 1996, Japan, the European Union, and the United States filed suits with the WTO’s Dispute Settlement Body against Indonesia’s national car program, claiming that the tax and tariff exemptions were in violation of Indonesia’s obligations under various WTO agreements. A dispute settlement panel was established in June 1997.

5. Indonesia’s financial system had undergone significant liberalization by the mid-1990s, although restrictions remained on foreign entry. Major reforms over the previous decade and a half had included deregulation of interest rates, reduction in the coverage of directed credit schemes, granting of licenses for new private banks and a decline in the role of the state banks. The 10 foreign banks operating in Indonesia in 1997 obtained their licenses in the late 1960s. Since then, the entry of foreign banks was limited through the requirement either to form joint ventures (with a maximum of 85 percent foreign ownership) or to buy shares of domestic banks.
on the stock exchange, where the maximum foreign holding was set at 49 percent (Gulde, 1997).

6. The IMF’s trade policy advice to Indonesia during 1996–97 emphasized further reduction of all forms of trade protection. During the 1996 and 1997 Article IV consultations, IMF staff urged the Indonesian authorities to eliminate nontariff barriers, lower tariffs, remove export controls, dismantle private and public import and export monopolies in key commodities, and abolish ad hoc tax exemptions and privileges (Box 2) (IMF, 1997c). The IMF argued that eliminating the remaining structural rigidities in the economy was essential for improving productivity, efficiency, and economic governance (IMF, 1997d); it stressed that the existence of monopolies and cartels and the granting of special privileges to individual firms undermined investor confidence. The 1997 Article IV mission also proposed an easing of the regulations that limited the entry of new foreign banks.

7. The IMF mission drew on econometric work by staff suggesting that further trade liberalization would improve Indonesia’s medium-term prospects for export growth. A selected issues paper (SIP) for the 1997 Article IV consultation (McDermott, 1997) estimated that trade liberalization measures (specifically, the reduction of import tariffs and export taxes) during 1980–94 accounted for 40 percent of the expansion of Indonesia’s manufactured exports over that period. Counterfactual simulations indicated that more trade liberalization would have resulted in even better performance, and that future liberalization would lead to further improvements in export performance. But there was no analysis by staff, or reference to analysis by others, of the costs of specific policies highlighted in the 1997 staff report, such as the import and distribution monopoly in agricultural products and the export restrictions in forestry products. And while a separate SIP (Gulde, 1997) identified concentrated bank ownership as one of the main problems of the Indonesian banking sector, that paper did not include measures to liberalize financial services trade (such as easing the entry of

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**Box 2. Indonesia: Trade and Industrial Liberalization Issues Listed in the 1997 Article IV Staff Report**

1. **External trade restrictions**
   - Domestic protection is still high and variable, with an effective rate of protection for the import-competing sector of 28 percent.
   - Nontariff barriers affect 23 percent of imports, including quantitative restrictions on certain goods and exclusive import rights.
   - Export bans and export taxes affect key products (especially palm oil, rattan, and other agricultural and forestry products) and levies are extensive.

   **Staff recommendations:**
   - Lower all tariffs that are above 25 percent.
   - Complete WTO and AFTA commitments, including lowering most tariffs to 0 percent or 5 percent and others to 10 percent by 2003.
   - Eliminate nontariff barriers especially restrictions on wheat, rice, sugar, and oilseeds.
   - Abolish export taxes, licensing requirements, and levies, and simplify administrative procedures.

2. **Marketing regulations**
   - Exclusive licensing rules grant monopoly distribution rights for rice, cloves, soybeans, and flour.
   - Forestry concessions are restricted to existing processors. Cartels dominate cement, plywood, and paper sectors.
   - Price controls exist for rice, sugar, cement, petroleum products, bus and rail transportation, gas, and electricity.

   **Staff recommendations:**
   - Open industries to competition.
   - Establish and enforce competition law which prohibits anticompetitive practices, including cartels.
   - Eliminate remaining price controls.

3. **Foreign investment restrictions**
   - Six sectors are closed to foreign direct investment including taxi and bus transportation and local shipping, and another 17 sectors are restricted (including milk, saw milling, plywood, and aircraft).

   **Staff recommendations:**
   - Liberalize restrictions on foreign direct investment.

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2 Trade distortions were proxied by the ratio of import tariff revenue to total imports plus the ratio of export tax revenue to total exports, smoothed to remove cyclical fluctuations; nontariff barriers and export bans were excluded due to data limitations. Based on this measure, trade distortions fell dramatically from around 18 percent in 1970 to around 5 percent in 1996 (McDermott, 1997).
and received, financial support for strengthening Indonesia’s banking sector.

8. The authorities agreed in principle with the desirability of further trade liberalization but were noncommittal about removing special concessions. Indonesia already had commitments to the WTO and the ASEAN Free Trade Area (AFTA) for further trade liberalization. Under those agreements, most tariffs would be reduced to within the range of 0–10 percent, with an estimated average unweighted tariff rate of 7 percent, by 2003. With regard to the elimination of marketing monopolies and special privileges, the authorities indicated only that those issues “would be addressed in a phased manner” (IMF, 1997c). The authorities did not think it necessary to relax entry requirements for foreign banks, pointing to the large growth in the number of foreign institutions operating in cooperation with local enterprises as evidence that the existing regulations were not a major constraint.

The 1997 SBA-supported program

9. Not long after the conclusion of the 1997 Article IV consultation, Indonesia was severely affected by market contagion in the region. The rupiah, which had been allowed to float in August 1997, came under intense pressure in the wake of the Thai baht crisis, forcing the authorities to raise short-term interest rates to very high levels. The rupiah depreciation and high interest rates created difficulties for the banking and corporate sectors, precipitating a financial crisis. The loss of market confidence surprised the IMF, which had considered Indonesia’s macroeconomic policies to be sound. In October 1997, after several weeks of intensive consultations with Fund staff and management, the Indonesian authorities sought, and received, financial support for a three-year program under the SBA. The SBA-supported program was jointly funded by the World Bank and the Asian Development Bank.

10. With no ready explanation for the cause of the crisis, IMF staff homed in on the economy’s underlying structural problems. The theory was that these problems, such as banking sector weaknesses, trade distortions, and poor governance, were masked by Indonesia’s strong fundamentals before the crisis but came to the fore once the crisis hit. According to the staff, the weak banking system exposed the country to a shift in financial market sentiment; the lack of transparency in decisions affecting the business environment increased uncertainty and adversely affected investor confidence; and long-standing rigidities in the form of domestic trade regulations and import monopolies impeded economic efficiency and competitiveness. Although a few Executive Directors were unconvinced by this theory, the IMF Board endorsed the wide-ranging adjustment program, whose key planks included restructuring the financial sector and eliminating impediments to foreign and domestic trade.

11. From the start, IMF management instructed staff to take a demanding stance on structural measures, including various trade-related policies. Targeted for elimination were import restrictions, various monopolies, and some large national projects linked to the President’s family and friends. IMF staff and management were advised by the “Berkeley mafia,” a group of U.S.-educated Indonesian economists, that cronyism and corruption (“the family”) were at the root of Indonesia’s problems and were scaring off much-needed foreign investment. The IMF staff worked closely with the Indonesian economic team, a group of reform-minded ministers who were themselves anxious to deal with some of those problems and wanted the Fund’s help to counter opposition from other ministers who favored active industrial policies. The IMF staff were also told to draw on the World Bank, which had a field office and a large presence in Jakarta.

12. Obtaining agreement on a critical mass of structural reforms proved to be the most difficult part of the program negotiations. Once in the field, the IMF mission found it could get little traction in this area with the President. The national car program, Bulog’s trading monopoly on food products, the plywood cartel, and strategic industries were particularly contentious issues. The mission was under pressure from IMF headquarters to do more; even though the national car case was concurrently being deliberated at the WTO, the IMF’s then Policy Development and Review Department (PDR)

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3 In June 1997, the government announced another trade deregulation package, reducing import tariffs (to an unweighted average of 12 percent), easing the public sector monopoly on raw sugar, cutting the export tax on crude palm oil and its derivatives, and easing customs documentation requirements for exports. In September 1997, import duties on a number of raw materials and intermediate products were reduced and preshipment financing was provided to stimulate exports.

4 At the Board discussion of the 1997 Article IV consultation, the Indonesian Executive Director quoted from a Financial Times editorial of June 13, 1996 which criticized industrial countries (particularly the United States and the European Union) for warning developing countries such as Indonesia (as well as Brazil, China, and Malaysia) against using infant-industry protection to support the development of automobile manufacturing while they themselves engaged in equally egregious policies to protect their own industries (IMF, 1998).

5 The summing up of the Board discussion of the 1997 Article IV consultation in July 1997 stated that “the strong fundamentals of the Indonesian economy had helped it to largely avoid the contagion effects from events in the region” (IMF, 1997d).

6 One Board member likened the program to applying a broad-spectrum antibiotic.
The import monopoly of soybean, garlic, and wheat flour imports was replaced by import tariffs of 10–20 percent on the three commodities, to be reduced to 5 percent in 2003. Bulog retained its distribution monopoly of wheat flour in the domestic market for the next three to five years, and continued to maintain its monopoly on rice and sugar.

13. When the SBA-supported program faltered within weeks of its seemingly successful launch, IMF staff pinpointed policy slippages in every area and called for further trade reforms to help restore market confidence. While the tariff reductions in chemicals, steel, and fishery products and the liberalization of imports of wheat and wheat flour, soybeans, and garlic were implemented as planned, at the same time the government simultaneously introduced a new export ban on palm oil to alleviate domestic shortages of cooking oil. The IMF Board specified several structural measures that were needed immediately to bring the program back on track, including: ceasing special privileges and protections for private projects and companies, particularly the national airline project; dismantling Bulog’s control over domestic distribution and eliminating its import monopoly in sugar; dismantling export cartels, notably for plywood and cloves; and liberalizing foreign investment regulations for banks. Those measures, plus several additional ones, were included in the revised MEFP of January 15, 1998 (Table 3).

14. But the government’s commitment to reform was widely questioned. A few days after signing the revised MEFP, the President announced that the national car and airplane projects would continue without state assistance. In February 1998, the government announced that the clove monopoly would be replaced by a “partnership” of the Clove Marketing Board, cooperatives, and clove-cigarette factories that would function in the same way as the original monopoly. In March 1998, the President named as the new trade minister his close friend who ran Apkindo, the plywood export cartel that the IMF wanted dismantled. While Apkindo’s formal authority to set prices and output was abolished, the cartel shortly afterwards instituted a new centralized shipping service to enable it to retain de facto control of the sector (IMF, 1998h).

15. Meanwhile, Indonesia’s trade flows all but seized up. As the banking system practically ceased operating, foreign banks stopped accepting letters of credit written by Indonesian banks, and firms whose banks had been closed had difficulty finding new banks to service their needs. There were reports of shipments of food into Indonesia being delayed and exporters with confirmed orders being unable to import their inputs. The Singapore government proposed a multilateral facility to guarantee trade finance, but the G-7 countries, Indonesia’s largest trading partners, preferred to rely on bilateral trade financing deals to help their own exporters.

16. Food prices skyrocketed. Several factors were responsible, including a drought which affected the rice crop; the sharp depreciation of the rupiah which raised the price of food imports; the collapse of the banking system, which made it difficult for food importers to open letters of credit; and the dismantling of Bulog’s monopolies on agricultural commodities, which affected the agency’s role in food price stabilization and food distribution. Expectations of large increases in food prices led to speculative and panic-driven hoarding, which exacerbated the inflation and led to riots. IMF staff advised the government to reduce tariffs on imported food and eliminate restrictions on inter- and intraprovincial trade. But an...
Table 3. Indonesia: Key Trade Liberalization Measures under the 1997 SBA-Supported Program

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<tbody>
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<td><strong>Tariffs</strong></td>
<td><strong>Nontariff Barriers</strong></td>
</tr>
<tr>
<td>Reduce tariffs on most chemical products by 5 percentage points and tariffs on fishery products from 10–20 percent to 5 percent by January 1, 1998.</td>
<td>Cut export taxes on rattan, leather, cork, ores and waste aluminum products in November 1997.</td>
</tr>
<tr>
<td>Phase out any remaining quantitative import restrictions and other nontariff barriers that protect domestic production (other than those that may be justified for health, safety, environment and security reasons) over the program period.</td>
<td>Implement ahead of schedule the ruling of the WTO dispute panel with respect to the national car project.</td>
</tr>
<tr>
<td>Reduce tariffs on items currently subject to rates of 15–25 percent by 5 percentage points by end-March 1998.</td>
<td>Modify regulations concerning foreign ownership of financial institutions to facilitate entry of international banks and investors into the Indonesian banking system.</td>
</tr>
<tr>
<td>Reduce most tariffs for steel/metals beginning January 1, 1999.</td>
<td>Simplify and further expand the list of activities open to foreign investors over the next three years.</td>
</tr>
<tr>
<td>Reduce tariffs on chemical, steel/metal and fishery products further to 5–10 percent by 2003.</td>
<td>Study the retail sector with a view to partially opening this sector up to foreign investors.</td>
</tr>
<tr>
<td>Reduce temporary import tariffs on soybeans and dried garlic (20 percent) and wheat flour (10 percent) to 5 percent by 2003.</td>
<td></td>
</tr>
<tr>
<td>Cut tariffs on all food items to a maximum of 5 percent; reduce tariffs on nonfood agricultural products by 5 percentage points by February 1, 1998.</td>
<td></td>
</tr>
<tr>
<td>Reduce tariffs on nonfood agricultural products to a maximum of 10 percent by 2003.</td>
<td></td>
</tr>
<tr>
<td>Abolish import restrictions on all new and used ships by February 1, 1998.</td>
<td>Reduce export taxes on logs, sawn timber, rattan, and minerals to a maximum of 10 percent ad valorem and impose appropriate resource rent taxes in March 1998.</td>
</tr>
<tr>
<td>Dissolve restrictive marketing arrangements for cement, paper and plywood; allow cement producers to export with only a general exporter's license by February 1, 1998.</td>
<td>Remove the recently imposed ban on palm oil exports and replace it by an export tax not exceeding 20 percent in March 1998.</td>
</tr>
<tr>
<td>Remove the recently imposed ban on palm oil exports and replace it by an export tax not exceeding 20 percent in March 1998.</td>
<td>Replace remaining export taxes and levies by resource rent taxes as appropriate; eliminate all other export restrictions over the program period.</td>
</tr>
<tr>
<td>Remove restrictions on branching of foreign banks by February 1, 1998.</td>
<td>Dissolve restrictive marketing arrangements for cement, paper and plywood; allow cement producers to export with only a general exporter's license by February 1, 1998.</td>
</tr>
<tr>
<td>Lift restrictions on branching of foreign banks by February 1, 1998.</td>
<td>Limit Bulog’s monopoly on rice; take effective action to allow free competition in the sale or distribution of flour and the importation and marketing of sugar by February 1, 1998.</td>
</tr>
<tr>
<td>Lift restrictions on branching of foreign banks by February 1, 1998.</td>
<td>Discontinue special tax, customs, or credit privileges granted to the national car by January 1998.</td>
</tr>
<tr>
<td>Lift restrictions on branching of foreign banks by February 1, 1998.</td>
<td>Lift restrictions on branching of foreign banks by February 1, 1998.</td>
</tr>
<tr>
<td>Lift restrictions on branching of foreign banks by February 1, 1998.</td>
<td>Submit to the parliament a draft law to eliminate restrictions on foreign investment in listed banks by June 30, 1998.</td>
</tr>
<tr>
<td>Lift restrictions on branching of foreign banks by February 1, 1998.</td>
<td>Issue a revised and shortened negative list of activities closed to foreign investors by June 30, 1998.</td>
</tr>
</tbody>
</table>
### Table 3 (concluded)

<table>
<thead>
<tr>
<th>Tariffs</th>
<th>Nontariff Barriers</th>
<th>Export Taxes/ Restrictions</th>
<th>State Trading Monopolies</th>
<th>Trade-Related Subsidies</th>
<th>Trade in Services</th>
</tr>
</thead>
<tbody>
<tr>
<td>MEFP, April 10, 1998 (IMF, 1998g)</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Reduce export taxes on logs, sawn timber, rattan, and minerals to: 30 percent by April 22, 1998. [Prior action for logs and sawn timber]; 20 percent by end-December 1998 [Structural performance criterion for logs and sawn timber]; 15 percent by end-December 1999; 10 percent by end-December 2000.</td>
<td></td>
<td></td>
<td>Announce dismantling of the joint marketing body for plywood by end-March 1998. [Prior action]</td>
<td></td>
<td>Lift restrictions on foreign investment in wholesale trade by April 22, 1998. [Prior action]</td>
</tr>
<tr>
<td>Phase in resource rent taxes on logs, sawn timber, rattan, and minerals.</td>
<td>Replace quantitative restrictions on palm oil, olein, and stearin with an export tax of no more than 40 percent by April 22, 1998. [Prior action]</td>
<td>Review the export tax on palm oil, olein, and stearin regularly for possible reduction based on market prices and the exchange rate, and reduce it to 10 percent by end-December 1999.</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

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1 Indicates that the measure was implemented on schedule.
2 Indicates that the measure was subsequently modified.
The staff had also insisted on the elimination of fuel subsidies and export restrictions on palm oil, which may have exacerbated the problem by raising the price of fuel and cooking oil.

17. The first program review was prolonged and contentious, and the economic and political situation deteriorated even further. The IMF scaled down some of its demands, notably by allowing the government to continue subsidizing food not just through Bulog but also through private sector importers. But it also included a range of prior actions on log export taxes, the plywood monopoly, palm oil export restrictions, and liberalization of wholesale trade (Table 3). Social unrest boiled over in May 1998; widespread rioting and looting severely undermined business confidence, especially within the ethnic Chinese community, and damaged the distribution system. The Soeharto government fell and was replaced by that of B. J. Habibie.

18. When the SBA-supported program was cancelled and replaced with an EFF arrangement in July 1998, the existing trade conditionality was carried over to the new program. The reduction of export taxes on logs and sawn timber to 20 percent was elevated to a performance criterion. Food security issues took on greater importance; as one of the measures to stabilize the rice market, the government eliminated Bulog’s last remaining monopoly and allowed private traders to import rice (IMF, 1998q). The focus of trade-related conditionality shifted towards privatization, introducing a competition law and an investment law establishing equal treatment for domestic and foreign investors, and developing mechanisms for regular adjustment of administered food and fuel price increases. The World Bank assumed a leading role in issues related to trade policy and trade financing, privatization, environmental policies, food security, and the social safety net (IMF, 1998q).

19. The 1998 EFF-supported program was followed by another EFF-supported program in January 2000, with further trade policy commitments. The MEFP for the second EFF-supported program included commitments to: establish a three-tier tariff structure (0 percent, 5 percent, and 10 percent) for all goods except alcohol and automobiles by end-2003; eliminate all exemptions from import tariffs (except those that were part of international agreements) and remove all existing nontariff barriers (except those maintained for health and safety reasons) during the program period; review the forestry sector taxation policy in consultation with the World Bank in January 2000, and ensure that the forest resource royalty rate captured at least 60 percent of the economic rent from logs; and eliminate all other export restrictions (e.g., licensing requirements or government approval on logs, coffee, and wood products) by end-2000, with the exception of those needed under the international agreements. At the same time, the program allowed for new transitional import tariffs on rice (a specific tariff to be applied through August 2000) and sugar (a 25 percent import tariff to be phased down over three years) (IMF, 2000a).

**Assessment**

20. Indonesia’s SBA-supported program was one of the prominent IMF arrangements of the late 1990s that led to a rethink of structural conditionality. Critics such as Feldstein (1998) and Radelet and Sachs (1998) argued that the structural reforms were simply a distraction from the financial crisis. Later IEO (2003) concurred, noting that “detailed and extensive structural conditionality, particularly in areas that are not macro-critical, is not helpful to crisis resolution” and that “[t]he crisis should not be used as an opportunity to seek a long agenda of reforms just because leverage is high, irrespective of how justifiable they may be on merits.”

21. At the time, however, the existing guidelines were broad enough to include trade liberalization as a normal part of IMF-supported programs (Table 2). PDR had developed the TRI in August 1997 and had started to think about using this in designing and monitoring the trade liberalization components of Fund-supported programs. In November 1997, PDR staff calculated in an internal memo that Indonesia’s SBA would take the country’s TRI from 5 to 1 within two to three years, but hesitated to publicize the figures, because the methodology had limitations (e.g., it did not incorporate tariff dispersion and exemptions) and because it would draw attention to the relatively weak trade policy content of Thailand’s SBA-supported program, which had been signed three months earlier.11

22. The trade policy conditionality in Indonesia’s SBA-supported program was not well thought-out. Trade liberalization and overall structural reform were seen by IMF staff and management as crucial to reestablishing investor confidence by signaling a clean break with the past. But the staff were clearly out of their depth when it came to designing and negotiating trade conditionality, and the World Bank’s (limited, mostly microeconomic) input was not found to be particularly helpful. IMF staff did not present a convincing macroeconomic case for why those particular trade reforms were necessary other than arguing in general terms that the reforms

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11 The memo noted that Thailand’s TRI was 6 in 1997 but its SBA program involved no trade liberalization measures; in fact, import tariffs were increased on 12 consumer goods items for revenue reasons.
would increase economic efficiency. In fact, the standard “small country” assumption did not apply to Indonesia’s trade in many commodities, and some of Indonesia’s trade restrictions were linked to wider problems, such as food security and forestry management, in which the Fund had no mandate and no expertise. For example, Bulog could not be simply wiped out and replaced by competitive private traders—dismantling the complex system of price setting and import and distribution monopolies created side effects that staff did not foresee, such as increased uncertainty and food price volatility. Reducing export restrictions on logs contributed to the deforestation problem, prompting widespread criticism by environmental groups (Barr, 2001; Mainhardt, 2001; Tockman, 2001). Some trade liberalization measures were futile: reducing import tariffs on food was of little help when firms could not obtain trade credit to import food and the distribution network had been wrecked.

23. Some of the trade policy conditionality came close to overstepping the IMF’s boundaries. The WTO’s dispute settlement panel had already started to decide the case brought by Japan, the United States, and the European Union against the national car project, but the IMF would not wait for the outcome. By insisting that Indonesia implement ahead of schedule the ruling of the WTO dispute panel, the Fund essentially prejudged the panel’s decision and overrode the compliance period that was allowed under WTO rules (typically around 15 months). In addition, commitments made under the Fund-supported program to liberalize trade in financial services, such as lifting restrictions on branching of foreign banks and on foreign investment in listed banks, were bound as part of Indonesia’s commitments under the General Agreement on Trade in Services (GATS) (IMF, 1998a), whereas IMF guidelines had explicitly stated that the Fund could not require a borrowing country to make a binding commitment to the WTO on trade liberalization that was undertaken in the context of a Fund-supported program (Table 2).

24. In the end, the trade policy conditionality was not very effective. By the IMF’s measure, Indonesia’s TRI fell from 5 to 4 in 1998 with no change thereafter. The improvement was entirely due to tariff reductions—the (unweighted) average tariff was reduced from 13 percent to 9.5 percent in 1998 and, in line with Indonesia’s commitments to the WTO and AFTA, gradually down to 7 percent in 2003. The success of the other trade measures was mixed; Khatri (2004) noted that the sweeping “regime change” initiated by the SBA program resulted in less predictability for businesses, and some of the reforms were subsequently reversed. The outcomes of some of the more prominent trade policy commitments are discussed below:

- **The national car.** In January 1998, the government discontinued all special tax, customs, and credit privileges granted to the national car (IMF, 1998g). In July 1998, the WTO panel ruled that the local content requirements and special privileges were in violation of Indonesia’s WTO commitments. Production of the Timor car ceased shortly afterwards. Kia Motors formally withdrew from the joint venture in 1999. TPN was taken over by the Indonesian Bank Restructuring Agency. In early 2000, the Indonesian government reimposed the ban on luxury vehicle imports and negotiated with Kia to revive the national car project, but the agreement with Kia fell apart in 2001 in a dispute over tax incentives (Hale, 2001). The government remains embroiled in a lawsuit with TPN’s owners over the sale of the company’s assets.

- **Bulog’s soybean, wheat, and sugar monopolies.** The government dismantled Bulog’s trading monopoly in soybeans, garlic, and wheat flour in January 1998 and eliminated Bulog’s trading monopoly in sugar and sole distribution rights in wheat flour in June/July 1998; both steps were taken a couple of months later than indicated in the MEFPs (IMF, 1997i, 1998a). However, there was little additional competition as private sector participation in those activities was inhibited by (exchange rate) subsidies that were granted only to Bulog (IMF, 1998b). The government extended Bulog’s subsidies to all market participants, also a couple of months later than indicated in the MEFP (IMF, 1998g). However, the subsidized commodities were promptly re-exported for a profit, causing the government to impose export bans in July 1998 to ensure adequate domestic supplies (IMF, 1998n). In September 1998, the subsidies on sugar, wheat, and soybeans were abolished together with their import duties, and

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12 IMF staff and management justified some of the reforms as necessary to correct misgovernance—an argument that was probably valid but should not have been expected to win over the President (“RI’s macroeconomy affected by graft, monopoly,” Jakarta Post, November 12, 1997).

13 The panel found, inter alia, that Indonesia had acted inconsistently with Article 2 of the Trade-Related Investment Measures Agreement and Articles I and III:2 of the GATT 1994, and recommended that the Dispute Settlement Body request Indonesia to bring its measures into conformity with its obligations under the WTO Agreement. See http://www.wto.org/english/tratop_e/dispu_e/cases_e/ds54_e.htm.

14 “Suharto’s son sues Indonesian minister over car case,” Reuters, August 12, 2008.
Bulog’s imports of those commodities ceased (IMF, 1998a). The export bans were lifted in May 1999. As noted earlier, in early 2000, the government—with the Fund’s approval—reimposed a (transitional) 25 percent tariff on sugar imports to protect the domestic industry (IMF, 2000a). The following year, the government—without the Fund’s approval—limited the number of sugar importers to four state-owned plantations; as none of the four had the experience or the funding to import sugar, the task fell back to Bulog. In 2003, Bulog was transformed into a semi-profit-oriented state-owned company with an undefined but potentially wide-ranging role.\footnote{17}

- **Export taxes/restrictions on palm oil.** The government banned the export of all crude palm oil products in January 1998 in an effort to stabilize the domestic price of cooking oil, but agreed to replace the ban with an export tax of not more than 20 percent after March 1998 (IMF, 1998a). However, the move was postponed in the face of soaring international prices for crude palm oil and its derivatives. In April 1998, the commitment was revised to an export tax of no more than 40 percent, to be reduced to 10 percent by end-1999 (IMF, 1998g). The export tax was raised to 60 percent in July 1998. The high export tax did not result in lower prices for cooking oil—with the depreciated rupiah, exports were still more profitable than domestic sales—forcing the government to control the distribution of the commodity through Bulog. Only when international crude palm oil prices began a downward trend was the export tax cut—to 40 percent in February 1999, 30 percent in June 1999, and 10 percent in July 1999.

- **Export taxes/restrictions on logs.** The government initially committed to reduce export taxes on logs and sawn timber to 10 percent (from 200 percent) and impose appropriate resource rent taxes by March 1998 (IMF, 1998a). This was subsequently revised to a more gradual timetable of export tax reductions: to 30 percent by mid-April, 1998, 20 percent by end-1998, 15 percent by end-1999, and 10 percent by end-2000 (IMF, 1998g). The reductions were implemented on schedule except for the second one (a performance criterion under the 1998 EFF-supported program), which was delayed by three months. Log exports increased. Environmentalists complained that the export tax reduction encouraged illegal logging and the domestic wood-processing industry complained of a shortage of raw materials. In response, the government imposed a temporary ban on log exports in October 2001, and made the ban permanent in June 2002 (Resosudarmo and Yusuf, 2006).

25. The IMF missed the opportunity to take a proactive role in coordinating trade finance during the financial crisis. IMF management was unwilling to work with the Singaporeans and others to come up with a multilateral solution and was unresponsive to the entreaties of the WTO Director-General to do more to resolve the problem of trade finance.\footnote{18} Given that the IMF was, by that time, being widely blamed for exacerbating the financial crisis, a visible effort to take the lead in coordinating trade finance would have gone some way toward rehabilitating its public image.

## C. Korea

### Trade policy regime and IMF advice before the 1997 program

26. In the late 1990s, Korea’s trade regime was rated by the IMF as “moderately restrictive.” A series of import liberalization programs beginning in the early 1980s had eliminated virtually all nontariff barriers on manufactured imports and lowered tariff rates on manufactured imports to industrial-country levels. In 1997, Korea’s aggregate score on the TRI was 4, based on an “open” rating of 1 (the lowest) in the tariff category and a “moderate” rating of 2 (out of 3) in the nontariff barrier category. The unweighted average tariff rate was about 9 percent, tariff dispersion was relatively low (other than for some agricultural products), and the use of tariff exemptions was limited and transparent. However, so-called adjustment tariffs (supplementary duties) of up to 100 percent were imposed on various products (e.g., agricultural and fishery products, clothing, footwear, and toys) to protect domestic producers; the list of products was determined annually and ranged from 38 to 68 items. There were some nontariff barriers in the agricultural sector, such as state import monopolies for certain agricultural products, import quotas on rice, and restrictive import licensing for beef and cattle (WTO, 1996a).

\footnotesize


18 See Box 8 in Background Document 2.
Box 3. Korea: OECD Accession and Financial Services Liberalization

Korea’s 1996 accession to the OECD was contingent upon its acceptance of the following rules affecting trade in financial services: (i) the Code of Liberalization of Capital Movements, which requires OECD members to remove specific restrictions on capital flows including foreign direct investment in financial services and foreign portfolio investment; (ii) the Code of Liberalization of Current Invisibles Operations, which requires OECD members to remove specific restrictions on cross-border trade in financial services; and (iii) the OECD Declaration on International Investment and Multinational Enterprises, which provides for national treatment principles for foreign-owned enterprises.

Reservations to both codes and exceptions to the national treatment principles are permitted. According to Dobson and Jacquet (1998), Korea availed itself of the opportunity to exercise this option, accepting only 69 percent of the codes on financial liberalization (compared to the OECD average of 89 percent), although it committed to phase out many of its reservations and exceptions by 2000.

In September 1996, the Korean government announced that it would phase in the following reforms to liberalize the flow of foreign portfolio investment and foreign direct investment in financial services: foreign banks and securities firms from OECD countries would be permitted to establish subsidiaries in Korea by 1998; foreign investors from OECD countries would be allowed to establish and hold 100 percent ownership of any type of financial institution by December 1998; foreign investment consulting firms from OECD countries would be able to offer their services without establishing a commercial presence in Korea by 1999; and aggregate foreign investment ceilings for investors from OECD countries would be phased out by 2000 (Dobson and Jacquet, 1998).

27. Foreign access to Korean markets was more restricted for services than for manufactures. In the mid-1990s, the share of industries eligible for foreign direct investment was around 85 percent for services compared to 98 percent for manufacturing. The finance and business services, transport, and communications industries were among the least accessible to foreign participation (WTO, 1996a). In the early 1990s, Korea had undertaken reforms to liberalize financial services trade—easing restrictions on foreign bank entry; granting foreign securities firms (limited) access to the domestic market; deregulating overseas bond issuance and foreign borrowing by financial institutions and corporations (which remained subject to government approval); and liberalizing trade-related short-term financing. But the policy stance was characterized as a “lukewarm and partial opening” (Hwang, Shin, and Yoo, 2003). Cross-border trade was not allowed in the banking sector.19 A five-year reform program starting in 1993 that sought to enhance the efficiency of the financial sector reduced the degree and scope of government intervention in the sector.20 As part of the reform program, the scope of financial activities allowed for foreign banks was broadened to include local branch establishment, and regulations governing the operations of foreign securities firms were eased (Hirschhofer, 1995; Hwang, Shin, and Yoo, 2003). In 1996, Korea made further commitments to liberalize financial services trade as part of its accession to the Organization for Economic Cooperation and Development (OECD) (Box 3).

28. The IMF’s trade policy advice to Korea during 1995–96 focused mainly on further liberalizing imports. An SIP prepared for the 1995 Article IV consultations (Tzanninis, 1995) highlighted a number of issues that had created frictions in Korea’s bilateral trade relations: the import diversification program, restrictions on trade in financial services, and non-tariff barriers for agricultural imports and automobiles. In the 1996 Article IV consultation, IMF staff encouraged the authorities to speed up their plans to reduce the number of items covered by the import diversification program and to abolish the program as soon as possible (IMF, 1996e) (Box 4). But staff did not analyze the impact of the import diversification program or the expected effect of its elimination.

29. There was much discussion of the pace of capital account liberalization and domestic financial sector reform. The authorities favored a grad-

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19 Limited cross-border trade was allowed under the Foreign Exchange Management Act as part of permitted capital transactions (Hwang, Shin, and Yoo, 2003).
20 Interest rates were deregulated; government intervention in credit allocation by financial institutions (through policy loans, mandatory lending ratios, and credit controls) was scaled back; and measures were introduced to enhance the autonomy of bank management, ease restrictions on financial institutions’ business activities, and improve bank supervision. The program also entailed a

significant—although not complete—liberalization of capital controls (Hirschhofer, 1995).
that the program be repealed, as it violated Korea’s obligations under the General Agreement on Tariffs and Trade (GATT). However, Japan never brought a formal complaint to the GATT dispute settlement system, preferring instead to rely on political and diplomatic channels to resolve the issue (Ahn, 2004).

In 1994, the Korean government agreed to reduce the product coverage by half over the next five years. Subsequently, with its accession to the OECD in 1996, Korea agreed to eliminate the import diversification program by the end of 1999.

The 1997 SBA-supported program

30. In November 1997, Korea requested IMF assistance to overcome a financial crisis.22 Overinvestment and weakening export prices had driven an unprecedented number of highly leveraged conglomerates (chaebols) into bankruptcy, and this, together with a steep decline in stock prices, had severely weakened the financial system, leading to downgrades by international credit rating agencies and a sharp tightening in the availability of external finance. IMF staff noted that “[w]hile the contagion effects of developments in Southeast Asia were a contributing factor, the magnitude and speed of the deterioration owed much to the fundamental weaknesses in Korea’s financial and corporate sectors,” notably a lack of commercial orientation in financial institutions and lax prudential supervision (IMF, 1997j).

31. IMF staff diagnosed the cause of the crisis as a collapse in market confidence due to concerns about the soundness of the financial system, mounting short-term external debt, and dwindling reserves. Accordingly, the centerpiece of the three-year SBA-supported program was a comprehensive plan to restructure the financial sector, including opening it to foreign investment to promote competition and efficiency. The MEFP of December 3, 1997 included prior actions and commitments to accelerate foreign entry into the domestic financial sector through the establishment of foreign bank subsidiaries and brokerage houses, participation by foreign financial institutions in mergers and acquisitions of domestic financial institutions, and purchases by foreign banks of equity in domestic banks (IMF, 1997k). These measures were grouped under capital account liberalization measures.

32. Trade liberalization measures were also considered necessary. Immediately after Korea’s request for assistance, PDR began looking into trade reform measures that could be included in the program. An internal PDR memo suggested that it would be reasonable for the program to move Korea to a TRI rating of 1 over the two- to three-year program period (the same target as for Indonesia); it listed possible prior actions, first-year reforms, and medium-term

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21 Fund staff constructed different medium-term adjustment scenarios under alternative assumptions about the pace and scope of capital account opening. The sensitivity analysis suggested that a somewhat faster pace of capital account liberalization would imply somewhat larger current account deficits in the near term that could be comfortably financed but could reduce the ability of the economy to respond to unfavorable external developments, such as an unexpected deterioration in the terms of trade. A much faster pace of capital account liberalization would risk complicating short-run macroeconomic management and could place significant upward pressure on the exchange rate (Adams, 1996).

22 At that time, Korea’s last IMF arrangement was an SBA-supported program that ended in March 1987 (Table 1). A staff team visited Korea during October 1997 to conduct the 1997 Article IV consultation discussions, but the economic situation deteriorated significantly shortly afterwards and the consultation was continued into 1998.
Table 4. Korea: Key Trade Liberalization Measures under the 1997 SBA-Supported Program

<table>
<thead>
<tr>
<th>Tariffs</th>
<th>Nontariff Barriers</th>
<th>Trade-Related Subsidies</th>
<th>Trade in Services</th>
</tr>
</thead>
<tbody>
<tr>
<td>MEFP, December 3, 1997 (IMF, 1997k)</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
Set a timetable at the time of the first full review to eliminate the import diversification program in line with WTO commitments.

Set a timetable at the time of the first full review to eliminate restrictive import licensing in line with WTO commitments.

Set a timetable at the time of the first full review to eliminate trade-related subsidies in line with WTO commitments.

Announce plans to propose to the first session of the National Assembly immediately after the elections an amendment of the related laws to allow foreign financial institutions to participate in mergers and acquisitions of domestic financial institutions in a friendly manner and on equal principle. For merchant banks, foreign participation will be allowed up to 100 percent. [Prior action]

Effective immediately, allow foreign banks to purchase equity in domestic banks without restriction, provided that the acquisitions contribute to the efficiency and soundness of the banking sector. [Prior action]

Allow foreign financial institutions to establish bank subsidiaries and brokerage houses by mid-1998.

MEFP, December 24, 1997 (IMF, 1997m) | | |  
Phase out the import diversification program (covering 113 items) [committed to the WTO by end-1999]; liberalize 25 items by December 30, 1997; liberalize an additional 40 items by July 1998; liberalize an additional 32 items by December 1998; liberalize the remaining items by June 1999.

Reduce the number of items subject to adjustment tariffs from 62 to 38 by January 1, 1998.

Harmonize import certification procedures with WTO standards and strengthen their implementation.

Submit to the National Assembly a bill to abolish three trade-related subsidies, and abolish one subsidy administratively at the time of National Assembly approval, expected in March 1998 (committed to the WTO by end-1998).

Announce the binding of financial services liberalization agreed with the OECD as part of commitments to the WTO in January 1998.


Allow foreign banks and brokerage houses to establish subsidiaries by March 31, 1998.

MEFP, February 7, 1998 (IMF, 1998d) | | |  
Review existing import certification procedures and present a plan to streamline them and bring them in line with international practice by August 15, 1998.

Review all existing subsidy programs and their economic rationale. Present a proposal for rationalizing existing subsidy programs by November 15, 1998.

Issue a presidential decree following passage of the Banking Act (in December 1997) to provide transparent guidelines governing foreign investment in domestic financial institutions by February 28, 1998.

Allow foreign banks and brokerage houses to establish subsidiaries by March 31, 1998. [Structural performance criterion]
<table>
<thead>
<tr>
<th>Date</th>
<th>Description</th>
</tr>
</thead>
</table>
Submit legislation to abolish regulations that prohibit foreigners from becoming bank managers by June 30, 1998.  
Submit legislation to abolish restrictions on foreign ownership of land and real estate properties on the basis of national treatment by June 30, 1998.  
Increase the permitted equity ownership by foreigners of Korean telephone service providers from 33 percent to 49 percent by January 1, 1999. |
| MEFP, July 24, 1998 (IMF, 1998b) | Increase foreign ownership ceilings on publishing of newspapers (to up to 33 percent) and publishing of periodicals (to up to 50 percent) by January 1, 1999.  
Permit foreigners to engage in deep sea foreign freight transport by August 1, 1999. |
| MEFP, March 10, 1999 (IMF, 1999b) | Submit a revised financial services offer to the WTO consistent with OECD commitments by January 19, 1999. |

1 Indicates that the measure was implemented on schedule.
program targets for trade liberalization, including elimination of nontariff barriers, trade-related subsidies, and restrictions on foreign investment, as well as reduction of agricultural import tariffs. The December 3 MEFP included commitments to begin eliminating trade-related subsidies, restrictive import licensing, and the import diversification program, and to streamline and improve the transparency of the import certification procedures (IMF, 1997k). Table 4 lists the trade policy-related commitments in this MEFP.

33. The initial program failed to restore confidence and was quickly replaced by a strengthened one with more financing and more structural conditions, including on trade. Days after the initial program announcement, uncertain political support and damaging leaked information about Korea’s reserves and short-term debt had led to an increase in financial turmoil. In response, the Korean authorities worked with the IMF (and the World Bank) to strengthen their economic program.23 IMF staff formed an interdepartmental working group to come up with detailed, concrete, and time-bound trade reform measures that could help to reinforce the structural component of the program. The revised program—announced on December 24, 1997, in conjunction with an additional disbursement from the SRF—featured more specific measures to open the economy, including: reducing the number of items subject to adjustment tariffs; announcing that Korea would bind (as a WTO commitment) the financial services trade liberalization it had agreed with the OECD; abolishing four trade-related subsidies some nine months ahead of its WTO commitment; and phasing out the import diversification program six months ahead of its OECD/WTO commitment (Table 4).

34. Further trade liberalization measures—covering services in particular—were added in subsequent program reviews. The requirement to allow foreign banks and brokerage houses to establish subsidiaries by end-March 1998 was made a structural performance criterion at the first quarterly review in February 1998. The first quarterly review also included measures to open securities dealing, insurance, leasing, and other property-related business to foreigners. The second quarterly review (in May 1998) added measures to open telephone services and the third quarterly review (in July 1998) added measures to open deep sea freight transport and newspaper and periodical publishing to foreign ownership (Table 4).

35. The United States pushed for tough conditionality on trade. While IMF staff were negotiating the program with the Korean authorities, U.S. computer chip, steel, and automobile companies—some of which had initiated complaints against allegedly unfair trade practices by Korea—vigorously lobbied their government to attach trade conditions to the IMF program.24 The Korean media observed that a U.S. Treasury official stayed at the same hotel as the IMF mission team and attended their meetings. The Korean finance minister himself speculated that the United States and Japan must have requested certain conditions to open Korea’s goods and financial markets.25 The U.S. administration continued to pressure the IMF on trade conditionality even after the revised program was approved. In January 1998, the U.S. Trade Representative (USTR)’s Office sent, via the U.S. Executive Director, a detailed list of trade policy measures proposed for the program, including measures to liberalize trade in goods (e.g., lowering tariff and nontariff barriers in specific goods, especially automotive imports and agricultural imports) and services (financial services and telecommunications services in particular), and measures to limit government interference in commercial lending decisions affecting the semiconductor, automobile, steel, shipbuilding, and agricultural sectors.26 According to IMF staff, several such communications were received during the course of the program. At a congressional hearing in March 1998, the USTR testified that her office and other government agencies were actively monitoring Korea’s (and Indonesia’s) compliance with the Fund’s trade-related commitments.27 The U.S. Omnibus Appropriations Act signed in October 1998 tied additional U.S. funding for the IMF to several conditions including the requirement that IMF borrowing countries be made to liberalize trade.

36. The IMF justified its inclusion of trade conditionality in the Korean (and Indonesian) programs as necessary and appropriate. At a press conference in December 1997, the First Deputy Managing Director

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23 Korea graduated from World Bank borrowing in 1994, but as part of the international assistance package in response to the financial crisis, the Bank provided structural adjustment loans in 1997 and 1998 to support reforms in financial sector restructuring, corporate sector restructuring, and labor market reform.


26 In October 2002, the European Union filed a WTO dispute against Korea, alleging that “corporate restructuring subsidies” (in the form of debt forgiveness, debt and interest relief, and debt-equity swaps) provided through government-owned and -controlled banks to certain Korean shipbuilding companies were inconsistent with Korea’s obligations under the Safeguards and Countervailing Measures Agreement. See Box 6 in Background Document 2.

27 Statement of Ambassador Charlene Barshevsky, USTR, Testimony before the Subcommittee on Trade of the House Committee on Ways and Means, Hearing on Asia Trade Issues, February 24, 1998.
In response to Feldstein’s (1998) criticism that the Asian crisis programs (especially Korea’s) included excessive structural conditionality, the FDMD said it was not clear why Feldstein considered trade liberalization an unnecessary interference with the proper jurisdiction of a sovereign government whilst banking sector reform was not, or why extensive structural conditionality was “acceptable” in Fund-supported programs in the transition economies but not in Asia (Fischer, 1998).

Assessment

37. The relatively extensive trade conditionality in Korea’s SBA-supported program was out of proportion to the initial restrictiveness of Korea’s trade policy regime. At a general level, the program was modeled after the Indonesian SBA, where a commitment to structural reforms was considered necessary to restore market confidence. But while it is reasonable to argue that weaknesses in the financial and corporate sectors contributed to the Korean crisis, there is no indication that trade restrictions had any effect on market confidence. Prior to the crisis, trade restrictions barely featured in the IMF’s dialogue with Korea; the only trade restriction that IMF surveillance missions had highlighted regularly was the import diversification program. Fund staff had to scramble to learn more about Korea’s trade policies—adjustment tariffs, trade-related subsidies, and import certification procedures—as the program was being negotiated. They had scant information, for example, about the nature of the four trade-related subsidies that were to be removed, let alone any indication of how economically meaningful those subsidies were.28 Unlike in Indonesia, the World Bank did not help on the trade front. However, the collaboration with the Korean authorities was much smoother than in Indonesia and the measures were more straightforward—many simply involved accelerating the timetable of commitments that had already been made to the OECD and/or the WTO.

38. No meaningful or concrete effort was made to justify the trade liberalization measures as macro-critical. It is hard to see why a bilateral trade issue like the import diversification program (that was already scheduled to be dismantled) would be relevant for resolving the financial crisis. One could also question the need to liberalize financial services trade during a financial crisis that had been caused in part by lax prudential supervision—surely the preferred sequencing would have been to strengthen prudential supervision first and then liberalize, rather than do both simultaneously. In general, while the trade liberalization measures were likely to have been desirable for Korea’s medium-term growth, the reasons for including such measures in a program explicitly addressing an immediate crisis were not made clear. The same conclusion was reached in IEO (2003).

39. The underlying reason for the trade liberalization measures was mainly political. IMF staff interviewed for this evaluation were candid in their admission that the trade conditions were inserted to please certain shareholders, particularly the U.S. and Japanese governments, so that they would in turn persuade their commercial banks to roll over Korea’s external debt.29 The U.S. Treasury was clearly not shy with its suggestions for trade conditionality, but for any given trade condition included in the program it is impossible to determine whether the impetus came from within or outside the Fund.30

40. This may have damaged the IMF’s credibility. With no convincing economic reason for the inclusion of trade conditionality in the program, and given the U.S. government’s overt efforts to put pressure on the Fund, Koreans (and others) concluded that the trade measures were included at the request of the Fund’s major shareholders in return for their financial support.31 The IMF did not manage to convince the public of its independent judgment, “tarnishing

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28 A Fund memo identified the subsidies as: (i) the microcomputer assistance program; (ii) the export losses program; (iii) the development market program; and (iv) the investment market program. The first program was characterized as a subsidized loan; the other three were “related to tax exemptions in one form or other.”

29 See IEO (2003) on the developments leading up to the decision to urge a coordinated rollover on creditor banks, and the outcome of the rollover.

30 IEO (2003) noted the active engagement of the United States in the Korean program but allowed that this was understandable to a certain extent, given the importance of U.S. bilateral support in resolving the crisis. The evaluation found no evidence that the specific policy measures mentioned were included “solely because large IMF shareholder governments demanded them.”

31 See for example “Koreans fume at alleged U.S. and Japanese intervention in IMF deal,” Associated Press, December 4, 1997 and “IMF bailouts subject Korea Inc. to U.S.,” Korea Herald, March 3, 1998. Kapur (1998) stated that: “According to fund sources, conditions such as the one asking Korea to speed up the opening of its automobile and financial sectors reflected pressures from major shareholders (Japan and the United States).” Stiglitz (2001) characterized the trade conditionality in Korea’s SBA as “a crude political power play,” and noted that the Fund’s effectiveness was “weak-
the technocratic reputation that is essential to the credibility of its prescriptions” (Kapur, 1998). The events may have also inadvertently hurt the image of others—there is no evidence, for example, that the Japanese government sought to use its influence on the Fund the way the U.S. government did, but it was widely assumed to have tried.

41. The trade conditionality also came close to crossing into WTO territory. Korea had already committed at the WTO to undertake a number of the trade measures that featured in the IMF-supported program, such as phasing out trade-related subsidies and the import diversification program. By agreeing to remove those trade restrictions earlier than scheduled, Korea sacrificed some adjustment time, although IMF staff broke no rules in making those requests and the sacrifice was small (six to nine months). But the IMF contravened its own guidelines on “cross-conditionality” when it required that Korea (like Indonesia before it) bind its financial services liberalization at the WTO (Table 2).

42. Overall, the trade conditionality was effective in opening the Korean economy a little earlier than planned, though by the IMF’s own measure it was not a success. The import diversification program was eliminated, four trade-related subsidies were abolished, and the number of items subject to adjustment tariffs was reduced (Table 4). Instead of declining, Korea’s overall TRI remained at 4, then actually rose to 5 (reflecting an increase in the unweighted average tariff) in 2000. Korea continues to levy adjustment tariffs of 11–57 percent on various products to protect domestic industries from import surges; the authorities claim that these adjustment tariffs are within Korea’s WTO bindings (WTO, 2008).

43. The financial services liberalization measures (not measured by the TRI) were generally hailed, but they were not without controversy. The reforms—including allowing foreign banks and securities firms to establish domestic subsidiaries, allowing up to 100 percent foreign ownership of Korean financial institutions, and allowing foreign nationals to become directors of Korean banks—were characterized by the WTO (2000) as a “remarkable opening of the [financial] services sector.” Fund staff reckoned that foreign capital was instrumental in the restructuring and stabilization of the Korean banking system: foreign private-equity funds acquired three failing banks, restructured them, and sold their stakes to Citigroup and Standard Chartered (Semblat, 2006). By 2005, foreign banks’ share of assets in the Korean banking system stood at 21 percent, compared with 4 percent in 1997. The Koreans were less enthusiastic. The foreign private-equity funds were criticized for making hefty profits from their sales of stakes in Korean banks. According to a 2005 Bank of Korea study, the foreign firms were focused on short-term capital gains and not the long-term development of Korea’s financial sector (Kang and Kim, 2005).

44. In the late 1990s, Ukraine’s trade regime was rated by the IMF as “moderately restrictive.” After some initial progress in establishing a liberal import and export regime during 1994–95, Ukraine’s trade policy drifted toward protectionism in 1996–98 (Box 5). In 1998, Ukraine’s aggregate TRI was 5, based on a “relatively open” tariff rating of 2—the unweighted average tariff was 12.7 percent—and a “moderate” nontariff barrier rating of 2. There were import quotas on agricultural goods and an import ban on used cars (Box 5). Exports of livestock and hides were subject to export taxes of 30–75 percent (IMF, 1997e) and exports of sunflower seeds were subject to export deposits and indicative export prices.

45. Trade in services was hampered by uneven privatization and deregulation efforts and a generally difficult environment for private sector activity and

D. Ukraine

Trade policy regime and IMF advice before the 1998 program

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45. Trade in services was hampered by uneven privatization and deregulation efforts and a generally difficult environment for private sector activity and

32 The report noted that foreign financial institutions helped raise the overall standard of Korea’s financial services sector by introducing advanced banking practices and new products. Hence, it argued that selling the banks to foreign financial institutions rather than foreign private equity funds would have been more beneficial to the development of the country’s banking sector.


34 “Korean court clears KEB, frees up Lone Star for stake sale,” Euro Week, November 27, 2008.


foreign direct investment. Thousands of large- and medium-scale enterprises in sectors including energy, transportation, and communications were placed on a “negative privatization list.” The banking sector, in contrast, was mostly privatized by 1998, although it was still at a relatively early stage of development and an effective regulatory system was only gradually being created. Since independence, many private banks had been established in an environment characterized by low entry costs (no minimum statutory capital requirements initially) and limited banking supervision. Despite the large number of banks, Ukraine’s banking system was small by international standards and confidence in the banking system was low. This partly reflected the legacy of the centrally planned system but also the period of hyperinflation that Ukraine had experienced shortly after independence (IMF, 1999c). There was some resistance to foreign banks: total foreign capital participation in the equity ownership of the Ukrainian banking system was capped at 15 percent, foreign bank branches were banned (though wholly-owned subsidiaries were allowed), and minimum capital requirements were higher for foreign banks than for domestic banks. By most accounts these restrictions were not really binding, however; according to IMF (1999c) by mid-1998 there were some 28 banks with foreign capital participation (including eight with 100 percent foreign ownership, up from two in mid-1996); those banks mostly focused on corporate financing and were not engaged in retail banking.

46. Ukraine applied to join the WTO in November 1993 but had made little headway in its accession negotiations. The limited progress was due to the slow pace of market and trade reform: Ukraine ranked near the bottom of the transition league tables updated annually by the European Bank for Reconstruction and Development and its trade policies came under strong criticism from the European Union, the United States, Japan, and Canada.37 In 1994, Ukraine signed a partnership and cooperation agreement with the European Union. The agreement, which entered into force in March 1998, was designed to bring Ukraine into line with the legal framework of the single European market and the WTO system and also provided for the establishment of a free trade area further down the road. One of the first actions the European Union took under the agreement was to initiate formal dispute consultations with Ukraine over the tax breaks and other privileges granted to the country’s automobile industry.

47. The IMF used program conditionality to liberalize Ukraine’s (goods) trade regime. Ukraine had three SBAs during 1995–98: April 1995–April 1996; May 1996–February 1997; and August 1997–August 1998. All three programs featured trade liberalization commitments, including in the form of prior actions and structural benchmarks (Box 6). One of the main

objectives of the 1995 SBA was to strengthen export performance; in concluding the 1995 Article IV consultation, Executive Directors “urged the authorities to remove all remaining export restrictions, especially to abolish the system of indicative export prices, to eliminate uncertainties about prevailing legislation, and to fully liberalize grain marketing” (IMF, 1996a). The export liberalization conditions were largely met, though not without delays. During the 1997 Article IV consultation, the staff team commended the authorities for maintaining “generally liberal trade policies” and resisting protectionist pressures (IMF, 1997f) but several Directors “underscored the need for a stronger commitment by the authorities to trade liberalization” (IMF, 1997g). At the same time, in the 1997 SBA the scope of trade

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**Box 6. Ukraine: Key Trade Conditionality in the 1995, 1996, and 1997 SBA-Supported Programs**

**1995 SBA-Supported Program**

*MEFP, March 3, 1995 (IMF, 1995a)*

- Eliminate all remaining export quotas and licenses other than on grain and goods subject to voluntary export restraints (VERs) under international agreements. (Prior action)
- Abolish quotas and licenses on grain exports by end-June 1995. (Structural benchmark)
- Remove the government’s authority to delay or prohibit exports (other than for health and security reasons and to implement international agreements) under the scheme for registering export contracts. (Prior action)
- Eliminate the system of state orders and state contracts (including for foreign trade purposes), other than to meet the government’s own needs, narrowly defined. (Prior action)
- Refrain from adopting any new legislation that directly or indirectly poses obstacles to exports. Continue to avoid resort to quantitative restrictions.
- Complete the privatization of at least 1,000 medium and large enterprises, including agricultural distribution, storage, and transportation companies, by end-June, 1995. Identify a list of at least 100 enterprises in which substantial blocks of shares are to be available, at auction, for foreign participation. (Structural benchmark)

**1996 SBA-Supported Program**

*MEFP, April 22, 1996 (IMF, 1996b)*

- Complete the privatization of at least 70 percent of shares of at least 2,000 medium and large enterprises, including in agricultural distribution, storage, and transportation, by end-July 1996. (Structural benchmark)
- Refrain from adopting any new legislation that directly or indirectly poses obstacles to exports.

**1997 SBA-Supported Program**

*MEFP, August 6, 1997 (IMF, 1997f)*

- Abolish all export duties except on live animals and cow hides. (Prior action)
- Abolish the system of indicative prices for exports, with the exception of live animals, cow hides, and goods subject to VERs and actual antidumping actions. (Prior action)
- Liberalize the Special Export Regime so that registration of exports is an automatic process and for statistical purposes only. (Prior action)
- Abolish the export surrender requirement. (Prior action)
- Reduce the maximum import tariff rate to 30 percent, with possible exceptions covering less than 1 percent of total imports. (Prior action)
- Reduce the number of distinct tariff rates to 6 by end-December 1997.
- Reduce the number of commodity positions (at the 4-digit level) subject to combined ad valorem and specific import tariffs to no more than 80. (Prior action) Phase out the remaining mixed tariffs, reducing them by one-third by end-March 1998 and by another one-third by end-June 1998. (Structural benchmark)
- Harmonize the remaining excise taxes on domestic and foreign production by end-March, 1998. (Structural benchmark)
- Continue to ensure that certification rules and procedures for imports are WTO compliant and nondiscriminatory.
- Allow foreigners to buy seats at the commodity exchanges. (Prior action)
- Simplify the licensing procedures for foreign commercial banks and expedite applications in process to allow them greater access to the Ukrainian market.
- Submit to parliament a new customs code consistent with international standards. (Prior action)
- Screen customs procedures and documentation, improve control over goods in transit, and improve the coordination of customs collection with the State Tax Administration.
conditionality was broadened to include import tariff reduction, liberalization of trade in financial services, and improvements in customs administration.

48. IMF missions did not directly address the liberalization of trade in services. However, they consistently stressed broader behind-the-border issues such as privatization, de-monopolization, reducing government intervention in the economy, and improving the business climate. In the negotiations for the 1997 SBA program, IMF staff underscored the need to improve the overall health of the banking system. The authorities responded that they intended to take several steps to improve banking supervision and regulation, to deal with problem banks, and to increase the efficiency of the banking system, including simplifying the licensing procedures for foreign commercial banks and expediting the applications in process to allow them greater access to the Ukrainian market (IMF, 1997f).

The 1998 EFF-supported program

49. The 1997 SBA-supported program went off-track after the first review as government finances spun out of control. To finance the growing budget deficit, the government had borrowed heavily through the Treasury bill market, which attracted domestic and nonresident participants, and had even been able to issue foreign currency bonds in international capital markets. But in the wake of the financial crises in Asia, which subsequently spread to Latin America and Russia, Ukraine’s external financing prospects dried up. The government had to resort to the central bank to finance its budget deficit and debt service payments, which in turn put pressure on the exchange rate.38

50. The IMF Board approved a three-year EFF arrangement in August 1998, just as the financial crisis broke out. IMF staff and the Ukrainian authorities had earlier discussed an EFF-supported program to succeed the 1996 SBA-supported program, but a lack of parliamentary support for key adjustment measures in the proposed EFF-supported program—including a reluctance to commit not to intensify import restrictions—resulted in agreement on a one-year SBA-supported program instead, in 1997. IMF staff still believed that a medium-term program was needed to correct Ukraine’s institutional shortcomings and put it on a sustainable growth path, and the discussions for an EFF-supported program were revived when a new parliament was formed after the 1998 elections (Stone, 2002). When the financial situation deteriorated in the wake of adverse developments in Russia (only days before the IMF Board meeting to discuss the program request), the EFF arrangement was adjusted to reflect short-term stabilization needs as well as medium-term structural reforms (IMF, 2005c). Staff (and the Board) were concerned about the risks to the program from the financial crisis but decided to push ahead with the EFF-supported program rather than lose the opportunity to seal the “long-awaited adjustment package” (IMF, 1998p).

51. The EFF-supported program envisaged fundamental structural reforms, but trade liberalization was not heavily emphasized. The structural reforms were mainly aimed at reducing the government’s role in the economy and promoting private sector development, improving governance, and reforming the agricultural and energy sectors. Trade liberalization was included among the structural reforms but was not their main focus.39 The authorities reduced tariffs and tariff exemptions as prior actions for the program. The staff considered Ukraine’s trade regime to be already “relatively liberal and open” based on its TRI rating of 5 out of 10, and did not anticipate a reduction in the rating as a result of the trade liberalization measures outlined in the program (IMF, 1998o). This view was not challenged by PDR or by the Board (although the USTR did express her dissatisfaction to the Fund and the WTO over the relatively low level of trade conditionality in the Ukraine program compared to the earlier Asian programs). Table 5 summarizes the main trade-related conditions in the EFF-supported program. Included among the structural measures was a commitment to reduce barriers to the entry of foreign banks by simplifying licensing procedures and by lifting the limit of 15 percent on total foreign capital participation in the equity ownership of the Ukrainian banking system.

52. Serious budgetary slippages delayed the completion of the first program review; in response, the authorities resorted to an import surcharge to help keep the fiscal program on track. The IMF mission considered the imposition of the (uniform 2 percent) import surcharge in May 1999 “regrettable” but “unavoidable” given the difficult fiscal situation and the difficulties in implementing corrective structural revenue reforms.40 Staff urged the authorities

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38 Ukraine’s hryvnia, which was introduced in 1996, was pegged to the U.S. dollar within a narrow band.

39 The World Bank was also actively involved in Ukraine, mainly in sectoral projects such as public sector reform, agricultural sector reform, energy sector reform, financial sector reform, and privatization (IMF, 1998p). There is little evidence of Bank-Fund collaboration on trade policy issues.

40 During the first program review in January/February 1999, the mission learnt that despite the commitment to reduce tax exemptions, the zero-rating of VAT on electricity, imported gas, and coal had been extended for 1999 and a tax moratorium on agriculture had been imposed. The authorities explained that they had little choice due to strained relations between the government and parliament.
**Table 5. Ukraine: Key Trade Liberalization Measures under the 1998 EFF-Supported Program**

<table>
<thead>
<tr>
<th>Tariffs</th>
<th>Nontariff Barriers</th>
<th>Export Taxes/Restrictions</th>
<th>Customs Administration</th>
<th>Trade-Related Subsidies</th>
<th>Trade in Services</th>
</tr>
</thead>
<tbody>
<tr>
<td>MFEP, August 11, 1998 (IMF, 1998o)</td>
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<tr>
<td>Reduce the average import tariff (using 1996 weights, excluding energy products) to no more than 7.5 percent (January 1998 level).</td>
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<tr>
<td>[Prior action]</td>
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<td>Adopt a resolution limiting the frequency of import tariff adjustments to no more than twice a year for the rest of 1998 and 1999, and to no more than once a year thereafter.</td>
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<tr>
<td>[Prior action]</td>
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<td>Reduce the number of commodity positions (at the 4-digit level) subject to mixed specific/ad valorem import tariffs to no more than 25 by December 31, 1998.</td>
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<tr>
<td>[Structural performance criterion]</td>
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<tr>
<td>Limit exceptions to the maximum tariff of 30 percent to items covering no more than 0.8 percent of total imports by July 1, 1998.</td>
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<td>Reduce the maximum tariff to 25 percent (with a few exceptions covering less than 0.8 percent of total imports) and reduce the (unweighted) average import tariff to no more than 13.3 percent by December 31, 1999.</td>
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<tr>
<td>Reduce the maximum tariff to 20 percent (with a few exceptions covering less than 0.5 percent of total imports) and reduce the average import tariff to no more than 10 percent by December 31, 2000.</td>
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</tbody>
</table>

Ensure that any import protection measure which could become necessary to prevent injury to domestic producers is price-based, precisely defined, temporary, and nondiscriminatory and introduced only after appropriate procedures consistent with WTO rules are followed.

Further harmonize Ukrainian legislative and normative acts with international and European ones, and conclude and implement agreements on mutual recognition of conformity assessments (certification) in order to remove obstacles to trade in line with WTO principles.

Continue ensuring the non-discriminatory character of certification procedures.

Reduce barriers to the entry of foreign banks, including by increasing flexibility of the limit of 15 percent on total foreign capital participation in the equity ownership of the Ukrainian banking system by June 30, 1998.

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1. [Prior action]

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Eliminate remaining export duties on animal skins and hides by November 15, 1998.

Eliminate the advance export deposit requirement on sunflower seeds by December 31, 1998.

Refrain from introducing any new restrictions on exports throughout the program period.

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Introduce payment of market interest on advance deposits on exports of sunflower seeds.

[Prior action]

Eliminate remaining export duties on animal skins and hides by November 15, 1998.

Eliminate the advance export deposit requirement on sunflower seeds by December 31, 1998.

Refrain from introducing any new restrictions on exports throughout the program period.

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Impose reporting requirements on importers of gas on volume and value of gas imports and payments by July 1, 1998.

Adopt a new customs code that is consistent with international standards by December 1998.

Improve customs administration, including the following measures: (i) consult with the World Customs Organization or other appropriate agency to develop a valuation database on import prices by December 1998; (ii) create specialized units for post clearance review of tariff classification and valuation by June 1999; (iii) implement the valuation database covering 60 percent of imports and phase out the use of indicative values by June 2000.

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Eliminate import tariff exemptions with the exception of those on imports directly related to Chernobyl programs, humanitarian assistance, bilateral and multilateral technical assistance programs, and no more than five special foreign investment projects. [Prior action]

Refrain from granting any new import tariff exemptions throughout the program period.
### Table 5 (continued)

<table>
<thead>
<tr>
<th>Event Date</th>
<th>Action Description</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>MEFP, August 26, 1999 (IMF, 1999g)</strong></td>
<td>Remove the export duty on hides and skins by end-December 1999. Veto the law introducing export duties on sunflower seeds. [Prior action]</td>
</tr>
<tr>
<td><strong>MEFP, December 5, 2000 (IMF, 2000e)</strong></td>
<td>Reduce the export tax on sunflower seeds to 10 percent by December 31, 2000. [Structural benchmark] Complete a review of the free economic zones (FEZs) and special investment regimes (SIRS) by April 30, 2001. [Structural benchmark] Establish a timetable for the phasing out of exemptions in the FEZs and SIRS on the basis of the review by June 2001.</td>
</tr>
<tr>
<td>Tariffs</td>
<td>Nontariff Barriers</td>
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<td>------------------------------------------------</td>
<td>-------------------------------------------------</td>
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<tr>
<td>MEF, August 31, 2001 (IMF, 2001a)</td>
<td>Enact Law on the Customs Tariff; introduce the new harmonized tariff system. [Prior action]</td>
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<td>Approve laws on copyright and allied rights, on inventions, and on the enforcement of responsibility for violation of intellectual property. [Prior action]</td>
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<tr>
<td></td>
<td>Simplify documentation requirements for domestic and external trade in grains and reduce registration fees at the exchanges; abolish the requirement to register domestic grain transactions; and suspend the mandatory declaration of grain stocks. [Prior action]</td>
</tr>
</tbody>
</table>

1 Indicates that the measure was implemented on schedule.
2 Indicates that the measure was not implemented.
to remove the surcharge by end-1999 and replace it with other revenue measures such as eliminating tax exemptions and zero-rating the value-added tax (VAT) on electricity, imported gas and coal. The IMF agreed to augment the EFF arrangement in view of the deterioration in Ukraine’s external environment.  

53. At the same time, the government began to consider imposing an export duty on sunflower seeds to boost budget revenues and assist domestic vegetable oil producers. There was vigorous domestic lobbying both for the tax (by oilseed crushers) and against it (by oilseed growers and traders). IMF staff strongly opposed the measure, arguing that it would harm Ukraine’s export performance and would violate the commitment not to introduce new restrictions on exports during the program period.41 In July 1999, the parliament went ahead and approved a 30 percent export tax on sunflower seeds but the move was vetoed by the President; the tax was subsequently lowered to 23 percent and signed into law in September 1999. Fund staff criticized the export tax as being “among the worst possible means of raising budgetary revenues.”42  

54. The program went off-track shortly afterwards and was suspended for more than a year. Besides the sunflower seed export tax, many more serious problems—including nonobservance of quantitative and structural performance criteria, insufficient progress on structural reforms, and an incident involving misreporting of the central bank’s international reserves—contributed to the derailment of the program (IMF, 2005c). IMF staff had several discussions with the Ukrainian authorities to try to bring the program back on track, but eliminating the export tax was one of the conditions to which the authorities would not agree. By September 2000, the mission team was ready to drop the demand, but Fund management and other departments argued that that could weaken the program conditionality by too much. When the Fund re-engaged and completed the fourth review in December 2000, the compromise was to reduce the export tax on sunflower seeds to 10 percent by the end of the year as a structural benchmark (Table 5). But the program went off-track again, and only one more (delayed) review was completed after that (IMF, 2001a).  

55. After the EFF arrangement expired in 2002, Ukraine had one more IMF-supported program during the evaluation period but no more trade conditionality. After 2001, the focus of Ukraine’s trade (and broader structural) reforms shifted to WTO accession and the Fund provided encouragement for this goal in every Article IV consultation. In early 2004, Ukraine requested, and the Fund approved, a twelve-month precautionary program under the SBA aimed at promoting economic growth and helping to lay the foundations for membership in the WTO and eventually the European Union. The specific reforms needed for WTO accession were left to the World Bank to monitor under its Programmatic Adjustment Loan program (IMF, 2004a).  

56. One of the conditions for WTO membership was to allow foreign banks to open branches in Ukraine. The central bank, government, and parliament wrestled over this issue from 2002 to 2006; the central bank (backed by the President) submitted proposals to change the legislation several times during this period but parliament rejected the proposals each time. IMF staff largely stayed out of this issue. A Financial Sector Assessment Program (FSAP) mission in 2003 simply noted that foreign bank involvement in Ukraine had been modest, particularly compared with that in other transition countries (IMF, 2003a). During this time, IMF staff increasingly drew attention to the rapid credit growth that was taking place in Ukraine and the risks that it posed for banking sector stability. The staff implicitly endorsed the idea of greater foreign bank entry, reasoning that this would increase competition and efficiency and improve risk management practices (IMF, 2005b, 2006c). An SIP for the 2004 Article IV consultation (Schaechter, 2004) argued that the relatively low degree of foreign ownership in Ukraine’s banking sector raised concerns that the credit boom could be unsustainable. As foreign interest in Ukraine’s banking sector grew, a follow-up SIP to the 2003 FSAP (Ong, Schaechter, and Sologub, 2005) made some recommendations for improving banking regulation and supervision, including raising the minimum capital adequacy ratio in the short term and preparing a contingency plan for crisis management in the medium term. It was not until 2008, when foreign participation in the banking system became “significant,” that staff sounded the alarm about the need to develop better cross-border supervisory arrangements: the 2008 update for the FSAP called for “[u]rgent action … to strengthen consolidated supervision and supervisory cooperation,” including closer and more effective cooperation with home country supervisors, and noted that the growing importance of foreign-owned banks increased the risk of spillovers from foreign bank failures on to Ukrainian subsidiaries, and had to be considered in Ukraine’s contingency planning (IMF, 2008a).

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42 “IMF slams Ukraine’s planned sunseed export duty,” Reuters, September 21, 1999.
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57. Given that the primary focus of Ukraine’s EFF-supported program was on growth-enhancing structural reforms, the inclusion of trade conditionality was entirely appropriate. Critics have characterized the program as “an extreme example of the proliferation of conditions” (Stone, 2008) and the Fund itself acknowledged that the program became known for “excessive structural activism” (IMF, 2005c). But the EFF-supported program was designed first and foremost as a medium-term adjustment program to address structural obstacles to growth rather than as a short-term program to overcome a financial crisis, so the emphasis on structural conditionality was justifiable. Certainly, trade reforms were macro-relevant for the Ukrainian economy in 1998, given its poor transition record and disappointing growth performance and in light of its aspirations to join the WTO.

58. Yet the IMF focused much less on trade liberalization in Ukraine than it did in some of the Asian crisis programs. IMF staff considered Ukraine’s TRI of 5 to be acceptable and not in urgent need of reduction, when barely a year earlier Indonesia and Korea, with similar ratings, were seen to require significant trade reforms. The IMF was not swayed by the USTR’s call for more trade conditionality. The Avtozaz-Daewoo deal had echoes of Indonesia’s national car project, yet the IMF was silent on this issue.43 Interviews with the staff revealed that trade liberalization was low on their list of priorities in Ukraine, being crowded out by more pressing structural issues such as privatization, agricultural reform, and tax reforms.

59. The IMF was prepared to be flexible on trade policy issues. The IMF endorsed the introduction of a temporary import surcharge during the program, even though PDR had argued forcefully against such measures in a guidance note issued to staff earlier in the year (Table 2). But trade policy was not the only area in which the Fund was prepared to cut corners in Ukraine. Ukraine was a “difficult counterpart” highly resistant to trade and other structural reforms yet partly because of “major shareholder pressure” the Fund repeatedly bent over backwards to stay involved in the hopes of “tipping the balance toward reformers.” (IMF, 2005c.) Interviews with the staff reinforced Stone’s (2002) observation that the Fund “repeatedly bent the rules in Ukraine’s favor” because “the G-7 [had] made it clear that it expected the IMF to reach some pragmatic accommodation with the recalcitrant Ukrainian authorities.”

60. The most significant and controversial trade condition—the removal of the export tax on sunflower seeds—was not sufficiently analyzed. IMF staff relied on the standard textbook arguments without examining the structure of the sunflower seed market or quantifying their analysis. They noted that Ukraine was one of the world’s largest producers and exporters of sunflower seeds and that the tax would impose a “significant” deadweight cost, but they did not estimate the optimum tax or the deadweight cost, and hence could not make a compelling case that reducing the tax was critical for achieving key program objectives (IMF, 2005c). They argued that “the tax was emblematic of the ability of powerful groups (in this case, domestic oilseed crushing plants) to bend the rules of the game to their advantage at the expense of weaker groups (in this case, growers of sunflower seeds)” (IMF, 2005c). But in fact there were large (foreign) and small (domestic) interests on both sides of the issue: the Ukrainian Grain Association, which opposed the tax, included among its members large American and European oilseed trading companies that provided financial support to the oilseed growers.44 And staff were largely ignorant of the actual implementation of the tax, notably, the extent to which it was avoided or evaded. In interviews for this evaluation, staff confirmed that no analysis was done on the sunflower seed export tax issue because none was considered necessary, either (according to some staff) because the issue was relatively insignificant and had simply been blown out of proportion, or (according to others) because the standard textbook arguments were considered to be unassailable.

61. The IMF was effective in generating an active debate in Ukraine on the pros and cons of the export tax, even if it was unsuccessful in eliminating the tax on its terms. A Factiva search turned up numerous media reports on the issue between 1998 to 2001, including both assenting and dissenting views within and outside the government. In the event, the structural benchmark to cut the export tax to 10 percent by end-2000 was not met; in June 2001, the tax was reduced to 17 percent instead of 10 percent and “the sunflower seed issue was quietly dropped from the [Fund’s] agenda” (IMF, 2005c). In July 2005, as a precondition for WTO accession, parliament adopted legislation to lower the export tax by one percentage point per year upon WTO membership until it reached 10 percent (IMF, 2005c). In December 2008, a gov-

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43 Fund staff did argue strongly against the tax incentives in free economic zones but did not manage to convince the Ukrainian authorities.

44 Cargill subsequently opened a huge sunflower seed processing plant in Donetsk oblast in April 2000 (“Cargill set to shake up Ukraine sunseed market,” Reuters, April 6, 2000).
ernment proposal to abolish the (14 percent) export tax was once again rejected by the parliament.\footnote{Ukraine lawmakers reject scrapping sunflower seeds export tax,” Dow Jones Newswires, December 24, 2008.}

62. The IMF may have been successful in reducing import tariffs (eventually) although it is not certain that the tariff cuts will stick. Ukraine’s TRI rating fell from 5 to 4 in 2002 when its unweighted average tariff dropped from 12.7 percent to 7 percent. But in December 2008, the parliament voted to impose an additional temporary duty on all imports to address balance of payments difficulties.\footnote{“Ukrainian president worried IMF might cancel loans due to increase of import duties,” Kyiv Post, December 24, 2008. The import duty was subsequently restricted to two goods (cars and refrigerators) but thus far has not been implemented.}

63. Ukraine further opened its banking sector though the IMF did not push very hard on this issue. The 15 percent limit on the capital that could be owned by foreign banks was eliminated in 1999 (IMF, 1999c). The central bank announced a uniform minimum statutory capital requirement of €5 million for newly formed banks, in line with international standards, in 2005 (Ong, Schaechter, and Sologub, 2005). In November 2006, parliament finally passed the bill allowing foreign banks to establish branches in Ukraine. In May 2008, Ukraine acceded to the WTO. Six months later, after the economy and the banking system were hit hard by a sharp decline in steel prices and a reversal of capital flows, Ukraine requested, and the Board approved, a two-year SBA-supported program. IMF staff estimated a banking capitalization need of at least 8 percent of GDP; most of the large institutions, including foreign banks, were expected to be able to raise capital on their own but could apply for public recapitalization funds if needed. The authorities began to strengthen the monitoring of banks, including via enhanced cross-border supervisory cooperation (IMF, 2008c).

### E. Brazil

#### Trade policy regime and IMF advice before the 1998 program

64. In the late 1990s, Brazil’s trade regime was rated by the IMF as “moderately restrictive.” Despite a significant trade liberalization program in the early 1990s and the adoption of the common external tariff regime of the Common Market of the South (MERCOSUR) in 1995, import tariffs remained high and the dispersion of rates gave rise

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**Box 7. Brazil: Trade Liberalization During 1990–98**

Brazil undertook a significant program of trade reforms during 1990–93: it abolished all quantitative import controls and most export controls; eliminated the list of prohibited imports; allowed automatic access to import licenses; suspended external financing requirements for imports; removed most direct export subsidies, fiscal incentives for exporters, and import tariff exemptions; eliminated export taxes and the system of minimum export prices; and implemented a multi-year tariff reduction program (IMF, 1994a). In 1991, Brazil ratified the treaty of MERCOSUR to create a common market with Argentina, Paraguay, and Uruguay from January 1, 1995. The agreement stipulated a common external tariff structure ranging from 0 to 20 percent on about 85 percent of all traded goods from January 1, 1995; most of the remaining 15 percent of goods (classified as national exceptions, capital goods, or computer goods) were to be brought in line with the common external tariff rates by 2001, and all of them by 2006. Tariffs on intra-MERCOSUR trade were generally prohibited, but each member was allowed to maintain tariffs for approved items (until January 1, 1999 for Argentina and Brazil and January 1, 2000 for Paraguay and Uruguay) (IMF, 1995c).

Brazil started implementing the MERCOSUR tariff reduction program in September 1994, earlier than required by the agreement. But whereas the trade liberalization of the early 1990s had a limited impact on import flows because of the depreciation of the cruzeiro and depressed domestic demand, the subsequent expansion of the economy and appreciation of the new currency, the real, in late 1994 produced trade deficits that contributed to a protectionist backlash. In response, the government raised tariffs on a range of consumer goods imports in March 1995; tariffs on intermediate inputs were reduced at the same time, hence, the overall effect was to increase the average nominal and effective rates of protection, particularly for automobiles (IMF, 1997b). Some of the tariff increases were rolled back in 1996, but in that same year, quotas were introduced on imports of certain categories of textiles and a provisional “safeguard” tariff of 70 percent was used to protect the toy industry (IMF, 1997a).

In November 1997, in response to the economic crisis created by the turmoil in world financial markets and after consulting with its MERCOSUR neighbors, Brazil implemented an across-the-board increase on all tariff items (inside and outside the common external tariff), raising the ceiling from 20 to 23 percent (USTR, 1998).
to high rates of effective protection in some sectors, notably automobiles and computers.\(^1\) Several retrograde steps were taken in 1995–97, including sector-specific and across-the-board tariff increases (Box 7). In 1998, Brazil’s aggregate TRI was 5 out of 10, with a “relatively open” tariff rating of 2 (based on an unweighted average tariff of 14.6 percent) and a “moderate” nontariff barrier rating of 2. Nontariff barriers included quotas on automobile imports (Box 8) and import licensing for certain products (USTR, 1998). Export restrictions applied to sugar and ethyl alcohol (to ensure sufficient domestic supply), raw hides and skins, and sawn timber. Various export incentives were in place including tax and duty exemptions/reductions for inputs to export industries, export performance requirements, and export finance programs. The Programa de Financiamento às Exportações (Proex), established in 1991

\(^{47}\) The “information law” protected the computer sector with a nominal tariff of up to 50 percent (IMF, 1998c).

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**Box 8. Brazil: Automobile Sector Policies**

The automobile sector in Brazil has traditionally been highly protected. After a brief attempt to open the sector to foreign competition in the early 1990s, the Brazilian government reverted to protectionist policies in 1995, raising import tariffs from 20 percent to 70 percent and (re-)imposing import quotas (WTO, 1996b). Brazil justified the quotas to the WTO as being necessary for balance of payments reasons. However, the Fund testified at the WTO Committee on Balance-of-Payments Restrictions (CBR) in October 1995 that Brazil’s international reserves had “risen to high levels” and that its resort to quotas on car imports was “of particularly serious concern because of the distortionary nature of the restrictions” (WTO, 1995). The CBR agreed with the Fund and told Brazil to remove the quotas.

Brazil replaced the import quotas with a new “car industry regime” that halved the tariff to 35 percent for vehicles imported by foreign automakers operating in Brazil but kept it at 70 percent for vehicles manufactured by foreign automakers with no Brazilian operations. The new rules also required cars assembled in Brazil to have at least 60 percent of their component parts manufactured domestically (or within MERCOSUR).\(^1\) In July 1996, Japan filed a complaint at the WTO, charging that the preferential tariffs favored U.S. and European automakers who had extensive operations in Brazil and discriminated against Japanese automakers who did not.\(^2\) Brazil then designed a tariff quota system, allowing 50,000 cars from Japan, Korea, and the European Union to enter at the 35 percent tariff rate over the next 12 months.\(^3\) In August 1996, the United States filed complaints at the WTO against the tariff quota system and the local content requirement of Brazil’s car industry regime, and in May 1997, the European Union also filed a complaint at the WTO.\(^4\) Brazil settled the WTO disputes out of court. Japan and the European Union dropped their complaints in August 1997 after Brazil extended the tariff quotas for another year and lowered the in-quota and out-of-quota tariff rates.\(^5\) The United States dropped its complaint in March 1998 after Brazil agreed to accelerate its plans to phase out the trade-distorting investment requirements.\(^6\)

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\(^6\) “U.S. to end probe after reaching auto deal with Brazil,” *Reuters*, March 16, 1998.
of private and/or foreign companies in areas of the economy from which they were barred previously, notably shipping, telecommunications, and natural gas distribution through pipelines (IMF, 1995c).

66. Brazil was (and is) a frequent user of the WTO’s contingency measures; it was also on the receiving end of WTO complaints. According to the WTO, Brazil initiated 52 antidumping investigations between 1995 and 1998, making it the seventh largest user of WTO contingency measures during that period.\(^\text{48}\) In June 1996, Brazil used its new safeguards legislation to provide protection to its toy industry (IMF, 1997a). In the same month, Canada filed a WTO dispute against Brazil regarding Proex’s interest rate equalization scheme. Canada argued that the scheme provided financial terms that were more advantageous than purchasers of Brazil’s Embraer aircraft would have obtained from commercial lenders or from export credit agencies had they purchased from other countries, and that hence it constituted an export subsidy that unfairly affected Canada’s own aircraft manufacturer, Bombadier, and violated WTO rules. A dispute settlement panel was established in July 1998.\(^\text{49}\) Complaints were also lodged against Brazil’s automobile sector policies by Japan, the European Union, and the United States during 1996–97, but those were settled out of court (Box 8).

67. The IMF’s trade policy advice to Brazil during this period focused on the need to reverse the slide into protectionism evidenced in 1995–96 and to seek a faster pace of trade liberalization than envisaged under MERCOSUR. In the 1996 and 1997 Article IV consultations, the IMF noted that Brazil’s import tariffs remained relatively high and urged the authorities to bring the rates down and, more generally, to develop a medium-term agenda of purposeful and additional trade liberalization (IMF, 1997a, 1998b). The IMF Managing Director echoed the same message in an interview with the local media.\(^\text{50}\) These calls reflected those made at the time by other multilateral organizations (e.g., WTO, 1996b). Interviews with the IMF mission teams from this period revealed that they did not use the TRI as an assessment tool in Brazil’s case, arguing that it was too “blunt” given the complexities of the Brazilian trade policy regime; instead the missions tended to rely on their own information about Brazil’s trade regime, supplemented by the WTO’s 1996 trade policy review. Staff reports and background documents for the 1995, 1996, and 1997 Article IV consultations described—sometimes in great detail—changes in the level and dispersion of Brazil’s tariff structure, developments in MERCOSUR, and Brazil’s export promotion policies, but the reports were purely descriptive; they provided no analysis to support the staff’s views.

68. The IMF was particularly critical of Brazil’s automobile sector policies. In the 1996 and 1997 Article IV consultations, IMF staff highlighted the “considerable protection” that the high tariffs and local content and export performance requirements afforded the automobile sector, pointing out that although those policies had resulted in a large expansion of automobile trade in the region, the trade had come at a “significant cost” to MERCOSUR customers (IMF, 1997a, 1998b). Several IMF Directors called for a reduction in the protection provided to the automobile sector (IMF, 1998e).

69. IMF staff were divided on how to approach the Proex issue. PDR was concerned that the Proex scheme could constitute an export subsidy in contravention to the WTO Subsidies Agreement, and urged the mission to raise the issue with the Brazilian authorities and advise them to consult with the WTO. But the mission team agreed with the authorities that the Proex subsidies—at less than 0.1 percent of GDP—were insignificant and that their elimination was unlikely to have a major beneficial impact on the fiscal accounts or the balance of payments. The mission thus simply noted that credit provided under export prefinancing facilities “should be granted at market rates” (IMF, 1997a) and did not look any further into the issue.

### The 1998 SBA-supported program

70. Brazil’s macroeconomic situation deteriorated dramatically in the wake of the Russian crisis in August 1998. The real had come under significant pressure in the last quarter of 1997 as the Asian crisis spread to other emerging markets and the international financial environment worsened, but confidence had recovered rapidly thanks to a prompt monetary and fiscal response by the government. However, as external pressures eased, so did the fiscal stance. The deterioration in the public finances and persistent external current account deficits left Brazil vulnerable to contagion from the Russian crisis in August 1998. In November 1998, the government requested support from the IMF in the form of a three-year SBA-supported program.\(^\text{51}\) This program marked the beginning of a succession of IMF programs until 2005.

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\(^{48}\) http://www.wto.org/english/tratop_e/adp_e/adp_e.htm.

\(^{49}\) http://www.wto.org/english/tratop_e/dispu_e/cases_e/ds46_e.htm.

\(^{50}\) “IMF chief blasts Brazil on trade,” Reuters, January 27, 1997.

\(^{51}\) IMF support was to be complemented by support from the World Bank and the Inter-American Development Bank; by bilateral loans through the Bank for International Settlements from the United States, Canada, the European Union, Switzerland, and Norway; and by a bilateral loan from Japan.
71. The 1998 SBA-supported program focused mainly on fiscal adjustment policies; trade policy did not feature in the program. The November 13, 1998 MEFP contained one vague paragraph on trade policy, in which the government committed to “continue the policy of trade liberalization” through regional integration (MERCOSUR), to “aim to increase trade with countries outside the region,” and not to impose trade restrictions that were inconsistent with its WTO commitments or for balance of payments reasons. The government stood firm on its export promotion policies, allowing only that they would be “in line with WTO regulations” (IMF, 1998r). The IMF mission pointed to the recent introduction of protectionist non-tariff barriers such as stiffer measurement and quality standards, flat import fees, and nonautomatic licensing for selected imports, but accepted the authorities’ argument that those measures would not appreciably affect imports.

72. PDR’s Trade Policy Division was concerned about the absence of trade conditionality but its objections were overruled. Though the Trade Policy Division staff pointed out that Brazil’s resort to protectionism in response to the Asian crisis was setting a bad example for the region, the MEFP only subjected Brazil to the minimum standards of WTO disciplines, which left room for increased protectionist measures and were inconsistent with the IMF’s internal guidelines on trade policy reform. No trade conditionality was added in subsequent program reviews.

73. Canada (unsuccessfully) pushed for the IMF to address the issue of export subsidies. The Canadian Executive Director argued that Brazil’s export subsidies were an inefficient and trade-distorting use of public resources and urged the Fund to address the issue, specifically in the context of possible new conditionality attached to the SBA. In April 1999, the WTO dispute settlement panel found Brazil’s export subsidies to be in violation of the Subsidies Agreement, but Brazil immediately appealed the decision. In their discussions with IMF staff, the Canadian authorities argued that the 1997 Indonesia program had provided a precedent for the Fund to make the provision of financial support conditional on the implementation of WTO rulings. The staff, however, declined to use the leverage provided by the SBA to pressure the Brazilian authorities to respond to the WTO ruling.

74. The IMF did not use the program to open Brazil’s financial sector or to bind its financial sector commitments under the GATS. Brazil participated in the 1997 WTO negotiations on financial services, but did not ratify its commitments or take the necessary steps to make them binding under the GATS. Financial sector reform was not a major issue in the SBA which included only two structural benchmarks aimed at further enhancing the regulatory framework and supervision of the banking system (IMF, 1998r). Interviews with the staff indicated that for much of the period under evaluation they were focused more on crisis resolution issues than on the potential for opening the financial services sector. Some staff members did not consider financial services trade to be an issue of concern for Brazil while others said they were aware of the relatively restrictive nature of trade in financial services but did not pursue the issue because management and the authorities were not supportive.

75. The IMF did not include any trade conditionality in its subsequent lending arrangements with Brazil. However, the Fund continued, in the context of Article IV consultations, to call for reductions in trade barriers, at first in the form of unilateral tariff reductions, then—after the authorities explained that they dealt with trade policy issues only in a reciprocal setting—more generally “on a bilateral, regional, and multilateral basis” (e.g., IMF, 2000d, 2001c). PDR on several occasions highlighted concerns over Brazil’s entry barriers to foreign services providers (including financial institutions) but the missions did not take up this issue in program or surveillance discussions. An SIP for the 2001 Article IV consultation (Belaisch, 2002) argued that it was not a lack of foreign competition but rather the oligopolistic market structure of the banking system that explained the relatively limited depth and efficiency of bank intermediation in Brazil compared with other countries.

52 The World Bank provided support for social protection, social security reform, administrative reform, and banking reform, but not trade reform.
53 In August 1999, the WTO’s appellate body upheld all the findings of the panel, but Brazil refused to comply with the decision. The case went to arbitration and Canada was authorized to take appropriate countermeasures against Brazil. In 2001, Canada decided to introduce export subsidies of its own to help Bombardier compete with Embraer. Brazil immediately filed a countersuit at the WTO. In 2002, the dispute panel ruled that Canada’s subsidies violated the Subsidies Agreement; the case also went to arbitration and Brazil was authorized to take countermeasures against Canada (http://www.wto.org/english/tratop_e/dispu_e/cases_e/ds222_e.htm).
54 Belaisch (2002) noted that foreign banks had gained substantial market share in Brazil since the mid-1990s by acquiring domestic banks (greenfield investment by foreign banks is not allowed). By mid-2001, more than half of the top 50 banks had some foreign participation in their capital, in most cases with controlling-interest business. Yet the increased foreign participation had not dramatically changed the efficiency or intensity of competition in the Brazilian banking system. Similar observations were made in Carvalho (2002) and McKinsey Global Institute (2003).
Assessment

76. The absence of trade conditionality in the 1998 SBA-supported program (and subsequent programs) is striking when viewed against the IMF’s trade policy advice to Brazil prior to the program. In the years before the program, the IMF had consistently highlighted Brazil’s still-restrictive trade regime as an impediment to productivity growth. To be sure, trade conditionality would not have been critical for restoring macroeconomic stability under the Fund-supported program, but this was not the only criterion in use at the time: a year earlier, the IMF Board had called for trade liberalization to play an increasingly important role in Fund-supported medium-term adjustment programs and the guidelines on “WTO-consistency” instructed staff to program faster and deeper trade reforms than would have been required by WTO commitments (Table 2). Yet the staff did not elic the Brazilian authorities anything beyond an assurance not to impose trade restrictions that were inconsistent with their WTO commitments. Staff ignored the guidelines that required them to assess trade reforms by reporting the TRI at the outset of the program and the estimated index after the implementation of program measures. There is no indication that the staff used the TRI at all and no indication that anyone noticed.

77. The absence of trade conditionality is striking also when viewed against the global environment during that period. The IMF’s May 1999 World Economic Outlook highlighted “a worrisome increase in pressures for protection in Latin America” in the wake of the Asian and Russian crises—notably, an increase in trade tensions within MERCOSUR between Argentina and Brazil (IMF, 1999d). The size and importance of its economy meant that Brazil’s problems could have had a significant regional impact. In view of such concerns, the IMF should have pressed for a stronger commitment from the government not to engage in further protection, even if the protection was allowed under WTO rules. Fortunately, Brazil did not intensify its trade restrictions and the 3 percent increase in MERCOSUR’s common external tariff was removed by end-2000 as planned.

78. The absence of trade conditionality for Brazil stands in stark contrast to other large programs in emerging market countries during that period. Many of the same policies that the IMF insisted be reformed or abolished in Indonesia, Korea, and Ukraine—e.g., preferential policies in the automobile sector, export taxes on key commodities, and restrictions on foreign bank entry—went unmentioned in Brazil’s SBA-supported program(s). In retrospect, this was the right choice as those policies were not particularly critical for resolving the problems at hand in Brazil. But it raises the question of the IMF’s evenhandedness since the same policies were, arguably, not particularly macro-critical in Indonesia, Korea, and Ukraine either. Was the Fund playing it safe in Brazil after being criticized for excessive structural conditionality in the earlier programs? The timing suggests otherwise: the Fund’s initiative to streamline structural conditionality started only in 2000 (Table 2) and in fact, Ukraine’s EFF-supported program, signed just three months before Brazil’s, was “a leading example of excessive structural activism” (IMF, 2005c).

79. The staff’s decision not to press for the elimination of Proex subsidies was entirely appropriate but appeared arbitrary after the unfortunate precedent set in Indonesia’s 1997 SBA-supported program. The staff argued—correctly—that the Fund should not appear to use the leverage provided by the program to put pressure on one party in a bilateral trade dispute that the WTO was adjudicating. But Canada was not wrong to point out that the same argument did not seem to apply in the case of Indonesia’s national car dispute. The only difference was that Indonesia had four WTO complaints against its national car (from Japan, the European Union, and the United States) whereas Brazil—having successfully settled its automobile disputes with the same three trading partners just before the program started—only had Canada’s complaint against its export subsidies. The Fund’s decision thus seemed to suggest that some major shareholders were more major than others.

80. The staff’s light touch vis-à-vis trade in financial services was also broadly appropriate given the lack of compelling evidence linking restrictions to performance in that sector. In the program context, certainly, the Fund would not have been justified in pushing for stronger commitments to open financial services trade, and staff were right not to consider doing so. In surveillance discussions, however, IMF missions could have engaged the authorities on the pros and cons of improving the contestability of Brazilian banking by introducing greater clarity

55 IEO (2003) suggested that slightly more ambitious structural conditionality would likely have reduced Brazil’s vulnerability to external shocks; this finding was echoed in the Fund’s own ex post assessment of Brazil’s programs (IMF, 2006a), although neither study mentioned trade policy specifically.

56 IEO (2003) also contrasted the limited structural conditionality in Brazil’s 1998 SBA with the broad structural conditionality found in the East Asian programs the previous year.

Brazil’s trade policies did not appear to be of major concern to the United States during that time. The United States had a large trade surplus vis-à-vis Brazil and its exports were not significantly affected by Brazil’s intensification of trade restrictions during 1996–97.
and security in market access conditions for foreign financial institutions (World Bank, 2004).

F. Turkey

Trade policy regime and IMF advice before the 1999 program

81. In the late 1990s, Turkey’s trade regime was rated by the IMF as “moderately restrictive.” Turkey liberalized its trade regime—historically highly protective—when it formed a customs union with the European Union in 1996 (Box 9). Manufactured goods tariffs were pared down to EU levels, but agricultural tariffs remained very high as the customs union did not cover agriculture and services. In the Uruguay Round, Turkey undertook to reduce its agricultural export subsidies but did not make any commitments to cut financial support to its agricultural producers. In 1999, Turkey’s score on the aggregate TRI was 5 out of 10, with a “relatively open” tariff rating of 2 (based on an unweighted average tariff of 13.7 percent) and a “moderate” nontariff barrier rating of 2, reflecting policies such as import quotas on textiles and clothing; import licensing on certain telecommunications equipment, machinery, motor vehicles, chemicals, and other goods; and a state import monopoly for alcohol. Export taxes and export bans existed on several broad categories of products (WTO, 1998).

82. Turkey’s service sectors were very slowly beginning to open up. Most of them were dominated by large state-owned enterprises/monopolies, e.g., Turk Telekom (telecommunications) and Ziraat and Halk Banks (banking). Although Turkey liberalized its financial sector, including foreign entry, in the 1980s, foreign banks played only a very small role in the financial system (IMF, 1996c).

83. The IMF was very supportive of the Turkey-EU customs union. Fund staff listed numerous potential benefits that could be expected as a result of the customs union, such as: lower prices of imported products for industries that relied on imported raw materials and investment goods; efficiency improvements brought about by increased competition with EU producers; no more EU quotas on Turkish textile and clothing exports; improved market access to third countries with whom the European Union had preferential trade agreements; and technology transfer from an increased flow of foreign direct investment (IMF, 1996c). The staff noted that the impact of the customs union on the Turkish economy would depend on “complementary policies … to keep the fiscal deficit from rising as a result of the loss of tariff revenues.” Directors welcomed the implementation of the customs union, noting that it “opened major growth opportunities for the country” (IMF, 1996d). Once the customs union was in place, the Fund essentially stopped paying attention to trade policy issues in Turkey.

84. IMF staff did advise Turkey to cut agricultural subsidies, but from the viewpoint of improving the fiscal position rather than liberalizing trade. In June 1998, the IMF agreed to an 18-month Staff-Monitored Program (SMP) to lower Turkey’s inflation to the single digits over three years.58 The

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58 During the 1990s, the monetization of large and growing fiscal deficits had led to average annual inflation of almost 80 percent.
linchpin of the disinflation effort was to be a sustained fiscal consolidation. In this context, IMF staff observed that agricultural subsidies weighed heavily on the budget and that agricultural tariff protection was excessive; they advised the authorities to reduce agricultural support prices closer to international levels and to eliminate input subsidies and subsidized credit to the agricultural sector (IMF, 1998l; Orsmond, 1998). The SMP included commitments to limit agricultural support price increases in 1999 to targeted, rather than past, inflation rates and to gradually eliminate the interest rate subsidy on agricultural credits (IMF, 1998k).

**The 1999 SBA-supported program**

85. In December 1999, the Turkish government requested a three-year SBA-supported program in support of its new disinflation and fiscal adjustment program. The framework of the SMP had proven too weak to stop the deterioration in the fiscal accounts: in the absence of major structural reforms, fiscal policy had quickly turned expansionary in the face of weakening economic activity (compounded by the knock-on effects of the Russian crisis on Turkish exports), the announcement of early elections, and the devastation wrought by the August 1999 Marmara earthquake. As a result, the new government that took office in mid-1999 had to contend with recession, high real interest rates, and rapidly rising public debt. The objective of the 1999 SBA-supported program was to bring Turkey’s unsustainable public sector debt dynamics and high inflation under control by breaking inflationary expectations once and for all; this was to be accomplished through a strong fiscal adjustment and a preannounced crawling peg exchange rate anchor (IMF, 1999h).

86. The 1999 SBA-supported program had a wide-ranging structural reform agenda that did not include trade reforms per se but did include trade-related reforms in agriculture. As in the SMP, the primary goal of these reforms was to improve the fiscal situation. In the area of agricultural reform, the program included measures to: reduce the spread between the support price and the projected world market price for cereals and adjust the import tariff so that the tariff-inclusive import price would be above the support price in 2000–01; discontinue unofficial government support to industrial crops by granting full autonomy to agricultural sales cooperatives and their unions (a structural benchmark for the completion of the first review); 59 and phase out the credit subsidy to farmers (also a structural benchmark). Fund staff estimated the primary fiscal cost of the various agricultural policies to be around 2 percent of GNP (Moalla-Fetini, 1999). Agricultural reform issues were subsequently picked up by the World Bank under an Economic Reform Loan that was approved in May 2000 (IMF, 2000b).

87. No trade conditionality was introduced in Turkey’s subsequent SBA-supported programs (2002–05 and 2005–08), although IMF staff addressed trade policy issues sporadically during 2002–07. In the staff reports for the 2002 and 2005 SBA-supported programs, Fund staff stated that trade policy conditionality was not included because Turkey’s trade regime was “only moderately restrictive” (IMF, 2002a, 2005a). During the discussions for the 2005 SBA-supported program, the staff recommended lowering agricultural tariffs and rethinking any agricultural reforms that would move the system from direct income support back to more distortionary production subsidies, but they did not include these issues in program conditionality because agricultural reforms were being handled by the World Bank (IMF, 2005a). In the 2002 and 2004 Article IV consultations, the staff called attention to Turkey’s high agricultural tariffs and “overuse” of antidumping measures (IMF, 2002b, 2004b)—the same points that were highlighted in the WTO’s 2003 trade policy review of Turkey (WTO, 2003). 60

88. One trade-related issue that emerged in the mid-2000s was the expiration of international textile and clothing quotas in January 2005. Fund staff noted that the elimination of quotas under the WTO’s Agreement on Textiles and Clothing (ATC) would pose a significant challenge to Turkish exporters—particularly in the EU market where Turkey’s textile and clothing exports were protected by quotas on exports from competitors such as China, India, and Pakistan; they estimated that the export loss could cut GNP growth by 0.3–0.4 percent in 2005. Turkey would also need to remove its own quotas on textile and clothing imports when the ATC expired (IMF, 2004b). The authorities had been nulling a cut in the VAT for textile products since 2004, well before the expiration of the ATC. Aside from providing relief to domestic textile and clothing producers, the proposed cut in the VAT was ostensibly aimed at reducing tax evasion. Fund staff argued strongly against this move, noting that the standard 18 percent VAT rate in Turkey was not high by international standards, that cutting the VAT rate at a time of the government. They typically purchased commodities directly from farmers, undertook primary processing and packaging, and resold the commodities to final users (Orsmond, 1998).

59 Agricultural sales cooperatives and their unions were authorized to undertake support purchases of industrial crops on behalf of the government.

60 The coverage of trade policy developments in the 2004 Article IV staff report drew on WTO (2003).
of strong domestic demand and a widening current account deficit was risky, and that ad hoc rate cuts for specific sectors ran counter to best practice and undermined policy credibility (IMF, 2005a).61 In the MEFP for the 2005 SBA-supported program, the government committed not to change VAT rates or coverage during the program period (excluding previously agreed rate reductions for health care, education services, and certain food items, in line with EU directives) (IMF, 2005a).

Assessment

89. The level of trade conditionality in the 1999 SBA-supported program was commensurate with the IMF staff coverage of trade policy prior to the program. The staff report for the 1999 SBA-supported program request did not mention Turkey’s TRI or explain why trade reforms were omitted from the program. The staff report for the 1999 SBA-supported program was commensurate with the IMF staff coverage of trade policy prior to the program period (excluding previously agreed rate reductions for health care, education services, and certain food items, in line with EU directives) (IMF, 2005a).

90. The IMF may have missed the opportunity to include tariff reduction in the overhaul of agricultural support policies. The agricultural reform policies that were outlined in the December 1999 MEFP and subsequently elaborated and implemented with the help of the World Bank aimed to reduce the burden of support on the economy and move Turkey’s agricultural policies closer to those of the European Union by replacing the potentially more production-distorting measures with a less distortionary direct support system. But the reforms did not address the relatively high tariff protection in agriculture—even though IMF staff had identified this as a key component of Turkey’s agricultural support policies (Orsmond, 1998; Moalla-Fetini, 1999) and the WTO had criticized it as “a tax not just on consumer welfare but also implicitly on manufacturing and services that compete[d] with agriculture for production factors” (WTO, 1998). According to the WTO, Turkey’s simple average applied most-favored-nation tariff rate for agricultural products was 28.3 percent in 2007 (WTO, 2007b)—higher than the European Union’s, at 18.6 percent (WTO, 2007a).

91. In subsequent programs, the IMF proved ineffective in persuading the authorities not to yield to protectionist pressures arising from the expiration of ATC quotas. IMF staff gave sound advice against selective VAT cuts—their arguments were eminently sensible. However, the authorities were not totally convinced, as evidenced by their discussions with Fund staff and management and by their public statements.63 In January 2005, Turkey imposed import quotas on a number of textile products from China, taking advantage of the textiles-specific safeguards clause written into China’s WTO accession protocol. In March 2006, the Turkish authorities went ahead and cut the VAT rate to 8 percent on textile products. IMF staff reiterated their objections and came up with further (sensible) arguments against the VAT cut, that is, that targeted tax reductions ran counter to program commitments to simplify the tax structure and would invite calls from other sectors for similar treatment (IMF, 2006b).64 But there is no indication that the staff discussed alternative options with the authorities, such as program augmentation under the Trade Integration Mechanism; staff interviewed pointed out that Turkey’s loan was already in the very high brackets and that besides, they were not in favor of policies that would delay Turkey’s adjustment to the post-ATC environment. In the event, the authorities (again) agreed to avoid introducing any further rate reductions (IMF, 2006b) but (again) reneged when they cut the VAT rate to 8 percent for the tourism sector in 2007.

G. Overall Evaluation

92. In the cases studied there was no obvious correlation between trade conditionality and initial trade restrictiveness. All five countries restricted their trade to similar extents prior to their IMF-supported programs, as measured by the Fund’s own TRI as well as other assessments (Table 6). But the amount of trade conditionality in the five programs differed significantly: Indonesia had a relatively large number

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61 The FDMD discussed the VAT cut at length with the Turkish finance minister during a meeting in Washington in April 2004.
62 The staff reported Turkey’s TRI (5) in 2002 but not in 2005 after the Board decided against publishing the TRI in staff reports.
63 “Turk minister sees positive developments with IMF,” Reuters, February 19, 2004; “Finance ministry working to cut VAT on textiles,” Turkish Daily News, April 16, 2005. In his conversation with the IMF FDMD in April 2004, the Turkish finance minister said that the VAT cut had been put aside only temporarily for the seventh review of the (2002) SBA-supported program.
64 See also “IMF criticizes Turkey’s VAT rate cut on textiles,” Reuters, March 9, 2006.
of trade conditions, Korea and Ukraine had some, Brazil and Turkey none.

93. There was no obvious correlation between trade conditionality and the Fund’s coverage of trade issues prior to the program. Preprogram coverage of trade policy issues was minimal in Korea and Turkey—indicating a perceived low degree of macro-relevance—yet one of these countries had substantial trade conditionality while the other had none. On the other hand, the Fund argued strongly and consistently for further trade liberalization in Indonesia and Brazil yet only applied trade conditionality in Indonesia and not Brazil. In all cases, the Fund’s preprogram coverage of trade policy issues tended to be superficial, being limited mostly to reporting but not analyzing policy changes. Thus when trade conditionality was included in a program, Fund staff were often unable to explain why those policies were targeted, let alone to quantify their macroeconomic effects.

94. There was no obvious correlation between trade conditionality and the financial crises that necessitated the programs. Each of the five programs was introduced to address a capital account crisis and loss of market confidence, although each of the crises had anything to do with trade. The closest that trade reforms came to meeting the macro-criticality criterion for the Fund’s structural conditionality was in the case of Indonesia, where many of the trade liberalization measures (e.g., dismantling import monopolies) were also seen as measures to improve governance.

95. Because trade reforms were not crucial (except arguably in the case of Indonesia), Fund staff had some leeway in choosing whether or not to include them in the structural adjustment package. As these were high-profile (and in most cases high-access) programs, political considerations were often the deciding factor. 66 This was most obvious in the case of Korea, where the Fund inserted trade conditionality to win U.S. and Japanese support, and Ukraine, where the Fund capitulated on trade (and other) issues in order to accommodate the G-7. The international, and often highly political, nature of trade policy made it more likely to be taken up by Fund members—trading partners/competitors of the program country—hoping to exploit the leverage provided by the Fund program. Fund management and staff picked through the lobbying on a case-by-case basis; their decisions were inevitably arbitrary.

66 A background paper for the IEO’s 2008 evaluation of IMF governance made the same observation: “Although formal procedures are in place to safeguard staff autonomy, shareholders are able to exercise substantial informal influence over the content of conditionality that is not subject to scrutiny, as in the cases of Indonesia and Korea” (Stone, 2007).

Table 6. Indonesia, Korea, Ukraine, Brazil, and Turkey: Trade Restrictiveness

<table>
<thead>
<tr>
<th></th>
<th>Aggregate TRI (1 to 10)</th>
<th>Tariff Rating (1 to 5)</th>
<th>Unweighted Average Tariff Rate (Percent)</th>
<th>NTB Rating (1 to 3)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Indonesia (1997)</td>
<td>5</td>
<td>2</td>
<td>13.0</td>
<td>2</td>
</tr>
<tr>
<td>(No WTO TPR before the program.)</td>
<td></td>
<td></td>
<td></td>
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<tr>
<td>Korea (1997)</td>
<td>4</td>
<td>1</td>
<td>9.0</td>
<td>2</td>
</tr>
<tr>
<td>“Agriculture and significant services sectors have remained largely insulated from international competition, creating economic distortions at home and political frictions abroad.” (WTO, 1996a.)</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Ukraine (1998)</td>
<td>5</td>
<td>2</td>
<td>12.7</td>
<td>2</td>
</tr>
<tr>
<td>(No WTO TPR before the program.)</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Brazil (1998)</td>
<td>5</td>
<td>2</td>
<td>14.6</td>
<td>2</td>
</tr>
<tr>
<td>“[F]requent tariff adjustments give an appearance of uncertainty to the trade and investment régime. A series of potentially trade distorting measures taken since 1995 stand in sharp contrast to Brazil’s general record of reform.... Greater co-ordination, transparency and a more measured response to requests for assistance from specific sectors would help Brazil translate its stated commitment to free trade into actions more clearly consistent with its development needs and with a stronger multilateral trade system.” (WTO, 1996b.)</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Turkey (1999)</td>
<td>5</td>
<td>2</td>
<td>13.7</td>
<td>2</td>
</tr>
<tr>
<td>“[T]he current trend of increasing support in [the agricultural] sector is contrary to the liberalization seen elsewhere in the economy. This sectoral imbalance could be a tax not just on consumer welfare but also implicitly on manufacturing and services that compete with agriculture for production factors.” (WTO, 1998).</td>
<td></td>
<td></td>
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</tr>
</tbody>
</table>
96. In some cases, trade conditionality was included for symbolic purposes. Prime examples were the abolition of the national car and import monopolies in Indonesia and the elimination of the sunflower-seed export tax in Ukraine. According to senior Fund staff, in cases where wide-ranging structural reforms were necessary, the Fund often had to be pragmatic and focus only on select well-known policies. Although these policies and the Fund conditionality directed at them captured a great deal of media attention, they were not subject to rigorous—or indeed, any—analysis because their deleterious effects were thought to be obvious and staff resources were considered to be better used elsewhere.

97. Rules and guidelines were sometimes disregarded. PDR’s request for staff reports to assess trade reforms in medium-term programs was ignored half the time: only Ukraine’s 1998 request for an EFF-supported program and Turkey’s 2002 request for an SBA-supported program incorporated the requisite information. The guidelines on “WTO-consistency” also seemed to be taken lightly: the Fund insisted that Indonesia and Korea bind their financial services liberalization in the GATS, despite admonitions to avoid such “cross-conditionality” (Table 2). In 2002, the definition of “cross-conditionality” in Fund guidelines shifted toward a situation “under which the use of the Fund’s resources would be directly subjected to the rules or decisions of other organizations” (IMF, 2002c).

98. Interagency cooperation was less than it could have been. Only in Indonesia was the World Bank active in trade policy issues, but the Bank’s credibility there was close to zero as it was perceived as a supporter of the Soeharto government. In the other case study countries, the World Bank’s focus was elsewhere: in Korea, on financial sector reform, corporate restructuring, and social sector reforms; in Ukraine, on public sector reform, agricultural sector reform, energy sector reform, financial sector reform, and privatization; in Brazil, on social protection, social security reforms, and state-level administrative reforms; and in Turkey, on banking and public sector reforms, social support, and agricultural reform. Cooperation with the WTO was also imperfect. WTO trade policy reviews were referred to only in staff reports for Brazil and Turkey, but only after 2000; they were not used in designing Fund programs. The Fund was slow to share its documents with the WTO Secretariat in the early days of the Asian crises, but this glitch was quickly resolved. More seriously, the Fund overstepped its boundaries in Indonesia’s national car case when it anticipated the judgment of the WTO dispute panel and overrode the panel’s decision on the implementation period.

99. The trade conditionality was somewhat, but not totally, effective. Some of the trade reforms were sustained; most of these were reforms bound by commitments to the WTO and/or other organizations such as the OECD (e.g., financial services liberalization measures in Indonesia and Korea and elimination of the import diversification program and trade-related subsidies in Korea) or by commitments in existing or potential preferential trade agreements (e.g., tariff reduction in Indonesia and reform of agricultural support policies in Turkey). Some of the trade conditions—the symbolic ones especially—stirred up an active policy debate in the program country even if they were ultimately not implemented as planned. Some of the trade reforms were subsequently reversed: these tended to be measures that were not carefully thought through at the outset (e.g., the elimination of Bulog’s monopolies and log export taxes in Indonesia) and measures that could be undone without violating WTO or other commitments (e.g., tariff increases within WTO bound rates in Ukraine).

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