STATEMENT: IN DEFENSE OF COUNTERTRADE

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Although multilateral trade transactions involving cash or credit are more advanced forms of doing business than barter, it is my view that they will never replace it. Countertrade, a modern-day mode of barter, plays an important role in world trade. Despite widespread use, countertrade has been the subject of dogmatic and ideologically-based criticism that is often based on faulty economic analyses.

In the early 1970s, the United States and other OECD countries actively supported long-term countertrade dealings with socialist countries [1]. The rhetoric of policy-makers in these countries has changed, however, and countertrade is now attacked as dangerous to world trade [2]. Western authors, for example, usually depict countertrade as a parasitic phenomenon proliferated by the socialist countries with the aim of unloading otherwise unsaleable goods on Western partners. They allege that countertrade undermines the General Agreement on Tariffs and Trade ("GATT") system, which condemns reciprocity and bilateralism. Some argue that the world market, which acts as a regulator of comparative advantage, is distorted by countertrade activity. Others maintain that countertrade is used to charge free market economy countries with the inefficiencies and high production costs of state-controlled economies.

These viewpoints manifest both political and ideological considerations. Although we cannot discount the present political climate of East-West relations, I suggest that we separate the trade and political issues for discussion purposes in order to avoid confusing economic and political considerations.

Opponents of countertrade advance two sets of economic arguments. First, they contend that countertrade is detrimental to the seller, or to both parties [3]. Second, they allege harmful "external" ramifications, such as protectionism and the closing off of part of the free market. It should be noted with reference to the first set of arguments that trade statistics for the 1970s suggest that the demand for countertrade has increased not only in East-West trade but also in North-South and West-West relations [4]. Furthermore, trade experts expect barter-like practices to increase in every region of the globe [5]. These observa-

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tions suggest that countertrade has become an economic necessity that profits all parties involved.

Nevertheless, some commentators believe that countertrade is dangerous to the parties themselves. Philip S. Beckerman concludes that: “in some instances... everyone pays and no one benefits” [6]. His hypothetical case, involving the sale of Indonesian pepper in exchange for goods manufactured in the U.S., however, is not persuasive. Beckerman states that if the U.S. firm overestimates the quality of the Indonesian product, or if the demand for the product in the United States is weak, the firm may suffer a loss. Alternatively, the firm may negotiate a lower purchase price, arguing that it will have to pay a “handsome” commission to a middleman, e.g. Philipp Brothers, Inc., to distribute the goods in the United States. The costs of countertrade are thus borne by the seller. Therefore, it appears that the risks inherent in countertrade transactions do not differ from those present in other transnational dealings.

Commentators also argue that countertrade benefits only the exporting country. Exporting countries engage in countertrade for well-known reasons: the need to balance chronic trade deficits, currency volatility, high interest rates, and credit shortages. For many governments countertrade is the only available means to reduce their external debt and obtain necessary commodities. Their partners, however, often find that countertrade requirements are difficult to carry out.

Despite the arguments to the contrary, there are virtually no data confirming that “switches”, “barter”, “buybacks” or other forms of countertrade assume an inherently “parasitic posture” [7]. While it is true that countertrade allows Eastern countries to export goods that might not otherwise be saleable on an open international market, and to import Western goods that they desire, it is also true that countertrade permits Western countries to find markets for goods that are unsaleable in the West [8]. Rather than viewing countertrade as being parasitic, a better attitude would be, as stated by a General Electric executive, that: “We have to think, as a country, that half a loaf is better than none.”

It should also be remembered that the percentage of Eastern products which are difficult to sell in the West is very low. For example, a large proportion (43%) of the buyback goods imported by the OECD countries from Eastern Europe consists of energy products for which there is a steady demand in the West. Another 30% of Western imports from that region consists of intermediate goods, primarily chemicals, which also can be easily sold. Only about 2% of East European imports are consumer goods [9].

The second set of economic arguments against countertrade is based on allegations that countertrade harms parties other than those directly involved in the agreement. It is argued that countertrade harms the competitors of the importing and exporting nations, and constitutes a threat to the GATT system.

The argument that countertrade harms nations whose goods compete with

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those of the importing nations fails to recognize that any contract, not only countertrade agreements, will close off a portion of the market, thereby harming competitors. Using Beckerman's example of Indonesian pepper, it is true that if Indonesia sells its pepper at a drastically reduced price in exchange for badly needed manufactured goods, her neighbors who also export pepper will be hurt. However, under these circumstances Indonesia would make the same decision absent a countertrade agreement. Furthermore, it makes no difference to neighboring competitors whether the price cut benefits the countertrader, a middleman, or the final purchaser of the pepper.

It is also argued that countertrade poses a threat to domestic competitors of the exporting company. Acknowledging that large buyback agreements can increase competition in an importing country. I cannot accept the proposition that they are inherently more disruptive or dangerous than any other import. On the contrary, thanks to the joint efforts of Western legislators and importers, the risks of market disruption and cut-throat competition resulting from long-term compensation agreements are much lower than in other areas. First, the legislators have provided Western competitors with a plethora of special and often highly discriminatory relief measures, some of which are available even in the absence of proof of injury, e.g. Section 701 of the Trade Agreements Act. Second, Western countertraders, risking legal sanctions, take great pains to avoid underpricing or suddenly increasing the volume of imported goods [10]. These forces serve to greatly reduce competition in the domestic marketplace from countertraded goods.

Finally, countertrade critics condemn countertrade as a threat to the GATT system of open and multilateral trade. It is true that the reciprocity requirement built into countertrade often encourages bilateralism. It is also clear that countertrade policies are aimed at protecting local industries. Given the current global economic situation, however, countertrade is justified as a necessary, and perhaps the least offensive, method of dealing with huge trade deficits, which are a major obstacle to expanding transnational commerce.

In the present world of protracted recession, huge trade deficits, cash and credit shortages, economic sanctions, and trade wars, it is unrealistic to expect a completely free-trade code of conduct, even from countries that favor cash/credit transactions. In the midst of our prolonged global recession, even the richest countries, including the United States and the countries of Western Europe, have resorted to erecting protectionist barriers. It is estimated that between 40 and 48% of international trade is conducted under some sort of nontariff restraints. It is clear, therefore, that countertrading nations are not alone in practising protectionism.

When viewed against the backdrop of such crude protectionist schemes as voluntary restraints, quotas, bureaucratic harassment, and lists of prohibited imports [11], countertrade is probably the least objectionable method of reducing trade deficits. This is especially true when one realizes that, unlike the
above-listed protectionist practices, countertrade facilitates the expansion rather than the reduction of the overall volume of world trade. Thus, many Western European businessmen recognize that countertrade constitutes an “interface tool” or mechanism devised to transfer the economic needs and potentials of one system (nonmarket economies) to another system (free market economies) [12].

As noted, the global recession has motivated most countries to adopt protectionist measures rather than a policy of unfettered free trade. Those who continue to advocate such free trade appear to be basing their arguments on an economic model of the world that no longer corresponds to reality. They correctly observe that the unprecedented growth in world trade during the years 1948–1978 was facilitated by the GATT country pledges to reduce tariffs and eliminate other trade barriers. They fail to recognize, however, that the three decades of trade boom were largely the result of post-war recovery and stable monetary conditions around the world. These conditions no longer exist. The world economic order is plagued by recession and monetary instability. Until these conditions pass, the weaker economies should be permitted to maintain some degree of protection. This policy would, in fact, be consistent with GATT, which allows member states to resort to such measures in special circumstances.

In conclusion, although countertrade arguably involves greater risk than cash/credit transactions and sometimes serves to freeze bilateral relations, these disadvantages are outweighed by advantages such as the exchange of goods otherwise unsaleable by either side, protection of local industry, reduction of trade deficits, and debt-repayment. Moreover, countertrade appears to be the least offensive form of home market protection in a world where such protection is necessary for all countries. The growing skill of special clearing houses, countertrade subsidiaries, and banks allows for more symbiotic relationships between buyers and sellers and for improvements in the distribution of bartered goods. Nevertheless, rigid countertrade policies should be treated by the countries adopting them as a harsh economic necessity entailing more risk for their traders than for their partners. Such risks include the effects of selling goods which have not achieved world quality and the traders' inability to establish their own marketing channels and goodwill.
Notes

[1] Thus, for instance, the deal between Occidental Petroleum Corp. and the Soviet Union, under which the U.S. firm has been buying ammonia for sale in the United States from plants that it helped to finance and construct in the exporting country, had been first approved by the U.S. government and then challenged under Section 406 of the 'Trade Act. See S.A. Baker and R.O. Cunningham, Legal Constraints on Countertrade, 5 J. Comp. Bus. & Cap. Mkt. L. (1983), this issue.


[6] Beckerman, supra note 3. According to J. de Miramon "the return to barter reduces the urgency of a more rational cost-price structure, a multilateral trade framework and currency convertibility", supra note 5, at 12. 15.


[8] "Countertrade may be the only way in which technology thoroughly exploited in the West, can still be licensed for a valuable consideration. It may also be the most feasible way for a licensor to be assured access to its licensee's operation for purposes of quality control." P. Ehrenhaft, Insuring U.S. Participants' Interests in Countertrade, 5 J. Comp. Bus. & Cap. Mkt. L. (1983), this issue.

[9] Source: OECD statistics quoted by J. de Miramon, supra note 5, at 13. While the same report shows that countertrade accounts for less than 15% of the total East-West trade, other sources estimate that compensation transactions represented a much higher proportion, namely 25–30% of total world trade at the beginning of the 1980s. See New Restrictions on World Trade, Business Week, July 19, 1982, at 118.

[10] Thus, for instance, the agreement between Occidental Petroleum and the Soviet F.T.O. involving the ammonia deal provided that the imports were to be priced no lower than prevailing market prices. It also provided for importing steady quantities of ammonia in order to avoid disrupting the U.S. market. Baker & Cunningham, supra note 2. According to A. Romoli, "The anticipated flood of exports of chemical products to EEC markets has not materialized yet." See infra note 12.
