IMPORT LICENSING IN NEW ZEALAND

INTRODUCTION

This article discusses the objectives of the import licensing system in New Zealand and sketches out both the historical background to the system and the way in which it currently operates. The economic effects of quantitative restrictions are also set out in a straightforward fashion. An earlier article described the tariff arrangements in New Zealand and this should be read in conjunction with the present piece. A later companion article will discuss the more general problems with the protective system in this country and the economic rationalisation underlying the need for a review of protective measures operating in New Zealand.

New Zealand has had a system of import licensing, applied with varying degrees of intensity, from 1938 to the present day. Currently, about 23 percent of imports are subject to quantitative restrictions under licensing, although of course this figure gives no indication of the volume of imports which are totally excluded by the system.

OBJECTIVES

The principal objectives of the licensing system appear to have been twofold:

(1) To help conserve foreign exchange, in order to assist the balance of payments situation.

(2) To protect domestic industry, in order to promote the establishment and expansion of manufacturing enterprises with the associated objectives of diversifying the industrial structure of the economy (to reduce reliance on the agricultural sector) and to facilitate employment growth.

This second objective is of course related to the first, in the sense that advocates of protection by import licensing invariably also argue that this encourages import substitution activities which in turn assist the balance of payments.

At different times, these primary objectives have been supplemented by a series of subsidiary aims, such as the desire to affect the mix of imports — away from finished goods and in favour of raw materials, components and capital equipment — the geographical origin of imports, the type of goods (essentials versus luxury goods, etc.), the type of manufacturing establishments encouraged to set up or expand in New Zealand, the domestic/foreign ownership mix of such enterprises, and the degree of concentration or competition within various domestic industries (i.e. the number of firms in an industry).

These various aims have not always been clearly spelt out, and neither has the justification for the use of licensing rather than some other mechanism such as the use of tariffs (which are generally thought by economists to be more efficient in an economic sense) or the free market mechanism to promote industrial development; and the use of the exchange rate allied with monetary and fiscal policies to achieve the desired balance of payments position.

Opponents of licensing have usually queried the ability of bureaucrats to reach sound decisions on what are essentially complex issues which may well be resolved more efficiently and effectively by alternative means which allow market forces to play at least some part. These sorts of issues surrounding the use of quantitative restrictions have often been debated vigorously at a popular level but in the past have too seldom been analysed in depth on the basis of appropriate economic research.

More recently, however, a series of individual industry studies have called into question in a serious manner the nature of New Zealand's protective system and have called for major policy reviews. One of these, in the textiles area, is already being implemented and other studies are expected to follow. A later article will discuss these matters more fully.

Apart from these industry reviews, a range of other policy measures have been taken in recent years to promote a restructuring of New Zealand industry by encouraging export growth and gradually facilitating an easing of the protective mechanisms. These moves include a rationalisation of tax incentives for exporters, the introduction of the supplementary minimum prices scheme for farmers, some easing of foreign investment policy, the adoption of a more flexible exchange rate system, a substantial widening of the forward exchange arrangements, and the removal of generalised price control.

THE HISTORY OF IMPORT LICENSING IN NEW ZEALAND

Import licensing, first introduced in December 1938, is a relatively recent phenomenon compared to the use of the customs tariff which was first introduced in the early 1840's. At the time of its introduction the New Zealand Government imposed total import control and export licensing regulations for balance of payments reasons. The regulations aimed to ensure that overseas debt services could be met and that sufficient funds would be available for essential imports. Under the import control regulations introduced at that time the importation of goods was prohibited except under a licence or a specific exemption. The nature and extent of import licensing controls have varied over time with, in some periods, controls being applied to allocations of foreign exchange in general rather than specific imports, although the general principles remained the same.

The years of World War II from 1939 to 1945 were a period when New Zealand could sell all the export commodities that it could produce while the availability of imported goods was largely governed by the needs of the war effort. There was some expectation that after the war ended import licensing might be removed when controls which had been necessary for war purposes were being dismantled. However, import licensing was retained even though the late 1940s saw assured markets and better prices for New Zealand's exports while imports were restricted by the difficulty in obtaining supplies from countries which were primarily concerned with their own post-war reconstruction.

The early 1950s brought high export prices, particularly for New Zealand's wool. This, coupled with the change of Government in late 1949 when the National Party first came to power, resulted in a significant relax-

ation in the level of import controls as a large number of commodities were exempted from licensing requirements. The National Government believed that the system of import controls which had been developed by the previous Government contributed to rising costs and inefficiency. The Import Advisory Committee was established to overhaul the import licensing system and its administration. This resulted in changes which made the licensing regulations more consistent in their application to goods coming from 'sterling area' and other countries. The changes included the reclassification of a large number of items into categories which were exempt from licensing. A further area of change was in the introduction of non-remittance licensing where licences could be issued to persons wishing to import goods, using for payment their own personally held foreign funds. Abuses of the scheme later resulted in it being modified to permit people to import only goods for their own use and subsequently the scheme was phased out.

During its first period in office the National Government maintained a commitment to dismantling the import licensing system. The extent to which import policy was liberalised can be gauged by the fact that in the 1957 Licensing Schedule only 209 item codes were controlled compared with 950 in 1950. For the same period the number of item codes for which no allocation of licences were made fell from 333 to 27. The value of licensed private imports as a percentage of all private imports dropped from 99.5 percent to 13.0 percent between 1950 and 1957.

At the end of 1957 New Zealand was entering one of its recurrent balance of payments crises as a result of a decline in prices for exports and a rise in import payments. At the same time the Labour Government returned to power and at the beginning of 1958 announced that a policy of overall import licensing would be re-instated immediately. Under the new policy of foreign exchange allocation, overseas funds were allocated to meet all basic needs for imported foodstuffs and, so far as possible, factories were able to get the amount of raw materials required to maintain full production although significant cuts were made in other items.

During the 1960s there was some relaxation of import controls as and when the New Zealand foreign exchange situation permitted. The return to a National Government in 1960 resulted in an easing of the licence allocations in the 1961 Import Licensing Schedule. However, during that year foreign exchange reserves dropped to a low level, the Government adopted more restrictive measures and the 1961 licensing period was extended to June 1962. From 1963 onwards the Government returned to its policy of progressive removal of import controls, the results of which may be seen in figure 1 where the percentage of imports brought in under various authorities are shown for succeeding years. By the early 1970s about 30 percent of imported goods remained subject to import licensing control and this was further reduced to approximately 23 percent by 1979 as can be seen in figure 1.

During the 1970s a new role for import licensing emerged with the introduction of a scheme designed to encourage manufacture for export. Under this scheme 'replacement licences' could be automatically granted to permit the replacement of components used in the manufacture of products for export. The use of import licensing to control the importation of some raw materials and machinery provides the Government with a further means of controlling the establishment of any new industry. In recent years more emphasis has been placed on a new industry's ability to be internationally competitive and to develop without the level of protection afforded by import licensing at times in the past. Unfortunately, New Zealand's dependence upon imports has remained, although the import pattern has changed from a concentration on consumer goods to one with an emphasis on materials, plant and equipment. Developed behind the protective framework provided by the customs tariff, import licensing and a frequently over-valued exchange rate, only a comparatively small range of manufacturing plants succeeded in becoming competitive on international markets without the help of other incentives.

As the country entered a prolonged period of depressed terms of trade in 1974 it became necessary for the Government to take action to correct an acute balance of payments problem. To tighten controls on those goods still subject to licence, the licensing schedules in the following several years generally provided for a constant value of imports with only relatively minor extensions. Devaluation of the New Zealand dollar and increases in the price of imports meant that in volume terms the imports subject to licensing which were allowed access were progressively reduced. Nevertheless this formed only a small part of the overall balance of payments policy.

As the initial policies adopted proved inadequate to promote adjustment to the country's balance of payments problems, the Government was forced to introduce a variety of measures. These aimed, through making exporting more profitable, to encourage manufacturers to move more vigorously into exporting. The measures included some rationalisation of tax incentives for exporters, the introduction of a supplementary minimum prices scheme for farmers, the adoption of a new exchange rate setting mechanism, and the implementation of an industry studies programme which aims to rationalise activity within certain industry groups in the economy in order to enhance their efficiency and competitiveness.

A limited system of tendering for additional import licenses was introduced in 1980. The objective of this system is to increase flexibility, encourage efficiency and to create a more competitive environment among the manufacturing industries. It is explained more fully in the following section.

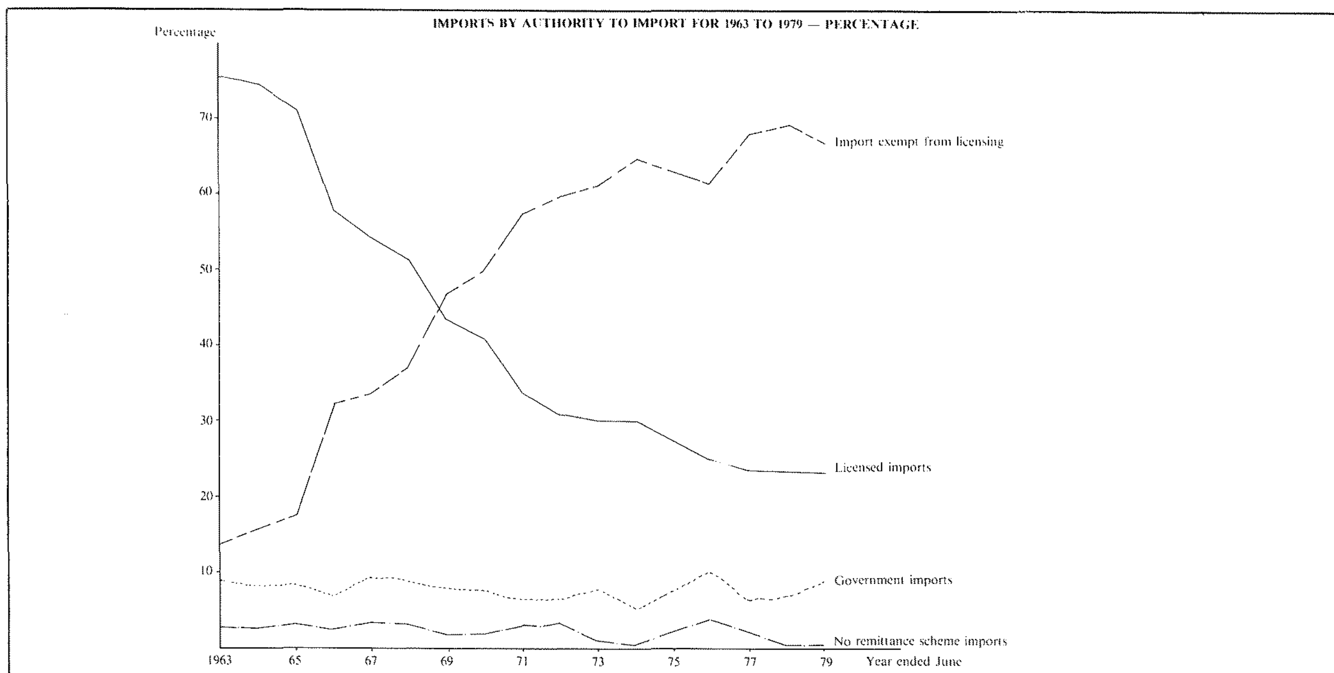
THE NEW ZEALAND IMPORT LICENSING SYSTEM

Government control over imports, through import licensing, has been a significant component of New Zealand's balance of payments policy for much of the period since 1938. The extent to which it has been utilised for this purpose has varied considerably with other policies such as exchange rate and fiscal policy providing the main policy elements on certain occasions. The 1958 and 1967 balance of payments crises were examples. Over the years the emphasis on a balance of payments function seems to have diminished with the protection of domestic industry and employment being seen as the more important roles.

(a) The Basic Import Licensing System

The allocations of licences for goods subject to import control is set out each year in a lengthy document known as the Import Licensing Schedule. This lists all classes of goods, identifying, for the 'ensuing licensing period', those goods which are exempt, those for which special

FIGURE 1



Source: Department of Statistics.

licences are issued only on a case-by-case basis and, for all others, the value of licences which may be allocated relative to previous licensing period levels.

Import licences, which are issued by the Department of Trade and Industry, must be obtained before licensed goods may be imported. Import regulations provide that imported goods must reach New Zealand during the period of licence validity which extends from 1st July to 30th June. In the case of goods shipped in a vessel calling on several New Zealand ports the relevant date is that of the first port visited.

Licences are issued in terms of a particular item code[1] and may be used to import only the goods specified. Three main types of provision exist:

(i) *Exempt Items*: An import licence is not required for the importation of goods under this category. At present approximately 75 percent by value of New Zealand's total private imports are exempt from import control. This category covers a wide field ranging from raw materials to finished consumer goods and machinery. It includes most primary products (the notable exception being wheat), raw materials and components of any type not made in New Zealand, for example base chemicals, fertilisers and heavy machinery. The importation of some exempt items such as citrus fruit is subject to control via monopoly selling arrangements which include requirements that fruit from certain sources such as Pacific Island nations be accorded preference.

(ii) *Basic Items*: Licences for these items are granted according to the percentage allocation indicated in the schedule. This means, for individual importers, that the basic allocation licence value for particular goods in the ensuing period will be determined either by the value of the licence issued to them in the preceding period or the amount they imported during that period. However, the provision of a basic allocation for goods does not preclude the granting of licences above the basic allocation or the granting of licences to importers who do not qualify because of past entitlements. There are a large number of 'basic' items with some of the more important goods covered by this category including tyres and tubes, paper products and periodicals.

(iii) *Special Licences*: Requests are considered individually in the light of current requirements and local production. This involves the exercise of discretion in individual cases.

(b) Recent Changes

The 1979 Budget announced three new import licensing policies. These were designed to enhance New Zealand's export competitiveness. They aim to encourage the transfer of resources into export activities and deal with instances where protection has allowed manifestly excessive costs to emerge in domestic raw material, components and capital equipment industries. These policies have since been implemented and are outlined below.[2]

(i) *The Export Production Assistance Scheme* aims specifically to facilitate export competitiveness. These licences allow the importation of raw materials and components not made in New Zealand, in cases where these are to be used for producing export goods. Licences of this type may also be issued when it can be shown that the use of raw materials or components of New Zealand origin would for reasons of price, quality or

(1) An item code is used to identify a product or group of products which may be imported under that particular number. The actual goods which may be imported under a particular licence item code are determined by the Customs Tariff of New Zealand 1974 as it applies with respect to the individual tariff items specified against each licence item code.

(2) More detailed information on these may be obtained from the Department of Trade and Industry.

technology prejudice export sales of the finished product concerned, provided a sufficient net foreign exchange benefit accrues to New Zealand.

(ii) *The Product Rationalisation Policy* aims to encourage the transfer of resources into export production. Licences will be issued for finished goods where a manufacturer seeks to rationalise his business by ceasing production of the goods concerned and diverting the released resources into export activities. It is necessary to establish in such instances that a net foreign exchange advantage will accrue. These licences are issued for one year at a time, although the Department of Trade and Industry is able to give assurances of continuity. This is subject to an annual review of the results of the rationalisation programme, including export achievements and evidence that the importing programme is not unduly harming other efficient manufacturers. If after two years none or very few of the promised benefits to New Zealand's export economy have occured then the company's import licence holding for production rationalisation may be discontinued.

(iii) *The Excessive Price/Quality Differentials Policy* aims to encourage cost containment within industry generally by providing improved access to price efficient overseas sources. Licences are issued when it can be established that the price of domestically manufactured raw materials, components, or plant and equipment is manifestly 'excessive' or that their technology or quality is 'significantly deficient'.

In addition the Government, in that same Budget, announced its intention to introduce a tendering scheme for some import licences. This scheme is the first move towards a more comprehensive restructuring of import licensing in New Zealand. Under this scheme licences additional to those available under the existing scheme are made available by tender. Each tenderer offers to pay a premium above the face value of the licence and the extra licences go to the highest bidder. Through allowing the price mechanism to work, a wider range of goods should be made available and areas of manufacture where imported goods can compete against domestic goods will be identified, even after the payment of the premium. The latter effect should encourage more competitive manufacturing in New Zealand, although the manufacturers affected will still enjoy greater protection than is afforded by tariff protection alone because of the premium paid on the licence.

An important aspect of this tendering scheme is that the successful tenders and all bids are published in the New Zealand Gazette. This provides the commercial community with additional information about the supply and demand of various imported commodities. It also indicates to what extent the present rate of duty could provide an effective level of import protection and identifies those areas where there is a greater or lesser degree of unsatisfied demand for goods.

From the Government's viewpoint the scheme will provide useful information on competitive strengths and weaknesses of industries. Overall, a tendering system has the distinct advantage that it allows import licences to be directed to those areas where the need is greatest. At the same time the licences are allocated without the undesirable effects that can result from administrative allocation while retaining the certainty of direct control. Another important benefit of tendering is that it redirects any monopoly profit associated with licences from importers to the Government.

IMPORT LICENSING AND THE G.A.T.T.

New Zealand was one of the original contracting parties to the General Agreement on Tariffs and Trade (G.A.T.T.) which aims, by way of multi-lateral negotiations, to reduce quantitative and tariff barriers to trade and provide a forum for the discussion and settlement of problems and disputes which arise in international trade. In practice the high ideals underlying the Agreement have not been realised although significant progress has been made in certain areas.

Article XI contains a general prohibition against the maintenance or introduction of import licensing. However, in this and subsequent Articles there are a number of exceptions to the general rule which permit restrictions to be maintained and in some cases extended. In some of these exceptions a distinction was made between restrictions affecting agricultural products and those affecting non-agricultural trade. In the latter case the only Article which can be invoked to justify new quantitative restrictions is the market disruption clause, Article XIX, which permits members to use temporary quotas in the presence of 'serious injury' or threatened injury to domestic producers. However in the case of agricultural commodities a number of other clauses can be invoked to justify restrictive practices.

It is in this bias against trade in agricultural products that New Zealand has found cause to consider that the GATT has proved ineffective in removing or reducing barriers to trade in the 'reciprocal and mutually advantageous' fashion that was envisaged when the Agreement was drawn up. While significant reductions have been achieved in the level of quantitative restrictions imposed on non-agricultural products the same cannot be said concerning restrictions on agricultural products. Indeed the reverse has been the case. It is in this context that there has been evident a growing reluctance on the part of agricultural exporting countries to agree to further concessions in non-agricultural trade without the promise of comparable concessions in agricultural trade.

NEW ZEALAND/AUSTRALIA TRADE

Since the mid 1960's the trading relationship between New Zealand and Australia has been built around the provisions of the New Zealand/Australia Free Trade Agreement (N.A.F.T.A.) which created a partial system of the free trade between the two countries. Details of this agreement, adjustments and effects upon trade between the two countries were discussed in an earlier article.[3]

The main thrust of NAFTA has been towards the reduction and removal of duties on specified ranges of products traded between New Zealand and Australia. For this reason less attention has been paid to the continuation of other restrictive practices by both countries.

This is not really surprising since one of the distinctive features of NAFTA has been the heavily qualified nature of the commitment made to the concept of free

(3) The Customs Tariff in New Zealand; Reserve Bank of New Zealand *Bulletin*, July 1980, p.223.

trade. There are safeguards permitting temporary suspension or even withdrawal of items entered in Schedule A (the schedule listing items to move automatically to an unrestricted free trade status). An escape clause allows either country to suspend its obligations, unilaterally if necessary in respect to any good which has been imported in quantities considered sufficient to cause serious injury to its producers. Each country is also permitted to maintain import licensing restrictions provided these also apply to third countries, and may impose such restrictions to meet balance of payments needs. However, it should be pointed out that neither country has used the safeguard provisions of the agreement to either suspend Schedule A obligations or withdraw goods from the Schedule. In addition, although not necessarily committed to remove import licensing on Schedule A goods, New Zealand has, in accordance with the aims of NAFTA, progressively opened up access for Australia on many Schedule A goods (bearing in mind that a significant proportion of Schedule A items are already exempt from licensing control).

As well as granting special Schedule A licences, to date about 175 items have been granted licence on demand status, that is, licences are issued against firm orders without limit, as part of this ongoing process. In practice, over recent years, neither country has re-imposed import controls on Schedule A goods. New Zealand has deliberately avoided re-imposing import controls against Australia where Schedule A items have been recontrolled, while Australia has not placed import restrictions against New Zealand where Schedule A items have been subject to global import controls.

The overall success or failure of an agreement such as NAFTA depends largely on the attitudes of the contracting parties. There has been progress in freeing up trade of selected products, but with 70 percent of trade now covered by Schedule A, additions to the Schedule have slowed down. This is because the remaining areas cover, in the main, manufacturing industry in which there is competing production on each side of the Tasman.

Recognition in both countries of the shortcomings in the present arrangements has resulted in moves to re-examine the whole New Zealand/Australia trading relationship. A series of discussions at official and ministerial levels have taken place over the last year in an effort to find a formula which can overcome the constraints which have increasingly been stifling further expansion and freeing up of trade under NAFTA.

ECONOMIC EFFECTS

The import licensing system is designed to regulate the total volume and composition of imports. As such, it does not operate to influence the demand for imports (other than in an indirect sense). Thus, if licensing is effective in reducing the supply of imports below the level of demand for imports, this excess monetary demand for imports will tend to spill over into either higher prices for the available volume of imports or increased re-directed demand for domestically produced goods and services (many of which will in turn have an import content of their own). In practice, some combination of these effects is likely to occur.

Because licensing forces at least some imports to become scarce, the excess of demand over supply will force up prices and add to inflation. As well, a narrower range of products will be available. The final consumer will incur these costs while the holders of the licences (the importers) will be beneficiaries in the form of higher profits, although some of the gain may accrue to the overseas supplier if he is able to raise his prices above what they may have been in the absence of licensing. If the licence holding importer is efficient however, and assuming the existence of alternative potential suppliers abroad, then it is most likely that the bulk of the 'monopoly profit' will accrue to the importer with a possible additional profit also for any other domestic distributors such as other wholesalers and retailers handling the licensed goods.

If the Government wishes to siphon off these 'excess' profits for the benefit of the taxpayer, then it may do this by auctioning or selling import licences. This procedure has only recently been contemplated in New Zealand despite its obvious appeal in equity terms. If a licensing system is operated, the cost is borne by consumers who therefore should at least be compensated by the gains in the form of monopoly profits accruing to the community as a whole via, say, an auction arrangement conducted by the Government (thereby achieving a revenue effect similar to that of tariffs).

Quantitative restrictions which succeed in holding the level of imports below market demand without pushing up prices of the imported goods (say by the simultaneous use of price control or the existence of some other market rigidity) will divert the excess demand to other non-licensed imports or to domestically produced goods and services. In other words, licensing may reduce the supply of imports but fails to eliminate the basic cause of the excess demand. The latter simply works its way into other channels. This is why licensing invariably fails to regulate balance of payments current account deficits — as New Zealand's lengthy experiments with import controls have amply demonstrated.

It is true that licensing protects domestic industry but it is uncertain whether this leads to higher employment, especially in the long run. The protective effect arises from the influences just discussed; licensing bars some imports, makes other imports more expensive than otherwise, and diverts demand from imports to domestic output. Each of these effects helps local producers.

The problem is that at the same time licensing reduces competition for domestic manufacturers and may indeed protect local establishments which are inefficient by international standards. If this process goes on for long enough — and in New Zealand it has been operating for over 40 years — the protected industries grow and flourish but at the cost to the community of higher domestic prices and an industrial structure which becomes increasingly uncompetitive by international standards. The community is effectively subsidising local producers who themselves often find difficulty in producing for export.

Moreover, these producers are invariably dependent, sometimes heavily so, on imported raw materials, components for local assembly, and capital equipment. These types of imports become a higher proportion of total imports while the relative significance of imports of finished goods declines. This is what happened in New Zealand over a number of years, to the extent that consumer goods are now only 23 percent of total imports compared with 39 percent 40 years ago. There are limits of course to how far such a process can go.

This process reduces the flexibility of the economy to respond to balance of payments fluctuations, a flexibility which is normally seen as important in a small

relatively open economy such as New Zealand which is still heavily dependent on exports of a narrow range of primary commodities (meat, wool, dairy, and forestry products accounted for 70 percent of total exports in the year ended June, 1980).

The reason adaptability to external changes is reduced is linked to the fact that when a widely protected and relatively large sector of the economy is producing predominantly for local consumption and is itself dependent on imports, this sector is not readily able to turn to export markets at the time of a domestic downturn (which may be internationally induced, such as by a terms of trade decline).

Furthermore, this sort of sector becomes an increasingly important employer of labour which means that any cuts in imports, say, in response to a balance of payments crisis, will lead to employment difficulties. The latter are likely to be less of a problem if there is adequate scope in the short term to reduce imports of finished goods rather than the raw materials and components on which local producers (and employers) are dependent. This scope is now very limited in New Zealand.

On economic grounds, the only convincing cases made out for protection are those associated with the infant industry argument and as a defence against dumping by other countries. The infant industry argument states that newly established local industries need protection from overseas competition for a period of time while they become established and grow to a sufficient scale; after which the protection afforded by import licensing can be reduced as the industries become internationally competitive.

It has been noted before, in the earlier *Bulletin* article on the customs tariffs, that the infant industry justification for protecting domestic industries can be criticised on several counts. Once in place the protective device is often very difficult to remove without creating disruption to the protected industries. The ability of planners to pre-select accurately those industries that will eventually be able to withstand international competition is far from perfect. The protective device, while in place, induces distortions in the economy which may seriously undermine more efficient sectors. In particular, existing exporters may suffer from the higher cost structure induced by import controls. The longer licensing continues, the less will be the incentive for the protected producers of import substitutes to seek the cheapest and most efficient methods of production.

The anti-dumping argument is equally subject to criticism. Any foreign exporter can only continue to export indefinitely at excessively low prices if the rest of his markets or economy subsidises the activity. It is then to the importing country's benefit to allow the dumped goods in since they are the recipient of the subsidy. On the other hand if it appears to be only a short-term phenomenon aimed at causing the collapse of an otherwise viable domestic industry then the appropriate response is probably to establish specific restrictions excluding only the products of the offending company or country.

On the face of it, import controls appear to promote local industry and employment by protecting these activities. In turn, it is sometimes argued that these import substitution effects are helpful to the balance of payments. But over the longer run, as has been suggested above, excessive protection simply props up internationally uncompetitive activities, skewing the structure of the economy away from necessarily efficient foreign exchange generating activities and towards high cost, home based industries. This process eventually alters the composition of imports, employment and domestic output in such a way as to make the economy less flexible in the face of international fluctuations and, in a sense, more foreign exchange dependent. The events of the decade of the 1970's — high oil prices, slower economic growth rates in our trading partners, lower terms of trade for New Zealand — have illustrated the difficulties of adapting the structure of the New Zealand economy in the face of a well entrenched, heavily protected manufacturing sector, large segments of which are unable to compete successfully either on overseas markets or against imports in the domestic market.

Import licensing then, far from solving the country's overseas deficit problems, has encouraged the growth of uncompetitive industries and is now seen by many economists to have been a major contributor to the lack of adaptability of the economy to the problems of the past decade or two. The essence of the matter is that quantitative restrictions on imports promote the misallocation of resources.

The controls are also difficult to administer. How do Government officials decide which industries and activities should get import licences, who should get them, how much should be allocated, and so on? Once a licence has been issued to a particular importer, he is likely to be in a favoured position in succeeding years — the system inevitably has a strong administrative historical bias. Arbitrary decisions can not be avoided when there are no market signals to guide the bureaucrats. The risk of corruption requires vigilance on the part of the authorities: licences are valuable yet are usually handed out 'free' to importers. It should not be surprising if at times there is over-enthusiastic non-price competition for licences.

From the private sector's point of view, licensing is also administratively inefficient because of the uncertainties it may create for firms — will they get licences or will they not? — and the need to devote significant administrative resources to seeking and justifying licence allocations. Beyond this, there are the additional lags introduced into the process, to say nothing of the frustrations which such a system may engender. Once licences have been obtained, there may be a reduced incentive to be as efficient as otherwise, given the backing of the monopoly profit element referred to earlier.

In summary, an import licensing system has the following economic effects:

- It adds to inflation; directly by adding to the price of the licensed goods; and indirectly by protecting and encouraging the development of high cost local industries.
- It fails to resolve balance of payments problems because although it may initially appear to reduce the supply of some imports, licensing does little to dampen the demand side of the market. The excess demand will spill over into non-licensed imports or domestic output which itself is likely to be import dependent. In any case, there is a reluctance to use licensing vigorously to reduce an overseas deficit because of the unemployment consequences of such action, consequences which manufacturers can directly and publically attribute to the import controls.

- Import licensing redistributes income by making imports and locally produced goods more expensive for consumers, who thereby lose; by facilitating the earning of 'excess' or 'monopoly' profits by the holders of import licences; and by encouraging and propping up inefficient, high cost domestic activities which are in effect subsidised by consumers and the rest of the community.
- It thus encourages an inappropriate industrial structure for the economy and although in the short run employment may be higher than in the absence of licensing, in the long run employment is threatened by being concentrated in import-dependent, internationally uncompetitive activities; by the resultant lack of flexibility of the economy to respond to overseas fluctuations in economic activity; and by the eventual need for the economy to adjust to these problems i.e. for some restructuring to take place, possibly on a substantial scale (as now appears to be the need in New Zealand).
- Licensing is also administratively cumbersome and arbitrary, involving an historical bias and requiring fine judgments by officials who, through no fault of their own, may not be well placed to ensure that their assessments and decisions are superior to those which would be made by a more market based system.
- The quantitative effects of licensing on real income are uncertain, but conventional economic analysis suggests that direct controls of this sort are a net cost to the community, but one which unfortunately may only become apparent with the passage of time. Because of this, an economy may tend to get locked into a licensing system because so many sectors of the community are, or see themselves as, dependent on protection. On the other hand, the cost of the subsidy to the wider community may be diffuse and less amenable to ready understanding or popular rationalisation.

In any case, most parties would agree that any move away from licensing towards, say, a system based on tariffs should be part of a wider package of moves to rationalise the industrial structure and should allow adequate time for adjustment to avoid excessive short term transitional costs such as in the form of factory closures and unemployment. Indeed the short term costs may be seen as so substantial as to militate against rapid or meaningful progress in easing the protective mechanisms which prop up inefficient but nevertheless currently operating enterprises. The long term gains advocated by economists may simply seem to be too far off.

If this view prevails, the problems analysed above will of course accumulate and get even worse, so that sustainable economic growth, led by an expansion of exports to ease the foreign exchange constraint, will become even more difficult to achieve.

Change is costly and takes time, but in the final analysis it may be unavoidable. This is the case in favour of action sooner rather than later to ease New Zealand away from import controls; and the case for pressing on with the industry studies programme. And when, under the studies, transitional costs are identified which appear to be beyond the capacity of the industry concerned to absorb, assistance can be planned so that the desired restructuring need not be jeopardised by the costs of making the changes.

A switch from licensing to tariffs is generally favoured on the grounds that the latter is a more efficient (or less inefficient) protective mechanism. Tariffs push up the prices of imports, thereby protecting local manufacturers, but do not cut off the supply of imports in as arbitrary a manner as direct controls. The market mechanism has a more important role to fill under tariffs, thereby allowing the community to express their preferences more clearly. In addition, tariffs yield revenue for Government (rather than monopoly profits for licence holders), can be adjusted in relative terms and can be phased out gradually over time, whereas licensing tends to be absolute in its impact. It involves specific decisions on quantities regardless of price; tariffs influence prices, but then allow quantities to adjust freely. All in all, tariffs are generally seen as a preferable instrument to licensing on economic grounds.

Beyond this, it could be argued that an appropriate exchange rate is to be preferred to either tariffs or licensing, but if it is accepted that some form of protection will normally be used then tariffs have advantages over direct controls.

CONCLUSION

Import licensing is a method of direct control over the quantity and composition of imports which has been used in New Zealand for many years. As with all such direct intervention mechanisms, it suffers from the serious disadvantage that it may appear to reduce the supply of imports but does not resolve the fundamental problem which led to an excess demand for imports, which is an excess of aggregate domestic monetary demand over the total supply of goods and services. So long as such an excess monetary demand exists, balance of payments deficits will persist and inflation generally will be facilitated. Thus an external deficit problem must be handled by a combination of exchange rate policy and monetary and fiscal policies.

Licensing protects domestic industry and thus appears to promote employment. But, in the longer run, import controls may be counter productive in the sense that they protect inefficient high cost industries, bias production away from internationally tradeable goods, reduce the responsiveness of the economy to fluctuations originating abroad, and make employment and output more import dependent. Thus the longer run effect of licensing may be to worsen the foreign exchange constraint and inhibit sustainable economic growth on which employment depends. Protection objectives can be handled more efficiently by tariffs, which are also more readily amenable to phased reductions over time, thus assisting the longer term efficiency and international competitiveness of a country's industrial structure.