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STATEMENT OF

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BEFORE THE

SUBCOMMITTEE ON DEPARTMENT OPERATIONS,
RESEARCH, AND FOREIGN AGRICULTURE
HOUSE COMMITTEE ON AGRICULTURE

ON

THE AGRICULTURAL EXPORT ENHANCEMENT PROGRAM

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Mr. Chairman and Members of the Subcommittee:

We are pleased to be here today to discuss with you our ongoing work on the agricultural Export Enhancement Program which was announced in May of this year. Our work is being conducted at your request as well as the requests of Senator Grassley, Chairman of the Senate Judiciary Subcommittee on Administrative Practice and Procedure, and Senator Harkin, a member of the Senate Committee on Agriculture, Nutrition, and Forestry.

As you know, our work on agricultural export subsidies goes back to the early 1970s, when we issued a series of reports on the Department of Agriculture's management of the Wheat Export Subsidy Program. Those reports identified several weaknesses and abuses in the subsidy program, especially the payment of excessive subsidies to U.S. exporters. The attachment to this statement lists a number of our reports related to agricultural trade.

The declining competitiveness of the United States in the world agricultural market and decreasing U.S. agricultural exports characterize the environment in which the current Export Enhancement Program was established. U.S. agricultural exports have declined substantially from the 1981 record level of 162 million tons valued at $44 billion. At the time the Export Enhancement Program was announced, the U.S. government projected that 1985 exports would fall to 137 million tons valued at $33.5 billion. In 1980 the United States supplied nearly 60 percent of the world's grain import needs whereas in 1985 it was projected the United States would supply less than 45 percent.

DESCRIPTION OF THE EXPORT ENHANCEMENT PROGRAM

The establishment of the Export Enhancement Program grew out of discussions between the former Director of the Office of Management and Budget and the Senate leadership in May of this year. As a result of the discussions, the Secretary of Agriculture announced on May 15 that up to $2 billion worth of surplus agricultural commodities owned by the Commodity Credit Corporation (CCC) would be made available over a 3-year period as a bonus to U.S. exporters to expand sales of specified U.S. agricultural commodities in targeted markets. In practice, this bonus is a subsidy-in-kind which enables exporters to lower the price of their commodities to be competitive with subsidized foreign agricultural exports.

The objectives of the program are to increase U.S. farm product exports and to encourage trading partners to begin serious negotiations on agricultural trade problems.

According to guidelines established by the interagency Economic Policy Council, each initiative under the program (i.e., announcement of commodity and market to be targeted) is to meet the following criteria: (1) additionality, i.e., sales are to increase U.S. agricultural exports above those that would have occurred in the absence of the program, (2) targeting, i.e., sales are to be targeted at market opportunities to displace competitors who are subsidizing their exports, (3) cost effectiveness, i.e., sales are to result in a net plus to the overall economy, (4) budget neutrality, i.e., sales are not to increase budget outlays above those that would have accrued in the absence of the program.

As of October 1, the CCC had issued announcements containing the terms and conditions of six initiatives targeting wheat or wheat flour, one for Algeria, two for Egypt, two for the Yemen Arab Republic, and one for Morocco. The initiatives represent total potential sales of 3.1 million metric tons of wheat and 650 thousand metric tons of wheat flour. To date only the two initiatives for Egypt have resulted in sales--500 thousand metric tons of wheat and 175 thousand metric tons of wheat flour valued at about $87 million, which includes about $23 million in bonus commodities. The announcements contained information concerning the operating procedures of the program, which may vary from initiative to initiative. Under each procedure, however, interested exporters must first qualify by meeting a variety of requirements, including evidence of experience in exporting agricultural commodities.

GAO OBSERVATIONS

Our observations are an interim assessment based on our work to date, which has included a review of pertinent documents and interviews with officials of the Departments of Agriculture and State, the Office of the U.S. Trade Representative, the Office of Management and Budget, U.S. grain exporters, and trade associations.

Based on our preliminary work, we have the following observations about whether the program can achieve its goals and objectives and about the management of the program.

--The six initiatives under the Export Enhancement Program announced to date target four countries and two related commodities--wheat and wheat flour. Potential future activity is limited by current criteria. The targeting aspect of the program is perhaps the primary cause for limiting the amount of activity. According to the targeting criterion, the subjects of the initiatives are to be competitors who are subsidizing their exports. To date, all the initiatives have been directed against the European Community. However, not all markets where subsidizing competitors sell are likely to be targeted. This is because of the additional concern that competitors who do not subsidize their exports not be hurt by the program. This limits the number of potential markets. Furthermore, the probability of targeting the Soviet Union, which purchased approximately one third of the European Community's wheat exports last year, is remote because of foreign policy considerations. This is a market in which the Community essentially did not participate in 1980.

--The targeting aspect of the program could cause traditional U.S. commercial customers to view the program as discriminatory. Long-standing commercial customers for U.S. agricultural exports who are not given the opportunity to buy discounted commodities may react negatively and seek other sources of supply. Given the world surplus in major agricultural commodities, other suppliers are readily available.

--The program initiatives announced thus far have involved only wheat and wheat flour. Although in principle the program includes all agricultural commodities, even those not contained in CCC stocks, the potential for using the program for other commodities appears limited. According to recent government assessments, there will be little opportunity for broader use of the program under current targeting criteria. Furthermore, there are complexities associated with targeting a non-CCC commodity and providing a bonus with commodities that are in CCC stocks.

--According to Agriculture, additionality under the program is forecast to be limited due to the fungibility of grain and other agricultural commodities and to the likelihood that a large percentage of European Community exports displaced by the program will be diverted to other markets, at the expense of both non-subsidizing competitor and U.S. commercial exports. Agriculture estimates a net 33 percent additionality for the major initiatives announced thus far; that is, actual net exports that would not have been made without the program are estimated at one third of the sales made under the program. The relatively low estimate of additionality means that the effective subsidy under the program is very high. If it takes the equivalent of $200 million in CCC stocks to support a $1 billion sale, and actual additional sales are only about $330 million, then the subsidy element for the net increase in exports is about 60 percent. Hence, if the Agriculture Department's estimate of additionality is correct, most additional sales under the program will consist of CCC bonus commodities, so the direct impacts on commercial markets and farm incomes are likely to be slight.

--Additionality of exports in targeted markets may be short-lived, as reflected by the 1983 subsidized wheat flour sale to Egypt. In this case, when the subsidy lapsed, the market share that had been captured as a result of the subsidy reverted to European Community suppliers.

--In the past, the United States has had some success in using offsetting export subsidies to encourage agreements that restrict these practices, at least in the area of concessionary export financing. Therefore, there is a basis to expect that, in the agricultural sector, counter-subsidies may be of some use in bringing subsidizing competitors to the negotiating table. However, the existing surplus stocks and the fungibility of agricultural commodities mean that subsidized exports squeezed out of one country's market by the program can be diverted to other markets. Foreign actions to offset U.S. export subsidies or to find new markets will raise the cost of competitor export subsidies. We do not know how much their costs will increase, but given the limited scope of the program we question whether these increased costs will be sufficient to bring about the desired negotiations.

--Agriculture views the program as a commercial one not subject to cargo preference law. However, a recent district court decision contained language indicating that cargo preference requirements would not be limited to foreign aid cargoes but would also apply to other types of surplus commodities procured through a federal government program. If this broad reading of the cargo preference provisions is upheld on appeal, the Export Enhancement Program could be affected. However, even under the narrower view, the program could be challenged as a "concessional" program subject to cargo preference requirements if the subsidies provided are deemed to result in concessionary prices. Resolution of this issue is important since cargo preference requirements would increase program costs and undermine its objectives.

--The Export Enhancement Program Advisory Committee consists of eight members who were recommended to be on the Committee by various trade associations. Its first meeting was not open to the public because the Secretary of Agriculture determined that information discussed would be market sensitive. Given the fact that potential program beneficiaries participate in these meetings, closed sessions create the appearance of potential conflict of interest.

In the final analysis, the Export Enhancement Program represents a limited response to the declining competitiveness of the United States in the world agricultural market. Our preliminary review indicates that the likelihood of significantly increasing U.S. agricultural exports or encouraging a reduction in foreign export subsidies is minimal.

Mr. Chairman, this concludes my statement. I would be happy to respond to any questions you may have at this time.

ATTACHMENT

GAO REPORTS ON AGRICULTURAL TRADE

July 9, 1973, "Russian Wheat Sales and Weaknesses in Agriculture's Management of Wheat Export Subsidy Program," B-176943

February 12, 1974, "Exporters' Profits on Sales of U.S. Wheat to Russia," B-176943

April 29, 1974, "U.S. Actions Needed to Cope with Commodity Shortages," B-114824

April 11, 1975, "The Agricultural Attache Role Overseas: What He Does and How He Can be More Effective for the United States," B-133160

February 12, 1976, "Assessment of the National Grain Inspection Systems," RED-76-71

March 3, 1976, "Agriculture's Implementation of GAO's Wheat Export Subsidy Recommendations and Related Matters," ID-76-39

May 28, 1976, "Grain Marketing Systems in Argentina, Australia, Canada, and the European Community; Soybean Marketing System in Brazil," ID-76-61

May 2, 1977, "Issues Surrounding the Management of Agricultural Exports," Vol. I and II, ID-76-87

October 26, 1979, "Stronger Emphasis on Market Development Needed in Agriculture's Export Credit Sales Program," ID-80-01

July 27, 1981, "Lessons To Be Learned From Offsetting the Impact of the Soviet Grain Sales Suspension," CED-81-110

June 15, 1982, "Market Structure and Pricing Efficiency of U.S. Grain Export System," GAO/CED-82-61; and Supplement, "An Economic Analysis of the Pricing Efficiency and Market Organization of the U.S. Grain Export System," GAO/CED-82-61S

April 9, 1985, "Controls Over Export Reporting and Futures Trading Help Ensure Fairness, Integrity, and Pricing Efficiency in the U.S. Grain Marketing System," GAO/RCED-85-20

June 18, 1985, "Transportation of Public Law 480 Commodities--Efforts Needed to Eliminate Unnecessary Costs," GAO/NSIAD-85-74

September 13, 1985, "Compendium of GAO Reports Pertaining to Public Law 480 from July 1973 through August 1985," GAO/NSIAD-85-96

September 23, 1985, "Current Issues in U.S. Participation in the Multilateral Trading System," Chapter 2, "GATT Discipline Weak for Agricultural Trade," GAO/NSIAD-85-118

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