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Market Promotion Program Could Be More Effective

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U.S. DEPARTMENT OF AGRICULTURE:
MARKET PROMOTION PROGRAM COULD BE MORE EFFECTIVE

SUMMARY STATEMENT BY ALLAN I. MENDELOWITZ, DIRECTOR
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The Market Promotion Program (MPP) was created to encourage exports of U.S. agricultural products. In fiscal years 1986-93, over $1.25 billion was authorized for MPP and its predecessor, the Targeted Export Assistance program. MPP operates through not-for-profit associations that either run market promotion programs themselves or pass the funds along to commercial firms to promote their own brand-name products. About 60 percent of MPP funds go to generic promotions; the balance supports brand-name promotions.

The Foreign Agricultural Service (FAS), which administers MPP, has taken steps to focus and tighten requirements for program funding. Nevertheless, we believe that additional changes need to be made in the program to address the following problem areas:

- FAS has not designed the program to ensure that MPP funds increase the overseas promotional activities of commercial firms participating in the program rather than simply replacing funds that would have been spent anyway.

- FAS lacks criteria regarding the length of time commercial firms can remain in the program or the circumstances under which these firms should assume the sole responsibility for their export promotion activities.

- FAS has not identified the circumstance under which foreign firms can participate in the program, nor established objectives for including small, medium-sized, and new-to-export firms in the program.

- FAS relies on unverified data regarding the U.S. content and processing of products in allocating MPP funds.

FAS is required to evaluate the effectiveness of MPP. In the past, FAS has attempted to do so by linking MPP-funded promotional efforts to increased exports. However, to fully evaluate the program FAS must also be able to show that successful market promotion efforts would not have been undertaken without MPP funding.

Lastly, FAS officials told us they see a conflict between MPP's primary objective--to increase exports--and the Appropriation Committee's 1993 direction regarding the types of firms and products to be served by MPP. Congress may wish to clarify its intent by amending the MPP's authorizing legislation.

Mr. Chairman and Members of the Subcommittee:

I am pleased to be here today to discuss the Department of Agriculture's Market Promotion Program (MPP). During fiscal years 1986-93, over $1.25 billion has been authorized for MPP and its predecessor, the Targeted Export Assistance (TEA) program. My testimony will address the historical development of the program and its management and operations. I will also highlight several important program-related issues that we believe need to be addressed by Congress and the Department of Agriculture to improve the program.

BACKGROUND

In 1985, to reverse the decline in U.S. agricultural exports and to counter the negative effects on U.S. exports of unfair foreign trade practices, the Food Security Act (P.L. 99-198) authorized the TEA program. The TEA program provided funds to support market development activities for commodities adversely affected by unfair foreign trade practices.

In 1990, the TEA program was replaced by MPP, which was authorized by the Food, Agriculture, Conservation, and Trade Act of 1990 (P.L. 101-624). MPP is administered by the Department of Agriculture's Foreign Agricultural Service (FAS). MPP helps finance overseas promotional activities for U.S. agricultural products. MPP, like its predecessor, was created to develop, maintain, and expand U.S. agricultural exports. Unlike the TEA program, however, MPP gives priority to, but does not limit participation to, commodities adversely affected by unfair foreign trade practices.

MPP provides funding primarily for consumer-related promotions of high-value[1] generic and brand-name products. Generic activities involve the efforts of not-for-profit organizations to increase the total market for their commodities with no emphasis on a particular brand. Brand-name activities help commercial firms establish consumer loyalty to a particular brand. About 60 percent of all program activities now support generic promotions, with the remaining 40 percent funding brand-name promotions.

MPP operates through not-for-profit organizations that either run market promotion programs themselves or pass the funds along to commercial firms to spend on their own market promotion efforts. From fiscal year 1986 through fiscal year 1992, 64 not-for-profit organizations have participated in the program. It is the not-for-

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[1]High-value agricultural products are generally classified into three groups: semi-processed products (e.g., flour, oilseed meal, and animal fats); highly processed consumer-oriented products (e.g., processed meats and dairy products); and high-value unprocessed consumer-oriented products (e.g., fresh fruit, eggs, and nuts).

profit organizations, operating under interim program regulations, that determine which firms receive funds and how much they receive.

MPP now operates on a cost-sharing basis with its participants. Under the current MPP interim regulations, participants must contribute a minimum of 5-percent of their own resources for generic promotions; previously, they were encouraged, but not required, to contribute. For brand-name activities, commercial firms are generally reimbursed not more than 50 percent of their eligible expenses.[2]

FAS had a three-stage application approval process for the 1992 and 1993 program. In the first stage, a committee of senior marketing specialists reviewed each application to determine compliance with the requirements specified in the interim regulations. In the second stage, the commodity divisions analyzed the content of each proposal and prepared recommendations for the allocation level, required cost-share level, and ceiling levels by country and generic versus branded activities. The commodity divisions used criteria specified in MPP interim regulations to arrive at their funding allocation recommendations. In the final stage, a committee chaired by the FAS Assistant Administrator for Commodity and Marketing Programs made adjustments to the divisions' funding recommendations, because the total recommended funding allocations exceeded the funds available.

For the fiscal year 1992 funding allocation process, the committee used five factors to make the final allocations, according to FAS: (1) the presence of an unfair foreign trade practice; (2) the proposed contribution (cost-share) level; (3) the proposed budget size in relation to exports; (4) the proposed budget size in relation to the expected change in exports; and (5) the 1991 export performance in relation to 1991 goals and/or forecasts. The allocation factors enter into the decision-making process in a weighted formula. For the fiscal year 1993 funding process, the committee included two additional allocation factors--U.S. content and processing--in response to language contained in the fiscal year 1993 Agriculture Appropriations Committee's conference report (H.R. Rep. No. 102-815, Aug. 7, 1992).

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[2]Commercial firms could receive more than 50-percent reimbursement if (1) the commodity being promoted had a favorable decision by the U.S. Trade Representative under Section 301 of the 1974 Trade Act and if the U.S. Trade Representative has not terminated action taken as result of such favorable decision; and (2) the commercial entity was reimbursed at more than 50 percent for eligible expenses under the TEA program during fiscal year 1990, with the reimbursement rate being phased down, beginning with fiscal year 1991, to a level of 50 percent by fiscal year 1995.

MPP PROGRAM CRITERIA DO NOT ADDRESS IMPORTANT FACTORS

FAS uses a number of factors to allocate MPP funds among the various eligible applicants. However, we believe that the current funding process for MPP does not address a number of important factors. Specifically, FAS has no assurance that MPP funds are used to increase the overseas promotional activities of commercial firms participating in the program rather than simply replacing funds that would have been spent anyway. In addition, there are no criteria addressing the graduation from MPP of commercial firms in the program. FAS also has not addressed the issues of the participation of foreign versus domestic firms and large versus small firms. Lastly, FAS has only limited information regarding the U.S. content and processing of products promoted with MPP funds, one of the criteria used in the funding decision.

No Assurances That MPP Funds Increase Promotional Activity

FAS does not require commercial firms to demonstrate that MPP funds will be used to increase promotional activities. The lack of such a requirement affords firms the opportunity to substitute MPP funds for promotional expenditures they would possibly have otherwise undertaken with their own funds. FAS currently has no way of knowing the extent to which this practice may be occurring. We believe that the participation of firms in the program with significant prior export experience and with multi-million dollar advertising budgets suggests that greater controls over program participation are needed.

Other government incentive programs restrict the provision of government assistance to covering those expenses that are greater than previous expenditure levels. For example, the research and development tax credit provides a 20-percent tax credit for certain expenditures, but only to the extent that current-year expenditures exceed the average annual amount of such expenditures in the specified base-period. The base-period for the credit is generally the average amount of the prior 3 years' expenditures. No such criterion exists for MPP.

While FAS does not collect sufficient information to determine whether funding substitution is occurring, there is some evidence that suggests it may be occurring. For example, we reviewed the files for 16 firms funded by one of the not-for-profit organizations we visited. Of the 16 firms, 15 requested MPP funds for markets in which they were already promoting their brand-name products. In one case, a firm with 14 years of export experience requested MPP funds for a total of 31 markets. In five of the markets, the firm had at least 10 years of promotional experience with the brand-name product prior to participation in MPP.

We also found that MPP funds make up a relatively insignificant portion of the advertising budgets of some firms in the program, thus raising a question as to whether MPP program funds are substantial enough to cause firms to undertake promotional activity in addition to that which they had already planned. For example, we found that 13 of the 200 largest advertisers listed in the 1992 Standard Directory of Advertisers received MPP funds during 1992. The 13 firms received a total of $9 million in MPP funds. The advertising budgets for each of the 13 firms ranged from $45 million to $538 million. On average, the MPP funds represented less than 1 percent of their advertising budgets for 1992.

MPP Lacks a Program Graduation Requirement

FAS has no restrictions on the length of time that commercial firms can continue to receive MPP funds. FAS believes that market promotion is a long-term effort and opposes eliminating funding to firms showing success in meeting FAS-approved export goals. This view is counter to congressional concerns that certain restrictions are necessary.

The Congress has previously questioned whether MPP recipients need continued long-term funding. The Food, Agriculture, Conservation, and Trade Act of 1990 directed FAS to evaluate each MPP recipient to determine whether continued program assistance was necessary for market maintenance. However, FAS has not developed specific criteria to make the required evaluations.

A relatively small number of firms (17) have received TEA/MPP funds for 7 straight years--since the programs' inception. Many more (136) have participated in the program for 5 or more years. During the 5- to 7-year period, these firms received the bulk of the brand-name program funds. While these firms represented approximately 11 percent of the total number of participating firms, they received about 66 percent of the funds allocated for brand-name promotions during fiscal years 1986-92. Appendix I shows the number of years firms participated in the MPP/TEA brand-name program.

No Criteria on Foreign Firm Participation

Concerns about foreign firm participation in MPP were expressed by Members of Congress during the 1992 legislative session. They were concerned about the possibility of MPP subsidizing a foreign firm in a market in which a U.S. corporation was trying to compete without MPP support. FAS officials acknowledged this possibility but made no changes to the program to address this concern.

The conference report accompanying the 1993 agriculture appropriation directed that MPP "funds should be allotted to U.S.-based participants which export agricultural products." However, FAS has continued to allocate funds to eight not-for-profit organizations that support foreign-based firms. FAS officials stated they believed that the report language did not exclude foreign firms from the program. FAS officials added that increased emphasis on U.S. content and processing contributed to meeting the conference report's objective of encouraging more U.S.-based participation.

The brand-name program is administered by the not-for-profit organizations, which in turn may choose to allow foreign firms to be beneficiaries under the program.[3] FAS requires only that the participating organization's criteria for distributing program funds among brand-name participants be objective and reasonably related to its worldwide promotional goals.

In the early part of 1992, FAS asked not-for-profit organizations to provide information on the domestic and foreign ownership of commercial firms funded under MPP. Information they provided showed that at least $78 million[4] of MPP funds from fiscal year 1986 through fiscal year 1992 went to foreign firms not based in the United States. This amount represented nearly 20 percent of the total funds allocated for brand-name promotions during the 7-year period. Appendix II shows the distribution of funds to foreign and domestic firms for promoting brand-name products.

Some not-for-profit organizations fund foreign firms exclusively, while others fund few, if any, foreign firms. Of the 64 not-for-profit organizations active in the MPP brand-name program during fiscal years 1986-92, only nine provided funds to foreign corporations. These nine promoted products containing U.S. cotton, raisins, peanuts, soybeans, rice, honey, seafood, sunflower seeds, or walnuts.

According to representatives of FAS and not-for-profit participant organizations, providing MPP funds to foreign firms is consistent with the program's goals and objectives. They stated that the primary goal of MPP is to increase U.S. agricultural exports. They said that the use of foreign firms increases export demand for U.S agricultural products, since products marketed by foreign firms with MPP funds are made with U.S. commodities. They explained that foreign firms are sometimes better situated to promote and export U.S. agricultural products in certain foreign markets because they have greater name recognition, superior distribution networks, and

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[3]The only exceptions are commercial entities that participate in MPP's Export Inceptive Program (MPP/EIP). FAS directly provides these firms with funds for branded promotions. According to MPP regulations, all of the firms participating in MPP/EIP must be U.S. commercial entities.

[4]The $78 million does not include funds provided to U.S. subsidiaries of foreign corporations.

more knowledge of the foreign market than domestic companies. In addition, a not-for-profit organization's representative said that foreign firm participation can be particularly useful in cases where U.S. access to a foreign market is restricted.

While the goal of MPP is to benefit U.S. farmers, the program can also benefit other enterprises. By funding foreign firms, we believe that MPP may make it more difficult for U.S. firms to compete and obtain a foothold in foreign markets. The funding of foreign companies may produce short-term gains in the exporting of U.S. agricultural commodities, but those gains may come at the expense of U.S. firms trying to compete in those foreign markets.

Participation Levels of Small Firms Not Known

In an attempt to focus program funding, the conference report accompanying the fiscal year 1993 agriculture appropriation bill recommended that FAS change the program to encourage the participation of small-, medium-sized, and new-to-export firms. However, FAS does not collect information on the size of firms participating in the program. Therefore, it does not have the information needed to assess whether fiscal year 1993 funding increased for small-, medium-sized, and new-to-export firms.

To evaluate current representation, FAS is surveying firms participating in the program to obtain information on, among other things, the size of firms currently receiving MPP funding. FAS plans to use the information obtained as the basis for its recommendations on MPP eligibility requirements.

Because FAS does not collect information on the size of firms receiving MPP funds, we used various business directories to obtain information on the size characteristics of the top 50 firms funded during fiscal year 1992. Collectively, the top 50 firms received nearly 64 percent, or $48.5 million, of the $76.4 million allocated to brand-name promotions that year.

We found 11 firms that appear to meet the Small Business Administration's (SBA) size standards for small businesses.[5] The 11 firms received a total of $8.5 million, or 17.6 percent, of MPP funding for the top 50 firms during fiscal year 1992. Our analysis did not include the other 556 firms receiving MPP funding for brand-name promotions during fiscal year 1992 nor whether the firms were new-to-export, this information was not readily available. The overall MPP participation rate of small businesses is probably

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[5]SBA established standards by industry using Standard Industrial Classification codes to define companies that meet its criteria for federal assistance for small firms. The size standards are specified either as the maximum number of employees or annual receipts for a business to be considered small.

higher than observed in the top 50 firms because smaller firms are generally less likely to be the recipients of the largest MPP allocations.

FAS and representatives of not-for-profit organizations were concerned that the emphasis on smaller and new-to-export firms would exclude larger companies from the program. They explained that larger companies with significant export experience can often use program funds more efficiently and effectively than smaller or new-to-export firms. As a result, they felt the participation of larger firms benefits U.S. agricultural producers more significantly because they could export a larger volume of agricultural products or commodities than smaller firms. Furthermore, they noted that the participation of large firms also benefits smaller firms. For example, they pointed to the activities of a large winery participating in the program. According to FAS officials, this winery purchases much of its grapes from hundreds of smaller grape growers. Accordingly, this large winery's success in increasing its exports also benefits smaller growers.

In our opinion, whether a firm should receive government funding for export promotion should depend on both the ability to effectively use the funds as well as the demonstrated need for the funds. While large firms may more effectively use MPP funds to increase exports of U.S. agricultural products, the resources available to such firms may indicate they have no demonstrable need for government assistance. Such firms generally have the capability to fund their own foreign market development programs. Smaller firms typically have a greater need for government assistance because of their more limited infrastructure for marketing overseas.

Limited Assurance MPP Promotes Predominantly U.S. Grown And Processed Products

The 1993 Appropriations Committee's 1993 conference report directed FAS to ensure that MPP promotes agricultural products that are predominantly U.S. grown and manufactured. While FAS developed criteria for using content in funding MPP recipients a year earlier and modified the criteria to meet this direction, we believe it has little assurance that firms are actually meeting their content claims. FAS also included U.S. processing as one of the factors considered during the fiscal year 1993 funding process. However, FAS did not obtain information on U.S. processing and had to make assumptions regarding the extent of U.S. processing.

In response to the conference report, FAS changed its funding allocation process for fiscal year 1993. FAS added a factor that lowered the score for not-for-profit organizations that represented products containing less than 100-percent U.S. content. FAS also for the first time recognized U.S. processing in the allocation process.

This change in the allocation process was significant because program applicants requested $349.2 million from MPP, which had an appropriation of $147.7 million. After reviewing applications for compliance with program regulations, FAS used seven factors to allocate funds to MPP applicants. The seven factors were: (1) the presence of an unfair foreign trade practice, (2) the proposed level of the applicant's commitment of its funds, (3) the proposed budget in relation to exports and expected change in exports, (4) the applicant's 1992 export performance, (5) the applicant's expected change in market share, (6) the degree of U.S. content, and (7) the extent of U.S. processing.

U.S. content

MPP regulations issued in August 1991 do not restrict program participation to products that have 100-percent U.S. content. Regulations permit full funding for products that have at least 50-percent U.S. content by weight (exclusive of added water). Products that have less than 50-percent U.S. content are eligible for proportionally less funding.

In fiscal year 1992, practically all not-for-profit organizations stated that the brand-name products they funded had at least 50-percent U.S. content. Of the 59 MPP applicants, 37 said that the U.S. content was 100 percent; 7 stated that the U.S. content was at least 50 percent; 5 stated that the U.S. content ranged somewhere between 50 and 100 percent; and 1 stated that the U.S. content ranged from 14 to 100 percent. There were nine applicants who did not state the U.S. content of their products, however, based upon the nature of their products they appeared to us to contain predominantly U.S. content. For example, one such application was for the generic promotion of apples grown in western New York State.

While FAS has established a funding allocation process that includes consideration of the level of U.S. content and processing, the information it used in its funding decisions was based on unverified data. FAS officials told us that they did not verify U.S. content of brand-name products before 1993. Instead, they relied on statements made in MPP applications. Starting in 1993, FAS' Compliance Review Staff began to review the support for the certifications made regarding U.S. content during their audits of participants.

FAS Compliance Review Staff typically limit their work to the not-for-profit organizations and do not as a rule audit the commercial entities performing brand-name promotions. We believe this situation severely limits the ability of the Compliance Review

Staff to assess the accuracy of statements regarding the U.S. content of brand-name products promoted with MPP funds.

Not-for-profit organizations similarly relied on unverified statements on U.S. content. Representatives of the not-for-profit organizations we contacted explained that they only reviewed the U.S. content of a product on an "exception" basis. For example, some commercial firms will request assistance from the not-for-profit organizations to determine if their product meets the minimum 50-percent U.S. content required for full funding.

U.S. processing

Currently, FAS does not ask for information on the extent of a product's U.S. processing. As a result, FAS officials made assumptions regarding U.S. processing in order to decide on fiscal year 1993 funding. FAS officials stated that they assumed the level of U.S. processing by the nature of the product and the presence or absence of foreign brands in the program.

EVALUATING MPP EFFECTIVENESS

FAS is required to evaluate MPP effectiveness by the Food, Agriculture, Conservation, and Trade Act of 1990 and the conference report accompanying the fiscal year 1993 MPP agriculture appropriation. We believe such an evaluation will be methodologically difficult because of the many uncontrollable variables that affect the success of international marketing efforts. These variables include foreign exchange rate fluctuations, changes in foreign commodity production, and changes in foreign government policies.

FAS has claimed success for the program by linking MPP-funded promotions to increased exports. However, a credible evaluation requires much more than this association. For example, even if a brand-name promotion effort results in identifiable increases in exports, unless FAS can convincingly demonstrate that the promotion effort would not have been undertaken without MPP assistance, those increases in exports cannot be attributed solely to the program.

FAS CONFUSION OVER MPP GUIDANCE

FAS officials indicated in recent congressional hearings, as well as in discussions with us, that it would be beneficial for the Congress to clarify the intent of MPP. They stated that in their view the direction provided by the conference report accompanying the fiscal year 1993 agriculture appropriation bill conflicts with the guidance provided in the 1990 legislation enacting MPP. Specifically, FAS officials believe that the primary goal of MPP is to help U.S. farmers by increasing U.S. agricultural exports.

They told us that certain direction provided by the conference report limits their ability to increase U.S. agricultural exports. For example, to make their point officials referred to the conference report requirement that MPP funds be allocated to small businesses. They observed that MPP was not originally intended to be a small business development program.

While these officials recognize the existence of more specific guidance in the conference report, they continue to believe that increasing U.S. agricultural exports is the MPP's overriding goal. Accordingly, Congress may wish to clarify its intent by amending the enabling MPP legislation.

Mr. Chairman and Members of the Subcommittee, this concludes my prepared statement. I will be happy to answer any questions that you or the Subcommittee may have.

LENGTH OF PARTICIPATION BY COMMERCIAL FIRMS IN THE TEA/MPP BRAND-NAME PROGRAM, FISCAL YEARS 1986-92

Years funded	Number of firms	Percent of all firms	TEA/MPP funding (millions)	Percent of total brand-name program
7	17	1.4	$146.9	35.6
6	55	4.4	71.6	17.3
5	64	5.1	54.1	13.1
4	129	10.2	49.6	12.0
3	149	11.8	37.9	9.2
2	287	22.8	31.3	7.6
1	560	44.4	21.6	5.2
Total	1,261	100.0	$413.1	100.0

Source: Foreign Agricultural Service.

DISTRIBUTION OF MPP FUNDS TO FOREIGN AND DOMESTIC FIRMS FOR THE PROMOTION OF BRAND-NAME PRODUCTS

During the early part of 1992, the Foreign Agricultural Service (FAS) began obtaining information on the domestic and foreign ownership of commercial firms receiving Market Promotion Program (MPP) funds for brand-name promotions. Not-for-profit organizations were asked to categorize firms receiving MPP/Targeted Export Assistance (TEA) program funds during fiscal years 1986-92 using one of three designations: (1) U.S. firms, (2) subsidiary of U.S. firms, and (3) foreign-owned firms. Not-for-profit organizations were not asked to identify subsidiaries of foreign corporations. Tables II.1 and II.2 combine U.S. firms and subsidiaries of U.S. firms into a single category.

FAS did not verify the information provided by the not-for-profit organizations. FAS officials noted that the not-for-profit organizations sometimes contacted the commercial firms or relied on their best judgment when categorizing firms.

Table II.1: MPP Funds Provided to U.S. and Foreign Firms for Brand-name Promotions, Fiscal Years 1986-92

Dollars in millions

Fiscal year	U.S. firms		Foreign firms		Total MPP funds
	MPP funds	Percent of annual funding	Dollars	Percent of annual funding	
1986	$17.3	90.6	$1.8	9.4	$19.1
1987	30.4	83.3	6.1	16.7	36.5
1988	29.7	79.0	7.9	20.9	37.6
1989	61.3	83.9	11.8	16.1	73.1
1990	59.8	79.7	15.2	20.3	75.0
1991	76.8	80.6	18.5	19.5	95.3
1992	59.1	77.4	17.3	22.7	76.4
Total	**$334.8**	**80.9**	**$78.6**	**19.0**	**$413.4**

Source: FAS.

Table II.2: Number of U.S. and Foreign Firms Receiving Funds for Brand-name Promotions, Fiscal Years 1986-92

Fiscal year	U.S. firms		Foreign firms		Total
	Number	Percent of annual funding	Number	Percent of annual funding	
1986	91	91.0	9	9.0	100
1987	176	61.3	111	38.7	287
1988	172	55.5	138	44.5	310
1989	350	74.6	119	25.4	469
1990	385	77.3	113	22.7	498
1991	462	77.5	134	22.5	596
1992	446	73.6	160	26.4	606
Total[a]	891	70.6	370	29.3	1,261

[a]Numbers do not add due to firms receiving funds in more than 1 year.

Source: FAS.

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