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BY THE COMPTROLLER GENERAL

Report To The Congress

OF THE UNITED STATES

Stronger Emphasis On Market Development Needed In Agriculture's Export Credit Sales Program

Since 1956 the Commodity Credit Corporation has financed over $7 billion in agricultural exports under its Export Credit Sales Program. Originally initiated to help dispose of surplus commodities, the Program has become a primary means of developing foreign markets for U.S. exports.

GAO recommends several administrative and statutory changes to strengthen the Program's market development objective.

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COMPTROLLER GENERAL OF THE UNITED STATES
WASHINGTON, D.C. 20548

B-114824

To the President of the Senate and the
Speaker of the House of Representatives

This is our report on the need for stronger emphasis on market development in Agriculture's Export Credit Sales Program.

Copies of this report are being sent to the Director, Office of Management and Budget, and to the Secretaries of State, Agriculture and the Treasury.

Elmer B. Staats
Comptroller General
of the United States

Enclosure

COMPTROLLER GENERAL'S
REPORT TO THE CONGRESS

STRONGER EMPHASIS ON MARKET DEVELOPMENT NEEDED IN AGRICULTURE'S EXPORT CREDIT SALES PROGRAM

D I G E S T

One of the Department of Agriculture's major export promotion programs is the Commodity Credit Corporation's Export Credit Sales Program. In 1978, this Program financed $1.6 billion in agricultural exports (about 6 percent of total U.S. exports of $27.3 billion).

The Program is designed to supplement private export financing with interest-bearing Government credits of up to 3 years. It is not based on formal government-to-government agreements and its terms are non-concessional; that is, interest rates on credits are above the rates at which the Corporation borrows from the U.S. Treasury.

The Program has been self-supporting, with an excellent record of repayments. Fiscal year 1979 operation costs for salaries and computer time are estimated at $1 million.

More active management of the Program is needed, however, to help maintain and develop markets for U.S. agricultural exports. Agriculture's Office of the General Sales Manager which administers the program should:

--Intensify efforts to develop strategic marketing plans.

--Tighten regulations and review procedures to reduce the risk of replacing cash sales.

--Reaffirm the Programs's market development objective.

--Reduce the influence of economic and political considerations on decisions.

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--Strengthen compliance with regulations through more reviews and audits of selected U.S. exporters' records.

COMMODITY AND COUNTRY PRIORITIES AND MARKET SHARE GOALS

The Office of the General Sales Manager has not established specific commodity and country priorities or market share goals for the Program. Instead of actively managing the Program, the Office has passively reviewed requests for credit case by case. Virtually any credit can be justified on the broad objective of maintaining and developing markets. The absence of specific plans makes the Program more vulnerable to the influence of secondary economic and political considerations.

In 1978 and 1979 congressional testimony, the General Sales Manager indicated that the Foreign Agricultural Service would develop country-by-country strategic market plans which would incorporate information on foreign competitors and establish the most effective combination of direct private sales, Government credits, and market promotion. However, little progress has been made. (See p. 16.)

-DLG03176

The Office of the General Sales Manager should work with the Foreign Agricultural Service and the Economics, Statistics, and Cooperatives Service to establish overall commodity and country priorities and develop country marketing plans which include U.S. market share goals and target levels for the Export Credit Sales Program. This effort should include systematically collecting, analyzing, and using more information on foreign competition. (See specific recommendations on pp. 17, 22, and 23.)

-DLG03177

CREDIT AND INCREASED EXPORTS

Commodity Credit Corporation credits have aided agricultural exports but Agriculture studies indicate that the gain in exports is probably significantly less than the amount of credits granted. (See p. 24.) Despite official concern and statements to the contrary, GAO found that the Program does not have safeguards to avoid replacement of cash or privately financed sales. (See p. 33) Some country lines of credit had been established even though justification documents indicated that credits might displace cash sales. (See p. 32.)

Prior to July 11, 1978, Program regulations included a provision precluding the registration of sales made before the availability of a country line of credit unless the sales were made contingent on the availability of credit or the Corporation determined that registration would be in the interest of Program objectives. This provision was considered a cardinal principle of the Program, the violation of which could lead to wholesale replacement of cash sales. Nevertheless, the provision was revoked, thereby allowing the registration of "old" sales of all eligible commodities. (See p. 27.)

Agriculture should reinstate this provision prohibiting the registration of sales made prior to the date that financing becomes available. (See recommendation on p. 33.)

REAFFIRMATION OF BASIC PROGRAM OBJECTIVES

The Program provides significant economic benefits to the governments of major recipient countries. For this reason, the amounts and terms of some credits are the subject of bilateral government negotiations and are influenced by U.S. foreign policy considerations.

Recipient countries receive substantial economic benefits in the form of domestic budget and balance-of-payments support. For example, in 1978 the Corporation approved a $170-million, 3-year repayment credit for wheat and feed grains for Korea. Subsequently, it was learned that a Korean Government agency

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imported the commodities and resold them on repayment terms of 90 days or less. In 1978, Agriculture auditors reported a similar situation in the Philippines. (See p. 40.)

The Office of the General Sales Manager has objected to the use of the credits for economic suport of foreign countries, but the practice continues. However, a 1965 opinion of the Justice Department found that the Program was not subject to the Cargo Preference Act, on the basis that sales of a commercial nature were involved. If the program continues to be used for economic support of another country's domestic budget and balance of payments, Justice, using the same reasoning, might decide that the Program is required to comply with the Cargo Preference Act. (See pp. 11 and 37.) If the Program was subject to the Act, the additional shipping cost would make U.S. exports noncompetitive. The Office of the General Sales Manager should reaffirm the Program's basic objective to develop foreign markets for U.S. agricultural products. It should also insure that foreign users and not governments receive the full benefits of the credits. (See p. 45 for specific recommendations.)

The Congress could strengthen the Program's market development objective by amending the Food for Peace Act of 1966 to add conditions on the granting of short-term credits similar to those for intermediate credit financing of agricultural exports in the Agricultural Trade Act of 1978. The latter Act prohibits the use of intermediate credits unless the Secretary of Agriculture determines that the final sale will:

> "(A) develop, expand, or maintain the importing nation as a foreign market, on a long-term basis, for the commercial sale and export of United States agricultural commodities without displacing normal commercial sales, or

"(B) otherwise improve the capability of the importing nation to purchase and use, on a long-term basis, United States agricultural commodities."

The 1978 law also provides that "Intermediate credit financing may not be used to encourage credit competition, or the purpose of foreign aid or debt rescheduling."

Amending the Food for Peace Act to add similar restrictions on short-term credits would assist the Office of the General Sales Manager in restricting credits to countries and to amounts which could be justified on market development grounds. (See p. 46.)

ASSURING COMPLIANCE WITH ADMINISTRATIVE REGULATIONS

GAO found that compliance with administrative regulations was good, except that U.S. exporters were not providing documents evidencing entry of financed commodities into destination countries. Followup by the Office of General Sales Manager to secure these documents was limited. Program regulations do not require evidence of entry documents for credits with repayment terms of 12 months or less. Also, exporters request numerous amendments to financing agreements which are almost always approved without verification.

The Office of the General Sales Manager should verify that Commodity Credit Corporation-financed commodities reach their intended destinations and that amendments to financing agreements are based on valid reasons. (See specific recommendations on p. 54.)

AGENCY COMMENTS

There was general agreement among the agencies that market shares, priorities, and targets could provide a useful overview for managing the Program. The Office of the General Sales Manager agreed in principle but indicated that these should not be applied rigidly. (See app. III.)

The Office also said that the principle of additionality--fostering sales that would not otherwise occur--is fundamental to the Program's market development goal. Other agencies agreed, but there was no consensus on what actions would best assure that credit sales do not replace normal commercial sales. The Office did not propose any management actions it might take, although it rejected GAO's proposals. (See app. III.)

The Foreign Agricultural Service agreed with GAO that the July 1978 change in Program regulations weakened the Program's market development objective and the concept of additionality. Chapter 4 examines in depth why GAO believes a formal review system is necessary to help management determine whether the extension of credit will replace other cash sales and why the Program regulation should be reinstated.

The Office of the General Sales Manager agreed in principle that actions should be taken to assure that the economic benefits of credits are passed through to end users, but it defined these as the actual buyers and not the ultimate consumers. It did not state that it would take any of the recommended actions (See app. III.) The Department of State and Agriculture's Office of Inspector General agreed with our recommendations. (See apps. V and VII.)

The Office of the General Sales Manager has no objection to GAO's recommendation that the Congress amend the Food for Peace Act of 1966; however, it said that if the Congress did so, it should allow some flexibility. The Foreign Agricultural Service concurred with this recommendation and its intent. (See apps. III and IV.)

The Office of the General Sales Manager disagreed with many of the recommendations to improve compliance with administrative regulations. It objected to requiring entry documents for all shipments and to establishing and implementing procedures to physically verify the entry of commodities into the designated countries. (See app. III.)

Other agency comments are addressed in the body of the report, beginning on page 23.

Contents

ABBREVIATIONS

CCC	Commodity Credit Corporation
GAO	General Accounting Office
OGSM	Office of the General Sales Manager

CHAPTER 1

INTRODUCTION

Agricultural exports play a major role in overall U.S. trade and in reducing the current annual U.S. trade deficit. In fiscal year 1978, agricultural exports reached an all-time high of $27.3 billion, while imports totaled $13.9 billion, creating a trade surplus of $13.4 billion. This contrasts with nonagricultural exports of $104 billion, imports of $152 billion, and a resulting trade deficit of $48 billion. Nearly 6 percent of the 1978 agricultural exports were financed under the Commodity Credit Corporation's (CCC) Export Credit Sales Program, which the Department of Agriculture said helped to achieve 1978's all-time high export total.

The Export Credit Sales Program was initiated by Agriculture on February 7, 1956, to allow the CCC to dispose of its surplus stocks by financing sales on short-term credit. The emphasis of the Program shifted to foreign market development as CCC inventories were reduced and privately owned stocks were made eligible for financing under the Program. Until the early 1970s, the Program was relatively small, but by 1978 it had a budget of $1.7 billion. As an indication of this rapid growth, over half of the total Program credits of $7.0 billion were made available between fiscal years 1975-78.

The Export Credit Sales Program operates under 2 legislative authorities. Section 5(f) of the Commodity Credit Corporation Charter Act (15 U.S.C. § 714c(f)) authorizes the CCC to use its general powers to "Export or cause to be exported, or aid in the development of foreign markets for agricultural commodities." Section 4 of the Food for Peace Act of 1966 (7 U.S.C. § 1707a) provides that "Commercial sales of agricultural commodities out of private stocks on credit terms of not to exceed three years may be financed by Commodity Credit Corporation under its Export Credit Sales program." Two documents outline the policies and regulations governing the Program--the CCC Board Docket, "Financial Arrangements Required by CCC Under its Export Credit Sales Program," and "Regulations Covering Export Financing of Sales of Agricultural Commodities Under the Commodity Credit Corporation Export Credit Sales Program, GSM-5."

PROGRAM DATA

In fiscal year 1978, the Export Credit Sales Program's budget reached a record level of $1.7 billion and actual disbursements totaled $1.58 billion; importers from 22 countries purchased 18 different commodities under the Program.

Table 1 shows the Program's budgets and actual disbursements from 1973 through 1979.

Table 1

Fiscal year	Approved budget	Actual disbursements
	(millions)	
1973	$1,100.0	a/$1,029.0
1974	415.0	297.9
1975	415.0	248.6
1976	900.0	621.4
Transition quarter	125.0	335.5
1977	1,000.0	755.3
1978	1,700.0	1,582.6
1979	1,565.0	b/1,340.6
1980 (proposed)	725.0	

a/Includes $460 million to the Soviet Union.

b/As of August 24, 1979.

Countries

The Export Credit Sales Program has financed exports to 84 different countries. The number of recipient countries each year has varied from as many as 44 to as few as 18. Table 2 shows the 10 principal recipients since the Program began and during fiscal year 1978.

Korea and Poland have been the Program's major participants, accounting for a third of all credits. The third largest historical participant, the Soviet Union, accounts for 8 percent, or about half of Poland's total, and made purchases only in 1973 and 1974. Japan, the fourth largest participant, has not received credits since 1974 because it is considered a cash market for U.S. agricultural exports.

Table 2

Country	Overall total		1978 total	
	Rank	Amount	Rank	Amount
Republic of Korea	1	$ 1,290,188,808	2	$432,273,739
Poland	2	1,086,977,351	1	504,663,756
Soviet Union	3	549,692,565	(a)	-
Japan	4	424,881,676	(a)	-
Portugal	5	345,899,671	3	176,285,240
Philippines	6	342,524,188	7	53,546,546
Peru	7	333,887,380	6	74,223,456
Greece	8	305,014,634	5	79,176,513
Pakistan	9	250,758,460	4	95,905,166
United Kingdom	10	240,064,487	(b)	-
Chile	(b)	-	8	45,787,732
Romania	(b)	-	9	22,998,385
Thailand	(b)	-	10	19,269,292
Total, top 10 countries		$5,169,889,220		$1,504,129,825
Total, all countries		$7,047,826,606		$1,582,603,590
Percent of credits to top 10 countries		73		95

a/Not eligible in 1978.

b/Not in top 10 dollar amount financed.

Commodities

The commodities eligible for financing under the Program are subject to change according to the Department of Agriculture's assessment of availability in exportable quantities. Since 1956, a total of 31 different commodities have been financed. In fiscal year 1978, only 18 commodities were financed. Table 3 shows the commodities accounting for the largest dollar sales since 1956 and during fiscal year 1978.

Wheat, the predominate commodity financed, has accounted for nearly 32 percent of all Program credits since 1956, while corn and raw cotton have accounted for 22 percent and 19 percent, respectively. Collectively, these three commodities have accounted for 73 percent of all credits. No commodity, however, has had a consistent growth pattern;

all of them exhibit a "roller-coaster pattern"--up one year and down the next. For example, although wheat is the leading commodity, it was not eligible for the Program in 1975 and 1976.

Table 3

Commodity	Total Program		1978 Total	
	Rank	Dollar amount	Rank	Dollar amount
Wheat	1	$2,246,524,184	1	$467,730,645
Corn	2	1,549,139,054	2	439,413,783
Cotton, raw	3	1,334,299,944	3	229,634,592
Tobacco, unmanufactured	4	534,591,300	6	46,089,741
Grain sorghums	5	289,643,089	7	45,523,203
Soybean oil	6	233,123,443	9	38,922,639
Rice	7	182,865,916	10	16,550,828
Soybean meal	8	178,796,053	4	116,841,824
Soybeans	9	147,233,110	5	94,756,592
Barley	10	122,250,611	8	40,296,343
Total, top 10 commodities		$6,818,466,704		$1,535,760,190
Total, all commodities		$7,047,826,606		$1,582,603,590
Percent of credits to top 10 commodities		97		97

PROGRAM MILESTONES

During the Export Credit Sales Program's 23 years, it has undergone several significant changes in purpose and/or size.

February 7, 1956 - Program initiated to help dispose of excess CCC stocks of agricultural commodities.

February 28, 1967 - Credits made available for export of privately owned stocks of agricultural commodities.

December 23, 1971 - Criteria established for determining eligible commodities and countries; market development stated as basic criterion for country eligibility.

Fiscal year 1973 - Annual Program level exceeds $1 billion as credits are made available for Soviet grain purchases.

Fiscal year 1978 - Record budget authorization of $1.7 billion and disbursements of $1.58 billion.

October 21, 1978 - Agricultural Trade Act of 1978 (Public Law No. 95-501, 92 Stat. 1685) makes the People's Republic of China eligible for credits.

SCOPE OF REVIEW

We reviewed the authorizing legislation, past and current regulations, and reports and studies relating to the Export Credit Sales Program. We reviewed files and interviewed officials in the Department of Agriculture's Office of the General Sales Manager, which is responsible for the Program. We also interviewed other Agriculture officials, including several former Agricultural Attaches, to learn how they had used the Program while serving overseas. To verify compliance with Program regulations, we reviewed a statistical random sample of 48 financing agreements made with U.S. exporters and the related financial records.

We visited and surveyed, through a formal questionnaire, 45 exporters in 8 cities; these exporters accounted for almost 75 percent of all Program credits in fiscal year 1978 and exported 14 of the 18 commodities financed. We also interviewed 7 tobacco exporters in Virginia and North Carolina as a preliminary confirmation of the issues prior to soliciting views from a large group of exporters.

We reviewed the fiscal year 1978 annual reports made to Agriculture by several U.S. Market Development Cooperators (trade associations or producer groups) whose export promotion activities are partially funded by Agriculture to determine how they used the Program in their marketing plans. As a followup to the information obtained from these reports, we interviewed 11 cooperators in 7 cities to gather additional information and to obtain their views on the Program.

Formal comments on this report were received from the agencies involved and are incorporated where applicable. (See apps. III through VIII.) We also met with officials of the Office of the General Sales Manager and Treasury to discuss their comments.

CHAPTER 2

HOW THE PROGRAM WORKS

The Export Credit Sales Program is foremost among the Department of Agriculture's programs for promoting agricultural exports. 1/ It is a self-sustaining, short-term, commercial program, administered by the Office of the General Sales Manager (OGSM), and provides financing from 6 months to 36 months at commercial rates for eligible commodities and countries. Interest rates are reviewed monthly and generally have been higher than the cost of money borrowed by the CCC from the U.S. Treasury.

PROGRAM OBJECTIVE

The current Program objective, as stated in the Quarterly Report of the General Sales Manager, is "to maintain and develop markets and to increase U.S. commercial sales of agricultural commodities which are in need of export assistance." According to the report, the Program "is designed to avoid replacement of cash sales per se and private financing." Administrative regulations add that a consideration in providing credit will be the extent to which the credit will "permit expanded consumption of agricultural commodities in the importing country and thereby increase total commercial sales of agricultural commodities." As part of this objective, credits are intended for additional exports.

Other important considerations are whether credit financing will

--permit U.S. exporters to meet competition from other countries;

--prevent a decline in U.S. commercial export sales;

--substitute commercial dollar sales for sales made pursuant to Public Law 480 or other concessional programs; and

--result in a new use of the agricultural commodity in the importing country.

1/Other current activities include Public Law 480, Non-Commercial Risk Assurance, Intermediate Credit, and Foreign Market Development Programs.

COMMODITY ELIGIBILITY

CCC regulations give authority to designate eligible commodities to the President or the Vice President of CCC, who is also the General Sales Manager. Commodity designations are based on supply use data developed by Agriculture's commodity estimates committees and on determinations that the commodities are available in quantities for export. A prerequisite to designating a commodity as eligible is a determination that CCC financing will increase overall commercial exports.

Eligible commodities are announced monthly by the Office of the General Sales Manager. Commodities in the latest announcement include all the major grains, tobacco, cotton, breeding cattle and swine, and rice. A complete list of eligible commodities is included in appendix I.

COUNTRY ELIGIBILITY

All countries are eligible for CCC credit except those prohibited by (1) Department of Commerce regulations (2) Executive orders (Cuba, North Korea, Vietnam), and (3) the Jackson-Vanik Amendment to the Trade Act of 1974 (19 U.S.C. 2432), which prohibits financing to nonmarket (Communist) countries except those having most-favored-nation status or for which waivers have been provided. All other countries are considered on a case-by-case basis.

The major Program users in 1978 were Poland, Korea, Portugal, and Pakistan. Appendix II contains a complete list of countries which have used the Program.

BUDGET CYCLE AND COUNTRY ALLOCATION

Because of constantly changing market conditions, the Export Credit Sales Program's budget has fluctuated yearly. The initial budget determinations are made months in advance of implementation and are invariably altered to accommodate changing credit needs and commodity priorities. The initial budget request and subsequent updates are a result of the following process.

1. OGSM reviews U.S. supply-demand projections, which pinpoint the commodities most in need of export assistance, and export projections developed by the Foreign Agricultural Service.

2. OGSM supplements these analyses by assessing the financial needs of a country and by

projections and responses of the Agricultural Attaches of the credit needs of the country.

3. OGSM takes into consideration other market development programs, including probable allocation of Public Law 480 funds, and expected commercial sales.

From these factors, a budget is developed country by country and commodity by commodity. The final overall Program level and allocations are approved by the Office of Management and Budget, acting on behalf of the President and with the advice of the Secretary of Agriculture.

The budget is financed by funds made available through the borrowing authority of the CCC. The Program's proposed budget has always been included for review in Agriculture's congressional budget submission. Agriculture's fiscal year 1979 Appropriations Act (Public Law 95-448, 925 Stat. 1073, 1082(1958) established the first ceiling for the Program and set it at a maximum $2.2 billion.

ESTABLISHING COUNTRY LINES OF CREDIT

Lines of credit are established by countries. The Office of the General Sales Manager responds to requests for lines of credit from foreign countries, importers, U.S. exporters, or U.S. Agricultural Attaches. No specific criteria have been developed, but, in determining whether or not a line of credit should be approved, OGSM considers the (1) need for protecting or increasing the U.S. share of the market, (2) probability that U.S. sales for cash will decrease, (3) financial ability of the country to repay the credits, and (4) availability of the commodities sought by the country. To help arrive at decisions, Agricultural Attaches are asked about the countries' interests in and needs for credits and financial reports are prepared on the countries' foreign exchange earnings, balance-of-payments positions, and total financial and debt structures.

The advice and counsel of the National Advisory Council on International Monetary and Financial Policies 1/ is sought

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1/The Council, consisting of representatives of Treasury, State, Commerce, Export-Import Bank, and Federal Reserve System, was established by Executive Order 11269 on Feb. 14, 1966, and is responsible for coordinating U.S. Government foreign lending.

when the credit involves a foreign bank's letter of credit for a period longer than 12 months or for more than $4 million. It is not required, regardless of the length or amount of credit, when a U.S. bank guarantees the credit.

New or extended lines of credit are announced through press releases which specify the country, commodity, amount, and credit terms. The press releases are made available to major market news services, trade publications, U.S. exporters, foreign embassies, and U.S. Agricultural Attaches in the countries involved.

PROCESSING OF SALES

After the press announcements have been released stating that credit financing is available, U.S. exporters who have negotiated firm contracts with foreign buyers can register sales with OGSM and request financing. Thereupon, financing agreements are issued to the exporters, guaranteeing that financing will be available. At this time, foreign buyers arrange for foreign bank letters of credit drawn in favor of the CCC to cover the value of the commodities to be financed. Foreign banks issue the letters of credit and arrange confirmation of the letters for at least 10 percent with U.S. banks which confirm the letters and advise the CCC.

When the commodities have been loaded aboard the vessels, the exporters furnish evidence of export and assignment of the accounts receivable; certifications of quantity, quality, and value delivered; and invoices breaking out the port values. These documents and letters of credit are reviewed to determine that they are acceptable to CCC and, if so, the U.S. exporters are paid the f.o.b. port values of the commodities.

The flow chart on the next page shows the process of an individual transaction from the time an exporter requests registration of a sale until he receives payment.

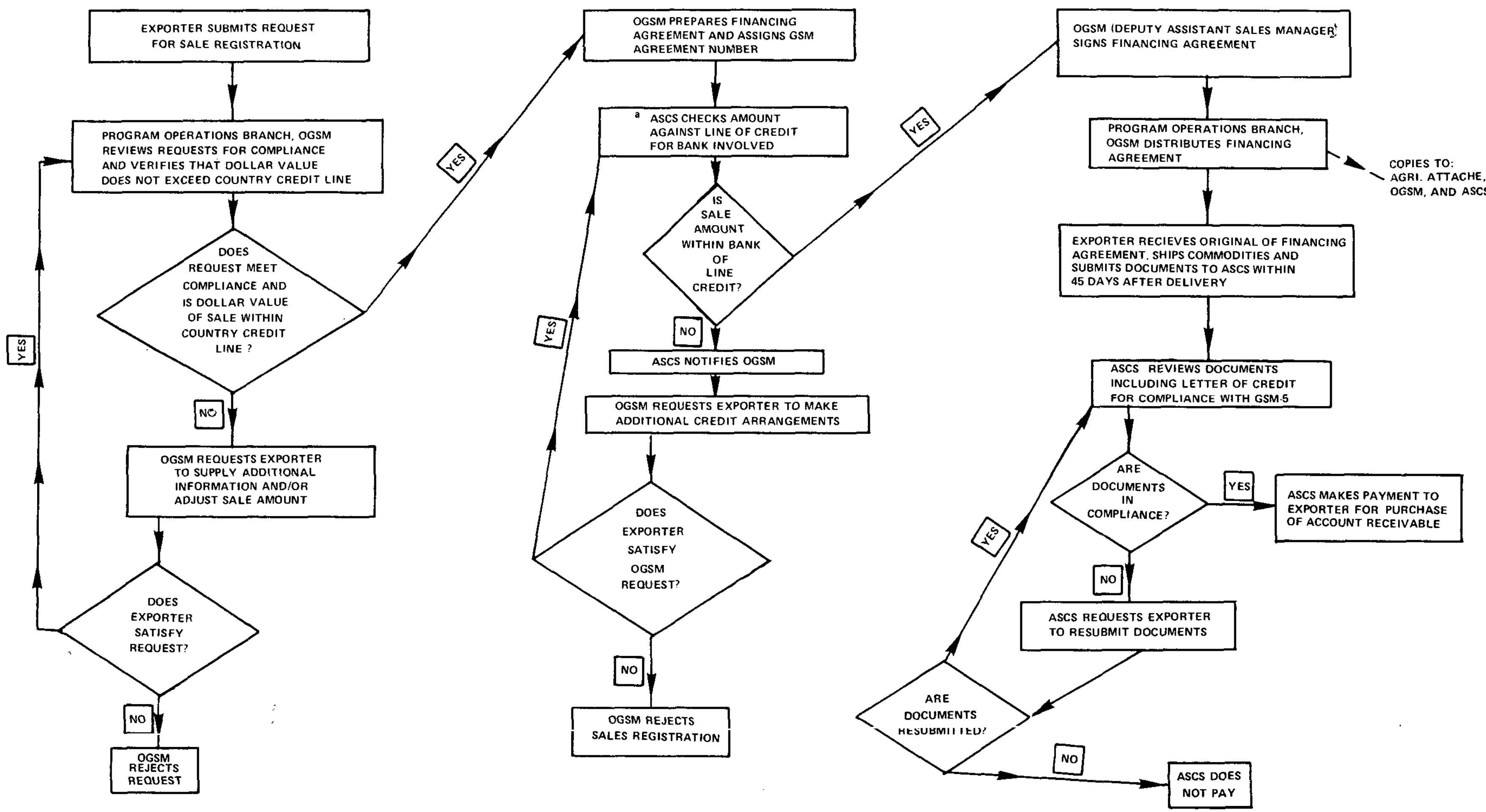
When the exporters are paid, the CCC collects against the letters of credit for the value of the commodities financed plus interest, in accordance with terms of the financing agreements.

PROGRAM FEATURES

Commercial nature

According to a 1965 opinion of the Justice Department, the Export Credit Sales Program is not subject to the

EXPORT CREDIT SALES PROGRAM
PROCESSING OF SALES FROM REGISTRATION TO PAYMENT



a AGRICULTURE STABILIZATION AND CONSERVATION SERVICE

Cargo Preference Act 1/. The opinion noted that:

> * * *if the terms of sale * * * are utilized only to the extent necessary to enable export sales to be made on the best terms obtainable in light of competitive conditions prevailing in the world markets, and not for the purpose of aiding or assisting a foreign nation or its economy, the Cargo Preference Act would not apply to export cargoes resulting from such sales."

Sales agreements are consummated between exporter and importer as usual commercial transactions. The foreign importer may or may not be an agency of the foreign government, but the exporter is always a private U.S. entity.

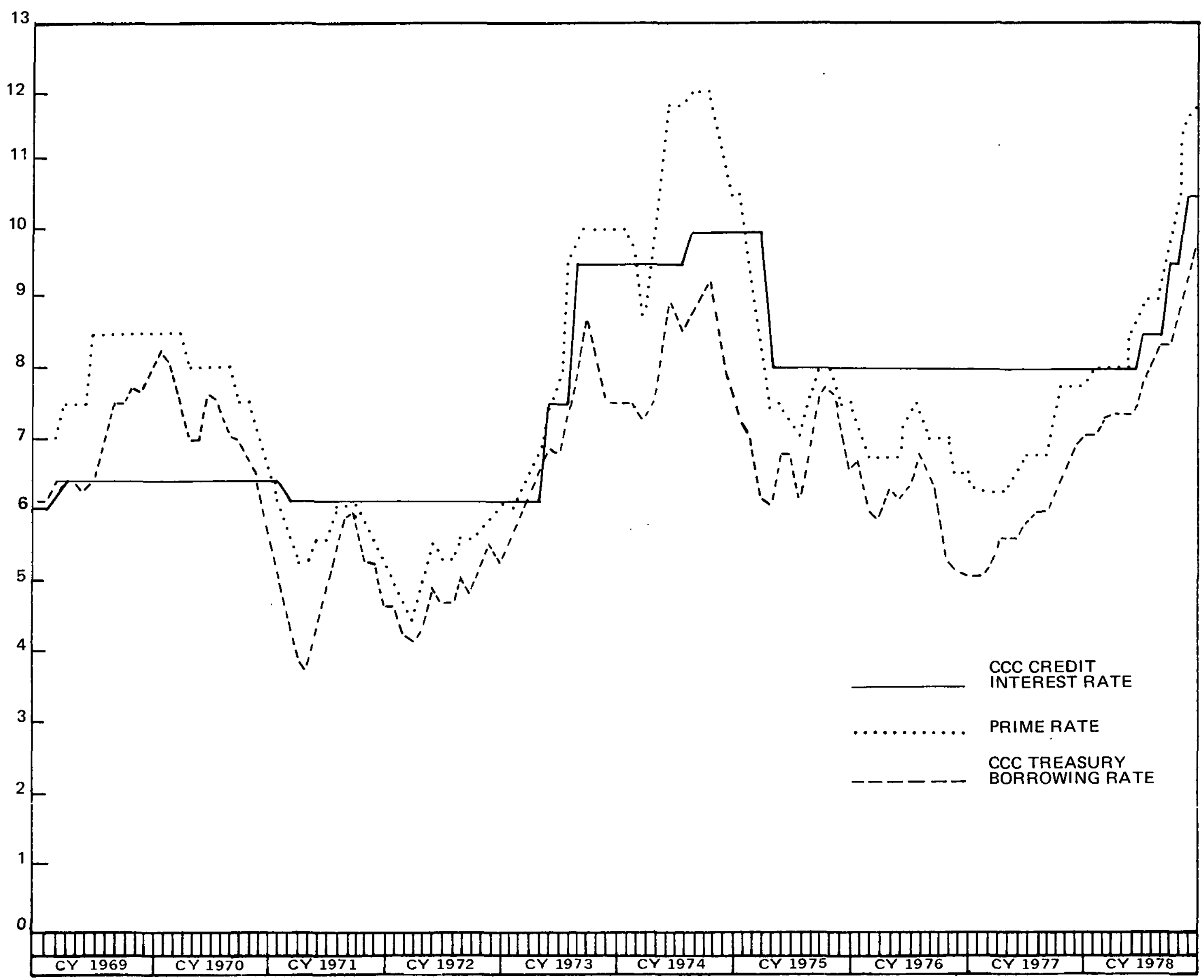
Interest rates and repayment period

The General Sales Manager, after consultation with the Controller of the CCC, determines what interest rates are to be charged. Interest rates for CCC credit are reviewed and announced monthly. At the reviews, the interest rates and terms of foreign competition are not the principal criteria, rather, the major concern is to maintain a "commercial" rate above the cost of money to the CCC to prevent the Program from falling under the purview of the Cargo Preference Act. The repayment period is set according to the credit needs of the importers; 77 percent of the fiscal year 1978 credits were repayable in 3 years.

As of September 1, 1979, annual interest rates were 11.5 percent for U.S. banks and 12.5 percent for foreign banks. The normal guidelines for setting the rate is the midpoint between the CCC borrowing rate and the U.S. prime rate. The CCC's interest rates have usually exceeded its cost of money, as shown in the graph on the next page.

1/Under the Cargo Preference Act (46 U.S.C. 1241 (b)), at least 50 percent of all commodities furnished by the United States "to or for the account of any foreign nation without reimbursement" must be moved in U.S. ships. GAO has recommended to Congress on two earlier occasions (CED-78-116, June 8, 1978; ID-78-31, Aug. 18, 1978) that the cargo preference laws be clarified as to the types of programs to which they should apply.

MONTHLY COMPARISON OF INTEREST RATE



According to a 1977 Department of Agriculture study, few, if any, foreign lending institutions charge lower interest rates than the CCC and most of them charge considerably more. This, plus the fact that foreign credit sources generally do not provide loans for commodity imports in excess of 90 days, makes CCC credit attractive to importers.

Operation costs and bad-debt losses

It is generally recognized that the Program is self-sustaining; however, the interest cost of funds borrowed from the Treasury for the Program cannot be isolated from total borrowings of the Commodity Credit Corporation. Payment received on a credit line is pooled with other receipts and used for other CCC needs; the CCC borrows in accordance with its overall needs, not for financing any one program. To the extent that disbursements in one fiscal year exceed repayments of financing provided during the previous 3 years, a net outlay for the year would result.

Fiscal year 1979 Export Credit Sales Program operation costs for salaries and computer time are estimated at $1.0 million, and disbursements totaled $1.6 billion.

The Program has had an excellent record of repayments, but it has had to reschedule payments for some countries. As of March 31, 1979, Zaire and Peru were the only countries with overdue principal and interest payments, which amounted to $10,059,144. Additionally, as of May 11, 1979, a claim amounting to $7,980,271 is pending against Intra-Bank Beirut, Lebanon, which ceased operations on October 15, 1966. Settlement of the claim is being handled in accordance with terms agreed to by CCC and the Government of Lebanon; an allowance for a loss of $1.3 million, the difference between the balance of the claim and the offered price, has been established.

CHAPTER 3

NEED TO ESTABLISH PRIORITIES

AND MARKET SHARE GOALS

To accomplish the goal of the Export Credit Sales Program, the Office of the General Sales Manager needs to establish country and commodity priorities and market share goals. An integral part of this planning should be to systematically collect, analyze, and use information about foreign competition. We found that country and commodity priorities or market share goals based on the Program's market development objective have not been developed and that sufficient competitor data is not available to do this. Also, the Agricultural Attaches, a principle source of information, are not fully utilized.

The absence of commodity and country goals affords Program officials great flexibility to adjust funding levels for changes in supply and demand. Without specific goals and objective criteria, the Program's effectiveness cannot be measured, and it is more vulnerable to the influence of secondary economic and political considerations. (See ch. 5.)

LACK OF COUNTRY AND COMMODITY PRIORITIES

The 1977 Department of Agriculture task force study on the role of CCC credit and Agriculture's export market development activities concluded that there was an overall need for greater planning and for establishing commodity and country export priorities. The study concluded that CCC's Program targeting efficiency was only moderately good and that "much of the program effort is being dispersed to low priority commodities and countries with less need for credit than others" and recommended that an attempt be made to develop country and commodity priorities for a more efficient and effective allocation of CCC credits.

Instead of actively managing the Program according to established priorities and goals, OGSM passively reviews requests for credit case by case. As the following example shows, almost any explanation can be used to approve credits under the broad objective of maintaining and developing markets; however, the need for some credits appears to be questionable.

Tobacco credits

In dollar terms, tobacco is the fourth most important agricultural export financed by CCC credits. Of the approximately $535 million in tobacco exports financed through fiscal year 1978, about 47.8 percent of the credits went to three countries; the United Kingdom received $201.4 million (37.6 percent), Australia, received $32.9 (6.1 percent), and New Zealand received $21.5 million (4.0 percent). Tobacco is the only commodity ever financed for Australia and New Zealand under CCC credits and, except for a 1976 credit for raisins, the only commodity financed for the United Kingdom since 1974.

Agriculture's statistics indicate that these countries are predominantly "cash" markets for U.S. tobacco exports; exports for cash or private credit terms for fiscal years 1973 through 1977 averaged 87 percent for Australia, 68 percent for New Zealand, and 86 percent for the United Kingdom. The statistics also indicate that since 1973 the U.S. market shares in Australia and the United Kingdom have declined in relation to imports from other foreign suppliers.

OGSM justified fiscal years 1978 and 1979 credits for tobacco exports to these three countries on the grounds that the credits would help to maintain U.S. market shares. For example, the 1979 justifications contended that without credits, the rising prices of U.S. tobacco "would probably force the buyers to seek lower priced leaf from alternate sources." We found the need for these credits questionable because they were used to finance transactions between only one major importing company and one U.S. exporting company. For the last 2 fiscal years, tobacco credits were established for Australia, New Zealand, and the United Kingdom for the total amounts requested by the importing company. These country credit lines were used exclusively by these two companies to finance a major portion of their businesses in the three countries; the remaining portions were financed on regular commercial terms.

Officials of the U.S. exporting company told us that its foreign customer's annual purchases of U.S. tobacco are based on import requirements which take into account the price and quality of U.S. tobacco in a particular crop year. Once the decision has been made to purchase a certain quantity of U.S. tobacco for shipment during the year, the importer arranges financing for its purchases. CCC credits were requested for the United Kingdom, Australia, and New Zealand because CCC's financing terms were better than those available commercially either in the destination countries or through the U.S. exporter.

Documents in OGSM files show the following sequence of events and the role of fiscal year 1979 CCC credits in these transactions.

1. U.S. exporter sells tobacco to foreign importer.

   June 28, 1978, sale to United Kingdom
   July 14, 1978, sale to Australia
   July 19, 1978, sale to New Zealand

2. Exporter requests country lines of credit.

   August 11, 1978, $8 million for Australia
   August 11, 1978, $5 million for New Zealand
   August 17, 1978, $10 million for the United Kingdom

3. Country lines of credit are announced for the amounts requested.

   September 11, 1978

4. Exporter's request received for registration of sales for full amounts of established credits.

   September 13, 1978

5. Finance agreements approved in the amounts requested by exporter.

   September 15, 1978

This sequence shows that CCC credits were established and used to finance sales already made, which casts doubt on OGSM's justification that the credits were needed to help maintain the U.S. shares of the Australian, New Zealand, and United Kingdom tobacco markets.

Commitment to priorities and market shares

The General Sales Manager supports the development of detailed market plans. In congressional testimony in early 1978, he said that the Foreign Agricultural Service staff would be developing country-by-country strategic market plans to establish the most effective combination of direct private sales, Government credit, and market promotion activities. However, we could identify only a few such country plans. Two of the earliest plans, for Poland and Indonesia, were drafted in the fall of 1977 and were never finalized. A

Program official described these two as market analyses rather than market development plans. Since then, marketing plans have been undertaken only for Sri Lanka and Romania.

In March 1979, during congressional hearings, the General Sales Manager again stated the need for commodity and country goals or priorities and for market shares.

A planning staff within the Foreign Agricultural Service was established in March 1978 and was authorized 11 positions. However, personnel ceilings have prevented the filling of all positions and as of May 1979, 7 of the authorized positions were filled.

CONCLUSIONS

The Export Credit Sales Program lacks specific commodity and country priorities and market share goals. As a result decisions are based on case-by-case examinations, and individual credits, some of which appear to have questionable effectiveness, can be justified on the broad objective of maintaining and developing markets. Without specific priorities and goals, the Program lacks objective criteria for measuring its effectiveness and is more vulnerable to the influence of secondary economic and political considerations.

RECOMMENDATIONS

We recommend that the Secretary of Agriculture direct the Office of the General Sales Manager to work with the Foreign Agricultural Service and the Economics, Statistics, and Cooperatives Service to:

--Establish commodity and country priorities for export activities.

--Develop specific overall U.S. market share goals for high priority commodities and countries.

--Establish target levels within these overall goals for the Export Credit Sales Program.

AGENCY COMMENTS AND OUR EVALUATION

The Treasury Department agreed that greater stategic planning is needed in establishing CCC lines of credit. In general, the Office of the General Sales Manager also agreed, and stated that market shares, priorities, and targets could provide a useful overview. However, OGSM believed they should not be applied rigidly, as mandatory priorities would not serve the interest of the Export Credit Sales Program, but should respond to actual requests.

Agriculture's Economics, Statistics, and Cooperatives Service also commented on the need for specific priorities and goals, noting that the lack of such goals suggests a need for research to establish both marketing plans and criteria for judging "the need for credit". This could help make OGSM less vulnerable to charges of being swayed by short-term political and other pressures and of taking a "passive role". The Service stated that it is presently conducting country strategic market studies.

The Foreign Agricultural Service also concurred with our recommendation to establish priorities and develop market share goals. At the time of our review, it had made little progress toward developing marketing plans. Since then, as it noted, the target countries have been identified and a strategic plan for Sri Lanka has been completed, establishing a market share goal for both U.S. wheat and feed grains. Additionally, the Foreign Agricultural Service recommended a level for programing credit into Sri Lanka for a specified time period.

We still believe there should be a more structured approach for establishing commodity and country priorities and market share goals and that the work begun by the Foreign Agricultural Service should be continued. Additionally, research efforts to develop both market studies and criteria for judging the need for credit should be closely coordinated among all Agriculture agencies.

Because of the Economics, Statistics, and Cooperatives Service's comments, we modified our recommendations to make it clear that the Office of the General Sales Manager should work not only with Foreign Agricultural Service but also with the Economics, Statistics, and Cooperatives Service in developing and establishing Program priorites and goals.

LACK OF ESSENTIAL COMPETITOR DATA

OGSM has stated, and we concur, that answers to the following questions are necessary for effective management of the Export Credit Sales Program.

--What is the U.S. market share for the particular commodity in the importing country?

--Who are the other suppliers of the commodity?

--What is the importing country's need for credit and what is its ability to repay a loan?

--What terms are being offered by competitors?

OGSM does collect, summarize, and analyze data to answer the first three questions; however, it has very limited information about competitors' credit terms. In addition, the information now reported by the Agriculture Attaches; Economics, Statistics, and Cooperatives Service; and U.S. exporters does not provide sufficient data to determine which countries have the greatest need for export credits. As a result, export credits have been given to countries when need has not been clearly established. In our opinion, information about competitors' credit terms could also be helpful in establishing country and commodity priorities and market share goals.

Need for credit information

According to OGSM, information about competitors' credit terms is difficult to gather since most countries, unlike the United States, do not publish credit information. In addition, credit is only one factor considered by importers together with price, quality, reliability of supplies, and transportation. Agricultural exporting countries use numerous strategies besides credit to promote exports, and as they increase their abilities to effectively produce agricultural products, their aggressiveness to promote their exports will also increase. For example, Canada, the U.S. major wheat competitor, about 10 years ago adopted the 20-year old U.S. practice of providing trips for wheat importers to teach them the latest developments in Canadian wheat production and processing.

To promote U.S. commercial export sales, U.S. credit terms must be better than other credit available to the importers and attractive enough to meet the competition from other countries. However, pressures to export certain commodities and to maintain a rate that is above the cost of money to the CCC exert the greatest influence on establishing interest rates.

Files contain limited information

During fiscal year 1978, the Commodity Credit Corporation authorized credit lines for various commodities to 25 countries. However, the Office of the General Sales Manager had foreign competition credit information for only 8 of the 25 countries, and interest rates and repayment terms on some transactions for only 5 of these 8 countries.

Each year, OGSM requests information from the U.S. Agricultural Attaches in order to project credit needs in importing countries, plan effectively, and obtain budget funds. The fiscal year 1978 request asked the Agricultural Attaches to:

--List the commodities and quantities for which financing would be needed and which would be likely to increase U.S. exports.

--Identify total import needs and probable origin of supplies by commodities.

--Identify probable portion of U.S. share for cash sales and state why credit is needed (e.g., to increase U.S. share or to meet competition).

--Estimate additional exports that might result if financing were available.

The Attaches' responses generally did not give specific reasons why credit was needed. In those instances where credit was justified to meet the competition, the competitor was sometimes identified but the credit terms offered or any other strategy used were not discussed.

We also noted a few instances when the Agricultural Attache made recommendations which OGSM did not follow. For example, in 1976 an Attache was asked whether, in his opinion, a credit to Yugoslavia should be closed so that "funds could be used for sales opportunities elsewhere." The Attache agreed that this should be done because Yugoslavia had no intention of using the credit and Brazil was offering Yugoslavia a lower price and interest rate. The line of credit was not withdrawn, however, and data from available records did not show why. An official stated that probably the pressure to close the line of credit was reduced when the budget for the year was later increased.

In our opinion, more information should be on record to explain not only why the line of credit was not withdrawn but also why it went unused. The records do not indicate whether or not Yugoslavia actually made purchases from Brazil and if so, why. Such information is important in determining if the Export Credit Sales Program can enable U.S. exporters to meet competition from other countries.

Information provided by Agricultural Attaches

According to OGSM, Agricultural Attaches are the best and primary source of current and reliable information about the countries for which they are responsible. The Agricultural Attaches regularly submit several reports relative to production, consumption, and trade.

Agricultural Attaches are in ideal positions to accumulate and report credit information, since they are in contact with host-government officials, trade representatives, the American business community, and other countries' attaches and representatives. However, several former Attaches told us they were not required to submit scheduled reports on competitor terms, although they responded to requests. They did not actively seek any credit information but developed it as the opportunity arose. In their opinion, the information was difficult to obtain.

Alternative sources of credit information

Although competitor's credit information is difficult to obtain and is usually received after the fact, every alternative should be explored. Two such alternatives are the Economics, Statistics, and Cooperatives Service and the exporters that use the Export Credit Sales Program.

The Service researches and evaluates foreign agricultural policies to determine their effects on U.S. foreign agricultural trade. Although it does not normally include the financial aspects of these policies in its research, it has made such studies for OGSM on another program.

From interviews with 45 U.S. exporters, we found that most of them knew the price, quality, and service offered by foreign competitors, and 33 percent received credit information they considered reliable. The main source of credit information came from overseas agents, but brokers, buyers, bankers, and trade associations also provided information. Several of the exporters said they volunteer information to OGSM, but there is no formal mechanism for relaying competitor information. OGSM might find this limited information useful; for example, several of the exporters trading in cotton stated that to their knowledge, no other competitor offered any credit; if credit was arranged, it was through private banks and at much higher rates and shorter repayment terms than those offered by the Export Credit Sales

Program. In fact, these exporters told us that most cotton sales to Korea would be made for cash if CCC credit was not available; a sale might be postponed temporarily but eventually, in a month's time perhaps, it would be completed.

CONCLUSIONS

Information about competitors' credit terms and repayment periods is important in order to develop country and commodity priorities and market share goals and to evaluate how the Export Credit Sales Program compares with credit offered by U.S. competitors. The Office of the General Sales Manager has limited information about competitors' interest rates and repayment terms, and the information that is available is not systematically collected and analyzed. In the absence of such an evaluation, what other competitors are offering can have only a minimal effect on determining interest rates for the Program.

We recognize the difficulties of obtaining competitor information. Competing suppliers of agricultural commodities do not make public their credit arrangements; many transactions involve negotiated prices, interest, promotion services, and transportation, thereby making accurate comparisons difficult. Nonetheless, we believe that OGSM should attempt to systematically collect, analyze, and use competitor information in its Program administration.

RECOMMENDATIONS

To improve the system of collecting information, we recommend that the Secretary of Agriculture direct the Office of the General Sales Manager to:

--Establish procedures to assure the systematic collection and analysis of competitor information in order to determine the market development role of the Export Credit Sales Program.

--Survey U.S. exporters annually to obtain pertinent information, such as foreign credit terms, problem areas, and suggestions for Program improvement.

--Expand its annual request to the Agricultural Attaches to include analyses of foreign competition and credit information.

We also recommend that the Economics, Statistics, and Cooperatives Service initiate studies to evaluate the credit aspect of foreign competition, including analyses of the credit terms offered by U.S. competitors.

AGENCY COMMENTS AND OUR EVALUATION

The Treasury Department agreed with the recommendation that Agricultural Attaches should thoroughly explore all sources of information about competing foreign credit terms and that it would be useful to have them submit scheduled reports on competitive conditions in key market countries.

The Office of the General Sales Manager concurred that its information about foreign competitors' credit terms is limited but added that such information will never be complete. It also said it would continue to solicit such information from Agricultural Attaches and other sources, but cautioned that the reported information may be neither accurate nor complete.

OGSM's comments gave no indication that it would specifically establish procedures to assure the collection and analyses of competitor information or expand its annual request to the Agricultural Attaches to include analyses of foreign competition and credit information.

OGSM commented that the report alleged that U.S. cotton shippers do not believe the Export Credit Sales Program is necessary. We did not intend to imply that the Program was not necessary for all cotton sales; but, as stated in the report, some exporters told us that most cotton sales to Korea would be made for cash if CCC credit was not available.

Also, OGSM stated that it would seek the opinion of the American Cotton Shippers Council as to whether CCC credit on cotton shipments to Korea is useful and necessary. We believe it is desirable for OGSM to seek this information as well as competitor information from all available sources; however, we question whether for Korea the Shippers Council could be considered completely objective, since it was responsible for implementing old-sales registration of cotton sales in Korea through an agreement with the Spinners and Weavers Association of Korea.

CHAPTER 4

HAS THE PROGRAM INCREASED U.S. EXPORTS

WITHOUT REPLACING COMMERCIAL SALES?

A basic principle of the Export Credit Sales Program is that the extension of credit to the importing country will increase total U.S. sales of agricultural commodities without replacing cash or privately financed sales. We found that, throughout the Program's history, Agriculture officials have worried about replacing cash sales but no management system has been developed which would minimize the risk. In fact, the possibility of replacing cash sales has increased as a result of a recent change in Program regulations. Information based on countries' past purchasing patterns indicates possible replacement of cash sales. Also, many sales contracts are not subject to the availability of export credits.

We believe that the Export Credit Sales Program has generally contributed to overall expansion of U.S. agricultural exports. However, we found that the need for some export credits is questionable.

EFFORTS TO MEASURE ADDITIONALITY

In reviewing requests for credit, the Office of the General Sales Manager makes no formal attempt to prove that the credit will lead to additional sales. Only several internal Department of Agriculture studies have addressed the subject of "additionality."

Special 1970 study

A 1970 Agriculture study was undertaken to develop optimal export and domestic program strategies for wheat. The study included a review of all Agriculture programs, whose principal objectives were to contribute to balancing wheat demand and supply so as to maintain U.S. farm prices and farm incomes.

The study stated that an increase in short-term credit or in other programs displaced, to some degree, U.S. cash sales or sales made under Agriculture export programs. At the same time, it was pointed out that there was little doubt that such sales also would displace some sales of competing foreign suppliers. To the degree that this happened, U.S. exports under the Export Credit Sales Program were "additional," and Program effectiveness is measured by the amount of additional exports that can be attributed to its use.

Based on a probability concept of additionality, the study concluded it was reasonable to expect that about 50 percent of the fiscal year 1971 sales under the Program may have been additional to U.S. exports. This figure was derived from the fact that the U.S. share of commercial wheat trade in the seven countries which purchased wheat under the Program was about 50 percent.

<u>1977 CCC credit and market development study</u>

In 1977, an Agriculture task force reviewed past and current strategies for promoting agricultural exports, including market development programs and options for improving export efforts.

The task force noted that the Export Credit Sales Program's ability to generate additional exports of U.S. farm products or to achieve other purposes had never been evaluated. It cited as reasons an apparent limited demand by Program officials as well as conceptual, methodological, and data difficulties. The study notes that:

--In the absence of well-documented evidence of Program effectiveness, one can only rely on the general conditions under which a high level of additional exports might occur.

--The effectiveness of CCC credit depends on whether it is used primarily to increase the purchasing power of importers (private or government) or to meet foreign competition. The purchasing power and competitive effects of any particular credit are not mutually exclusive, but the impact of CCC credit depends to some extent on how the country and commodity situations are selected. Credit could be targeted primarily to supplement an importer's purchasing power or to meet situations of intense competition or it could be targeted for a dual effect.

--The existing targeting process emphasized the support of importers' purchasing power. In cases where this was so, the net addition to U.S. agricultural exports was probably low because only a small portion of the increase in purchasing power provided by the credit would be used to import additional agricultural commodities. The rest of the increase would be used to import other items.

--With more aggressive targeting of credit to meet competition, the potential for additional exports could be improved, at least temporarily. For any one sale, the use of credit might yield either zero or 100 percent additional exports; that is, the sale would be either made or lost. Over a number of transactions, the expected U.S. gain would be related to its overall share of world trade in a commodity. For example, with a 40-percent share of world wheat trade, the probability for additional wheat exports from an aggressive U.S. strategy could run as high as 60 percent.

The 1970 and 1977 Agriculture studies discussed theoretical measures for gauging the additionality of CCC credits but neither led to major changes in the Export Credit Sales Program which might better assure that credits resulted in additional U.S. exports. In fact, the 1977 study was never finished and the OGSM representative disassociated himself from the task force effort.

Barter program system guarded against displacing cash exports

A barter program was operated from the mid-1950s through 1973, when it was suspended because the strong demand for U.S. agricultural commodities made this export incentive unnecessary. The barter program was orginally intended to be used selectively in countries where a price advantage would measurably increase exports by adding to straight cash sales. The accomplishment of this objective was to be assured through a system of commodity and country eligibility determinations.

From 1957 to around May 1972, an intra-departmental committee developed recommendations for commodity and country eligibility based on established criteria. A barter export designation was assigned to each combination of eligible country and commodity. For example, the designation "A" was assigned to countries where it appeared that U.S. exports could be increased through barter sales but which had a history of substantial cash sales. The designation "X" was assigned to countries where there was a little or no likelihood that barter exports would increase sales. The designation "B" was assigned to countries in fair-to-poor external financial positions or which had not been or were expected to become substantial cash markets. Thus, applications for financing assistance to these countries could be quickly assessed against the designations and determinations could be made as to whether further investigations were warranted.

Our 1973 report, "Improved Management Information System Needed for Eximbank's Capital Loan Program" (B-114823), cites the system as an example of how to help management determine whether assistance is essential to an export sale. A 1974 Agriculture audit report, "Barter Export Program" (60158-1-Hq), noted some administrative problems but pointed out that the additionality committee was a proper approach in determining commodity and country eligibility.

We did not attempt to evaluate the effectiveness of the system, but we are including this information to illustrate the feasibility of developing a system for determining additionality.

POLICY AND REGULATION CHANGES

Before July 1978, sales made prior to the approval of a country line of credit were generally not eligible for the Export Credit Sales Program unless they were made contingent upon the the availability of CCC credit. However, the regulations have now been amended to permit registration of such sales in order to give exporters more flexibility.

From 1956 to 1978, Program policy and regulations concerning the displacement of cash sales were continuously being liberalized. The policy initially required that a prior determination be made that cash sales would not be replaced if a credit sale was approved. In October 1956 this policy was revised. CCC officials felt that sufficient information had been obtained to indicate that the extension of credit, as a general matter, tended to increase sales. Therefore, a determination as to the displacement of cash sales would not be made on an individual basis.

By 1971, policy documents did not specifically mention the displacement of cash sales as a consideration for approving credit; instead the basic criterion was the usefulness of credit in maintaining or expanding exports, with particular attention to whether the United States was holding its share of the market and receiving a fair share of increased imports.

Program regulations were amended in July 1978 to permit the registration of sales prior to the approval of a country line of credit. An OGSM official stated that the regulations were changed to allow exporters more flexibility in making sales. According to an OGSM memorandum concerning the change:

> "Limiting CCC financing to sales made after the announcement of the line of credit is in direct contradiction of broader market development policy of this Administration which is to encourage customers to buy substantially ahead of shipment, to buy during seasonally depressed price intervals for shipment throughout the year, and to engage in a form of indicative planning by purchasing ahead."
>
> * * * * *
>
> "Our only reason for limiting the eligibility of CCC financing to new sales is to substantiate for the record that exports under this program are additional to cash business."

We examined selected fiscal year 1977 financing agreements. In our sample, $7.8 million in cotton sales to Korea had been made before the country line of credit was established. Some of the sales were made as much as 8 months before the credit had been established, and all were made before the regulations were amended to permit such registration. Subsequently, we found that OGSM knowingly accepted and registered $100 million in cotton sales to Korea which had been made before the line of credit was established.

According to OGSM, failure to permit old-sale registrations would have resulted in the importers canceling their contracts, possible loss of U.S. sales, and market share losses to the United States. Therefore, OGSM made an exception to the regulations and registered prior sales against a new line of credit. Although OGSM finally approved the request to finance these sales to Korea, it expressed concern that such a precedent could have adverse effects on the Program. A 1977 memorandum to the General Sales Manager noted that:

> "It is presumed that all other 'old sales' were made for cash and to finance them would constitute a replacement of cash sales. This is contrary to a cardinal principle of the Program * * *. It is important that we resist * * * registration of old sales * * *. The result would be wholesale replacement of cash sales and abandonment of a cardinal Program principle. * * * this would be extremely difficult to explain to Congress * * * and certainly could jeopardize the entire CCC Credit Program."

OGSM had earlier made another exception for cotton sales to Korea. During fiscal year 1975, because of adverse market conditions, OGSM permitted the registration of approximately $143.3 million in cotton sales. During this period, cotton prices dropped from about 80¢ to 40¢ a pound and several countries, including Korea, had "bought forward" substantial quantities of cotton. Textile demand also dropped sharply. A massive cancellation of contracts--about 1.4 million bales of cotton, or one-fourth of U.S. projected exports--was considered a real possibility. To prevent this, OGSM authorized the financing of "old sales."

Regardless of the merits of the 1975 and 1977 decisions to register old cotton sales, we believe that amending the regulations to permit registration of such sales of all commodities further erodes management's ability to determine when credit sales are additional to cash sales. Registration of such sales should be reserved for extreme or unusual circumstances dictated by market conditions.

NEED FOR EXPORT CREDITS IS QUESTIONABLE FOR SOME COUNTRIES

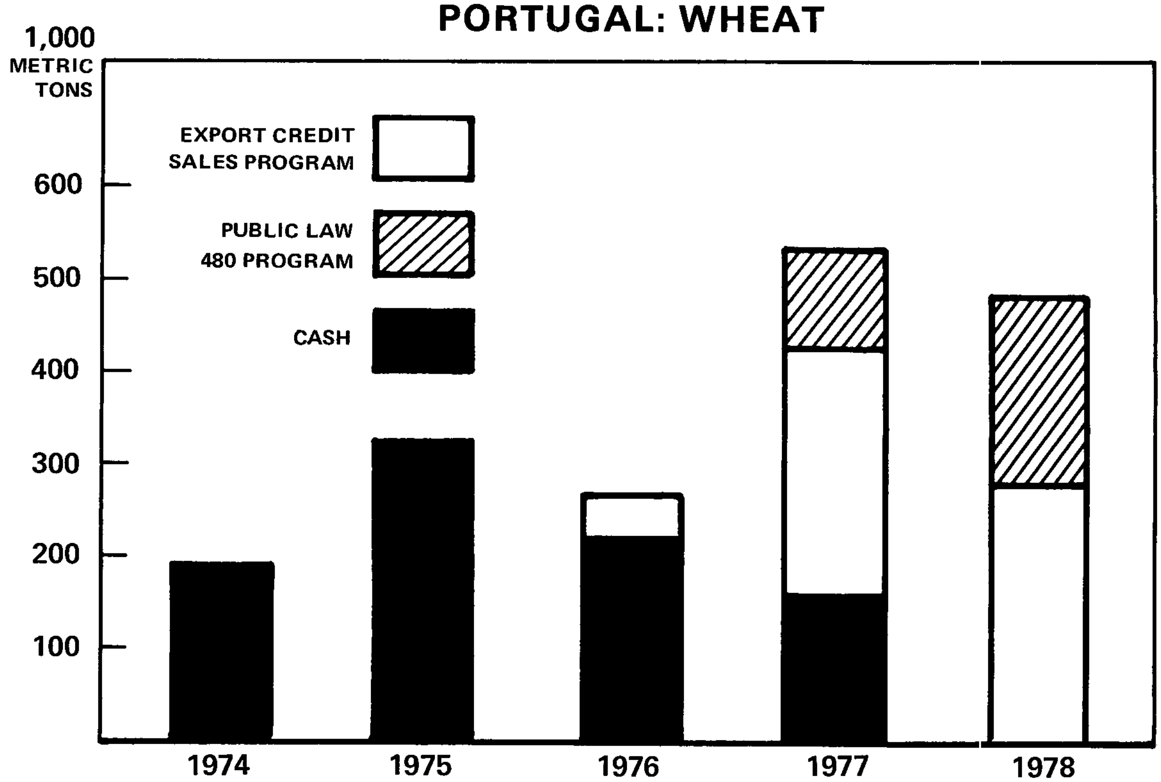
Our analysis of information available to OGSM raised questions concerning the possible replacement of cash sales by credits extended to certain countries. Furthermore, a review of selected exporter contracts showed that in many cases sales were not contingent upon the availability of export credits. Thus, the need for some credits is questionable and they may not be contributing to the overall expansion of U.S. agricultural exports.

Analysis of trends in selected countries

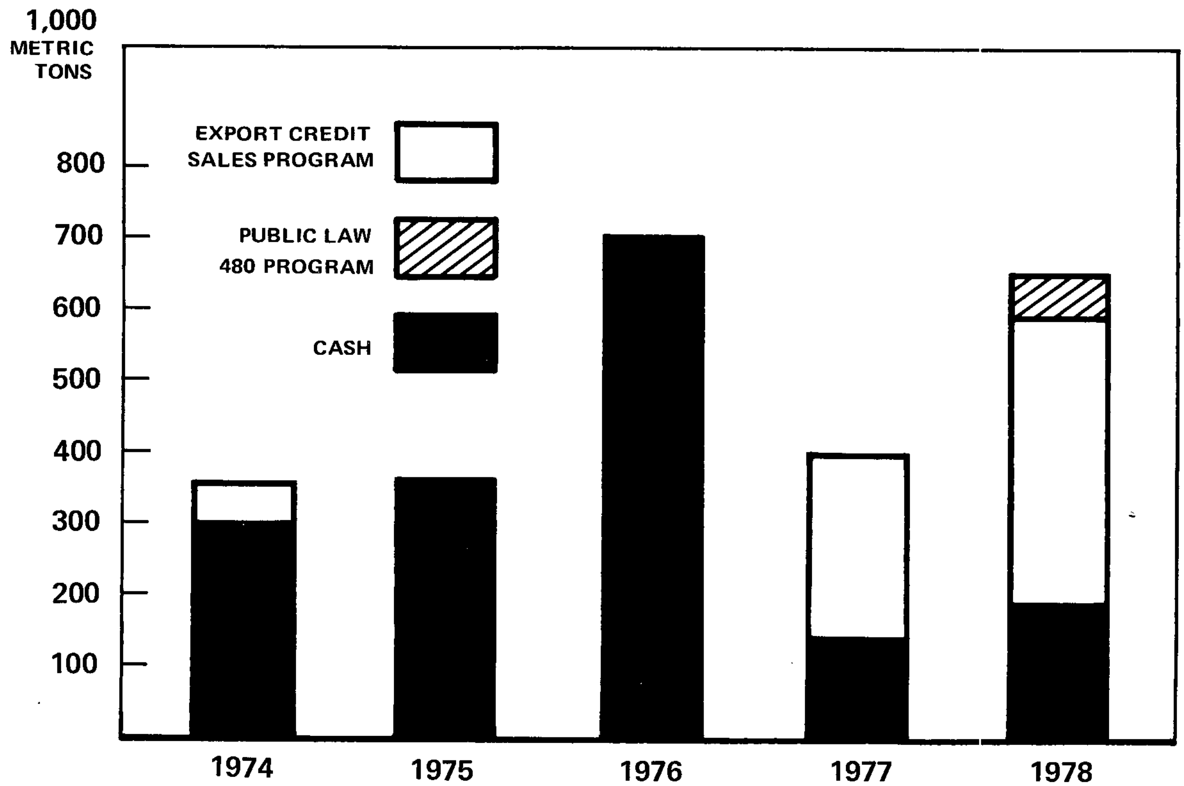
A recent OGSM memorandum states that additionality can be substantiated better by statistical analysis. In view of this, we analyzed export credit sales of major commodities to selected countries over a period of 5 years. Data for the analyses was obtained from OGSM commodity-country fact sheets.

The following analyses for Portugal, the Philippines, and Korea show that as export credit sales increased other commercial sales declined. In some cases, the decline in cash sales was substantial.

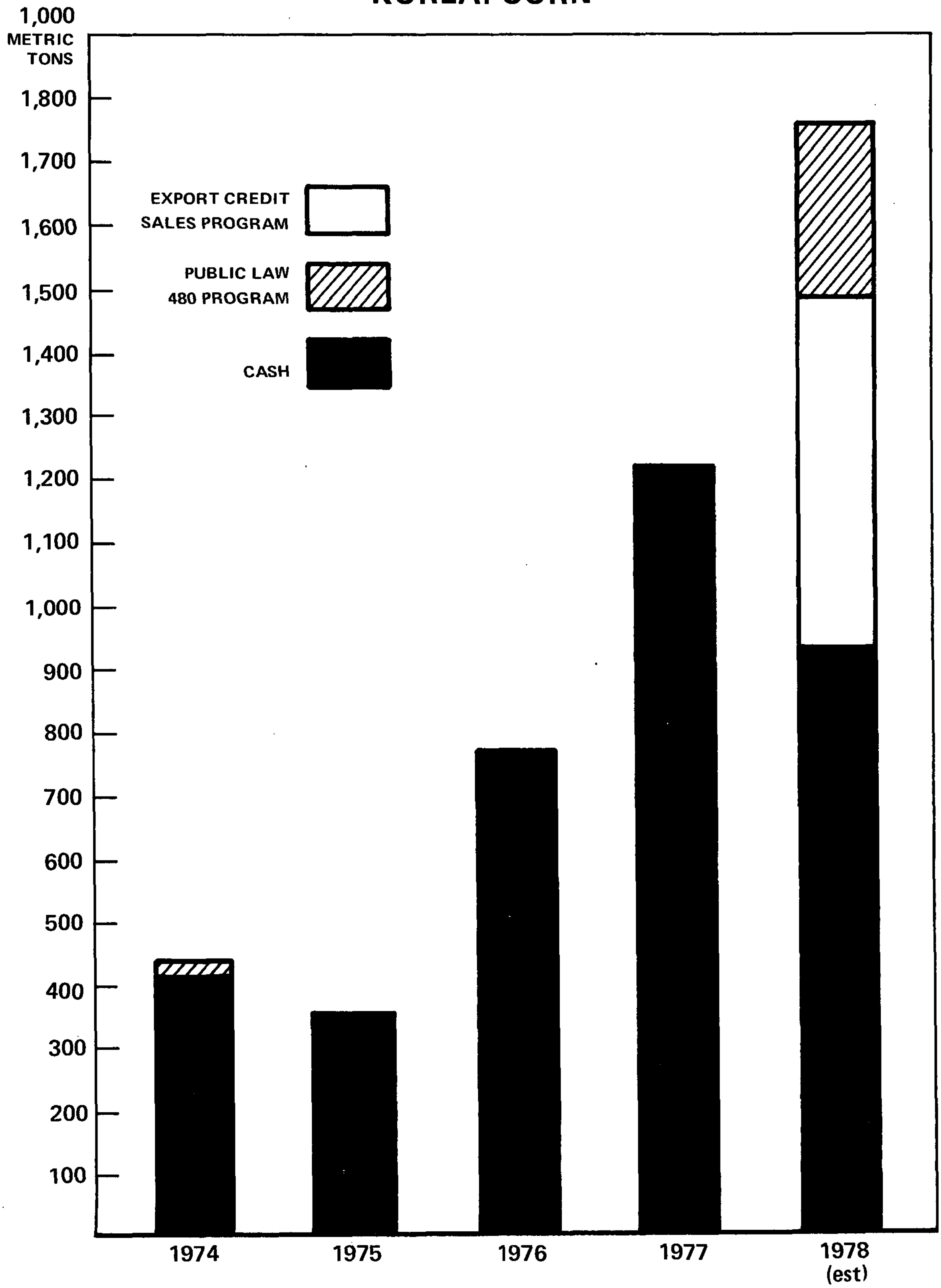
PORTUGAL: WHEAT



PHILIPPINES: WHEAT



KOREA: CORN


1,000
METRIC
TONS
1,800
1,700
1,600
1,500
1,400
1,300
1,200
1,100
1,000
900
800
700
600
500
400
300
200
100
EXPORT CREDIT
SALES PROGRAM
PUBLIC LAW
480 PROGRAM
CASH
1974
1975
1976
1977
1978
(est)

We found few documents to support or evaluate OGSM's actions for approving the credits. Verbal explanations were provided, but these explanations, according to an OGSM official, had to be approached on a case-by-case basis. For example, credit was extended to:

--Portugal for wheat because U.S. support of the Government of Portugal was increasing, foreign policy considerations were a factor, and U.S. credit was needed to maintain the market.

--The Philippines for wheat because the United States was facing increased competition and was threatened with loss of this market.

--Korea for corn because the industries using it were developing; the United States was facing increasing competition and loss of the market.

Our analyses underscores that the approval of credits can be explained on the basis of the broad objective--to maintain and develop markets and increase U.S. sales--even when such approval may result in a replacement of existing cash sales.

Sales not contingent on availability of credit

From our examination of selected contracts, we found that in many instances the contracts did not specify that the sales are contingent upon CCC credit and the importers had the option of making payment either in cash or by letters of credit. For example, on sales contracts with Korea, the importers could usually pay by either a sight letter of credit or Korean foreign exchange. Few of the exporters we interviewed stated that sales contracts were contingent upon the availability of CCC credit. In fact, financial terms are often prearranged before the importer is ready to purchase. We also noted that at least two contracts which originally specified cash payment were later changed to specify payment using export credits.

Some 1978 export credit justifications suggest cash sales may be displaced

OGSM's fiscal year 1978 justification letters to the National Advisory Council on International Monetary and Financial Policies cited each of the Program objectives in explaining why a line of credit should be provided. These explanations included a need to meet competition, reduce U.S. inventory levels, and maintain the U.S. share of the market. In at least four of the letters, OGSM expressed concern that cash sales might be replaced. However, the extension of credits to the countries was explained by citing Program objectives as the basis.

CONCLUSIONS

Agriculture's efforts to determine whether the Export Credit Sales Program results in additional exports of agricultural commodities or merely replaces other commercial sales have been limited. In fact, a recent change in regulations increases the risk that the Program will replace other cash sales.

Because of the broad Program objectives, almost any explanation can be provided to extend credits. Our review did not attempt to measure or quantify additionality. By certain examples, we have indicated that Program officials have sufficient information to suspect possible replacement of cash sales. Despite the availability of information and the longstanding concern about displacing cash sales, OGSM has not developed a review system to aid in minimizing the risk.

RECOMMENDATIONS

We recognize that it is difficult to determine additionality and that there is no system for absolutely insuring that the extension of credit will not replace other cash sales. However, more stringent regulations and review procedures would minimize the risk of replacing cash sales, and we recommend that the Secretary of Agriculture direct the Office of the General Sales Manager to:

--Reinstate the provision (1488.5, paragraph (b)) in the GSM-5 regulations which precluded the registration of sales made prior to the date that financing became available.

--Review a statistical sample of exporters' sales contracts each year to verify whether sales were contingent on the availability of credit.

--Establish a formal review system that will assist management in determining whether credits actually increased U.S. agricultural exports.

AGENCY COMMENTS AND OUR EVALUATION

Office of the General Sales Manager

OGSM stated that the principle of additionality was fundamental to the Export Credit Sales Program's goal of market development. It agreed that CCC credit sales should not displace other commercial sales, but stated that some displacement of normal commercial or cash sales was inevitable with CCC credit financing.

OGSM explained the July 1978 change in Program regulations on the grounds that the previous prohibition against the registration of sales made prior to the date that financing became available "caused bunching up and distortion of markets, caused shipping congestion at ports, and on balance worked against CCC's overall program of (domestic) price stabilization." OGSM asserted that the old policy caused market distortions because foreign buyers could not finance forward purchases under the Program and had to concentrate their purchases in a short space of time rather than purchasing when prices were depressed. OGSM contended that the change in regulations to allow financing of forward purchases made the Program more consistent with CCC's domestic price stabilization program. It also stated that the change better served the goal of market development, which it defined as including maintenance of existing markets as well as seeking new sales.

OGSM felt that making an annual sampling of exporters' sales contracts to find out whether sales were contingent on CCC credit would not be useful in getting to the root of the problem of additionality.

OGSM did not specifically comment on our recommendation that it establish a formal review system to assist in determining whether credits actually increased agricultural sales. In a later meeting to discuss our report and OGSM comments, however, agency officials indicated an unwillingness to accept this recommendation because they felt it would restrict flexibility of Program management. They further stated that there had been administrative problems connected with the use of an intradepartmental "additionality" committee under the barter program.

Foreign Agricultural Service

The Foreign Agricultural Service agreed that the market development objectives and the concept of additionality had been weakened by the change in regulations to permit financing of sales made prior to the establishment of a country line of credit. The Service, however, disagreed with our recommendation that the Program regulations should be tightened by reinstating the provision which precluded the financing of such sales because it felt that flexibility was important for market development.

The Foreign Agricultural Service also commented that the evidence was inconclusive on whether the gain in exports was significantly less than the amounts of CCC credits granted. It cited some preliminary work which indicated that there may be a large multiplier for export credits which confirms the concept of additionality and stated that it would like to study this matter further.

Other agencies

The Departments of State and Treasury agreed that there was a need to strengthen strategic planning and analysis to better assure that CCC credits lead to additional exports. State also expressed the view that the use of CCC credits to satisfy traditional customers appeared in some cases to create a dependency on those credits, whereas the purpose of the credits is to develop and establish long-term markets for normal U.S. commercial exports. State, therefore, believed that CCC should put greater emphasis on market development as opposed to market retention.

Our evaluation

OGSM and other concerned agencies agreed that the principle of additionality was fundamental to the Program's goal of market development. There was, however, no consensus on what actions should be taken to better assure that CCC credit sales do not replace normal commercial sales. OGSM rejected our recommendations and did not propose any alternative management actions it might take.

We believe there is sufficient concern and evidence that some CCC credits have displaced normal commercial sales to warrant changes in OGSM's regulations and review procedures. We find it difficult to reconcile OGSM's statement, that additionality is a fundamental principle of the Program, with its refusal to make any changes which might minimize the risk of displacing cash sales. Furthermore, we continue to believe, as does the Foreign Agricultural Service, that the July 1978 change in Program regulations weakened the market development objective of the Program and the concept of additionality. OGSM furnished us with no evidence that the prior policy of accepting only new sales for financing had caused market distortions and shipping congestion or had worked against CCC's overall program of price stabilization. Exports financed under CCC credits are a small portion (6 percent in 1978) of total agricultural exports. It is difficult to believe, therefore, that the adverse effects of the old regulations, although they might vary by commodity, could have been as serious as OGSM's comments imply. In addition, comments on the significance of forward purchases were restricted to only one commodity financed under the Program--cotton. As we noted, special exceptions to the prior policy of not registering old sales were made for cotton sales in 1975 and 1977. We continue to believe that registration of such sales should be reserved for extreme or unusual circumstances dictated by market conditions and that the change in regulations allowing registration of these sales for all commodities was unwarranted. We, therefore, reiterate our recommendation that OGSM reinstate provision 1488.5, paragraph (b) in the GSM-5 regulations.

We also disagree with OGSM's view that our recommendations to annually survey a statistical sample of exporters' sales documents would not be useful in helping to determine whether the sales were contingent on CCC credits. In our examination of selected contracts, we found two instances of cash sales which were later changed to specify payment using CCC credits. We believe that in these instances there was a direct replacement of cash sales by CCC credits. We recognize that the usefulness of examining exporters' sales contracts to help determine additionality has been lessened by the July 1978 change in regulations and agree with OGSM that such a survey might not get to the "root" of the problem of additionality. We believe, however, that it would provide valuable information which OGSM now lacks, including whether or not a firm sales contract existed prior to the application for and granting of CCC credit. In this regard, we note the instance discussed in chapter 6 in which a tallow exporter was granted CCC credit without having a firm sales contract.

CHAPTER 5

ECONOMIC AND POLITICAL EFFECTS

ON PROGRAM OBJECTIVES

CCC credits provide significant economic benefits to major recipient countries; therefore, the Export Credit Sales Program has become important to bilateral political relations. For certain countries, Program decisions have involved formal bilateral government negotiations and consideration of U.S. foreign policy objectives.

There are no statutory prohibitions against providing economic support or seeking foreign policy objectives through the use of CCC credits. Nevertheless, foreign economic needs and political considerations are not included in CCC's statutory authority to "export or cause to be exported, or aid in the development of foreign markets for agricultural commodities." Agriculture officials are concerned about the intrusion of economic support or political considerations into the Export Credit Sales Program's decisionmaking. Emphasis on these secondary objectives, based upon the Justice Department's opinion, might subject the Program to the provisions of the Cargo Preference Act. (See p. 11.)

If the Program was not exempt, at least 50 percent of the financed commodities would have to be transported in U.S. ships, and, according to Agriculture officials, this requirement would raise shipping costs to the point that U.S. exports would be noncompetitive.

Agriculture officials, therefore, have attempted to preserve the commercial nature of the Program by (1) refusing requests for formal government-to-government agreements, (2) insisting that recipient governments pass credit benefits on to private buyers, and (3) resisting the intrusion of secondary economic support and political objectives into Program decisionmaking.

FOREIGN GOVERNMENTS RECEIVE ECONOMIC BENEFITS FROM CCC CREDITS

Foreign governments benefit economically from CCC credits through (1) receiving balance-of-payments support by deferring full payment for imported commodities for up to 3 years and (2) generating resources for domestic budgets through controlling the commodity imports and the internal prices and terms of repayment. In some countries the government, rather than the end consumer, has been the major beneficiary of CCC credits.

Under the Export Credit Sales Program, the foreign importer becomes the credit beneficiary. The value of the CCC credit depends on the difference between the terms of the credit and the alternative means of financing available to the importer. CCC credits have usually carried higher interest rates than those at which CCC has borrowed from the Treasury but have still been generally below international lending rates. Of more importance to the foreign importer, the majority of CCC credits have been extended for the maximum repayment terms of 3 years, as shown below. In contrast, commercial bank financing of agriculture trade is customarily limited to repayment in 6 months or less.

	Fiscal year			
	1977		1978	
Credits	(millions)	(percent)	(millions)	(percent)
Registered, total	$799	100	$1,634	100
Repayable in 3 years	679	85	1,254	77
Repayable in less than 3 years	120	15	380	23

OGSM officials prefer that the benefits of CCC credits be received by private buyers when possible; however according to a 1977 Agriculture study, most of the importers that received CCC credits were foreign government agencies or were operating under fairly strict import and foreign exchange regulations. The study estimated that less than 5 percent of CCC credits were extended directly to private importing firms that acted virtually as independent agents. An OGSM official advised us that this estimate was wrong, but he was unable to provide a better estimate.

Recent credits for Korea and the Philippines demonstrate how governments can use CCC credits to support domestic budgets.

1978 Korean credit for wheat and corn

In April 1978, Korea's Economic Planning Board requested CCC financing of wheat and corn on 3-year repayment terms. The request cited an urgent need to continue domestic grain price supports and stated that the government's Grain Management Fund had incurred a gradually increasing deficit due in part to a bumper 1977 rice crop. The Board proposed to replenish the Fund by allocating to it a share of the counterpart or domestic funds generated by the sale of U.S. agricultural commodities imported under CCC credits.

On May 3, 1978, OGSM representatives met with a Korean Government official and worked out an arrangement to continue the U.S. monopoly on Korean purchases in exchange for an additional line of CCC credit for wheat and feed grains (including corn) purchases totaling $170 million. The credit was to be repaid over a 3-year period instead of the 1-year terms previously provided for CCC-financed purchases of these grains. Although it was agreed that the Korean Government would control the credit, OGSM felt that it had assurances that purchases would continue to be made by private Korean buyers and that the government would pass on meaningful benefits of CCC credit terms to these buyers, presumably 1-year repayment terms. OGSM approved the credit on May 12, 1978.

OGSM later learned that a Korean Government agency would import the commodities and resell them to end users on repayment terms of 90 days or less. OGSM protested this arrangement and raised the issue of government siphoning of credit benefits in negotiations for 1979 credits.

Korean assurances on use of 1979 credits

During November 1978 meetings on fiscal year 1979 credits, Agriculture officials indicated a willingness to extend 3-year repayment terms for all commodities financed under CCC credits, with the understanding that the same terms would be extended directly to Korean buyers. The Korean representatives requested 3-year terms but proposed that the Government of Korea decide what terms would be extended to Korean buyers. The issue was not settled during the meetings.

Korean officials, disappointed by Agriculture's insistence that credit benefits be passed on to private buyers, intimated they would diversify Korea's sources of agricultural imports. In December 1978, the American Embassy in Seoul suggested a compromise to Agriculture of a 1 to 2 year phaseout period before the Korean Government would lose the domestic budget benefits of CCC credits. Agriculture persisted in its position, and in late December 1978 it received written assurance from the Korean Government that the full benefits of the CCC credit repayment period for fiscal year 1979 would be extended directly to Korean buyers. The Korean

Government made no commitment on other internal payment terms, such as price, interest, and other charges, which private buyers would have to pay, thereby retaining considerable latitude to generate domestic budget support through control of CCC credit. Furthermore, the written assurance clearly stated that it did not apply to the $170 million credit granted in May 1978 for wheat and feed grains. Korea intended to continue using the local currency generated under this credit for domestic budget support of its Grain Management Fund.

Philippine credits

For a number of years, the Philippine Republic has used CCC credits for domestic budget support. A response to a 1970 Department of Agriculture survey stated that the Philippine Government received the major benefit from CCC credits for wheat, cotton, and tobacco by means of special charges and shorter repayment terms imposed on private buyers. Such practices continued in 1978.

According to a January 1978 newspaper article, the Philippine National Grain Agency imported wheat under a 3-year CCC credit and resold it to domestic millers at substantially higher prices and shorter repayment terms. The newspaper article triggered a Department of Agriculture audit review; the auditors found no apparent irregularities in the CCC financing of these wheat sales but concluded that the Philippine Government, not the millers and general population, was the beneficiary of the CCC credit. In their opinion, the use of sales proceeds by the government should have been of legitimate concern to OGSM because the Program was not intended as a moneymaking source for foreign governments.

We found that OGSM is concerned about the Philippine use of CCC credits, but this concern is somewhat ambivalent. The reported response of an OGSM official to the Philippine wheat transactions was that the terms of resale and any ensuing profits were internal matters for the Philippine Government. However, OGSM documents concerning cotton and tobacco purchases indicate concern over government siphoning of the advantages of CCC credit by means of the Development Bank of the Philippines, which required textile mills and tobacco manufacturers to pay for CCC-financed imports on shorter repayment terms and at higher interest rates than those of the CCC credits.

On October 31, 1978, OGSM announced CCC credits of $50 million in fiscal year 1979 for the Philippines. The credit line was established on 360-day repayment terms, thereby avoiding an International Monetary Fund restriction on new 1 to 5-year debts. Eligible commodities included wheat, $24 million; feed grains, $4 million; soybean meal, $10 million; and tobacco, $12 million.

According to a report from the Agricultural Attache in Manila, beginning with fiscal year 1979, tobacco manufacturers would receive the full benefit of the terms of the CCC credit for tobacco since the Philippine Development Bank would not be involved in these purchases. Of the other eligible commodities, only wheat sales of $20.1 million were registered as of May 8, 1979, and, as in the past, the Philippine National Grain Authority arranged these wheat purchases. OGSM had no information on the terms under which the Authority resold the wheat to domestic millers. Therefore, we could not determine whether the benefits of the CCC credits were passed through to the millers. Nevertheless, unlike the situation in Korea, we found no evidence that OGSM requested or received Philippine assurances that the millers would receive the full benefits of the credit.

DECISIONS ARE INFLUENCED BY POLITICAL CONSIDERATIONS

Recent Export Credit Sales Program decisions on credits for the two largest recipients, Korea and Poland, have been subject to formal bilateral government negotiations. Because of the political considerations, the Department of State has sought to influence Program decisions in these and other countries and had a major role in establishing the Program level for Poland for fiscal year 1979.

Korea negotiations

In November 1977, the Korean Minister of Economic Planning wrote to the American Embassy in Seoul requesting a long-term supply agreement for future purchases of wheat, corn, soybeans, and cotton under Public Law 480 and CCC credits. The American Embassy recommended approval of the request on the grounds that such agreements would serve U.S. commercial, economical, and political interests. The Department of State responded that, although Korea was a valued customer of U.S. agricultural commodities, it was not U.S. practice to enter into long-term binding agricultural commodity agreements.

As discussed on page 38, the Korean Minister in April 1978 requested a government-to-government agreement for CCC financing of wheat and corn on 3-year repayment terms. An informal agreement on the amount and use of the credit was reached in subsequent negotiations, and OGSM announced the $170 million credit in May 1978.

In late July 1978, the Government of Korea requested CCC credits for 1979 imports of wheat, feed grains, cotton, and tallow. A high-level meeting was arranged to discuss the request, and on November 21 and 22, 1978, the first United States-Republic of Korea Conference on Agricultural Credit was held in Washington, D.C. The Koreans requested $525 million in CCC credits for fiscal year 1979. The United States responded that most of the CCC budget was already committed and, therefore, only about $400 million could be provided, consisting of $170 million in new credits and approximately $230 million in credits which had already been announced for Korea. In addition, the United States offered $125 million to $150 million in coverage under the Non-Commercial Risk Assurance Program (GSM-101). As discussed previously, a major issue at the conference was whether the terms of the CCC credits would be passed on to private Korean buyers. The 2-day conference closed with a Korean agreement to consider the U.S. offer and a mutual agreement to hold further consultations in Seoul in mid-December 1978.

Scheduling difficulties precluded the proposed December meeting. Nevertheless, in late December, the Korean Government formally accepted the U.S. offer and in its written acceptance provided assurance that private Korean buyers would receive the full benefit of the repayment period of the new credits. The government also expressed no interest in use of the Non-Commercial Risk Assurance Program for 1979 imports.

On January 5, 1979, the Department of Agriculture announced the establishment of the new $170-million line of credit for Korea.

<u>Polish negotiations</u>

The decision concerning fiscal year 1979 credits to Poland began with bilateral negotiations in July 1978 and ended on January 5, 1979, with public announcement of $200 million in CCC credits on 3-year repayment terms and $100 million in coverage under the Non-Commercial Risk Assurance Program. The decisionmaking included two formal government-to-government conferences and an unprecedented high-level U.S. interagency review.

The Polish request for credits was first presented during the July 10 and 11, 1978, meetings of the United States-Polish Joint Working Group on Development of Agricultural Trade. On August 25, the Polish Embassy in Washington formally requested $500 million to $550 million in credits for various commodities. In late September, $200 million in credits was approved and announced. On November 7, the Joint Working Group met and the United States advised that a decision would be made shortly on the approximately $300-million balance.

In considering the Polish request, the Department of Agriculture faced a budget allocation problem. The fiscal year 1979 budget was $1.5 billion, but carryovers from 1978 plus new lines of credit totaled about $980 million by the end of October 1979. Against the balance of about $520 million, Agriculture had Poland's request for $300 million, Korea's request for about $525 million, and requests from other countries for lesser amounts. The country allocation of the remaining budget became the subject of an interagency review.

On November 1, 1978, the Policy Review Committee of the National Security Council met to discuss CCC credits for Poland. The key issue in this unprecedented meeting was whether Poland should receive approximately the same amount of credit (about $500 million) as was granted in fiscal year 1978. To provide $300 million worth of credit in addition to the $200 million in credit announced in September 1978, Agriculture would have to drastically reduce the budget allocations for Korea and several other countries. In line with its statutory objective of maximizing U.S. agricultural exports, Agriculture preferred to extend up to $300 million in coverage under the Non-Commercial Risk Assurance Program instead of providing additional CCC credit to Poland. The State Department, on political considerations, wanted to grant the full $300 million in CCC credits, thereby keeping the Program at the same level as the preceding year and providing support for the Polish Government. The Treasury Department preferred a mix of new CCC credits and coverage under the GSM-101 program.

As a result of the meeting, a decision was reached to provide Poland with $200 million in additional CCC credit, if the President approved a $100-million budget increase for the Export Credit Sales Program and $100-million coverage under the GSM-101 program.

At the request of the State Department, another meeting was held on December 4, 1978, to allocate the uncommitted balance of the Program's fiscal year 1979 budget. Representatives of the Departments of State and Agriculture and the Office of Management and Budget agreed to country allocations for Poland, Korea, and five smaller participants in the Program.

RESTRICTIONS ON USE OF INTERMEDIATE CREDITS

Recent legislation authorizing intermediate credit financing for agricultural exports contains specific restrictions on the use of these credits.

The Agriculture Trade Act of 1978 (7.U.S.C.A.§ 1707a(b)) authorizes the Department of Agriculture to provide, among other things, intermediate credits for 3 to 10 years to (1) establish foreign commodity reserve stocks, (2) export breeding animals, (3) establish facilities in importing countries for handling, marketing, processing, storing, or distributing imported agricultural commodities, and (4) meet credit competition.

The law prohibits the use of intermediate credits unless the Secretary of Agriculture determines that the financed sale will:

> "(A) develop, expand, or maintain the importing nation as a foreign market, on a long-term basis, for the commercial sale and export of United States agricultural commodities without displacing normal commercial sales; or
>
> "(B) otherwise improve the capability of the importing nation to purchase and use, on a long-term basis, United States agricultural commodities."

The 1978 law further provides that "Intermediate credit financing under this subsection may not be used to encourage credit competition, or for the purpose of foreign aid or debt rescheduling."

CONCLUSIONS

The Export Credit Sales Program provides significant economic benefits to major recipient countries and has become important in U.S. political relations with these countries.

There are no statutory prohibitions against providing economic benefits or seeking foreign policy objectives through the use of CCC credits. Nevertheless, these are not specifically authorized purposes of the Program.

Agriculture officials are concerned about and have resisted the encroachment of economic and political considerations because they fear the Program might become subject to the Cargo Preference Act. They are also concerned when recipient governments fail to pass through the benefits of credits to private buyers or end users. For example, as a condition to fiscal year 1979 credits, Agriculture insisted on and received a written assurance from the Korean Government that the full benefits of the repayment period would be extended to private Korean buyers. Agriculture officials, however, have not been completely successful in their efforts to resist the influence of secondary objectives or to insure a complete pass-through of credit benefits to end users.

We believe there is a need to reaffirm the basic Program objective of foreign market development. There is also a need to insure that foreign end users, not their governments, receive the full benefits of CCC credits.

RECOMMENDATIONS

We recommend that the Secretary of Agriculture direct the Office of the General Sales Manager to:

--Emphasize to the major recipient governments that it is not the purpose of the Export Credit Sales Program to provide economic support of a country's domestic budget or balance of payments.

--Determine whether the economic benefits of CCC credits are being passed through to the end users in recipient countries.

--Seek written assurances from those governments which control the use of credits that they will pass through the full credit benefits to end users.

--Shorten the repayment terms of CCC credits for those countries which continue to maintain significant differences between the terms of CCC credits and the internal terms of payment.

The Congress may wish to strengthen the market development objective of the Export Credit Sales Program. In our opinion, certain statutory restrictions against providing intermediate credit financing are also consistent with the objectives of this shorter-term Program. Application of these restrictions should assist the Office of the General Sales Manager in restricting credits to countries and amounts which could be justified on market development grounds. Specifically, we believe that credits should not be provided unless there is a positive determination that they will develop, expand, or maintain long-term foreign markets without displacing commercial sales and that credits should not be provided for the purpose of foreign aid or debt rescheduling.

We recommend, therefore, that Congress amend the Food for Peace Act of 1966 to add restrictions to the Export Credit Sales Program similar to those provided by the Agricultural Trade Act of 1978 for intermediate credit financing of agricultural exports.

AGENCY COMMENTS AND OUR EVALUATION

OGSM, State, and Agriculture's Office of Inspector General agreed in principle with our recommendations about assuring that the economic benefits of CCC credits are passed through to end-users, whom OGSM defined as the actual buyers and not the ultimate consumers. OGSM, however, did not state that it would take any of the specific actions we recommended.

Agriculture's Office of Inspector General added its view that legislative changes would be required to implement the recommendation that OGSM shorten the length of credits to countries which maintain significant differences between the terms of CCC credit terms and internal terms of payment.

OGSM, elaborating on its policy of who should receive the benefits of CCC credits, stated that:

> "* * * our concern is not necessarily with the ultimate end-user * * * It has been and remains the policy of the GSM [General Sales Manager] to assure that the benefit of the financing goes to the person making the decision to buy U.S. agricultural commodities in preference to agricultural exports from competitors of the United States.
>
> "In an increasing number of countries, the Government--or a Government-buying agency--is the buyer and the one that makes the decision.

The only countries where problems have been encountered in getting the benefits to the buyers have been Korea, the Philippines and Indonesia."

In other words, OGSM uses credits to influence the buyer--government, government agency, or private--to purchase U.S. commodities. It appears to be of little concern to OGSM whether the benefits of the CCC credits are passed on to the end users or final consumers of the commodity. OGSM has objected to government siphoning of the credit benefits in countries and for commodities where private importers or buyers exist (in Korea, wheat and corn and in the Philippines, cotton and tobacco), but does not appear to question the pass-through of benefits where no private importers or buyers exist (in Poland, all commodities and in the Philippines, wheat). Judged from the viewpoint of making a sale, OGSM's position seems pragmatic. However, from the viewpoint of market development, we believe OGSM should be concerned whether the benefits are passed through to the end user or ultimate consumer.

Concerning its efforts to assure that private buyers and not the host governments receive the benefits of CCC credits, OGSM said that "After long and tough negotiations, OGSM was finally successful in getting Korea to agree to pass the <u>full benefits</u> of CCC financing to the buyer". (Underscoring supplied.) As we stated, the Korean Government only promised in its December 1978 letter that the full benefits of the repayment period would be extended directly to Korean buyers; it made no commitment on the other internal payment terms, such as price, interest, and any other charges which private buyers would have to pay.

OGSM also claimed that in the Philippines CCC had attained the objective of assuring that private buyers of cotton and tobacco received the full benefits of CCC financing by limiting the repayment terms. Contrary to this claim, the record shows that the Philippine Government asked for 360-day repayment terms on fiscal year 1979 credits, thereby avoiding an International Monetary Fund restriction on new 1 to 5 year debts. As stated in our report, the Agricultural Attache in Manila reported after the announcement of the credit that, beginning with fiscal year 1979, tobacco manufacturers would receive the full benefit of the CCC terms since the Philippine Development Bank would not be involved in these purchases. Cotton was not eligible for the 1979 credit line and the Attache made no mention of any change in Philippine policy on cotton imports.

The Department of State objected to our discussion of the bilateral negotiations on Korean and Polish credits and the influence of economic and political considerations on Program decisions. State said that bilateral negotiations were necessary in these cases and that it was not clear how the CCC Program was adversely affected. It expressed concern that criticism of other agencies' involvement in the CCC decisionmaking might weaken CCC's ability to make sound, informed decisions on credit allocations. State felt that the Program would be improved through more frequent consultations with other agencies, either individually or through an expansion of the advisory role of the National Advisory Council on International Monetary and Financial Policies. If the Council's role was expanded, State suggested that the Council review all proposed CCC credit lines, not just a portion of those involving foreign bank letters of credit. State further proposed that CCC should provide at least 7 days for review of credit proposals before they were taken before the Council.

The Department of the Treasury also believed the Program would be improved if Agriculture sought more advice from Treasury, State, Commerce, the Export-Import Bank, and the Federal Reserve System.

Our evaluation

Our discussion of the formal bilateral government negotiations concerning CCC credits for Korea and Poland is not intended as criticism per se of these negotiations. Instead, it is intended to demonstrate the point that the CCC Program, while it is not a government-to-government program, has become subject to bilateral negotiations in the major recipient countries of Korea and Poland because of its economic significance and therefore, importance, in bilateral political relations. Furthermore, we believe that the National Security Council's meeting on CCC credits for Poland and the December 1978 interagency meeting to allocate the uncommitted balance of the fiscal year 1979 budget were significant departures from the traditional method of establishing credits and opened the decisions to the influence of secondary economic and foreign policy considerations.

We agree with Agriculture that the development of foreign markets is and should be the primary Program objective. We also share some of the concerns of Agriculture officials about the recent intrusion of secondary considerations on Program decisions. We do not recommend, as State suggested in its comments, the elimination of economic and political considerations from Program decisionmaking. In fact, we believe that this probably would be impossible and unrealistic. We do believe, however, that the Program needs a stronger market development emphasis, and our recommendations are aimed at improving planning and analysis and reaffirming the Program's primary objective of foreign market development.

We did not specifically review the National Advisory Council's advisory role and influence on the CCC Program and therefore have not reached any conclusion as to whether its role should be expanded. We agree in principle with Treasury's comment that the National Advisory Council "forum is the appropriate way to coordinate the U.S. Government's international financial policy." We also agree in principle with the statements by Treasury and State that members of the Council have expertise and resources which could benefit the CCC Program.

With regard to the mechanics of the Council review, Agriculture since 1973 has had an understanding with the Council that it need not submit proposed credits for review unless the credits involve a foreign bank letter of credit for longer than 12 months or more than $4 million. Under this guideline, the Council does not review a number of proposed credits. For example, the fiscal year 1979 credits of $50 million for the Philippines and the $23 million in tobacco credits for Australia, New Zealand, and the United Kingdom were not submitted for review because they were established on the basis of 100 percent U.S. bank letters of credit. Considering the size of some of the credits not being reviewed, we believe, in line with State's suggestion, that the Council should review all proposed credits, that it would be appropriate for the Council and Agriculture to reexamine their understanding about which proposed credits should be reviewed. Similarly, the Council and Agriculture might assess State's proposal that the Council receive information on proposed credits at least 7 days before they are presented to the Council.

Only OGSM and the Foreign Agricultural Service specifically commented on our recommendation that Congress consider amending the Food for Peace Act of 1966 to add restrictions to the Export Credit Sales Program similar to those provided by the Agricultural Trade Act of 1978 for intermediate credit financing of agricultural exports. The Foreign Agricultural Service concurred with this recommendation, agreeing that it would reaffirm the market development objective of the Program and reduce the influence of foreign economic and political considerations on Program decisions. OGSM had no objection to the recommendation but added that, if Congress acted favorably on it, the legislative language should allow for some flexibility.

Chapter 6

IMPROVEMENTS NEEDED TO ASSURE PROGRAM COMPLIANCE WITH ADMINISTRATIVE REGULATIONS

The Export Credit Sales Program is financed in accordance with the GSM-5 regulations. Exporters are generally complying with the regulations, but some areas need improvement. We also noted some questionable practices used extensively by the exporters without adequate explanation.

In our opinion, improved management procedures are needed and should be implemented to assure better administration of the Program.

REGISTERING AND CONFIRMING SALES AND DISBURSING FUNDS TO EXPORTERS

In reviewing files for 48 randomly selected financing agreements, we found that sales are generally registered by exporters in accordance with the 16 requirements set forth in the GSM-5 regulations and then properly confirmed by OGSM. All 48 requests met at least 12 of the requirements. Requirements not met are shown below.

Requirements not met	Number of requests not in compliance
Name of U.S. bank confirming loan	43
Month that documents will be presented for payment	31
Level of tolerance for variance of quantity shipped	29
Statement that agreement is contingent upon resale (note a)	1

a/Required only when the commodity will be sold through an intervening purchaser.

In our opinion, the absence of the required data on the registrations was not sufficient to reject these requests since the data could be derived from the requests or from other available documents. For example, when the month for payment was not indicated, the date of delivery usually was stated, which would indicate when the documents would be submitted for payment. When the name of the confirming U.S. bank was omitted, the name of the foreign bank issuing the letter of credit was indicated on the request application. Also, we noted that OGSM routinely allows a 5-percent deviation from the approved dollar value and quantity and does not reject the request when the tolerance level is not stated.

Confirmation that a sale is registered and that financing is available occurs when OGSM mails a copy of the financing agreement to the exporter. We found no indication that exporters were not being notified, since the agreement files we reviewed all contained copies of the financing agreements. Additionally, all of the exporters we interviewed had been notified about their requests. However, several exporters were concerned that too much time elapsed from the submission of requests to register sales until they were actually notified of the results. We found that it took OGSM 3 to 28 days to process an exporter's request to register a sale whereas many exporters felt they should be notified within 48 hours.

Before funds can be disbursed to the exporter, CCC must receive (1) a Combined Application for Disbursement, Assignment of Account Receivable and Certification, and (2) supporting documents, including the sales invoice, bank obligations, and bill of lading evidencing export. For the agreements we examined, all required documents had been provided and no payments had been made before the required documents were submitted. The majority of the exporters believed that the administrative procedures for the Program were relatively uncomplicated and that the required documents were easy to provide. However, several exporters did complain that, as a result of the Agricultural Stabilization and Conservation Service disbursement process, delays are experienced in receiving payment after submitting the documents.

CGSM is notified when agreements cannot be fulfilled

Exporters are required to notify OGSM when they are unable to fulfill their obligations under an agreement. We found that exporters generally comply with this requirement. Our sample included four agreements, totaling $2.6 million, which had been canceled by the exporters. In each case, the exporter notified OGSM within 2 months from the agreement approval date; however, reasons for the cancellations could not be determined from the records or by OGSM officials.

In our opinion, while cancellations do not appear to be a serious problem, OGSM should seek reasons for them.

COUNTERPRODUCTIVE MANAGEMENT PRACTICES

GSM-5 regulations permit financing agreements to be amended if the amendments are in the interest of the CCC. Exporters make extensive use of the admendment process, and OGSM does not attempt to verify the reasons for such amendments. Also, a recent change in the GSM-5 regulations (see ch. 4) permits the registration of sales contracted prior to the approval of a country line of credit. In our opinion, the extensive use of amendments and the change in the regulations do not provide management with adequate control to assure proper implementation of the Program and to assure that Program objectives are being fulfilled.

Minimal efforts made to verify reasons for amendments

Possible amendments include extension of delivery or export periods and increase in value of the registered sale as long as the quantity is within the allowable tolerance range. For example, deliveries must be made within the period stated on the financing agreement or the agreement becomes invalid. However, if delivery is delayed for causes beyond the control of the exporter, the period may be extended.

Of the 48 financing agreements reviewed, 37 contained at least one request to amend the original agreement and only one request was not approved. Of 53 total amendments, 29 either increased or decreased the value of the agreements, 16 extended the delivery dates, and 8 changed the confirming bank. In many cases, OGSM was given no reason for the amendments; even when reasons were given, no attempt was made to verify them. For example, exporters often requested amendments because of shipping difficulties due to late arrivals or slow carrier loading, but OGSM never attempted to substantiate whether the carriers were in fact late or had problems in loading. Furthermore, OGSM was never given or sought reasons why four agreements were completely canceled.

ENTRY DOCUMENTS NOT SUBMITTED PROPERLY

Regulations require that, when financing will exceed 12 months, exporters must provide OGSM with documents within 90 days after shipment from the United States substantiating that commodities have entered the foreign countries. The documents must identify the commodity and quantity shipped and the date of entry into the designated country and be signed by a customs official, the importer, or an independent representative. However, the quality of the commodity does not have to be stated.

We reviewed 42 shipments requiring entry documents and found that they were provided for only 20 shipments. Documents for 3 of the 20 shipments were submitted more than 90 days after the delivery of the commodity. OGSM officials stated that the followup for nonsubmission of documents receives a low priority in relation to their total workload; however, they said they would be assigning a staff member full time for this purpose.

We reviewed selected agreements at the exporters and found that entry documents, when required, had usually been obtained and had subsequently been provided to OGSM. A number of exporters stated that they had experienced problems in obtaining documents from some importers.

Although OGSM is increasing its efforts to obtain entry documents, it has not attempted to physically verify receipt of the commodities in importing countries.

The available records did not indicate any diversions, but we believe that improved management procedures are needed and should be implemented to assure better administration of the Program.

CONCLUSIONS

Exporters generally comply with the GSM-5 regulations; the primary deficiency in compliance is OGSM's failure to assure proper submission of entry documents. Under the GSM-5 regulations, only those commodities with financing terms of more than 12 months are subject to this requirement. Agriculture officials told us that there is no effort by either their auditors or the Agricultural Attaches to verify that commodities are received in the designated country.

We did not attempt to verify that the commodities were actually received in the designated country, and the available records did not indicate any diversions. However, we believe that the integrity of any control system rests on compliance with its regulations. The current procedure of excluding from controls the commodities financed for 12 months or less creates a double standard, which raises questions about the importance of the requirement at all. We also believe that the absence of a physical verification procedure implies a weakness in the controls needed to assure compliance. A verification procedure will not eliminate diversion, but it would reduce that possibility and insure that commodities are shipped and received in the proper quantity and quality.

Additionally, in our opinion, exporters make excessive use of the amendment process and OGSM's approval of amendments appears to be the rule rather than the exception. We believe the reasons for amendments should be verified.

RECOMMENDATICNS

We recommend that the Secretary of Agriculture direct the Office of the General Sales Manager to:

- --Ensure that entry documents are properly submitted.
- --Amend GSM-5 regulations to require entry documents for all shipments, including those for commodities financed for 12 months or less.
- --Establish amd implement procedures to physically verify on a selected basis the entry of commodities into the designated country.
- --Develop and implement procedures, including examination of sales contracts and other pertinent documents, to verify exporters' reasons for requesting amendments before approving these amendments.

AGENCY COMMENTS AND OUR EVALUATION

Submission of entry documents

The Office of the General Sales Manager agreed that an entry document should be submitted within 90 days from the date of shipment unless the exporter is unable to obtain the document for reasons beyond his control.

We reviewed 42 shipments requiring entry documents and found that the documents were provided for only 20 shipments. OGSM pointed out that since then all entry certificates have been received and stated that it now has one person working on this matter and has established internal controls to send reminder notices when the entry certificates are not received.

<u>Amend regulations to require entry documents for all shipments and physically verify entry of commodities</u>

OGSM objected to our recommendations to require entry documents for all shipments and to establish and implement procedures to physically verify the entry of commodities into the designated country.

At this time, OGSM stated, it is unsure whether the entry certificate requirement should be maintained for financing agreements with 24 or 36-month credit periods. OGSM stated that the requirement was added after a problem of diversion had occurred under the Barter Program but that no diversion had ever occurred under the CCC Export Credit Sales Program.

Whether diversions have in fact occurred is unknown. We note that neither Agriculture auditors nor the Agriculture Attaches have tried to verify that commodities are received in the designated countries. Also, as the Office of Inspector General stated in its comments, it does not specifically test whether the commodities financed under the Program are received but discusses and tests as deemed necessary all Agriculture program activities during regular audits. It has not identified instances of non-receipt of commodities. Furthermore, it did not disagree with our comments on physical verification; however, it believes the need for formal procedures should be closely examined in view of the low priority it would establish for this effort.

Apparently, we had unintentionally implied that there should be physical verification of entry for every shipment. It was our intent that verifications be carried out by the Agricultural Attaches and auditors on a selected basis. The Foreign Agricultural Service raised no objections to this recommendation.

We still believe it is desirable to obtain assurance that commodities are shipped and received in the designated country. Verification would provide assurance that commodities are not being transshipped to cash markets or countries where CCC intended to permit only shorter credit terms.

Require entry certificates to verify quality of commodities

OGSM believed that our recommendation to require entry certificates to verify the quality of commodities would be an onerous requirement and that it would be unreasonable to expect foreign customs officials, who usually fill out certificates, to establish the quality. We are concerned that the quality of CCC-financed commodities meet the foreign customers' specifications. However, we agree with OGSM that our recommendation would be too dificult to implement and, therefore, we have deleted it.

Develop and implement procedures to verify exporter's reasons for amendments

In general, OGSM agreed with the spirit of our recommendation that it should not arbitrarily accept all amendment requests. However, OGSM opposes any controls in the amendments procedure which are likely to cause unnecessary delays in financing export sales.

The enactment of our proposals to develop and implement procedures, including examination of sales contracts and other pertinent documents, to verify reasons for requesting amendments could help to prevent the future occurrence of problems, such as OGSM noted on credits extended to Korea for tallow.

OGSM commented that it required one tallow exporter to furnish evidence of sales because it believed that tallow exporters were filing requests for financing before firm sales had actually been made. We were advised that the procedures to register tallow sales were changed for fiscal year 1979 in response to an exporter's complaint that another exporter actually registered a sale without a contract and used the entire credit line of $4 million. The details of this instance were as follows.

On May 9, 1978, a request was made to have OGSM establish an additional $4-million line of credit for tallow to be delivered to Korea through September 1978. On May 19, OGSM announced the establishment of the new $4-million line of credit. Less than 30 minutes later, an exporter requested by telex registration of a sale for the entire credit. It provided OGSM a contract number as required by regulation, but our examination of the supporting documents showed that no contract existed.

This line of credit, when announced, specified that delivery be completed by August 31, 1978. This was later amended as the exporter requested that the delivery date be extended. There were at least 6 requests for amending the delivery date, none of which stated a reason. The last approved amendment requested that the delivery period be extended to January 15, 1979. This request was received by OGSM after the expiration date of the financing agreement.

Subsequent to the above incident, OGSM required that all requests for registration of tallow sales be supported by copies of the contracts specifying the amounts and unit prices for each sale.

Nonetheless, to avoid the possibilities that some funds approved under a financing agreement might not be used and that a single exporter could tie up funds at the expense of other exporters without having a firm sale, we believe that OGSM should develop and implement procedures to verify exporters' reasons for amendments. Such procedures should not be so cumbersome as to substantially delay the present approval process but should provide OGSM with adequate assurance that amendments serve the best interests of the Program.

Other comments

OGSM commented that many exporters telephone OGSM prior to sending their cables and that it tells the exporters that funds are assigned to them under a credit line pending receipt of their cables. The exporter is given a financing agreement number which it can send to the bank issuing the letter of credit. We were advised after meeting with OGSM officials that this procedure needed clarification. The officials stated that telephone registration is not an official approval but only serves to inform the exporter that an existing credit line is open and that funds are available. Actual receipt of a written request to register a sale is necessary before OGSM can officially assign funds.

In regard to our analysis that it took OGSM as long as 28 days to process a financing agreement, OGSM said that these statements could mislead the reader concerning the speed and efficiency of its operations and that one should not imagine that the typical exporter is waiting impatiently for OGSM to approve its financing agreement.

OGSM stated, and we concur, that the average processing time for the agreements sampled was actually 6 business days. The average number of calendar days was a little over 9 days. As noted on p. 51 the majority of the exporters believed that the Program's administrative procedures were relatively uncomplicated. However, on the subject of notification, many exporters felt they should be notified within 48 hours.

COMMODITIES ELIGIBLE FOR FINANCING UNDER THE EXPORT CREDIT SALES PROGRAM (note a)

Barley

Breeding cattle

Breeding swine

Yellow corn

Cotton

Cottonseed meal

Cottonseed oil

Linseed oil

Linseed meal

Complete-mixed feed (containing at least 85 percent eligible commodities)

Oats

Peanut oil

Potatoes (including seed potatoes)

Dehydrated potatoes

Protein concentrates (containing at least 75 percent eligible commodities)

Rice

Sorghums

Soybeans

Soybean meal

Soybean oil

Edible soy-protein

Sunflowerseed meal

Sunflowerseed oil

Tallow

Tobacco

Wheat and wheat flour

a/As of May 3, 1979.

COUNTRIES THAT RECEIVED FINANCING UNDER THE EXPORT CREDIT SALES PROGRAM March 30, 1956 to September 30, 1978

	(thousands)
Algeria	$ 2,859
Angola	1,076
Australia	32,876
Austria	354
Bahamas	7
Belgium	26,044
Bolivia	31,711
Brazil	25,573
Cameroon	34
Chile	105,980
China, Republic of	19,898
Colombia	1,202
Costa Rica	153
Cuba	695
Cyprus	21,342
Czechoslovakia	8,927
Denmark	10,039
Dominican Republic	30,619
Ecuador	4,105
Egypt	123,405
El Salvador	872
Finland	$ 257
France	7,627
Germany	89,926
Ghana	7,399
Greece	305,015
Guadeloupe	273
Guatemala	10,838
Guinea	276
Haiti	13,751
Honduras	1,372
Hong Kong	9,822
Hungary	5,827
Iceland	428
India	13,895
Indonesia	67,458
Iran	82,325
Ireland	39,637
Israel	3,338
Italy	83,170
Jamaica	4,144
Japan	424,882
Jordan	4,669

	(thousands)
Korea	$1,290,189
Kuwait	104
Lebanon	31,703
Liberia	6,261
Libya	779
Malaysia	13,613
Malta	1,163
Mexico	23,022
Morocco	95,727
Mozambique	154
Netherlands	50,402
Netherlands Antilles	2,129
New Zealand	21,530
Nicaragua	2,800
Norway	29,721
Pakistan	250,758
Panama	621
Philippines	342,524
Peru	333,887
Poland	1,086,977
Portugal	345,900

	(thousands)
Romania	$181,162
Saudi Arabia	18
Senegal	1,798
Somalia	201
South Africa	95,861
Soviet Union	549,693
Spain	33,207
Sri Lanka	14,894
Sudan	31,054
Sweden	1,600
Switzerland	328
Syria	6,911
Thailand	90,893
Trinidad-Tobago	622
Tunisia	23,695
United Kingdom	240,064
Uruguay	840
Venezuela	5,924
Yugoslavia	187,747
Zaire	27,222
TOTAL	[a]$7,047,827,000

a/Figures may not add due to rounding.

United States Department of Agriculture
Office of the General Sales Manager
Washington, D.C. 20250

TO: J. K. Fasick, Director
International Policy, GAO

FROM: Fred Welz, Acting General Sales Manager
Office of the General Sales Manager

SUBJECT: OGSM Response to GAO Audit ID-79-44

Our general reaction to the GAO audit of the CCC Export Credit Sales Program (GSM-5) is in agreement with the general tenor of the study, but in disagreement with some of the specific elements of analysis and proposals for change.

We actively support GAO's contentions that the primary goal of the program should be market development, that allocation of funds must be planned, that CCC credit sales should not displace other commercial sales, and that control procedures must be maintained to ensure that the goals of the program are being realized.

Our disagreements with the audit come on certain specific points, often concerning your interpretation and analysis of the way our program operates. We have attached a detailed response to your recommendations. Often the report has mistaken simplicity and flexibility for lack of planning and control. The GSM-5 Program works and works well, partly because of its simplicity. Instead of trying to impose a tangle of administrative controls on the market, we respond to the needs of the market, the exporters and the foreign importers.

We feel that some parts of the report were too optimistic about the possibility of quantifying and applying concepts such as additionality, market shares, target levels, etc. to decisions which must be made with speed and flexibility. Some controls which you wish to apply to our sales registrations procedures have been tried and abandoned in the past because we found that they hamper the purpose of our program. Other solutions which you propose have contributed to administrative problems in other U.S. Government programs. In some cases, as we have pointed out in our detailed response, the report did not take into account the essential controls existing in our operations but instead proposed solutions which would either hamper our operations or add nothing to them.

In spite of our objections to certain specific elements of analysis in the GAO study, we agree basically that additional information could be put into our planning effort, that Congress could reaffirm the goal of the short-term credit program, and that commodities and countries should be chosen for financing with the overriding goal of maintenance and expansion of U.S. agricultural export markets.

Attachment

SPECIFIC RECOMMENDATIONS ON LACK OF COUNTRY-COMMODITY PRIORITIES - CHAPTER 3

Recommendations - (a) Establish commodity and country priorities for export activities, (b) Develop specific overall U.S. market share goals for high priority commodities and countries, and (c) Establish target levels within these overall goals for the Export Credit Sales Program.

Comment - The GAO report suggests that the Export Credit Sales Program lacks specific commodity and country priorities and market share goals. At the beginning of the fiscal year, OGSM allocates most of its budgeted funds to specific commodities and countries by weighing the relative merits of applications for credit. Requests for the establishment of credit lines come from private foreign importers, foreign governments or U.S. exporters. The requests, which are channeled principally through our world-wide network of FAS agricultural attaches, far exceed the available budgeted funds. Before the beginning of the fiscal year, agricultural attaches are encouraged to submit specific requests or inform us of potential opportunities to increase U.S. exports.

Although we feel that it is more efficient to respond to actual requests rather than to guess who might be persuaded to accept CCC credit, we would welcome any information which could aid our analysis in establishing credit lines. In 1978, the Planning and Evaluation Division of FAS began to prepare Long Range Strategic Marketing Plans for individual countries. Currently, the staff assigned to these studies is being increased. We would be happy to have as much input from this area as staffing and resources permit.

We feel that any such studies would be most usefully developed in long-range terms. In contrast, a rigid and time-consuming administrative process to set mandatory priorities would not serve the interests of our program. Our current program works well because it is simple and responds to the market. We feel that our approach would be more accurately characterized as "flexible" rather than "passive."

In general, we are actively seeking additional information from FAS and other sources which could aid our current decision-making process. Market shares, priorities and targets should not be applied rigidly, but could provide a useful overview.

SPECIFIC RECOMMENDATIONS ON COMPETITOR DATA - CHAPTER 3

Recommendations - (a) Establish procedures to assure the systematic collection and analysis of competitor information in order to determine the market development role of the Export Credit Sales Program, (b) Survey U.S. exporters annually to obtain pertinent information, such as foreign credit terms, problem areas, and suggestions for program improvements, (c) Expand annual request to the Agricultural Attaches to include analyses of foreign competition and credit information, and (d) The Economics, Statistics, and Cooperative Service should initiate studies to evaluate the credit aspect of foreign competition, including analyses of the credit terms offered by U. S. competitors.

Comment - The GAO report observes correctly that OGSM's information about foreign competitors' credit terms is limited. Such information as exists, including reports from Attaches and from private exporters, is used when OGSM considers the establishment of credit lines. OGSM would like to know more about interest rates in foreign countries. As noted in the GAO report, we do keep files on this information and we will continue to request and receive such information from our attaches and other sources. Nevertheless, we recognize that this information will never be complete.

The government of the United States is the only government which publishes information about its credit terms on a systematic basis. Information about foreign credit terms from informal sources is often impossible to verify. Neither buyer nor seller has reason to be candid with us; on the contrary, each has cause to deceive us. Most of the larger exporters of U.S. grain also merchandise grain originating elsewhere. Some may have other reasons to be less than fully candid. Thus, we cannot be sure that reported information is either accurate or complete.

We have and we shall continue to solicit such information from our agricultural attaches, and to consider information available from private sources. Some information, however,will always remain incomplete and unverifiable. Consequently, we would caution against giving too much weight to the results of such a survey.

We also would like to address a point made in the text of this section of the GAO report. An allegation was made that U.S. cotton shippers do not feel that the CCC Export Credit Sales Program is necessary. This statement is not consistent with the impression we have from our numerous contacts with the industry. Nevertheless, since the allegation was made, we shall seek the opinion of the American Cotton Shippers Council as to whether CCC credit on cotton shipments to Korea is useful and necessary.

SPECIFIC RECOMMENDATIONS - CHAPTER 4

Recommendations - (a) Reinstate the provision (1488.5, para. (b)) in the GSM-5 regulations which precluded the registration of sales made prior to the date the financing became available, (b) review a statistical sample of exporters' sales contracts each year, to verify whether sales were contingent on the availability of credit, and (c) Establish a formal review system that will assist management in determining whether credits actually increased agricultural sales.

Comment - GAO suggests that in abandoning the policy of accepting only new sales, CCC has begun to lose sight of the goal of market development.

The policy was changed in 1978 because it was seen that it caused bunching up and distortion of markets, caused shipping congestion at ports, and on balance worked against CCC's overall program of price stabilization.

The advantage of refusing to finance forward purchases is that such a policy would seem to be a stronger mechanism for guaranteeing that CCC credit is used not to replace existing sales, but to finance new ones--the concept of additionality. CCC is concerned with the concept of additionality, as one of various major goals. However, CCC's export promotion activities should operate in harmony with its domestic program, which is designed to stabilize agricultural prices in the United States. If we require foreign buyers who use CCC credit to conform their purchases and deliveries precisely to our fiscal year, we create a number of distortions. In particular, the foreign buyers must concentrate their purchases in a short space of time, instead of purchasing when prices are depressed.

For cotton, used as an example in the GAO report, it is not uncommon to have forward purchasing two years before delivery. Such purchases are in line with planning and stability not only in the foreign country, but in the United States as well. Forward purchasing increases the stability of U.S. agricultural commodity prices, benefitting U.S. producers and consumers.

In addition to the goals of price stabilization and development of new export markets, CCC has the goal of maintaining existing markets. This is an essential component of a market development strategy. In the long run, consistent foreign demand is more important to U.S. farmers than erratic one-time sales.

We may return to GAO's example of Korea. Korea has been financing a huge and successful drive for economic development, using foreign credit from CCC and from many other sources. Although it may be true that Korea could be forced to purchase some commodities for cash at given times, the cash might well be generated from other foreign borrowings. It is probable that at the time the Koreans made the purchases cited in the report, they were hoping to obtain financing for them. If the United States refused to supply credit, it is possible that in the long run foreign competitors would begin to offer the credit which the United States refused and U.S. producers would lose markets.

This is not to argue that all U.S. sales to Korea should be financed by CCC credit, but only to show that the concepts of additionality and market development are complex. A narrow short-run view of the concept of additionality could lead to an exaggerated push to develop new markets at the expense of existing ones. The complex issues of market development are considered at length by OGSM prior to the establishment of credit lines.

CCC wishes to work with the commercial markets and facilitate trade. We found that the policy on forward purchasing prior to 1978 was a significant inconvenience to the users of our program. We feel that GAO's recommendation, which would impose a fiscal year, with a rigid beginning and end on all commercial transactions (both purchases and deliveries), is not consistent with our market development program or our price stabilization program.

OGSM recognizes that as a practical matter, specific amounts of additionality cannot be proven or disproven. Some displacement of normal commercial or cash sales is inevitable with CCC credit financing. CCC does not supply credit for sales to Japan, or to many cash markets of Western Europe, where the credit clearly would displace commercial sales. In many other countries, the issue of additionality is more complex.

OGSM does not feel that we will get to the root of the problem of additionality by choosing a sample of exporters' sales contracts and investigating whether the sales were contingent on obtaining financing. Exporters ordinarily do not make contingent sales because they cannot hedge them. Consequently, we do not feel that the proposed review of exporter's contracts will be useful.

To summarize, we agree with GAO that OGSM's overriding goal should be toward market development and we use the concept as our major criterion in establishing credit lines. We define market development as including maintenance of existing markets as well as seeking new sales. We do not feel that it serves the goal of market development to attempt to proscribe forward purchasing and we feel that an investigation of whether specific sales were contingent on financing would not get to the root of the question of additionality.

Also, we feel that an oversimplified attempt to quantify additionality could lead to incorrect policy prescriptions. Nevertheless, the principle of additionality remains fundamental to the success of our goal of market development.

SPECIFIC RECOMMENDATIONS - CHAPTER 5

Recommendations - (a) Emphasize to major recipient governments that the purpose of the program is not to provide economic support of a country's domestic budget or balance of payments, (b) Determine whether the full benefits of CCC credit are being received by end-users in recipient countries, (c) Seek written assurances from governments which control the use of credits that they will pass through the full credit benefits to end-users, and (d) Shorten the length of CCC credits to those countries which continue to maintain significant differences between the terms of CCC credits and the internal terms of payment.

Comment - OGSM feels that the goal of market development should override political considerations in the Export Credit Sales Program and thus we agree with these recommendations in principle. We would, however, like to make some clarifications on the material in the text of the report.

The discussion of the problem of end users should be clarified. We presume that in discussing end users, GAO is referring to the actual buyer, since our concern is not necessarily with the ultimate end user. The purpose of the financing is to increase U.S. export sales. It has been and remains

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the policy of the GSM to assure that the benefit of the financing goes to the person making the decision to buy U.S. agricultural commodities in preference to agricultural exports from competitors of the United States.

In an increasing number of countries, the Government--or a Government-buying agency--is the buyer and the one that makes the decision. The only countries where problems have been encountered in getting the benefits to the buyers have been Korea, the Philippines and Indonesia.

After long and tough negotiations, OGSM was finally successful in getting Korea to agree to pass the full benefits of CCC financing to the buyer. For private purchases of cotton and tobacco in the Philippines, CCC finally attained this objective by limiting the repayment terms. Wheat was not at issue in the Philippines, since a government purchasing agency purchases grains. In Indonesia, this problem has never been resolved satisfactorily. Indonesia has received credit under the program only in 1976 and 1977.

In dealing with foreign governments, CCC must retain a degree of flexibility. We would like to apply standard procedures to all countries, but the purpose of the program is to sell U.S. agricultural commodities, not to antagonize customers. Successful foreign market penetration and successful dealing with foreign governments often requires a posture of negotiation.

SPECIFIC RECOMMENDATIONS TO CONGRESS - CHAPTER 5

Recommendations - Congress should consider amending the Food for Peace Act of 1966 to add restrictions to the Export Credit Sales Program which provide that: --credits should not be provided unless there is a positive determination that they will develop, expand, or maintain long-term foreign markets without displacing commercial sales, and--credits should not be provided for the purpose of foreign aid or debt rescheduling.

Comments - OGSM would like to reaffirm that the major goal of the program has always been to maintain and increase markets for U.S. agricultural exports. We believe the program has achieved a good measure of sucess. While OGSM would have no objection if Congress wishes to write a legislative mandate for this goal for the short term credit program as it has already done for the intermediate credit program, we would observe that the delineation between market development and balance of payments relief is seldom as clear-cut as the GAO report would suggest.

Indeed, if such legislation is proposed, we hope that Congress will recognize that because of rapid fluctuations in demand for U.S. agricultural commodities, it is virtually impossible to make an absolute determination at the time credit is being considered that credit sales will not displace other commercial sales. Therefore, we recommend that if Congress acts favorably on this recommendation, the legislative language should allow for some flexibility. Further, the language should make clear that the concern is for U.S. sales and not those of competing nations.

APPENDIX III

6

SPECIFIC RECOMMENDATIONS - CHAPTER 6

1. Recommendation - Ensure that entry documents are promptly submitted.

   Comment - We agree that entry documents should be submitted within 90 days from the date of shipment unless the exporter is unable to obtain the document for reasons beyond his control. We now have one person giving a great deal of time to this matter and internal controls have been established to send reminder notices when the entry certificates are not received promptly. It should be noted that all entry certificates for all the files sampled by the auditors have been received.

2. Recommendation - Amend GSM-5 regulations to require entry documents for all shipments, including those for commodities financed for 12 months or less.

   Comments - The evidence of entry requirement was added to the CCC Export Credit Sales Regulations after a problem of diversion of shipments to Austria had occurred under the Barter Program. No diversion had ever occurred under the CCC Export Credit Sales Program, but the entry certificate requirement was added as a further safeguard. By requiring entry certificates, CCC wished to prevent the possibility that commodities financed for periods longer than 12 months would be shipped to countries to which CCC intended to permit only 6 or 12 month credit terms.

   Since the institution of the Program in 1956, over $8 billion of agricultural exports have been financed. During this period of time, no diversion of agricultural shipments under the CCC Export Credit Sales Program has ever been uncovered either by program managers or through audits. A letter of credit is always required of the importer, and thus a bank in the importing country always establishes a line of credit for the importer. The importer's interest in the arrival of the shipment and his liability to the bank (and consequently to CCC) through the letter of credit gives us a strong guarantee that we will learn of any failure of the shipment to arrive.

We are reexamining the question of whether the requirement of entry certificates adds significantly to our guarantees that the commodities arrive in the country specified in the financing agreement. Consequently, we are unsure at this time whether the entry certificate requirement should be maintained for financing agreements with 24 or 36 month credit periods.

Also, CCC wishes to comply with Section I of Presidential Executive Order 12044, dated March 23, 1978, which states in part that program regulations: "...shall not impose unnecessary burdens on the economy, on individuals, on public or private organizations, or on State and local governments." and further states that "...regulations shall be developed through a process which ensures that: ...compliance costs, paperwork and other burdens on the public are minimized."

In view of the above, we feel that it would be inappropriate at this time to extend the entry certificate requirement to financing agreements with 6 and 12 month credit terms.

3. Recommendation - Require entry certificate to verify the quality of the commodities.

   Comment - Entry certificates are usually filled out by a foreign customs official. Therefore, it would be unreasonable to expect the foreign customs official to establish a quality of a grain shipment or other agricultural shipment. Also, in some cases the importing country may not have inspection facilities to determine if the grain actually meets the quality called for in the contract. In most cases, the importer's letter of credit will require an operative statement since the U.S. confirming bank is usually required to review documents such as the weight and inspection certificates to ensure that the quality and grade as called for in the export contract has been shipped to the importer. CCC does not finance the commodity until the operative statement has been received. In addition, we require the exporter to furnish a statement to CCC stating that he has exported the quality of the commodity as called for in his export sales contract. In one instance, CCC was notified by the importer that he had received a lower quality of cotton than what was actually called for in the contract. CCC's investigation of this matter through the cooperation of our Ag Attache disclosed that the importer had a legitimate complaint. As a result, CCC required the exporter to repay the financing plus interest. Upon receipt of payment from the exporter CCC then released the letter of credit that the importer had established in favor of CCC.

   Since serious quality problems are likely to come to the attention of CCC under the present system and since foreign certification of quality would be an onerous requirement, CCC does not feel that this recommendation should be implemented.

4. Recommendation - Establish and implement procedures to physically verify the entry of commodities into the designated country.

   Comment - The importer in all probability would notify CCC that the goods were not received and any false documents sent by the exporter would be fairly easy to verify. Further guarantee of physical entry, such as providing a U.S. Agricultural Attache to meet every shipment financed by CCC would be a costly and burdensome process. Furthermore, CCC financed shipments go to many countries where no U.S. Agricultural Attache is in residence.

   CCC does not feel that physical verification of entry is feasible for every shipment. However, we would call on Attaches as deemed essential for spot checks in connection with their other travels to port facilities.

5. Recommendation - Develop and implement procedures, including examination of sales contracts and other pertinent documents, to verify exporter's reasons for requesting the amendment before approving such amendments.

Comments - Often amendments are due to factors beyond the exporter's control. Imports are often controlled by a foreign government agency and the agency may arbitrarily change the bank issuing the letter of credit, the importing firm, etc. Verification of the reason for an amendment could involve a notification by a foreign government and would be a time consuming and unnecessary complication. For example, CCC should not be concerned if the exporter wishes to amend the financing agreement to change the name of the bank provided the bank has been approved by CCC to issue letters of credit within its limitations.

In regard to shipping delays, we could ask the shipping company to verify that it is at fault in delays. This could also lead to complications and might cause unnecessary delays in financing the sale. Probably the only time when a shipping delay should be verified carefully would be when it carries the transaction into the next fiscal year since such an amendment could affect the next fiscal year's budget.

In regard to changes in value, a distinction should be made between decreases and increases. Decrease in value within the tolerance often results from not fulfilling the upward tolerance of the export sales contract. Adding too many conditions to the amendment for a decrease could influence some exporters to avoid notifying CCC immediately that all the funds approved under the financing agreement will not be needed. The result could be that residual funds would not be identified and restored to the credit lines for use before the end of the fiscal year.

Increases are examined fairly carefully and the reason for the increases are obtained from the exporter. In some cases sales are made on basis pricing whereby the price will be established at a later date. Depending on how the market reacts after the sale has been made and when the price is established, an increase may later be required.

In general, the purpose of the CCC program is to promote U.S. exports. The establishment of verification procedures for amendments which are time consuming and costly to the exporter or the importer increases the difficulty of trading and works against the purpose of the program. However, this does not mean that CCC should arbitrarily accept amendment requests merely because a request has been made. In fact, CCC has denied requests for an extension of the export period when the exporter is unable to verify if the importer is actually planning to open a letter of credit. Also, on the CCC credits extended to Korea for tallow during the 1979 fiscal year, OGSM required the exporter to furnish evidence of their sales transactions before approving any financing. This action was taken because we felt that requests for financing by exporters of tallow were being filed before firm sales had actually been made. Similar actions have been taken in the past in the case of tobacco credits.

CCC agrees with the spirit of the GAO recommendation that amendments should not be granted without examination, but feels that GAO's analysis should have differentiated the different types of amendments.

CCC does not feel that it is necessary in most cases to require justification when an exporter requests a minor decrease in value or requests a change from one bank to another CCC-approved bank. Such justifications, particularly if they required the submission of documents, would add nothing to the protection of CCC's program and to the extent that they caused delays in shipments or disbursements, would do significant harm to the program. We note that GAO uncovered no losses or harm resulting from CCC's policy on amendments.

CCC does require justification for extension of a shipping date or an increase in the value financed. In cases where there is any reason to suspect the possibility of misrepresentation and damage to CCC's program, CCC can and does require the submission of sales contracts or other documents. Amendments are denied when there is a substantive reason for denial, but the basic purpose of CCC's program is to facilitate exports, not to create unnecessary administrative obstacles to speedy and efficient exportation of agricultural commodities. Consequently, CCC opposes any unnecessary controls in the amendments procedure which are likely to cause unnecessary delays in financing the export sale.

COMMENTS ON STATEMENTS IN THE TEXT OF CHAPTER 6

OGSM would like to reply to several remarks made in the text of chapter six, but not included in the recommendations.

1. Requirements for registration. --GAO's review of 48 CCC financing agreements indicated that the exporter's request did not always include all requirements as set forth in the GSM-5 regulations. As GAO pointed out in their report, the absence of some of this information does not justify rejection of an exporter's request.

   Most of the information required by the regulations is essential to the registration. OGSM will never register a sale where port value, quantity, delivery period, or other essential information is lacking. Nevertheless, there are some elements, such as tolerance of shipments, or use of an intervening purchaser, which are not applicable to every sales contract. Some information is obtainable from other records to which CCC has access. As a matter of policy, we do not deny a request when certain minor elements are not included in the sales registration.

2. Delays in Processing Agreements. --One of the most serious allegations in the GAO analysis was that it took OGSM as long as 28 days to process a financing agreement. This allegation was even more serious when coupled with the implication that the mailed financing agreement was the first confirmation to the exporter that his sale was registered. We feel that these statements could mislead the reader concerning the speed and efficiency of our operation. In reference to the alleged delay, we have reexamined the files which GAO used as the basis of their report and found that such apparent delays were actually the result of modifications to the original registration.

Often an exporter will register a sale with CCC and subsequently notify us that a second bank will issue a letter of credit to cover part of the sale already registered under the first bank. Since ASCS Fiscal accounting procedures do not permit us to approve more than one issuing bank under a single financing agreement, we will issue a new agreement for the amount financed through the second bank and reduce the first agreement by the same amount. Since the date the request is received for financing determines the interest rate, the date of the original request will be shown on the modified agreement rather than the date of the request for modification.

Typically, several days are required from the time that a cable arrives until the financing agreement is signed and sent to the exporter. The cable must be delivered from the mail room, checked over, typed, registered in our record systems, sent to Fiscal Division, ASCS, for approval, sent to the Assistant Sales Manager for his signature, and returned to Program Operations Branch, Export Programs Division for mailing to the exporter. This careful verification procedure is necessary for the processing of the financing agreements. To the Auditor, looking at the original registration date and the date the modified agreement was signed, it appeared as if it had taken OGSM as many as 28 days in one case to process the agreement. The true lapse of time from the date the modification was received until the time the financing agreement was signed was actually six business days which was also the average processing time for those agreements sampled by the auditors.

One should not, however, imagine that the typical exporter is waiting impatiently for OGSM to approve his financing agreement. Even if OGSM could guarantee that every financing agreement would be mailed out within three days of receipt, the system would be too slow for many exporters. Many exporters telephone CCC prior to sending their cable. In the telephonic registration, they are told that funds are assigned to them under the credit line pending receipt of their cable and they are given a financing agreement number which they can send to the bank issuing the letter of credit. Other exporters may send the cable in first and then telephone to verify that the cable has arrived and then receive their financing agreement number.

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Although the report did not include a recommendation to improve our procedures in processing financing agreements, we still feel that this section of the report could be misleading to the readers and wrong conclusions could be drawn by assuming that OGSM was negligent in processing financing agreements on a timely basis. Therefore, we recommend that the report be changed accordingly to include our comments as stated above.

APPENDIX IV

United States Department of Agriculture
Office of the General Sales Manager
Washington, D.C. 20250

AUG 9 1979

Mr. J. Kenneth Fasick
Director, International Division
U.S. General Accounting Office
441 G Street, N.W.
Washington, D.C. 20548

Dear Mr. Fasick:

Enclosed are additional comments on the GAO Report on Export Credit Sales prepared by the Foreign Agricultural Service.

Sincerely,

Kelly Harrison

Kelly Harrison
General Sales Manager

Enclosure

UNITED STATES DEPARTMENT OF AGRICULTURE
FOREIGN AGRICULTURAL SERVICE
WASHINGTON, D.C. 20250

AUG 9 1979

TO: Kelly Harrison
General Sales Manager

FROM: Thomas R. Hughes
Administrator

SUBJECT: GAO Report on Export Credit Sales

This is in response to the GAO Audit of the CCC Export Credit Sales Program (GSM-5). We request that you make it part of the record.

That report contained four major recommendations, three of which have direct impact on our foreign market development efforts. These are:

(1) intensify efforts to develop strategic marketing plans;

(2) strengthen regulations and review procedures to reduce the risk of replacing cash sales; and

(3) reaffirm the market development objective of the program and reduce the influence of foreign economic and political considerations on its decision.

We concur wholeheartedly with your first recommendation. We also believe that we have made significant progress toward implementing this recommendation. GAO is correct in stating that personnel ceilings have prevented us from fully staffing the strategic planning unit. However, we have not let this prevent us from laying much of the groundwork required to develop country strategic marketing plans. Working closely with OGSM, our initial efforts went to prepare a "plan for planning." That is, we came to an agreement as to the goals of the strategic planning effort, decided upon the information required in a completed country strategic marketing plan, established a timetable for completion of these plans, and mapped out the operational aspects of the implementation process. We then decided to use the initial plans as models for future reference. While these models were being prepared, we recognized the need for establishing priorities for our planning effort. We, therefore, decided to do two things. First, we surveyed our agricultural attaches worldwide, our market development cooperators, our Commodity Programs division directors here in FAS, and other individuals from OGSM and ESCS to seek from them their assessment of country priorities by commodity for our strategic marketing plans. This gave us a broad overview as to where the high potential growth markets will be during the next three to five years and beyond.

Kelly Harrison 2

Second, we recognized the need for a financial analysis of these same markets to determine our customers' financial viability. It is not enough that there is a high growth market in a certain country if that same country cannot eventually pay for the U.S. agricultural products it purchases. Your office has been doing signficant work in financial forecasting. We combined your financial forecasts with our marketing survey to give a unified country priority for the development of our strategic marketing plans.

This gives us a ranking of countries based on their long-term potential for growth in agricultural export sales. The countries are grouped by regions and these regional rankings will be used in setting priorities for future market development efforts. Our long-term objective is to marshall our resources to obtain a specific increase in agricultural exports to target countries within a specified time frame. We are attaching a copy of our letter to the market development cooperators for your information. This letter details the steps necessary to initiate the implementation phase of the strategic planning program.

The GAO report further proposes that we: (a) develop a specific overall U.S. market share for high priority countries; and (b) establish target levels within these overall goals for the U.S. Credit Sales Program. Now that the target countries have been identified, the completed strategic plans will address both of these problems. We can cite as an example the completed strategic plan for Sri Lanka. In that plan, we have set a market share goal for both U.S. wheat and feed grains arising from a growing livestock industry. We further recommended a level for programming credit into Sri Lanaka for a specified time period.

GAO's next major recommendation concerns strengthening regulations and review procedures to reduce the risk of replacing cash sales. They further recommend to reinstate the provision 1488.5, Para. (b) in the GSM-5 Regulations which precluded the registration of sales made prior to the date that financing became available. We agree with this recommendation, in part. We believe the market development objectives and the concept of additionality have been weakened through the inclusion of the provision that sales made prior to the issuance of a credit line may be registered as eligible for financing. We do not think that it is necessary to tighten the regulations because flexibility is important for market development. Of importance is that market development aspects of the CCC program are covered.

GAO's third major recommendation states that, "...Congress may also wish to strengthen the market development objective of the program by amending the Food for Peace Act of 1966 to add conditions on the granting of short-term credits similar to those of the Agricultural Trade Act of 1978..." They further state that these statutory requirements should assist the Office of the General Sales Manager in

Kelly Harrison 3

restricting credits to countries and in amounts which could be justified on market development grounds. FAS concurs with this recommendation. This would reaffirm the market development objective of the program and reduce the influence of foreign economic and political considerations on its decisions.

There are also several other points on which we would like to comment:

1. GAO states that the only marketing plans that have been undertaken since 1977 were for Sri Lanka and Romania. We have also undertaken marketing plans for China and Nigeria.

2. GAO indicates that agricultural studies show that the gain in exports is probably significantly less than the amounts of CCC credits granted.

We believe that the evidence on point 2 is inconclusive. Some preliminary work that we have done shows that there may be a large multiplier for export credit which would confirm the concept of additionality. The multiplier seems to depend on the specific country, commodity, and assumptions made. Other studies would agree with the conclusions that GAO has made. As they stated, "our review did not attempt to measure or quantify additionality." For these reasons we would like to do further work on this matter, as we believe it may have a significant impact on the administration of the CCC program.

Attachment

APPENDIX IV

UNITED STATES DEPARTMENT OF AGRICULTURE
FOREIGN AGRICULTURAL SERVICE
WASHINGTON, D.C. 20250

JUL 11 1979

TO: Market Development Cooperators

FROM: Jimmy D. Minyard Jimmy D. Minyard
Assistant Administrator
Foreign Market Development

SUBJECT: Strategic Program Planning

Last fall, we established a Program Planning Branch in the Planning and Evaluation Division. In my letter of September 20, 1978, I described the organization and responsibilities of this group. We have made significant progress in further defining the objectives of our strategic program planning effort and in organizing the work of the branch.

We recently completed a ranking of countries based on their long-term potential for growth in agricultural export sales. The countries are grouped by region, and these regional rankings will be used in setting priorities for future market development efforts. Our long-term objective is to marshall our resources to attain a specific increase in agricultural exports to target countries within a specific time frame.

The vehicle for coordinating this effort will be the country strategy plan. The plan will include as needed: (1) recommendations for program strategies, and (2) recommendations for market development activities.

These recommendations will be designed to overcome transportation bottlenecks and lack of host country storage and handling facilities if appropriate. Financing options for facilities construction and the focus of trade policy will also be addressed.

The Program Planning Branch will include input from all appropriate sources in order that the completed plans reflect the best judgment of all parties concerned. Your input is essential.

The Program Planning Branch will inform OGSM of priority countries and discuss allocation of funds for specific countries and projects. They will also contact the Office of Transportation for suggestions on what transportation and/or dredging projects should be included for possible future benefits in the target countries. OGSM will be involved again at this point since Title III and/or intermediate credit could be a source of funds for some of these projects.

Once country plans are completed and strategies agreed upon, the plans will be distributed with the following instructions:

1. PL 480 and CCC Credit--The plan should be used as a framework, where appropriate, to program PL 480 and CCC credit sales for the next three to five years. Any dollar value suggested will be flexible and reflect an intent by the United States to capture specific market shares of particular commodity markets.

2. Commodity Programs--The plan should be used by the Deputy Directors for Marketing as the basis for evaluating incoming marketing plans.

3. Cooperators--The plan should be used to initiate specific market development activities in target countries to assist in achieving market share goals.

4. Agricultural Attaches--The plan should be used in working with the host government to build a strong and stable market for U.S. products.

5. Export Trade Services Division--The division should include target countries in their decisions concerning exhibits, sales teams, and other activities.

Steps have already been taken to ensure that the analysts in the Program Planning Branch be kept informed of all activities related to the various countries. They will be provided with commodity studies, attache reports, trip reports, and any background or other information that could be used in preparing the studies. They will also be contacted prior to foreign travel by FAS or OGSM staff. This will enable travelers to collect valuable, on-the-spot information to round out what is available here. We have also asked that the analysts be invited to appropriate USDA meetings concerning their countries of responsibility.

Attached are copies of the country listings by region and rank. The Program Planning Branch is not yet fully staffed. Currently, Gordon Nicks is responsible for Europe and Bill Randolph for the Middle East and Africa. Additional analysts will be assigned as soon as possible. In the interim, please contact Vernon Harness if you have any information concerning the other regions.

APPENDIX IV

This undertaking will require considerable coordination in order to make the concept of strategic planning work. It is our intent that there will be both uniformity and continuity in the strategic country plans, and that we will attach specific due dates for completion of the assigned regional studies. It is possible that some individuals may be in the position of working on more than one plan at a time. It is important that our due dates be respected in order to act upon a market development strategy rather than to react to specific short-term supply situations.

When we realize what is at stake in long-term opportunities for agricultural exports, we feel that the potential results will more than justify the efforts required in this process.

UNITED STATES DEPARTMENT OF AGRICULTURE
OFFICE OF INSPECTOR GENERAL
WASHINGTON, D.C. 20250

JUL 24 1979

Mr. J. K. Fasick, Director
International Division
General Accounting Office
Rm. 4804, 441 G Street, N.W.
Washington, D.C. 20548

Dear Mr. Fasick:

Office of Inspector General's comments on your draft report entitled "Stronger Market Development Emphasis Needed in Administering Agriculture's Export Credit Sales Program" are attached.

The Department's Office of the General Sales Manager will send its comments on the report directly to you.

Sincerely,

L. L. FREE
Acting Assistant Inspector General
Administration, Congressional
Reporting & Liaison

Attachment

UNITED STATES DEPARTMENT OF AGRICULTURE
OFFICE OF THE INSPECTOR GENERAL
WASHINGTON, D.C. 20250

OFFICE OF INVESTIGATION

July 17, 1979

SUBJECT: GAO Report, Stronger Market Development Emphasis Needed in Administering Agriculture's Export Credit Sales Program (79-97)

TO: L. L. Free, Acting Assistant Inspector General for Administrator, Congressional Reporting, and Liaison

OIG generally concurs with the GAO draft report and in some instances, such as importing country practices and extended delivery periods, have previously expressed our concerns to OGSM/FAS.

However, it should be recognized that some of the questions addressed are not easily resolved.

This is especially true with respect to additionality and end user benefits. For example, GAO recommends that OGSM shorten the length of CCC credits to those countries which continue to maintain significant differences between terms of CCC credits and the internal terms of payment.

We agree with this recommendation, but believe that in the absence of statutory requirements with respect to internal terms of payment by end users or use of the program for foreign aid there is a need for legislation to affirm that foreign end users are to receive the benefit of CCC credits.

Although we do not specifically test whether commodities financed under the Export Credit Sales Program are received in foreign countries, we discuss and test as deemed necessary, all USDA program activities during our regular Attache audits. This work has identified end user conditions similar to those noted by GAO, but has not identified instances of non-receipt of commodities.

We do not believe there is a high risk of non-shipment or diversion of commodities financed under this program. Although we do not disagree with the GAO comments on physical verification of commodity arrival, we believe the need for formal procedures should be closely examined in view of the low priority we would establish for this effort. During overseas audits we will continue to be alert for any violations of Export Credit Sales regulations.

APPENDIX V

With respect to comments on page 52, the initial audit review resulted primarily in internal OIG memorandums. Our reported position was noted as a General Comment in audit report 07091-22-FO, Review of Agricultural Attache Offices in Asia. In this comment we stated "We recognize the complexities of this issue and potential conflicts with accomplishment of program objectives if additional requirements were placed on Export Credit Sales. However, if ECSP continues to generate short-term funds for participating countries, we believe consideration should be given to encouraging or requiring these countries to use the funds for mutually agreed development purposes. Also, country requests for three-year credit needs to be carefully evaluated, especially where it is known that recipient country requires accelerated repayments from end users. FAS and OGSM should coordinate in exploring the feasibility of these approaches."

The OIG conclusions are accurately noted by GAO but the impression could be erroneously left that an official report was issued in response to the newspaper article about the Philippine practices.

HUBERT N. SPARKS
Director, Foreign Operations
Staff

U.S. DEPARTMENT OF AGRICULTURE
ECONOMICS, STATISTICS, and COOPERATIVES SERVICE
WASHINGTON, D.C. 20250

July 25, 1979

SUBJECT: GAO Report on Export Credit Sales

TO: Thomas McDonald, Jr.
GAO Liaison, OGSM

THROUGH: Charles Hanrahan, Acting Chief CE
Trade Policy Branch

The GAO Report on the Export Credit Sales Program appears to be well-written and accurate. It highlights several important criticisms of the export credit program that merit careful consideration. In addition, it either directly or indirectly suggests the desirability of a major support role for ESCS. By what it does not say, it also raises some questions about the relationship between OGSM and ESCS.

The report criticizes the absence of a strategy for allocating export credit by country and commodity. This suggests a need for research to establish both marketing plans and criteria for judging the "need for credit". It also criticizes the lack of work done to promote "additionality"--the use of CCC credits to expand the volume of total agricultural exports, as opposed to the mere substitution of credit sales for cash sales.

Both of these criticisms suggest the value of closer coordination between OGSM and ESCS. OGSM could meet these criticisms either by expanding its own staff, or by coordinating more closely with work done in ESCS and FAS. The GAO recommendations advise a closer collaboration with FAS in setting marketing goals. They also suggest a need for background research and analysis on "need" for credit, ability to repay, comparable credit terms by foreign competitors, and additionality. These are all areas in which ESCS's country and regional expertise could be exploited in support of OGSM. For instance, on page 33, GAO recommends that ESCS initiate foreign credit studies to support the OGSM program. This is the kind of research support that ESCS can, and is prepared, to undertake.

The GAO report fails to mention any relationship between the export credit program and the agricultural credits extended by the Export-Import Bank. No mention is made of the "Gentlemen's Agreement" on credit adhered to by many major trading nations which sets minimum terms for credit for nonagricultural exports. Also the link between food aid and commercial credit is ignored, largely

-2-

because the programs operate separately. At least a conceptual link, in terms of phasing out food aid to certain countries, should be recognized. ESCS can assist in providing research and analysis to support the development of a cohesive, longer-term framework in which OGSM programs can operate. This could help make OGSM less vulnerable to charges of being swayed by short-term political, and other, pressures and of taking a "passive role".

Some elements of the report suggest a lack of familiarity on GAO's part with the existing relationship between OGSM and ESCS that may reflect the ad hoc nature of some of those relations. One example, on page 31, is GAO's minimization of the role that ESCS plays in providing financial information about individual countries. Another relates to the report's statement that OGSM has not completed its country strategic market plan for Indonesia. GAO appears unaware that ESCS is currently working on an Indonesia market study. This suggests another area of potential fruitful cooperation between the two agencies--the planning and execution of country market studies.

Eileen M. Manfredi

EILEEN M. MANFREDI
Agricultural Economist
Trade Policy Branch

DEPARTMENT OF STATE

Washington, D.C. 20520

August 1, 1979

Mr. J. Kenneth Fasick
Director
International Division
U.S. General Accounting Office
Washington, D. C.

Dear Mr. Fasick:

I am replying to your letter of June 29, 1979, which forwarded copies of the draft report: "Stronger Market Development Emphasis Needed in Administering Agriculture's Export Credit Sales Program".

The enclosed comments on this report were prepared by the Deputy Assistant Secretary for International Resources and Food Policy.

We appreciate having had the opportunity to review and comment on the draft report. If I may be of further assistance, I trust you will let me know.

Sincerely,

Roger B. Feldman

Roger B. Feldman
Deputy Assistant Secretary
for Budget and Finance

Enclosure:
As stated

GAO DRAFT REPORT: "STRONGER MARKET DEVELOPMENT EMPHASIS NEEDED IN ADMINISTERING AGRICULTURE'S EXPORT CREDIT SALES PROGRAM"

With some exceptions we concur with the observations and recommendations contained in this report. The principal area where our views diverge from those of GAO is in the discussion of the economic and foreign relations implications of the Commodity Credit Corporation (CCC) Export Credit Sales Program (Chapter 5).

We share wholeheartedly the concerns that CCC credits have been allocated without adequate analysis of their impact on incremental agricultural exports (Chapter 4). Too frequently the CCC justification for individual credit lines is grounded solely on the claim that there exists a growing foreign demand for specific commodities and the conclusion drawn that credits are needed to capitalize on this market opportunity. This begs the question of whether US exporters through aggressive marketing efforts could not increase sales to the same countries without the assistance of CCC credits. Also, the employment of CCC credits largely to satisfy traditional customers appears in some cases to create a dependency on those credits, whereas the purpose of CCC credits is to develop and establish long term markets for normal US commercial exports. We agree that the CCC should put greater emphasis on market development as opposed to market retention.

Our principal comment on the GAO report centers on Chapter 5, "Economic and Political Considerations have Encroached on the Basic Objective of Developing Markets", which argues that eliminating such considerations will enhance the effectiveness of the CCC credit program. The evidence cited to support this contention is less than convincing. In objecting to formal bilateral discussions (in which USDA presented the USG position) with recipient countries prior to setting levels and conditions for credit lines, it is not clear how the CCC program was adversely affected.

-2-

In the Korean case cited, the major problem was the need for more controls over the ultimate use of the credits. It is obvious that correcting this situation could only come through direct discussions with Korean authorities. In the case of Polish credits there is no indication that the additional financing granted following interagency deliberations had an adverse impact on incremental agricultural exports.

Other recent cases of inter-agency discussions not referenced in the GAO study would strongly support the need for greater reliance on the expertise of other government agencies. For example, information on Peru's economy provided by the State Department and Treasury proved to be crucial to the decision by the CCC to grant Peru additional credits in 1979. Had these agencies not been consulted an important market opportunity might have been lost.

We are concerned that the report's criticism of the involvement by other agencies in the CCC decision making process may, in fact, weaken CCC's ability to make sound, informed decisions on credit allocations. If the CCC is to place greater emphasis on evaluating credit needs, credit worthiness and foreign competition as recommended in the GAO study, it makes more sense to seek out additional, pertinent information on which to base such judgments. This could be accomplished by more frequent consultations with other agencies, either individually or through an expansion of the advisory role of the National Advisory Council (NAC). If the latter were preferred, we suggest that the NAC review all proposed CCC credit lines, and not, as is currently the case, only a portion of those credits requiring foreign bank letters of credit. Also, to allow adequate consideration of credit justifications, CCC should provide at least seven days for review of credit proposals before they are taken before the NAC. Thus, we believe the section in the GAO report on the NAC (page 13) should be expanded and strengthened to reflect the benefits which would accrue the CCC program by greater reliance on the expertise of other NAC agencies.

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We find puzzling the statement in Chapter 5 that the "intrusion of economic support or political considerations into the (CCC) program decision process may jeopardize the program's exemption from the Cargo Preference Act" (page 58). In our view, what distinguishes CCC credits from concessional assistance is the commercial nature of the credits as defined by the terms of the credits, not the possible secondary effects of such credits on the importing country's economy or policies. We cannot deny, of course, that a country may consider CCC credits as more than a market development tool. In addition, there appears to be a conflict between the opinion rendered by the Attorney General in 1965 establishing the grounds for excluding the CCC from the Cargo Preference Act and GAO's assertion that CCC credits automatically provide balance of payments support.

We concur with GAO's recommendation that USDA establish mechanisms to insure that recipient governments pass on the full credit benefits to end-users and not absorb a portion of those benefits in the form of budget subsidies. We believe that by removing all such forms of credit manipulation on the part of recipient governments, any possible threat to the cargo preference exclusion would be eliminated.

Thank you for the opportunity to comment on this draft report.

Michael Calingaert
Deputy Assistant Secretary for
International Resources and Food Policy

DEPARTMENT OF THE TREASURY
WASHINGTON, D.C. 20220

OFFICE OF
ASSISTANT SECRETARY
FOR INTERNATIONAL AFFAIRS

August 13, 1979

Dear Mr. Fasick:

Thank you for giving the Treasury Department the opportunity to comment on the GAO's draft, "Stronger Market Development Emphasis Needed in Administering Agriculture's Export Credit Sales Program." We found the draft to be perceptive and useful, although we have a few suggestions for further improvement.

We agree strongly with the draft's fundamental thrust that greater strategic planning is needed in establishing CCC lines of credit. We feel, however, that the goal underlying that strategic planning should be to foster agricultural exports which would not otherwise have taken place (the additionality principle). Market development and market maintenance, the CCC goals you describe in your draft, are really aspects of the additionality principle. For that reason, we would suggest you elaborate on why a stronger market development emphasis would serve the larger goal of additionality.

In this connection I would also suggest you increase the amount of analysis devoted to the National Advisory Council's role in the CCC program. It is our view that the Agriculture Department would be better served if it were to seek the advice from the NAC agencies on a more consistent and fundamental basis. The NAC forum is the appropriate way to coordinate the U.S. Government's international financial policy and its member agencies constitute a reservoir of resources relevant to the CCC's activities.

As a concomitant point, we agree with the draft's recommendation that our Agricultural Attaches should thoroughly explore <u>all</u> sources of information about competing foreign credit terms. It would be useful, as the

- 2 -

draft implies, to have these Attaches submit scheduled reports on competitive conditions in key market countries. In this connection, it might be useful for Agriculture to consider using the exchange of information facilities available to the U.S. Government in the area of export financing.

I hope you find this letter helpful in your deliberations. I look forward to seeing the GAO report, when it is complete.

Sincerely,

John D. Lange

John D. Lange

Mr. J. K. Fasick
Director
United States General Accounting Office
International Division
Washington, D.C. 20548

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