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Long-Term Bilateral Grain Agreements With the Soviet Union and China

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The Honorable Patrick Leahy
Chairman, Committee on Agriculture,
Nutrition and Forestry
United States Senate

The Honorable George E. Brown, Jr.
Chairman, Subcommittee on Department Operations,
Research, and Foreign Agriculture
Committee on Agriculture
House of Representatives

At your request, we reviewed the U.S. long-term bilateral grain agreements (LBGAS) with the Soviet Union and China. This report provides (1) a history and analysis of these agreements, (2) information on the volume and value of U.S. grain exports to these two countries, and (3) some observations on the extent to which the United States has benefitted from the agreements.

The United States has entered into LBGAS with only two countries—the Soviet Union and China. The first 5-year agreement with the Soviet Union covered 1976 to 1981 and had two 1-year extensions, while the second 5-year agreement covered 1983 to 1988, with a recent 2-year extension. The 4-year agreement with China covered 1981 to 1984. These LBGAS established frameworks for grain trade whereby the Soviet Union and China agreed to purchase minimum quantities of wheat and corn from the United States; in return, the U.S. government agreed to facilitate the sale of those commodities at prevailing market prices for a set number of years. Actual sales under the LBGAS were to be transacted between private U.S. grain traders and Soviet and Chinese government buying agencies.

Results in Brief

LBGAS with the Soviet Union and China have contributed to some stability in U.S. and international grain markets, especially in tight supply situations. Since the early 1980s, however, worldwide grain markets have been in oversupply and Chinese grain production has increased dramatically. Although the Soviets continue to favor LBGAS to meet a substantial portion of their grain import needs, the Chinese now favor purchasing grain outside the framework of an LBGA, and have not entered into new LBGAS with any country since 1984.

Background

Historically, the United States has generally opposed long-term agreements on the grounds that they run counter to free trade policies. However, in the early 1970s, large unanticipated purchases of U.S. grain by the Soviet Union and rapidly increasing demand for agricultural commodities worldwide caused a generally tight supply situation with high domestic food prices. As a result, in 1975, U.S. policymakers concluded that an LBGA with the Soviet Union was appropriate to ensure less disruptive markets. The purpose of the first LBGA with the Soviets was to minimize market disruptions caused by Soviet purchases of U.S. grain while promoting an orderly expansion of trade between the two countries. By 1983, world supply conditions had changed significantly and surpluses were characteristic of the grain market. The second LBGA with the Soviets was intended to expand grain trade with a potentially large customer in a surplus market. In entering into a 4-year LBGA with the Chinese in 1981, U.S. officials noted that they were merely formalizing U.S. participation in a potentially large market and placing the United States on an equal footing with Canada and Australia, other major suppliers of grain to China that already had long-term agreements with that country. Maintaining a better knowledge of the large Soviet and Chinese markets was an objective of all three LBGAS.

The United States continues to maintain that LBGAS have trade-distorting effects and proposed in July 1987 that all government support programs that distort agricultural trade be phased out worldwide over a 10-year period.[1] An implication of the U.S. proposal was that the United States was willing to renounce LBGAS if all other exporting countries (e.g., Australia and Canada) did the same. Nonetheless, with the second LBGA with the Soviet Union due to expire in September 1988, the United States began negotiations in March 1988 to enter into a third 5-year agreement. One official of the Office of the U.S. Trade Representative noted that, even if a new 5-year agreement were reached with the Soviet Union, it would expire well within the 10-year period proposed for phasing out all agricultural support programs.

First LBGA With the Soviet Union

A 1970 Soviet government decision to upgrade the quality of the Soviet diet through increased beef and poultry production resulted in unusually large and unanticipated purchases of grain in 1972 when Soviet grain harvests were poor. The Soviets purchased about 9.5 million metric tons (MMT) of wheat and 3.7 MMT of corn from the United States that

[1]See our report, Agricultural Trade Negotiations: Initial Phase of the Uruguay Round (GAO/NSIAD-88-144BR) May 1988.

year and significant amounts from other exporters.[2] Again in 1975, the Soviets purchased large quantities of wheat and corn from the United States without prior announcement. In both years, consumer prices increased as a result of the massive grain purchases by the Soviets and the cumulative purchases of others concerned with covering future needs.

The United States lacked information on Soviet market potential and had no systematic method for either tracking grain exports or requiring large importers to communicate their intentions to purchase U.S. grain. As a result, the U.S. government initiated a number of actions during the early 1970s to protect the domestic grain market, including signing a joint agreement to exchange agricultural information with the Soviets (June 1973) and implementing an export reporting system to provide for early warning in cases of short supply of heavily exported agricultural commodities (Oct. 1973). In September 1975, the U.S. government announced that no future sales to the Soviet Union would occur until an LBGA was successfully negotiated.

The LBGA with the Soviet Union was signed on October 20, 1975, to become effective October 1, 1976. The 1975 LBGA provisions are outlined in appendix I. Under the LBGA, the Soviets were to purchase a total of at least 6 mmt of wheat and corn annually in approximately equal portions. The LBGA allowed the Soviets to purchase an additional 2 mmt of grain without consulting the U.S. government unless U.S. supplies were less than 225 mmt, in which case the U.S. government could reduce the quantity of grain available for purchase by the Soviets. The LBGA required consultations if the Soviets wished to purchase or U.S. companies wished to sell grain over the 8 mmt maximum. No specific price was outlined in the LBGA; rather, grain purchases were to be made "at the market price prevailing for these products at the time of purchase/sale." Through two 1-year extensions, the LBGA ran through September 1983.

During the 7 years the first LBGA was in effect, the Soviets did not make large, unexpected, disruptive purchases as in previous years. During each of the 7 agreement years[3] except 1980, the Soviets essentially met the 3-mmt minimum purchase amounts of wheat and corn called for in the LBGA. (See table I.2.) U.S. wheat exports during the 7 years totaled

[2]Soviet wheat and corn purchases represented about 31 and 12 percent, respectively, of total U.S. wheat and corn exports in 1972.

[3]For LBGAs with the Soviet Union, an agreement year covers Oct. 1-Sept. 30. The 1980 agreement year is the year ending Sept. 30, 1980.

about 25 mmt, valued at about $4.1 billion, and corn exports about 44 mmt, valued at about $5.3 billion.

Although the U.S.-Soviet grain trade ran relatively smoothly during the first 3 years of the LBGA, it was affected by national security and foreign policy concerns during the last 2 years. In October 1979, as a result of a poor harvest that year, the Soviets sought and obtained U.S. government approval to purchase 25 mmt of grain during the 1980 agreement year. In January 1980, however, in response to the Soviet invasion of Afghanistan in December 1979, President Carter announced an agricultural embargo; Soviet purchases of grain would be limited to 8 mmt, the maximum amount guaranteed under the LBGA. President Reagan lifted the embargo in April 1981 and the United States and the Soviet Union agreed to a 1-year extension of the LBGA (through Sept. 30, 1982).

Although the embargo may have had some symbolic value, its success was limited because the Soviets were able to purchase needed grain from other major producers, including Argentina, Australia, Canada, and the European Community. The embargo was not without costs to the United States. The Economic Research Service of the U.S. Department of Agriculture (USDA) estimated the gross cost of the embargo at over $2 billion. More significantly, the embargo disrupted grain trade patterns as Argentina, Australia, Canada, and the European Community attempted to maintain their increased shares of the Soviet market. According to a 1983 International Trade Commission report, major U.S. grain and soybean exporting companies reported that (1) the U.S. reputation as a reliable supplier of agricultural commodities to the world market suffered as a result of the embargo and (2) the embargo had encouraged other competitor countries to increase agricultural production and exports.[4] The U.S. share of Soviet wheat and corn imports dropped significantly following the embargo as indicated in appendix I. (See tables I.3 and I.5.)

In the aftermath of the grain embargo to the Soviet Union, the Congress enacted legislation to enhance congressional oversight over embargoes and imposed other limits on the use of agricultural embargoes. Several statutes were designed to protect the sanctity of contracts entered into prior to the establishment of an embargo. (See app. I.)

[4]USDA's Economic Research Service noted that although the embargo probably contributed to the declining U.S. share of the Soviet market, other factors increased production and competition by other grain suppliers. These included increased worldwide demand in the 1970s and more protectionist policies of the European Community and others.

Second LBGA With the Soviet Union

About the time the second LBGA was signed, good quality wheat was readily available from a number of sources and was in oversupply. The United States was dominant in the international corn market with more than half the world's corn exports. Because the Soviets had relied on U.S. corn to maintain livestock production since the early 1970s, U.S. negotiators were apparently able to use U.S. domination in the corn market as leverage to increase the amounts of U.S. wheat the Soviets agreed to purchase.

U.S. officials hoped that the new agreement would help to restore the reputation of the United States as a reliable supplier and begin to normalize U.S.-Soviet trade relations. Following the 1980 embargo, the Soviets had concluded bilateral agreements for agricultural commodities with several countries, including Canada and Argentina, and the U.S. share of the Soviet wheat market was expected to fall.

The provisions of the second LBGA with the Soviet Union are outlined in appendix I. Under the second LBGA, the Soviets were to purchase a total of 9 mmt of wheat and corn, with the minimum annual quantities of each grain being 4 mmt.[5] Whereas the first LBGA allowed the United States to reduce the quantity of grain available for purchase if total U.S. supplies fell below 225 mmt, the second agreement contained no escape clause. Also, the first LBGA did not address quality but the second agreement stated that the U.S. government was prepared to be of assistance on questions of grain quality. Like the first LBGA, the second agreement called for grain sales to be made at "the market price prevailing for these products."

During the 5 years ending September 30, 1988, U.S. exports to the Soviet Union totaled about 23.6 mmt of wheat, valued at about $2.8 billion, and about 36.1 mmt of corn, valued at about $4.2 billion. While the Soviets purchased the required 4 mmt of corn during each of the 5 agreement years, they purchased only 2.9 mmt of wheat during the second year and less than 0.2 mmt of wheat during the third year. Price considerations significantly affected grain trade during the period of the second LBGA. According to Soviet, U.S. government, and U.S. grain company officials, price was the primary reason Soviet wheat purchases were below the LBGA minimums. U.S. and Soviet officials have interpreted the price provision in the LBGA differently. USDA officials noted that, since the product

[5]The Soviets could purchase soybeans and/or soybean meal in the proportion of one ton for two tons of grain, but the minimum annual quantities of wheat and corn had to be no less than 4 mmt each.

cited in the LBGA was clearly U.S. grain, the price cited was the prevailing U.S. price. The Soviet position has been that "market price" refers to prevailing world prices, and world wheat prices were at times substantially lower than U.S. wheat prices.

U.S.-Soviet differences on the price of U.S. wheat were exacerbated by the fact that the U.S. Export Enhancement Program (EEP), an agricultural export subsidy program established in May 1985, lowered the price of wheat to many importers but not to the Soviet Union. The United States excluded the Soviet Union from the EEP for foreign policy reasons until August 1986.[6] Moreover, the initial offer to the Soviets on August 1, 1986, did not provide for a sufficient subsidy to make U.S. wheat prices competitive. The price issue was fundamentally resolved in April 1987, when the United States offered 4 mmt of wheat to the Soviets at a price made competitive by an increased subsidy. Although there may continue to be differing interpretations of the phrase "market price prevailing for these products," it now seems clear that the Soviets buy only when the U.S. price is competitive with those of other exporters. The 4 mmt of wheat purchased by the Soviets during the 4th agreement year was subsidized through the EEP as was the almost 9 mmt of wheat purchased during the 5th agreement year. The total amount of subsidy provided during the 2 years was about $450 million.[7]

With the second LBGA due to expire in September 1988, U.S. and Soviet officials began negotiations on a new LBGA in March. Major issues of controversy concerned quantity and price. The U.S. negotiating objective had been to ensure substantially higher minimum annual Soviet purchases of grain than the 9 mmt under the second LBGA. The Soviets wanted more specific language regarding price but, according to a USDA official, the United States did not see the necessity for more specific language.

The Soviets also wanted the LBGA to provide for better access for their ships to U.S. ports as well as a general commitment to increase bilateral trade between the two countries. The United States wanted a "pure grain agreement." On November 28, 1988, failing to reach agreement on

[6]See our report, Implementation of the Agricultural Export Enhancement Program (GAO/NSIAD-87-74BR) Mar. 1987.

[7]It should be noted that the Soviets' large purchases of wheat in 1972 were subsidized by USDA through its wheat export subsidy program. That subsidy program was terminated in 1973 when U.S. prices became competitive with those of other exporters.

a new LBGA, U.S. and Soviet officials agreed to extend the second LBGA 27 months, through December 1990.

As of January 31, 1989, the United States had offered 4 mmt of wheat to the Soviets through the EEP, and the Soviets had purchased 2 mmt. The total amount of subsidy provided during the 6th agreement year was about $46 million as of that date.

LBGA With China

Through the early 1970s, Canada and Australia were the primary grain suppliers to China. However, in 1972, China purchased grain from the United States for the first time, and in 1973, more than 50 percent of China's wheat and corn imports were from the United States. U.S. grain exports to China fluctuated widely after trade was resumed in 1972. In October 1980, the United States and China entered into a 4-year LBGA, effective January 1, 1981. At that time, China had LBGAs with Canada, Australia, Argentina, and France. U.S. officials noted that the LBGA placed the United States on an equal footing with all other major suppliers and was recognition of China's grain purchasing potential.

The provisions of the 4-year LBGA with China are outlined in appendix II. Under the LBGA, China was to purchase a total quantity of "at least 6 to 8 mmt" of U.S. wheat and corn annually, with corn representing approximately 15 to 20 percent of total purchases. Under "exceptional circumstances" the United States could supply less or China could purchase less than the minimum quantities. However, the Chinese were required to limit their purchases from other suppliers proportionally under such circumstances. The LBGA called for transactions to be made at "prevailing market prices."

During the 4 years the LBGA was in effect, China purchased a total of about 20.8 mmt of U.S. wheat, valued at about $3.3 billion, and about 3.5 mmt of corn, valued at about $409 million. While total grain sales were well above the 6 mmt minimum during the first 2 years of the LBGA, they amounted only to about two thirds of the 6 mmt minimum during each of the last 2 years. The Chinese purchased only 0.5 mmt of corn in 1981 and none in 1984 even though the LBGA called for corn purchases to be approximately 15 to 20 percent of the total quantity of grain purchases. The shortfall in Chinese imports of U.S. grain in 1983 coincided with improved grain harvests in China and with a dispute between the two countries over U.S. imports of Chinese textiles. The textile conflict was resolved in July 1983, but despite several assurances by the Chinese to purchase the minimum amounts of grain specified in the LBGA, China did not purchase those minimum amounts.

China's reduced purchases of U.S. grain during the last 2 years of the LBGA can be attributed to increased Chinese grain production and the price and quality of U.S. grain. According to a Chinese trade official, the Chinese obtained no benefit from purchasing relatively expensive U.S. grain when cheaper grain was available on the world market. Also, Chinese officials said they routinely informed USDA about the low quality of U.S. grain.

The LBGA permitted China to reduce grain purchases below the agreement levels "by virtue of exceptional circumstances" but prior consultations were required. According to a USDA official, China did not request consultations concerning its intention to purchase less than the minimum amount of total grain in 1983 and 1984.

Since the LBGA with China lapsed at the end of 1984, China has purchased wheat on the open market when its domestic production levels did not meet its needs. As in the case of the Soviet Union, the United States did not offer China subsidized wheat when the EEP was first established in May 1985. Chinese officials told us that the U.S. policy of not offering subsidized grain to China was discriminatory. China, in fact, requested that the United States offer grain under the program on several occasions. In January 1987, the United States first offered wheat to China under the EEP. During 1987, the United States offered and the Chinese purchased 4 mmt of wheat under the EEP, and during 1988, about 7.2 mmt. The total amount of subsidy provided during the two years was about $330 million. With respect to corn, China's circumstances have changed. According to an Economic Research Service official, China has been a net exporter since 1984/85 and is committed to export 7.5 mmt yearly. Current Chinese policy is to purchase grain as needed on the open market and not to enter into any long-term grain agreements.

Conclusions

While U.S. grain exports to the Soviet Union and China have been significant in terms of total U.S. grain exports since 1976, it is not clear how significant the LBGAs were in influencing these countries to purchase grain from the United States. The LBGAs appeared at the outset to provide a secure outlet for U.S. grain exports, but neither the Soviet Union nor China was willing to purchase U.S. grain when U.S. prices were significantly above those of other exporters. In retrospect, this might have been expected, since the LBGAs were in essence voluntary and unenforceable agreements and their price provisions were ambiguous. Also, the potential of the LBGAs for increasing U.S. exports has at times been limited by U.S. foreign policy actions, most notably, the 1980 partial embargo of grain to the Soviet Union.

If and when discussions begin again on a new LBGA with the Soviet Union, price and quantity are again likely to be issues. In addition, the issues of Soviet ship access to U.S. ports and increased bilateral trade are likely to be raised by the Soviets as they were during discussions leading to the extension of the LBGA. If Soviet agricultural reform results in increased domestic grain production, it might affect the Soviets' continuing interest in the use of LBGAs.

Objectives, Scope, and Methodology

The Chairman of the Senate Committee on Agriculture, Nutrition, and Forestry and the Chairman of the Subcommittee on Department Operations, Research, and Foreign Agriculture, House Committee on Agriculture, asked us to review the U.S. experience under the long-term bilateral grain agreements with the Soviet Union and China. We examined the history of events leading to the agreements, determined the volume and value of trade under them, and assessed the extent to which they have served U.S. interests.

We interviewed officials from USDA's Foreign Agricultural Service and Economic Research Service, the Department of State, the Office of the U.S. Trade Representative, and the Congressional Research Service. We also interviewed Soviet and Chinese embassy officials and representatives from each country's trade office operating in the United States. We also met with representatives of U.S. grain companies and trade associations.

As agreed with you, we did not obtain official agency comments on this report but did receive informal comments on a draft of our report from USDA's Foreign Agricultural Service and Economic Research Service, the Office of the U.S. Trade Representative, and the Department of State. These comments were considered and changes made in the report as appropriate.

Our work was performed in accordance with generally accepted government auditing standards.

As agreed with your offices, we are distributing this report to other congressional offices and to appropriate executive agencies and will also make it available to others upon request. The report was prepared under the direction of Allan I. Mendelowitz, Director, Trade, Energy, and Finance Issues. Other major contributors are listed in appendix III.

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Abbreviations

EC	European Community
EEP	Export Enhancement Program
LBGA	Long-term bilateral grain agreement
mmt	million metric tons
USDA	U.S. Department of Agriculture

LBGA With the Soviet Union

Background

The Soviet Union has historically emphasized the domestic production of grain to satisfy its internal needs. It has imported wheat from various sources since 1955 to alleviate any shortfalls in production. Through 1970, the Soviets were net exporters of coarse grain, with average exports of 1.7 million metric tons (MMT) annually from 1960 to 1970.

Following a decision to upgrade the quality of the Soviet diet through increased beef and poultry consumption, the Soviets' 1970 5-year plan emphasized the importance of grain production to expand livestock inventory. In 1972, however, the Soviets did not achieve the planned grain production and, rather than slaughter livestock as they had done in the past, they imported grain to maintain the livestock. The Soviets purchased about 9.5 MMT of wheat and 3.7 MMT of corn that year from the United States and significant amounts from other exporters. These purchases represented about 31 percent of total U.S. wheat exports and about 12 percent of total U.S. corn exports that year and prompted other large purchases of U.S. wheat by buyers concerned with covering future needs. These overall purchases greatly increased U.S. domestic and world prices.[1]

Again in 1975 Soviet grain production was poor and the Soviets purchased grain on the world market with no advance notice, including 4 MMT of wheat and 9.8 MMT of corn from the United States. Once again, these purchases caused U.S. consumer prices to increase.

Table I.1 shows Soviet corn and wheat production and imports from 1970 to 1988. In 1972, and again in 1975, corn and wheat imports rose dramatically.

[1]See our report, Exporters' Profits on Sales of U.S. Wheat to Russia B-176943, Feb. 12, 1974, p. 21.

Table I.1: Soviet Corn and Wheat Production and Imports

Figures in million metric tons

Year	Corn		Wheat	
	Production[a]	Imports[b]	Production[a]	Imports[a]
1970	9.4	0.3	99.7	0.5
1971	8.6	2.1	98.8	3.5
1972	9.8	4.1	86.0	15.6
1973	13.2	4.8	109.8	4.5
1974	12.1	2.2	83.9	2.5
1975	7.3	12.3	66.2	10.1
1976	10.1	5.0	96.9	4.6
1977	11.0	10.9	92.2	6.6
1978	9.0	9.6	120.8	5.1
1979	8.4	14.6	90.2	12.1
1980	9.5	11.1	98.2	16.0
1981	8.0	17.3	80.0	19.5
1982	13.5	6.3	86.0	20.2
1983	12.0	8.7	79.0	20.5
1984	13.6	20.3	68.6	28.1
1985	14.4	10.3	78.1	15.7
1986	12.5	7.6	92.3	16.0
1987	14.8	8.1	83.3	21.5
1988[c]	16.5	15.3	88.0	13.0

[a]Year ending June 30.

[b]Year ending September 30.

[c]Estimate.

Source: U.S. Department of Agriculture.

During the early 1970s, U.S. policy makers became increasingly concerned with the fluctuating nature of the domestic grain market. The erratic Soviet grain purchases were of particular concern. The United States lacked information on the potentially huge Soviet market and had no systematic method for either tracking grain exports or requiring large importers to communicate their intentions to purchase U.S. grain.

As a result of these concerns, the U.S. government initiated actions to protect the domestic grain market from severe disruption. In June 1973, the United States and the Soviet Union signed a joint agreement to exchange economic and statistical information. In October of that year, the U.S. Department of Agriculture (USDA) implemented an export reporting system to provide early warning in cases of short supply of heavily exported agricultural commodities. Also in 1973, U.S. soybean exports to all markets were temporarily halted because of short supply. In 1974, the U.S. grain harvest was somewhat lower than projected and on October 4, the administration asked two grain companies to voluntarily suspend corn sales to the Soviets. On October 19, the Soviets agreed to limit their purchases to 2.2 MMT of corn, ending the need for the embargo.

In July 1975, the administration embargoed grain exports to the Soviets after they suddenly purchased nearly 10 MMT of grain in one week. U.S. grain companies were asked to suspend future sales to the Soviet Union until the size of the U.S. grain crop was established. In September, President Ford announced that future sales to the Soviets would be suspended until an LBGA was successfully negotiated.

First LBGA

The 5-year LBGA signed in October 1975 was to be in effect from October 1, 1976 to September 30, 1981. The purpose of the LBGA was to minimize market disruptions caused by very large Soviet purchases of U.S. grain while promoting an orderly expansion of trade between the two countries. Under the agreement, the Soviets were to make annual purchases of at least 6 MMT of U.S. wheat and corn in approximately equal portions. They could purchase an additional 2 MMT of grain without consulting the U.S. government unless U.S. supplies were less than 225 MMT, in which case the U.S. government could reduce the quantity available for purchase. The Soviets agreed to space their grain purchases evenly throughout each year.

The LBGA called for consultations between the Soviet Union and the United States (1) every 6 months to discuss the implementation of the agreement and (2) whenever the Soviets wished to purchase or U.S. companies wished to sell grain over the maximum specified in the agreement. The LBGA provided for no specific price, stating only that purchases of grain would be made "at the market price prevailing for these products at the time of purchase/sale." The grain was to be purchased from private commercial sources in the United States.

Although the first LBGA was scheduled to lapse in September 1981, it was extended twice, each time for an additional year.

Grain Trade Under First LBGA

During the 7 years that the first LBGA was in effect, Soviet grain purchases were not characterized by the large, disruptive, unexpected purchases of the previous years. U.S. wheat sales over the 7 years totaled about 25.2 mmt, valued at about $4.1 billion, and corn sales about 44 mmt, valued at about $5.3 billion. During each of the 7 agreement years except 1980, the Soviets essentially met the 3-mmt minimum purchase amounts for corn and wheat, as specified in the LBGA. (See table I.2.) They purchased far more corn than wheat, with corn being used in the increasingly important livestock sector.

Table I.2: U.S. Grain Exports to the Soviet Union During First LBGA

Figures in million metric tons

Agreement Year[a]	Wheat	Corn	Total
1977	3.0	2.9	**5.9**
1978	3.4	10.5	**13.9**
1979	3.8	9.8	**13.6**
1980	2.3	5.3	**7.6**
1981	3.7	4.9	**8.6**
1982	6.0	7.5	**13.5**
1983	3.0	3.1	**6.1**
Total	**25.2**	**44.0**	**69.2**

[a]Year ending September 30.
Source: USDA.

Although grain trade between the United States and the Soviet Union ran relatively smoothly during the first 3 years of the 5-year LBGA, it was affected by national security and foreign policy concerns during the last 2 years. The Soviets had a poor harvest in 1979 and had sought and obtained approval from the U.S. administration in October of that year to purchase 25 mmt of grain during the 1980 agreement year. However, in January 1980, in response to the Soviet invasion of Afghanistan the previous month, the United States imposed a partial embargo on grain sales. President Carter announced that Soviet purchases would be limited to the 8 mmt maximum amount guaranteed under the LBGA. Subsequently, the Carter administration authorized Soviet purchases of the same amount of grain for the last year of the LBGA.

In April 1981, President Reagan lifted the embargo. USDA favored the resumption of normal grain trade but the Department of State opposed it because of the situation in Afghanistan. The administration ultimately favored extending the 1975 agreement and the United States and the Soviets agreed to extend it through September 30, 1982.

In December 1981, the United States announced it would impose economic sanctions against the Soviet Union in response to the imposition of martial law in Poland earlier that month. The sanctions included banning negotiation of a new LBGA. The existing agreement, however, was extended for another year, through September 30, 1983. In April 1983, President Reagan lifted the ban on negotiating a new agreement with the Soviets and the second 5-year agreement was signed in August to become effective October 1, 1983.

Effects of 1980 Embargo

The legal basis for the U.S. partial embargo of grain exports to the Soviet Union was the Export Administration Act of 1979, as amended, which gave the President the authority to impose export controls for foreign policy reasons. The embargo limited grain sales to the 8 mmt of wheat and corn specified in the 1975 LBGA. These sales were allowed in order to comply with Article II of the LBGA that stated that the United States "shall not exercise any discretionary authority available to it under United States law to control exports of wheat and corn purchased for supply" to the Soviet Union.

In implementing the embargo, the United States announced that all grain sales over the 8 mmt specified in the LBGA would be halted and that USDA would purchase all undeliverable grain contracts with the Soviet Union.[2] The Soviets had previously been granted permission to purchase up to 25 mmt of U.S. grain in 1980 because of their poor harvest that year. The embargo was aimed at reducing Soviet livestock production. President Carter stated that the embargo would not starve Soviet citizens but was designed to affect the quality of Soviet diets.

The success of the grain embargo was limited because the Soviets were able to purchase needed grain from other major grain producers, including Argentina, Australia, Canada, and the European Community (EC).[3] Moreover, the embargo probably had an even more detrimental long-term impact on U.S. grain exports to the Soviets as it disrupted grain trade patterns. Argentina, Australia, Canada, and the EC attempted to maintain their shares of the Soviet market. Although the embargo was eventually lifted and a second LBGA signed, the U.S. share of the Soviet market remained well below the level of the late 1970s until 1984 in the case of corn and 1988 in the case of wheat. (See tables I.3, I.4, and I.5.)

[2]According to the Economic Research Service (ERS), USDA purchased 8.9 mmt of corn and 4.2 mmt of wheat at a gross cost of $2.2 billion. The net cost was lower due primarily to the subsequent resale of contracts purchased from grain companies.

[3]See our reports, Suspension of Grain Sales to Soviet Union: Monitoring Difficult—Shortfall Substantially Offset (C-CED-81-1) Mar. 1981 and Lessons to be Learned from Offsetting the Impact of the Soviet Grain Sales Suspension (CED-81-110) July 1981.

According to an International Trade Commission report of December 1983, officials of major U.S. grain and soybean exporting companies reported that (1) the U.S. reputation as a reliable supplier of agricultural commodities to the world market suffered as a result of the embargo and (2) the embargo had encouraged other competitor countries to increase agricultural production and exports.[4]

Table I.3: Wheat Exports to the Soviet Union

	Percent exported by						
Year[a]	U.S.	Canada	Australia	Argentina	EC	Other	Total (mmt)
1976	40	32	12	12	0	4	**10.1**
1977	63	26	9	2	0	0	**4.6**
1978	50	26	5	17	0	3	**6.7**
1979	57	39	2	0	0	2	**5.1**
1980	33	18	23	17	6	5	**12.1**
1981	19	28	16	19	6	13	**16.0**
1982	34	24	12	15	8	7	**20.3**
1983	14	34	5	20	16	11	**20.8**
1984	21	28	8	18	18	7	**20.5**
1985	22	27	8	15	22	8	**28.1**
1986	1	31	2	15	33	10	**15.7**
1987	5	37	8	4	39	8	**16.0**
1988[b]	57	20	0	3	14	5	**21.5**

[a]Year ending June 30.

[b]Estimate.

Source: USDA.

[4]ERS noted that although the embargo probably contributed to the declining U.S. share of the Soviet market, other factors increased production and competition by other grain suppliers. These included increased worldwide demand in the 1970s and more protectionist policies of the EC and others.

Table I.4: Coarse Grain Exports to the Soviet Union[a]

Year[b]	U.S.	Canada	Australia	Argentina	EC	Other	Total
	Percent exported by						
							(mmt)
1976	65	9	5	1	3	17	**15.6**
1977	82	4	2	4	4	6	**5.7**
1978	78	2	0	14	2	5	**11.7**
1979	83	1	0	14	2	0	**10.0**
1980	61	7	7	17	1	7	**18.3**
1981	28	13	2	46	3	8	**18.0**
1982	33	17	0	39	3	8	**26.0**
1983	28	14	0	43	2	14	**12.5**
1984	52	4	1	28	2	13	**11.6**
1985	60	3	4	15	10	9	**26.9**
1986	41	5	0	10	12	24	**13.7**
1987	37	20	0	13	14	16	**11.0**
1988[c]	42	3	0	4	20	31	**10.0**

[a]Coarse grains include rye, oats, barley, millet, sorghum, and mixed grains as well as corn.

[b]Year ending June 30.

[c]Estimate.
Source: USDA.

Table I.5: Corn Exports to the Soviet Union

Year[a]	United States (mmt)	United States (%)	Total (mmt)
1976	9.2	75	**12.3**
1977	4.2	83	**5.0**
1978	8.6	80	**10.9**
1979	7.2	75	**9.6**
1980	9.9	68	**14.6**
1981	4.4	37	**11.8**
1982	8.0	45	**17.7**
1983	3.1	42	**7.4**
1984	5.9	68	**8.7**
1985	14.9	73	**20.3**
1986	6.3	60	**10.4**
1987	4.1	58	**7.1**
1988	4.2	58	**7.3**

[a]Year ending June 30.
Source: USDA.

Congressional Actions on Embargoes

Following the grain embargo to the Soviet Union, the Congress enacted legislation to enhance its oversight of embargoes and imposed other limits on the use of agricultural embargoes. The Agriculture and Food Act of 1981 (P.L. 97-98) makes the imposition of a selective agricultural embargo, i.e., an embargo not imposed on all commodities exported to that country, an expensive and cumbersome proposition by requiring significant levels of compensation to farmers. Several statutes aim at protecting the sanctity of contracts entered into prior to the establishment of an embargo; for example, two statutes specifically protect such contracts and a third emphasizes non-interference with pre-existing contracts during an embargo as a matter of policy.

The contract sanctity provision in the Futures Trading Act of 1982 applies to any embargo of agricultural commodities. It protects any agricultural export sales contract entered into before an embargo is announced so long as the contract requires delivery within 270 days from the date of the embargo. The provision does not apply to a period for which the President has declared a national emergency or Congress has declared war.

The contract sanctity provision in the Export Administration Act of 1979, as amended, applies only to embargoes imposed for foreign policy reasons. It generally protects pre-existing contracts except when the President determines and certifies to the Congress that (1) a breach of the peace poses a serious and direct threat to the strategic interest of the United States, (2) interference with pre-existing contracts will be instrumental in remedying the threat, and (3) the export controls will continue only so long as the direct threat persists.

Finally, the Food Security Act of 1985 establishes, as a matter of policy, that embargoes on agricultural products should be imposed only in times of national emergency and that even in those instances pre-existing contracts should not be interfered with.

Second LBGA

After three rounds of negotiations, the United States entered into a second 5-year LBGA with the Soviet Union on August 25, 1983. The second agreement altered several provisions of the first agreement, including those dealing with quantity, type of grain, and additional sales. It also eliminated the escape clause. As in the first agreement, grain sales were to be made "at the market price prevailing for these products." Finally, the second agreement incorporated a quality provision.

Whereas a primary purpose of the earlier LBGA had been to minimize market disruptions caused by large, unanticipated Soviet purchases of U.S. grain, the second LBGA was signed at a time when grain was in oversupply on world markets. U.S. officials hoped that the new agreement would help to restore the U.S. reputation as a reliable supplier and begin to normalize U.S.-Soviet trade relations. Since the 1980 embargo, the Soviets had concluded LBGAs with Canada, Argentina, Brazil, and Hungary, which would supply much of the Soviet grain and soybean import requirements. As a result, the U.S. share of the Soviet grain market was expected to fall.

Under the second LBGA, the Soviets (1) agreed to purchase 9 mmt of wheat and corn, (2) could substitute soybeans and/or soybean meal at a ratio of one ton of soybeans for 2 tons of grain, but the minimum annual quantities of wheat and corn had to be no less than 4 mmt each, and (3) could purchase an additional 3 mmt of grain annually without advance notice or consultations.

When the United States entered into the negotiations with the Soviets for the second LBGA, the administration wanted to increase overall U.S. grain sales to the Soviets. The Soviets agreed to increase minimum annual grain purchases from 6 mmt to 9 mmt, including minimum wheat and corn purchases of 4 mmt each. Since the Soviets had been relying on U.S. corn to maintain their livestock production since the early 1970s, U.S. negotiators were apparently able to use U.S. domination in the corn market as leverage to increase Soviet purchases of U.S. wheat. The United States and the Soviets also agreed to include soybeans, which were to be used as livestock feed.

The amount of grain the Soviets could purchase over the minimum without consultation was increased from 2 mmt to 3 mmt, which the United States deemed acceptable in view of increasing U.S. grain production. The Soviets had initially wanted to increase the level of allowable additional purchases without consultation by more than 1 mmt to ensure food security and to provide for flexibility. However, when the minimum purchase level was increased to 4 mmt for both corn and wheat, the Soviets agreed to the 1-mmt increase.

The Soviets had believed that the short supply escape clause in the first LBGA was discriminatory since the United States could "escape" from minimum sales when U.S. supply was low but the Soviets could not "escape" from minimum purchases when their domestic production was high. During the 1983 negotiations, the Soviets proposed that this situation be equalized and no escape clause was included in the second agreement.

The Soviets wanted the second LBGA to include a grain quality provision while the United States did not, noting that no other U.S. customer received such governmental assurance. The United States ultimately did agree to the Soviet request, but the quality clause was not a guarantee per se. The second LBGA stated that the U.S. government was "prepared to use its good offices as appropriate and within the laws in force in the USA to be of assistance on the questions of the appropriate quality of the grain to be supplied from the USA to the USSR."

Grain Trade Under Second LBGA

While Soviet purchases of corn have essentially met the 4-mmt minimum specified in the second LBGA, wheat purchases totaled less than 3 mmt in 1985 and only 0.15 mmt in 1986. (See table I.6.) Total wheat exports during the 5 years were about 23.6 mmt, valued at about $2.8 billion, and corn exports about 36.1 mmt, valued at about $4.2 billion. In addition, exports of soybeans and soybean products amounted to 0.4 mmt in 1984, less than 50,000 metric tons in 1985, 1.5 mmt in 1986, 0.1 mmt in 1987, and 2.1 mmt in 1988, for a total of 4.1 mmt over the 5 years at a value of $925 million. Of the total wheat exports, the 13 mmt exported in 1987 and 1988 was subsidized through the Export Enhancement Program (EEP). (See below.) A total of about $450 million in subsidies was provided to U.S. exporters to make U.S. prices competitive during those 2 years.

Table I.6: U.S. Grain Exports to the Soviet Union During Second LBGA

Figures in million metric tons

Agreement Year[a]	Wheat	Corn	Total
1984	7.6	6.3	**13.9**
1985	2.9	14.5	**17.4**
1986	0.2	6.4	**6.6**
1987	4.1	3.9	**8.0**
1988	8.8	5.0	**13.8**
Total	**23.6**	**36.1**	**59.7**

[a]Year ending September 30.
Source: USDA.

Although they purchased only 2.9 mmt of wheat in 1985, the Soviets claimed that they were in compliance with the LBGA in that their combined total grain purchases in that agreement year were more than 18 mmt, far in excess of the agreed minimum of 9 mmt. They also noted that in the 1986 agreement year they purchased 1.5 mmt of soybeans; therefore, since the LBGA allows for one ton of soybeans to be counted as two tons of grain, their total (0.15 mmt of wheat, 6.5 mmt of corn, and 1.5 mmt of soybeans equaling 3.0 mmt of grain) was over 9.6 mmt of grain, which exceeded the agreed minimum of 9 mmt.

U.S. officials do not believe that the Soviets purchased the amounts of grain required in the LBGA in either agreement year, since the agreement contains no provision for combining wheat, corn, and soybean purchases. They noted that the agreement states that "the minimum annual quantities of wheat and corn shall be no less than 4 mmt each."

According to Soviet, USDA, and U.S. grain company officials, price was the primary reason that Soviet wheat purchases were below the minimum called for in the LBGA. The agreement stipulated no specific price for any commodity but rather called for grain sales to "be made at the market price prevailing for these products," and U.S. and Soviet officials interpreted this provision differently. USDA officials argued that, since the product cited in the agreement was clearly U.S. grain, the price cited was the prevailing U.S. price. On the other hand, the Soviets asserted that market price referred to the prevailing world wheat price, which sometimes was substantially lower than the U.S. price.

In addition to the price consideration, Soviet trade officials stated that concerns over U.S. grain quality and reduced hard currency caused them to curtail U.S. wheat imports. They also told us that a reorganization within the Soviet government in late 1985 caused delays in grain purchasing decisions. Price, however, appears to have had the greatest influence on Soviet purchases of U.S. grain.

During consultations with the Soviets, USDA officials pointed out that in prior years the Soviets had purchased U.S. grain when the U.S. price was somewhat above the world price. Soviet trade officials told us that premium prices had been paid in the past because superior U.S. port and storage facilities had allowed the Soviets to plan purchases and space shipments so that vessels arrived in Soviet ports at intervals to allow for offloading without clogging those ports.

Price Issue and the Export Enhancement Program

U.S.-Soviet differences over the price of U.S. grain were exacerbated by the fact that a U.S. agricultural export subsidy program, the Export Enhancement Program (EEP), which was established in May 1985, lowered the price of wheat to many importers, but not to the Soviet Union.[5] The price issue was fundamentally resolved in April 1987 when the United States offered wheat to the Soviets at competitive wheat prices through the EEP.

Through the EEP, USDA provides bonuses to U.S. exporters to enable them to sell at competitive prices. The EEP was generally targeted at customers of the European Community which the United States claimed was unfairly subsidizing its exports. A major objective of the EEP was to put pressure on the EC to come to the negotiating table with respect to liberalizing trade in agriculture. Initially, the EEP was not made available to the Soviet Union because of foreign policy reasons.[6] Consequently, the United States had lowered the price of wheat to such countries as Algeria, Egypt, and Morocco, but not to the Soviet Union. Soviet trade representatives told us that U.S. policy discriminated against the Soviet Union and so, beginning in the 1985 agreement year, the Soviets bought significantly less wheat from the United States.

To encourage the Soviets to purchase the minimum quantities of U.S. grain specified in the second LBGA, USDA made an offer of wheat to the Soviet Union through the EEP on August 1, 1986. There were no discussions between the Soviets and the United States prior to the offer being announced. Initially, USDA offered a bonus (subsidy) of $13 per metric ton to U.S. exporters for wheat sales to the Soviet Union, but this amount did not enable U.S. exporters to lower their prices sufficiently to induce Soviet purchases. The bonus was increased to $15 per metric ton 2 weeks later. The Soviets still did not purchase U.S. wheat offered through the EEP, and the offer expired on September 30, 1986, i.e., at the end of the 1986 agreement year. It should be noted that EEP offers to other countries were generally valid for one year but that the offer to the Soviet Union was valid only for the 2 months remaining in the 1986 agreement year. Soviet trade representatives told us that they did not buy U.S. wheat through the EEP because the U.S. price was simply too high despite the $15 bonus to U.S. exporters. The Soviets did purchase wheat from the EC at this time.

[5] It should be noted that while the EEP did lower prices to many importers of U.S. wheat, it was not offered to a number of key buyers of U.S. grain, including Japan and South Korea.

[6] See our report, Implementation of the Agricultural Export Enhancement Program (GAO/NSIAD-87-74BR) Mar. 1987.

In April 1987, following discussions in Moscow, the United States again offered wheat to the Soviets under the EEP. The new offer was for 4 mmt of wheat, the minimum amount called for in the LBGA, and was valid for one year. U.S. grain companies sold the wheat at $80 per ton, and bonuses provided by USDA ranged between about $40 and $45 per ton. During October 1987 consultations, Soviet representatives stated that the Soviet Union would buy U.S. grain only if the U.S. price met the world price. On several occasions, the Soviets noted that they were not asking the United States to provide grain at subsidized prices, only that the U.S. price be competitive with the prices of other exporters.

In the 1988 agreement year, the United States offered about 8.8 mmt of wheat to the Soviets under the EEP and the Soviets bought all the wheat available under the program. The bonuses provided by USDA ranged between $20 and $45 per metric ton. According to ERS, the weighted average of bonuses for the 13 mmt total of wheat provided under the EEP during the 2 years was $35 per ton. The total amount of subsidy provided during the 1987 and 1988 agreement years was about $166 million and $281 million, respectively.

Extension of Second LBGA

In March 1988, U.S. and Soviet officials began negotiations on a new LBGA since the current one was due to expire September 30. Major issues of controversy concerned quantity and price. The U.S. negotiating objective was to ensure substantially higher minimum annual Soviet purchases of grain than the 9 mmt under the earlier LBGA. The Soviets wanted more specific language regarding price but, according to a USDA official, the United States did not see the necessity for more specific language. The Soviets also wanted the LBGA to include a provision for better access for their ships to U.S. ports as well as a general commitment to increase bilateral trade between the two countries. After four negotiating sessions, the second LBGA expired without agreement on either a new LBGA or on an extension of the existing one. After two additional negotiating sessions, and failing to reach agreement on a new LBGA, U.S. and Soviet officials agreed on November 28 to extend the second LBGA 27 months, through December 1990. The Secretary of Agriculture and U.S. Trade Representative indicated that the extension would continue to stabilize grain trade between the two countries and added that the extension would facilitate future negotiations by allowing subsequent agreements to run concurrently with the Soviet Union's 5-year planning process.

If and when discussions begin again on a new LBGA, quantity and price are again likely to be issues. In addition, the issues of Soviet ship access to U.S. ports and increased bilateral trade are likely to be raised by the Soviets as they were during discussions leading to the extension of the second LBGA. If Soviet agricultural reform results in increased domestic grain production, it might affect the Soviets' continuing interest in the use of LBGAS.

Subsequent to the extension of the second LBGA, the United States offered 4 mmt of wheat to the Soviets through the EEP. As of January 31, 1989, the Soviets had purchased 2 mmt and the total amount of subsidy provided during the 6th agreement year was about $46 million as of that date.

LBGA With China

Background

In 1961, the Chinese began importing large quantities of wheat to enhance the nutrition of its urban population. The grain imports were initially considered temporary, but they continued, and through the early 1970s, Canada and Australia were the primary suppliers. In 1972, China purchased wheat and corn from the United States for the first time, and in 1973 U.S. grain sales represented 50 percent of Chinese grain imports. U.S. grain sales to China fluctuated widely, from none in some years to approximately 5 mmt in 1973 and again in 1978.

On October 21, 1980, the United States and China entered into a 4-year LBGA, effective January 1, 1981. At the time, China had LBGAs with Canada, Australia, Argentina, and France. According to U.S. officials, the United States entered into the 1981 agreement to increase its knowledge of the Chinese market and to expand grain sales to that potentially huge market. In concluding the agreement, U.S. officials noted that they were merely formalizing U.S. participation in the market and placing the United States on an equal footing with China's other major suppliers.

Whereas a primary purpose of the first U.S. LBGA with the Soviet Union was to minimize market disruptions caused by Soviet purchases of U.S. grain, Chinese grain purchases had never disrupted the U.S. grain market. According to USDA, the LBGA with China was recognition of China's enormous grain purchasing potential. Anticipated population growth and shifts to urban areas and Chinese policies designed to improve the standard of living were expected to result in increased Chinese grain imports.

According to USDA officials, the LBGA with China was also designed to enhance the U.S. image as a reliable supplier of grain. The agreement was negotiated shortly after the 1980 U.S. grain embargo to the Soviet Union. According to U.S. exporters, potential U.S. customers were expressing concern at that time that the United States was an unreliable supplier of grain.

Diplomatic relations were re-established between the United States and China on January 1, 1979, after 30 years of non-recognition of China by the United States. Early in 1980, a general trade agreement was ratified, providing most-favored nation status to both countries. U.S. agricultural sales to China totaled about $600 million in 1978, almost $1 billion in 1979, and were estimated at $2 billion in 1980 when the LBGA was signed. USDA viewed the grain agreement, along with the growth in trade, as a milestone in the U.S. relationship with China.

1981 LBGA

The 4-year LBGA with China provided for minimum quantities of grain to be purchased, annual consultations, and an escape clause. Specifically, the LBGA called for minimum annual purchases of between 6 and 8 mmt of wheat and corn, with corn representing approximately 15 to 20 percent of total sales. China could purchase 1 mmt over the maximum of 8 mmt without advance notice. Under "exceptional circumstances," the United States could supply less than the minimum quantities, but prior consultations between the two parties were required and supplies to other customers would have to be limited proportionally. Similarly, after prior consultations, China could limit its purchases to less than the minimum quantities, as long as it limited its purchases from other suppliers proportionally. It was agreed that transactions would be made at "prevailing market prices" in accordance with normal commercial terms.

The LBGA was intended to facilitate grain trade between the two countries. China was encouraged to meet any increased grain requirements by purchasing U.S. grain, and both countries were to avoid excessive volatility in their grain trade. China was to space its purchases of U.S. grain and the United States was to maintain stable U.S. market conditions.

Grain Trade Under the LBGA

Over the 4 years the LBGA was in effect, the Chinese purchased about 20.8 mmt of wheat, valued at about $3.3 billion, and about 3.5 mmt of corn, valued at about $400 million, as shown in table II.1.

Table II.1: U.S. Grain Exports to China During the LBGA

Figures in million metric tons

Year	Wheat	Corn	Total
1981	7.4	0.5	**7.9**
1982	6.8	1.6	**8.4**
1983	2.5	1.4	**3.9**
1984	4.1	0.0	**4.1**
Total	**20.8**	**3.5**	**24.3**

Source: USDA.

As shown, total grain sales were well above the 6-mmt minimum during the first 2 years of the agreement but represented only about two thirds of the minimum during each of the last 2 years. Furthermore, the LBGA called for corn to represent approximately 15 to 20 percent of total grain sales (at least 0.9 of the 6 mmt of grain), and purchases of corn were below that amount in 1981, a year when total grain sales were relatively high. Purchases of wheat dropped precipitously in 1983, and there was a 2.1-mmt shortfall from the 6-mmt minimum amount specified in the LBGA.

In consultations with the United States, the Chinese indicated that the 1983 shortfall would be made up in 1984 and that the 6-mmt minimum for 1984 would be honored as well. However, 1984 purchases were again well below the minimum and did not include corn. The shortfall in 1983 coincided with improved grain harvests in China and with a dispute between the two countries over U.S. imports of Chinese textiles. In January 1983, the United States imposed quotas on imports of Chinese textiles and China retaliated by decreasing its purchases of U.S. grain and cotton. After the textile conflict was resolved in July 1983, China made several assurances to purchase the minimum amounts of grain specified in the LBGA, but it did not do so.

According to a Chinese trade official, once the textile controversy was resolved, China did begin purchasing U.S. grain. However, as Chinese production was increasing dramatically at that time, China had a limited need for imported grain. Agricultural production increased because of (1) an incentive program which provided additional income to farmers for increased production, (2) a government policy that attempted to match crops with land best suited for them, (3) irrigation projects, (4) education of the farmers, (5) favorable weather, and (6) increased use of fertilizers. During the 4 years that the LBGA was in effect, China moved from being a corn importer to a corn exporter.

Table II.2: Chinese Corn and Wheat Production and Imports

Figures in million metric tons

	Corn		Wheat	
Year	Production[a]	Imports[b]	Production[a]	Imports[a]
1976	48.0	0.0	50.4	3.2
1977	49.5	0.1	41.1	8.6
1978	55.9	3.0	53.8	8.0
1979	60.0	2.0	62.7	8.9
1980	62.6	0.8	55.2	13.8
1981	59.2	1.1	59.6	13.2
1982	60.3	2.6	68.4	13.0
1983	68.2	0.1	81.4	9.6
1984	73.4	0.1	87.8	7.4
1985	63.8	0.4	85.8	6.6
1986	70.9	1.6	90.0	8.5
1987	79.8	0.2	87.8	15.0
1988[c]	75.0	0.2	87.5	15.0

[a]Year ending June 30.

[b]Year ending September 30.

[c]Estimate.
Source: USDA.

During the early 1980s, the world's grain supply increased dramatically. U.S. grain prices were somewhat higher than world prices at this time. Consequently, China reduced its grain purchases from the United States. Also, Chinese officials said they informed USDA during routine consultations about the low quality of U.S. grain. These officials were primarily concerned that the insecticide sprayed on grain to minimize insect infestation might make it unsafe for human consumption. They also noted other quality issues, including foreign materials and dirt, insects, and high moisture levels. According to ERS, Chinese complaints of low quality were widely considered to be an excuse and the real reason for lower imports was China's reduced needs.

According to the terms of the LBGA, China was allowed to reduce grain purchases below the agreement levels "by virtue of exceptional circumstances." However, prior consultations were required and, according to a USDA official, China did not request consultations concerning its intention to purchase less than the minimum amount of total grain in 1983 and 1984.

The LBGA further required China to proportionally reduce grain purchases from other suppliers in the event of "exceptional circumstances." However, it purchased about 400,000 metric tons of corn less than the 900,000 tons suggested in the LBGA in 1981 while it increased its corn purchases from Thailand by 2,000 tons. Also, China purchased no corn from the European Community in 1980, but it purchased 18,000 tons in 1981. In 1984, China purchased no corn from the United States after having imported over 1.3 MMT in 1983. While China did reduce its purchases of corn from Argentina in 1984, it did not reduce its purchases from Thailand proportionally.

China's purchases of U.S. wheat also fell below the agreed minimums in both 1983 and 1984, but it did not always proportionally reduce purchases from other suppliers. As shown in table II.3, China actually increased its purchases of wheat in 1983 from three of the four countries that compete with the United States. In 1984, Chinese wheat purchases from the United States increased, but they were still below the LBGA minimum and Chinese purchases of Australian wheat increased dramatically.

Table II.3: Chinese Wheat Imports From Major Grain Suppliers

Figures in million metric tons

Grain Supplier	1981	1982	1983	1984
Argentina	0.1	0.1	2.9	(a)
Australia	1.3	2.1	0.4	2.3
Canada	3.0	3.5	4.7	3.2
EC	0.6	0.7	0.9	(a)
United States	7.6	6.9	2.5	4.1

[a]Less than 50,000 metric tons.
Source: USDA.

Grain Trade Since the LBGA

During the 2 years after the LBGA expired, in 1985 and 1986, U.S. grain sales to China decreased drastically, but thereafter sales increased significantly. See table II.4.

Table II.4: U.S. Grain Exports to China Since the LBGA

Figures in million metric tons

Year	Wheat	Corn	Total
1985	0.7	0.0	**0.7**
1986	0.0	0.1	**0.1**
1987	1.9	1.3	**3.2**
1988[a]	5.7	0.0	**5.7**
Total	**8.3**	**1.4**	**9.7**

[a]Through November 30, 1988.
Source: USDA.

China continued to purchase wheat on the world market after 1984, but made a decision not to purchase grain through LBGAs. The U.S. market share of Chinese wheat imports was less than 10 percent during 1985 and 1986, primarily because of the relatively high U.S. price. Chinese trade officials told us that the U.S. policy of not offering subsidized wheat to China under the EEP was discriminatory. China, in fact, requested that the United States offer grain under the program on several occasions.

In January 1987, China was offered wheat for the first time under the EEP. During 1987, the United States offered and the Chinese purchased 4 mmt of wheat under the EEP, and during 1988, about 7.2 mmt. The total amount of subsidy provided during the two years was about $330 million. With respect to corn, China's circumstances have changed. According to an Economic Research Service official, China has been a net exporter since 1984/85 and is committed to export 7.5 mmt yearly. Current Chinese policy is to purchase grain as needed on the open market and not to enter into any long-term grain agreements.

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