United States General Accounting Office

GAO

Testimony

Before the Committee on Agriculture, House of Representatives

For Release on Delivery
Expected at
1:30 p.m., EDT
Wednesday,
June 14, 1995

AGRICULTURAL TRADE

Competitor Countries' Foreign Market Development Programs

Statement of Allan I. Mendelowitz, Managing Director
International Trade, Finance, and Competitiveness
General Government Division

AGRICULTURAL TRADE: COMPETITOR COUNTRIES' FOREIGN MARKET DEVELOPMENT PROGRAMS

SUMMARY OF STATEMENT BY ALLAN I. MENDELOWITZ, MANAGING DIRECTOR INTERNATIONAL TRADE, FINANCE, AND COMPETITIVENESS GENERAL GOVERNMENT DIVISION

As Congress develops the 1995 Farm Bill and determines what support to provide for export programs, one consideration is the activities of our major competitors. The multilateral trade agreement of the Uruguay Round of the General Agreement on Tariffs and Trade will reduce agricultural subsidies but will not limit funding for market development activities such as advertising, retail promotions, and market research.

GAO's recent report on foreign market development programs for high-value products in France, Germany, the United Kingdom, and the Netherlands found that although these countries spend far more than the United States for total agricultural support, they spent much less on foreign market development of high-value products in 1993, the year for which GAO collected data. Furthermore, foreign market development was financed primarily by the private sector in the European countries but by the government in the United States.

The Market Promotion Program (MPP) is the U.S. Department of Agriculture's major foreign market development program. GAO has raised concerns about the effectiveness of MPP-funded activities and the inability to assure that the program is funding additional activities rather than simply replacing funds that would have been spent anyway. Because many of our European competitors rely more on private sector funding for their marketing organizations, they have greater incentive for assuring that promotional activities are effective, and there are fewer concerns about additionality.

The United States already has in place structures similar to the privately funded European marketing organizations--the U.S. "check-off" marketing boards. However, these boards focus on domestic promotion and spend little of their own money on export promotion of high-value products. Relying more on the U.S. private sector to fund the cost of foreign market development through an alternative such as a check-off program offers the option of reducing government expenditures while still maintaining our foreign market development efforts.

Another issue related to agricultural competitiveness is the activities of state trading enterprises (STEs). STEs are entities that engage in trade and that are owned, sanctioned, or otherwise supported by the government. GATT contains provisions designed to prevent STEs from becoming obstacles to trade and requires member countries to report on the impact their STEs have on trade. Compliance with GATT reporting requirements has been low, so little information about STEs exists. The Uruguay Round agreement contained several measures designed to improve reporting of STEs, but it is too early to tell if these measures will be effective.

Mr. Chairman and Members of the Committee:

I am pleased to be here today to testify before this Committee about the foreign market development activities for agriculture of competitor countries and their implications for U.S. foreign market development. In addition, at your request I will be providing you with a status report on our review of state trading enterprises (STEs).

A CHANGING TRADE ENVIRONMENT

As Congress writes the 1995 Farm Bill, the U.S. Department of Agriculture (USDA) and the U.S. agricultural sector face a changing environment for world agricultural trade. New markets are emerging in East Asia, Latin America, Eastern Europe, and elsewhere that have the potential to become major consumers of imported agricultural products. The composition of agricultural exports is changing as well. U.S. and world agricultural trade no longer consists primarily of trade in a few major bulk commodities, such as corn, wheat, and soybeans. Two-thirds of total world agricultural trade and over half of U.S. agricultural trade now consist of high-value products, such as fresh fruits and vegetables, dairy products, and processed foods. International agricultural trade is also becoming increasingly competitive, as more of our competitors use sophisticated marketing practices, and as new countries, particularly in the developing world, seek to develop markets for their exports.[1]

The new multilateral trade agreement of the General Agreement on Tariffs and Trade (GATT), commonly referred to as the Uruguay Round (UR) agreement, will also affect agricultural trade. It will provide greater market access and thus more opportunities for increasing U.S. exports. It will also limit the extent to which the United States and our competitors, particularly in the European Union (EU), can provide subsidies to the agricultural sector to support exports.

THE ROLE OF FOREIGN
MARKET DEVELOPMENT

The U.S. government currently has a number of programs and activities designed to help increase agricultural exports. These programs, which were valued at $6.6 billion in fiscal year 1994, include direct export subsidies, food assistance programs, USDA's Foreign Agricultural Service's (FAS) attaché service, export credit guarantee programs, and market development programs. In today's tight budget environment, Congress is looking carefully at the need for all government programs and expenditures, including expenditures for promoting exports. To assist Congress

---

[1]See International Trade: Market-Oriented Strategy Would Help Lead U.S. Agriculture Into the Future (GAO/T-GGD-94-177, June 23, 1994).

as it develops the 1995 Farm Bill and considers what support if any to provide for export programs, my statement today will focus on what some of our major competitors are doing with regard to foreign market development for high-value products, and whether the United States could apply the competition's experiences to U.S. conditions. These observations are based on past GAO reviews of U.S. and competitor country market development programs.

Foreign market development is, of course, only one type of export promotion or assistance. Other types include direct export subsidies, domestic subsidies, and internal price supports, which also affect exports. While we will not be focusing on these other forms of support today, it should be recognized that governments in the EU spend far more than the United States for total agricultural support. According to FAS, total EU agricultural spending was $44.4 billion in 1993, including $11.7 billion in direct export subsidies. In comparison, total U.S. agricultural spending was $16 billion in fiscal year 1993, including $1.2 billion in direct export subsidies. These European export subsidies support not just bulk products, but also high-value products such as meats, dairy, fruits, and vegetables.

Foreign market development includes programs and activities such as advertising, consumer promotion, trade servicing, and market research. Market development is more often aimed at promoting high-value products rather than bulk commodities. Unlike purchasing decisions for bulk commodities, which are based largely on price, purchasing decisions for high-value products depend also on product attributes like brand name, packaging and quality image and are thus more affected by an exporter's skill in developing and marketing the product.

The multilateral trade agreement of the GATT Uruguay Round will reduce the extent to which countries can provide export subsidies to agriculture, including high-value products. However, the UR agreement does not limit the extent to which countries can fund market development activities. There has been some concern that the UR agreement may therefore lead European governments to shift funds previously spent on export subsidies toward market development programs. However, early indications are that this is not the case. In cables sent this year, FAS attachés in Europe reported they have not seen signs of plans to increase government funding of foreign agricultural market development in most EU countries; many countries, in fact, plan to reduce government support for market development in the coming years.

It should be noted that foreign market development is only one of many factors that help determine a country's agricultural exports. A country's foreign currency exchange rate and the underlying competitiveness of its food and agricultural industry are key. Agricultural support policies and direct export subsidies also play a role. As a result, it is very difficult to make definitive judgments about the effectiveness of any country's efforts to develop foreign markets.

FOUR EUROPEAN COUNTRIES' SPENDING ON FOREIGN MARKET DEVELOPMENT

We recently examined the foreign market development programs of four European countries--France, Germany, the United Kingdom, and the Netherlands--and compared them with the foreign market development programs of the United States.[2] The four European countries are among the world's largest exporters of high-value products and compete with U.S. exporters on many products. While these countries spend far more than the United States in total agricultural support and export subsidies, this was not the case for market development. All four European countries we reviewed spent less on their foreign market development programs than did the United States in 1993 as a percentage of high-value product exports. Furthermore, foreign market development was financed primarily by the private sector in the European countries but by the federal government in the United States.

Total spending in 1993 on foreign market development programs for high-value products (including both public and private spending) varied considerably in the four competitor countries, ranging from about $13 million for the United Kingdom to about $76 million for France, based on FAS estimates and information provided by the European marketing organizations. The United States, in comparison, spent about $151 million in 1993 on foreign market development for high-value products, mostly through USDA's Market Promotion Program (MPP).

The United States also spent more on foreign market development than each of the four European countries as a percentage of high-value product exports. For every $10,000 in high-value product exports, the United States, including both public and private spending, spent about $65 on foreign market development, compared with $30 by France, $21 by the Netherlands, $19 by Germany, and $15 by the United Kingdom.

The European countries' foreign market development programs are financed mostly by the private sector, generally through mandatory producer levies or user fees. Foreign agricultural market development programs in the United States, however, rely more on government spending, primarily through MPP. Government expenditures in the four European countries represented from zero

[2]See Agricultural Trade: Five Countries' Foreign Market Development for High-Value Products (GAO/GGD-95-12, Dec. 14, 1994).

percent to 42 percent of the country's total spending on programs for foreign market development in 1993. By contrast, the U.S. government funded about 80 percent of all U.S. spending on programs for foreign market development of high-value products in 1993.

DIFFERENCES IN U.S. AND EUROPEAN FOREIGN MARKET DEVELOPMENT

The European marketing organizations we reviewed carry out foreign market development activities similar to those in the United States. The activities conducted generally include market research, consulting services, trade servicing, consumer promotions, advertising, and sponsorship at trade shows.

While European activities are generally similar, U.S. programs tend to place more emphasis on consumer advertising than do the European programs. U.S. companies or producer groups often use MPP funds to finance product advertising campaigns, which tend to be an expensive form of market promotion. European marketing organizations tend to focus more on less expensive activities like trade shows and in-store promotions rather than direct media advertising.

In addition, the fundamental structure for foreign market development is different in three of the four European countries than in the United States. France, Germany, and the United Kingdom each rely primarily on a centralized marketing organization to promote their exports. Each country's major marketing organization promotes nearly all of its high-value products and provides an array of services to exporters. The Netherlands does not have a single primary market development organization but rather a number of independent commodity boards and trade associations. The United States has a decentralized system whereby not-for-profit trade associations conduct most high-value product marketing activities overseas, with their money derived largely from federal funds.[3]

COMPARING THE EXPERIENCES OF OTHERS TO USDA'S MARKET PROMOTION PROGRAM

[3]Most of these funds come from MPP, which focuses on high-value products. The USDA's Foreign Market Development Program, known as the Cooperator Program, also supports foreign market development, mostly for bulk products. FAS also provides a variety of services to U.S. agricultural exporters through its attaché service and through its AgExport Services Division. This division helps fund such promotional activities as trade shows, publications, and trade missions.

MPP, which serves as USDA's major foreign market development program for high-value products, has come under increasing scrutiny over the years. In the past, we have expressed several concerns about the program. As we have testified,[4] the large number of variables that determine export levels makes it very difficult to show how the amount spent on MPP affects the level of U.S. agricultural exports. Furthermore, FAS has no way of assuring that money provided under the program is supporting additional promotional activities rather than simply replacing funds that private industry would have spent anyway. Also, FAS lacks criteria to determine when MPP participants no longer continue to need federal funding and should be graduated from the program.

The foreign market development programs of many of our European competitors do not face these issues to the same degree since their market development activities are conducted and prioritized by organizations funded largely by the private sector. Increased private sector funding creates incentives for effective programs since producers and exporters have more of their own money at stake. It also diminishes concern over whether or not public money is being given to producers to fund activities they would have undertaken anyway with their own funds.

The United States already has in place structures similar to the European marketing organizations. Generic promotion and research programs funded through voluntary industry contributions have existed at the local, state, and regional levels for more than 50 years. In addition, there are 19 federally authorized generic promotion and research programs, commonly known as "check-off" programs. These check-off programs, run by marketing boards such as the American Egg Board, the Honey Board, and the National Pork Board, conduct research and promotional activities with funds raised from a small mandatory levy on producers or other members of an industry.

In several foreign countries, these types of national agricultural marketing programs--with funds raised at least partially through levies on the private sector--play a major role in those countries' export promotion activities. By contrast, most U.S. marketing boards that promote high-value products focus primarily on the U.S. domestic market. They spend a small portion of their own funds for export activities.[5]

---

[4]See U.S. Department of Agriculture: Improvements Needed in Market Promotion Program (GAO/T-GGD-93-17, Mar. 25, 1993).

[5]See Agricultural Marketing: Comparative Analysis of U.S. and Foreign Promotion and Research Programs (GAO/RCED-95-171, Apr. 28, 1995).

If Congress wishes to maintain a foreign market development program and reduce government spending, relying more on the U.S. private sector to fund the cost of foreign market development through an alternative such as a check-off program offers an option. It could serve to reduce government expenditures in a time of tight budgets without necessarily reducing the amount of funds available for foreign market development. It could also increase the incentives for assuring that foreign market development activities are effective, since those who benefit from the activities would have more of their own money at risk.

- - - - -

PRELIMINARY REVIEW OF
STATE TRADING ENTERPRISES

Mr. Chairman, in addition to my testimony on foreign market development, I would like to briefly add some remarks on the activities of state trading enterprises, known as STEs. STEs are generally considered to be government or nongovernment entities that engage in trade and are owned, sanctioned, or otherwise supported by the government. Generally accepted examples include the Australian Wheat Board, the Canadian Wheat Board, and the New Zealand Dairy Board. As you know, you and 17 other members of the House and Senate requested that we report on the activities of agricultural STEs in the post-Uruguay Round world trading environment. I would like to give you an overview of our preliminary observations.

I mentioned at the beginning of my testimony that new agricultural markets are emerging throughout the world. The activities of STEs in the agriculture sector are relevant to U.S. producers and exporters as they attempt to sell U.S. agricultural products abroad. Some STEs are primarily engaged in export activities and may compete with U.S. exporters for access to third-country markets. Other STEs are primarily engaged in import activities and may determine the extent to which U.S. products are able to enter their countries' markets. The activities of STEs are also relevant to U.S. producers who sell only in the domestic market, as some STEs export their products to the United States.

ARTICLE XVII OF GATT
ADDRESSES STES

STEs are generally subject to GATT disciplines and are specifically addressed in article XVII of GATT. STEs in the agriculture sector are also subject to the new disciplines on agricultural trade that resulted from the Uruguay Round.

When GATT was established in 1947, some member countries had active state trading programs and wanted to ensure their governments' right to engage in market activities. However, it was recognized that when governments have a dual role as market regulator and market participant, they can act in ways that protect domestic producers and disadvantage foreign producers. The drafters of GATT recognized that STEs, especially those with a monopoly of imports or exports, could be operated so as to create serious obstacles to trade. To address this concern, GATT states, in essence, that member countries' STEs should make purchases or sales in accordance with commercial considerations and should not deliberately discriminate against foreign competition. The GATT also requires that STEs permit the enterprises of other members to compete for these purchases and sales in accordance with customary business practice.

Article XVII establishes a number of guidelines and requirements with respect to STE operations. For example, it stipulates that

-- STEs shall act in a manner consistent with the principles of nondiscriminatory treatment;

-- STEs shall make any purchases or sales in accordance with commercial considerations and shall allow enterprises from other member countries the opportunity to compete;

-- member countries shall notify other GATT members of the products imported into and exported from their territories by STEs; and

-- member countries are not required to provide confidential information that (1) would impede law enforcement, (2) would be contrary to the public interest, or (3) would prejudice their STEs' legitimate commercial interests.

Additional requirements for reporting information about STEs were contained in a questionnaire published in 1960. Every 3 years, GATT members are to provide full responses to this questionnaire that asks them to list their STEs, the products for which STEs are maintained, and the reason and purpose for maintaining STEs. It also asks them to provide certain information about how their STEs function and statistics that indicate the extent of trade accounted for by STEs. Ideally, the information collected should provide enough transparency over STE operations to determine whether or not STEs, because of their relationships with their governments, are creating unfair obstacles to trade.

Also, according to article II (para. 4), countries that have negotiated with other GATT members to provide a certain level of protection for domestic producers cannot allow their STEs to operate in a way that affords a level of protection greater than was negotiated. In addition, references generally made in GATT to import or export restrictions include those made effective through STEs.

Because of definitional and procedural weaknesses, GATT member countries have generally viewed article XVII as ineffective, and compliance with the requirements of article XVII has been poor. Comparatively few countries have provided information to GATT about STEs, and the information that has been provided has done little to illuminate the full nature and extent of STEs in GATT member countries, how they operate, or their impact on world trade.

The UR agreement attempted to address some of these problems through an Understanding on the Interpretation of Article XVII. The understanding provided a definition of STEs and implemented procedural measures designed to improve the information available about STEs and the level of compliance with article XVII. For example, the understanding allows GATT members to challenge the information other countries submit about their STEs through a process called "counternotification." It also sets up a working party that is charged with reviewing information received about STEs and making recommendations, if necessary, to modify the questionnaire in order to obtain better information.

In the post-Uruguay Round environment, some officials of the new World Trade Organization (WTO) said they expect the number of countries reporting STEs to increase. However, because the next set of responses to the questionnaire is not due until June 30, 1995, it is too early to tell whether the changes resulting from the Uruguay Round will lead to a better understanding of the activities of STEs.

The effectiveness of article XVII is especially important given that countries like the People's Republic of China, Russia, and Ukraine have applied to join GATT/WTO. These countries' economies, and others like them, are dominated or heavily influenced by national and local governments. While some of these countries are undertaking privatization efforts to move toward more market-oriented economies, the role of STEs in GATT/WTO will increase if these countries become members.

The U.S. Trade Representative (USTR) and FAS are both involved in monitoring the activities of other countries' STEs and the disciplines placed on them. USTR officials participate in the working party on article XVII, which will monitor compliance with the new requirements related to STEs. USTR officials also participate in the Committee on Agriculture, which will monitor implementation of UR commitments in the agriculture sector. While the committee presently has a small role relative to STEs, USTR and FAS officials have communicated to GATT/WTO officials and members that the United States hopes to engage in further discussions about agricultural STEs within the committee. Additionally, FAS staff monitor STE activities in the countries where the staff are located and prepare reports about what they learn.

- - - - -

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

(280141)

Ordering Information

The first copy of each GAO report and testimony is free. Additional copies are $2 each. Orders should be sent to the following address, accompanied by a check or money order made out to the Superintendent of Documents, when necessary. Orders for 100 or more copies to be mailed to a single address are discounted 25 percent.

Orders by mail:

U.S. General Accounting Office
P.O. Box 6015
Gaithersburg, MD 20884-6015

or visit:

Room 1100
700 4th St. NW (corner of 4th and G Sts. NW)
U.S. General Accounting Office
Washington, DC

Orders may also be placed by calling (202) 512-6000
or by using fax number (301) 258-4066, or TDD (301) 413-0006.

Each day, GAO issues a list of newly available reports and testimony. To receive facsimile copies of the daily list or any list from the past 30 days, please call (301) 258-4097 using a touchtone phone. A recorded menu will provide information on how to obtain these lists.

United States
General Accounting Office
Washington, D.C. 20548-0001

Bulk Mail
Postage & Fees Paid
GAO
Permit No. G100

Official Business
Penalty for Private Use $300

Address Correction Requested