

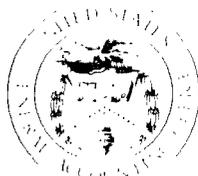
GAO

Report to the Chairman, Subcommittee
on Economic Resources and
Competitiveness, Joint Economic
Committee, U.S. Congress

May 1990

ECONOMIC
ASSISTANCE

Integration of
Japanese Aid and
Trade Policies



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**National Security and
International Affairs Division**

B-239036

May 24, 1990

The Honorable David R. Obey
Chairman, Subcommittee on Economic
Resources and Competitiveness
Joint Economic Committee
Congress of the United States

Dear Mr. Chairman:

This report responds to your request that we review Japanese foreign economic assistance and trade policies and determine the extent to which Japan integrates these policies. You expressed concern that U.S. foreign assistance programs are not integrated with U.S. international trade policies. Therefore, we also present information on U.S. programs and policies.

We limited our review to economic assistance programs, and thus excluded military assistance and Export-Import Bank lending.

Historically, promoting trade interests has been an important motivating factor behind Japanese assistance, producing a program that provides comparatively great commercial benefits due to its sectoral and geographic concentration. Japanese economic assistance is heavily oriented toward infrastructure projects. Such projects can provide significant commercial benefits, as they tend to require procurement of high value added goods with subsequent need for maintenance and repair, and can open new markets for donor country firms. Also, Japanese assistance is provided primarily to Asian countries, where it reinforces existing Japanese trade relationships. Japan requires recipients to procure significant portions of assistance-financed goods and services in Japan. Certain other aspects of the Japanese system also help to ensure that commercial benefits will accrue to Japan, primarily through a relatively high degree of private sector involvement in development assistance project planning and administration.

Japanese economic assistance funding has greatly expanded in recent years, largely as a means for Japan to make a contribution to responsibility sharing among leading western industrialized countries, commensurate with its status as an economic power. Japan has taken a series of actions to liberalize procurement requirements and to expand the program's geographic and sectoral focus. Nonetheless, the program largely

retains its traditional focus and so continues to be more commercially oriented than U.S. assistance.

The United States also requires recipients to utilize a significant portion of assistance funds to procure goods and services from U.S. firms. However, U.S. economic assistance has a different focus, which results in less of a direct commercial orientation. Trade promotion has not been a prominent consideration in U.S. assistance efforts. U.S. assistance is intended to advance several goals, including support for basic human needs and economic restructuring. The United States concentrates its economic assistance in countries of particular security and political interest with which the United States does not necessarily conduct a great volume of trade. The United States provides comparatively little support for projects in areas, such as transportation, construction, and telecommunications, that can provide substantial commercial opportunities. U.S. emphasis on economic restructuring may provide trade and investment benefits in the long term, as recipient economies improve and open up to foreign private investment.

The United States could increase the commercial orientation of its foreign assistance programs by emphasizing projects that provide greater trade opportunities and by assigning greater weight to U.S. foreign trade patterns in allocating funds among recipient countries. However, such changes would clearly require difficult choices among the numerous competing demands on the U.S. program, especially in light of federal spending limitations. U.S. assistance could also be more closely tied to procurement in the United States. However, this would have a limited trade impact without a corresponding shift in the sectoral focus of U.S. assistance. Also, reducing linkages between foreign assistance and trade promotion for all donor countries has been a long-standing U.S. policy objective.

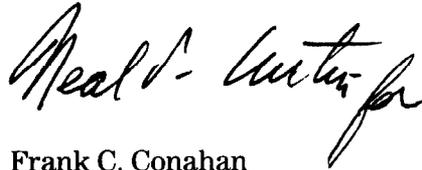
Further information on the results of our review are in appendix I. Appendix II presents details on the tying of U.S. assistance to procurement in the United States. Appendix III provides additional information on disbursement of U.S. assistance funds to U.S. and non-U.S. sources. Our scope and methodology are in appendix IV.

We did not obtain written agency comments on this report. However, we discussed it with officials of the Department of State and the Agency for International Development, and their comments have been incorporated in the report where appropriate.

As arranged with your office, unless you publicly announce its contents earlier, no further distribution of this report will be made until 30 days from its issue date. At that time, copies of this report will be sent to the appropriate congressional committees; the Administrator of the Agency for International Development; the Secretary of State; and other interested parties.

This report was prepared under the direction of Harold J. Johnson, Director, Foreign Economic Assistance Issues, who may be reached on (202) 275-5790 if you or your staff have any questions. Other major contributors are listed in appendix V.

Sincerely yours,

A handwritten signature in cursive script, appearing to read "Frank C. Conahan".

Frank C. Conahan
Assistant Comptroller General

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Abbreviations

| | |
|-----|--------------------------------------|
| AID | Agency for International Development |
| DA | Development Assistance |
| ESF | Economic Support Fund |

AID and Trade Policy Integration

Japan now ranks with the United States as one of the world's two largest source countries for foreign economic assistance. In the early 1970s Japan disbursed about one-third as much assistance as the United States. However, as shown in table I.1, Japanese economic assistance has increased rapidly since then, while U.S. spending has remained comparatively level.

Table I.1: Comparison of U.S. and Japanese Net Economic Assistance Volume, 2-Year Averages^a

| Dollars in millions | | | | |
|---------------------|---------|---------|---------|---------|
| | 1970-71 | 1975-76 | 1980-81 | 1987-88 |
| United States | \$8,006 | \$7,997 | \$8,480 | \$9,201 |
| Japan | 2,677 | 3,062 | 5,463 | 7,756 |

^aAmounts are expressed in constant 1987 dollars and exchange rates. Repayments on earlier loans are taken into account in producing this table of net amounts. Both Japan and the United States have large loan volumes outstanding.

Source: Organization for Economic Co-operation and Development, Development Assistance Committee.

In 1988, Japan's net disbursements for economic assistance amounted to about \$9.1 billion, while net U.S. disbursements were about \$9.8 billion.¹ Expressed as a percentage of Gross National Product, Japanese assistance rose from .23 to .32 percent between 1970 and 1988, while the U.S. commitment declined from .31 to .20 percent. Both countries provide substantial portions of this assistance through multilateral organizations—about 25 percent of total commitments for Japan in 1987 and about 21 percent for the United States.

Subsidized loans make up the largest portion of bilateral Japanese assistance. They accounted for about 60 percent of disbursements to recipients in 1987. Most of the remainder was divided between grants for development projects and programs (about 19 percent) and technical assistance (about 16 percent). Two agencies created specifically for such purposes implement most of this assistance—the Overseas Economic Cooperation Fund for loans, and the Japan International Cooperation Agency for most grants.

Most U.S. bilateral economic assistance obligations are made under three programs, administered primarily by the Agency for International

¹United States military assistance, commonly included in congressional deliberations on U.S. foreign assistance, is excluded from this review. In recent years, military assistance has made up slightly more than one-third of total U.S. foreign assistance. In 1989, for example, including these funds would raise the U.S. total from \$9.7 to \$15.1 billion.

Development (AID)—Development Assistance (DA), the Economic Support Fund (ESF), and Food for Peace. About 27 percent of the 1987 bilateral obligations were made under DA, which supports projects in various areas, ranging from agriculture to science and technology. About 47 percent of the 1987 obligations were made under ESF, which provides project support, cash transfers, and support for commodity imports to address economic, structural and development problems in countries of particular security and political interest to the United States.² About 18 percent were made through Food for Peace, which provides food aid through grants and loans for procurement of U.S. agricultural commodities.³ With the exception of Food for Peace loans, nearly all of this assistance is provided as grants.⁴

Commercial Orientation of Japanese Assistance

Japan's economic assistance system has been more heavily influenced by commercial considerations than has the U.S. system. Japanese assistance programs have their origins in post-World War II war reparations efforts. However, export promotion was clearly a primary consideration in these programs' early development. Ensuring access to vital raw materials and creating a favorable climate for investment overseas have also been important influences on Japanese aid policy. These concerns prompted concentration of Japanese funds in Asian countries where Japan has had historically close economic and political ties.

Commercial considerations have also been a factor in Japan's focus on improving recipient country economic infrastructure. These considerations have reinforced the Japanese conviction that adequate infrastructure provides the basis for real private sector-led growth and, therefore, should be the focus of economic assistance efforts.

Compared with other types of development work, economic infrastructure projects provide relatively greater opportunities for Japanese firms to realize commercial benefits. These projects tend to be capital intensive and require procurement of large amounts of high value added goods that can be provided by donor countries, such as construction, transportation, and telecommunications equipment. Follow-on economic

²About 54 percent of the 1987 obligations made through the DA and ESF programs supported specific projects; about 41 percent was distributed as ESF cash transfers; and about 5 percent went for ESF commodity import programs.

³The remaining 8 percent was comprised of a variety of programs, including migration and refugee assistance, the Peace Corps, and international narcotics control.

⁴Loans constituted about 6 percent of non-food aid disbursements in 1987.

benefits can be realized by providing maintenance services and replacement parts.

Of potentially greater importance, substantial market entry opportunities may be achieved through provision of goods that establish donor country firms in recipient country markets in such areas as transportation or telecommunications. Infrastructure work also provides the means necessary for Japan to obtain needed raw materials from recipient countries.

As Japan's economy has grown, it has identified economic assistance as a non-military vehicle through which it can make a larger contribution to responsibility sharing among leading industrialized countries. Japan has no basic foreign aid law, its legislature (the Diet) provides little policy guidance, and no single ministry is in charge of economic assistance. Decisions are made by negotiation among several government agencies, notably the Ministries of Foreign Affairs, Finance, and International Trade and Industry, each with its own interests and objectives. The orientation of the program is continuously shaped by these discussions. Narrowly defined commercial benefits continue to be a factor, but the aid program is now regarded as a means for Japan to play a larger positive role in the international community. International pressure from the United States and other countries has been a leading consideration in the recent funding increase. Raising assistance spending is regarded as an appropriate means for Japan to act in a non-military manner to take on greater global responsibilities commensurate with its economic strength.

Until the early 1970s, a large portion of U.S. economic assistance was devoted to infrastructure projects. However, a major re-evaluation of the U.S. program resulted in "New Directions" legislation instructing AID to emphasize basic human needs activities. Infrastructure work, and associated opportunities for capital goods exports, have declined greatly since then.

U.S. economic assistance has many officially designated goals but, with the exception of the Food for Peace program, direct trade promotion is not a prominent consideration.⁵ In fact, reducing donor country linkages between foreign assistance and trade promotion has been a U.S. policy objective since the mid-1970s. U.S. policy has emphasized addressing

⁵Developing export markets for U.S. agricultural commodities is a primary objective for the Food for Peace program, which is authorized under the Agricultural Trade and Development Act of 1954.

basic human needs and integrating developing economies into the international economic system. The ESF is oriented toward advancing such goals in the interest of stability and security in countries of strategic/political importance to the United States.

Congressional earmarking, mainly for specific countries, but also for functional programs, controls the allocation of nearly all ESF funds and about half of DA funds, limiting AID's ability to fund infrastructure projects in most countries. Sufficient amounts are currently allocated to permit capital projects in the larger non-cash transfer recipients of ESF assistance (e.g., Egypt, Pakistan, the Philippines, and certain Central American countries). AID officials estimate that because of prior Agency commitments, only about 15 percent of new DA funds, in any given year, could be made available for new priorities such as infrastructure projects.

Linking Assistance With Domestic Procurement

Both Japan and the United States require recipients to procure a portion of goods and services obtained with assistance funds from donor country firms. According to the Japanese government, about 19 percent of gross Japanese bilateral disbursements in 1987 were tied to procurement from Japanese firms. (See table I.2.) About 28 percent of Japanese disbursements were awarded on a partially untied basis, allowing developing country firms to compete with Japanese companies. The remaining 52 percent was untied, or open to procurement from any country.⁶

Table I.2: Tying Status of Japanese Bilateral Economic Assistance, 1987, Gross Disbursements

Dollars in millions

| | Tied | | Partially untied | | Untied | | Total |
|--------------|----------------|-------------|----------------------|-------------|----------------|-------------|----------------|
| | Percent | Percent | Percent | Percent | Percent | Percent | |
| Loans | \$29 | (1) | \$1,682 ^a | (43) | \$2,236 | (57) | \$3,947 |
| Grants | 1,151 | (57) | | | 855 | (43) | 2,006 |
| Total | \$1,180 | (19) | \$1,682 | (28) | \$3,091 | (52) | \$5,953 |

^aOn partially untied loans, up to 50 percent of goods may be procured from developed country firms.
Source: Government of Japan

⁶The Organization for Economic Co-operation and Development's Development Assistance Committee defines economic assistance as tied when goods and services may be obtained in the donor country or from a limited number of other countries not numerous enough to qualify the assistance as partially untied. Assistance is partially untied when procurement may be from the donor country and substantially all developing countries. Untied aid is available for essentially worldwide procurement.

Tying provisions vary by program and by project within programs. Almost all of the tied Japanese assistance is delivered as grants, including grant funds devoted to technical assistance.⁷ All of the funding open to procurement from developing country as well as Japanese firms was through loans. About 43 percent of Japan's 1987 loan disbursements were partially untied while the remaining 57 percent were untied. These figures, however, do not reflect the recent Japanese movement toward greater untying. Loan commitments for 1987, which do not show the carryover effect of prior year tying policies, were only 32 percent partially untied and 68 percent untied.

Linkage of U.S. economic assistance with domestic procurement also varies by program, project, and recipient. AID did not have statistics available that would permit an accurate portrayal of U.S. tying. Our review of AID records showed that about 77 percent of overall U.S. bilateral assistance obligated through the three main programs was theoretically tied in 1987, including all commodities provided to recipients as food aid.⁸ However, for two reasons, this figure may overstate the degree to which U.S. assistance is actually tied. First, AID policies on project and nonproject assistance allow authorization for local cost financing and other waivers to expand the universe of eligible suppliers in the interest of increased project efficiency, among other considerations. Nonproject assistance provided through cash transfers and commodity imports under ESF (nearly one-half of ESF and DA assistance in 1987) is normally tied to procurement in the United States. However, waivers permitting broader procurement are sometimes provided for project grants.

Second, AID's method of estimating local costs in arriving at the overall tying figures may underestimate actual procurement opportunities open to developing country firms. Although AID regulations tie procurement under DA and ESF loans and grants for specific projects to U.S. sources, local cost purchases financed through project assistance may include goods from any developing country. Additional discussion of U.S. tying is in appendix II. Table II.1 shows the statistics we developed, based on

⁷Procurement provisions for project grants are specified on a case-by-case basis. Procurements from recipient country firms are always permitted, while untying to include third countries is provided in most cases, with no limit on the portion of goods that may be procured from non-Japanese sources. Grant funding for technical assistance, most of which is tied to Japanese sources, made up about 40 percent of all bilateral grant aid.

⁸A portion of the funding for ocean freight costs incurred in transferring food aid to recipients is untied.

information provided by AID, on the allocation of U.S. assistance among the three tying categories.

Substantial Procurement From Donor Countries

Although precise figures are not available for either country, substantial portions of both Japanese and U.S. assistance are used to procure goods and services from donor country firms.

According to the Japanese government, about 43 percent of procurements under economic assistance loans in 1988 went to Japanese firms, while 57 percent went to non-Japanese sources. Official data for grants are not available, although Japanese officials did estimate that about one-third of grant procurement is done in recipient countries.

The information that was available from AID shows about 43 percent of gross U.S. aid disbursements under the three main programs in 1987 going to U.S. sources. (See app. III.)

This overall figure substantially understates actual procurement of U.S. goods and services with assistance funds because available AID figures show all ESF cash transfer funds being disbursed to foreign parties. Accounting for these funds in this manner does not provide any information on who receives these funds from recipient governments. In fiscal year 1987, ESF cash transfer funds were largely tied to U.S. procurement. During fiscal years 1987 and 1988, AID issued formal guidance to establish a closer relationship between cash transfers and procurement in the United States. ESF cash transfers can have an additional trade benefit, in that they are sometimes used by private sector firms in recipient countries to procure U.S. goods, thereby encouraging development of U.S. links to recipient country firms.

Japanese Administrative Practices Help Ensure Commercial Benefits

In addition to overall tying requirements, several aspects of the Japanese administrative system further help to ensure commercial benefits for Japan. These include relying on recipient requests to determine allocation of funds, tying funds used for project planning and administration, and prearranging goods to be procured with commodity loans.

Since beginning its aid program following World War II, Japan has relied on recipient requests to determine how funding will be distributed. Japan has a relatively small foreign assistance administrative structure

which does not permit substantial efforts in assisting developing countries to identify projects or plan development strategies.⁹

This system satisfies Japan's desire to avoid being seen as intruding into the internal affairs of recipient countries, as it theoretically allows recipients to make their own decisions on development priorities. In reality, however, requirements for official requests can be so complicated that recipient countries may not have the expertise to develop and submit requests independently. The practical effect of the system has been to permit the Japanese private sector considerable influence over the development of proposals. Companies involved in such work will naturally invest their time in project ideas that will provide themselves or affiliated companies with substantial follow-on contracts.

Tying funds used for project planning and administration helps ensure that much of the contracting for project execution will go to Japanese firms. Many of the individuals we interviewed informed us that when Japanese companies design projects, procurement specifications naturally tend to be such that Japanese companies are best suited to fulfill them. Also, many of the interviewees believe the integrated nature of Japanese commercial networks makes it quite likely that firms related to those performing planning or administrative tasks, through official affiliation or long-standing professional association, will be in a good position to submit bids by having advance information. This will have an effect on contract awards, even though international competitive bidding procedures are officially used to solicit bids.

Japanese assistance supports private sector input on project planning through technical assistance grant funding devoted to development surveys and through tied engineering services on loans. The Japan International Cooperation Agency's technical assistance funding supports the work of Japanese consulting engineers undertaking a variety of studies, from broad regional development plans to feasibility studies on specific projects. Support for such activity was the Agency's largest single category of expenditure in 1987. Until recently, all members of teams performing such studies had to be Japanese citizens.

Components of Overseas Economic Cooperation Fund loans devoted to consulting engineer services, including project design, are partially

⁹In 1987 the total number of staff in the relevant bureau of the Ministry of Foreign Affairs, economic cooperation staff in diplomatic missions, the Japan International Cooperation Agency and the Overseas Economic Cooperation Fund was 1,396. In contrast, AID had 4,616 staff in Washington D.C., and in overseas missions as of April 1990.

untied for most recipients. Japanese firms, therefore, have a competitive advantage in obtaining contracts for such services, although firms from newly industrialized countries like Korea and Taiwan have had some success. The United States also ties engineering and professional services on capital projects. However, this provision has minimal effect because of the low level of U.S. support for work in the infrastructure area.

The Japan International Cooperation Agency and the Overseas Economic Cooperation Fund do not have sufficient staff to administer the projects they fund. They rely on the private sector to perform needed technical and administrative tasks. Prime contractors on grant-funded projects must be Japanese. Partial untying for consulting services on loans to most countries places Japanese companies in a very competitive position for obtaining this business.

Procurements under commodity loans, which made up about 20 percent of all lending in 1987, are untied. However, lists of goods to be purchased with loan funds must be agreed upon in advance with Japanese authorities. Japanese policy concerning such loans directs procurement toward support for infrastructure development, with associated trade benefits for Japan. In contrast, the United States specifies the goods, such as arms, that cannot be procured with commodity import funds.

Japanese Efforts to Untie Assistance

Largely in response to criticism from other donor countries, including the United States, Japan announced an official policy of gradual untying for economic assistance lending in 1978, and since then has eliminated nearly all fully tied lending.¹⁰ Partially tied lending remains significant, though Japan is gradually moving toward untying for goods on a country-by-country basis.

Beyond changing the official tying status, some specific steps have been taken to alter the administrative features that provide Japanese firms an advantage. A minor concession has been made on grants, in that the Japan International Cooperation Agency now permits up to 25 percent of survey teams to be made up of non-Japanese nationals. The Agency has also engaged foreign firms to administer some grant programs, including a \$500-million program for Sub-Saharan Africa. As for loans, engineering consultant services have been untied for a few recipients,

¹⁰In 1978, about 13 percent of Japanese economic assistance loans were fully tied.

such as Malaysia and Brazil, and untying for additional countries is under consideration.

Japan's Continuing Commercial Orientation

Beyond those provisions concerning procurement, Japan's assistance continues to be allocated to countries and to purposes that provide it with a more commercial orientation than U.S. programs. Japanese assistance remains concentrated in Asia, where it works to reinforce and further develop close economic relations with developing nations in which Japan would, in any case, have a high level of economic interest.

Japan has expanded the geographic scope of its program, particularly by increasing assistance for Africa. However, during the 1980s, Japan has provided more than two-thirds of its bilateral assistance to Asian recipients. Much of this has gone to countries where Japan has substantial trade relations. In 1987, Japan disbursed about 54 percent of its net bilateral assistance to seven Asian countries¹¹, where it conducted about one-third of its total trade with all developing countries. Overall, the volume of trade Japan conducts with these countries is 7 to 9 times greater than the flow of assistance, depending on whether exports or imports are used to make the comparison.

Given Japanese concern with assuring access to critical raw materials, it is significant to note that some of these recipient countries are substantial suppliers of such products to Japan. For example, Japan imported about \$6.3 billion in oil and gas products from Indonesia in 1987 (about 75 percent of all its imports from that country) and more than \$3.8 billion in oil, gas, and wood products from Malaysia (about 81 percent of all Japanese imports from Malaysia.)

The United States, in contrast, concentrates its economic assistance in countries of particular security and political interest, most prominently in the Middle East and Central America, with which the United States does not conduct a great volume of trade. Seven strategically important countries¹² accounted for about 45 percent of gross U.S. bilateral assistance obligations in the three main programs in 1987—Egypt and Israel alone accounted for about 27 percent of the total. The volume of trade that the United States conducts with these countries is about double the

¹¹Indonesia, China, the Philippines, Bangladesh, India, Thailand, and Malaysia.

¹²Israel, Egypt, Pakistan, the Philippines, El Salvador, Costa Rica, and Honduras.

level of assistance provided, but represents less than 10 percent of U.S. trade with developing countries.

Also relevant to the greater commercial orientation of Japan's program is the fact that Japan continues to emphasize improving recipient country economic infrastructure through projects and commodity loans. The United States, on the other hand, places greater emphasis on program assistance in support of economic restructuring and basic human needs. These comparisons are shown in table I.3.

Table I.3: Major Bilateral Aid Uses, 1986-1987, Percentages of Commitments

| Use | Donor | |
|-------------------------|-------|---------------|
| | Japan | United States |
| Economic Infrastructure | 44 | 4 |
| Industry | 8 | 1 |
| Program Assistance | 22 | 51 |
| Social Infrastructure | 15 | 20 |
| Food Aid | 1 | 14 |
| Agriculture | 10 | 10 |
| | 100 | 100 |

Source: Organization for Economic Co-operation and Development, Development Assistance Committee

As shown in table I.3, during 1986-87, about 52 percent of Japanese bilateral assistance was devoted to economic infrastructure and industrial development, as compared to about 5 percent of U.S. assistance. Transportation and energy projects accounted for the largest part of this assistance. For Japan, the 52 percent represents a decline of about 6 percentage points devoted to such projects since the mid-1970s.¹³ Because infrastructure loans and grants tend to require commitment of relatively large amounts of money at a time, they are a good mechanism for Japan to distribute its growing economic assistance budget, while maintaining relatively low staffing levels.

The United States provided about one-half of its economic assistance as program assistance. The largest portion of this was ESF cash transfers and commodity import programs designed to assist strategically important countries like Israel and Pakistan to meet balance-of-payment and

¹³Some perspective on the focus of Japanese assistance can be obtained by citing a few examples from major recipient countries. Nearly one-half of all lending to China in 1987 was provided for railway expansion and electrification. Other major projects included expansion of port facilities, telecommunications improvements, and a hydroelectric power plant. The largest single loan-financed project in the Philippines in 1987 was the development of a coal-fired power plant; the largest in Thailand was the expansion of the Thai telephone network.

budget requirements. Food aid constitutes a large share of the remainder, while DA funds are most heavily invested in areas such as agriculture, health and education.¹⁴ Where substantial ESF project funding has been available, AID has undertaken infrastructure work. In Egypt, for example, AID has committed more than \$2 billion since the mid-1970s to water and wastewater projects, and to development of electric power capacity.

¹⁴Of the various functional accounts within the DA program, the largest amount obligated in 1987 (about \$687 million) was for projects in agriculture, rural development, and nutrition. Projects in the areas of population planning, health, child survival, and education and human resources development accounted for about \$673 million.

Tying of U.S. Assistance

Table II.1: Tying Status of U.S. Bilateral Economic Assistance, 1987, Actual Obligations

| Dollars in millions | | | | | | |
|-----------------------------|----------------|-------------|------------------|-------------|--------------------------|--|
| | Percent | | Percent | | Total | |
| | Tied | Percent | Partially untied | Percent | | |
| DA and ESF: | | | | | | |
| projects | \$1,988 | (66) | \$940 | (31) | \$80 (3) \$3,008 | |
| cash transfers ^a | 1,762 | (76) | 115 | (5) | 444 (19) 2,321 | |
| commodity imports | 288 | (100) | | | 288 | |
| Subtotal | \$4,038 | (72) | \$1,055 | (19) | \$524 (9) \$5,617 | |
| Food for Peace ^b | 1,592 | (94) | | | 103 (6) 1,695 | |
| Total | \$5,630 | (77) | \$1,055 | (14) | \$627 (9) \$7,312 | |

^aESF cash transfers are made to further balance-of-payments relief and policy reform in recipient countries. Therefore, no specific procurement is the object of these transfers. In 1987, however, AID introduced a requirement for recipient countries to maintain ESF transfers in specific dollar accounts and these funds are now frequently tied to either procurement from the United States, or debt repayment to the United States, or to a multilateral institution. We reviewed AID documentation and allocated funds among the three tying categories to reflect the actual circumstances surrounding each transfer.

^bStatistics on the Food for Peace program include obligations made under section 416(b) of the Agricultural Act of 1949.

Source: Agency for International Development

As briefly discussed in appendix I, the statistics on U.S. assistance that we developed from AID data may, for two reasons, overstate the portion of assistance that is actually tied to U.S. sources. First, the universe of eligible countries is often expanded through individual project waivers and, second, local costs may be underestimated.

For DA and ESF funding, AID practices allow for expansion of the universe of countries from which goods and services may be procured through waivers to a project's assigned geographical code (e.g., United States only, developing countries, or free world countries, including industrialized countries). Waivers are infrequently granted for commodity imports. Agency officials stated that waivers are usually not necessary in this area because recipients have great latitude in choosing the products that they will purchase with provided funds. Because projects require specific goods and services, waivers are sometimes provided for procurement of the needed items.

However, comprehensive data on the portions of grants and loans for which non-U.S. procurement is permitted is not available. Our data could not take into account the use of waivers at the project authorization stage because this information is not aggregated beyond the level of

individual projects. AID regional bureaus have been directed to aggregate information on their use of waivers in missions for which they are responsible. However, this information is incomplete. We incorporated in our analysis the information that was available on waivers granted in fiscal year 1987.

While DA grants and ESF loans and grants for specific projects are, in principle, tied to procurement in the United States, local cost purchases are made on a partially untied basis. Local costs are expenditures that are met by exchanging appropriated U.S. funding for local currencies. The level of local costs met by the United States is determined on a case-by-case basis, and can vary a great deal. Such funding is always awarded on a partially untied basis; it may be used to procure items originating in other developing countries, in addition to the recipient and the United States. In submitting statistics to the Organization for Economic Co-operation and Development's Development Assistance Committee, AID estimates that on average, local cost financing makes up 21 percent of project costs.¹ We used this figure in calculating local cost allocations and included such costs in the table as partially untied aid, along with other funds which were clearly awarded on a partially untied basis.²

Actual AID-financed local costs may be higher than 21 percent. We requested and received actual local cost allocation figures from five AID missions in countries suggested by AID as a representative sample of U.S. recipients.³ Overall, local cost allocations accounted for about 31 percent of obligations in these countries. Also, a recent AID study found that for fiscal year 1988, about 64 percent of project procurements in Thailand were designated for local cost support, and hence would be awarded on a partially untied basis.

¹AID uses a 25-percent estimate for local cost financing in least developed countries.

²For example, all project obligations in least developed countries are partially untied.

³Cameroon, Indonesia, Jamaica, Pakistan, Zaire.

Disbursements to U.S. and Non-U.S. Sources

Table III.1 shows statistics that we developed from AID information on the disbursement of funds to firms with U.S. addresses through the main U.S. economic assistance programs. Because AID does not collect detailed information on the distribution of funds to U.S. and non-U.S. sources, this table is based on AID's best estimates. As discussed in appendix I, this table substantially understates actual procurement from the United States, because it displays all funds provided in the form of cash transfers as being disbursed to foreign governments, while ESF cash transfers are, in principle, tied to procurement in the United States.

It was not feasible to assemble more detailed information on the disbursement of ESF cash transfers because of the manner in which AID records have been kept. Beginning during fiscal year 1987 recipients have had to submit records accounting for the expenditure of all funds provided through cash transfers. Prior to this there was generally no such obligation. Also, cash transfer account records are kept by individual AID missions in recipient countries.

Table III.1: U.S. Bilateral Economic Assistance Disbursements to U.S. and Non-U.S. Sources, 1987

| | Percent | | | | Total |
|-----------------------------|----------------|-------------|----------------|-------------|----------------------------|
| | U.S. | Percent | | Non-U.S. | |
| | Sources | | Sources | Percent | |
| Development Assistance | \$480 | (32) | \$994 | (67) | \$1,474 |
| Economic Support Fund: | | | | | |
| Projects | 206 | (32) | 441 | (68) | 647 |
| Commodity Imports | 328 | (90) | 37 | (10) | 365 |
| Cash Transfers | 3 | (0) | 2,110 | (100) | 2,113 |
| Food for Peace ^a | 1,689 | (97) | 58 | (3) | 1,747 |
| Total | \$2,706 | (43) | \$3,640 | (57) | \$6,346^b |

^aStatistics on the Food for Peace program include disbursements made under section 416(b) of the Agricultural Act of 1949.

^bThe total for U.S. bilateral assistance presented in table II.1 includes only assistance funded by fiscal year 1987 obligations. The table III.1 total includes all disbursement occurring in fiscal year 1987, regardless of the year of obligation. The difference between the two totals stems from this difference between the base periods for obligations and disbursements.

Source: Agency for International Development.

Scope and Methodology

To determine how Japan integrates its foreign assistance and trade policies, we obtained information on its economic assistance programs and, for comparison purposes, we developed similar information on U.S. economic assistance programs. We conducted work both in the United States and in Japan. We discussed Japanese and U.S. policies and practices with officials of the Department of State and AID, all relevant Japanese government agencies, Japanese and American academic experts and representatives of companies involved in development work from both countries. We also traveled to Indonesia to view both donor countries' assistance operations in the field. We obtained statistical information on relevant programs from both governments and from the Organization for Economic Co-operation and Development's Development Assistance Committee. The report is primarily based on 1987 data. This was the most recent year for which comparable data was available for both countries.

Our work was conducted from July 1989 through February 1990 in accordance with generally accepted government auditing standards.

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