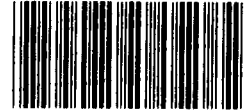


GAO

Testimony



143323

For Release
on Delivery
1:30 p.m. EST
March 6, 1991

DEVELOPMENT ASSISTANCE:
AID's Energy Programs and
Debt-for-Nature Swaps

Statement of
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Before the Subcommittee on Human Rights and
International Organizations
Committee on Foreign Affairs
House of Representatives



050769 / 143323

Mr. Chairman and Members of the Subcommittee:

We are pleased to be here today to discuss our ongoing work concerning the Agency for International Development's (AID) energy assistance activities. Specifically, you asked us to comment on three questions: (1) whether AID is helping developing countries meet their energy needs, (2) what priority AID has given to providing energy assistance to these countries, and (3) whether AID's energy assistance activities are directed toward minimizing the contribution to global warming. You also asked us to comment on the issue of debt-for-nature and debt-for-development swaps. Before summarizing our key points, I would like to say that, since we have not completed our reports, my comments today should be regarded as preliminary. Our formal reports should be issued in the near future.

SOME ENERGY ASSISTANCE PROVIDED

In response to your first question, we found that AID is helping some developing countries meet their energy needs, but the nature and extent of that help in individual countries varies substantially. AID's energy assistance is heavily oriented toward improving efficiency in energy generation, distribution and use and laying the necessary groundwork for larger investments by the private sector and the multilateral development banks. According to AID, about two-thirds of the agency's funding is directed toward improving energy efficiency and conservation in developing countries. Much of this assistance is directed at upgrading Egypt's electricity generating facilities. However, AID supports a

wide variety of smaller energy efficiency and conservation activities in other countries. For example, in Costa Rica, AID's centrally funded Office of Energy supported a comprehensive study of efficiency improvements in all phases of the energy system.

AID's policy dialogue and technical assistance efforts have helped to facilitate an increased role of the private sector in the energy area and to direct multilateral development bank funding toward increasing energy efficiency, encouraging private sector development, and improving the use of renewable energy sources.

In Guatemala, for example, the AID mission, in collaboration with AID's Regional Development Office, has pursued policy dialogue aimed at permitting the private sector's participation in the energy sector, deregulating prices and achieving greater energy efficiency. In response, the Government of Guatemala now permits the private sector to sell power from cogeneration projects to the government's central utility. An AID-supported pricing study in Guatemala helped resolve an important obstacle standing in the way of a \$50 million Inter-American Development Bank project in Guatemala aimed at supporting private cogeneration programs.

ENERGY IS RELATIVELY LOW PRIORITY

In response to your second question, energy assistance to developing countries remains a low priority for AID.

AID's energy obligations over the last decade have averaged about \$200 million a year, or about 2 percent of AID's total annual economic assistance. Fiscal year 1990 funding was \$206 million. Most of this was targeted to 2 countries. Egypt received \$112 million or 54 percent of the total funds available, and Pakistan received \$57.8 million or 28 percent of the total. The remaining assistance levels for other countries pale by comparison. For example, the missions in Guatemala, Kenya, and Thailand obligated \$1.6 million, \$148,000 and \$45,000 respectively, and some received even less or none at all.

Obviously, the high levels of AID's Economic Support Funds going to Egypt and previously to Pakistan¹ played a large role in the distribution of energy assistance funds. In these countries the AID missions expended large amounts of Economic Support Funds on major power projects. Most other AID missions have not had funds available for such large capital-intensive projects and thus have limited their energy assistance to low cost technical assistance and policy dialogue activities.

The decentralized nature of AID also affects the priority accorded the energy sector. The basic responsibility for establishing mission priorities lies with individual AID mission directors, and priorities by functional areas vary greatly from mission to

¹Funding for Pakistan has been suspended because of its ongoing nuclear weapons program.

mission. We noted this during our fieldwork in Latin America, where energy assistance practices differed greatly among the missions.

Decentralization also affects the ability of the centrally funded activities to influence what takes place at the mission level. AID's Office of Energy received more than a 50-percent increase in funding from 1989 to 1990, and for fiscal year 1991, the Office was allocated about \$20 million. Despite these increases, the Energy Office still receives only about 10 percent of the funds allocated to energy programs, and the Office's role has been primarily to serve as an advocate for energy assistance in AID missions and provide technical assistance and project support on a worldwide basis. The Office's ability to make an impact depends largely on cooperation from individual AID missions.

Another indication of the low priority accorded the energy sector is the low number of AID staff assigned to the area. AID employs very few energy professionals in positions dedicated exclusively to energy. In 1989, the number of direct hire energy positions throughout AID was 16. The Global Warming Initiative portion of the 1990 appropriations act encouraged AID to add staff with expertise in relevant fields, such as energy. AID had created 26 new positions through December 1990--3 direct hire and 23 contract hires; however, the AID missions expressed almost no interest in

hiring energy specialists. The hiring effort was channeled towards obtaining more broadly focused environmental expertise.

GLOBAL WARMING

By encouraging greater efficiency, facilitating private sector and multilateral development bank investment, and providing limited support for planning and renewable energy, AID's energy assistance does address global warming concerns. However, global warming is only the latest in a long series of goals that AID is attempting to address with its energy assistance; this issue has had a marginal impact on the orientation of agency programming.

DEBT SWAPS

Now let me turn briefly to the issue of debt-for-nature and debt-for-development swaps--a concept developed by Dr. Thomas Lovejoy when he was at the World Wildlife Fund, and supported by AID. The idea is to provide some debt relief to developing countries and at the same time provide local currency resources to carry out environmental or development programs.

The first debt swap of this type was in Bolivia in 1987. Using a donation of \$100,000, Conservation International was able to reduce Bolivia's external debt by \$650,000. The purpose of this swap was to preserve a public park and the surrounding areas. Since that time, 13 other countries have participated in debt-for-nature or debt-for-development swaps, reducing the aggregate face value of

their debts by about \$132 million as of fiscal year 1990. Complete data is not available on the total cost of reducing the debt by this amount, but it exceeds \$22 million. AID's total contribution in debt swaps has amounted to about \$6 million for eight countries through fiscal year 1990.

During our review we learned that the concept has many proponents as well as many skeptics. The advantages and disadvantages of debt swap arrangements clearly depend on the perspective one takes. For example, of the \$132 million in face value of debts swapped, nearly \$87 million was from one country, Costa Rica. Since this amount represents less than 2 percent of Costa Rica's \$4.4 billion external debt, one can immediately see that debt swaps are not a major vehicle for debt relief. On the other hand, the swaps have allowed countries to apply local currency resources to environmental activities that were not otherwise funded in their budgets; this is clearly an advantage.

Some economists we spoke with raised a concern about the potential inflationary impact of debt swaps on developing countries. They pointed out that under these arrangements, additional local currency could enter the local economy without an accompanying inflow of real resources. Host government officials we spoke with acknowledged the potential for such inflation but pointed out that by converting dollar debt to local currency-denominated bonds and

using the bond interest to carry out the program activities, the inflationary risk could be minimized.

Another issue raised by some economists during our review was whether the hard-currency resources that nongovernmental and private organizations use to buy the debt on the secondary market would provide greater benefits if it was given directly to the indebted country. They argued that providing the resources directly would provide the country with a "real" resource that could exceed the value of the country's reduced debt service obligations. Again, host-country officials we spoke with said that this issue was one that they analyzed and evaluated very carefully when negotiating a debt swap package, and that they only entered into debt swap agreements when it was advantageous to their countries.

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Mr. Chairman, this concludes my formal remarks. We would be happy to respond to any questions you might have.