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USING AID TO EXPAND EXPORTS

A report to the U.S. Treasury Department

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I. Objective and approach

Earlier this year the Government of Belgium sent a trade mission to Thailand to investigate steps which should be taken to increase Belgiam exports to Thailand. One of the major recommendations of the trade mission was that the Government of Belgium should initiate a program of financial and technical assistance to Thailand. The reasoning of the trade mission - faulty or not - is that aid makes trade, at least in Thailand.

The approach used in this report is somewhat like assuming that the U.S. Government were in the shoes of Belgium - but with respect to all of the developing countries. If we were starting fresh, how would we use foreign assistance - the AID program specifically - to build a basis for expanded U.S. exports to aid recipients in the years ahead. This is the general objective of this report.

Its emphasis is on the use of aid to open, build, and preserve markets in developing countries in the sense of medium and long-term follow-on effects. It does not consider those additionality measures relating to host country import and exchange control systems, nor proposals relating to the problem of 50-50 shipping requirements. These are already receiving intensive attention from the U.S. Government. In this respect, the report is almost entirely concerned with the design of programs - sectoral assistance, credit programs, technical assistance arrangements, private enterprise incentives, and related matters.

This report will first seek to identify some specific ways of using AID programs to encourage U.S. exports and will then consider the policy and administrative implications of such actions.

II. Programming Possibilities

A. Whole Sector Programs or Systems

If experience is any guide, there are probably a number of opportunities for a foreign aid program in a country to concentrate in one sector or in one industry in order to seek a dominant U.S. influence and maximize follow-on export effects. In some cases the critical measure may be early identification of an emerging new industry. This may entail only timely technical assistance programming and normal U.S. commercial contacts. In other cases, the key program may be adequate U.S. Government loan financing. Both loans and grants of technical assistance may be desirable in some circumstances. Special promotional efforts by the U.S. Government, including organization of a consortium of U.S. private companies, may be deemed desirable under certain conditions.

In 1966, the U.S. Government financed a study projecting the probable growth of the electric power industry of Thailand by 1975. Equipment requirements in the amount of $240 million were estimated for generation, transmission, and distribution facilities. There would be in addition a considerable impact on the demand for consumer products related to the availability of electricity. There seemed to be sufficient U.S. export opportunity flowing from this situation to lead to a proposal that further work be done to estimate in detail the specific end-items required and to consider with American industry what it could be given sufficient lead time to compete effectively for the business. The proposal was rejected earlier this year on the grounds that "its chief value would be concerned with American export promotion".

The United States, through its AID program has opened up markets for telecommunications equipment in several countries. It may have failed to capitalize on being first in the market in a number of instances. In Iran, the termination of U.S. foreign aid, including technical assistance, was followed by the entry of the French in providing long-range planning assistance to the Iranian Government for its telecommunications system which will require heavy equipment purchases over the next several years. It is entirely likely that French technical assistance in telecommunication planning will lead to a favored French supplier position.

It has been reported that U.S. discouragement of Pakistan's request for American telecommunications management contract assistance and the subsequent funding of such assistance by the U.N. Development Program resulted in a German firm providing personnel under leaves of absence in order to serve the U.N.-financed project. It would be natural and hardly sinister for there to develop between the Government of Pakistan telecommunications officials and German (or other European) suppliers considerably closer relations on all aspects of telecommunications equipment procurement. The question arises whether the use of U.S. funds through its U.N. contributions to obtain European sources of technical assistance for Pakistan is a better way of carrying out an export expansion objective than financing American services of this kind under the AID program.

The market for telecommunications equipment in developing countries in the next few years will grow rapidly. This is a field which should receive careful consideration by the U.S. in deliberately concentrating AID financing resources in order to go after the export business.

A deliberate effort to concentrate AID financing in the development of the emerging timber industry in Turkey might open and develop a market for American machinery and equipment in that industry. This effort would probably require drawing on U.S. companies for technical assistance of various kinds. It would require viewing the development of the timber industry as a whole system. Agriculture, transportation, and other sectors or sub-sectors are also best treated as systems with respect to decision making on equipment procurement.

The growing systems orientation of recipient countries provides a favorable basis to improve the U.S. competitive position. The systems orientation not only permits the application of modern management technique in which the U.S. is recognized as a leader, but also defines a business opportunity which is large enough to engage the interest of American companies interested in the economies of scale. This approach also permits long-range planning between the U.S. Government and U.S. industry in pursuing business of this kind.

At the same time, such programming may conflict with established concepts of "balanced" programs or with the existing pattern of AID mission organization and staffing. It would require a willingness to turn down other possibilities for financing, which might be more attractive in cost-benefit terms from the viewpoint of the country. It would incur costs arising from the effort to identify and transform into projects a particular industrial potential such as the timber industry. The issue for the U.S. Government is whether its own cost-benefit calculations should assign a high value to the potential for U.S. exports as a benefit.

B. Investing in modern marketing systems

Another major area of coincidence of interest between the export expansion objectives of the United States and the economic growth objectives of recipient countries may exist in removal of bottlenecks to market enlargement. Aid programming could support a program of modernizing distribution facilities serving American products as part of an effort to establish modern marketing systems in a country.

1. Credit

Installment credit and acceptance finance companies can create and enlarge markets which in turn can make feasible investment in local assembling as well as increased U.S. exports. It is not impossible to conceive of U.S. loans or guaranties in local currency to banks in support of expanded credit for distributors of selected U.S. machinery and equipment. It may also be possible for AID to lend to a private development bank in a way enabling relending for 18 months to an acceptance finance company serving distributors of American consumer durables. This kind of financing may be an efficient use of working capital during the period that development projects for long-term financing are being developed. Specific arrangements for the use of AID loans which support U.S. export expansion requires country-by-country study. In Turkey, for example, considerable interest has been shown in U.S. financing to establish an equipment leasing enterprise which is a specialized form of financing.

2. <u>Transport and Storage</u>

Refrigerated trucks, cold storage equipment and other specialized means of moving and storing perishables are of growing importance in developing countries as well as an important U.S. export field. AID attention to assessing and developing "refrigerated marketing systems" as eligible projects in particular countries would provide the early start and compatibility of components needed to establish a strong market position of U.S. equipment. AID financing for warehousing projects which provide U.S. distributors with the quick delivery of off-the-shelf service is especially important in large country markets or for multi-country marketing. Financing of "distribution parks" owned or leased by several U.S. companies sharing common facilities and financing is another possibility of support for U.S. exporters which will tend to strengthen host country marketing efficiency.

3. <u>Repair and Technical Services</u>

Where AID project financing can link credit and warehousing with repair and technical services for U.S. machinery and equipment, it can provide a powerful competitive "equalizer" for U.S. exporters. One form of financing would be for AID to share with one or more U.S. manufacturers the costs of establishing and staffing a repair services school in one or more recipient countries. A major American producer of electrical appliances recently considered seeking this kind of assistance but decided against it reportedly because dealing with AID was too complicated. Where a school for repairmen was part of a warehousing project or a "distribution park" the financing burden might be spread over several companies. The key point is training on U.S. equipment being marketed in the country. The potential value of U.S. financing of training young men to repair air conditioning, refrigeration, communications, water supply, waste disposal and other kinds of equipment is high, both for U.S. exporters and for a recipient government interested in generating jobs and upgrading skills.

At a higher level of training, industrial technicians are being trained in Karachi at the Swedish Technical Institute on Swedish switch boxes and conduits. The tendency will be for these technicians to order Swedish products based on their familiarity with the equipment gained at the Institute.

At the level of engineering services for major pieces of hardware, it may be feasible to fund from AID technical assistance money the costs of technical services. The sale of large American electrical generators, for example, might be facilitatec if such services were provided but the price quoted to the foreign customer did not include the high cost of American engineering and technical services associated with installing, testing and teaching the customer how to operate and maintain the equipment. The cost of American services are probably considerably higher than those offered by European and Japanese vendors. The American firm would improve the competitive position if its price was based on equipment cost only because of the AID support. AID could provide such services by maintaining an open-end contract with major suppliers to provide technical services on an AID work order basis. This kind of AID-financed technical assistance is as useful as many other kinds, but it is directly linked to an export.

C. Promotion and Market Development

Our knowledge of internal marketing of imports, how goods move, how they are financed, how they are stored, and how they are promoted is sufficiently imperfect to justify investing some money in detailed studies of markets in selected countries. Little if any AID research funds have been used to investigate the specific 'imensions of the area of coincidence of interest of developing countries and of U.S. export expansion goals or to explore specific project possibilities.

One problem of particular interest is what it would take for an American trading company to challenge British and French trading companies in Africa. Should the U.S. foreign aid program encourage and support with loans and grants a private effort to build an American marketing network in African countries which are now or will represent significant markets in the years ahead? African leaders in many countries now dominated by British and French trade have often expressed their desire to broaden Africa's international trade and investment relations.

Financing accommodations of various kinds have been developed to help prospective American investors meet "the high cost of looking". AID requested in FY 1968 over $2 million to cover up to half the cost of pre-investment feasibility and market studies and various information programs for investors. Under other programs AID provides very substantial sums of technical assistance funds for contracts with 15 U.S. financial institutions for the identification and promotion of private investment opportunities in Africa. Additional amounts are earmarked for studying large-unit private agricultural investment. Similar support for investors is provided in programs for Latin America, the near East, South Asia and East Asia.

Should trade development piggy-back on investment development activities? Perhaps the contracts with the 15 U.S. financial institutions to find and promote investments in Africa should be revised to invite them to identify ways to broaden U.S. export markets. In the same vein, the technique used for investment promotion may be in part adaptable for trade promotion. American companies have received 100% financing to study the market in Latin America for possible investment in nutritious food processing plants. Subject to host country permission, AID might consider financing market testing efforts by American companies interested in exporting new products especially beneficial to health and other conditions of life in the country. More generally, should investment guaranties be extended to American investment in warehousing facilities, training schools, or other physical distribution and marketing facilities.

It is often claimed that one of the underlying weaknesses of U.S. exports is the lack of aggressiveness and interest of the American sales effort as compared with Europeans. It has been pointed out, for example, that in Pakistan, European suppliers are represented by their own nationals, whereas American companies are represented by local agents. The charge is that local agents are not as effective in advancing the interests of American companies as Americans would be. Further, Europeans offer free "business" trips to Pakistani businessmen and heads of government corporations. The Japanese offer free feasibility studies. The British promote particular products. European and Japanese companies seem to send more teams to investigate export and investment possibilities than do U.S. companies. Finally, the relationship between European governments and European business is much closer than in the United States.

Some of these disadvantages could be offset by some of the actions discussed earlier. Most of them seem to be rectifiable by the judicious application of money. In this connection, the experience with financing of agricultural market development under P.L. 480 may be instructive.

According to the Department of Agriculture, about $70 million in local currencies have been expended for market development since the inception of P.L. 480. In addition, cooperating private trade and agricultural groups have contributed about $47 million of their own resources for the same purpose, making a total of $117 million applied to foreign agriculture market development from 1954 through 1966. The major expenditure in market development activities has been cooperative programs carried out by the U.S. Department of Agriculture and private trade and agricultural groups. The U.S. Department of Agriculture reports that during the impact years of the agricultural market development program dollar exports of U.S. agriculture commodities and products have increased from $2 billion to nearly $5 billion with part of the credit being given to the market development program for this increase.

To the extent that local currency funds are available and host countries would agree to the application of these funds for broader market development purposes, then several promising activities suggest themselves. These include the local currency financing for the marketing, warehousing and related activities discussed earlier. In addition, such financing may be one way of coping with visits, travel, market research and a variety of trade promotion measures. The precedent of covering local costs under P.L. 480 for private American agricultural groups offers a basis for extending this kind of accommodation to support a local office for particular industrial groups. Another possibility is lending an amount of local currency to a local American bank for relending to suppliers who want to establish their own representation in the country but want financing to cover the local costs for the first two or three years.

D. Reorienting AID for export promotion

It is doubtful that AID/Washington or AID overseas missions are well organized for taking U.S. balance of payments problems fully into account in AID programming. It is also doubtful that leaving to the discretion of AID missions the matters of designating an individual as "aid additionality coordinator" (possibly in addition to his other duties) is an adequate effort. There are two major considerations. First, is the need for deliberate seeking out of U.S. AID export expansion opportunities rather than "taking them into account". This is a full-time programming task. Second, program decision making for all practical purposes appears to take place in regional offices not in planning or coordinating offices. The staff responsibility should be fixed so that the effort is part of the mainstream of AID programming and becomes a matter of initiating new efforts in the field.

It would also seem useful to have an independent and careful review of Reg. 1 and related administrative arrangements to assure the U.S. Government and U.S. business that the regulations are not in serious conflict with U.S. balance of payments objectives. Such a review may identify issues relating to legislative changes which may be desirable. In some countries AID-financed goods are regarded as less desirable than other financing because of AID procurement regulations. In some countries, the large companies who know how to operate within the credit system and the foreign exchange control system appear to be able to get their requirements met from non-AID sources. It is possible to get the impression that the most efficient local companies operate with European suppliers and with free foreign exchange, while the smaller and least efficient traders operate with AID financing. If the same is true with respect to U.S. exporters, the cumulative effect is to reinforce higher prices for AID goods and to have them distributed by those least likely to build follow-on markets.

AID might also wish to consider means to assure its access to top grade technical people so necessary in influencing highly qualified foreign technicians. The near technological monopoly which Europeans accuse the United States of having does not fully filter through to the lesser developed countries. To the extent that the United States enjoys leadership in the world, we should be enjoying the results which would flow from applying such leadership to shaping the nature of industrial development and management in the lesser developed countries. There are few overall export expansion tools more powerful than exporting this know-how to the lesser developed countries. It is very clear that our best technical talent does not go abroad. There are a variety of reasons for this which are well-known. One which is not often discussed is AID's reluctance to finance the high salaries customary for high level technicians in the United States. AID contracts are financing salary scales which in almost all cases do not exceed $26,000 a year. In certain fields, this kind of limitation keeps the top men outside the AID contract and discriminates in favor of sending lower-calibre people abroad. In a world where U.S. commercial leadership will turn on the quality of its technical talent, this kind of a contracting system is hardly consistent with U.S. balance of payments objectives.

III. Implications of Emphasizing U.S. export expansion

The foregoing array of possible measures which could be taken to use AID assistance for export expansion include several which are undoubtedly contrary to existing law, policy, or administrative practice. The array, however, does help to surface several issues and thus may facilitate decision-making on management of such assistance.

It is important to keep in mind that the possible actions discussed above will not produce effects this year or next year and in this respect should be regarded as part of a long-range program. If U.S. balance of payments stringencies may be expected to continue for several years, programs of the kind identified earlier may be justifiable in a cost-benefit sense. Perhaps another way of putting the matter is to consider whether such a program, had it been installed five years ago, would be yielding helpful results now. A decision not to intensify an export-expansion effort using AID resources presupposes judgement that a) other U.S. balance of payments improvement measures make such a program unnecessary; b) such a program would not have a significant effect on U.S. exports; or c) the costs to the U.S. of such a program are unreasonable in relation to expected benefits.

Suggestions of techniques for using foreign assistance for export expansion are essentially suggestions of "gimmicks" unless they are related to some overall strategy for relating AID to U.S. balance of payments goals. Because these techniques and the range of possible actions are inevitably and directly linked with policy, some general remarks on this subject may be in order.

A. Is AID responsible for export promotion?

Ingenuity in conceiving, negotiating and implementing major new actions to enhance additionality and follow-on sales undoubtedly exists in abundance in AID - in Washington and overseas. It is not and will not be adequately exercised until export expansion becomes a major measure of effectiveness of AID programs. Any objective observations of how AID works abroad lead to a strong impression that U.S. export expansion is not at the forefront of AID programming and that AID often regards the use of the AID program for this purpose as damaging politically to the United States and damaging to the development effort of the recipient country.

Probably both worries are overstated. Recent official U.S. Government discussions with host countries suggest that these governments (1) recognize the need for the U.S. Government to concern itself with this subject and (2) want to cooperate in efforts to help use AID for this purpose. Further, it is not entirely clear that the pace of development of recipient countries in the past few years would have been significantly slower if export expansion _had_ been the major objective of the AID program.

It is interesting to compare the effort and attention which accompanied the inception of the P.L. 480 program with the export expansion program. Agricultural sales were pushed full-time and all the time amid prophecies of political disasters which would follow vigorous sales efforts. In a relatively short time, P.L. 480 commodities were being programmed and justified as being entirely consistent and indeed critical to the achievement of development goals.

AID programs are especially susceptible to conflicting claims for funds and attention - war on hunger, water for peace, private investment, health, education counter-insurgency, birth control, and others. Demands for attention to additionality can easily be regarded in the field as the latest irritating "nouvelle vogue" which must be"handled" but not be allowed to interfere with the serious business of "the program". There is no reason to expect continuing and effective efforts unless such efforts become clearly a major goal of AID as an agency and a measure of the effectiveness of its staff. It cannot be a major effort of AID if it is a minor or part-time occupation of someone in an AID mission. It must be in the mainstream of programming, of policy, and of promotion of staff.

A serious effort to find, develop, negotiate and operate AID programs which will expand U.S. exports demands not only a sharply accelerated level of attention, but a sharply different way of looking at aid. An interesting set of issues would be posed for the U.S. Government if AID economic assistance goals were changed to make the expansion of U.S. exports as important as the acceleration of economic growth in recipient countries. Would the annual aid request attract more support from the Congress and from the business community if AID became a much more active instrument of U.S. balance of payments policy? Once the program is viewed in this light, the searching for countries to be taken off the AID list becomes a rather different problem. It may be much more desirable to maintain concessional technical assistance programs in such countries. An investment in a technical assistance grant to a country that would normally be considered as a candidate for termination of aid might offer attractive balance of payments payout as measured by future U.S. commercial sales of equipment flowing from the presence of U.S. technicians. If AID is not considered the proper vehicle for funding export expansion efforts, should the Department of Commerce seek funds for this purpose? Or should AID contract with or otherwise transfer AID funds to the Department of Commerce to design and administer technical assistance programs with significant export follow-on potential?

As the size of AID shrinks and as the number of AID countries declines, two consequences follow. On the one hand, the size of the problem of assuring additionality may shrink. On the other hand, U.S. Government will lose a program which represents one of the most flexible and promising financing instruments to build long-term follow-on exports. As AID money becomes smaller, it can be argued that more of it should be used for export expansion purposes. This could be done only at the sacrifice of other urgent U.S. objectives. In this light, a case can be made that AID funds or other funds should specifically be sought for use in export expansion activities.

B. <u>What are some reasonable next steps?</u>

In light of the foregoing, it may be useful to develop two or three model country programs which are deliberately designed to reflect high priority U.S. export expansion goals in order to test feasible mixes of AID activities. A body of such experience in several countries is needed as a guide for determining an appropriate level of AID funding globally. Even if it were decided that programs to encourage follow-on exports should be financed from current levels of technical assistance (running at about $250 million annually) the experience in developing model programs in a few countries would provide highly valuable information.

In this connection, the field work of the Additionality Working Group earlier this year was a good beginning. Much more time, however, is required to convert an existing program into a fully integrated "additionality program". The tough job will be to provide sustained and skillful attention to the detailed design and negotiation of actual projects or systems.

In addition to developing model country programs, some of the activities discussed earlier could begin immediately. These include the review of Reg. 1, earmarking of AID research funds, and exploring practical ways of linking work going on in investment surveys with trade development